IRS will allow foreign tax credit for previously noncreditable French taxes

The IRS has issued a statement saying it will no longer challenge claims for foreign tax credits (FTCs) related to the French Contribution Sociale Generalisee (CSG) and Contribution au Remboursement de la Dette Sociale (CRDS) taxes. Let's take a closer look.

Statutory rules

Internal Revenue Code Section 901 generally permits taxpayers to claim an FTC for income, war profits and excess profits taxes paid or accrued during the tax year to any foreign country or to any U.S. possession.

However, Sec. 317(b)(4) of the Social Security Amendments of 1977 (SSA) provides that taxes paid by any individual to a foreign country with respect to any period of employment or self-employment covered under the Social Security system of that foreign country, and in accordance with the terms of an agreement pursuant to Sec. 233 of the SSA, aren't deductible or creditable against the U.S. income tax of that individual.

Sec. 233 of the SSA authorizes agreements with foreign countries to establish "totalization arrangements" concerning the Social Security system of the United States and those of other countries. In other words, taxes paid to a foreign country in accordance with a Social Security totalization agreement aren't eligible for the FTC.

Taxpayers have 10 years to file a claim for refund of U.S. tax with respect to an FTC. The 10-year period begins the day after the regular due date for filing the return (without extensions) for the year to which the foreign taxes relate.

Tax Court's view

With respect to the CSG and CRDS, the U.S. Tax Court recently concluded in *Eshel* that SSA Sec. 317(b)(4) precluded a taxpayer's FTCs for CSG and CRDS taxes paid to France. The court noted that, though they were enacted after the effective date of the U.S.-French Totalization Agreement and not specifically listed in it, the CSG and CRDS were covered by, or within the scope of, the Totalization Agreement because they amended or supplemented the French Social Security laws enumerated in the Totalization Agreement.

The taxpayers in *Eshel* appealed the court's decision to the U.S. Court of Appeals for the District of Columbia. It reversed and remanded the case to the Tax Court.

As part of its filings for the remanded case, the IRS stated that the U.S. and France memorialized through diplomatic communications an understanding that the CSG and CRDS taxes aren't Social Security taxes covered by the Totalization Agreement. Accordingly, the IRS won't challenge FTCs for CSG and CRDS payments on the basis that the Totalization Agreement applies to those taxes.

Good news

The tax agency's statement is good news for those with financial holdings in France who may claim the FTC. If you're in this situation, ask your tax advisor for further explanation and assistance. •