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IRS ends challenge to creditability of French CSG and CRDS

Executive Summary

In documents filed on June 13, 2019 with the U.S. Tax Court in *Eshel v. Commissioner* (Docket No. 8055-12), which is on remand from the U.S. Court of Appeals for the District of Columbia (D.C. Circuit), the IRS indicated that it will no longer assert that taxpayers are precluded from claiming foreign tax credits for the contribution sociale généralisée (CSG) and the contribution pour le remboursement de la dette sociale (CRDS). As a result, US citizens and resident aliens who pay the CSG and CRDS in France may now claim foreign tax credits to offset their US income tax. Additionally, they potentially may file claims for refund of US income tax by claiming foreign tax credits for CSG and CRDS paid in the last 10 years under Internal Revenue Code Section 6511.

Background

Before its recent change in position, the IRS disallowed foreign tax credits for CSG and CRDS under provisions of US law that prohibit a credit or deduction for a tax paid in accordance with a social security totalization agreement. The issue litigated in *Eshel* was whether CSG and CRDS were actually covered by the US-France Social Security Totalization Agreement (Totalization Agreement) and therefore not creditable under applicable US law.

The Totalization Agreement entered into force before the enactment of CSG and CRDS, but nonetheless provides that it would also apply to a tax based on a subsequently enacted law that "amends or supplements" the laws imposing the social taxes described in the Totalization Agreement. Consequently, in *Eshel*, whether or not CSG and CRDS were covered by the Totalization Agreement depended on whether the laws imposing CSG and CRDS amended or supplemented the French social tax laws specified in the Totalization Agreement.

In its April 2014 decision, the Tax Court agreed with the IRS that the laws enacting CSG and CRDS amended or supplemented the French social tax laws described in the Totalization Agreement. *Eshel v. Commissioner*, 142 T.C. 197 (2014). The phrase "amends or supplements" is not defined in the Totalization Agreement. In interpreting the phrase, the Tax Court applied a plain meaning approach, referring to US dictionaries to define "amend" and "supplement." As a result, the Tax Court determined that the laws enacting CSG and CRDS amended and supplemented the French social tax laws in the Totalization Agreement because: (1) the provisions enacting CSG and CRDS are in the part of the French Code where the social security laws are located; (2) both CSG and CRDS are administered and collected in the same manner as the other social taxes described in the Totalization Agreement; and (3) they were enacted to address systemic funding shortfalls in the French social security system.

The petitioners in *Eshel* appealed the Tax Court decision to the D.C. Circuit, which reversed, finding that the Tax Court had failed to follow general principles of treaty interpretation when it referred to US dictionaries to interpret the Totalization Agreement. The appeals court indicated the text of the Totalization Agreement required consideration of French law in evaluating whether CSG and CRDS amended or supplemented the French social tax laws in the Agreement. It also noted that to the extent any ambiguity remained after reviewing French law in interpreting the Agreement, the Tax Court was required to consider the shared expectations of the United States and France regarding the Totalization Agreement. *Eshel v. Commissioner*, 831 F.3d 512 (D.C. Cir. 2016). The appeals court remanded the case to the Tax Court for further proceedings consistent with its opinion, instructing the lower court to obtain the official views and shared expectations of the US and French governments regarding the Totalization Agreement.

The June 13, 2019 documents the IRS filed in Tax Court indicate that the US government, represented by the Department of State, and the French government now have a shared understanding that the laws enacting CSG and CRDS do not amend or supplement the French social tax laws listed in the Totalization Agreement. As a result, the IRS will no longer disallow foreign tax credits for CSG and CRDS.

More background regarding the *Eshel* case can be found in [Tax Alert 2016-1462](#).

Implications

The IRS concession in *Eshel* is a significant development for US taxpayers who have lived and worked in France and paid the CSG and CRDS. US taxpayers may file claims for refund of US income tax for past years by claiming foreign tax credits for CSG and CRDS paid or accrued 10 years from the due date of the return for the tax year the foreign taxes were paid or accrued.

Taxpayers should be aware that France recently enacted a new withholding tax regime, which was implemented at the beginning of 2019. French income tax was previously assessed and paid in the year following the year accrued. France has instituted an "annee blanche" where income taxes are forgiven for 2018, to avoid taxpayer's paying withholding taxes and prior year income taxes concurrently. Thus, individuals using the foreign tax credit accrual method are finding that they do not have sufficient foreign tax credits to offset their US tax for 2018. They also do not have sufficient carryover foreign tax credits, due, in many cases, to not having been able to credit CSG and CRDS prior years before the IRS concession.

This insufficient foreign tax credit carryover for 2018 may be corrected if US taxpayers file amended returns claiming foreign tax credits for CSG and CRDS paid in the last 10 years. EY can assist US taxpayers in determining whether they can benefit by filing amended returns that increase their foreign tax credits and carryovers for the CSG and CRDS paid in the last 10 years.

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