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Omnibus Spending Bill Makes Long-Awaited Technical Corrections to Several PATH Act Provisions

On March 23, 2018, President Trump signed the Consolidated Appropriations Act of 2018 (the "Omnibus Act"), an omnibus government spending bill that includes technical corrections to previously enacted tax provisions. The Omnibus Act should have been a great opportunity for Congress to clarify ambiguities and correct glitches in the Tax Cuts and Jobs Act (TCJA). However, political differences got in the way and only one change to the TCJA, relating to the so-called "grain glitch" under Section 199A, made it into the Omnibus Act.

Although the Omnibus Act did little to clarify provisions of the TCJA, it does include technical corrections for several other tax bills, including the Protecting Americans From Tax Hikes Act of 2015 (PATH Act), signed by President Obama in December 2015. The technical corrections to the PATH Act relate to, among other things, qualified foreign pension funds (QFPFs) and the Foreign Investment in Real Property Tax Act of 1980 (FIRPTA).

The concept of a QFPF was introduced into law with the PATH Act, which added Section 897(l) to the Internal Revenue Code. The PATH Act provided that QFPFs and entities that are wholly owned by a QFPF are exempted from FIRPTA and FIRPTA withholding.

For these purposes, the PATH Act explained that a QFPF is any trust, corporation, or other organization or arrangement that meets the following requirements: (1) it was created or organized under foreign law; (2) it was established to provide retirement or pension benefits to participants or beneficiaries that are current or former employees (or persons designated by such employees) of one or more employers in consideration for services rendered; (3) it does not have a single participant or beneficiary with a right to more than 5% of its assets or income; (4) it is subject to government regulation and provides annual information reporting about its beneficiaries to the relevant tax authorities in the country in which it is established or operates; and (5) under the laws of the country in which it is established or operates, either contributions to such fund that would otherwise be subject to tax under such laws are deductible or excluded from the gross income of such fund or taxed at a reduced rate, or taxation of any investment income of such fund is deferred or such income is taxed at a reduced rate.

Following the enactment of the PATH Act, there were uncertainties with some of the requirements necessary for treatment as a QFPF. The second requirement was problematic for pension funds that were not formed for employees of a specific company, including foreign governmental pension funds. These types of funds were unsure whether they were able to satisfy the requirement since participation in these funds is so broad, which makes it difficult to establish that they provide retirement or pension benefits to participants or beneficiaries that are current or former employees of one or more employers in consideration for services rendered.

In an attempt to clarify any confusion, the Omnibus Act revised the second requirement, explicitly stating that a government-established fund that provides public retirement or pension benefits may qualify as a QFPF, as well as a fund established by more than one employer to provide retirement or pension benefits to their employees, such as a multiple-employer or multiemployer plan.

In addition to uncertainties stemming from the second requirement, the fourth requirement also caused some confusion for pension funds from certain countries. In some countries, pension funds are not required to report information to the local tax authority because they instead report to another non-tax government entity. Additionally, in some countries there is no requirement for government pension funds to report to the government at all because they are considered to be a part of the government. To address these types of scenarios, the Omnibus Act revised the language of the fourth requirement to allow pension funds to meet the requirement if the relevant information is made available to tax authorities even if it is not actually provided to them.

The fifth requirement also caused confusion for pension funds from countries with no income tax system, such as the United Arab Emirates. In countries with no income taxes it was not possible to satisfy the fifth requirement since investment income would not be taxed at all, as opposed to at reduced rates. The Omnibus Act revised the language of the fifth requirement to explicitly provide that a QFPF could qualify if its income was excluded from taxation altogether.

In addition to the changes made to clarify the requirements to be qualified as a QFPF, the Omnibus Act also clarified that for purposes of FIRPTA, a QFPF is not treated as a nonresident alien individual or as a foreign corporation. This change can be interpreted in a way that indicates that a QFPF would not be considered a "foreign person" for purposes of determining whether a REIT is domestically controlled. This is very favorable for REITs and investors in REITs since gain from the sale of stock of a REIT is not taxable under FIRPTA if the REIT is domestically controlled (meaning less than 50% of the REIT's stock was held directly or indirectly by foreign persons throughout the applicable testing period).

The Omnibus Act also makes several other technical corrections to PATH Act provisions relating to FIRPTA. One such change involves qualified collective investment vehicles (QCIVs). The Omnibus Act clarifies that the QCIV exception to FIRPTA can only be met if the QCIV is eligible for benefits under a comprehensive income tax treaty with the U.S. and the dividends article in the treaty imposes conditions on the benefits allowable in the case of dividends paid by a REIT.

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