Tax Insights
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Services

Federal Circuit narrows treaty-based FTC relief

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In brief

What happened?

The US Court of Appeals for the Federal Circuit on August 31, 2026, issued decisions in *Estate of Paul Bruyea v. United States*, No. 2025-1563, and *Christensen v. United States*, No. 2024-1284, holding that foreign tax credits (FTCs) available under the relevant provisions of the US-Canada and US-France income tax treaties cannot be used to offset the net investment income tax (NIIT) imposed under Section 1411.

In *Bruyea*, the Federal Circuit reversed the Court of Federal Claims and held that the US-Canada income tax treaty does not provide an FTC against the NIIT independent of the Internal Revenue Code. The court focused on treaty language providing that US relief from double taxation is available "in accordance with" and "subject to" the provisions and limitations of US law. The court referred to this treaty language as the "U.S. Law Limitation" and held that it incorporates domestic-law restrictions governing not only the computation of an FTC, but also whether the credit is available at all.

In *Christensen*, the court applied the same general approach to the US-France income tax treaty and held that a similar U.S. Law Limitation applies to Article 24(2)(b), even though that limitation is not expressly repeated in that subparagraph.

Why is it relevant?

The decisions specifically address the availability of treaty-based FTCs against the NIIT, but the Federal Circuit's interpretation of treaty language making the relief subject to US law potentially could have broader implications for the interaction between US income tax treaties and domestic FTC rules. Many US income tax treaties require the United States to provide FTC relief "in accordance with the provisions and subject to the limitations" of US law. *Bruyea* reads that language broadly. The court treated domestic FTC law as governing both the amount and the availability of treaty-based credits and stated, in addressing the US-Canada treaty, that the Code governs "in all instances except when the Convention expressly states that it does not."

The decisions do not hold that an income tax treaty can never modify domestic FTC rules. The Federal Circuit recognized that express treaty provisions can alter otherwise applicable Code limitations. In particular, the court pointed to provisions in the US-Canada income tax treaty that deem certain income to arise in Canada and thereby overcome the source-based limitation of Section 904. Those provisions are referred to as re-sourcing provisions.

The decisions nevertheless could place greater importance on identifying an express treaty basis for departing from an applicable domestic FTC restriction. Current treaty practice provides additional context. For example, the 2022 US-Croatia treaty uses the formulation "to the extent allowed under the law of the United States (as it may be amended from time to time)," making still more explicit the connection between treaty-based FTC relief and domestic-law limitations.

Actions to consider

Taxpayers and advisors with material positions that depend on treaty-based variations from the domestic FTC regime should consider reviewing those positions in light of *Bruyea* and *Christensen*. In particular, they should consider whether the treaty expressly departs from that restriction.

In detail

Background

The cases concern whether income tax treaties may provide FTC relief against the NIIT imposed under Section 1411 when the Code itself does not permit an FTC against that tax.

The relevant US-Canada treaty provision provides that the United States will provide relief from double taxation by allowing a credit against US tax for the appropriate amount of Canadian tax. United States tax is defined as the federal income taxes imposed by the Internal Revenue Code of 1986. The treaty modifies the general grant of an FTC by adding a qualifier: "[i]n accordance with the provisions and subject to the limitations of the law of the United States (as it may be amended from time to time without changing the general principle hereof)." The Federal Circuit referred to this treaty language as the "U.S. Law Limitation."

The US-France income tax treaty contains a similar commitment for the United States to provide a credit against US tax on income and a similar U.S. Law Limitation in Article 24. In *Christensen*, the principal dispute concerned whether that limitation also applies to Article 24(2)(b), which provides relief for US citizens resident in France, even though the U.S. Law Limitation is not expressly repeated in that subparagraph.

Both cases had produced taxpayer-favorable judgments in the Court of Federal Claims. In *Bruyea*, the lower court held that the US-Canada income tax treaty could independently provide a credit against the NIIT and interpreted the U.S. Law Limitation as governing the computation, rather than the existence, of treaty-based credits. In *Christensen*, the lower court allowed relief under Article 24(2)(b) based on its conclusion that the U.S. Law Limitation did not extend to that provision.

The Federal Circuit's analysis in *Bruyea*

The Code does not permit an FTC against the NIIT

The Federal Circuit first concluded that the Code itself does not permit FTCs against the NIIT. Sections 27 and 901 generally authorize FTCs only against taxes imposed under chapter 1 of the Code, while the NIIT is imposed under chapter 2A.

Although the court acknowledged that it was not clear why Congress placed the NIIT in chapter 2A, it presumed that Congress acted intentionally and with knowledge of the existing FTC regime. On that basis, the court concluded that Congress's placement of the NIIT outside chapter 1 excluded it from the Code-based FTC regime.

The treaty does not create an independent credit

The taxpayer argued that the US-Canada treaty independently creates a credit that may be used against the NIIT notwithstanding the Code. The Federal Circuit rejected that position.

The court focused on the treaty's U.S. Law Limitation. In the Federal Circuit's view, that limitation incorporates domestic-law restrictions not merely for purposes of computing the amount of a treaty-based FTC, but also in determining whether the credit is available in the first place. The court therefore expressly rejected the Court of Federal Claims' conclusion that the U.S. Law Limitation was limited to computational provisions.

Of potentially broader significance, the Federal Circuit stated that the U.S. Law Limitation, and therefore the Code, governs "in all instances except when the Convention expressly states that it does not."

The Federal Circuit pointed to the US-Canada income tax treaty's re-sourcing provisions as an example of an express departure from domestic FTC rules. Those provisions deem certain income to arise in Canada and thereby overcome the source-based limitation of Section 904 that otherwise could restrict the availability of an FTC. The court reasoned that these express departures would have been unnecessary if treaty-based FTCs otherwise operated independently of the Code.

Observation: The court's treatment of the U.S. Law Limitation potentially affects treaty-based FTC positions that depend on obtaining a result different from domestic law. The decision could increase the importance of determining whether the treaty expressly displaces the particular Code limitation at issue. Taxpayers also should trace the history and content of the relevant domestic law provision for any indication of whether the legislature intended to override treaties.

The court rejects broader treaty arguments

The Federal Circuit also rejected the argument that the treaty's broad coverage of "United States tax on income" was sufficient to permit a credit against the NIIT. Although the parties agreed that the NIIT falls within that term, the court characterized that conclusion as only "the start of the analysis." In the court's view, the U.S. Law Limitation still determines whether the treaty credit is available against the covered tax.

The taxpayer also relied on the treaty's general objective of avoiding double taxation. Although the parties agreed that avoidance of double taxation is the "general principle" protected by the treaty's limitation on subsequent changes in US law, the court held that the treaty does not guarantee elimination of every instance of double taxation. It therefore concluded that Congress's creation of the NIIT without an available FTC did not impermissibly change that general principle.

Finally, the Federal Circuit treated the relevant treaty language as unambiguous and declined to rely on extrinsic materials supporting the taxpayer's interpretation, including the Treasury Technical Explanation, the State Department's Letter of Submittal, and a letter from the Canada Revenue Agency.

The Federal Circuit's analysis in *Christensen*

In *Christensen*, the Federal Circuit applied the same general approach to the US-France income tax treaty.

The taxpayers argued that Article 24(2)(b), which provides relief for US citizens resident in France, operates independently of the U.S. Law Limitation appearing at the beginning of paragraph 2 because the limitation is not expressly repeated in subparagraph (b).

The Federal Circuit rejected that argument. It held that the U.S. Law Limitation applies throughout the relevant provisions of Article 24, including subparagraph (b). The court therefore reversed the taxpayer-favorable judgment.

Interaction between treaties and later-enacted domestic law

The decisions are also relevant to the traditional analysis of the interaction between later-enacted statutes and existing treaty obligations.

Courts generally seek to interpret statutes and treaties harmoniously before concluding that a later-enacted statute overrides an earlier treaty, with the last-in-time rule becoming relevant where the two cannot be reconciled. The Code itself directs that its provisions be applied with "due regard" to applicable US treaty obligations, and Congress has demonstrated elsewhere in the Code that it knows how to address expressly the relationship between domestic tax rules and treaty obligations.

The Federal Circuit did not conclude that Congress expressly overrode the US-Canada income tax treaty when it enacted the NIIT. It also declined to reach the government's alternative argument that the NIIT, as later-enacted legislation, would prevail over an inconsistent treaty provision.

Instead, the court concluded that there was no conflict between the Code and the treaty to resolve. In the court's words, "The Convention and the Code are aligned." Under its interpretation, the U.S. Law Limitation causes the treaty itself to incorporate the relevant domestic-law restrictions.

Observation: This reasoning has significance beyond the NIIT. Under the Federal Circuit's approach, subsequent changes to domestic FTC law could affect treaty-based relief where the treaty's U.S. Law Limitation incorporates those restrictions, without first requiring the court to find a conflict between the treaty and later-enacted legislation.

Practical considerations

The immediate consequence of *Bruyea* and *Christensen* is that taxpayers seeking to use the relevant US-Canada and US-France income tax treaty provisions to claim FTCs against the NIIT face adverse Federal Circuit precedent, following similarly unfavorable precedent in the Tax Court in *Toulouse v. Commissioner*, 157 T.C. 49 (2021).

Taxpayers and advisors with material positions that depend on treaty-based variations from the domestic FTC regime should consider reviewing those positions. Relevant questions include whether the treaty contains an applicable U.S. Law Limitation, whether a contrary domestic-law restriction applies, whether the treaty expressly provides a departure from that restriction, and whether Congress has expressed its intent to override treaties or not to do so.

Let's talk

For a deeper discussion of how these decisions might affect your business, please contact:

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