



BDO Seidman, LLP  
Accountants and Consultants

August 2005

## Subject:

### IRS Issues Additional Guidance on Dividends Received Deduction For 965 Repatriations and Releases Form 8895

# International Tax Alert

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## Date\Timing:

Section 965 is elective for a single taxable year, which must be either the taxpayer's last taxable year beginning before October 22, 2004, or its first taxable year beginning after such date. The deduction for qualifying dividends is reported on Form 8895, which is attached to the corporation's tax return.

## Affecting:

Corporations which are U.S. shareholders of a controlled foreign corporation and which elect to claim the deduction

## New Guidance:

On August 19, 2005, the Service released Notice 2005-64, which is the third in a series of notices providing guidance on IRC § 965. Prior guidance was provided in Notice 2005-10, 2005-6 I.R.B. 474, and Notice 2005-38, 2005-22 I.R.B. 1100.

Notice 2005-64 provides additional guidance in the following areas:

- Identification of Cash Dividends – as explained in detail in section 3 of the Notice, a U.S. shareholder receiving cash from a partnership or disregarded entity or a cash distribution of previously taxed income (PTI) from a CFC that exceeds the cash dividends paid to the respective entity may specifically identify the portion of the cash received that is to be treated as the cash dividend for which the deduction may be claimed. Identification is made on Form 8895, Part V.

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## New Guidance:...(continued)

- Disallowance of Tax Credit and § 78 Gross Up - As explained in detail in section 4 of the Notice, § 965 does not modify the calculation of deemed paid taxes under § 902 and §960. Thus, tax and earnings pools are reduced by the amounts attributable to distributed earnings without regard to the application (or non-application) of the dividends received deduction. The § 78 gross up amount applies only to the amount of the dividend to which the election does not apply (i.e. taxes attributable to the remaining 15 percent).
- Treatment of Expenses Related to A Qualifying Dividend - In sections 5 and 6 of the Notice, it specifically lists expenses that that will be disallowed under § 965(d)(2). The Notice also addresses the treatment of various expenses with several examples.
- Minimum Taxable Income Amount – Section 7 of the Notice provides additional guidance on the provisions of § 965(e)(2), which require that the U.S. shareholder’s taxable income for the year of the dividend shall in no event be less than the nondeductible amount of the dividends received. Included in this section is guidance on the calculation and use of NOL’s for the year the dividend is received.
- Overall Foreign Losses and Separate Limitation Losses – Guidance on the effect of dividend payments on the OFL and separate limitation losses is set forth in section 8.
- Restrictions on Use of Credits to Offset Tax on Nondeductible CFC Dividends – Section 9 includes additional guidance on the availability of prior year minimum tax credits and foreign tax credits for use against the tax liability created by the minimum tax amount attributable to the nondeductible CFC dividends.
- “Other Guidance” – Section 10 addresses several other issues such as the applicability of general tax principles to § 965 planning (e.g. “substance-over-form,” etc.), the effect of dividend payments to partnerships or disregarded entities during made during the base period years on the base period amount, the definition of the United States. This section also provides for clarification and modification of various provisions of Notice 2005-10 and Notice 2005-38.

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