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IRS Issues Regulations on Transactions Designed to Artificially Generate Foreign Tax Credits

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WASHINGTON — The Internal Revenue Service and Treasury Department today announced the release of proposed regulations that would disallow foreign tax credits for foreign taxes purportedly paid in connection with certain artificially engineered, highly structured transactions.

Foreign tax credits are designed to relieve U.S. taxpayers from double taxation of their foreign source income. Transactions addressed by the regulations, in contrast, are structured so that a U.S. taxpayer voluntarily subjects itself to foreign tax where an ordinary business transaction generally would result in little or no foreign tax paid by the U.S. taxpayer.

"The proposed regulations complement the vigorous enforcement efforts of the IRS to identify and, in appropriate cases, to challenge the tax benefits claimed in these foreign tax credit generator transactions under principles of existing law," said IRS Chief Counsel Donald L. Korb.

The significant impact of these transactions on the U.S. tax base was brought to the attention of the IRS by members of the Joint International Tax Shelter Information Centre (JITSIC). JITSIC is an information exchange arrangement under which the U.S., the U.K., Canada, and Australia exchange information bilaterally on tax avoidance schemes.

The IRS is aggressively pursuing cases uncovered through JITSIC or other sources involving inappropriate claims of foreign tax credits. Foreign tax credit abuse is among the IRS's top compliance concerns for large corporate taxpayers.

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