February 9, 2024

Internal Revenue Service
CC:PA:LPD:PR (Notice 2023-80)
Room 5203
P.O. Box 7604
Ben Franklin Station
Washington, DC 20044

Response to Request for Comments on Notice 2023-80 – Guidance Regarding the Foreign Tax Credit and Dual Consolidated Losses in Relation to the GloBE Model Rules, and Extension and Modification of Temporary Relief in Notice 2023-55

Dear Office of Associate Chief Counsel (International):

We appreciate the opportunity to comment on the rules described in Notice 2023-80 ("the Notice").

Forte International Tax, LLC is an international tax software and services firm focused on global tax analysis and reporting. Our firm advises numerous clients on topics that are addressed in the Notice, and we are grateful for the government's efforts to provide guidance in the uniquely challenging issues that will arise in coordinating US and foreign rules relating to the implementation of Pillar Two.

Section 1 – Overview

The Notice's Overview Section lays out the GloBE Model Operating Rules in the following order of priority: (1) Covered Taxes (other than Controlled Foreign Company Tax Regimes ("CFC Tax Regimes") and certain cross-border taxes); (2) QDMTT; (3) CFC Tax Regimes and certain other cross-border taxes; (4) IIR; and (5) UTPR. Thus, a QDMTT is computed without regard to taxes paid pursuant to a CFC Tax Regime.

By following this ordering, US CFC taxes are not impacted by taxes imposed under an IIR and UTPR, and calculation circularity is avoided. Otherwise, if taxes under an IIR or a UTPR were included in a constiuent entity's tested income, US taxable income or if a US foreign tax credit was allowed, calcuation circularirty may result if the net amount of CFC taxes were impacted. Therfore, we suggest the US treatment of an IIR or UTPR tax should not be included tested income, US taxable income and a foreign tax credit should not be allowed.

Section 2 – GloBE Model Rules and the Foreign Tax Credit

In adherence to the GloBE ordering rules described above, the Notice makes a clear distinction between a QDMTT, which is not a Final Top-up Tax, and IIR and UTPR which meet the definition of Final Top-up Taxes. It accomplishes this by defining a Final Top-up Tax as follows:

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> A foreign income tax (tested tax) is a final top-up tax if, in computing the tested tax, the foreign tax law takes into account: (a) the amount of tax imposed on the direct or indirect owners of the entity subject to the tested tax by other countries (including the United States) with respect to the income subject to the tested tax, or (b) in the case of an entity subject to the tested tax on income attributable to its branch in the foreign country imposing the tested tax, the amount of tax imposed on the entity by its country of residence with respect to such income.

With respect to its US treatment, a QDMTT is not a Final Top-up Tax because it does not take into account any US CFC taxes. On the contrary, IIR and UTPR taxes are final Top-up Taxes if they do take into account US CFC taxes.

We do not take exception to this definition, because it conforms with the GloBE ordering rules and does not in itself create calculation circularity.

However, we do not agree with the inclusion of Final Top-up Taxes in tested income or in the US shareholders' Section 78 gross-up without the allowance of a foreign tax credit. As an alternative, we propose a rule that specifically allocates any Final Top-up taxes to a Constituent Entity's Section 959(c)(3) earnings and profits. As well, we propose that this allocation would be made as an adjustment to the Constituent Entity's earnings and profits at the end of its taxable year, such that it does not impact any calculations relevant to the taxable year to which those taxes relate.

This approach eliminates computational circularity, and properly adjusts the Constituent Entity's earnings and profits for the economic cost of the Final Top-up tax. Distributions of 959(c)(3) earnings and profits are subject to the Section 245A dividends received deduction and any related foreign income taxes are non-creditable.

Additional Concerns with the Notice's Section 78 Treatment

If the decision is taken to retain the section 78 gross up treatment for Final Top-up Taxes, there is a host of technical issues that the Notice does not address. The income that results from section 78 treatment has to be basketed under section 904 and will increase the FTC limitation in the category to which it is allocated. The general rule of Treas. Reg. 1.861-20 concerning the allocation of taxes provides that:

> A foreign income tax (other than certain in lieu of taxes described in paragraph (h) of this section) is allocated and apportioned to the statutory and residual groupings that include the items of foreign gross income included in the base on which the tax is imposed. Each such foreign income tax (that is, each separate levy) is allocated and apportioned separately under the rules in paragraphs (c) through (f) of this section.

When section 78 turns the foreign tax into income, the income is presumably allocated to the same section 904(d) category that the tax would have been allocated if it were creditable.

In Section 2.03, the Notice provides that the amount of tax imposed under an IIR, UTPR, or QDMTT is computed separately from any other levy imposed by a foreign country. This is

intended to ensure consistent treatment of an IIR, UTPR, and QDMTT regardless of the manner in which a foreign country enacts an IIR, UTPR, or QDMTT under its foreign tax law.

Thus, if an IIR is imposed on passive income, the gross up would presumably be treated as passive income. This would suggest that IIR and UTPR taxes have to be allocated to the constituent entities in order to determine the correct section 904 treatment of the section 78 amount.

Additional QDMTT Allocation Key Guidance May be Helpful

The mechanics of the Notice's QDMTT Allocation Key results in each Low-Taxed Constituent entity within the same jurisdiction having the same overall effective tax rate for US tax purposes. Further guidance should make clear that this rule should not conflict with the allocation and apportionment of income taxes for foreign tax credit purpose as prescribe by Treas. Reg. 1.861-20.

Section 3 – GloBE Model Rules and Dual Consolidated Losses

With regard to the DCL rules, it is clear that Congress intended to prevent the double utilization of losses in multiple countries through tax consolidation. However, measuring ETR on the basis of the net income in a country (GloBE Rules) is not the kind of double benefit that the DCL rules sought to curtail.

Pillar Two is in the nature of an anti-abuse rule. To scale back the application of an anti-abuse rule on the basis of multi-entity netting does not constitute double loss utilization. To treat such a scale-back of an anti-abuse rule as double loss utilization would be to extend the original scope of the DCL rules in a way that Congress could not have foreseen. This is the kind of change that should be affected through legislation, if at all.

Conclusion

In summary, we recommend that Final Top-up Taxes should not result in calculation circularity for the income tax years to which they relate. To accomplish this, we suggest a rule that specifically allocates those taxes to Section 959(c)(3) earnings as of the end of the low-taxed constituent entity's computational tax year.

We thank you for the opportunity to provide comments on Notice 2023-80.

Sincerely,

Forte International Tax, LLC