



MULTISTATE INCOME/FRANCHISE TAX

Nebraska Supreme Court upholds taxation of section 965 income

Tax Alert

Overview

On August 30, 2024, the Nebraska Supreme Court affirmed the order of the district court in *Precision Castparts Corp. v. Neb. Dep't of Revenue*, 317 Neb. 481, and concluded that income included under Internal Revenue Code ("IRC") section 965 does not qualify as dividends deemed to be received for purposes of the Nebraska dividend received deduction under Neb. Rev. Stat. 77-2716(5).

This Tax Alert summarizes the Nebraska Supreme Court's decision in this case.

Background

The taxpayer in this case contended that the income included in its 2017 federal tax return under IRC section 965 represented retained earnings of its foreign subsidiaries and should be deducted from its Nebraska taxable income as "dividends deemed to be received from corporations" under Neb. Rev. Stat. 77-2716(5). The Nebraska Department of Revenue ("Department") disagreed, however, and denied the taxpayer's request to amend its Nebraska corporate income tax return to deduct the 965 income. The taxpayer appealed the assessment. In its decision, the district court held for the Department and agreed that the income was subject to tax under Nebraska law. The taxpayer then appealed to the Nebraska Supreme Court.

Decision

The main issue before the court was whether the amounts included in federal taxable income under IRC section 965 qualified as a dividend "deemed to be received" such that it was deductible under Neb. Rev. Stat. 77-2716(5). In its decision, the Nebraska Supreme Court cited the U.S. Supreme Court decision *Moore v. United States*, 144 S. Ct. 1680, in which the Court characterized IRC section 965 as employing pass-through treatment, meaning that earnings of controlled foreign corporations (CFCs) are attributed to shareholders without requiring an actual distribution, similar to the "longstanding taxation of partnerships, S corporations, and subpart F income."

Ultimately, the Nebraska Supreme Court concluded that the income is not a dividend under federal tax law because no actual distribution was made, and IRC section 965 does not explicitly state that the income inclusion should be treated as dividends. The court based its decision on the plain and ordinary meaning of the statutory language in section 965 and the U.S. Supreme Court's characterization of IRC section 965 income in *Moore*. Consequently, under the holding of the case, IRC section 965 income does not qualify as dividends deemed to be received under Neb. Rev. Stat. 77-2716(5) and is not deductible for Nebraska income tax purposes.

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