

## AL DOR issues guidance regarding IRC Section 965 deemed repatriation impact on Alabama taxpayers

### Overview

On April 27, 2018, the Alabama Department of Revenue (AL DOR) issued a Notice regarding the IRC Section 965 transition tax, specifically the deemed repatriation income impact upon Alabama corporate, partnership, and individual taxpayers.<sup>1</sup>

This tax alert summarizes the significant elements of the Notice and provides some taxpayer considerations.

### Guidance for C corporations

In the Notice, the AL DOR states that for corporate taxpayers, the IRC Section 965 repatriation income “is being reported separately for federal purposes (not on the federal return),” even though the underlying repatriation income is “still considered a component of federal taxable income.”<sup>2</sup> As a result, the Notice provides specific instruction on how to report federal repatriation income for Alabama income tax purposes.

For Alabama corporate taxpayers, the Notice provides that items of income/expense related to IRC Section 965 that are reported on the federal “IRC 965 Transition Tax Statement” must be reported on Schedule A of the Alabama Form 20C in the following manner:

- Any items of IRC Section 965 income must be reported on Alabama Schedule A, line 9, Form 20C (Other Additions), along with a brief description of the source of income.
- Any items of IRC Section 965 expense must be reported on Schedule A, line 23 or 24, Form 20C (Other Subtractions), with a brief description of the expense.
- IRC Section 965 income (net of related deductions) may be offset by a dividends received deduction (DRD) if the corporate taxpayer reporting the deemed dividend owns more than 20% of the controlled foreign corporation from which the deemed dividend is received. If claiming this DRD, the Notice indicates that a statement should be attached to the return which supports the amount claimed on Schedule A, line 18 of the Form 20C.<sup>3</sup>
- The Notice also explains that Alabama will require a copy of the federal “IRC 965 Transition Tax Statement” for documentation.

Generally, this methodology aggregates Alabama taxable income associated with IRC Section 965 income with other Alabama taxable income, and no separate payment is required for Alabama tax attributable to IRC Section 965 income.<sup>4</sup>

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<sup>1</sup> Notice: IRC Section 965 – Guidance for Corporate Filers, Partnerships, S Corporations, and Individual Taxpayers, April 27, 2018, available [here](#).

<sup>2</sup> *Id.*

<sup>3</sup> The DRD statement attached to the return is required to provide the name, taxpayer ID and ownership interest of the controlled foreign corporation from which the IRC Sec. 965 deemed dividend was received.

<sup>4</sup> The Alabama DOR has not yet addressed the potential apportionment implications of IRC Section 965 income.

### **Guidance for partnerships**

The Notice explains that because the “Alabama Form 65 is patterned closely after the Federal Form 1065,” the reporting requirements for IRC Section 965 income and expense for Alabama partnerships “mirrors” the partnership’s federal reporting.<sup>5</sup> Therefore, for partnerships IRC Section 965 income must be reported on Alabama Form 65, Schedule K, line 11, Other Income. Any deductions related to IRC Section 965 are to be reported on Schedule K, line 15, Other Deductions.<sup>6</sup>

The Notice does not directly address partnerships that file Alabama Nonresident Composite Payment Returns, Alabama Form PTE-C, on behalf of nonresident individual taxpayers. However, the Notice’s instruction to include IRC Section 965 income on Alabama Form 65 Schedule K, line 11, and IRC § 965 deductions on Schedule K, line 15, appears to result in IRC Section 965 income being included in the Alabama composite tax base with no representation of the IRC Section 965 deductions. As a consequence, it appears that nonresident partners impacted in this manner will need to file Alabama nonresident individual tax returns to claim IRC Section 965 deductions flowing through the partnership and potentially receive refunds of Alabama composite tax.

### **Guidance for S-Corporations and individuals**

The Notice explains that the Alabama tax treatment of S corporations and individuals is similar in that IRC Section 965 will not apply if an S corporation or individual is a direct shareholder of a foreign corporation that is subject to the provisions of IRC Section 965.<sup>7</sup> However, Alabama individual taxpayers will be required to report any flow through IRC Section 965 income by virtue of owing an interest in a partnership with direct ownership in foreign corporations that may be subject to IRC Section 965 provisions.<sup>8</sup> As a result, for individuals, taxable income reported for federal income tax purposes may be different than Alabama taxable income. The Notice states that such differences should be disclosed on the Alabama individual income tax return.<sup>9</sup>

### **Considerations**

Taxpayers who believe they may be impacted by this Notice are advised to consult with their Alabama tax advisors for further assistance.

## **Contacts:**

If you have questions regarding this Notice issued by the Alabama Department of Revenue or other Alabama tax matters, please contact any of the following Deloitte Tax professionals:

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<sup>5</sup> Notice: IRC Section 965. April 27, 2018

<sup>6</sup> *Id.*

<sup>7</sup> *Id.*

<sup>8</sup> The AL DOR’s reasoning for this difference in treatment between direct shareholder interests versus indirect shareholder interests through a partnership is not provided in the Notice.

<sup>9</sup> Notice: IRC Section 965. April 27, 2018

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