

GIL 24-19-1 Income Tax: Section 965 Transition Tax for Tax Year 2017

Supersedes GIL 24-18-1, issued December 21, 2018

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September 13, 2019

Dear XXXX,

This guidance is in response to several inquiries regarding Nebraska's treatment of Internal Revenue Code Section 965 repatriation income. Based on the information provided in those requests we are providing this General Information Letter (GIL), which clarifies and supersedes GIL 24-18-1.

GILs address general questions; provide analysis of issues; and direct taxpayers to the Nebraska statutes, DOR regulations, revenue rulings, or other sources of information to help answer a question. A GIL is a statement of current DOR policy, and taxpayers may rely on DOR to follow the principles or procedures described in a GIL until it is rescinded or superseded. You may also find current regulations, revenue rulings, information guides, taxpayer rulings, and other GILs at revenue.nebraska.gov that may be helpful to you.

The Tax Cuts and Jobs Act (TCJA), enacted in 2017, amended IRC § 965. The amendment required taxpayers to include in income an amount (IRC § 965(a) inclusion amount) based on the accumulated post-1986 deferred foreign income of certain foreign corporations that they own either directly or indirectly through other entities. Other taxpayers may have inclusions in income under IRC § 965(a) due to ownership of deferred foreign income corporations (DFICs) through U.S. shareholder pass-through entities. IRC § 965 also allows for a deduction (IRC § 965(c) deduction).

Nebraska law conforms to the IRC § 965 provisions, except for the elections to pay the tax in installments or to defer the tax.

IRC § 965(a) Inclusion Income on Nebraska Returns.

Any IRC § 965(a) income included in the taxpayer's federal return must also be included in its Nebraska return. Report the IRC § 965(a) income on the appropriate lines of the Nebraska returns as follows:

C corporations: Line 8, Nebraska Schedule A, Form 1120N.

S corporations: Line 6, Nebraska Schedule A, Form 1120-SN.

Partnerships: Line 7, Nebraska Schedule A, Form 1065N.

Individuals: An individual should not modify the federal adjusted gross income (AGI) reported to the IRS. Nebraska taxation begins with federal AGI, which includes the inclusion amount.

IRC § 965(c) deduction on Nebraska Returns.

Any IRC § 965(c) deduction allowed on the taxpayer's federal return may also be deducted on its Nebraska return. The taxpayer must attach a copy of the IRC § 965 Transition Tax Statement to the Nebraska return when filed. Report the IRC § 965(c) deduction on the appropriate Nebraska returns as follows:

C corporations: Line 18, Nebraska Schedule A, Form 1120N.

S corporations: Line 16, Nebraska Schedule A, Form 1120-SN.

Partnerships: Line 17, Nebraska Schedule A, Form 1065N.

Individuals: An individual cannot modify the federal AGI reported to the IRS. Nebraska taxation begins with federal AGI, which includes the deduction amount.

Foreign Dividends Deduction on Nebraska Returns.

Nebraska law allows a deduction from federal taxable income or federal adjusted gross income, to the extent so included, for any dividends or deemed dividends treated as foreign dividends under the IRC and related Treasury Regulations (Neb. Rev. Stat. § 77-2716(5)). Examination of the IRC, Treasury Regulations, and related Tax Court cases establish that the net IRC § 965 inclusion income (IRC § 965(a) inclusion – IRC § 965(c) deduction) is not a foreign dividend. Under the IRC, a dividend generally is a distribution of property out of its earnings and profits made by a corporation to its shareholders under specific rules. See I.R.C. § 316. Income recognized under IRC § 965(a) is added to subpart F income and does not meet the definition of dividend nor is it deemed a dividend in the IRC or related Treasury Regulations. Any dividend deduction claimed for the net IRC § 965(a) income will be disallowed.

Apportionment.

If the corporate taxpayer is taxable in both Nebraska and one or more other states, the income of the corporate taxpayer must be apportioned to Nebraska based on the Nebraska receipts as compared to all receipts as provided by Neb. Rev. Stat. §§ 77-2734.05 to 77-2734.15.

The realization of deferred earnings and profits of controlled foreign corporations since 1986 and the corresponding recognition of this income in a single year is a unique and non-recurring factual situation supporting a decision by the Tax Commissioner to allow special apportionment under the provisions of Neb. Rev. Stat. § 77-2734.15(2). The Tax Commissioner has determined that excluding IRC § 965(a) from a corporate taxpayer's sales factor altogether, or including this income in the sales factor numerator would produce incongruous results relative to other taxpayers. Therefore, for the last taxable year which begins before January 1, 2018 all corporate taxpayers must include the IRC § 965(a) income in their sales factor denominator, and exclude this income from their sales factor numerator. All other items of income must be apportioned according to the provisions of Neb. Rev. Stat. §§ 77-2734.01 through 77-2734.14 and the regulations adopted thereunder.

Amended Return.

An entity should file an amended return if it improperly reported its IRC § 965(a) income or improperly computed its sales factor. If an entity files an amended return by December 31, 2019, DOR will waive or abate any penalty or interest resulting from an entity's incorrect treatment of its IRC § 965(a) income on its 2017 Nebraska income tax return. Write "Amended pursuant to GIL 24-19-1" at the top of the amended return and DOR will automatically waive interest and penalty. There is no need to file a Form 21 or 21A to receive this relief.

For the Tax Commissioner

George Kilpatrick
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