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LB&I to Focus Audit Resources on Transition Tax and 'TCJA Planning'
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The IRS Large Business & International Division announced this week the launch of a new campaign targeting compliance with the so-called transition tax under section 965. The provision, enacted as part of the Tax Cuts and Jobs Act of 2017, required U.S. domestic companies to pay a one-time tax on all earnings previously deferred in their offshore subsidiaries.

Campaigns, initiated by LB&I in 2017, are an approach by which the Division concentrates its resources around specific issues of suspected non-compliance. Each time a new campaign is announced, LB&I outlines the strategies -- "treatment streams" -- it will apply in the area to improve compliance.

According to the LB&I website, the treatment streams to be utilized in the new section 965 campaign "will include conducting examinations as well as providing technical assistance to teams on 965, with a focus on identifying and addressing taxpayer populations with potential material compliance risk." Returns from tax years 2017 and 2018 will be selected for the inquiry.

A now-retired campaign, announced shortly after the transition tax was enacted, focused on taxpayer outreach to increase awareness of section 965 filing and payment obligations. Many taxpayers had filed their returns for 2017, the first year (for calendar year taxpayers) affected by section 965, before the IRS issued any guidance on the provision.

Press reports this week have suggested that the IRS is planning to focus on taxpayers' calculations of foreign subsidiary earnings and profits, as well as their split between cash and noncash E&P. Affected taxpayers should consider reviewing these calculations with outside advisors to identify any potential weaknesses and strategize how best to address them.

<u>'Other, Material Issues'</u>

The transition tax is expected to raise nearly $340 billion in tax revenue, so it should come as no surprise that LB&I is planning to devote significant resources to auditing section 965 compliance. However, the campaign is unusual in that it suggests a taxpayer whose return is selected for a section 965 focus can also expect a deeper dive on other elements of its compliance with the 2017 tax act. "It is anticipated that returns selected as part of the 965 campaign will also be risked and, if appropriate, examined for other material issues, especially issues related to TCJA planning," explains the LB&I website.

It is unclear what the phrase "TCJA planning" means here. It is possibly a nod towards anti-abuse rules until the new GILTI (global intangible low-taxed income) regime, or a signal that the IRS will be on the lookout for the so-called "gap year" planning that it targeted in temporary regulations issued under section 245A last summer. Many critics have questioned the IRS's authority to issue the section 245A guidance.

In light of the IRS's potentially broad focus, U.S. companies that paid the transition tax should consult with external advisors to risk-assess any large internal asset sales or restructurings in 2017 or 2018 that may have impacted their results under any of the new TCJA provisions.