

Part III - Administrative, Procedural, and Miscellaneous

Implementation of Executive Order 13789 (Identifying and Reducing Tax Regulatory Burdens)

Notice 2017-38

I. INTRODUCTION

On April 21, 2017, President Donald J. Trump issued Executive Order 13789, a directive designed to reduce tax regulatory burdens. The order instructed the Secretary of the Treasury to review all “significant tax regulations” issued on or after January 1, 2016, and submit two reports, followed promptly by concrete action to alleviate the burdens of regulations that meet criteria outlined in the order. Specifically, the President directed the Secretary, in consultation with the Administrator of the Office of Information and Regulatory Affairs, to submit a 60-day interim report identifying regulations that (i) impose an undue financial burden on U.S. taxpayers; (ii) add undue complexity to the Federal tax laws; or (iii) exceed the statutory authority of the Internal Revenue Service (IRS).¹ The order further instructs the Secretary to submit a final report to the President by September 18, 2017, recommending “specific actions to mitigate the burden imposed by regulations identified in the interim report.”²

II. SCOPE OF THE TREASURY DEPARTMENT’S REVIEW

From January 1, 2016, through April 21, 2017, Treasury and the IRS issued 105 temporary, proposed, and final regulations.³ During this time period, Treasury and the IRS issued one regulation—under Section 385 of the Internal Revenue Code—that the Office of Management and Budget designated as significant pursuant to Executive Order 12866. Executive Order 13789 provides, however, that in determining whether a regulation is significant for the purpose of this review, past determinations made pursuant to Executive Order 12866 are not controlling.

Fifty three of the 105 regulations issued during the relevant review period are minor or technical in nature and generated minimal public comment. To ensure a comprehensive review, Treasury treated the remaining 52 regulations as potentially significant and reexamined all of them for the purpose of formulating the interim report.⁴

¹ Executive Order 13789 § 2(a) (2017).

² *Id.* § 2(b).

³ This number excludes the following Federal Register documents: (1) corrections to proposed, temporary, or final regulations; (2) notices of proposed rulemaking cross-referencing temporary regulations required pursuant to 26 U.S.C. § 7805(e)(1); (3) notices of proposed rulemaking issued on or after January 1, 2016, for which a subsequent final rule was issued on or before April 21, 2017; (4) notices relating to public hearings; (5) notices withdrawing prior notices of proposed rulemaking; and (6) non-tax regulations jointly issued by the IRS and other Departments of the Federal Government.

⁴ See <https://www.treasury.gov/resource-center/tax-policy/Pages/Executive-Orders.aspx> for a list of the regulations that were reviewed.

Based on that reexamination, Treasury has identified regulations that meet the criteria of the President's order and qualify as significant in view of the Presidential priorities for tax regulation outlined in Executive Order 13789.⁵

III. REGULATIONS IDENTIFIED FOR BURDEN REDUCTION

Treasury has concluded that the following eight regulations meet at least one of the first two criteria specified by Section 2 of Executive Order 13789. Consistent with the order, Treasury intends to propose reforms—potentially ranging from streamlining problematic rule provisions to full repeal—to mitigate the burdens of these regulations in a final report submitted to the President.

1. Proposed Regulations under Section 103 on Definition of Political Subdivision (REG-129067-15; 81 F.R. 8870)

These proposed regulations define a “political subdivision” of a State (e.g., a city or county) that is eligible to issue tax-exempt bonds for governmental purposes under Section 103 of the Internal Revenue Code. The proposed regulations require a political subdivision to possess three attributes: (i) sovereign powers; (ii) a governmental purpose; and (iii) governmental control. Commenters stated that the longstanding “sovereign powers” standard was settled law and had been endorsed by Congress, and additional limitations were unnecessary. Commenters also stated that the proposed regulations would disrupt the status of numerous existing entities and that it would be burdensome and costly for issuers to revise their organizational structures to meet the new requirements of the proposed regulations.

2. Temporary Regulations under Section 337(d) on Certain Transfers of Property to Regulated Investment Companies (RICs) and Real Estate Investment Trusts (REITs) (T.D. 9770; 81 F.R. 36793)

These temporary regulations amend existing rules on transfers of property by C corporations to REITs and RICs generally. In addition, the regulations provide additional guidance relating to certain newly-enacted provisions of the Protecting Americans from Tax Hikes Act of 2015, which were intended to prevent certain spinoff transactions involving transfers of property by C corporations to REITs from qualifying for nonrecognition treatment. Commenters expressed concern

⁵ See Executive Order 12866 § 3(f) (1993) (defining “significant regulatory action” to include, *inter alia*, “any regulatory action that is likely to result in a rule that may ... [r]aise novel ... policy issues arising out of ... the President’s priorities”). To assess “undue financial burden,” Treasury considered the degree to which the regulation at issue imposed compliance costs or resulted in tax liabilities that exceed the minimum required to achieve the relevant statutory objectives. To assess “undue complexity,” Treasury considered the extent to which the regulation at issue imposed new substantive, computational, or other requirements not required to achieve the relevant statutory objectives, or introduced rules that added uncertainty for taxpayers.

that the REIT spinoff rules could result in over-inclusion of gain in some cases, particularly where a large corporation acquires a small corporation that engaged in a Section 355 spinoff and the large corporation subsequently makes a REIT election.

3. Final Regulations under Section 7602 on the Participation of a Person Described in Section 6103(n) in a Summons Interview (T.D. 9778; 81 F.R. 45409)

These final regulations provide that persons described in Section 6103(n) of the Internal Revenue Code and Treas. Reg. §301.6103(n)-1(a) with whom the IRS contracts for services—such as outside economists, engineers, consultants, or attorneys—may receive books, papers, records, or other data summoned by the IRS and, in the presence and under the guidance of an IRS officer or employee, participate fully in the interview of a person who the IRS has summoned as a witness to provide testimony under oath. Commenters objected to the IRS’s ability to contract with outside attorneys and permit them to question witnesses under oath, and the U.S. Senate Finance Committee approved legislation in 2016 that would prohibit the IRS from delegating to third-party contractors the authority under Section 7602. Treasury will review these regulations as they concern the outside attorneys under contract with the IRS to participate in the taking of compulsory testimony under oath.

4. Proposed Regulations under Section 2704 on Restrictions on Liquidation of an Interest for Estate, Gift and Generation-Skipping Transfer Taxes (REG-163113-02; 81 F.R. 51413)

Section 2704(b) of the Internal Revenue Code provides that certain non-commercial restrictions on the ability to dispose of or liquidate family-controlled entities should be disregarded in determining the fair market value of an interest in that entity for estate and gift tax purposes. These proposed regulations would create an additional category of restrictions that also would be disregarded in assessing the fair market value of an interest. Commenters expressed concern that the proposed regulations would eliminate or restrict common discounts, such as minority discounts and discounts for lack of marketability, which would result in increased valuations and transfer tax liability that would increase financial burdens. Commenters were also concerned that the proposed regulations would make valuations more difficult and that the proposed narrowing of existing regulatory exceptions was arbitrary and capricious.

5. Temporary Regulations under Section 752 on Liabilities Recognized as Recourse Partnership Liabilities (T.D. 9788; 81 F.R. 69282)

These temporary regulations generally provide: (i) rules for how liabilities are allocated under Section 752 solely for purposes of disguised sales under Section 707 of the Internal Revenue Code; and (ii) rules for determining whether “bottom-dollar payment obligations” provide the necessary “economic risk of loss” to be

taken into account as a recourse liability. Commenters stated that the first rule was novel and would unduly limit the amount of partners' bases in their partnership interests for disguised sale purposes, which would negatively impact ordinary partnership transactions. Commenters were concerned that the bottom-dollar payment obligation rules would prevent many business transactions compared to the prior regulations and suggested their removal or the development of more permissive rules.

6. Final and Temporary Regulations under Section 385 on the Treatment of Certain Interests in Corporations as Stock or Indebtedness (T.D. 9790; 81 F.R. 72858)

These final and temporary regulations address the classification of related-party debt as debt or equity for federal tax purposes. The regulations are primarily comprised of (i) rules establishing minimum documentation requirements that ordinarily must be satisfied in order for purported debt among related parties to be treated as debt for federal tax purposes; and (ii) transaction rules that treat as stock certain debt that is issued by a corporation to a controlling shareholder in a distribution or in another related-party transaction that achieves an economically similar result. Commenters to the documentation rules criticized the financial burdens of compliance, particularly with respect to more ordinary course transactions. Commenters also requested a longer delay in the effective date of the documentation rules. Commenters to the final transaction rules criticized the complexity associated with tracking multiple transactions through a group of companies and the increased tax burden imposed on inbound investments.

7. Final Regulations under Section 987 on Income and Currency Gain or Loss With Respect to a Section 987 Qualified Business Unit (T.D. 9794; 81 F.R. 88806)

These final regulations provide rules for (i) translating income from branch operations conducted in a currency different from the branch owner's functional currency into the owner's functional currency, (ii) calculating foreign currency gain or loss with respect to the branch's financial assets and liabilities, and (iii) recognizing such foreign currency gain or loss when the branch makes a transfer of any property to its owner. Commenters on the regulations stated that the transition rule in the final regulations imposes an undue financial burden on taxpayers because it disregards losses calculated by the taxpayer for years prior to the transition but not previously recognized. Commenters also stated that the method prescribed by the final regulations for calculating foreign currency gain or loss was unduly complex and costly to comply with, particularly where the final regulations differ from financial accounting rules.

8. Final Regulations under Section 367 on the Treatment of Certain Transfers of Property to Foreign Corporations (T.D. 9803; 81 F.R. 91012)

Section 367 of the Internal Revenue Code generally imposes immediate or future U.S. tax on transfers of property (tangible and intangible) to foreign corporations,

subject to certain exceptions. These final regulations eliminate the ability of taxpayers under prior regulations to transfer foreign goodwill and going concern value to a foreign corporation without immediate or future U.S. income tax. Some commenters stated that the final regulations would increase burdens by taxing transactions that were previously exempt, noting in particular that the legislative history to Section 367 contemplated an exception for outbound transfers of foreign goodwill and going concern value. Commenters also stated that an exception should be provided for transfers of foreign goodwill and going concern value in circumstances that would not lead to an abuse of the exception.

IV. REQUEST FOR COMMENTS

Treasury is requesting comments on whether the regulations described in this notice should be rescinded or modified, and in the latter case, how the regulations should be modified in order to reduce burdens and complexity. Comments from the public are due by August 7, 2017. Comments should be submitted to: Internal Revenue Service, CC:PA:LPD:PR (Notice 2017-38), Room 5205, P.O. Box 7604, Ben Franklin Station, Washington, DC 20224. Alternatively, comments may be hand-delivered Monday through Friday between the hours of 8:00 a.m. to 4:00 p.m. to: CC:PA:LPD:PR (Notice 2017-38), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, DC. Comments may also be submitted electronically via the following e-mail address: Notice.Comments@irs.counsel.treas.gov. Please include Notice 2017-38 in the subject line of any electronic submissions. Comments will be available for public inspection and copying.

Pursuant to Executive Order 13777, *Presidential Executive Order on Enforcing the Regulatory Reform Agenda*, Treasury is responsible for conducting a broader review of existing regulations, including tax regulations beyond those addressed in this notice. In a Request for Information published on June 14, 2017 (82 F.R. 27217), Treasury invited public comment concerning regulations that should be modified or eliminated in order to reduce unnecessary burdens. Comments in response to the Request for Information are due by July 31, 2017. In addition, in Notice 2017-28, Treasury and the IRS invited public comment on recommendations for the 2017-2018 Priority Guidance Plan for tax guidance, including recommendations relating to Executive Order 13777. Taxpayers may submit recommendations for tax guidance at any time during the year.