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subject: Section 4960 Excise Tax Refund Claims

This Generic Legal Advice Memorandum (GLAM) responds to your request for assistance regarding taxpayers' refund claims with respect to the excise tax on excess remuneration under Internal Revenue Code section 4960. This GLAM may not be used or cited as precedent. All references herein are to the Internal Revenue Code (the Code) and Income Tax Regulations, unless otherwise noted.

ISSUES

1. In circumstances in which a covered health insurance provider (CHIP) within the meaning of section 162(m)(6)(C) and an applicable tax-exempt organization (ATEO) within the meaning of section 4960(c)(1) ("Taxpayer") are part of the same affiliated group of organizations, whether remuneration paid to a covered employee of Taxpayer in excess of the $500,000 deduction limit under section 162(m)(6) is taken into account for purposes of calculating the excise tax on excess remuneration under section 4960(a)(1) with respect to Taxpayer.

2. If such remuneration is taken into account for purposes of calculating the excise tax, whether reliance on the reasoning in CCA 201752008 (December 4, 2017) (2017 CCA) constitutes a reasonable, good faith interpretation of the statute.

CONCLUSIONS

1. Yes, remuneration paid by Taxpayer is taken into account for purposes of calculating the excise tax under section 4960, because Taxpayer did not claim a deduction for the remuneration and no deduction was disallowed by reason of section 162(m).

2. Reliance on the reasoning in the 2017 CCA does not constitute a reasonable, good faith interpretation of section 4960. The 2017 CCA concluded that a portion of the $500,000 deduction limitation under section 162(m)(6) must be allocated to a tax-exempt taxpayer that is a member of an affiliated group that includes a CHIP. However, this conclusion was incorrect, because a tax-exempt organization may not claim a deduction for remuneration paid that is allocable to tax-exempt income, and thus such remuneration is not applicable individual remuneration under section 162(m)(6). More importantly, Taxpayer's position is inconsistent with the plain language of section 4960(c)(6), which requires that a deduction be disallowed by reason of section 162(m), because no amount of remuneration was disallowed by reason of section 162(m)(6). Further, Taxpayer's position is inconsistent with the legislative history, which explains that Congress intended to level the playing field between publicly held corporations and tax-exempt entities by imposing an excise tax on excess remuneration paid by tax-exempts. Under Taxpayer's position, any ATEO that has a CHIP as a member of an aggregated group of which it is a member would never owe any excise tax even though no deduction has been disallowed by reason of section 162(m).

FACTS

In order to respond to your request for advice on this recurring issue, we have developed the following hypothetical scenario to illustrate and clarify our position.

Taxpayer is a tax-exempt organization under section 501(c)(3) and thus is an ATEO under section 4960(c)(1). Taxpayer is a member of an affiliated group of entities that includes a number of ATEOs and taxable entities, including a taxable entity that provides health insurance coverage as defined in sections 9832(b)(1) and (b)(2) and meets the definition of a CHIP under section 162(m)(6)(C)(i) and Treas. Reg. §1.162-31(b)(4). Taxpayer and its affiliated entities (collectively, the "Aggregated Group") are considered an aggregated group under Treas. Reg. §1.162-31(b)(2) and are considered a related group of organizations under Treas. Reg. §53.4960-1(i). During the years at issue, the covered employees performed services relating to the ATEO's tax-exempt purposes and no remuneration paid by the ATEO to such employees was allocated to its unrelated business activities and claimed as a deduction on its Form 990-T (*Exempt Organization Business Income Tax Return*). To the extent that taxable members of the Aggregated Group paid remuneration to applicable individuals who were also covered employees of the ATEO, the taxable entities applied the deduction limit under section 162(m)(6) with respect to the aggregate applicable individual remuneration paid to such employees.

Taxpayer filed Form 4720 for tax years 2018 through 2021, paying section 4960 excise tax, and subsequently filed refund claims seeking refund of all section 4960 excise tax paid for those tax years with respect to remuneration paid to its covered employees. Taxpayer asserts that remuneration paid by the ATEOs within the Aggregated Group in excess of $500,000 to covered employees of the ATEOs is not treated as remuneration under section 4960(c)(6) for purposes of calculating the excise tax under section 4960. Taxpayer further asserts that its exclusion of the remuneration paid by the ATEOs within the Aggregated Group in excess of $500,000 in calculating the excise tax under section 4960 is based on the advice set forth in the 2017 CCA.

LAW

Section 4960 Authorities

Section 4960(a)(1) imposes a 21% excise tax on the sum of any remuneration paid by an ATEO to a covered employee in excess of $1 million plus any excess parachute payments made to the covered employee.

Section 4960(c)(2) defines a covered employee as any employee (including any former employee) of an ATEO if the employee is one of the five highest compensated employees of the organization for the taxable year or was a covered employee of the organization (or any predecessor) for any preceding taxable year beginning after December 31, 2016.[1]

Section 4960(c)(4)(A) provides that remuneration paid by a related organization, including a related taxable organization, is treated as paid by the ATEO. Under Treas. Reg. § 53.4960-1(i), any person—taxable or tax-exempt—that controls or is controlled by the ATEO, or is controlled by one or more persons that control the ATEO, is a related organization. Control is measured by more than 50 percent ownership, or the ability to appoint more than 50 percent of the board of directors of the organization. To the extent that a related organization pays remuneration subject to the excise tax, section 4960(c)(4)(C) allocates liability for the tax based on the pro rata amount of remuneration paid by each organization.

Section 4960(c)(6), which coordinates section 4960 with the deduction disallowance rules under section 162(m), provides, "Remuneration the deduction for which is not allowed by reason of section 162(m) shall not be taken into account for purposes of this section."

Section 4960 was added to the Code by section 13602 of the Tax Cuts and Jobs Act, Pub. L. 115–97, 31 Stat. 2054. 2157 (2017). The legislative history explains the purpose of section 4960:

[1] Section 70416 of the One, Big, Beautiful, Bill Act revised the definition of covered employee. For taxable years beginning after December 31, 2025, a covered employee is any employee of an ATEO (or any predecessor) and any former employee of an ATEO (or predecessor) who was such an employee during any taxable year beginning after December 31, 2016.

> The Committee believes that tax-exempt organizations enjoy a tax subsidy from the Federal government because contributions to such organizations are generally deductible and such organizations are generally not subject to tax (except on unrelated business income). As a result, such organizations are subject to the requirement that they use their resources for specific purposes, and the Committee believes that excessive compensation (including excessive severance packages) paid to senior executives of such organizations diverts resources from those particular purposes. The Committee further believes that alignment of the tax treatment of excessive executive compensation (as top executives may inappropriately divert organizational resources into excessive compensation) between for-profit and tax-exempt employers furthers the Committee's larger tax reform effort of making the system fairer for all businesses.[2]

Thus, Congress recognized that tax-exempt employers generally do not pay income taxes or take deductions for compensation and sought to align the tax treatment of excessive compensation between for-profit and tax-exempt employers.

The legislative history directly addresses the treatment of deductions for remuneration disallowed by reason of the analogous $1 million limit on deductible compensation contained in section 162(m) of the Code: "[R]emuneration of a covered employee that is not deductible by reason of the $1 million limit on deductible compensation is not taken into account for purposes of the provision."[3]

Notice 2019-9 (2019-04 IRB 403) provided initial guidance on section 4960. Regarding section 4960(c)(6), Notice 2019-9 provided the following Q/A:

> Q-38: Does section 4960 apply to amounts to which section 162(m) applies?
>
> A-38: (a) In general. Remuneration paid by a publicly held corporation within the meaning of section 162(m)(2) to a covered employee within the meaning of section 162(m)(3) generally is taken into account for purposes of section 4960. Similarly, remuneration paid by a covered health insurance provider within the meaning of section 162(m)(6)(C) to an applicable individual within the meaning of section 162(m)(6)(F) generally is taken into account for purposes of section 4960. However, any amount of remuneration for which a deduction is not allowed by reason of section 162(m) is not taken into account for purposes of section 4960.
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> (b) Example. The following example illustrates the rules of this Q/A-38:

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[2] H.R. Rep. No. 115-409, at 332-34 (2017); *accord*, H.R. Rep. No. 115-466, at 491-93 (2017).
[3] *Id.* at 334.

> Example. Employee A is an officer of Corporation X. Corporation X is a related organization as described in Q/A-7 with respect to an ATEO. A is also a covered employee of the ATEO. A receives compensation of $1.5 million from X, of which $500,000 is nondeductible by reason of section 162(m)(1). The amount of deduction disallowed under section 162(m) ($500,000) is not treated as remuneration for purposes of section 4960. However, the remuneration paid by X that is not disallowed by reason of section 162(m)(1) ($1 million) is treated as remuneration for section 4960 purposes.

On June 11, 2020, the Department of the Treasury (Treasury Department) and the Internal Revenue Service (IRS) published proposed regulations under section 4960 in the Federal Register (85 FR 35746) (the proposed regulations). The proposed regulations provided the following:

> (f) Coordination with section 162(m)—(1) In general. Remuneration paid by a publicly held corporation within the meaning of section 162(m)(2) to a covered employee within the meaning of section 162(m)(3) generally is taken into account for purposes of this section. Similarly, remuneration paid by a covered health insurance provider within the meaning of section 162(m)(6)(C) to an applicable individual within the meaning of section 162(m)(6)(F) generally is taken into account for purposes of this section. However, any amount of remuneration for which a deduction is disallowed by reason of section 162(m) is not taken into account for purposes of determining the amount of remuneration paid for a taxable year. Thus, if an amount of remuneration would be treated as paid under this section and a deduction for that amount is otherwise available but disallowed under section 162(m), that remuneration is not taken into account for purposes of determining the amount of remuneration paid for the taxable year under this section.
>
> (2) Five highest-compensated employees. Solely for purposes of determining an ATEO's five highest-compensated employees under § 53.4960-1(d)(2), remuneration for which a deduction is disallowed by reason of section 162(m) is treated as paid by the ATEO in the applicable year in which the remuneration would otherwise be treated as paid under paragraph (c)(1) of this section.
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> (3) Example. The following example illustrates the rules of this paragraph (f). For purposes of this example, assume any entity referred to as “ATEO” is an ATEO, any entity referred to as “CORP” is not an ATEO, and that all entities use a calendar year taxable year.

> (i) Example (Remuneration disregarded because a deduction is disallowed under section 162(m) in the year of vesting)—(A) Facts. CORP 1 is a publicly held corporation described in section 162(m)(2) that is not a health insurance issuer described in section 162(m)(6)(C). CORP 1 and ATEO 1 are related organizations and ATEO 1 is not a member of CORP 1's affiliated group (as defined in section 1504 (determined without regard to section 1504(b)). Employee A is a covered employee described in section 162(m)(3) of CORP 1 and a covered employee of ATEO 1. In 2021, CORP 1 pays Employee A $1.5 million as salary and ATEO 1 pays Employee A $500,000 as salary. But for application of section 162(m), the amount paid is otherwise deductible by CORP 1. The amount of remuneration subject to the deduction limitation under section 162(m)(1) is $500,000, the amount by which the compensation paid by CORP 1 exceeds the $1 million deduction limitation described in section 162(m)(1).
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> (B) Conclusion. The $500,000 not deductible under section 162(m) is not taken into account for purposes of determining the amount of remuneration paid by ATEO 1. Thus, ATEO 1 is generally treated as paying $1.5 million of remuneration to Employee A for the 2021 taxable year ($1 million salary from CORP 1 + $500,000 salary from ATEO 1). However, for purposes of determining ATEO 1's five highest-compensated employees for the 2021 applicable year, ATEO 1 is treated as paying $2 million of remuneration to Employee A ($1 million salary from CORP 1 that is deductible under section 162(m) + $500,000 salary from CORP 1 that is not deductible under section 162(m) + $500,000 salary from ATEO 1).

The proposed regulations described the issues that were being considered with respect to the coordination of sections 162(m) and 4960. Those issues included circumstances in which it was not known at the time that remuneration was deferred whether the remuneration would be subject to the section 162(m) deduction limitation when it was paid and circumstances in which an employee of an ATEO becomes a covered employee of a related publicly held corporation or related CHIP after the year in which an amount is treated as excess remuneration but before the year the remuneration is deductible (subject to the disallowance under section 162(m)). The proposed regulations suggested possible approaches and requested comments.

On January 19, 2021, the Treasury Department and IRS published final regulations in the Federal Register (T.D. 9938, 86 FR 6219). The final regulations did not provide any additional guidance on the coordination of sections 162(m) and 4960. Instead, the final regulations reserved a section for future guidance and provided in the preamble that "[u]ntil that future guidance is issued, taxpayers may use a reasonable, good faith approach with respect to the coordination of sections 4960 and 162(m) in circumstances in which it is not known whether a deduction for the remuneration will be disallowed under section 162(m) by the due date (including any extension) of the relevant Form 4720."

In addition to the specific transition guidance for section 162(m) in the preamble to the final regulations quoted above, consistent with statements in Notice 2019-9 and the preamble to the proposed regulations, the preamble to the final regulations also provides a general standard regarding reasonable, good faith reliance:

> Until the applicability date of these final regulations, taxpayers may also base their positions upon a reasonable, good faith interpretation of the statute that includes consideration of any relevant legislative history. Whether a taxpayer's position that is inconsistent with Notice 2019-09, the proposed regulations, or these final regulations constitutes a reasonable, good faith interpretation of the statute generally will be determined based upon all of the relevant facts and circumstances, including whether the taxpayer has applied the position consistently and the extent to which the taxpayer has resolved interpretive issues based on consistent principles and in a consistent manner. Notwithstanding the previous sentence, the preamble to Notice 2019-09 describes certain positions that the Treasury Department and the IRS have concluded are not consistent with a reasonable, good faith interpretation of the statutory language, and the proposed regulations and these final regulations reflect this view.

<u>Section 162(m) Authorities</u>

Section 162(a)(1) allows a deduction for "all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered."

Section 162(m)(6)(A) limits the section 162(a)(1) deduction to $500,000 for a taxable year for applicable individual remuneration (AIR) and deferred deduction remuneration (DDR) attributable to services performed by an applicable individual for a CHIP.

Section 162(m)(6)(C)(i)(II) provides that the term "covered health insurance provider" means any employer that is a health insurance issuer (as defined in section 9832(b)(2)) and with respect to which not less than 25 percent of the gross premiums received from providing health insurance coverage (as defined in section 9832(b)(1)) is from minimum essential coverage (as defined in section 5000A(f)).

Section 162(m)(6)(C)(ii) provides that two or more persons who are treated as a single employer under sections 414(b), (c), (m), or (o) are treated as a single employer for purposes of section 162(m)(6). Treas. Reg. §1.162-31(b)(2) defines an "aggregated group" as one or more persons treated as a single employer under section 162(m)(6)(C)(ii).

Section 162(m)(6)(D) defines applicable individual remuneration:

> (D) Applicable individual remuneration. For purposes of this paragraph, the term "applicable individual remuneration" means, with respect to any applicable individual for any disqualified taxable year, the aggregate amount allowable as a deduction under this chapter for such taxable year (determined without regard to this subsection) for remuneration … for services performed by such individual (whether or not during the taxable year). Such term shall not include any deferred deduction remuneration with respect to services performed during the disqualified taxable year.

Section 162(m)(6)(E) defines deferred deduction remuneration:

> (E) Deferred deduction remuneration. For purposes of this paragraph, the term "deferred deduction remuneration" means remuneration which would be applicable individual remuneration for services performed in a disqualified taxable year but for the fact that the deduction under this chapter (determined without regard to this paragraph) for such remuneration is allowable in a subsequent taxable year.

Section 162(m)(6)(F) provides that an applicable individual, with respect to any covered health insurance provider for any disqualified taxable year, is any individual (i) who is an officer, director, or employee in such taxable year, or (ii) who provides services for or on behalf of such covered health insurance provider during such taxable year.

Treas Reg. §1.162-31(a) describes the meaning of the term "otherwise deductible" as used elsewhere in the regulations under section 162(m):

> Paragraph (e) of this section sets forth rules on how the deduction limit applies to AIR and DDR that is otherwise deductible under chapter 1 of the Internal Revenue Code (Code) but for the deduction limitation under section 162(m)(6) (referred to in this section as remuneration that is otherwise deductible).

Treas. Reg. §1.162-31(e)(4)(i) provides that compensation paid by members of an aggregated group is combined for purposes of applying the $500,000 deduction limit:

> The total combined deduction for AIR and DDR attributable to services performed by an applicable individual in a disqualified taxable year allowed for all members of an aggregated group that are covered health insurance providers for any taxable year is limited to $500,000. Therefore, if two or more members of an aggregated group that are covered health insurance providers may otherwise deduct AIR or DDR attributable to services performed by an applicable individual in a disqualified taxable year, the AIR and DDR otherwise deductible by all members of the

> aggregated group is combined, and the deduction limitation is applied to the total amount.

Treas. Reg. §1.162-31(e)(4)(ii) provides for proration of the deduction limitation:

> If the total amount of AIR and DDR attributable to services performed by an applicable individual in a disqualified taxable year that is otherwise deductible by two or more members of an aggregated group in any taxable year exceeds the $500,000 deduction limit (as reduced by previously deductible AIR or DDR, if applicable), the deduction limit is prorated based on the AIR or DDR otherwise deductible by the members of the aggregated group in the taxable year and allocated to each member of the aggregated group.

CHIEF COUNSEL ADVICE 201752008

The 2017 CCA responded to questions regarding application of the $500,000 deduction limitation under section 162(m)(6) in circumstances in which an applicable individual receives AIR in a taxable year from both a taxable CHIP and a tax-exempt organization that are members of the same aggregated group.

Specifically, the 2017 CCA provided advice on allocating the section 162(m)(6) deduction limitation between two members of an aggregated group that included a tax-exempt hospital (Corporation Y) and a CHIP (Corporation X). The central issue was whether remuneration paid by Corporation Y is taken into account for purposes of allocating the $500,000 deduction limitation between X and Y even though Y is a tax-exempt entity, and as such cannot take a deduction for remuneration paid to employees (except to the extent such remuneration is allocable to any unrelated business taxable income). Counsel concluded that remuneration paid by a tax-exempt entity engaged in a related or unrelated trade or business is considered “otherwise deductible” regardless of whether the entity may use the deduction.

The 2017 CCA applied Treas. Reg. § 1.162-31(e)(4)(ii), which provides that the deduction limit is prorated based on the AIR “otherwise deductible” (defined in Treas Reg. § 1.162-31(a) as deductible but for the operation of section 162(m)(6)) by the members of the aggregated group in the taxable year and allocated to each member of the aggregated group. This section of the regulations interprets section 162(m)(6)(D), which provides that AIR for any disqualified taxable year is “the aggregate amount allowable as a deduction under this chapter for such taxable year (determined without regard to [section 162(m)]) for remuneration . . . for services performed by such individual.” Thus, the central issue addressed in the 2017 CCA was whether AIR is considered allowable without regard to section 162(m) under chapter 1 by a tax-exempt organization that is a member of an aggregated group. The 2017 CCA concluded that AIR paid by a tax-exempt organization is considered “otherwise deductible”:

> Neither § 162(m)(6) nor the regulations thereunder provide an exception for tax-exempt entities that are members of an aggregated group. Remuneration paid by a tax-exempt entity engaged in a related or unrelated trade or business is considered otherwise deductible regardless of whether the entity may use the deduction (for example, regardless of whether the entity has taxable income, such as unrelated business taxable income, against which the deduction may be taken).

Section 512 Authorities

Section 512(a)(1) provides that the term "unrelated business taxable income" means the gross income derived by any organization from any unrelated trade or business (as defined in section 513) regularly carried on by it, less the deductions allowed under chapter 1 of the Code which are directly connected with the carrying on of such trade or business, both computed with the modifications provided in subsection (b).

Treas. Reg. §1.512(a)-1(a) clarifies that to be deductible in computing unrelated business taxable income, expenses not only must qualify as deductions allowed by chapter 1 of the Code, but also must be directly connected with the carrying on of unrelated trade or business. To be directly connected with the conduct of unrelated business for purposes of section 512, an item of deduction must have proximate and primary relationship to the carrying on of that business.

Treas. Reg. §1.512(a)-1(c) provides that where personnel are used both to carry on exempt activities and to conduct unrelated trade or business activities, expenses and similar items attributable to such personnel (as, for example, items of salary) shall be allocated between the two uses on a reasonable basis.

ANALYSIS AND CONCLUSION

Taxpayer is described in section 501(c)(3) and was tax-exempt during the years at issue. Taxpayer was not subject to the deduction limitation under section 162(m)(1) because it was not a publicly-held corporation or affiliated with one. Taxpayer did not (and could not) claim any deductions for remuneration allocable to its tax-exempt income.[4] However, Taxpayer asserts that all remuneration paid to its covered employees in excess of $500,000 should be deemed disallowed by reason of section 162(m)(6), even though it was not, in fact, disallowed.

The distinction between the terms "allowable," as used in section 162(m)(6)(D) and "allowed," as used in section 4960(c)(6), is significant. Section 162(m)(6)(D) defines

[4] However, if a covered employee, who was also an applicable individual under section 162(m)(6), performed services relating to Taxpayer's unrelated trade or business, then Taxpayer would have properly allocated a portion of its remuneration paid to such employee as a deduction from unrelated business income under section 512(a)(1), In that case, part of such deduction would have been disallowed by reason of section 162(m)(6), and such amount properly would not be taken into account as remuneration for section 4960 purposes by reason of section 4960(c)(6).

applicable individual remuneration as “the aggregate amount *allowable* as a deduction under this chapter for such taxable year (determined without regard to [section 162(m)] (emphasis added). Section 4960(c)(6) provides that “[r]emuneration the deduction for which is not *allowed* by reason of section 162(m) shall not be taken into account for purposes of this section” (emphasis added). The courts and the Code distinguish between deductions that are “allowable” versus deductions that are “allowed”; those terms are not synonymous.

Virginian Hotel Corp v. Helvering, 319 U.S. 523 (1943), addressed the determination of the correct amount of depreciation to be deducted in calculating basis in property. The statute in effect during the taxable years at issue, provided that the basis upon which depreciation is to be "allowed" is the cost of the property with proper adjustments for depreciation "to the extent allowed (but not less than the amount allowable) under this Act or prior income tax laws." The Court held that a deduction is “allowed” if it is claimed by the taxpayer and not timely challenged by the Service, even if it is not properly “allowable” under the Code:

> Under our federal tax system, there is no machinery for formal allowances of deductions from gross income. Deductions stand if the Commissioner takes no steps to challenge them. Income tax returns entail numerous deductions. If the deductions are not challenged, they certainly are ‘allowed,’ since tax liability is the determined on the basis of the returns. Apart from contested cases, that is indeed the only way in which deductions are ‘allowed.’ Id. at 527.

Similarly, in Lenz v. Commissioner, 101 T.C. 260, 265 (1993), the court stated:

> ‘Allowable deduction’ generally refers to a deduction which qualifies under a specific Code provision whereas ‘allowed deduction’, on the other hand, refers to a deduction granted by the Internal Revenue Service which is actually taken on a return and will result in a reduction of the taxpayer's income tax.

Since Taxpayer did not (and could not) claim any deductions for remuneration attributed to its tax-exempt activities, Taxpayer did not pay any amount of “[r]emuneration the deduction for which is not allowed by reason of section 162(m).”

The purpose of section 4960(c)(6) is to avoid circumstances in which an amount is disallowed as a deduction under section 162(m) and is also taxed under section 4960. Therefore, it makes sense that Congress used the term “not allowed” in section 4960(c)(6) because Congress sought to avoid situations in which a deduction is disallowed under section 162(m) and the remuneration is also subject to the excise tax under section 4960. The legislative history makes this point explicit regarding the analogous limitation on deductions for compensation in excess of $1 million imposed on publicly held corporations by section 162(m)(1). Notice 2019-9 and the proposed and final regulations are clear that the phrase “not allowed by reason of section 162(m)” should be understood to mean that the deduction was actually disallowed by section 162(m). Otherwise, any related group of ATEOs and other entities that have a CHIP as a member of the aggregated group could avoid paying section 4960 excise tax on all remuneration paid to its covered employees. That result would be contrary both to the clear language of the statute and the congressional intent evident from the legislative history.

The legislative history of section 4960 notes that tax-exempt organizations generally are not subject to section 162(m), and the purpose of section 4960 is to level the playing field between taxable organizations and tax-exempt organizations with respect to the tax treatment of remuneration paid to highly compensated employees. In other words, Congress intended that employers be subject to either the excise tax or the deduction limitation on excess remuneration paid to highly compensated employees. They should not be able to avoid the excise tax entirely in circumstances in which a CHIP happens to be a member of the affiliated group, as Taxpayer asserts in its refund claims. Such an outcome would result in inconsistent treatment of substantially similar taxpayers and would be inconsistent with the purposes of section 4960 generally and the language of section 4960(c)(6).

Congressional intent here accords with the usual intent of coordination provisions in the Code—to avoid a double tax benefit (or, as here, a double tax detriment) for taxpayers. As the Supreme Court stated in *United States v. Skelly Oil Co.*, 394 U.S. 678, 684 (1969):

> [T]he Code should not be interpreted to allow [the taxpayer] 'the practical equivalent of double deduction,' *Charles Ilfeld Co. v. Hernandez*, 292 U.S. 62, 68 (1934), absent a clear declaration of intent by Congress. See *United States v. Ludey*, 274 U.S. 295 (1927).

Based upon the foregoing, remuneration paid by the Taxpayer in excess of the $500,000 deduction limit under section 162(m)(6) to its covered employees is taken into account for purposes of calculating the excise tax on excess remuneration under section 4960(a)(1).

The 2017 CCA Was Incorrect

The 2017 CCA advised that remuneration paid by a tax-exempt entity engaged in a related or unrelated trade or business is considered applicable individual remuneration, and thus is taken into account for purposes of allocating the $500,000 deduction limitation under section 162(m)(6), regardless of whether the entity has taxable income, such as unrelated business taxable income, against which the deduction may be taken. The 2017 CCA was incorrect with respect to its advice regarding whether remuneration allocable to tax-exempt income is treated as applicable individual remuneration, and thus taken into account for purposes of pro rating the $500,000 deduction limit under section 162(m)(6).

Treas. Reg. §1.162-31(e)(4)(i) provides that the total combined deduction for AIR and DDR attributable to services performed by an applicable individual in a disqualified taxable year allowed for all members of an aggregated group that are covered health insurance providers for any taxable year is limited to $500,000. The purpose of Treas. Reg. §1.162-31(e)(4)(ii) is to allocate the $500,000 deduction limit pro-rata based on applicable individual remuneration that is subject to the limitation under section 162(m)(6). Tax-exempt entities do not take remuneration deductions, except as permitted under section 512 for remuneration expenses allocable to unrelated business taxable income. Thus, remuneration that is allocated to a tax-exempt member of an aggregated group that is not deductible against unrelated business taxable income results in the loss to the aggregated group of the full $500,000 deduction limit. This in substance would result in a CHIP receiving less than the $500,000 remuneration deduction permitted under the statute. Such an interpretation would be inconsistent with the purposes of section 162(m)(6), which is to impose a deduction limit of $500,000 against taxable income of an aggregated group.

Reasonable, Good Faith, Interpretation

The remaining issue is whether Taxpayer's interpretation as reflected in its refund claims is a reasonable, good faith interpretation of section 4960. The preamble to the final regulations under section 4960 provides that "[u]ntil the applicability date of these final regulations, taxpayers may also base their positions upon a reasonable, good faith interpretation of the statute that includes consideration of any relevant legislative history." For the reasons explained below, Taxpayer's position does not qualify as a reasonable, good faith interpretation of section 4960.

The phrase "reasonable, good faith interpretation" is not defined in Notice 2019-9 or in the proposed or final regulations. In *Kraft Foods N. Am., Inc. v. United States*, 58 Fed. Cl. 507 (2003), the Court of Claims interpreted the meaning of a substantially similar phrase in the preamble of proposed regulations under section 3121(v)(2): "reasonable, good faith interpretation of section 3121(v)(2), taking into account pre-existing guidance." Like Taxpayer here, the taxpayer in *Kraft* sought refunds for taxes previously paid based on an interpretation of the applicable statute. The question for the court was whether the taxpayer's position was a reasonable, good faith interpretation of the statute. The court looked at what IRS guidance was available to the taxpayer when it filed amended returns seeking the tax refunds. *Id*. at 511. The court found that the IRS had issued a notice and proposed regulations specifically addressing the taxpayer's position, and the taxpayer acted unreasonably by ignoring the most authoritative guidance available at the time it filed the refund claims. *Id*. at 512.

The question of whether Taxpayer's claim for refunds is based on a reasonable, good faith interpretation of section 4960 is based on the guidance available to Taxpayer at the time it filed its refund claims. *Kraft*, 58 Fed. Cl. at 511. This includes the statute itself, any published guidance and the legislative history. In considering its position, Taxpayer had the text of TCJA, signed into law on December 22, 2017, and the text of the TCJA legislative history, published on November 13 and December 15, 2017. Taxpayer also had Notice 2019-9, and the proposed and final regulations.

Taxpayer's interpretation is not a reasonable interpretation of the statute because it is inconsistent with the clear language of section 4960(c)(6), which applies only to deductions "not allowed by reason of section 162(m)." As Notice 2019-9 and the proposed and final regulations state, section 4960(c)(6) applies only to remuneration "disallowed by reason of section 162(m)." Taxpayer did not report any remuneration disallowed by section 162(m)(6) on its tax returns.

In addition, Taxpayer's interpretation is inconsistent with the legislative history, which is clear that the intent of section 4960(c)(6) is to avoid a double tax detriment that might otherwise apply to taxpayers that have a deduction disallowed under section 162(m) with respect to remuneration that is also taxed under section 4960 and to level the playing field for excessive compensation paid by public corporations and tax-exempt organizations. Under Taxpayer's position, an ATEO that has a CHIP as a member of its affiliated group would never owe any section 4960 tax under any circumstances. Such a position would not result in a level playing field between taxable entities and tax-exempt entities.

Taxpayer asserts the 2017 CCA supports its position that remuneration in excess of $500,000 paid by Taxpayer and its related ATEOs is not taken into account as remuneration for purposes of section 4960(a)(1). The 2017 CCA was made available to taxpayers after the TCJA was passed (December 29, 2017) but was written and issued on December 4, 2017, prior to the enactment of the TCJA. Thus, the 2017 CCA did not and could not have considered section 4960 because it was written and issued before the TCJA was signed into law. Because it did not address section 4960, it cannot be considered the most authoritative guidance available with respect to interpreting the coordination between sections 162(m) and 4960.

Nevertheless, Taxpayer seeks to extrapolate the language about whether remuneration allocable to tax-exempt income is "otherwise deductible" from the 2017 CCA to the coordination rule under section 4960. Regardless of the reasoning of the 2017 CCA, the standard under section 4960(c)(6) is not whether the remuneration was otherwise deductible, but whether the deduction was disallowed by reason of section 162(m).

A CCA has no precedential value, and while a CCA may provide insight into the IRS's thinking on certain issues, it does not constitute an authoritative source, especially in a situation such as this one when it doesn't address the statute in question. In conclusion, Taxpayer's position based on the 2017 CCA cannot constitute a "reasonable, good faith interpretation" of section 4960, as the 2017 CCA was written prior to the enactment of section 4960 and does not address section 4960. Taxpayer, like the taxpayer in *Kraft*, acted unreasonably by ignoring the most authoritative guidance available: the Code , Notice 2019-9, and the proposed and final regulations. 58 Fed. Cl. at 512. Finally, the safe harbor included in the preamble to the final regulations explicitly alerted taxpayers that any "reasonable, good faith interpretation of the statute" must include "consideration of any relevant legislative history." Taxpayer's position based on the 2017 CCA is clearly contrary to the legislative history, and in light of the existing authoritative guidance, it was not reasonable to rely on the 2017 CCA. For the foregoing reasons, Taxpayer's position as reflected in its refund claims is not a reasonable, good faith interpretation of the statute.

Please call the EC branch at (202) 317-4572 if you have any further questions.