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KPMG report: Initial impressions, FAQs on "transition tax" under section 965 for 2018 returns

The IRS today posted a set of questions and answers (referred to as "FAQs") concerning issues relating to section 965 filing and reporting requirements for 2018 tax returns.

The FAQs—***Questions and Answers about Tax Year 2018 Reporting and Payments Arising under Section 965***—provide answers to questions related to tax year 2018 return filing and payment obligations arising under section 965—including reporting and payment obligations resulting from amounts included in income for the 2017 tax year.

A prior version of FAQs provide answers to questions regarding tax year 2017 return filing and payment obligations arising under section 965.

This report provides brief initial impressions and observations about the new FAQs.

Initial impressions about FAQs

FAQ 1 and FAQ 2 appear to be similar to those provided in the FAQs for 2017. Section 965 payments—whether for the full amount of the 2018 inclusion, the first installment payment for 2018 inclusions for which the taxpayer makes a section 965(h) election, or the second installment payment for 2017 inclusions for which the taxpayer made the section 965(h) election—are to be paid separately from "non-section 965" liabilities. Pursuant to the new FAQs, taxpayers will have additional options for the method of payment—now including EFTPS, wire transfers, or mail. Installment payments with respect to the 2018 inclusions (but not the second installment for 2017 inclusions) may also be made using electronic funds withdrawal. The IRS will issue payment vouchers six to eight weeks in advance of the due date, informing taxpayers of the amount of their second section 965 installment payment.

Next, the FAQs provide some “bad news” and some “good news.”

- FAQ 4 provides what may be viewed as the “bad news.” For 2018 inclusions for which the taxpayer makes the section 965(h) election to pay in installments, the IRS will follow the same approach that it followed in 2017—i.e., the IRS will apply any overpayments for 2018 to subsequent section 965 installments with respect to the 2018 inclusion, rather than to refund or credit the excess. Because taxpayers now have advance notice of the IRS’s intended rules of application, taxpayers need to plan accordingly to consider limiting any unnecessary overpayments and unintended application of payments.

- FAQ 3 provides the “good news.” A taxpayer that makes payments in 2018 that exceed the taxpayer’s regular tax liability and its second section 965(h) installment liability for 2017, may receive a refund or credit of the excess rather than having to apply it to the third and subsequent installments (this assumes the taxpayer does not have a section 965 inclusion for the 2018 tax year).

- FAQ 5 explains how the IRS will apply 2018 payments to a 2018 inclusion for which the taxpayer made the section 965 (h) election. This treatment will follow the same approach that the IRS took for 2017 inclusions—i.e., first, to regular [non-section 965] liability, and then to the section 965 liability.

- FAQ 6 requires the filing of Form 965 with the 2018 return if the taxpayer had a section 965 inclusion in either 2017 or 2018.

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