



[4830-01-p]

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[REG-101828-19]

RIN 1545-BP15

Guidance under Section 958 (Rules for Determining Stock Ownership) and Section 951A (Global Intangible Low-Taxed Income)

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations regarding the treatment of domestic partnerships for purposes of determining amounts included in the gross income of their partners with respect to foreign corporations. In addition, this document contains proposed regulations under the global intangible low-taxed income provisions regarding gross income that is subject to a high rate of foreign tax. The proposed regulations would affect United States persons that own stock of foreign corporations through domestic partnerships and United States shareholders of foreign corporations.

DATES: Written or electronic comments and requests for a public hearing must be received by **[INSERT DATE 90 DAYS AFTER PUBLICATION IN THE FEDERAL REGISTER]**.

ADDRESSES: Send submissions to: Internal Revenue Service, CC:PA:LPD:PR (REG-101828-19), Room 5203, Post Office Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to CC:PA:LPD:PR (REG-101828-19), Courier's Desk, Internal

Revenue Service, 1111 Constitution Avenue, N.W., Washington, DC 20024, or sent electronically, via the Federal eRulemaking Portal at www.regulations.gov (indicate IRS and REG-101828-19).

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations under §§1.951-1, 1.956-1, and 1.958-1, Joshua P. Roffenbender at (202) 317-6934; concerning the proposed regulations under §§1.951A-0, 1.951A-2, 1.951A-7, and 1.954-1, Jorge M. Oben at (202) 317-6934; concerning the proposed regulations under §1.1502-51, Katherine H. Zhang at (202) 317-6848 or Kevin M. Jacobs at (202) 317-5332; concerning submissions of comments or requests for a public hearing, Regina Johnson at (202) 317-6901 (not toll free numbers).

SUPPLEMENTARY INFORMATION:

Background

I. Subpart F Before Enactment of Section 951A

The Revenue Act of 1962 (the “1962 Act”), Pub. L. 87-834, sec. 12, 76 Stat. at 1006, enacted subpart F of part III, subchapter N, chapter 1 of the 1954 Internal Revenue Code (“subpart F”), as amended. See sections 951 through 965 of the Internal Revenue Code (“Code”).¹ Congress created the subpart F regime to limit the use of corporations organized in low-tax jurisdictions for the purposes of obtaining indefinite deferral of U.S. tax on certain earnings – generally earnings that are passive or highly mobile – that would otherwise be subject to Federal income tax. H.R. Rep. No. 1447 at 57-58 (1962); S. Rep. No. 1881 at 78-80 (1962). Subpart F generally

¹ Except as otherwise stated, all section references in this preamble are to the Internal Revenue Code.

requires a United States shareholder (as defined in section 951(b)) (“U.S. shareholder”) to include in its gross income (“subpart F inclusion”) its pro rata share of subpart F income (as defined in section 952) earned by a controlled foreign corporation (“CFC”) (as defined in section 957(a)) and its pro rata share of earnings and profits (“E&P”) invested in certain United States property by the CFC. See section 951(a)(1)(A) and (B) and section 956(a). For purposes of both section 951(a)(1)(A) and (B), the determination of a U.S. shareholder’s pro rata share of any amount with respect to a CFC is determined by reference to the stock of the CFC that the shareholder owns (within the meaning of section 958(a)). See sections 951(a)(1) and (2) and 956(a).

Section 957(a) defines a CFC as any foreign corporation if U.S. shareholders own (within the meaning of section 958(a)), or are considered as owning by applying the ownership rules of section 958(b), more than 50 percent of the total combined voting power or value of stock of such corporation on any day during the taxable year of such foreign corporation. Section 951(b) defines a U.S. shareholder of a foreign corporation as a United States person (“U.S. person”) that owns (within the meaning of section 958(a)), or is considered as owning by applying the ownership rules of section 958(b), at least 10 percent of the total combined voting power or value of stock of the foreign corporation. Section 957(c) generally defines a U.S. person by reference to section 7701(a)(30), which defines a U.S. person as a citizen or resident of the United States, a domestic partnership, a domestic corporation, and certain estates and trusts.

Stock owned within the meaning of section 958(a) is stock owned directly and stock owned indirectly under section 958(a)(2). Section 958(a)(2) provides that stock owned, directly or indirectly, by or for a foreign corporation, foreign partnership, foreign

trust, or foreign estate is considered to be owned proportionately by its shareholders, partners, or beneficiaries. Section 958(a)(2) does not provide rules addressing stock owned by domestic entities, including domestic partnerships.

Section 958(b) provides in relevant part that the constructive ownership rules of section 318(a) apply, with certain modifications, for purposes of determining whether any U.S. person is a U.S. shareholder or any foreign corporation is a CFC. These rules apply to treat a person as owning the stock owned, directly or indirectly, by another person, generally without regard to whether the person to or from which stock is attributed is domestic or foreign. In particular, section 318(a)(2)(A) provides in relevant part that stock owned, directly or indirectly, by or for a partnership is considered as owned proportionately by its partners, and section 318(a)(3)(A) provides that stock owned, directly or indirectly, by or for a partner is considered as owned by the partnership. Further, in determining stock treated as owned by partners of a partnership under section 318(a)(2)(A), section 958(b)(2) provides in relevant part that a partnership that owns, directly or indirectly, more than 50 percent of the voting power of a corporation is considered as owning all the stock entitled to vote. However, a U.S. person that is a U.S. shareholder of a CFC by reason of constructive ownership under section 958(b), but that does not own stock in the CFC within the meaning of section 958(a), does not have a subpart F inclusion with respect to the CFC.

II. Treatment of Domestic Partnerships as Entities or Aggregates of their Partners, in General

For purposes of applying a particular provision of the Code, a partnership may be treated as either an entity separate from its partners or as an aggregate of its partners. Under an aggregate approach, the partners of a partnership, and not the partnership,

are treated as owning the partnership's assets and conducting the partnership's operations. Under an entity approach, the partnership is respected as separate and distinct from its partners, and therefore the partnership, and not the partners, is treated as owning the partnership's assets and conducting the partnership's operations. Based upon the authority of subchapter K and the policies underlying a particular provision of the Code, a partnership is treated as an aggregate of its partners or as an entity separate from its partners, depending on which characterization is more appropriate to carry out the scope and purpose of the Code provision. See H.R. Rep. No. 83-2543, at 59 (1954) (Conf. Rep.) ("Both the House provisions and the Senate amendment provide for the use of the 'entity' approach in the treatment of transactions between a partner and a partnership No inference is intended, however, that a partnership is to be considered as a separate entity for the purpose of applying other provisions of the internal revenue laws if the concept of the partnership as a collection of individuals is more appropriate for such provisions."). See also Casel v. Commissioner, 79 T.C. 424, 433 (1982) ("When the 1954 Code was adopted by Congress, the conference report . . . clearly stated that whether an aggregate or entity theory of partnerships should be applied to a particular Code section depends upon which theory is more appropriate to such section."); Holiday Village Shopping Center v. United States, 5 Cl. Ct. 566, 570 (1984), aff'd 773 F.2d 276 (Fed. Cir. 1985) ("[T]he proper inquiry is not whether a partnership is an entity or an aggregate for purposes of applying the internal revenue laws generally, but rather which is the more appropriate and more consistent with Congressional intent with respect to the operation of the particular provision of the Internal Revenue Code at issue."); §1.701-2(e)(1) ("The Commissioner can treat a

partnership as an aggregate of its partners in whole or in part as appropriate to carry out the purpose of any provision of the Internal Revenue Code . . .”).

Consistent with this authority under subchapter K, the Treasury Department and the IRS have adopted an aggregate approach to partnerships to carry out the purpose of various provisions, including international provisions, of the Code. For example, regulations under section 871 treat domestic and foreign partnerships as aggregates of their partners in applying the 10 percent shareholder test of section 871(h)(3) to determine whether interest paid to a partnership would be considered portfolio interest under section 871(h)(2). See §1.871-14(g)(3)(i). An aggregate approach to partnerships was also adopted in regulations issued under section 367(a) to address the transfer of property by a domestic or foreign partnership to a foreign corporation in an exchange described in section 367(a)(1). See §1.367(a)-1T(c)(3)(i)(A). Similarly, the Treasury Department and the IRS adopted an aggregate approach to foreign partnerships for purposes of applying the regulations under section 367(b). See §1.367(b)-2(k); see also §§1.367(e)-1(b)(2) (treating stock and securities of a distributing corporation owned by or for a partnership (domestic or foreign) as owned proportionately by its partners) and 1.861-9(e)(2) (requiring certain corporate partners to apportion interest expense, including the partner’s distributive share of partnership interest expense, by reference to the partner’s assets).

III. Treatment of Domestic Partnerships as Entities or Aggregates for Purposes of Subpart F Before the Tax Cuts and Jobs Act

Since the enactment of subpart F, domestic partnerships have generally been treated as entities, rather than as aggregates of their partners, for purposes of determining whether U.S. shareholders own more than 50 percent of the stock (by

voting power or value) of a foreign corporation and thus whether a foreign corporation is a CFC. See §1.701-2(f), Example 3 (concluding that a foreign corporation wholly owned by a domestic partnership is a CFC for purposes of applying the look-through rules of section 904(d)(3)). In addition, domestic partnerships have generally been treated as entities for purposes of treating a domestic partnership as the U.S. shareholder that has the subpart F inclusion with respect to such foreign corporation. But cf. §§1.951-1(h) and 1.965-1(e) (treating certain domestic partnerships owned by CFCs as foreign partnerships for purposes of determining the U.S. shareholder that has the subpart F inclusion with respect to CFCs owned by such domestic partnerships). If a domestic partnership is treated as the U.S. shareholder with the subpart F inclusion, then each partner of the partnership has a distributive share of the partnership's subpart F inclusion, regardless of whether the partner itself is a U.S. shareholder. See section 702.

This entity treatment is consistent with the inclusion of a domestic partnership in the definition of a U.S. person in section 7701(a)(30), which term is used in the definition of U.S. shareholder by reference to section 957(c). It is also consistent with the legislative history to section 951, which describes domestic partnerships as being included within the definition of a U.S. person and, therefore, a U.S. shareholder. See, for example, S. Rep. No. 1881 at 80 n.1 (1962) ("U.S. shareholders are defined in the bill as 'U.S. persons' with 10-percent stockholding. U.S. persons, in general, are U.S. citizens and residents and domestic corporations, partnerships and estates or trusts."). Furthermore, entity treatment is consistent with sections 958(b) and 318(a)(3)(A), which treat a partnership (including a domestic partnership) as owning the stock owned by its

partners for purposes of determining whether the foreign corporation is owned more than 50 percent by U.S. shareholders.

In contrast to the historical treatment of domestic partnerships as entities for purposes of subpart F, foreign partnerships are generally treated as aggregates of their partners for purposes of determining stock ownership under section 958(a). See section 958(a)(2). Accordingly, whether a foreign corporation owned by a foreign partnership is a CFC is determined based on the proportionate amount of stock owned by domestic partners of the partnership and, if the foreign corporation is a CFC, partners that are U.S. shareholders have the subpart F inclusion with respect to the CFC.

IV. Section 951A

A. In general

The Tax Cuts and Jobs Act, Pub. L. 115-97 (the “Act”) established a participation exemption system for the taxation of certain foreign income by allowing a domestic corporation a 100 percent dividends received deduction for the foreign-source portion of a dividend received from a specified 10 percent-owned foreign corporation. See section 14101(a) of the Act and section 245A. The Act’s legislative history expresses concern that the new participation exemption could heighten the incentive to shift profits to low-tax foreign jurisdictions or tax havens absent base erosion protections. See S. Comm. on the Budget, Reconciliation Recommendations Pursuant to H. Con. Res. 71, S. Print No. 115-20, at 370 (2017) (“Senate Explanation”). For example, without appropriate limits, domestic corporations might be incentivized to shift income to low-taxed foreign affiliates, and the income could potentially be distributed back to domestic corporate shareholders without the imposition of any U.S. tax. See *id.* To prevent base erosion,

the Act retained the subpart F regime and enacted section 951A, which applies to taxable years of foreign corporations beginning after December 31, 2017, and to taxable years of U.S. shareholders in which or with which such taxable years of foreign corporations end.

Section 951A requires a U.S. shareholder of any CFC for any taxable year to include in gross income the shareholder's global intangible low-taxed income ("GILTI inclusion") for such taxable year in a manner similar to a subpart F inclusion for many purposes of the Code. See sections 951A(a) and (f)(1)(A); H.R. Rep. No. 115-466, at 641 (2017) (Conf. Rep.) ("[A] U.S. shareholder of any CFC must include in gross income for a taxable year its [GILTI] in a manner generally similar to inclusions of subpart F income."). Similar to a subpart F inclusion, the determination of a U.S. shareholder's GILTI inclusion begins with the calculation of relevant items – such as tested income, tested loss, and qualified business asset investment – of each CFC owned by the shareholder ("tested items"). See section 951A(c)(2) and (d) and §§1.951A-2 through -4. A U.S. shareholder then determines its pro rata share of each of these CFC-level tested items in a manner similar to a U.S. shareholder's pro rata share of subpart F income under section 951(a)(2). See section 951A(e)(1) and §1.951A-1(d).

In contrast to a subpart F inclusion, however, a U.S. shareholder's pro rata shares of the tested items of a CFC are not amounts included in gross income, but rather are amounts taken into account by the U.S. shareholder in determining the amount of its GILTI inclusion for the taxable year. Section 951A(b) and §1.951A-1(c). Thus, a U.S. shareholder does not compute a separate GILTI inclusion amount under

section 951A(a) with respect to each CFC for a taxable year, but rather computes a single GILTI inclusion amount by reference to all of its CFCs.

Section 951A itself does not contain specific rules regarding the treatment of domestic partnerships and their partners for purposes of GILTI. However, proposed regulations under section 951A that were published in the **Federal Register** on October 10, 2018, (REG-104390-18, 83 FR 51072) (“GILTI proposed regulations”) reflect a hybrid approach that treats a domestic partnership that is a U.S. shareholder with respect to a CFC (“U.S. shareholder partnership”) as an entity with respect to some partners but as an aggregate of its partners with respect to others. Under the hybrid approach, with respect to partners that are not U.S. shareholders of a CFC owned by a domestic partnership, a U.S. shareholder partnership calculates a GILTI inclusion amount and its partners have a distributive share of such amount (if any). See proposed §1.951A-5(b)(1). However, with respect to partners that are themselves U.S. shareholders of a CFC owned by a domestic partnership (“U.S. shareholder partners”), the partnership is treated in the same manner as a foreign partnership, with the result that the U.S. shareholder partners are treated as proportionately owning, within the meaning of section 958(a), stock owned by the domestic partnership for purposes of determining their own GILTI inclusion amounts. See proposed §1.951A-5(c). In the preamble to the GILTI proposed regulations, the Treasury Department and the IRS rejected a pure entity approach to section 951A, because treating a domestic partnership as the section 958(a) owner of stock in all cases would frustrate the GILTI framework by creating unintended planning opportunities for well advised taxpayers and traps for the unwary. However, the Treasury Department and the IRS also did not

adopt a pure aggregate approach to domestic partnerships for GILTI because such an approach would be inconsistent with the existing treatment of domestic partnerships as entities for purposes of subpart F.

The Treasury Department and the IRS received many comments in response to the hybrid approach of the GILTI proposed regulations. The comments generally advised against adopting the hybrid approach due primarily to concerns with complexity and administrability arising from the treatment of a partnership as an entity with respect to some partners but as an aggregate with respect to other partners. The comments also generally advised against adopting a pure entity approach because such an approach would result in different treatment for similarly situated taxpayers depending on whether a U.S. shareholder owned stock of a foreign corporation through a domestic partnership or a foreign partnership, which is treated as an aggregate of its partners for purposes of determining CFC status and section 958(a) ownership. The majority of comments on this issue recommended at least some form of aggregate approach for domestic partnerships for purposes of the GILTI regime; some of these comments suggested that an aggregate approach is supported by analogy to other situations where regulations apply an aggregate approach to partnerships. See, for example, §§1.954-1(g)(1) and 1.871-14(g)(3)(i).

In response to these comments, the Treasury Department and the IRS are issuing final regulations under section 951A in the Rules and Regulations section of this issue of the **Federal Register** (“GILTI final regulations”) that treat stock owned by a domestic partnership as owned within the meaning of section 958(a) by its partners for purposes of determining a partner’s GILTI inclusion amount under section 951A. The

Treasury Department and the IRS concluded that applying an aggregate approach for purposes of determining a partner's GILTI inclusion amount under section 951A is necessary to ensure that, consistent with the purpose and operation of section 951A, a single GILTI inclusion amount is determined for each taxpayer based on its economic interests in all of its CFCs. The GILTI final regulations apply to taxable years of foreign corporations beginning after December 31, 2017, and to taxable years of U.S. shareholders in which or with which such taxable years of foreign corporations end.

Some comments also recommended adopting an aggregate approach for purposes of section 951, especially if the GILTI final regulations adopt an aggregate approach. These comments generally asserted that there is insufficient policy justification for treating domestic partnerships differently than foreign partnerships for purposes of U.S. shareholder and CFC determinations because the choice of law under which a partnership is organized should be irrelevant. In this regard, these comments criticized entity treatment of domestic partnerships because it results in each partner including in income its distributive share of a domestic partnership's subpart F inclusion with respect to a CFC, even if that partner is not a U.S. shareholder itself and thus would not have had a subpart F inclusion with respect to such CFC if the domestic partnership were instead foreign.

B. High-tax gross tested income

Section 951A(c)(2)(A)(i) provides that the gross tested income of a CFC for a taxable year is all the gross income of the CFC for the year, determined without regard to certain items. See also §1.951A-2(c)(1). In particular, section 951A(c)(2)(A)(i)(III) excludes from gross tested income any gross income excluded from foreign base company income (as defined in section 954) ("FBCI") or insurance income (as defined

in section 953) of a CFC by reason of the exception under section 954(b)(4) (the “GILTI high tax exclusion”).

The GILTI proposed regulations clarified that the GILTI high tax exclusion applies only to income that is excluded from FBCI and insurance income solely by reason of an election made to exclude the income under the high tax exception of section 954(b)(4) and §1.954-1(d)(5). See proposed §1.951A-2(c)(1)(iii).

Numerous comments requested that the scope of the GILTI high tax exclusion be expanded in the final regulations. These comments asserted that the legislative history to section 951A indicates that Congress intended that income of a CFC should be taxed as GILTI only if it is subject to a low rate of foreign tax, regardless of whether the income is active or passive. Comments also suggested that the GILTI high tax exclusion does not require that income be excluded “solely” by reason of section 954(b)(4). The comments argued that the GILTI high tax exclusion could be interpreted to exclude any item of income that would be FBCI or insurance income, but for another exception to FBCI (for instance, the active financing exception under section 954(h) and the active insurance exception under section 954(i)). Of the comments recommending an expansion of the GILTI high tax exclusion, some recommended that the GILTI high tax exclusion apply to income taxed at a rate above 13.125 percent, while others recommended that the GILTI high tax exclusion apply to income taxed at a rate above 90 percent of the maximum rate of tax specified in section 11, or 18.9 percent. The comments recommended that the GILTI high tax exclusion be applied either on a CFC-by-CFC basis or an item-by-item basis.

Alternatively, comments recommended that the scope of the GILTI high tax exclusion be expanded under section 951A(f) by treating, on an elective basis, a GILTI inclusion as a subpart F inclusion that is potentially excludible from FBCI or insurance income under section 954(b)(4), or by modifying the GILTI high tax exclusion to exclude any item of income subject to a sufficiently high effective foreign tax rate such that it would be excludible under section 954(b)(4) if it were FBCI or insurance income. Other comments recommended the creation of a rebuttable presumption that all income of a CFC is subpart F income, regardless of whether such income is of a character included in FBCI or insurance income, and therefore, if the taxpayer chose not to rebut the presumption, the income would be excluded from gross tested income either because it is included in subpart F income (and thus excluded from gross tested income by reason of the subpart F exclusion under section 951A(c)(2)(A)(i)(II)) or because the income is excluded from subpart F income by reason of section 954(b)(4) (and thus excluded from gross tested income by reason of the GILTI high tax exclusion).

The GILTI final regulations adopt the GILTI high tax exclusion of the proposed regulations without change.

Explanation of Provisions

I. Partnerships

A. Adoption of aggregate treatment for purposes of section 951

After considering the alternatives, the Treasury Department and the IRS have concluded that, to be consistent with the treatment of domestic partnerships under section 951A, a domestic partnership should also generally be treated as an aggregate of its partners in determining stock owned under section 958(a) for purposes of section

951. Therefore, the proposed regulations provide that, for purposes of sections 951 and 951A, and for purposes of any provision that applies by reference to sections 951 and 951A (for example, sections 959, 960, and 961), a domestic partnership is not treated as owning stock of a foreign corporation within the meaning of section 958(a). See proposed §1.958-1(d)(1). Furthermore, the proposed regulations provide that, for purposes of determining the stock owned under section 958(a) by a partner of a domestic partnership, a domestic partnership is treated in the same manner as a foreign partnership. See *id.* This rule does not apply, however, for purposes of determining whether any U.S. person is a U.S. shareholder, whether a U.S. shareholder is a controlling domestic shareholder (as defined in §1.964-1(c)(5)), or whether a foreign corporation is a CFC. See proposed §1.958-1(d)(2). Accordingly, under the proposed regulations, a domestic partnership that owns a foreign corporation is treated as an entity for purposes of determining whether the partnership and its partners are U.S. shareholders, whether the partnership is a controlling domestic shareholder, and whether the foreign corporation is a CFC, but the partnership is treated as an aggregate of its partners for purposes of determining whether, and to what extent, its partners have inclusions under sections 951 and 951A and for purposes of any other provision that applies by reference to sections 951 and 951A.

For purposes of subpart F, a foreign partnership is explicitly treated as an aggregate of its partners, and rules regarding this aggregate treatment are relatively well-developed and understood. Therefore, rather than developing a new standard for the treatment of a domestic partnership as an aggregate of its partners, the Treasury Department and the IRS have determined that it would be simpler and more

administrable to adopt, by reference, the rules related to foreign partnerships for this limited purpose. The GILTI final regulations adopt the same approach for purposes of section 951A. See §1.951A-1(e). As a result, under the proposed regulations, stock owned directly or indirectly by or for a domestic partnership will generally be treated as owned proportionately by its partners for purposes of sections 951(a) and 951A and any provision that applies by reference to sections 951 and 951A.

The Treasury Department and the IRS have determined that, as a result of the enactment of the GILTI regime, it is no longer appropriate to treat domestic partnerships as entities that are separate from their owners for purposes of determining whether, and to what extent, a partner has an inclusion under section 951. Congress intended for the subpart F and GILTI regimes to work in tandem by providing that both regimes apply to U.S. shareholders of CFCs, that GILTI is included in a U.S. shareholder's gross income in a manner similar to a subpart F inclusion for many purposes of the Code, and that gross income taken into account in determining the subpart F income of a CFC is not taken into account in determining the tested income of such CFC (and, therefore, in determining the GILTI inclusion amount of a U.S. shareholder of such CFC). See section 951A(c)(2)(i)(II) and 951A(f); see also Senate Explanation at 373 ("Although GILTI inclusions do not constitute subpart F income, GILTI inclusions are generally treated similarly to subpart F inclusions."). As a result, treating domestic partnerships inconsistently for subpart F and GILTI purposes would be inconsistent with legislative intent.

Furthermore, inconsistent approaches to the treatment of domestic partnerships for purposes of subpart F and GILTI would introduce substantial complexity and

uncertainty, particularly with respect to foreign tax credits, previously taxed earnings and profits (“PTEP”) and related basis rules, or any other provision the application of which turns on the owner of stock under section 958(a) and, thus, the U.S. person that has the relevant inclusion. For example, if a domestic partnership were treated as an aggregate of its partners for purposes of GILTI but as an entity for purposes of subpart F, regulations would need to address separately the maintenance of PTEP accounts at the domestic partnership level for subpart F and the maintenance of PTEP accounts at the partner level for GILTI. Similarly, regulations would need to provide separate rules for basis adjustments under section 961 with respect to a domestic partnership and its CFCs depending on whether an amount was included under section 951 or section 951A. The increased complexity of regulations resulting from treating domestic partnerships differently for purposes of subpart F and GILTI would, in turn, increase the burden on taxpayers to comply with, and on the IRS to administer, such regulations. Conversely, aggregate treatment of domestic partnerships in determining section 958(a) stock ownership for purposes of determining a partner’s inclusion under both the GILTI and subpart F regimes will result in substantial simplification, as compared to disparate treatment, and will harmonize the two regimes.

The Treasury Department and the IRS also considered extending aggregate treatment for all purposes of subpart F, including for purposes of determining whether a foreign corporation is a CFC under section 957(a). However, the Treasury Department and the IRS determined that an approach that treats a domestic partnership as an aggregate for purposes of determining CFC status is inconsistent with relevant statutory provisions. As discussed in part III of the Background section of this preamble, the

Code clearly contemplates that a domestic partnership can be a U.S. shareholder under section 951(b), including by attribution from its partners. See sections 7701(a)(30), 957(c), 951(b), 958(b), 318(a)(2)(A), and 318(a)(3)(A). An approach that treats a domestic partnership as an aggregate for purposes of determining CFC status would not give effect to the statutory treatment of a domestic partnership as a U.S. shareholder.

By contrast, neither section 958(a) nor any other provision of the Code specifies whether and to what extent a domestic partnership should be treated as an entity or an aggregate for purposes of determining stock ownership under section 958(a) for purposes of sections 951 and 951A. According to the legislative history to the 1962 Act, section 958(a) is a “limited rule of stock ownership for determining the amount taxable to a United States person,” whereas section 958(b) is “a broader set of constructive rules of ownership for determining whether the requisite ownership by United States persons exists so as to make a corporation a controlled foreign corporation or a United States person has the requisite ownership to be liable for tax under section 951(a).” S. Rep. No. 1881 at 254 (1962). In light of the changes adopted in the Act (including the introduction of the GILTI regime), it is consistent with the intent of the Act to provide that domestic partnerships are treated in the same manner as foreign partnerships under section 958(a)(2) for purposes of sections 951(a) and 951A and any provision that applies by reference to sections 951 and 951A. As discussed in parts II and IV.A. of the Background section of this preamble, a domestic partnership may be treated as an aggregate of its partners or as an entity separate from its partners for purposes of a provision, depending on which characterization is more appropriate to carry out the

purpose of the provision. In this regard, the Treasury Department and the IRS have determined that treating a domestic partnership as an aggregate for purposes of sections 951 and 951A is appropriate because the partners of the partnership generally are the ultimate taxable owners of the CFC and thus their inclusions under sections 951 and 951A are properly computed at the partner level regardless of whether the partnership is foreign or domestic.

Based on the foregoing, the Treasury Department and the IRS have determined that a domestic partnership should be treated consistently as an aggregate of its partners in determining the ownership of stock within the meaning of section 958(a) for purposes of sections 951 and 951A, and any provision that applies by reference to section 951 or section 951A, except for purposes of determining whether a U.S. person is a U.S. shareholder, whether a U.S. shareholder is a controlling domestic shareholder (as defined in §1.964-1(c)(5)), and whether a foreign corporation is a CFC. See proposed §1.958-1(d). This aggregate treatment does not apply for any other purposes of the Code, including for purposes of section 1248. However, the Treasury Department and the IRS request comments on other provisions in the Code that apply by reference to ownership within the meaning of section 958(a) for which aggregate treatment for domestic partnerships would be appropriate. The Treasury Department and the IRS also request comments on whether, and for which purposes, the aggregate treatment for domestic partnerships should be extended to the determination of the controlling domestic shareholders (as defined in §1.964-1(c)(5)) of a CFC, such that some or all of the partners who are U.S. shareholders of the CFC, rather than the

partnership, make any elections applicable to the CFC for purposes of sections 951 and 951A.

B. Applicability date and comment request with respect to transition

The proposed regulations are proposed to apply to taxable years of foreign corporations beginning on or after the date of publication of the Treasury decision adopting these rules as final regulations in the **Federal Register** (the “finalization date”), and to taxable years of a U.S. person in which or with which such taxable years of foreign corporations end. See proposed §1.958-1(d)(4). With respect to taxable years of foreign corporations beginning before the finalization date, the proposed regulations provide that a domestic partnership may apply §1.958-1(d), as included in the final regulations, for taxable years of a foreign corporation beginning after December 31, 2017, and for taxable years of a domestic partnership in which or with which such taxable years of the foreign corporation end (the “applicable years”), provided that the partnership, domestic partnerships that are related (within the meaning of section 267 or 707) to the partnership, and certain partners consistently apply §1.958-1(d) with respect to all foreign corporations whose stock they own within the meaning of section 958(a) (generally determined without regard to §1.958-1(d)). See proposed §1.958-1(d)(4). A domestic partnership may rely on proposed §1.958-1(d) with respect to taxable years beginning after December 31, 2017, and beginning before the date that these regulations are published as final regulations in the **Federal Register**, provided that the partnership, domestic partnerships that are related (within the meaning of section 267 or 707) to the partnership, and certain partners consistently apply proposed §1.958-1(d)

with respect to all foreign corporations whose stock they own within the meaning of section 958(a) (generally determined without regard to proposed §1.958-1(d)). See *id.*

Once proposed §1.958-1(d) applies as a final regulation, §1.951A-1(e) and §1.951-1(h) (providing an aggregate treatment of domestic partnerships, but only for purposes of section 951A and limited subpart F purposes, respectively) would be unnecessary because the scope of those regulations would effectively be subsumed by §1.958-1(d). Therefore, the proposed regulations would revise the applicability dates of §1.951A-1(e) and §1.951-1(h), so that those provisions do not apply once the final regulations under section 958 apply.

Historically, domestic partnerships have been treated as owning stock within the meaning of section 958(a) for purposes of determining their subpart F inclusions, and thus PTEP accounts were maintained, and related basis adjustments were made, at the partnership level. Upon the finalization of the proposed regulations, domestic partnerships will cease to be treated as owning stock of foreign corporations under section 958(a) for purposes of determining a subpart F inclusion, and instead their partners will be treated as owning stock under section 958(a). The Treasury Department and the IRS request comments on appropriate rules for the transition to the aggregate approach to domestic partnerships described in the proposed regulations. Comments are specifically requested as to necessary adjustments to PTEP and related basis amounts and capital accounts after finalization. In addition, comments are requested as to whether aggregate treatment of domestic partnerships should be extended to other “pass-through” entities, such as certain trusts or estates.

Comments are also requested with respect to the application of the PFIC regime after finalization, and whether elections (including elections under sections 1295 and 1296) and income inclusions under the PFIC rules are more appropriately made at the level of the domestic partnership or at the level of the partners. Specifically, the Treasury Department and the IRS are considering the operation of the PFIC regime where U.S. persons are partners of a domestic partnership that owns stock of a foreign corporation that is a PFIC, some of those partners might themselves be U.S. shareholders of the foreign corporation, and the foreign corporation might not be treated as a PFIC with respect to such U.S. shareholders under section 1297(d) if the foreign corporation is also a CFC. Comments should consider how any recommended approach would interact with the determinations of a partner's basis in its interest and capital accounts determined and maintained in accordance with §1.704-1(b)(2).

II. GILTI High Tax Exclusion

A. Expansion to exclude other high-taxed income

In response to comments, the Treasury Department and the IRS have determined that the GILTI high tax exclusion should be expanded (on an elective basis) to include certain high-taxed income even if that income would not otherwise be FBCI or insurance income. In particular, the Treasury Department and the IRS have determined that taxpayers should be permitted to elect to apply the exception under section 954(b)(4) with respect to certain classes of income that are subject to high foreign taxes within the meaning of that provision. Before the Act, such an election would have had no effect with respect to items of income that were excluded from FBCI or insurance income for other reasons. Nevertheless, section 954(b)(4) is not explicitly restricted in

its application to an item of income that first qualifies as FBCI or insurance income; rather, the provision applies to “any item of income received by a controlled foreign corporation.” Therefore, any item of gross income, including an item that would otherwise be gross tested income, could be excluded from FBCI or insurance income “by reason of” section 954(b)(4) if the provision is one of the reasons for such exclusion, even if the exception under section 954(b)(4) is not the sole reason. Any item thus excluded from FBCI or insurance income by reason of section 954(b)(4) would then also be excluded from gross tested income under the GILTI high tax exclusion, as modified in these proposed regulations.

The legislative history evidences an intent to exclude high-taxed income from gross tested income. See Senate Explanation at 371 (“The Committee believes that certain items of income earned by CFCs should be excluded from the GILTI, either because they should be exempt from U.S. tax—as they are generally not the type of income that is the source of base erosion concerns—or are already taxed currently by the United States. Items of income excluded from GILTI because they are exempt from U.S. tax under the bill include foreign oil and gas extraction income (which is generally immobile) and income subject to high levels of foreign tax.”). The proposed regulations, which permit taxpayers to electively exclude a CFC’s high-taxed income from gross tested income, are consistent, therefore, with this legislative history. Furthermore, an election to exclude a CFC’s high-taxed income from gross tested income allows a U.S. shareholder to ensure that its high-taxed non-subpart F income is eligible for the same treatment as its high-taxed FBCI and insurance income, and thus eliminates an incentive for taxpayers to restructure their CFC operations in order to convert gross

tested income into FBCI for the sole purpose of availing themselves of section 954(b)(4) and, thus, the GILTI high tax exclusion.

For the foregoing reasons, the proposed regulations provide that an election may be made for a CFC to exclude under section 954(b)(4), and thus to exclude from gross tested income, gross income subject to foreign income tax at an effective rate that is greater than 90 percent of the rate that would apply if the income were subject to the maximum rate of tax specified in section 11 (18.9 percent based on the current rate of 21 percent). See proposed §1.951A-2(c)(6)(i). The election is made by the CFC's controlling domestic shareholders with respect to the CFC for a CFC inclusion year by attaching a statement to an amended or filed return in accordance with forms, instructions, or administrative pronouncements. See proposed §1.951A-2(c)(6)(v)(A). If an election is made with respect to a CFC, the election applies to exclude from gross tested income all the CFC's items of income for the taxable year that meet the effective rate test in proposed §1.951A-2(c)(6)(iii) and is binding on all the U.S. shareholders of the CFC. See proposed §1.951A-2(c)(6)(v)(B). The election is effective for a CFC for the CFC inclusion year for which it is made and all subsequent CFC inclusion years of the CFC unless revoked by the controlling domestic shareholders of the CFC. See proposed §1.951A-2(c)(6)(v)(C).

An election may generally be revoked by the controlling domestic shareholders of the CFC for any CFC inclusion year. See proposed §1.951A-2(c)(6)(v)(D)(1). However, upon revocation for a CFC inclusion year, a new election generally cannot be made for any CFC inclusion year of the CFC that begins within sixty months after the close of the CFC inclusion year for which the election was revoked, and that subsequent election

cannot be revoked for a CFC inclusion year that begins within sixty months after the close of the CFC inclusion year for which the subsequent election was made. See proposed §1.951A-2(c)(6)(v)(D)(2)(i). An exception to this 60-month limitation may be permitted by the Commissioner with respect to a CFC if the CFC undergoes a change of control. See proposed §1.951A-2(c)(6)(v)(D)(2)(ii).

Finally, if a CFC is a member of a controlling domestic shareholder group, the election applies with respect to each member of the controlling domestic shareholder group. See proposed §1.951A-2(c)(6)(v)(E)(1). A “controlling domestic shareholder group” is defined as two or more CFCs if more than 50 percent of the stock (by voting power) of each CFC is owned (within the meaning of section 958(a)) by the same controlling domestic shareholder (or persons related to such controlling domestic shareholder) or, if no single controlling domestic shareholder owns (within the meaning of section 958(a)) more than 50 percent of the stock (by voting power) of each corporation, more than 50 percent of the stock (by voting power) of each corporation is owned (within the meaning of section 958(a)) in the aggregate by the same controlling domestic shareholders and each controlling domestic shareholder owns (within the meaning of section 958(a)) the same percentage of stock in each CFC. See proposed §1.951A-2(c)(6)(v)(E)(2). Accordingly, an election made under proposed §1.951A-2(c)(6)(v) applies with respect to each item of income of each CFC in a group of commonly controlled CFCs that meets the effective rate test in proposed §1.951A-2(c)(6)(iii). The Treasury Department and the IRS request comments on the manner and terms of the election for the exception from gross tested income, including whether the limitations with respect to revocations and the consistency requirements should be

modified, such as by allowing the election to be made on an item-by-item or a CFC-by-CFC basis.

In general, the relevant items of income for purposes of the election under section 954(b)(4) pursuant to proposed §1.951A-2(c)(6) are all items of gross tested income attributable to a qualified business unit (“QBU”). See proposed §1.951A-2(c)(6)(ii)(A)(1). For example, a CFC that owns a disregarded entity that qualifies as a QBU may have one item of income with respect to the CFC itself (which is a per se QBU) and another item of income with respect to the disregarded entity. The proposed regulations provide that the gross income attributable to a QBU is determined by reference to the items of gross income reflected on the books and records of the QBU, determined under Federal income tax principles, except that income attributable to a QBU must be adjusted to account for certain disregarded payments. See proposed §1.951A-2(c)(6)(ii)(A)(2). The proposed regulations provide an example to illustrate the application of this rule. See proposed §1.951A-2(c)(6)(vi).

Comments are requested on whether additional rules are needed to properly account for other instances in which the income base upon which foreign tax is imposed does not match the items of income reflected on the books and records of the QBU determined under Federal income tax principles. For example, comments are requested on whether special rules are needed for associating taxes with income with respect to partnerships (including hybrid partnerships), disregarded entities, or reverse hybrid entities, and how to address circumstances in which QBUs are permitted to share losses or determine tax liability based on combined income for foreign tax purposes. Comments are also requested as to whether all of a CFC’s QBUs located

within a single foreign country or possession should be combined for purposes of performing the effective rate test in proposed §1.951A-2(c)(6)(iii) and whether the definition of QBU should be modified for purposes of the GILTI high tax exclusion in respect of the requirement to have a trade or business, maintain books and records, or other rules relating to QBUs.

Under §1.954-1(d)(3), the determination of taxes paid or accrued with respect to an item of income for purposes of the exception under section 954(b)(4) is determined for each U.S. shareholder based on the amount of foreign income taxes that would be deemed paid under section 960 if the item of income were included by the U.S. shareholder under section 951(a)(1)(A). Calculating the effective tax rate for purposes of the election under section 954(b)(4) with respect to gross tested income by reference to section 960(d) would not be consistent with the aggregate nature of the computation under section 960(d). Furthermore, the Treasury Department and the IRS have determined that the Act's change to section 960(a) from a pooling based approach to an annual attribution of taxes to income requires revising §1.954-1(d)(3). Therefore, the proposed regulations provide that for purposes of both the exception under section 954(b)(4) and the GILTI high tax exclusion, the effective rate of foreign tax imposed on an item of income is determined solely at the CFC level by allocating and apportioning the foreign income taxes paid or accrued by the CFC in the current year to the CFC's gross income in that year based on the rules described in the regulations under section 960 for determining foreign income taxes "properly attributable" to income. See §1.960-1(d), as proposed to be amended in 83 FR 63257 (December 7, 2018).

To the extent foreign income taxes are allocated and apportioned to items of income that are excluded from gross tested income by the GILTI high tax exclusion, none of those foreign income taxes are properly attributable to tested income and thus none are allowed as a deemed paid credit under section 960. See §1.960-1(e), as proposed to be amended in 83 FR 63259 (December 7, 2018). In addition, if an item of income is excluded from gross tested income by reason of the GILTI high tax exclusion, the property used to produce that income, because not used in the production of gross tested income, does not qualify as specified tangible property, in whole or in part, and therefore the adjusted basis in the property is not taken into account in determining qualified business asset investment. See §1.951A-3(b) and (c)(1).

The proposed regulations also clarify the scope of each item of income under §1.954-1(c)(1)(iii), consistent with the rules under §1.960-1(d)(2)(ii)(B), as proposed to be amended in 83 FR 63257 (December 7, 2018).

B. Applicability date

The changes related to the election to exclude a CFC's gross income subject to high foreign income taxes under section 954(b)(4) are proposed to apply to taxable years of foreign corporations beginning on or after the date that final regulations are published in the **Federal Register**, and to taxable years of U.S. shareholders in which or with which such taxable years of foreign corporations end.

Special Analyses

I. Regulatory Planning and Review – Economic Analysis

Executive Orders 13771, 13563, and 12866 direct agencies to assess costs and benefits of available regulatory alternatives and, if regulation is necessary, to select

regulatory approaches that maximize net benefits, including potential economic, environmental, public health and safety effects, distributive impacts, and equity. Executive Order 13563 emphasizes the importance of quantifying both costs and benefits, reducing costs, harmonizing rules, and promoting flexibility. The Executive Order 13771 designation for any final rule resulting from the proposed regulation will be informed by comments received. The preliminary Executive Order 13771 designation for this proposed rule is regulatory.

The proposed regulation has been designated by the Office of Information and Regulatory Affairs (OIRA) as subject to review under Executive Order 12866 pursuant to the Memorandum of Agreement (MOA, April 11, 2018) between the Treasury Department and the Office of Management and Budget regarding review of tax regulations. OIRA has designated this proposed regulation as economically significant under section 1(c) of the MOA. Accordingly, these proposed regulations have been reviewed by the Office of Management and Budget. For more detail on the economic analysis, please refer to the following analysis.

A. Need for the proposed regulations

The proposed regulations are required to provide a mechanism by which taxpayers can elect the high tax exception of section 954(b)(4) in order to exclude certain high-taxed income from taxation under section 951A and to conform the treatment of domestic partnerships for purposes of the subpart F regime with the treatment of domestic partnerships for purposes of section 951A.

B. Background

The Tax Cuts and Jobs Act (the “Act”) established a system under which certain earnings of a foreign corporation can be repatriated to a corporate U.S. shareholder without U.S. tax. See section 14101(a) of the Act and section 245A. However, Congress recognized that, without any base protection measures, this system, known as a participation exemption system, could incentivize taxpayers to allocate income – in particular, mobile income from intangible property that would otherwise be subject to the full U.S. corporate tax rate – to controlled foreign corporations (“CFCs”) operating in low- or zero-tax jurisdictions. See Senate Explanation at 365. Therefore, Congress enacted section 951A in order to subject intangible income earned by a CFC to U.S. tax on a current basis, similar to the treatment of a CFC’s subpart F income under section 951(a)(1)(A). However, in order to not harm the competitive position of U.S. corporations relative to their foreign peers, the global intangible low tax income (“GILTI”) of a corporate U.S. shareholder is effectively taxed at a reduced rate by reason of the deduction under section 250 (with the resulting U.S. tax further reduced by a portion of foreign tax credits under section 960(d)). *Id.*

The GILTI final regulations generally provide structure and clarity for the implementation of section 951A. However, the Treasury Department and the IRS determined that there remained two outstanding issues pertinent to the implementation of GILTI. The first of these issues pertains to the GILTI high tax exclusion under section 951A(c)(2)(A)(i)(III), which excludes from gross tested income any gross income excluded from foreign base company income (“FBCI”) (as defined in section 954) and insurance income (as defined in section 953) by reason of section 954(b)(4). The GILTI proposed regulations limited the application of the exclusion to income that would be

included in FBCI or insurance income but for the high tax exception of section 954(b)(4). See proposed §1.951A-2(c)(1)(iii). However, comments to the GILTI proposed regulations recommended that the statute be interpreted so that the GILTI high tax exclusion applies on an elective basis to a broader category of income, that is, any income that is subject to a high rate of foreign tax. Other comments suggested that because taxpayers have the ability to structure transactions so that they would qualify as FBCI or insurance income, the regulations should allow a taxpayer to elect to treat all income, or all high-taxed income, as FBCI or insurance income, with the result that such income would then be excluded from gross tested income under the GILTI high tax exclusion. Comments noted that, under the narrower application of the exclusion under the GILTI proposed regulations, taxpayers would be incentivized to affirmatively plan into subpart F income to permit such taxpayers to elect the high tax exception under section 954(b)(4) with respect to such income or to allow taxpayers to carry foreign tax credits attributable to such income to another taxable year under section 904(c). However, restructuring activities to convert gross tested income into subpart F income may cost significant time and money and is economically inefficient. The GILTI final regulations adopt this narrower application. See proposed §1.951A-2(c)(1)(iii). However, the preamble to the GILTI final regulations indicated that proposed regulations would be issued to propose a framework under which taxpayers would be permitted to make an election to apply the high tax exception of section 954(b)(4) with respect to income that would otherwise be gross tested income in order to exclude that income from gross tested income by reason of the GILTI high tax exclusion.

The second of these issues pertains to the treatment of domestic partnerships for purposes of the subpart F regime. A U.S. shareholder of a CFC is required to include in gross income its pro rata share of the CFC's subpart F income under section 951(a)(1)(A), the amount determined under section 956, under section 951(a)(1)(B), and its GILTI inclusion amount under section 951A(a). Since the enactment of subpart F, domestic partnerships have generally been treated as entities separate from their partners, rather than as aggregates of their partners, for purposes of the subpart F regime, including for purposes of treating a domestic partnership as the U.S. shareholder that has the subpart F inclusion with respect to a CFC owned by the partnership. However, the GILTI final regulations generally adopt an aggregate approach to domestic partnerships for purposes of section 951A and the section 951A regulations. See §1.951A-1(e)(1). Because the GILTI final regulations apply only for purposes of section 951A, absent the proposed regulations, a domestic partnership would still be treated as an entity for purposes of the subpart F regime. This inconsistency in the treatment of a domestic partnership for the purposes of section 951A and for purposes of the subpart F regime is problematic because it necessitates complicated coordination rules which could greatly increase compliance and administrative burden. Therefore, the proposed regulations conform the treatment of domestic partnerships for purposes of the subpart F regime with the treatment of domestic partnerships for purposes of section 951A.

C. Economic analysis

1. Baseline

The Treasury Department and the IRS have assessed the benefits and costs of the proposed regulations relative to a no-action baseline reflecting anticipated Federal income tax-related behavior in the absence of these proposed regulations.

2. Summary of Economic Effects

To assess the economic effects of the proposed regulations, the Treasury Department and the IRS considered economic effects arising from two provisions of the proposed regulations. These are (i) effects arising from the provision that provides substance and clarity regarding the application of the GILTI high tax exclusion in 951A(c)(2)(A)(i)(III) and (ii) simplification and coordination effects arising from conforming the treatment of domestic partnerships for purposes of subpart F with their treatment for purposes of section 951A.

The Treasury Department and the IRS have not undertaken quantitative estimates of these effects because any such quantitative estimates would be highly uncertain. For example, the proposed regulations include provisions that permit controlling domestic shareholders of CFCs to elect to apply the high tax exception of section 954(b)(4) to items of gross income that are subject to a foreign tax rate that is greater than 18.9 percent (based on the current U.S. corporate tax rate of 21 percent) for purposes of excluding such income from gross tested income under the GILTI high tax exclusion. Whether controlling domestic shareholders will choose to make the election will depend on their specific facts and circumstances, such as their U.S. expenses allocated to section 951A category income, their foreign tax credit position,

and the distribution of their foreign activity between high- and low-tax jurisdictions.² Because GILTI is new, the Treasury Department and the IRS do not have readily available data to project these items in this context. Furthermore, the election would be made with respect to qualified business units (QBU) rather than with respect to CFCs or specific items of income, and the Treasury Department and the IRS do not have readily available data on activities at the QBU level. In addition, due to the taxpayer-specific nature of the factors influencing a decision to utilize the GILTI high-tax exclusion, the Treasury Department and the IRS do not have readily available data or models to predict the marginal effective tax rates that would prevail under these provisions for the varied forms of foreign investments that taxpayers might consider and thus cannot predict with reasonable precision the difference in economic activity, relative to the baseline, that might be undertaken by taxpayers based on this election.

The proposed regulations also contain provisions to conform the treatment of domestic partnerships for purposes of subpart F with their treatment for purposes of section 951A. Under the proposed regulations, the tax treatment of domestic partners

² Specifically, the U.S. tax system reduces double taxation on a U.S. shareholder's GILTI inclusion amount by crediting a portion of certain foreign taxes paid by CFCs against the U.S. tax on the U.S. shareholder's GILTI inclusion amount. However, the U.S. foreign tax credit regime requires taxpayers to allocate U.S. deductible expenses, including interest, research and experimentation, and general and administrative expenses, to their foreign source income in the categories described in section 904(d) when determining the allowable foreign tax credits. The allocated expenses reduce net foreign source income within the section 904(d) categories, which can reduce allowable foreign tax credits. This may result in a smaller foreign tax credit than would be allowed if the limitation on foreign tax credits was determined based only on the local country tax assessed on the tested income taken into account in determining GILTI. The election to apply the high tax exception of section 954(b)(4) with respect to any high-taxed income allows taxpayers to eliminate the need to use foreign tax credits to reduce GILTI tax liability on such income by removing such income from gross tested income; however, taxpayers choosing the election will not be able to use the foreign tax credits associated with that income against other section 951A category income, and they will not be able to use the tangible assets owned by high tax QBU in their QBAI computation. Therefore, taxpayers will have to evaluate their individual facts and circumstances to determine whether they should make the election.

that are U.S. shareholders of a CFC owned by the domestic partnership differs from the tax treatment of domestic partners that are not U.S. shareholders of such CFC. The Treasury Department and the IRS do not have readily available data to identify these types of partners. The Treasury Department and the IRS further do not have readily available data or models to predict with reasonable precision the set of marginal effective tax rates that taxpayers might face under these provisions nor the effects of those marginal effective tax rates on economic activity relative to the baseline.

With these considerations in mind, parts I.C.3.a.ii and iii of this Special Analyses section explain the rationale behind the proposed regulations' approach to the GILTI high tax exclusion and qualitatively evaluate the alternatives considered. Part 1.C.3.b of this Special Analyses section explains the rationale for the coordination in the treatment of domestic partnerships and qualitatively evaluates the alternatives considered.

3. Economic Effects of Specific Provisions

The Treasury Department and IRS solicit comments on each of the items discussed in this Special Analyses section and on any other items of the proposed regulations not discussed in this section. The Treasury Department and the IRS particularly solicit comments that provide data, other evidence, or models that could enhance the rigor of the process by which the final regulations might be developed.

a. Exclusion of Income Subject to High Rate of Foreign Tax

i. Description

The proposed regulations permit U.S. shareholders of CFCs to make an election under section 954(b)(4) with respect to high-taxed income in order to exclude such income from gross tested income under the GILTI high tax exclusion. Under section

954(b)(4), high-taxed income is defined as income subject to a foreign effective tax rate greater than 90 percent of the maximum U.S. corporate tax rate (18.9 percent based on the current U.S. corporate tax rate of 21 percent). Under the proposed regulations, the determination as to whether income is high-taxed is made at the QBU level. However, an election made with respect to a CFC applies with respect to each high-taxed QBU of the CFC (including potentially the CFC itself), and a U.S. shareholder that makes the election with respect to a CFC generally must make the same election with respect to each of its CFCs. In general, the election may be made or revoked at any time, except that, if a U.S. shareholder revokes an election with respect to a CFC, the U.S. shareholder cannot make the election again within five years after the revocation, and then if subsequently made, the election cannot be revoked again within five years of the subsequent election.

ii. Alternatives Considered for Determining the Scope of the GILTI High Tax Exclusion

The Treasury Department and the IRS considered a number of options to address the types of income excluded from gross tested income by the GILTI high tax exclusion. The options were (i) to exclude from gross tested income only income that would be subpart F income but for the high tax exception of section 954(b)(4); (ii) in addition to excluding the aforementioned income, to exclude from gross tested income on an elective basis an item of gross income that is excluded by reason of another exception to subpart F, if such income is subject to a foreign effective tax rate greater than 18.9 percent; and (iii) to exclude from gross tested income on an elective basis any item of gross income subject to a foreign effective tax rate greater than 18.9 percent.

The Treasury Department and the IRS considered the other recommended options

discussed in part IV.B of the Background section, but determined that those other options are not authorized by the relevant statutory provisions.

The first option considered was to exclude from gross tested income only income that would be FBCI or insurance income but for the high tax exception of section 954(b)(4), which is the interpretation of the GILTI high tax exclusion in the GILTI proposed regulations. This narrow approach is consistent with a reasonable interpretation of the statutory text, which excludes from gross tested income only income that is excluded from subpart F income “by reason of section 954(b)(4).” Moreover, this approach is consistent with current regulations under section 954, which permit an election under section 954(b)(4) only with respect to income that is not otherwise excluded from subpart F income by reason of another exception (for example, section 954(c)(6) or 954(h)). However, under this approach, taxpayers with high-taxed gross tested income would have incentives to restructure their foreign operations in order to convert their gross tested income into subpart F income. For instance, a taxpayer could restructure its operations to have a CFC purchase personal property from, or sell personal property to, a related person without substantially contributing to the manufacture of the property in its country of incorporation, with the result that the CFC’s income from the disposition of the property is foreign base company sales income within the meaning of section 954(d). Any such restructuring may be unduly costly and only available to certain taxpayers. Further, such reorganization to realize a specific income treatment suggests that tax instead of business considerations are determining business structures. This can lead to higher compliance costs and

inefficient investment. Therefore, the Treasury Department and the IRS rejected this option.

The second option considered was to broaden the application of the GILTI high tax exclusion to allow taxpayers to elect under the high tax exception of section 954(b)(4) to exclude from gross tested income an item of gross income that is subject to a foreign effective tax rate greater than 18.9 percent, if such income was also excluded from FBCI or insurance income by reason of another exception to subpart F. Under this interpretation, income such as active financing income that is excluded from subpart F income under section 954(h), active rents or royalties that are excluded from subpart F income under 954(c)(2)(A), and related party payments that are excluded from subpart F income under section 954(c)(6) could also be excluded from gross tested income under the GILTI high tax exclusion if such items of income are high taxed within the meaning of section 954(b)(4). This broader approach represents a plausible interpretation of the GILTI high tax exclusion; that is, that an item of income could be excluded both “by reason of section 954(b)(4)” and by reason of another exception. However, this approach would provide taxpayers the ability to exclude their CFCs’ high-taxed income that would be subpart F income but for an exception (for example, active financing income), while denying taxpayers the same ability with respect to their CFCs’ high-taxed income that is not subpart F income in the first instance (for example, active business income), without any general economic benefit from such differential treatment. Furthermore, taxpayers with items of high-taxed income that are not subpart F income would still be incentivized to restructure their foreign operations in order to convert their high-taxed gross tested income into subpart F income, which poses the

same compliance costs and inefficiencies as the first option. Therefore, the Treasury Department and the IRS rejected this option.

The third option, which is adopted in the proposed regulations, is to provide an election to broaden the scope of the high tax exception under section 954(b)(4) for purposes of the GILTI high tax exclusion to apply to any item of income that is subject to a foreign effective tax rate greater than 18.9 percent. The proposed regulations permit controlling domestic shareholders of CFCs to elect to apply the high tax exception under section 954(b)(4) to items of gross income that would not otherwise be FBCI or insurance income. If this high tax exception is elected, the GILTI high tax exclusion will exclude the item of gross income from gross tested income. Under the election, an item of gross income is subject to a high rate of foreign tax if, after taking into account properly allocable expenses, the net item of income is subject to a foreign effective tax rate greater than 90 percent of the maximum U.S. corporate tax rate (18.9 percent based on the current U.S. corporate tax rate of 21 percent). This option therefore establishes a framework for applying the high tax exception under section 954(b)(4), including rules to determine the scope of an item of income that would otherwise be gross tested income to which the election applies and to determine the rate of foreign tax on such item.

The approach chosen by the proposed regulations is consistent with the legislative history to section 951A, which evidences an intent to tax low-taxed income of CFCs that presents base erosion concerns. The approach is also supported by a reasonable interpretation of the high tax exception of section 954(b)(4), which applies to “any item of income” of a CFC, not just income that would otherwise be FBCI or

insurance income. Furthermore, contrary to the first two options, this approach permits all similarly situated taxpayers with CFCs subject to a high rate of foreign tax to make the election with respect to such income to exclude it from gross tested income, and reduces the incentive for taxpayers to restructure their operations to convert their high-taxed gross tested income into subpart F income for U.S. tax purposes.

For taxpayers that make the election, this approach reduces the taxpayers' cost of capital on foreign investment by reducing U.S. tax on such taxpayers' GILTI relative to the baseline. At the margin, the lower cost of capital may increase foreign investment by U.S.-parented firms. Further, removing high-taxed tested income from the GILTI tax base could change the incentives for the location of tangible assets. The magnitude of these effects is highly uncertain because of the uncertainty surrounding the number and attributes of the taxpayers that will find it advantageous to make the election and because the relationship between the marginal effective tax rate at the QBU level and foreign investment by U.S. taxpayers is not well known. In addition, the impact of tax considerations on taxpayer investment decisions depends on a number of international tax provisions, many of which interact in complex ways.

iii. Alternatives Considered for Determining High-Taxed Income

The Treasury Department and the IRS next considered options for determining whether an item of income is subject to the foreign effective tax rate described in section 954(b)(4). The options considered were (i) apply the determination on an item-by-item basis; (ii) apply the determination on a CFC-by-CFC basis; or (iii) apply the determination on a QBU-by-QBU basis.

The first option was to determine whether income is high-taxed income within the meaning of section 954(b)(4) on an item-by-item basis. This approach would be consistent with the language of section 954(b)(4), which applies to an “item of income” of a CFC that is sufficiently high tax. However, this approach would be complex and difficult to administer because it would require analyzing each item of income to determine whether, under Federal tax principles, such item is subject to a sufficiently high foreign effective tax rate. In fact, for this reason, the current regulations that implement the high tax exception of section 954(b)(4) for purposes of subpart F income do not require an item-by-item determination and aggregate all items of income into separate categories of income for purposes of determining whether each such category is high tax. See §1.954-1(d)(2). Therefore, the Treasury Department and the IRS rejected this option.

The second option was to apply the determination based on all the items of income of the CFC. On the one hand, this approach would minimize complexity and would be relatively easy to administer. On the other hand, this approach could permit inappropriate tax planning, such as combining operations subject to different rates of tax into a single CFC. This would have the effect of “blending” the rates of foreign tax imposed on the income, which could result in low- or non-taxed income being excluded as high-taxed income by being blended with much higher-taxed income. The low-taxed income in this scenario is precisely the sort of base erosion-type income that the legislative history describes section 951A as intending to tax, and such tax motivated planning behavior is economically inefficient.

The third option, which is adopted in the proposed regulations, is to apply the high tax exception based on the items of gross income of a QBU of the CFC. Under this approach, the net income that is taxed by the foreign jurisdiction in each QBU must be determined. For example, if a CFC earned \$100x of tested income through a QBU in Country A and was taxed at a 30 percent rate and earned \$100x of tested income through another QBU in Country B and was taxed at 0 percent, the blended rate of tax on all of the CFC's tested income is 15 percent ($\$30x \text{ tax} / \$200x \text{ tested income}$). However, if the high tax exception applies to each of a CFC's QBUs based on the income earned by that QBU then the blending of different rates would be minimized. Although applying the high tax exception on the basis of a QBU, rather than the CFC as a whole, may be more complex and administratively burdensome under certain circumstances, it more accurately pinpoints income subject to a high rate of foreign tax and therefore continues to subject to tax the low-taxed base erosion-type income that the legislative history describes section 951A as intending to tax. Accordingly, the proposed regulations apply the high tax exception of section 954(b)(4) based on the items of net income of each QBU of the CFC.

iv. Affected Taxpayers

The proposed regulations potentially affect those taxpayers that have at least one CFC with at least one QBU (including, potentially, the CFC itself) that has high-taxed income. A taxpayer with CFCs that have a mix of high-taxed and low-taxed income (determined on a QBU-by-QBU basis) will need to evaluate the benefit of eliminating any tax under section 951A with respect to high-taxed income with the costs of forgoing the use of such taxes against other section 951A category income and the

use of tangible assets in the computation of QBAI. Taxpayers with CFCs that have only low-taxed income are not eligible to elect the high tax exception and hence are unaffected by this provision.

The Treasury Department and the IRS estimate that there are approximately 4,000 business entities (corporations, S corporations, and partnerships) with at least one CFC that pays a foreign effective tax rate above 18.9 percent. The Treasury Department and the IRS further estimate that, for the partnerships with at least one CFC that pays a foreign effective tax rate greater than 18.9 percent, there are approximately 1,500 partners that have a large enough share to potentially qualify as a 10 percent U.S. shareholder of the CFC.³ The 4,000 business entities and the 1,500 partners provide an approximate estimate of the number of taxpayers that could potentially be affected by an election into the high tax exception. The figure is approximate since there is an imperfect correspondence between high-taxed CFCs and high-taxed QBUs, and, furthermore, not all taxpayers that are eligible for the election would choose to make the election. The Treasury Department and the IRS do not have readily available data to determine how many of these taxpayers would benefit from the election.

Tabulations from the IRS Statistics of Income 2014 Form 5471 file⁴ further indicate that approximately 85 percent of earnings and profits before taxes of CFCs are

³ Data are from IRS's Research, Applied Analytics, and Statistics division based on E-file data available in the Compliance Data Warehouse, for tax years 2015 and 2016. The counts include Category 4 and Category 5 IRS Form 5471 filers. Category 4 filers are U.S. persons who had control of a foreign corporation during the annual accounting period of the foreign corporation. Category 5 filers are U.S. shareholders who own stock in a foreign corporation that is a CFC and who owned that stock on the last day in the tax year of the foreign corporation in that year in which it was a CFC. For full definitions, see <https://www.irs.gov/pub/irs-pdf/i5471.pdf>.

⁴ The IRS Statistics of Income Tax Stats report on Controlled Foreign Corporations can be accessed here: <https://www.irs.gov/statistics/soi-tax-stats-controlled-foreign-corporations>.

subject to an average foreign effective tax rate that is less than or equal to 18.9 percent, accounting for approximately 30 percent of CFCs. The data indicate several examples of jurisdictions with effective tax rates above 18.9 percent, such as France, Italy, and Japan. However, information is not readily available to determine how many QBUs are part of the same CFC and what the effective foreign tax rates are with respect to such QBUs. Furthermore, the determination of whether or not to elect the high tax exception will be made at the shareholder (not CFC) level, after having evaluated the full impact of doing so across all of the shareholder's CFCs. Taxpayers potentially more likely to elect the high tax exception are those taxpayers with CFCs that only operate in high-tax jurisdictions.

b. Domestic Partnership Treatment for Subpart F

i. Description

Under the statute, a U.S. shareholder of a CFC is required to include in gross income its pro rata share of the CFC's subpart F income under section 951(a)(1)(A), the amount determined under section 956, under section 951(a)(1)(B), and its GILTI inclusion amount under section 951A. The Code does not explicitly prescribe the treatment of domestic partnerships and their partners for purposes of subpart F. However, domestic partnerships have generally been treated as entities separate from their partners, rather than as aggregates of their partners, for purposes of subpart F, including for purposes of determining the amount included in the gross income of the domestic partnership (and the distributive share of such amount of its domestic partners) under section 951(a). The GILTI final regulations adopt an aggregate

approach to domestic partnerships, but this aggregate treatment applies only for purposes of section 951A.

ii. Alternatives Considered

The Treasury Department and the IRS considered two options for the treatment of domestic partnerships for purposes of subpart F. The first option was to retain the entity approach to domestic partnerships for purposes of subpart F. While this approach would be consistent with the longstanding entity approach to domestic partnerships for purposes of subpart F inclusions, it would result in domestic partnerships being treated inconsistently for purposes of subpart F and section 951A, despite both regimes applying to U.S. shareholders and their CFCs. This inconsistent treatment of domestic partnerships could result in a domestic partnership including subpart F income in gross income under section 951(a) and its partners including GILTI in their gross income under section 951A(a), which would introduce substantial complexity and uncertainty in the application of provisions that require basis and E&P adjustments with respect to CFCs and their U.S. shareholders for amounts included in income under sections 951(a) and 951A(a). This option would also continue the inconsistent treatment of domestic partnerships and foreign partnerships (which generally are treated as aggregates) for purposes of the subpart F rules, despite the lack of a substantial policy justification for treating domestic partners of a partnership differently based upon the law under which the partnership is created or organized. In this regard, this option would require “small” partners of a domestic partnership (that is, partners that are not themselves U.S. shareholders or CFCs owned by the domestic partnership) to include in income their distributive share of the domestic partnership’s

subpart F inclusion with respect to CFCs of which the small partners are not themselves U.S. shareholders. In contrast, if the domestic partnership were instead a foreign partnership, the small partners would not include any amount in gross income under section 951(a) (or a distributive share of such amount) with respect to CFCs of which such partners were not U.S. shareholders.

The second option would adopt an aggregate approach to domestic partnerships by treating stock owned by a domestic partnership as being owned proportionately by its partners for purposes of determining the U.S. shareholder that has the subpart F inclusion. This approach is consistent with the approach adopted for section 951A in the GILTI final regulations. Under this approach, a domestic partnership would not be the U.S. shareholder of a foreign corporation that includes subpart F income in its gross income under section 951(a). Instead, only the partners of the domestic partnership that are U.S. shareholders of a CFC owned through the domestic partnership would include subpart F income of the CFC in their gross income.

This approach is supported by public comments requesting harmonization of the treatment of domestic partnerships for purposes of the GILTI and subpart F regimes. The harmonization of the treatment of domestic partnerships for purposes of the GILTI and subpart F regimes is expected to result in substantial simplification of related rules (for example, previously taxed earnings and profits and related basis rules), consistency in the treatment of domestic partnerships and foreign partnerships, and the reduction of burden (both administrative burden and tax liability) on taxpayers that are small partners. This third option is effectuated in the proposed regulations by using the

existing framework for foreign partnerships, which is well-developed and more administrable than a new framework.

iii. Affected Taxpayers

The Treasury Department and the IRS estimate that there were approximately 7,000 U.S. partnerships with CFCs that e-filed at least one Form 5471 as Category 4 or 5 filers in 2015 and 2016.⁵ The identified partnerships had approximately 2 million partners, as indicated by the number of Schedules K-1 filed by the partnerships. This number includes both domestic and foreign partners, so it substantially overstates the number of partners that would be affected by the proposed regulations, which potentially affect only domestic partners.⁶ The proposed regulations affect domestic partners that are U.S. shareholders of a CFC owned by the domestic partnership because such partners will determine their subpart F inclusion amount by reference to their pro rata shares of subpart F income of CFCs owned by the partnership. Domestic partners that are not U.S. shareholders of a CFC owned by the domestic partnership will neither determine their own subpart F inclusion amount by reference to their pro rata shares of subpart F income of CFCs owned by the partnership nor include in their income a distributive share of the partnership's subpart F inclusion amount. This latter

⁵ Data are from IRS's Research, Applied Analytics, and Statistics division based on data available in the Compliance Data Warehouse. Category 4 filer includes a U.S. person who had control of a foreign corporation during the annual accounting period of the foreign corporation. Category 5 includes a U.S. shareholder who owns stock in a foreign corporation that is a CFC and who owned that stock on the last day in the tax year of the foreign corporation in that year in which it was a CFC. For full definitions, see <https://www.irs.gov/pub/irs-pdf/i5471.pdf>.

⁶ This analysis is based on the tax data readily available to the Treasury Department at this time. Some variables may be available on tax forms that are not available for statistical purposes. Moreover, with new tax provisions, such as section 951A, relevant data may not be available for a number of years for statistical purposes.

group is likely to be a substantial portion of domestic partners given the high number of partners per partnership, and they will have lower compliance costs as a result of the proposed regulations. Because it is not possible to precisely identify these types of partners based on available data, this number is an upper bound of partners who would have been affected by this rule had this rule been in effect in 2015 or 2016.

II. Paperwork Reduction Act

The collection of information in these proposed regulations is in proposed §1.951A-2(c)(6)(v). The collection of information in proposed §1.951A-2(c)(6)(v) is an election that a controlling domestic shareholder of a CFC may make to apply the high tax exception of section 954(b)(4) to gross income of a CFC. The election is made by attaching a statement to an original or amended income tax return in order to elect to apply the high tax exception of section 954(b)(4) to gross income of a CFC. For purposes of the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)) (“PRA”), the reporting burden associated with proposed §1.951A-2(c)(6)(v) will be reflected in the PRA submission associated with income tax returns in the Form 990 series, Form 1120 series, Form 1040 series, Form 1041 series, and Form 1065 series (see chart at the end of this part II for the current status of the PRA submissions for these forms). In 2018, the IRS released and invited comments on drafts of the above five forms in order to give members of the public advance notice and an opportunity to submit comments. The IRS received no comments on the portions of the forms that relate to section 951A during the comment period. Consequently, the IRS made the forms available in late 2018 and early 2019 for use by the public. The IRS is contemplating making additional changes to forms to take into account these proposed regulations.

The IRS estimates the number of affected filers to be the following:

Tax Forms Impacted		
Collection of information	Number of respondents (estimated)	Forms to which the information may be attached
§1.951A-2(c)(6)(v) Election to apply the high tax exception of section 954(b)(4) to gross income of a CFC	25,000 - 35,000	Form 990 series, Form 1120 series, Form 1040 series, Form 1041 series, and Form 1065 series

Source: MeF, DCS, and IRS's Compliance Data Warehouse

This estimate is based on filers of income tax returns with a Form 5471, "Information Return of U.S. Persons With Respect to Certain Foreign Corporations," attached because only filers that are U.S. shareholders of CFCs would be subject to the information collection requirements.

The current status of the PRA submissions related to the tax forms that will be revised as a result of the information collection in proposed §1.951A-2(c)(6)(v) is provided in the accompanying table. The reporting burdens associated with the information collection in the proposed regulations are included in the aggregated burden estimates for OMB control numbers 1545-0123 (which represents a total estimated burden time for all forms and schedules for corporations of 3.157 billion hours and total estimated monetized costs of \$58.148 billion (\$2017)), 1545-0074 (which represents a total estimated burden time, including all other related forms and schedules for individuals, of 1.784 billion hours and total estimated monetized costs of \$31.764 billion (\$2017)), 1545-0092 (which represents a total estimated burden time, including all other related forms and schedules for trusts and estates, of 307,844,800 hours and total estimated monetized costs of \$9.950 billion (\$2016)), and 1545-0047 (which represents

a total estimated burden time, including all other related forms and schedules for tax-exempt organizations, of 50.450 million hours and total estimated monetized costs of \$1,297,300,000 (\$2017)). The overall burden estimates provided for these OMB control numbers are aggregate amounts that relate to the entire package of forms associated with the applicable OMB control number and will in the future include, but not isolate, the estimated burden of the tax forms that will be revised as a result of the information collection in the proposed regulations. These numbers are therefore unrelated to the future calculations needed to assess the burden imposed by the proposed regulations. These burdens have been reported for other regulations related to the taxation of cross-border income and the Treasury Department and the IRS urge readers to recognize that these numbers are duplicates and to guard against overcounting the burden that international tax provisions imposed prior to the Act. No burden estimates specific to the forms affected by the proposed regulations are currently available. The Treasury Department and the IRS have not estimated the burden, including that of any new information collections, related to the requirements under the proposed regulations. The Treasury Department and the IRS estimate PRA burdens on a taxpayer-type basis rather than a provision-specific basis. Those estimates would capture both changes made by the Act and those that arise out of discretionary authority exercised in the final regulations.

The Treasury Department and the IRS request comments on all aspects of information collection burdens related to the proposed regulations, including estimates for how much time it would take to comply with the paperwork burdens described above for each relevant form and ways for the IRS to minimize the paperwork burden.

Proposed revisions (if any) to these forms that reflect the information collections contained in these proposed regulations will be made available for public comment at <https://apps.irs.gov/app/picklist/list/draftTaxForms.htm> and will not be finalized until after these forms have been approved by OMB under the PRA.

Form	Type of Filer	OMB Number(s)	Status
Forms 990	Tax exempt entities (NEW Model)	1545-0047	Approved by OIRA 12/21/2018 until 12/31/2019. The form will be updated with OMB number 1545-0047 and the corresponding PRA Notice on the next revision.
	Link: https://www.reginfo.gov/public/do/PRAViewICR?ref_nbr=201811-1545-003		
Form 1040	Individual (NEW Model)	1545-0074	Limited Scope submission (1040 only) approved on 12/7/2018 until 12/31/2019. Full ICR submission for all forms in 6/2019. 60 Day FRN not published yet for full collection.
	Link: https://www.reginfo.gov/public/do/PRAViewICR?ref_nbr=201808-1545-031		
Form 1041	Trusts and estates	1545-0092	Submitted to OIRA for review on 9/27/2018.
	Link: https://www.reginfo.gov/public/do/PRAViewICR?ref_nbr=201806-1545-014		
Form 1065 and 1120	Business (NEW Model)	1545-0123	Approved by OIRA 12/21/2018 until 12/31/2019.
	Link: https://www.reginfo.gov/public/do/PRAViewICR?ref_nbr=201805-1545-019		

III. Regulatory Flexibility Act

It is hereby certified that these proposed regulations will not have a significant economic impact on a substantial number of small entities within the meaning of section 601(6) of the Regulatory Flexibility Act (5 U.S.C. chapter 6).

Section 951A generally affects U.S. shareholders of CFCs. The reporting burden in proposed §1.951A-2(c)(6)(v) affects controlling domestic shareholders of a CFC that

elect to apply the high tax exception of section 954(b)(4) to gross income of a CFC. Controlling domestic shareholders are generally U.S. shareholders who, in the aggregate, own more than 50 percent of the total combined voting power of all classes of stock of the foreign corporation entitled to vote. As an initial matter, foreign corporations are not considered small entities. Nor are U.S. taxpayers considered small entities to the extent the taxpayers are natural persons or entities other than small entities. Thus, proposed §1.951A-2(c)(6)(v) generally only affects small entities if a U.S. taxpayer that is a U.S. shareholder of a CFC is a small entity.

Examining the gross receipts of the e-filed Forms 5471 that is the basis of the 25,000 – 35,000 respondent estimates, the Treasury Department and the IRS have determined that the tax revenue from section 951A estimated by the Joint Committee on Taxation for businesses of all sizes is less than 0.3 percent of gross receipts as shown in the table below. Based on data for 2015 and 2016, total gross receipts for all businesses with gross receipts under \$25 million is \$60 billion while those over \$25 million is \$49.1 trillion. Given that tax on GILTI inclusion amounts is correlated with gross receipts, this results in businesses with less than \$25 million in gross receipts accounting for approximately 0.01 percent of the tax revenue. Data are not readily available to determine the sectoral breakdown of these entities. Based on this analysis, smaller businesses are not significantly impacted by these proposed regulations.

	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
JCT tax revenue	7.7 billion	12.5 billion	9.6 billion	9.5 billion	9.3 billion	9.0 billion	9.2 billion	9.3 billion	15.1 billion	21.2 billion
Total gross	30727 billion	53870 billion	566676 billion	59644 billion	62684 billion	65865 billion	69201 billion	72710 billion	76348 billion	80094 billion

receipts										
Percent	0.03	0.02	0.02	0.02	0.01	0.01	0.01	0.01	0.02	0.03

Source: Research, Applied Analytics and Statistics division (IRS), Compliance Data Warehouse (IRS) (E-filed Form 5471, category 4 or 5, C and S corporations and partnerships); Conference Report, at 689.

The data to assess the number of small entities potentially affected by proposed §1.951A-2(c)(6)(v) are not readily available. However, businesses that are U.S. shareholders of CFCs are generally not small businesses because the ownership of sufficient stock in a CFC in order to be a U.S. shareholder generally entails significant resources and investment. The Treasury Department and the IRS welcome comments on whether the proposed regulations would affect a substantial number of small entities in any particular industry.

Regardless of the number of small entities potentially affected by proposed §1.951A-2(c)(6)(v), the Treasury Department and the IRS have concluded that there is no significant economic impact on such entities as a result of proposed §1.951A-2(c)(6)(v). As discussed above, smaller businesses are not significantly impacted by the proposed regulations. Furthermore, the requirements in proposed §1.951A-2(c)(6)(v) apply only if a taxpayer chooses to make an election to apply a favorable rule. Consequently, the Treasury Department and the IRS have determined that proposed §1.951A-2(c)(6)(v) will not have a significant economic impact on a substantial number of small entities. Accordingly, it is hereby certified that the collection of information requirements of proposed §1.951A-2(c)(6)(v) would not have a significant economic impact on a substantial number of small entities. Notwithstanding this certification, the

Treasury Department and the IRS invite comments from the public on the impact of proposed §1.951A-2(c)(6)(v) on small entities.

The treatment of domestic partnerships as an aggregate of their partners in these proposed regulations for purposes of subpart F would reduce the burden on partners that are not U.S. shareholders of a CFC owned by the partnership because these partners will no longer be required to include in income a distributive share of subpart F income. The proposed regulations would also reduce burden on domestic partnerships that hold CFCs because these partnerships would no longer be required to calculate their partners' distributive share of subpart F income, resulting in compliance cost savings for the affected partnerships. As described in section II of this Special Analyses section, the Treasury Department and the IRS estimate that there are approximately 7,000 U.S. partnerships with CFCs that e-filed at least one Form 5471 as Category 4 or 5 filers in 2015 and 2016.⁷ The identified partnerships had approximately 2 million domestic and foreign partners. However, this figure overstates the number of partners that would be affected by the proposed regulations, because the proposed regulations would not affect foreign partners of the affected U.S. partnerships. Of affected U.S. partnerships, business entities are a minority of the affected domestic partners. Because data to identify the size of domestic partners that are business entities are not readily available, this number is a high upper bound and is magnitudes greater than the

⁷ Data are from IRS's Research, Applied Analytics, and Statistics division based on data available in the Compliance Data Warehouse. Category 4 filer includes a U.S. person who had control of a foreign corporation during the annual accounting period of the foreign corporation. Category 5 includes a U.S. shareholder who owns stock in a foreign corporation that is a CFC and who owned that stock on the last day in the tax year of the foreign corporation in that year in which it was a CFC. For full definitions, see <https://www.irs.gov/pub/irs-pdf/i5471.pdf>.

number of affected domestic partners that are small businesses. Consequently, the Treasury Department and the IRS have determined that the proposed regulations will not have a significant economic impact on a substantial number of small entities. Accordingly, it is hereby certified that the proposed regulations would not have a significant economic impact on a substantial number of small entities.

Pursuant to section 7805(f) of the Code, this notice of proposed rulemaking has been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small businesses.

IV. Unfunded Mandates Reform Act

Section 202 of the Unfunded Mandates Reform Act of 1995 requires that agencies assess anticipated costs and benefits and take certain other actions before issuing a final rule that includes any Federal mandate that may result in expenditures in any one year by a state, local, or tribal government, in the aggregate, or by the private sector, of \$100 million in 1995 dollars, updated annually for inflation. In 2019, that threshold is approximately \$154 million. These proposed regulations do not include any Federal mandate that may result in expenditures by state, local, or tribal governments, or by the private sector in excess of that threshold.

V. Executive Order 13132: Federalism

Executive Order 13132 (entitled “Federalism”) prohibits an agency from publishing any rule that has federalism implications if the rule either imposes substantial, direct compliance costs on state and local governments, and is not required by statute, or preempts state law, unless the agency meets the consultation and funding requirements of section 6 of the Executive Order. These proposed regulations do not

have federalism implications and do not impose substantial direct compliance costs on state and local governments or preempt state law within the meaning of the Executive Order.

Comments and Requests for Public Hearing

Before the proposed regulations are adopted as final regulations, consideration will be given to any comments that are submitted timely to the IRS as prescribed in this preamble under the “ADDRESSES” heading. The Treasury Department and the IRS request comments on all aspects of the proposed regulations and on changes to forms related to the proposed regulations. See also parts I.B and II.A of the Explanation of Provisions section (requesting specific comments related to the aggregate approach to domestic partnerships and GILTI high tax exclusion, respectively).

All comments will be available at www.regulations.gov or upon request. A public hearing will be scheduled if requested in writing by any person that timely submits written comments. If a public hearing is scheduled, then notice of the date, time, and place for the public hearing will be published in the **Federal Register**.

Drafting Information

The principal authors of these regulations are Joshua P. Roffenbender and Jorge M. Oben of the Office of Associate Chief Counsel (International). However, other personnel from the Treasury Department and the IRS participated in their development.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

Proposed Amendments to the Regulations

Accordingly, 26 CFR part 1 is proposed to be amended as follows:

PART 1--INCOME TAXES

Paragraph 1. The authority citation for part 1 continues to read in part as follows:

Authority: 26 U.S.C. 7805.

Par. 2. Section 1.951-1 is amended by adding paragraph (a)(4) and revising the last sentence of paragraph (i) to read as follows:

§1.951-1 Amounts included in gross income of United States shareholders.

* * * * *

(a) * * *

(4) See §1.958-1(d)(1) for ownership of stock of a foreign corporation through a domestic partnership for purposes of sections 951 and 951A and for purposes of any other provision that applies by reference to section 951 or 951A.

* * * * *

(i) * * * Paragraph (h) of this section applies to taxable years of domestic partnerships ending on or after May 14, 2010, but does not apply to determine the stock of a controlled foreign corporation owned (within the meaning of section 958(a)) by a United States person for taxable years of the controlled foreign corporation beginning on or after the date of publication of the Treasury decision adopting these rules as final regulations in the Federal Register, and for taxable years of United States persons in which or with which such taxable years of the controlled foreign corporation end.

Par. 3. Section 1.951A-0 is amended by adding entries for §1.951A-7(a), §1.951A-7(b), and §1.951A-7(c) to read as follows:

§1.951A-0 Outline of section 951A regulations.

* * * * *

§1.951A-7 Applicability dates.

- (a) In general.
- (b) High tax exclusion.
- (c) Domestic partnerships.

Par. 4. Section 1.951A-2 is amended by revising paragraph (c)(1)(iii) and adding paragraph (c)(6) to read as follows:

§1.951A-2 Tested income and tested loss.

* * * * *

(c) * * *

(1) * * *

(iii) Gross income excluded from the foreign base company income (as defined in section 954) or the insurance income (as defined in section 953) of the corporation by reason of the exception described in section 954(b)(4) pursuant to an election under §1.954-1(d), or a tentative gross tested income item of the corporation that qualifies for the exception described in section 954(b)(4) pursuant to an election under paragraph (c)(6) of this section,

* * * * *

(6) Election for application of high tax exception of section 954(b)(4)--(i) In general. For purposes of section 951A(c)(2)(A)(i)(II) and paragraph (c)(1)(iii) of this section, a tentative gross tested income item of a controlled foreign corporation for a CFC inclusion year qualifies for the exception described in section 954(b)(4) if--

(A) An election made under paragraph (c)(6)(v)(A) of this section is effective with respect to the controlled foreign corporation for the CFC inclusion year; and

(B) The tentative net tested income item with respect to the tentative gross tested income item was subject to foreign income taxes at an effective rate that is greater than 90 percent of the rate that would apply if the income were subject to the maximum rate of tax specified in section 11.

(ii) Definitions--(A) Tentative gross tested income item--(1) In general. A single tentative gross tested income item with respect to a controlled foreign corporation for a CFC inclusion year is the aggregate of all items of gross income attributable to a single qualified business unit (QBU) of the controlled foreign corporation in such CFC inclusion year that would be gross tested income without regard to this paragraph (c)(6) and that would be in a single tested income group (as defined in §1.960-1(d)(2)(ii)(C)). For this purpose, a QBU is defined in section 989(a) and the regulations under that section, and a controlled foreign corporation's QBUs includes QBUs owned by the controlled foreign corporation in addition to the QBU that is the controlled foreign corporation. Therefore, a controlled foreign corporation may have multiple tentative gross tested income items.

(2) Income attributable to a QBU. Gross income is attributable to a QBU if the gross income is properly reflected on the books and records of the QBU. Such gross income must be determined under Federal income tax principles, except that the principles of §1.904-4(f)(2)(vi) (without regard to the exclusion described in §1.904-4(f)(2)(vi)(C)(1)) apply to adjust gross income of a QBU to reflect disregarded payments.

(B) Tentative net tested income item. A tentative net tested income item with respect to a tentative gross tested income item is determined by allocating and apportioning deductions (not including any items described in §1.951A-2(c)(5)) to the tentative gross tested income item under the principles of §1.960-1(d)(3) by treating

each single tentative gross tested income item as gross income in a separate tested income group.

(iii) Effective rate at which taxes are imposed. For a CFC inclusion year of a controlled foreign corporation, the effective rate with respect to the controlled foreign corporation's tentative net tested income items is determined separately for each such item. The effective rate at which taxes are imposed on a tentative net tested income item is--

(A) The U.S. dollar amount of foreign income taxes paid or accrued with respect to the tentative net tested income item, determined by applying paragraph (c)(6)(iv) of this section; divided by

(B) The U.S. dollar amount of the tentative net tested income item, increased by the amount of foreign income taxes referred to in paragraph (c)(6)(iv) of this section.

(iv) Taxes paid or accrued with respect to a tentative net tested income item. For a CFC inclusion year, the amount of foreign income taxes paid or accrued by a controlled foreign corporation with respect to a tentative net tested income item of the controlled foreign corporation for purposes of this paragraph (c)(6) is the U.S. dollar amount of the controlled foreign corporation's current year taxes (as defined in §1.960-1(b)(4)) that would be allocated and apportioned under the principles of §1.960-1(d)(3)(ii) to the tentative net tested income item by treating such tentative net tested income item as being in a separate tested income group. If the principles of §1.904-4(f)(2)(vi) apply to adjust the gross income of a QBU to account for disregarded payments as provided in paragraph (c)(6)(ii)(A)(2) of this section, the principles of §1.904-6(a)(2) apply to allocate and apportion foreign income taxes imposed by reason

of the disregarded payments. Except to the extent provided in the next sentence, the amount of foreign income taxes paid or accrued with respect to a tentative net tested income item, determined in the manner provided in this paragraph (c)(6), will not be affected by a subsequent reduction in foreign income taxes attributable to a distribution to shareholders of all or part of such income. To the extent the foreign income taxes paid or accrued by the controlled foreign corporation are reasonably certain to be returned by the foreign jurisdiction imposing such taxes to a shareholder, directly or indirectly, through any means (including, but not limited to, a refund, credit, payment, discharge of an obligation, or any other method) on a subsequent distribution to such shareholder, the foreign income taxes are not treated as paid or accrued for purposes of this paragraph (c)(6)(iv).

(v) Rules regarding the election--(A) Manner of making election. An election is made under this paragraph (c)(6)(v)(A) with respect to a controlled foreign corporation for a CFC inclusion year--

(1) By the controlling domestic shareholders (as defined in §1.964-1(c)(5)), by attaching a statement to such effect with an original or amended income tax return for the U.S. shareholder inclusion year of each controlling domestic shareholder in which or with which such CFC inclusion year ends, and including any additional information required by applicable administrative pronouncements; or

(2) In accordance with the rules provided in forms or instructions.

(B) Scope of election. An election made under paragraph (c)(6)(v)(A) of this section that is effective with respect to a controlled foreign corporation for a CFC inclusion year applies with respect to each tentative gross tested income item of the

controlled foreign corporation for the CFC inclusion year and is binding on all United States shareholders of the controlled foreign corporation.

(C) Duration of election. An election made under paragraph (c)(6)(v)(A) of this section is effective for a CFC inclusion year of a controlled foreign corporation for which the election is made and all subsequent CFC inclusion years of such corporation unless revoked by the controlling domestic shareholders of the controlled foreign corporation under paragraph (c)(6)(v)(D)(1) of this section.

(D) Revocation of election--(1) In general. Except as provided in paragraph (c)(6)(v)(D)(2) of this section, the election made under paragraph (c)(6)(v)(A) of this section with respect to a controlled foreign corporation for a CFC inclusion year is revoked by the controlling domestic shareholders of the controlled foreign corporation in the same manner as prescribed for an election in paragraph (c)(6)(v)(A) of this section.

(2) Limitations by reason of revocation--(i) In general. Except as provided in paragraph (c)(6)(v)(D)(2)(ii) of this section, if an election with respect to a controlled foreign corporation for a CFC inclusion year is revoked under paragraph (c)(6)(v)(D)(1) of this section, a new election cannot be made under paragraph (c)(6)(v)(A) of this section with respect to the controlled foreign corporation for any CFC inclusion year that begins within sixty months following the close of the CFC inclusion year for which the previous election was revoked, and such subsequent election cannot be revoked under paragraph (c)(6)(v)(D)(1) of this section with respect to the controlled foreign corporation for any CFC inclusion year that begins within sixty months following the close of the CFC inclusion year for which the subsequent election was made.

(ii) Exception for change of control. The Commissioner may permit a controlled foreign corporation to make an election under paragraph (c)(6)(v)(A) of this section or revoke an election under paragraph (c)(6)(v)(D)(1) of this section with respect to any CFC inclusion year within the sixty-month period described in paragraph (c)(6)(v)(D)(2)(i) of this section if more than 50 percent of the total combined voting power of all classes of the stock of the controlled foreign corporation entitled to vote as of the beginning of such CFC inclusion year are owned (within the meaning of section 958(a)) by persons that did not own any interests in the controlled foreign corporation as of the close of the CFC inclusion year for which the prior election or revocation with respect to the controlled foreign corporation became effective. For purposes of the preceding sentence, a person includes any person bearing a relationship described in section 267(b) or 707(b)(1) with respect to the person.

(E) Rules applicable to controlling domestic shareholder groups--(1) In general. In the case of a controlled foreign corporation that is a member of a controlling domestic shareholder group, an election is made under paragraph (c)(6)(v)(A) of this section or revoked under paragraph (c)(6)(v)(D)(1) of this section with respect to each member of the controlling domestic shareholder group (including any member that joins the controlling domestic shareholder group after the election or revocation) and the rules in paragraphs (c)(6)(v)(A) through (D) of this section apply by reference to the controlling domestic shareholder group.

(2) Definition of controlling domestic shareholder group. For purposes of paragraph (c)(6)(v)(E)(1) of this section, the term controlling domestic shareholder group means two or more controlled foreign corporations (each a member) if more than

50 percent of the total combined voting power of all classes of the stock of each corporation is owned (within the meaning of section 958(a)) by the same controlling domestic shareholder or, if no single controlling domestic shareholder owns (within the meaning of section 958(a)) more than 50 percent of the total combined voting power of all classes of the stock of each corporation, more than 50 percent of the total combined voting power of all classes of the stock of each corporation is owned (within the meaning of section 958(a)) by the same controlling domestic shareholders and each controlling domestic shareholder owns (within the meaning of section 958(a)) the same percentage of stock in each controlled foreign corporation. For purposes of the preceding sentence, a controlling domestic shareholder includes any person bearing a relationship described in section 267(b) or 707(b)(1) to the controlling domestic shareholder.

(vi) Example. The following example illustrates the application of this paragraph (c)(6).

(A) Example: Effect of disregarded payments between QBUs--(1) Facts--(i) FP, a controlled foreign corporation organized in Country A, conducts a trade or business in Country A (the Country A Business) and reflects items of income, gain, loss, and expense attributable to the Country A Business on the books and records of FP's home office. Under §1.989(a)-1(b)(2)(i)(A), FP is a QBU. FP's functional currency is the U.S. dollar. FP has a calendar year taxable year in both the United States and Country A. An election is made under paragraph (c)(6)(v)(A) of this section that is effective for FP's CFC inclusion year.

(ii) FP owns FDE, a Country B disregarded entity (within the meaning of §1.904-4(f)(3)(i)). FDE conducts activities in Country B that constitute a trade or business within the meaning of §1.989(a)-1(c) (the Country B Business), and reflects items of income, gain, loss, and expense attributable to the Country B Business on the books and records of FDE. Under §1.989(a)-1(b)(2)(ii)(B), the Country B Business conducted through FDE is a QBU. The Country B Business's functional currency is the U.S. dollar. FDE has a calendar year taxable year in Country B.

(iii) On Date A in Year 1, FDE accrues \$100x of interest income from X, an unrelated third party, and reflects the accrual on the books and records of the Country B

business. FP excludes the \$100x from foreign personal holding company income by reason of section 954(h). Subsequently, on Date B in Year 1, FDE accrues and pays \$20x of interest to FP. FP reflects the interest income item on the books and records of the Country A Business. FDE reflects the \$20x of interest expense on the books and records of the Country B Business.

(iv) Country A imposes no tax on income. Country B imposes a 25% tax on income. For Country B income tax purposes, FDE (which is not disregarded under Country B income tax principles) recognizes \$80x of taxable income (\$100x interest income, less a \$20x deduction for the interest paid to FP). Accordingly, FDE incurs a Country B income tax liability with respect to Year 1, the U.S. dollar amount of which is \$20x. For Federal income tax purposes, if FDE were not a disregarded entity (within the meaning of §1.904-4(f)(3)(i)), FP would recognize \$20x of income in Year 1, and FDE would recognize \$80x of taxable income in Year 1. Other than the \$20x expense accrued with respect to the income tax imposed by Country B, FP incurs no deductions in Year 1 for Federal income tax purposes.

(2) Analysis--(i) Under paragraph (c)(6)(ii)(A)(1) of this section, a separate tentative gross tested income item must be determined with respect to FP's Country A Business and Country B Business (each of which is a QBU). To determine the separate tentative gross tested income items with respect to its Country A Business and Country B Business, FP must determine the gross income that is attributable to the Country A Business and the Country B Business under paragraph (c)(6)(ii)(A)(2) of this section. Without regard to the \$20x interest payment from FDE to FP, gross income attributable to the Country A Business would be \$0 (that is, \$20x of interest income reflected on the books and records of the Country A Business, reduced by \$20x attributable to a payment that is disregarded for Federal income tax purposes). Similarly, without regard to the \$20x interest payment from FDE to FP, gross income attributable to the Country B Business would be \$100x (that is, \$100x of interest income reflected on the books and records of the Country B Business, unreduced by the \$20x payment from FDE to FP). However, the \$20x payment from FDE to FP is a disregarded payment within the meaning of §1.904-4(f)(3)(ii), and would, under the principles of §1.904-4(f)(2)(vi) (without regard to the exclusion described in §1.904-4(f)(2)(vi)(C)(1)), adjust the gross income of the Country A Business from \$0 to \$20x and the gross income of the Country B Business from \$100x to \$80x (in each case, by virtue of the \$20x disregarded interest payment from FDE to FP). Accordingly, FP's tentative gross tested income attributable to the Country A Business is \$20x and its tentative gross tested income attributable to the Country B Business is \$80x.

(ii) Under paragraph (c)(6)(ii)(B) of this section, because there are no deductions allocated or apportioned under §1.960-1(d)(3) to the tentative gross tested income items of the Country A Business, FP's tentative net tested income item attributable to the Country A Business is \$20x. Taking into account the \$20x deduction for Country B income taxes that are allocable to the Country B Business under §1.960-1(d)(3), FP's tentative net tested income item attributable to the Country B Business is \$60x under paragraph (c)(6)(ii)(B) of this section (tentative gross tested income of \$80x less the \$20x deduction).

(iii) Under paragraphs (c)(6)(iii) and (iv) of this section, for Year 1 (a CFC inclusion year of FP), the effective rate with respect to FP's \$60x tentative net tested income item attributable to its Country B Business is 25%: \$20x (the U.S. dollar amount of the Country B taxes accrued with respect to FP's tentative tested net income item attributable to the Country B Business) divided by \$80x (the U.S. dollar amount of FP's \$60x tentative net tested income item, increased by the \$20x amount of Country B income taxes accrued with respect to that tentative net tested income item), expressed as a percentage. Therefore, FP's tentative net tested income item attributable to the Country B Business was subject to foreign income taxes at an effective rate (25%) that is greater than 18.9% (which is 90% of the rate that would apply if the income were subject to the maximum rate of tax specified in section 11, which is 21%). Accordingly, the requirement of paragraph (c)(6)(i)(B) of this section is satisfied with respect to FP's tentative gross tested income item attributable to the Country B Business in Year 1. Further, the requirement of paragraph (c)(6)(i)(A) of this section is satisfied because an election described in paragraph (c)(6)(v)(A) of this section was made with respect to FP for Year 1. Accordingly, FP's \$80x item of tentative gross tested income attributable to its Country B Business qualifies for the high tax exception of section 954(b)(4) under paragraph (c)(6)(i) of this section.

(iv) FP's \$20x item of tentative net tested income attributable to its Country A Business is not subject to foreign income tax, and therefore does not satisfy the requirement of paragraph (c)(6)(i)(B) of this section. Accordingly, FP's \$20x item of tentative gross tested income attributable to the Country A Business does not qualify for the high tax exception of section 954(b)(4) under paragraph (c)(6)(i) of this section.

Par. 5. Section 1.951A-7 is revised to read as follows:

§1.951A-7 Applicability dates.

(a) In general. Except as otherwise provided in this section, sections 1.951A-1 through 1.951A-6 apply to taxable years of foreign corporations beginning after December 31, 2017, and to taxable years of United States shareholders in which or with which such taxable years of foreign corporations end.

(b) High tax exclusion. Section 1.951A-2(c)(1)(iii) and (c)(6) applies to taxable years of foreign corporations beginning on or after the date of publication of the Treasury decision adopting these rules as final regulations in the **Federal Register**, and to taxable years of United States shareholders in which or with which such taxable years of foreign corporations end.

(c) Domestic partnerships. Section 1.951A-1(e) applies to taxable years of foreign corporations beginning after December 31, 2017, and before the date of publication of the Treasury decision adopting these rules as final regulations in the **Federal Register**, and to taxable years of United States persons in which or with which such taxable years of foreign corporations end.

Par. 6. Section 1.954-1 is amended by:

1. Adding “or” to the end of paragraph (c)(1)(iii)(A)(2)(ii).
2. Removing and reserving paragraphs (c)(1)(iii)(A)(2)(iii) and (iv).
3. Adding paragraphs (c)(1)(iii)(A)(3) and (c)(1)(iv).
4. Removing the language “foreign base company oil related income, as defined in section 954(g), or” in the second sentence of paragraph (d)(1) introductory text.
5. Adding a new sentence after the fourth sentence in paragraph (d)(1) introductory text.
6. Removing the language “imposed by a foreign country or countries” in paragraph (d)(1)(ii).
7. Removing the language “in a chain of corporations through which a distribution is made” in the first sentence in paragraph (d)(2) introductory text.
8. Removing the language “(or deemed paid or accrued)” in paragraph (d)(2)(i).
9. Revising the heading and the first sentence of paragraph (d)(3)(i).
10. Removing the second sentence of paragraph (d)(3)(i).
11. Removing and reserving paragraphs (d)(4)(iii) and (d)(7).

The additions and revisions read as follows:

§1.954-1 Foreign base company income.

* * * * *

(c) * * *

(1) * * *

(iii) * * *

(A) * * *

(3) Amount of a single item. For purposes of paragraph (c)(1)(iii)(A) of this section, the aggregate amount from all transactions that falls within a single separate category (as defined in §1.904-5(a)(4)(v)) and is described in paragraph (c)(1)(iii)(A)(1)(i) of this section is a single item of income. Similarly, the aggregate amount from all transactions that falls within a single separate category (as defined in §1.904-5(a)(4)(v)) and is described in each one of paragraphs (c)(1)(iii)(A)(1)(ii) through (c)(1)(iii)(A)(1)(v) of this section is in each case a separate single item of income. The same principles apply for transactions described in each one of paragraphs (c)(1)(iii)(A)(2)(i) through (v) of this section.

* * * * *

(iv) Treatment of deductions or loss attributable to disqualified basis. For purposes of paragraph (c)(1)(i) of this section (and in the case of insurance income, paragraph (a)(6) of this section), in determining the amount of a net item of foreign base company income or insurance income, deductions or loss described in §1.951A-2(c)(5) are not allocated and apportioned to gross foreign base company income or gross insurance income.

(d) * * *

(1) * * * For rules concerning the application of the high tax exception of sections 954(b)(4) and 951A(c)(2)(A)(i)(III) to tentative gross tested income items, see §1.951A-2(c)(1)(iii) and (c)(6). * * *

* * * * *

(3) * * *

(i) In general. The amount of foreign income taxes paid or accrued by a controlled foreign corporation with respect to a net item of income for purposes of section 954(b)(4) and this paragraph (d) is the U.S. dollar amount of the controlled foreign corporation's current year taxes (as defined in §1.960-1(b)(4)) that are allocated and apportioned under §1.960-1(d)(3)(ii) to the subpart F income group (as defined in §1.960-1(d)(2)(ii)(B)) that corresponds with the net item of income. * * *

* * * * *

Par. 7. Section 1.954-1, as proposed to be amended at 83 FR 63200 (December 7, 2018), is further amended by:

1. Removing and reserving paragraph (d)(3)(ii).
2. Redesignating paragraphs (h)(1) and (h)(2) as paragraphs (h)(2) and (h)(3), respectively.
3. Adding a new paragraph (h)(1).
4. Removing the language "Paragraphs (d)(3)(i) and (ii)" in newly redesignated paragraph (h)(2) and adding "The last two sentences in paragraph (d)(3)(i)" in its place.

The addition reads as follows:

§1.954-1 Foreign base company income.

* * * * *

(h) * * *

(1) Paragraphs (c)(1)(iii)(A)(3) and (c)(1)(iv) of this section and portion of paragraph (d)(3)(i) of this section. Paragraphs (c)(1)(iii)(A)(3) and (c)(1)(iv) of this section and the first sentence of paragraph (d)(3)(i) of this section apply to taxable years of a controlled foreign corporation beginning on or after the date of publication of the Treasury decision adopting these rules as final regulations in the **Federal Register**.

* * * * *

Par. 8. Section 1.956-1, as amended May 23, 2019, at 84 FR 23717, effective July 22, 2019, is further amended by revising the first sentence of paragraph (g)(4) to read as follows:

§1.956-1 Shareholder's pro rata share of the average of the amounts of United States property held by a controlled foreign corporation.

* * * * *

(g) * * *

(4) Paragraphs (a)(2) and (3) of this section apply to taxable years of controlled foreign corporations beginning on or after July 22, 2019, and to taxable years of a United States shareholder in which or with which such taxable years of the controlled foreign corporations end, but the last sentence of paragraph (a)(2)(i) and paragraphs (a)(2)(iii) and (a)(3)(iv) of this section do not apply to taxable years of controlled foreign corporations beginning on or after the date of publication of the Treasury decision adopting these rules as final regulations in the **Federal Register**, and to taxable years of a United States shareholder in which or with which such taxable years of the controlled foreign corporations end. * * *

* * * * *

Par. 9. Section 1.958-1 is amended by:

1. Redesignating paragraph (d) as paragraph (e).
2. Adding a new paragraph (d).

The addition reads as follows:

§1.958-1 Direct and indirect ownership of stock.

* * * * *

(d) Stock owned through domestic partnerships--(1) In general. Except as otherwise provided in paragraph (d)(2) of this section, for purposes of section 951 and section 951A, and for purposes of any other provision that applies by reference to section 951 or section 951A, a domestic partnership is not treated as owning stock of a foreign corporation within the meaning of section 958(a). When the preceding sentence applies, a domestic partnership is treated in the same manner as a foreign partnership under section 958(a)(2) and paragraph (b) of this section for purposes of determining the persons that own stock of the foreign corporation within the meaning of section 958(a).

(2) Non-application for determination of status as United States shareholder or controlled foreign corporation. Paragraph (d)(1) of this section does not apply for purposes of determining whether any United States person is a United States shareholder (as defined in section 951(b)), whether any United States shareholder is a controlling domestic shareholder (as defined in §1.964-1(c)(5)), or whether any foreign corporation is a controlled foreign corporation (as defined in section 957(a)).

(3) Examples. The following examples illustrate the application of this paragraph (d).

(i) Example 1--(A) Facts. USP, a domestic corporation, and Individual A, a United States citizen unrelated to USP, own 95% and 5%, respectively, of PRS, a domestic partnership. PRS owns 100% of the single class of stock of FC, a foreign corporation.

(B) Analysis--(1) CFC and United States shareholder determinations. Under paragraph (d)(2) of this section, the determination of whether PRS, USP, and Individual A (each a United States person) are United States shareholders of FC and whether FC is a controlled foreign corporation is made without regard to paragraph (d)(1) of this section. PRS, a United States person, owns 100% of the total combined voting power or value of the FC stock within the meaning of section 958(a). Accordingly, PRS is a United States shareholder under section 951(b), and FC is a controlled foreign corporation under section 957(a). USP is a United States shareholder of FC because it owns 95% of the total combined voting power or value of the FC stock under sections 958(b) and 318(a)(2)(A). Individual A, however, is not a United States shareholder of FC because Individual A owns only 5% of the total combined voting power or value of the FC stock under sections 958(b) and 318(a)(2)(A).

(2) Application of sections 951 and 951A. Under paragraph (d)(1) of this section, for purposes of sections 951 and 951A, PRS is not treated as owning (within the meaning of section 958(a)) the FC stock; instead, PRS is treated in the same manner as a foreign partnership for purposes of determining the FC stock owned by USP and Individual A under section 958(a)(2) and paragraph (b) of this section. Therefore, for purposes of sections 951 and 951A, USP is treated as owning 95% of the FC stock under section 958(a), and Individual A is treated as owning 5% of the FC stock under section 958(a). USP is a United States shareholder of FC, and therefore USP determines its income inclusions under section 951 and 951A based on its ownership of FC stock under section 958(a). However, because Individual A is not a United States shareholder of FC, Individual A does not have an income inclusion under section 951 with respect to FC or a pro rata share of any amount of FC for purposes of section 951A.

(ii) Example 2--(A) Facts. USP, a domestic corporation, and Individual A, a United States citizen, own 90% and 10%, respectively, of PRS1, a domestic partnership. PRS1 and Individual B, a nonresident alien individual, own 90% and 10%, respectively, of PRS2, a domestic partnership. PRS2 owns 100% of the single class of stock of FC, a foreign corporation. USP, Individual A, and Individual B are unrelated to each other.

(B) Analysis--(1) CFC and United States shareholder determination. Under paragraph (d)(2) of this section, the determination of whether PRS1, PRS2, USP, and Individual A (each a United States person) are United States shareholders of FC and whether FC is a controlled foreign corporation is made without regard to paragraph (d)(1) of this section. PRS2 owns 100% of the total combined voting power or value of the FC stock within the meaning of section 958(a). Accordingly, PRS2 is a United States shareholder under section 951(b), and FC is a controlled foreign corporation under section 957(a). Under sections 958(b) and 318(a)(2)(A), PRS1 is treated as

owning 90% of the FC stock owned by PRS2. Accordingly, PRS1 is a United States shareholder under section 951(b). Further, under section 958(b)(2), PRS1 is treated as owning 100% of the FC stock for purposes of determining the FC stock treated as owned by USP and Individual A under section 318(a)(2)(A). Therefore, USP is treated as owning 90% of the FC stock under section 958(b) (100% x 100% x 90%), and Individual A is treated as owning 10% of the FC stock under section 958(b) (100% x 100% x 10%). Accordingly, both USP and Individual A are United States shareholders of FC under section 951(b).

(2) Application of sections 951 and 951A. Under paragraph (d)(1) of this section, for purposes of sections 951 and 951A, PRS1 and PRS2 are not treated as owning (within the meaning of section 958(a)) the FC stock; instead, PRS1 and PRS2 are treated in the same manner as foreign partnerships for purposes of determining the FC stock owned by USP and Individual A under section 958(a)(2) and paragraph (b) of this section. Therefore, for purposes of determining the amount included in gross income under sections 951 and 951A, USP is treated as owning 81% (100% x 90% x 90%) of the FC stock under section 958(a), and Individual A is treated as owning 9% (100% x 90% x 10%) of the FC stock under section 958(a). Because USP and Individual A are both United States shareholders of FC, USP and Individual A determine their respective inclusions under sections 951 and 951A based on their ownership of FC stock under section 958(a).

(4) Applicability date. Paragraphs (d)(1) through (3) of this section apply to taxable years of foreign corporations beginning on or after the date of publication of the Treasury decision adopting these rules as final regulations in the **Federal Register**, and to taxable years of United States persons in which or with which such taxable years of foreign corporations end. For taxable years that precede the taxable years described in the preceding sentence, a domestic partnership may apply those paragraphs to taxable years of a foreign corporation beginning after December 31, 2017, and to taxable years of the domestic partnership in which or with which such taxable years of the foreign corporation end, provided that the partnership, its partners that are United States shareholders of the foreign corporation, and other domestic partnerships that bear relationships described in section 267(b) or 707(b) to the partnership (and their United States shareholder partners) consistently apply paragraph (d) of this section with respect to all foreign corporations whose stock the domestic partnerships own within the

meaning of section 958(a) (determined without regard to paragraph (d)(1) of this section).

* * * * *

Par. 10. Section 1.1502-51 is amended by revising the last sentence in paragraph (b) and adding paragraph (g)(2) to read as follows:

§1.1502-51 Consolidated section 951A.

* * * * *

(b) * * * In addition, see §1.958-1(d).

* * * * *

(g) * * *

(2) The last sentence of paragraph (b) of this section. The last sentence of paragraph (b) of this section applies to taxable years of United States shareholders described in §1.958-1(d)(4).

Kirsten Wielobob

Deputy Commissioner for Services and Enforcement.

[FR Doc. 2019-12436 Filed: 6/14/2019 4:15 pm; Publication Date: 6/21/2019]