



GMS Flash Alert

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United States – IRS Appeals Decision Allowing FTC Claim Against Net Investment Income Tax

On December 18, 2023, the United States filed a notice of appeal against the decision of the U.S. Court of Federal Claims in the case of *Christensen v. United States*.¹ In this case, the court held that U.S. citizens residing in France may claim a foreign tax credit (FTC) against their net investment income tax (NIIT) liability based on the language of Article 24(2)(b) of the U.S.-France income tax treaty.

WHY THIS MATTERS

Under U.S. domestic tax law, an FTC is not allowed against the NIIT. The ruling by the U.S. Court of Federal Claims offers a potential avenue for certain taxpayers to offset the NIIT with foreign income taxes assessed on the same income pursuant to the U.S.-France income tax treaty. This could eliminate or reduce the double tax imposed by the United States and France on the same income that is subject to the U.S. NIIT. Further, this could reduce assignment costs for tax-equalized high-net-wealth employees.

The U.S. government has appealed the decision, thus most likely the IRS will suspend the processing of refund claims filed on this basis until the appeals process is complete.

Summary of the U.S. Court of Federal Claims Decision

The taxpayers, both U.S. citizens, are a married couple living in Paris who filed a joint return for 2015 – the tax year in issue. On their original return they reported foreign-source passive income and U.S.-source passive income on which they paid NIIT. In addition, they paid French income tax on their foreign-source passive income. In 2020, they filed an amended return for 2015, claiming a refund plus interest in relation to the NIIT imposed on their foreign-source passive income, which they claimed was offset by an FTC pursuant to the Relief from Double Taxation article (Article 24) of the treaty.

The court provided a detailed analysis of the treaty provisions and their relationship to the U.S. Internal Revenue Code FTC provisions. The court held that the taxpayers could not claim a treaty-based FTC against the NIIT under Article 24(2)(a) of the treaty because the wording of that subparagraph requires that the credit must be “in accordance with the provisions and subject to the limitations” of the Code. Specifically, the court held that Article 24(2)(a) is limited by Code sections 27 and 901(a), which only allow FTCs against tax imposed under Chapter 1 of the Code. Because the NIIT is imposed by Code section 1411, which is in Chapter 2A, it cannot be offset by FTCs under paragraph 2(a) of the treaty.²

However, the court held that Article 24(2)(b) of the treaty could be construed to allow U.S. citizens who are residents of France to claim a treaty-based FTC against NIIT for French income tax imposed on foreign-source income. Unlike Article 24(2)(a), Article 24(2)(b) does not include the “subject to the limitations ...” language and stands on its own as “Article 24(2)(b) neither contains nor refers to the Article 24(2)(a) limitations.” Hence, the taxpayers could claim a treaty-based FTC under Article 24(2)(b) for French income tax imposed on their passive foreign-source income to offset the NIIT imposed on that income.

As noted, the IRS has appealed the decision, therefore whether an FTC is available to offset the NIIT under the U.S.-France income tax treaty is uncertain.

KPMG NOTE

The deadline for FTC refund claims relating to tax year 2013 (the earliest year for which refund claims could be made) is on April 15, 2024.

FOOTNOTES:

1 *Christensen v. United States*, 168 Fed.Cl. 263 (U.S. Ct. Fed. Claims 2023), *appeal docketed*, No. 24-1284 (Fed. Cir. Dec. 22, 2023); see [Christensen v. US 20-935T | U.S. Court of Federal Claims | United States Courts](#).

2 Two previous cases have reached the same conclusion in relation to the same or a similar treaty provision: *Toulouse v. Commissioner*, 157 T.C. 49 (2021) (in relation to the U.S.-France income tax treaty), and *Kim v. United States*, 131 A.F.T.R.2d 2023-1394 (C.D. Ca. 2023) (in relation to the U.S.-South Korea income tax treaty).

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