

PUBLICATION

U.S. Tax Considerations for Corporate Dealings in Cuba

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On March 1, 2016, the Internal Revenue Service (IRS) issued Revenue Ruling 2016-8, which removed Cuba from a blacklist of foreign countries that are denied certain favorable tax rules under the Internal Revenue Code (IRC). The so-called blacklist, enacted by Congress under IRC § 901(j), penalized U.S. companies for performing business in Cuba. Effective December 22, 2015, U.S. companies that do business with the island nation may now utilize certain favorable tax rules that were previously unavailable before the IRS released Revenue Ruling 2016-8. Other unfavorable tax rules, however, related to U.S. individuals performing services and deriving income while in Cuba still remain in effect.

This tax alert highlights a number of important U.S. federal income tax provisions that should be considered before doing business in Cuba.

Allowable Foreign Tax Credits. The U.S. federal income tax rules permit foreign tax credits for U.S. entities that paid taxes to a foreign government. The foreign tax credit regime may provide relief from double taxation if permitted under other rules in the IRC and Treasury Regulations. Before Revenue Ruling 2016-8, foreign tax credits for taxes paid by a U.S. corporation to the Cuban government were denied under IRC § 901(j). The consequences resulted in double taxation by the U.S. and Cuban governments. Revenue Ruling 2016-8, however, permits relief from double taxation by allowing foreign tax credits for taxes paid to the Cuban government.

Deferred Taxation for Cuban Earnings by Foreign Subsidiary. U.S. entities with foreign subsidiaries are generally not taxed by the U.S. government until earnings from the foreign subsidiary are brought back to the U.S. in the form of a dividend. This results in the deferral of current U.S. taxation. A number of U.S. international tax rules, however, deny deferral of foreign source income earned abroad, which will result in current U.S. taxation. Before Revenue Rulings 2016-8 was released, income derived from Cuba by certain foreign entities was denied deferral from U.S. taxation. The effect resulted in the current U.S. taxation of any U.S. entity with a foreign subsidiary deriving income from Cuba. Revenue Ruling 2016-8 changes this tax result to permit deferral of U.S. taxation for any foreign subsidiary that does business in Cuba.

U.S. Individual Tax Considerations for Working in Cuba. The U.S. tax rules apply taxation based on worldwide income – foreign and domestic – earned by a U.S. individual. IRC § 911, however, provides an exception to U.S. taxation on foreign source income earned while a U.S. individual lives abroad. For 2016, the amount an individual may exclude from foreign earned income totals \$101,300. This favorable rule under IRC § 911 does not apply to an individual who earns income derived from performing services in Cuba. The result provides for U.S. taxation on all foreign earned income derived from Cuba. Revenue Ruling 2016-8 does not specifically address the favorable tax consequences permitted under IRC § 911, and therefore, all income derived by U.S. individuals from Cuban sources is subject to U.S. taxation. Until future Congressional or Executive action is made to address the tax results under IRC § 911, U.S. individuals are subject to U.S. taxation on income derived from the performance of services in Cuba. The Firm's Tax Group will continue to monitor any future progress related to IRC § 911.

Please remember that advice and counsel regarding your particular tax-related issues, including the potential impact of the developments referenced above on you, your business, or your organization, are dependent upon your specific facts and circumstances. For more information about how these issues may affect your business or related matters, contact the authors of this alert or any members of the Firm's Tax Group.