



# TaxNewsFlash

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## Foreign taxes paid on accumulated earnings offset under section 965 are creditable (federal district court)

A federal district court recently held that a U.S. corporation subject to tax on the accumulated undistributed earnings of its foreign subsidiaries under section 965(a) may credit foreign taxes paid on such earnings even though such earnings are offset by losses of other foreign subsidiaries under section 965(b). As a result, the taxpayer may be entitled to a refund of more than \$89 million.

The case is: *Fedex Corporation v. United States*, 20-cv-2794 (W.D. Tenn. March 31, 2023). Read the [court's order](#) [PDF 214 KB] (29 pages)

### Summary

The 2017 "Tax Cuts and Jobs Act" (TCJA) replaced the U.S. worldwide system of corporate taxation with a "territorial" system. As part of that change, a transition tax was imposed under section 965(a) on U.S. corporations' accumulated undistributed earnings of their foreign subsidiaries. Under section 965(b), U.S. corporations were allowed to offset those earnings with the losses of their unprofitable foreign subsidiaries.

The taxpayer was subject to tax under section 965(a) on the accumulated undistributed earnings of its foreign subsidiaries, but it was able to offset a portion of those earnings with losses under section 965(b). The taxpayer argued that foreign taxes paid on those offset earnings were creditable under sections 959, 960, and 965. Specifically, the taxpayer argued that it was entitled to a credit under the plain terms of the statute because (1) its distributed offset earnings were excluded from income under section 959, (2) those offset earnings are treated as dividends for which a credit is given under sections 901 and 902, and (3) the foreign taxes associated with the offset earnings were not previously deemed paid by section 960(a)(1). Because section 960(a)(3) unambiguously provides a credit, the taxpayer argued that the government cannot deny that credit by using a regulation to rewrite the statutory text.

The government responded that offset earnings are deemed to have been included in income under section 951 and thus the taxpayer's associated foreign taxes were deemed to have been paid already under section 960(a)(1), and section 960(a)(2) specifically states that foreign taxes previously deemed paid under section 960(a)(1) will not be credited again under section 960(a)(3). The government further argued that the foreign tax credit was created to alleviate the problem of double taxation, so it would be inappropriate to give a credit for offset earnings that are not subject to U.S. tax in the first place.

The taxpayer and the government filed cross-motions for partial summary judgment. Finding that the government's regulation is contradicted by the plain terms of the Code, the court granted the taxpayer's motion for partial summary judgment.

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