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DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[REG-101952-24]

RIN 1545-BR10

Income of Foreign Governments and of International Organizations

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations relating to the taxation of the income of foreign governments from investments in the United States. In particular, these proposed regulations provide guidance for determining when an acquisition of debt by a foreign government is considered to be commercial activity, and when a foreign government has effective control of an entity engaged in commercial activities. These proposed regulations will affect foreign governments that derive income from sources within the United States.

DATES: Written or electronic comments and requests for a public hearing must be received by **[INSERT DATE 60 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER]**.

ADDRESSES: Commenters are strongly encouraged to submit public comments electronically via the Federal eRulemaking Portal at *https://*www.*regulations.gov* (indicate IRS and REG-101952-24) by following the online instructions for submitting comments. Requests for a public hearing must be submitted as prescribed in the "Comments and Requests for a Public Hearing" section. Once submitted to the Federal eRulemaking Portal, comments cannot be edited or withdrawn. The Department of the Treasury (Treasury Department) and the IRS will publish for public availability any

comments submitted to the IRS's public docket. Send paper submissions to: CC:PA:01:PR (REG-101952-24), Room 5503, Internal Revenue Service, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044.

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, Jack Zhou at (202) 317-6938; concerning submissions of comments, requests for a public hearing, and access to a public hearing, Publication and Regulations Section at (202) 317-6901 (not toll-free numbers) or by email to *publichearings@irs.gov* (preferred).

SUPPLEMENTARY INFORMATION:

Authority

This document contains proposed amendments to the Income Tax Regulations (26 CFR part 1) under section 892 of the Internal Revenue Code (Code). These regulations are issued under the express delegations of authority under sections 892(c) and 7805(a) of the Code.

Background

I. *Overview*

This document contains proposed amendments to the Income Tax Regulations (26 CFR part 1) under section 892 of the Code relating to income of foreign governments (proposed regulations). Any terms used but not defined in this preamble have the meanings given to them in the proposed regulations.

Section 892(a)(1) provides that income of foreign governments received from investments in the United States in stocks, bonds, or other domestic securities owned by the foreign governments, or financial instruments held in the execution of governmental financial or monetary policy, or interest on deposits in banks in the United States of moneys belonging to the foreign governments, is not included in gross income and is exempt from taxation under subtitle A of the Code. Section 892(a)(2)(A) provides

that section 892(a)(1) does not apply to any income that is (1) derived from the conduct of any commercial activity (whether within or outside the United States), (2) received by a controlled commercial entity (CCE) or received (directly or indirectly) from a CCE, or (3) derived from the disposition of any interest in a CCE.

Section 892(a)(2)(B) provides that, for purposes of section 892(a)(2)(A), a CCE means any entity engaged in commercial activities (whether within or outside the United States) if the foreign government holds (directly or indirectly) any interest in the entity which (by value or voting interest) is 50 percent or more of the total of the interests in the entity, or holds (directly or indirectly) any other interest in the entity which provides the foreign government with effective control of the entity. Section 892(c) authorizes the Secretary to prescribe such regulations as may be necessary or appropriate to carry out the purposes of section 892.

II. *Regulations Addressing the Application of Section 892*

On June 27, 1988, the Treasury Department and the IRS published in the **Federal Register** a notice of proposed rulemaking (53 FR 24100) (1988 proposed regulations) with a cross-reference to temporary regulations under section 892 (TD 8211, 53 FR 24060) (1988 temporary regulations) to provide guidance under section 892.

On August 1, 2002, the Treasury Department and the IRS published § 1.892-5(a)(3) in the **Federal Register** (TD 9012, 67 FR 49864) to provide that the term “entity” for purposes of section 892(a)(2)(B) (defining “controlled commercial entity”) includes partnerships (2002 final regulations).

On November 3, 2011, the Treasury Department and the IRS published in the **Federal Register** a notice of proposed rulemaking (76 FR 68119) that would provide additional guidance for determining when a foreign government is engaged in commercial activities (2011 proposed regulations). On December 29, 2022, the

Treasury Department and the IRS published in the **Federal Register** a notice of proposed rulemaking (87 FR 80097) that would make changes to § 1.892-5T(b)(1) to provide exceptions to the general rule that a United States real property holding corporation (USRPHC), as defined in section 897(c)(2), which may include a foreign corporation, is treated as engaged in commercial activity and, therefore, is a CCE if the requirements of § 1.892-5T(a)(1) or (2) are satisfied (2022 proposed regulations).

The rules in the 2011 proposed regulations and the 2022 proposed regulations are finalized, with modifications, in the Final Rules section of this issue of the **Federal Register** (2025 final regulations). The 2025 final regulations also finalized proposed § 1.892-3(a)(4) (definition of financial instrument) of the 1988 proposed regulations.

Explanation of Provisions

I. *Definition of Controlled Entity*

Section 892 does not define the term "foreign government." The 1988 temporary regulations define a foreign government to consist only of integral parts and controlled entities of a foreign sovereign. Section 1.892-2T(a)(3) defines "controlled entity" to mean an entity that is separate in form from a foreign sovereign or otherwise constitutes a separate juridical entity if it satisfies certain requirements, including that it is wholly owned and controlled by a single foreign sovereign directly or indirectly through one or more controlled entities. The flush language of § 1.892-2T(a)(3) states "[a] controlled entity does not include partnerships or any other entity owned and controlled by more than one foreign sovereign."

The Treasury Department and the IRS are aware that the flush language of § 1.892-2T(a)(3) may be interpreted by taxpayers as referring only to partnerships owned by more than one foreign sovereign. The Treasury Department and the IRS are of the view, however, the better reading of this flush language is that partnerships, including ones wholly owned and controlled by a single foreign sovereign (including

indirectly through controlled entities), are not included in the term "controlled entity" for purposes of § 1.892-2T(a)(3). The concept of a controlled entity was developed to address the question of whether an entity separate from a foreign sovereign and otherwise subject to Federal income tax could be exempt from such tax under section 892.[1] Since an entity treated as a partnership for Federal tax purposes generally is not subject to such tax, without regard to the exemption under section 892, the question addressed by the concept of a controlled entity does not arise in the case of a partnership.[2] Therefore, the proposed regulations would clarify that a partnership for Federal tax purposes is not a controlled entity within the meaning of § 1.892-2T(a)(3). The proposed regulations would remove the flush language following § 1.892-2T(a)(3) and replace it with proposed § 1.892-2(a)(4), which would provide that a controlled entity, within the meaning of § 1.892-2T(a)(3), does not include any partnership for Federal tax purposes. The proposed regulations also would revise the concluding sentence of the flush language following § 1.892-2T(a)(3) to clarify that the rule is not confined to "foreign financial organizations" and to make other drafting changes.

II. *Acquisition of Debt*

A. *In general*

Proposed § 1.892-4(e)(1)(i) of the 2011 proposed regulations would provide in

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[1] *See* Rev. Rul. 75-298, 1975-2 C.B. 290 (providing criteria to determine whether an organization will be considered part of a foreign government for purposes of qualifying for exemption from Federal income tax pursuant to section 892), obsoleted by Rev. Rul. 2003-99, 2003-2 C.B. 388, and revoking Rev. Rul. 66-73, 1966-1 C.B. 174 (examining whether an organization constitutes a corporation for purposes of section 892).

[2] *See* section 701, which was enacted in 1954 and states that "[a] partnership as such shall not be subject to the income tax imposed by this chapter." Section 701 refers to "this chapter" (chapter 1) while section 892(a)(1) states that certain income of foreign governments is exempt "under this subtitle." However, the taxes for which section 892 provides an exemption (section 892(a)(1)) are described in chapter 1 of the subtitle.

part, under the heading titled “investments,” that subject to the provisions of proposed § 1.892-4(e)(1)(ii) and (iii) (rules on trading activities and investments made by a banking, financing, or similar business), loans and investments in stocks, bonds, and other securities are not commercial activities. Proposed § 1.892-4(e)(1)(iii) would provide that investments (including loans) made by a banking, financing, or similar business constitute commercial activities, even if the income derived from those investments is not considered to be income effectively connected to the active conduct of a banking, financing, or similar business in the United States by reason of the application of § 1.864-4(c)(5). A comment to the 2011 proposed regulations stated that there is uncertainty as to the circumstances in which loan origination is commercial activity. The Treasury Department and the IRS acknowledged the comment when finalizing proposed § 1.892-4(e)(1)(i) and (ii) in the 2025 final regulations and stated that the issue will be addressed by these proposed regulations.

The Treasury Department and the IRS are of the view that whether the activity of lending or otherwise acquiring debt, including at original issuance, qualifies as investment rather than commercial activity under section 892 is highly fact-dependent, so that a consideration of all facts and circumstances is needed to determine the appropriate characterization. Accordingly, the Treasury Department and the IRS are proposing these regulations to provide a framework for determining when acquiring any debt, including at original issuance, qualifies as investment for purposes of section 892.

The proposed regulations would provide as a general rule that all acquisition of debt is treated as commercial activity unless the acquisition is characterized as investment for purposes of section 892 under either of two safe harbors or under a facts-and-circumstances test. *See* proposed § 1.892-4(c)(1)(ii)(A). The term “debt” means an obligation treated as debt for Federal tax purposes, regardless of its legal form. Accordingly, proposed § 1.892-4(c)(1)(ii) would also apply to a financial

instrument, within the meaning of § 1.892-3(a)(4), that is treated as debt. An acquisition of debt undertaken as a dealer, as defined in § 1.864-2(c)(2)(iv)*(a)*, would be treated in any event as commercial activity.

The proposed regulations' framework would constitute the exclusive set of rules for determining whether acquiring debt, including at original issuance, is treated as investment and thus not as commercial activity for purposes of section 892. Whether debt acquisition is investment for purposes of section 892 would be, unless otherwise provided, determined without regard to whether the debt acquisition is treated as a trade or business for Federal tax purposes. Thus, no inference is intended from the proposed regulations as to the circumstances in which acquiring debt, including at original issuance, would or would not be a trade or business for other purposes of the Code, including section 864, section 162, or section 166 of the Code.

B. *Debt acquisition safe harbors*

Proposed § 1.892-4(c)(1)(ii)(B) would provide two safe harbors that treat debt acquired in a registered offering or in a qualified secondary market acquisition as investment for purposes of § 1.892-4(c)(1)(i) and, thus, not subject to the general rule of proposed § 1.892-4(c)(1)(ii)(A).

The first safe harbor would treat acquisitions of bonds or other debt securities acquired in an offering registered under the Securities Act of 1933, as amended (Securities Act), as investment provided that the underwriters of the offering are not related to the acquirer within the meaning of sections 267(b) and 707(b). Although the first safe harbor would except only offerings of debt securities registered under the Securities Act, the Treasury Department and the IRS recognize that the securities laws of some foreign countries may provide a regulatory framework for debt offerings sufficiently similar to the Securities Act such that this exception may appropriately apply in those circumstances. Comments are requested regarding the circumstances, if any,

in which the safe harbor should be extended to offerings registered under foreign securities laws in addition to the Securities Act.

The second safe harbor would treat a qualified secondary market acquisition of debt as investment for purposes of § 1.892-4(c)(1)(i). This generally would include acquisitions of debt traded on an established securities market provided that the acquirer is not purchasing from the issuer or participating in negotiation of the terms or issuance of the debt. A qualified secondary market acquisition must not be from a person that is under common management or control with the acquirer, unless that person acquired the debt as investment within the meaning of § 1.892-4(c)(1)(i). Comments are requested on this safe harbor, including the circumstances, if any, in which it should apply to an acquisition of debt that is not traded on an established securities market.

C. *Qualification as investment based on all facts and circumstances*

Proposed § 1.892-4(c)(1)(ii)(C) would provide that debt acquisitions that do not satisfy the safe harbors of proposed § 1.892-4(c)(1)(ii)(B) may be an investment based on consideration of all relevant facts and circumstances. In general, facts and circumstances would be relevant to the extent they indicate that the entity's expected return from acquiring the debt is exclusively a return on its capital rather than including a return on activities it conducts. The proposed regulations provide a non-exclusive list of relevant factors, in proposed § 1.892-4(c)(1)(ii)(C)*(1)* through *(8)*, that would apply in determining whether a debt acquisition is investment for purposes of § 1.892-4(c)(1)(i). Under this proposed analysis, all factors would be taken into account and, depending on the particular case, the weight given to each relevant factor (including factors not listed in the proposed regulations) may vary.

Comments are requested on whether proposed § 1.892-4(c)(1)(ii)(C) should include additional factors or examples of transactions undertaken by foreign

government investors. In particular, comments are requested on the circumstances, if any, in which acquisitions of distressed debt, broadly syndicated loans, revolving credit facilities, and delayed-draw debt obligations should be treated as investment rather than commercial activities for purposes of section 892.

D. *Other changes*

The proposed regulations would retain the exception for investments in "other securities" (which follows the reference to stocks and bonds) and retain the definition of "other securities" as "any note or other evidence of indebtedness" which includes loans. *See* proposed §§ 1.892-4(c)(1)(i) and 1.892-3T(a)(3). Accordingly, the proposed regulations would remove "loans" from the list of investments in § 1.892-4(c)(1)(i) of the 2025 final regulations that are not treated as commercial activities.

Additionally, the proposed regulations would withdraw the rule on banking, financing, or similar businesses in § 1.892-4T(c)(1)(iii). This is a conforming change given that the proposed regulations' framework would constitute the exclusive set of rules for determining whether acquiring debt, including at original issuance, is treated as investment and thus not as commercial activity for purposes of section 892.

The proposed regulations also would remove the phrase "or from an investment in net leases on real property" from the parentheses that follow "the holding of real property which is not producing income" in § 1.892-4(c)(1)(i). The clause that would be removed is duplicative of "the holding of net leases on real property," which is another activity identified in § 1.892-4(c)(1)(i) that is not a commercial activity. Thus, no substantive change to § 1.892-4(c)(1)(i) is intended by this removal. An additional non-substantive change is made in proposed § 1.892-4(c)(1)(i) that would add "the transfer of securities under a loan agreement which meets the requirements of section 1058" to the list of activities that are not commercial activities, rather than setting off that activity in its own sentence.

III. *Defining Effective Control*

Section 892(a)(2)(B) defines a CCE as any entity engaged in commercial activities (whether within or outside the United States) if the government (i) holds (directly or indirectly) any interest in such entity which (by value or voting interest) is 50 percent or more of the total of such interests in such entity, or (ii) holds (directly or indirectly) any other interest in the entity which provides the foreign government with effective control of the entity.

The 1988 temporary regulations provide that an entity that is engaged in commercial activities is a CCE if the foreign government has "effective practical control" of the entity. *See* § 1.892-5T(a)(2). The 1988 temporary regulations explain that effective practical control may be achieved through a minority interest which is sufficiently large to achieve effective control, or through creditor, contractual, or regulatory relationships which, together with ownership interests held by the foreign government, achieve effective control. For example, an entity engaged in commercial activities may be treated as a CCE if a foreign government, in addition to holding a minority interest (by value or voting power), is also a substantial creditor of the entity or controls a strategic natural resource which the entity uses in the conduct of its trade or business, providing the foreign government effective practical control over the entity. *See* § 1.892-5T(c)(2). Thus, under the 1988 temporary regulations, the term "other interest" in section 892(a)(2)(B)(ii) includes business relationships, and an interest in the entity for purposes of an analysis of effective control may exist when the foreign government has the ability to exert influence over the entity. A comment to the 2011 proposed regulations suggested that the regulations should be expanded to provide a more thorough definition of effective practical control with more specific examples. The Treasury Department and the IRS acknowledged the comment in the 2025 final regulations and stated that the issue will be addressed by these proposed regulations.

The proposed regulations would revise § 1.892-5T(c)(2) to provide further guidance on what constitutes effective control under section 892(a)(2)(B)(ii). The Treasury Department and the IRS are of the view that it is necessary and appropriate to define the terms "other interest" and "effective control" broadly to include circumstances in which a foreign government would have control over either the operational, managerial, board-level, or investor-level decisions of an entity. The proposed regulations would provide that, generally, effective control is achieved by any interest in the entity that, either separately or in combination, results in control over the operational, managerial, board-level, or investor-level decisions of the entity. All of the facts and circumstances related to the interests would be considered in determining effective control. Interests may include equity interests, voting power in the entity, debt interests, contractual rights in or arrangements with the entity or with holders of equity or other interests in the entity, certain business relationships with the entity or with other interest holders in the entity, regulatory authority over the entity, or any other arrangement or relationship that provides influence over the entity's operational, managerial, board-level, or investor-level decisions. (Although the 1988 temporary regulations provide guidance under section 892(a)(2)(B) using the term "effective practical control," the proposed regulations use the term "effective control" to be consistent with section 892(a)(2)(B)(ii) and the 2025 final regulations.)

For example, a foreign government would have effective control of an entity in a case in which it owns a minority equity interest in the entity that entitles that foreign government to appoint only one out of several directors of the entity, if that one director has the sole power to unilaterally appoint or dismiss the entity's manager. *See* proposed § 1.892-5(c)(2)(iii)(E) (*Example 4*). In contrast, a foreign government that holds only a minority interest by value and voting power in an entity, and no other interest, would not have effective control of the entity if the foreign government lacks the power (directly or

indirectly through other arrangements) to unilaterally elect the entity's board, choose its management, or otherwise direct the entity's operational, managerial, board-level, or investor-level decisions. *See* proposed § 1.892-5(c)(2)(iii)(B) (*Example 1*).

A foreign government would be deemed to have effective control of an entity if the foreign government is, or under § 1.892-5(a)(1) controls an entity that is, a managing partner or managing member of such entity, or holds or controls an entity that holds an equivalent role with respect to such entity under local law applicable to the entity. The Treasury Department and the IRS are of the view that these roles inherently carry control over an entity so that the facts-and-circumstances test is unnecessary to determine whether a foreign government has effective control of the entity. On the other hand, the mere right to be consulted with respect to operational, managerial, board-level, or investor-level decisions of an entity will not alone give rise to effective control.

Additionally, a foreign government would not need to hold any particular amount of (or any) equity in an entity to have effective control of the entity. For example, if a foreign government is a creditor of an entity with sufficient creditor rights to give it effective control, then that entity would be a CCE of the foreign government, and any interest payments (or other payments) made by the debtor entity to the foreign government would not qualify for the exemption under section 892. *See* proposed § 1.892-5(c)(2)(iii)(I) (*Example 8*) (finding effective control when creditor's rights generally included veto rights over the debtor's capital transactions and operating budget).

With respect to related foreign government entities, the proposed regulations would provide that the principles of § 1.892-5T(c)(1)(i) (attributing an interest owned directly or indirectly by an integral part or controlled entity to the foreign sovereign) apply for purposes of an effective control analysis. For example, if two controlled entities (within the meaning of § 1.892-2T(a)(3)) of the same foreign sovereign have direct or

indirect equity or non-equity interests in a corporation, all of those interests would be considered together for purposes of the effective control analysis with respect to either controlled entity. Comments are requested as to the circumstances, if any, in which a determination could be made that controlled entities (within the meaning of § 1.892-2T(a)(3)) are functionally independent of one another and therefore may be appropriately considered separately for purposes of an effective control analysis.

Comments are also requested as to the circumstances, if any, in which the holder of a minority equity interest in an entity should not be treated as having effective control (or as having at least 50 percent of voting power) of the entity if managerial or board-level decisions of the entity are subject to veto or "blocking" rights of the holder and other holders (for example, through consent rights, supermajority requirements, or otherwise).

Applicability Dates

These regulations are proposed to apply to taxable years 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). A foreign government within the meaning of §§ 1.892-2 and 1.892-2T may choose to apply § 1.892-2(a)(4), once finalized, to a taxable year of its directly or indirectly wholly-owned entities beginning before the finalization date if the period of limitations on assessment of the taxable year is open under section 6501, and provided that the foreign government consistently applies the rule in its entirety to the taxable year and all succeeding taxable years of its directly or indirectly wholly-owned entities beginning before the finalization date.

Special Analyses

I. *Regulatory Planning and Review – Economic Analysis*

These proposed regulations are not subject to review under section 6(b) of Executive Order 12866 pursuant to the Memorandum of Agreement (July 4, 2025)

between the Treasury Department and the Office of Management and Budget (OMB) regarding review of tax regulations.

II. *Paperwork Reduction Act*

The Paperwork Reduction Act of 1995 (44 U.S.C. 3501–3520) generally requires that a Federal agency obtain the approval of the OMB before collecting information from the public, whether such collection of information is mandatory, voluntary, or required to obtain or retain a benefit. There are no additional information collection requirements associated with these proposed regulations.

III. *Regulatory Flexibility Act*

Pursuant to the Regulatory Flexibility Act (5 U.S.C. chapter 6), it is hereby certified that this rulemaking 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. This certification is based on the fact that the proposed regulations affect foreign governments, including their controlled entities, with income from sources within the United States. Accordingly, the entities affected by the proposed regulations are not considered small entities, and a regulatory flexibility analysis under the Regulatory Flexibility Act is not required.

IV. *Section 7805(f)*

Pursuant to section 7805(f) of the Code, these proposed regulations will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact on small business.

V. *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. The 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.

VI. *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. The 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. Any comments submitted will be made available at *https://www.regulations.gov* or upon request.

A public hearing will be scheduled if requested in writing by any person who timely submits electronic or written comments. Requests for a public hearing are also encouraged to be made electronically. If a public hearing is scheduled, notice of the date and time for the public hearing will be published in the **Federal Register**.

Drafting Information

The principal authors of the proposed regulations are Jack Zhou of the Office of Associate Chief Counsel (International), and Joel Deuth, formerly of the Office of

Associate Chief Counsel (International). However, other personnel from the Treasury Department and the IRS participated in their development.

Statement of Availability of IRS Documents

IRS guidance cited in this preamble is published in the Internal Revenue Bulletin and is available from the Superintendent of Documents, U.S. Government Publishing Office, Washington, DC 20402, or by visiting the IRS website at *https://www.irs.gov*.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

Proposed Amendments to the Regulations

Accordingly, the Treasury Department and the IRS propose to amend 26 CFR part 1 as follows:

PART 1—INCOME TAXES

Paragraph 1. The authority citation for part 1 is amended by adding an entry for § 1.892-2 in numerical order to read in part as follows:

Authority: 26 U.S.C. 7805 * * *

* * * * *

Section 1.892-2 also issued under 26 U.S.C. 892(c).

* * * * *

Par. 2. Section 1.892-2 is added to read as follows:

§ 1.892-2 Foreign government defined.

(a) *Foreign government*—(1) *Definition*. For further guidance, *see* § 1.892-2T(a)(1).

(2) *Integral part*. For further guidance, *see* § 1.892-2T(a)(2).

(3) *Controlled entity.* For further guidance, *see* § 1.892-2T(a)(3).

(4) *Exceptions.* A controlled entity, within the meaning of paragraph (a)(3) of this section, does not include any partnership for Federal tax purposes. A controlled entity also does not include any entity owned and controlled by more than one foreign

sovereign. Thus, a foreign entity organized and wholly owned and controlled by multiple foreign sovereigns to invest jointly, or to foster economic, financial, and/or technical cooperation, is not a controlled entity for purposes of paragraph (a)(3) of this section.

(b) *Inurement to the benefit of private persons*. For further guidance, *see* § 1.892-2T(b).

(1) through (2) [Reserved]

(c) *Pension trusts*—(1) *In general*. For further guidance, *see* § 1.892-2T(c)(1) introductory text through (c)(1)(iv).

(i) through (v) [Reserved]

(2) *Illustrations*. For further guidance, *see* § 1.892-2T(c)(2).

(d) *Political subdivision and transnational entity*. For further guidance, *see* § 1.892-2T(d).

(e) A*pplicability date*. Paragraph (a)(4) of this section applies to taxable years beginning on or after [DATE OF PUBLICATION OF FINAL RULE]. However, a foreign government within the meaning of §§ 1.892-2 and 1.892-2T may choose to apply paragraph (a)(4) of this section to a taxable year of its directly or indirectly wholly-owned entities beginning before [DATE OF PUBLICATION OF FINAL RULE] if the period of limitations on assessment of the taxable year is open under section 6501, and provided that the foreign government consistently applies the rule in its entirety to the taxable year and all succeeding taxable years of its directly or indirectly wholly-owned entities beginning before [DATE OF PUBLICATION OF FINAL RULE].

Par. 3. Section 1.892-2T is amended by:

a. Removing the undesignated text under paragraph (a)(3)(iv); and

b. Adding paragraph (a)(4).

The addition reads as follows:

§ 1.892-2T Foreign government defined (temporary regulations).

(a) * * *

(4) *Exceptions*. For further guidance, *see* § 1.892-2(a)(4).

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Par. 4. Section 1.892-4, as amended in a final rule published elsewhere in this issue of the **Federal Register**, effective **[INSERT DATE OF PUBLICATION IN THE FEDERAL REGISTER]**, is amended by:

a. Revising paragraphs (c)(1)(i) through (iii); and

b. Adding a sentence after the first sentence of paragraph (d).

The revisions and addition read as follows:

§ 1.892-4 Commercial activities.

* * * * *

(c) * * *

(1) * * *

(i) *In general*. Subject to the provisions of this paragraph (c)(1)(i) and paragraphs (c)(1)(ii) through (c)(7) of this section, the following are not commercial activities: investments in stocks, bonds, and other securities (as defined in § 1.892-3T(a)(3)); investments in financial instruments (as defined in § 1.892-3(a)(4)); the holding of partnership equity interests; the holding of net leases on real property; the holding of real property which is not producing income (other than on its sale); the holding of deposits in any currency in banks; and the transfer of securities under a loan agreement which meets the requirements of section 1058. An activity will not cease to be an investment solely because of the volume of transactions of that activity or because of other unrelated activities.

(ii) *Acquisition of debt*—(A) *In general*. An acquisition of debt is considered a commercial activity for purposes of paragraph (b) of this section notwithstanding any other provision of this section, unless the acquisition qualifies as investment under the rules of paragraph (c)(1)(ii)(B) or (C) of this section. For purposes of this paragraph

(c)(1)(ii), the term *debt* means an obligation treated as debt for Federal tax purposes. For purposes of applying paragraphs (c)(1)(ii)(B) and (C) of this section, actions by an agent or a person otherwise acting on behalf of the acquirer are treated as the actions of the acquirer. An acquisition of debt undertaken as a dealer, as defined in § 1.864-2(c)(2)(iv)*(a)*, constitutes commercial activity without regard to paragraphs (c)(1)(ii)(B) and (C) of this section.

(B) *Safe harbors*. An acquisition of debt that satisfies paragraph (c)(1)(ii)(B)(*1*) or (*2*) of this section is treated as investment and not commercial activity for purposes of paragraph (c)(1)(i) of this section.

(*1*) *Registered offerings*. An acquisition of bonds or other debt securities in an offering registered under the Securities Act of 1933, as amended (15 U.S.C. 77a, *et seq*.), (*the Securities Act)*, provided that the underwriters of the offering are not related to the acquirer within the meaning of sections 267(b) and 707(b).

(*2*) *Qualified secondary market acquisitions*. An acquisition of debt traded on an established securities market, within the meaning of § 1.7704-1(b), provided that—

(*i*) The acquirer does not acquire the debt from the debt issuer or participate in the negotiation of the terms or issuance of the debt; and

(*ii*) The acquisition is not from a person that is under common management or control with the acquirer, unless that person acquired the debt as investment within the meaning of paragraph (c)(1)(i) of this section.

(C) *Investments in debt*. An acquisition of debt that does not satisfy either paragraph (c)(1)(ii)(B)(*1*) or (*2*) of this section may be an investment for purposes of paragraph (c)(1)(i) of this section based on all relevant facts and circumstances, including the following:

(*1*) Whether the acquirer solicited prospective borrowers, or otherwise held itself out as willing to make loans or otherwise acquire debt at or in connection with its

original issuance;

(*2*) Whether the acquirer materially participated in negotiating or structuring the terms of the debt;

(*3*) Whether the acquirer is entitled to compensation (whether or not labelled as a fee) that is not treated as interest (including original issue discount) for Federal tax purposes;

(*4*) The form of the debt and the issuance process, including, for example, whether the debt is a bank loan or instead a privately placed debt security pursuant to Regulation S or Rule 144A under the Securities Act;

(*5*) The percentage of the debt issuance acquired by the acquirer relative to the percentages acquired by other purchasers;

(*6*) The percentage of equity in the debt issuer held or to be held by the acquirer;

(*7*) The value of that equity relative to the amount of the debt acquired; and

(*8*) If debt is deemed to be acquired in a debt-for-debt exchange as a result of a significant modification under § 1.1001-3, whether there was, at the time of acquisition of the original unmodified debt, a reasonable expectation, based on objective evidence, such as a decline in the financial condition or credit rating of the debt issuer between original issuance and the time of the acquisition of the original unmodified debt, that the original unmodified debt would default.

(D) *Examples*—(*1*) *Assumed facts.* The rules of this paragraph (c)(1)(ii) are illustrated by the examples in this paragraph (c)(1)(ii)(D). Except as otherwise stated, the following facts are assumed for purposes of paragraphs (c)(1)(ii)(D)(*2*) through (*6*) of this section (*Examples 1* through *5*):

(*i*) FC is a foreign entity organized under the laws of country X and is treated as a corporation for Federal tax purposes; FC is a controlled entity of the government of country X under § 1.892-2T(a)(3);

(*ii*) FC has neither engaged in, nor has been attributed, any conduct of commercial activities for purposes of section 892;

(*iii*) FC has not previously acquired any debt; and

(*iv*) FC is not a dealer as defined in § 1.864-2(c)(2)(iv)*(a)*.

(*2*) *Example 1*: *Isolated debt financing as commercial activity*—(*i*) *Facts*. In year 1, representatives of FC offered, on behalf of FC, to provide debt financing to a foreign corporation. FC's representatives structured and negotiated the terms of that debt financing, and FC made a loan to the foreign corporation pursuant to those terms in year 1. FC does not own any equity in that corporation. The debt was not issued in a registered offering. All of the activities occurred outside the United States in year 1.

(*ii*) *Analysis*. FC's debt acquisition activity is commercial activity under this paragraph (c)(1)(ii), unless the acquisition qualifies as investment under paragraph (c)(1)(ii)(B) or (C) of this section. The debt acquisition does not qualify as investment under either of the safe harbors in paragraph (c)(1)(ii)(B) of this section because the debt was not issued in an offering registered under the Securities Act, and because FC materially participated in negotiating the terms of the debt through its representatives and acquired the debt at original issuance from the issuer. This debt acquisition also does not qualify as investment under paragraph (c)(1)(ii)(C) of this section because, through its representatives, FC held itself out as a lender and solicited, structured, negotiated, and funded the debt at original issuance, and because FC acquired the debt in the form of a loan and did not own any equity in the debt issuer. Although FC made only one loan in year 1, the number of loans does not change the determination that the acquisition is commercial activity under this paragraph (c)(1)(ii), regardless of whether FC is treated as engaged in a trade or business for purposes of section 162, section 166, or section 864(b).

(*3*) *Example 2: Debt financing as investment when combined with certain equity*

investments—(*i*) *Facts.* In year 1, FC owned 80 percent of a foreign corporation's equity interests, which had a total value of $100 million. During year 1, FC lent $50 million to the foreign corporation to finance the foreign corporation's activities. FC's management structured the terms of the debt in the form of a loan between FC and the foreign corporation. FC acquired the debt at original issuance without a registered offering. All of the activities occurred outside the United States in year 1.

(*ii*) *Analysis*. FC's debt acquisition activity is a commercial activity under this paragraph (c)(1)(ii), unless the acquisition qualifies as investment under paragraph (c)(1)(ii)(B) or (C) of this section. The debt acquisition does not qualify as investment under either of the safe harbors in paragraph (c)(1)(ii)(B) of this section because the debt was not issued in an offering registered under the Securities Act and because FC acquired the debt at original issuance from the issuer. Nonetheless, taking into account all relevant facts and circumstances, including those under paragraph (c)(1)(ii)(C) of this section, FC's acquisition of the foreign corporation's debt is investment for purposes of paragraph (c)(1)(i) of this section. FC did not hold itself out as a lender or solicit borrowers. Even though FC structured the terms of the debt and acquired the debt in the form of a loan, FC owned a substantial percentage of the equity interests in the debt issuer and acquired an amount of debt that is not significant relative to the value of FC's equity investment in the debt issuer. Accordingly, taking into account all relevant facts and circumstances, FC's debt acquisition qualifies as investment for purposes of paragraph (c)(1)(i) of this section, and therefore is not commercial activity under this paragraph (c)(1)(ii).

(*4*) *Example 3: Private placement of debt securities and U.S. Treasury securities as investment*—(*i*) *Facts.* In year 1, representatives of FC met with financial institutions unrelated to FC that were serving as placement agents for the debt of a number of domestic corporations. At those meetings, FC's representatives communicated FC's

interest in purchasing privately placed debt of U.S. corporate issuers and communicated the terms on which FC would be willing to purchase that debt. Based on those discussions, in the same year, FC purchased, at original issuance, ten privately placed debt securities of several domestic corporations. Each of the debt securities was offered by the placement agents under Regulation S through a private placement memorandum. FC purchased less than one-third by principal amount of each debt offering and at least one other unrelated purchaser purchased a larger percentage of each debt offering than FC. In addition, in the same year, FC purchased U.S. Treasury debt securities at original issuance in a public auction.

(*ii*) *Analysis*. FC's debt acquisition activities are commercial activities under this paragraph (c)(1)(ii), unless the acquisitions qualify as investments under paragraph (c)(1)(ii)(B) or (C) of this section. Because FC acquired the debt at original issuance from the issuers and not in offerings registered under the Securities Act, the acquisitions do not qualify for either of the safe harbors under paragraph (c)(1)(ii)(B) of this section. Nonetheless, taking into account all relevant facts and circumstances, including those under paragraph (c)(1)(ii)(C) of this section, FC's acquisitions of privately placed debt securities and of U.S. Treasury debt securities are investments for purposes of paragraph (c)(1)(i) of this section. The corporate debt was structured on behalf of the issuers by financial institutions unrelated to FC that were serving as placement agents. The U.S. Treasury debt securities were offered with terms and conditions set by the Treasury Department. FC did not hold itself out as a lender, solicit borrowers, or materially participate in structuring or negotiating the terms of the debt. Although FC did communicate to the placement agents for the corporate debt before issuance the terms on which FC would be willing to acquire the debt and bid in the auction of U.S. Treasury debt securities, these activities do not indicate material participation in the structuring or negotiation of the terms of the debt. Moreover, the corporate debt was offered to FC in

the form of a privately placed security, and FC was not the largest purchaser of any debt offering based on principal amount. Accordingly, taking into account all relevant facts and circumstances, FC's debt acquisitions qualify as investments for purposes of paragraph (c)(1)(i) of this section, and therefore are not commercial activities under this paragraph (c)(1)(ii).

(*5*) *Example 4: Debt modification as investment*—(*i*) *Facts.* In year 1, FC purchased debt of a foreign issuer, *X*, in secondary market acquisitions that qualify as investments under paragraph (c)(1)(ii)(B)(*2*) of this section (the *X Debt*). At the time of FC's acquisitions, the X Debt was not in default, and there were no objective indications at the time of the purchase of the X Debt, such as a declining trend in X's financial condition or credit rating, that X would default on the X Debt. In year 4, due to unexpected changes in market conditions, X defaulted on the X Debt. A committee of creditors of X, acting on behalf of all holders of the X Debt, negotiated with X to modify the terms of the X Debt, including extensions of maturity, deferral of interest payments, and changes in interest rates. FC did not participate in the creditors' committee, thus was not involved in any negotiations between the committee and X, and did not directly negotiate with X on any aspect of the X Debt. The modifications to the X Debt were significant modifications within the meaning of § 1.1001-3, and FC was deemed to acquire a new debt from X (the *Modified X Debt*) in exchange for the unmodified X Debt.

(*ii*) *Analysis*. FC's debt acquisition activity is commercial activity under this paragraph (c)(1)(ii), unless the acquisition qualifies as investment under paragraph (c)(1)(ii)(B) or (C) of this section. FC's deemed acquisition of the Modified X Debt does not qualify for either of the safe harbors under paragraph (c)(1)(ii)(B) of this section because FC is deemed to have acquired the Modified X Debt at original issuance from the issuer and not in an offering registered under the Securities Act. However, taking into account all relevant facts and circumstances, including those under paragraph

(c)(1)(ii)(C) of this section, FC's acquisition of the Modified X Debt qualifies as investment for purposes of paragraph (c)(1)(i) of this section because the X Debt was not in default at the time of FC's acquisition, at that time there was no expectation, based on objective indications, that X would default on the X Debt, and because FC did not participate in the creditors' committee which negotiated the terms of the Modified X Debt. Accordingly, FC's deemed acquisition of the Modified X Debt qualifies as investment for purposes of paragraph (c)(1)(i) of this section, and therefore is not treated as commercial activity under this paragraph (c)(1)(ii).

(*6*) *Example 5: Debt restructuring as commercial activity*—(*i*) *Facts*. The facts are the same as in paragraph (c)(1)(ii)(D)(*5*) of this section (*Example 4*), except that FC was a member of the creditors' committee of X, which materially participated in negotiating and structuring the terms of the Modified X Debt.

(ii) Analysis. In contrast to the acquisition in paragraph (c)(1)(ii)(D)(*5*) of this section (*Example 4*), FC's acquisition of the Modified X Debt is commercial activity under this paragraph (c)(1)(ii). Taking into account all relevant facts and circumstances, the acquisition does not qualify as investment under paragraph (c)(1)(i) of this section because FC was a member of the creditors' committee and, as a result, presumed to have materially participated in negotiating and structuring the terms of the Modified X Debt.

(iii) [Reserved]

* * * * *

(d) *Applicability date.* * * * Paragraph (c)(1) of this section applies to taxable years beginning on or after [DATE OF PUBLICATION OF FINAL RULE]. * * *

Par. 5. Section 1.892-4T is amended by revising paragraph (c)(1)(iii) to read as follows:

§ 1.892-4T Commercial activities (temporary regulations).

* * * * *

(c) * * *

(1) * * *

(iii) [Reserved]

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Par. 6. Section 1.892-5, as amended in a final rule published elsewhere in this issue of the **Federal Register**, effective **[INSERT DATE OF PUBLICATION IN THE FEDERAL REGISTER]**, is amended by:

a. Revising paragraph (c)(2); and

b. Adding a sentence after the second sentence of paragraph (e).

The revision and addition read as follows:

§ 1.892-5 Controlled commercial entity.

* * * * *

(c) * * *

(2) *Effective control*—(i) *Rule*. An entity engaged in commercial activity is a controlled commercial entity under paragraph (a)(1)(ii) of this section if a foreign government (within the meaning of § 1.892-2T(a)) has *effective control* of the entity. Except as provided in paragraph (c)(2)(ii) of this section, effective control is achieved by any interest in the entity that, directly or indirectly, either separately or in combination with other interests, results in control of the operational, managerial, board-level, or investor-level decisions of the entity. However, mere consultation rights with respect to operational, managerial, board-level, or investor-level decisions of an entity (such as extending the term of the entity's investment period, change in control of the entity, or liquidation of the entity) do not alone give rise to effective control. The determination of effective control is made considering all of the facts and circumstances related to the interests in an entity. Interests in an entity may include, for example:

(A) Equity interests;

(B) Debt interests;

(C) Voting rights in the entity, including the power to appoint directors or managers, and to veto decisions;

(D) Contractual rights in or arrangements with the entity, or with other interest holders in the entity;

(E) Business relationships with the entity, or with other interest holders in the entity, including as a major customer or a supplier having control over a strategic natural resource used in the entity's business;

(F) Regulatory authority over the entity; or

(G) Any other interest in or other relationship with the entity that may provide influence over decisions relating to the entity's operations, management, board-level, or investor-level matters.

(ii) *Special rule*. A foreign government is deemed to have effective control of an entity if the foreign government is, or under paragraph (a)(1) of this section controls an entity that is, a managing partner or managing member of such entity, or holds or controls an entity that holds an equivalent role with respect to such entity under local law applicable to the entity.

(iii) *Examples*—(A) *Assumed facts.* The application of this paragraph (c)(2) is illustrated by the examples in this paragraph (c)(2)(iii). Except as otherwise stated, the following facts are assumed for purposes of paragraphs (c)(2)(iii)(B) through (I) of this section (*Examples 1* through *8*):

(*1*) FX is a foreign entity organized under the laws of country C and is treated as a corporation for Federal tax purposes; FX is a controlled entity of the government of country C under § 1.892-2T(a)(3);

(*2*) Corp 1 is a corporation for Federal tax purposes that is engaged in commercial activities;

(*3*) Corp 1 has a single class of equity interest and, unless otherwise stated, Corp 1's governing documents or local law require that more than 50 percent of its equity holders approve the election of its directors, the selection of its officers, and certain major corporate decisions;

(*4*) FX owns less than 50 percent of the value or voting power in Corp 1 under paragraph (a)(1)(i) of this section and whether Corp 1 is a controlled commercial entity with respect to FX is determined under paragraphs (a)(1)(ii) and (c)(2)(i) of this section based on all of the facts and circumstances; and

(*5*) The remaining equity interests of Corp 1 are owned by several other investors unrelated to FX, none of which has control of Corp 1 within the meaning of paragraph (a)(1)(i) of this section.

(B) *Example 1*—(*1*) *Facts*. FX owns 40 percent of the equity in Corp 1. Two other investors each own 30 percent of the equity in Corp 1. FX is not a party to any arrangement with other equity holders or holders of other interests in Corp 1 that would give FX the right to elect a majority of Corp 1's directors or to appoint or replace officers of Corp 1. Under Corp 1's governing documents and local law, FX does not have the power to unilaterally authorize or veto a corporate action or appoint a majority of Corp 1's directors or officers, and FX does not hold any other interest in Corp 1, including by reason of any business relationship that provides it with influence over Corp 1.

(*2*) *Analysis*. Because FX holds only a minority equity interest in Corp 1, is not a party to any arrangement with other equity or other interest holders of Corp 1, does not have sufficient voting power to unilaterally authorize or veto Corp 1's actions or to appoint a majority of Corp 1's directors or officers, and does not otherwise hold any other interest in Corp 1, FX is not treated as having effective control of Corp 1. Accordingly, Corp 1 is not a controlled commercial entity with respect to FX.

(C) *Example 2*—(*1*) *Facts*. The facts are the same as in paragraph (c)(2)(iii)(B) of

this section (*Example 1*), except that FX and Corp 1 have an investment agreement in place when FX invests in Corp 1. The investment agreement provides criteria for what types of investments can be made by Corp 1, and provides no voting, operational, managerial, or other rights to FX with respect to Corp 1.

(*2*) *Analysis*. The investment agreement between FX and Corp 1 does not itself, or in combination with the other facts provided in paragraph (c)(2)(iii)(B) of this section (*Example 1*), give FX control of operational, managerial, board-level, or investor-level decisions of Corp 1. Thus, for the reasons stated in paragraph (c)(2)(iii)(B) of this section (*Example 1*), FX is not treated as having effective control of Corp 1. Accordingly, Corp 1 is not a controlled commercial entity with respect to FX.

(D) *Example 3*—(*1*) *Facts*. The facts are the same as in paragraph (c)(2)(iii)(B) of this section (*Example 1*), except that under Corp 1's governing documents, FX is entitled to participate in an investment committee and has the right only to discuss acquisitions and sales of property by Corp 1, but FX has no right to decide or execute such acquisitions or sales and no other rights with respect to Corp 1.

(*2*) *Analysis*. FX's rights arising from the investment committee for Corp 1 are mere consultation rights with respect to managerial decisions of Corp 1. Such rights do not themselves, or in combination with the other facts provided in paragraph (c)(2)(iii)(B) of this section (*Example 1*), give FX control of operational, managerial, board-level, or investor-level decisions of Corp 1. Thus, for the reasons stated in paragraph (c)(2)(iii)(B) of this section (*Example 1*), FX is not treated as having effective control of Corp 1. Accordingly, Corp 1 is not a controlled commercial entity with respect to FX.

(E) *Example 4*—(*1*) *Facts*. Under Corp 1's governing documents, FX is entitled to appoint one out of three directors of Corp 1. That director alone is authorized under Corp 1's governing documents to unilaterally appoint or dismiss the manager, an officer of Corp 1 whose responsibilities are to manage Corp 1's operations. FX does not

otherwise have sufficient voting power directly or through any arrangements with holders of equity or holders of other interests in Corp 1 to unilaterally authorize or veto any other Corp 1 action.

(*2*) *Analysis*. FX has, by reason of its equity interest, power that allows it to appoint a director who alone has the power to unilaterally appoint or dismiss Corp 1's manager, which provides FX with control over decisions as to the operations and management of Corp 1. Therefore, FX has effective control of Corp 1. Accordingly, Corp 1 is a controlled commercial entity with respect to FX.

(F) *Example 5*—(*1*) *Facts*. The facts are the same as in paragraph (c)(2)(iii)(E) of this section (*Example 4*), except instead of having the right to unilaterally appoint or dismiss the manager of Corp 1, FX's appointed director alone has rights to unilaterally veto dividend distributions, material capital expenditures, sales of new equity interests in Corp 1, and the operating budget of Corp 1.

(*2*) *Analysis*. The veto rights of FX's appointed director give FX control over decisions as to the operation of Corp 1. Therefore, FX has effective control of Corp 1. Accordingly, Corp 1 is a controlled commercial entity with respect to FX.

(G) *Example 6*—(*1*) *Facts.* Under Corp 1's governing documents, FX is entitled to appoint one out of three directors of Corp 1 and the remaining two directors are appointed by the other unrelated investors. However, one unrelated investor derives significant revenues from FX through other business dealings, and, as a matter of course, causes its appointed director to always vote in the same manner as FX's appointed director on all board decisions. That unrelated investor's and FX's appointed director's votes, when combined, constitute the majority of the Corp 1 board votes. FX does not otherwise have sufficient voting power to unilaterally authorize or veto any other Corp 1 action. FX does not hold any other interest in Corp 1.

(*2*) *Analysis*. FX's significant business relationship with the unrelated investor

constitutes an interest in Corp 1 under paragraph (c)(2)(i)(E) of this section. That interest indirectly provides FX, when combined with its equity interest, with the power to control Corp 1's board. Therefore, FX has effective control of Corp 1. Accordingly, Corp 1 is a controlled commercial entity with respect to FX.

(H) *Example 7*—(*1*) *Facts*. Corp 1's business consists primarily of extracting and marketing a mineral located in country C. FC, the government of country C, owns all rights to that mineral and regulates all businesses engaged in its extraction.

(*2*) *Analysis*. FX, by reason of FC's ownership of the mineral rights and the regulatory authority over the mineral's extraction, has the ability to substantially affect Corp 1's business. For purposes of paragraph (c)(2)(i) of this section, FC's ownership of the mineral rights and its regulatory relationship with Corp 1's business constitute FX's interests in Corp 1 under paragraphs (c)(2)(i)(E) and (F) of this section. Those interests indirectly provide FX with the power to control decisions as to the operation and management of Corp 1. Therefore, FX has effective control of Corp 1. Accordingly, Corp 1 is a controlled commercial entity with respect to FX.

(I) *Example 8*—(*1*) *Facts*. FX is a creditor of Corp 1. Under the credit agreement between FX and Corp 1, Corp 1 is subject to restrictions on the type of investments that Corp 1 can make, asset dispositions, levels of future borrowing, and dividend distributions by Corp 1. The credit agreement also provides FX with veto rights over dividend and stock repurchases, additional borrowing, capital expenditures, Corp 1's annual operating budget, and redemption of subordinated debt.

(*2*) *Analysis*. FX's creditor interest, based on the totality of the rights provided to FX by the terms of the credit agreement, provides FX with control over both investor-level and operational decisions of Corp 1. Therefore, FX has effective control of Corp 1. Accordingly, Corp 1 is a controlled commercial entity with respect to FX.

* * * * *

(e) *Applicability date*. * * * Paragraph (c)(2) of this section applies to taxable years beginning on or after [DATE OF PUBLICATION OF FINAL RULE]. * * *

* * * * *

Frank J. Bisignano,

Chief Executive Officer.

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