



TaxNewsFlash

United States



No. 2019-498
October 11, 2019

Notice 2019-58: Treatment of certain interests in corporations as stock or indebtedness, expiration of temporary regulations

The IRS today released an advance version of Notice 2019-58 concerning temporary regulations under section 385 on the treatment of certain interests in corporations as stock or indebtedness.

Read [Notice 2019-58](#) [PDF 10 KB]

Background

The U.S. Treasury Department and IRS on October 21, 2016, published in the Federal Register [final and temporary regulations](#) [PDF 723 KB] under section 385 addressing the treatment of certain interests in corporations as stock or indebtedness. The final regulations included documentation rules in Reg. section 1.385-2 and recast (and *per se* funding) rules in Reg. section 1.385-3. The temporary regulations included limited exceptions for certain cash management arrangements and coordination rules for partnerships and consolidated groups (Reg. sections 1.385-3T, -4T) (the temporary regulations).

On the same date, October 21, 2016, Treasury and the IRS published a [notice of proposed rulemaking](#) [PDF 219 KB] (the 2016 proposed regulations) in the Federal Register by cross-reference to the temporary regulations.

The temporary regulations were issued to provide limited exceptions for certain related-party debt, including certain short-term and working capital debt, ordinary course intercompany receivables incurred in purchasing inventory, and deposits accepted by a cash pool header. These exceptions provided an important “safety valve” to exclude certain debts that the IRS did not perceive as having a significant earnings-stripping potential. In addition, by excluding these items, the temporary regulations lessened the risk that repayment of these debts could be viewed as a redemptive distributions, which could have led to cascading applications of the *per se* funding rule.

The temporary regulations also included rules to coordinate the application of the recast rules in the context of partnerships and to members of consolidated groups, and included a provision that provided that all members of a consolidated group generally were treated as a single corporation (thus exempting transactions and debt between consolidated group members).

Notice 2019-58

Today, [Notice 2019-58](#) [PDF 10 KB] announces that, following the expiration of the temporary regulations under section 385, taxpayers may rely on the notice of proposed rulemaking cross-referencing the temporary regulations.

The temporary regulations expire on October 13, 2019. [Reg sections 1.385-3T(l); -4T(h).] Under today's notice, notwithstanding the temporary regulations' expiration, a taxpayer may rely on the 2016 proposed regulations for periods following the expiration of the temporary regulations until further notice is given, provided that the taxpayer consistently applies the rules in the 2016 proposed regulations in their entirety. In effect, reliance would be expected to keep the status quo in effect.

KPMG observation

Many practitioners anticipated that the recast rules would have been withdrawn, given the expiration of the temporary regulations. It is unclear whether after releasing the notice today whether the IRS is still considering a withdrawal.

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