

## Tax Notes

# Update on IRS Guidance for Foreign Branch Operations

By Ralf Ruedenburg, CPA, Partner

The IRS issued guidance on May 7, 2020 to provide relief for U.S. companies with temporary activities in foreign countries. Due to travel restrictions caused by the COVID-19 pandemic, employees of U.S. companies might not be able to return to the U.S. as planned and have to stay and work outside the U.S. longer than intended. Thus, these employees may conduct activities outside the U.S. that would not otherwise have been conducted in a foreign country. This article will address IRS considerations.

### Foreign Branch Operation?

If employees from U.S.-based companies work in a foreign country, and are not able to return to the U.S. due to COVID-19 related travel restrictions, there might be uncertainty as to whether these activities now give rise to

- a foreign branch separate unit for purposes of the dual consolidated loss rules, **or**
- an obligation to file Form 8858, Information Return of U.S. Persons With Respect to Foreign Disregarded Entities (FDEs) and Foreign Branches (FBs).

Typically, all facts and circumstances must be considered to determine whether the activities of a U.S. person outside the U.S. constitute a foreign branch operation. Evidence of the existence of a foreign branch includes, but is not limited to, the existence of an office or other fixed place of business used by employees or officers of the U.S. person in carrying out business activities outside the United States and the existence of a separate set of books and records.

If the IRS concludes that a foreign branch exists, dual consolidated loss rules would limit the ability of a U.S. corporation to include a net loss attributable to a foreign branch separate unit. Furthermore, Form 8858 would have to be completed and submitted to the IRS. This information return requires the taxpayer to provide detailed information about the FB and failure to file the Form would come with a \$10,000 penalty.

### Enter Pandemic

IRS guidance states that some temporary activities will not be taken into account for purposes of determining whether a U.S. corporation has a foreign branch. Specifically, if one or more employees of a U.S. taxpayer are not able to leave a foreign country due to COVID-19 travel restrictions, and conduct activities during any single consecutive period of up to 60 calendar days within calendar year 2020, the days spent in the foreign country and activities performed will not be taken into account for purposes of determining whether a U.S. corporation has a foreign branch.

It remains to be seen whether the IRS extends the 60-day period as travel restrictions will exceed – or already have exceeded – this threshold.

### Maintain Documentation

It is important that taxpayers maintain contemporaneous documentation to establish that the activities are temporary activities and should be prepared to provide the documentation to the IRS upon request. The documentation must include evidence that the activities would not have been performed in the foreign country if the individual had been able to return to the U.S.

## Summing Up

This guidance complements IRS guidance issued on April 21, 2020 where the IRS made clear that, under certain circumstances, up to 60 consecutive calendar days of U.S. presence that are presumed to arise from travel disruptions caused by the COVID-19 emergency will not be counted for purposes of performing the *substantial presence test* to determine U.S. tax residency.

## Contact Us

As always, if you need any assistance, please reach out to your PKF O'Connor Davies client service team or Ralf Ruedenburg, CPA, Partner at [rruedenburg@pkfod.com](mailto:rruedenburg@pkfod.com). We are here to help.

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