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DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[REG-115145-25]

RIN 1545-BR76

Section 898(c) Transition Rule for Allocating Foreign Taxes and Section 960(d)(4) Foreign Tax Credit Disallowance

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations that relate to allocating foreign taxes of foreign corporations affected by the repeal of the one-month deferral election and to the disallowance of foreign tax credits on certain distributions of previously taxed earnings and profits. The proposed regulations would affect taxpayers that operate in foreign countries through certain foreign corporations and taxpayers that claim the foreign tax credit.

DATES: Written or electronic comments and requests for a public hearing must be received by **[INSERT DATE 45 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-115145-25) 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 Once submitted to the Federal eRulemaking Portal, comments cannot be edited or withdrawn.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 comment submitted to the IRS's public docket. Send paper submissions to: CC:PA:01:PR (REG-115145-25), Room 5503, Internal Revenue Service, PO Box 7604, Ben Franklin Station, Washington, D.C. 20044.

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations related to section 898(c), Hayley Rassuchine at (202) 317-6936; concerning the proposed regulations related to section 960(d)(4), Le Chen at (202) 317-6936; and concerning submissions of comments and requests for a public hearing, Publications and Regulations at (202) 317-6901 (not toll-free numbers) or by sending an email to *publichearings@irs.gov* (preferred).

SUPPLEMENTARY INFORMATION:

Authority

This document contains proposed additions and amendments to 26 CFR part 1 (proposed regulations) under sections 898(c) and 960(d)(4) and certain other provisions of the Internal Revenue Code (Code). The proposed regulations are issued pursuant to the express delegation of authority under section 70352(c) of Public Law 119-21, 139 Stat. 72 (July 4, 2025), commonly known as the One, Big, Beautiful Bill Act (OBBBA), which provides that the Secretary of the Treasury or the Secretary's delegate (Secretary) shall issue regulations providing for the allocation of foreign taxes of foreign corporations affected by the repeal of section 898(c)(2). The proposed regulations are also issued pursuant to the express delegation of authority under section 960(f), which provides the Secretary with authority to prescribe such regulations as may be necessary or appropriate to carry out the provisions of section 960. Additionally, the proposed regulations are issued pursuant to the express delegation of authority under section 7805(a).

Background

I. *Repeal of Section 898(c)(2)*

Section 898 provides rules for determining the required taxable year of any specified foreign corporation. A foreign corporation is a specified foreign corporation if it is treated as a controlled foreign corporation (CFC) for any purpose under subpart F of subchapter N of chapter 1 of subtitle A of the Code, and if any United States shareholder (as defined in section 951(b)) (U.S. shareholder) owns (determined by applying the ownership rules of section 958) more than 50 percent of the stock of the CFC by vote or value on each testing day[1] (majority U.S. shareholder).

Section 898(c)(1) generally requires a specified foreign corporation to have the same taxable year as the taxable year of its majority U.S. shareholder (the majority U.S. shareholder year). However, prior to the enactment of the OBBBA, section 898(c)(2) generally permitted a specified foreign corporation to elect a taxable year beginning one month earlier than the majority U.S. shareholder year (one-month deferral election), subject to the consent of the Secretary. Section 70352 of the OBBBA repealed the one-month deferral election for taxable years of specified foreign corporations beginning after November 30, 2025. Section 70352(c) of the OBBBA provides that if a corporation is a specified foreign corporation as of November 30, 2025, its first taxable year beginning after November 30, 2025, will end at the same time as the first required year (within the meaning of section 898(c)(1)) ending after such date (first required year). Thus, a specified foreign corporation with a one-month deferral election in place will have a one-month taxable year as its first required year.

Section 70352(c) of the OBBBA provides a transition rule for specified foreign corporations required to change their taxable years due to the repeal of the one-month deferral election (the transition rule). Under the transition rule, the change to the

[1] Section 898(c)(3)(B) (redesignated by section 70352(a) of the OBBBA as section 898(c)(2)(B)) defines the testing days as the first day of the corporation’s taxable year, or the days during a representative period that the Secretary may prescribe. No final regulations have been issued that prescribe such a representative period.

specified foreign corporation's taxable year will be treated as initiated by the corporation and as having been made with the consent of the Secretary. The transition rule also directs the Secretary to issue regulations or other guidance allocating foreign taxes paid or accrued in the specified foreign corporation's first required year and its succeeding taxable year among those taxable years in the manner the Secretary determines appropriate to carry out the purposes of section 70352 of the OBBBA.

On November 25, 2025, the Treasury Department and the IRS issued Notice 2025-72, 2025-51 I.R.B. 840, describing rules expected to be included in forthcoming proposed regulations under: (1) section 70352 of the OBBBA regarding the transition rule, and (2) section 987 regarding the election to recognize pretransition section 987 gain or loss ratably over a transition period. The proposed regulations would contain the rules described in Notice 2025-72 related to the transition rule, with certain modifications discussed in this preamble, and other guidance but would not include the rules related to pretransition section 987 gain or loss. The Treasury Department and the IRS intend to issue a separate notice of proposed rulemaking in the near future relating to section 987 that includes proposed rules relating to the recognition of pretransition section 987 gain or loss.

II. *Section 960(d)(4)*

Section 901 generally provides that a taxpayer choosing to credit foreign income taxes is allowed a credit for certain foreign income taxes paid or accrued by the taxpayer plus, in the case of a domestic corporation, the taxes deemed to have been paid by the domestic corporation under section 960. Section 960(d) provides that, if any amount is includible in the gross income of a domestic corporation under section 951A (section 951A inclusion), the domestic corporation is deemed to have paid foreign income taxes with respect to the section 951A inclusion. Prior to the OBBBA, section 960(d)(1) provided that a domestic corporation that is a U.S. shareholder is deemed to have paid foreign income taxes in an amount equal to 80 percent of the product of the U.S. shareholder’s inclusion percentage and the aggregate of the tested foreign income taxes paid or accrued by its CFCs. Thus, section 960(d)(1) (prior to the OBBBA) effectively reduced the amount of foreign income taxes deemed paid with respect to a section 951A inclusion by 20 percent.

Section 70312(a)(1) of the OBBBA increased the percentage in section 960(d)(1) from 80 percent to 90 percent, thereby decreasing the reduction in foreign income taxes deemed paid from 20 percent to 10 percent. Section 70312(b) of the OBBBA added section 960(d)(4) to the Code, which correspondingly disallows a foreign tax credit for 10 percent of the foreign income taxes paid or accrued (or deemed paid under section 960(b)(1)) with respect to a distribution of previously taxed earnings and profits (PTEP) resulting from a section 951A inclusion. Section 70312(c)(2) of the OBBBA provides that section 960(d)(4) applies to foreign income taxes paid or accrued (or deemed paid under section 960(b)(1)) with respect to any amount excluded from gross income under section 959(a) by reason of a section 951A inclusion after June 28, 2025.

On December 4, 2025, the Treasury Department and the IRS issued Notice 2025-77, 2025-52 I.R.B. 872, announcing the intent to issue proposed regulations regarding section 960(d)(4), including the application of the effective date of section 960(d)(4). Notice 2025-77 provides guidance for determining the amount of foreign income taxes paid or accrued (or deemed paid) with respect to PTEP distributions resulting from a section 951A inclusion that are subject to the foreign tax credit disallowance under section 960(d)(4). The proposed regulations contain the rules described in Notice 2025-77.

Explanation of Provisions

I. *Proposed Regulations Implementing the Section 898(c) Transition Rule*

A. *Relevant foreign tax credit framework*

In general, under section 951(a)(1),[2] a U.S. shareholder of a CFC must include in gross income its pro rata share of the CFC's subpart F income for the year. Similarly, a U.S. shareholder's section 951A inclusion is based, in part, on its pro rata share of its CFC's tested income or tested loss for the taxable year. *See* § 1.951A-1(c). In computing a CFC's items of subpart F income and its tested income or tested loss, deductions (including taxes) properly allocable to such income are taken into account. *See, e.g.*, sections 954(b)(5) and 951A(b)(2)(A)(ii). A CFC's items of subpart F income and its tested income or tested loss are computed in the functional currency of the CFC and translated into U.S. dollars as net amounts using the average exchange rate for the CFC's taxable year. *See* sections 986(b) and 989(b)(3) and § 1.951A-1(d)(1).

Generally, an income item of a CFC that would otherwise be subpart F income may be excluded, pursuant to an election, under the high-tax exception from foreign base company income (high-tax exception) if the item is subject to an effective rate of foreign tax that is greater than 90 percent of the maximum rate of tax specified in section 11. *See* § 1.954-1(d). A similar election excludes from tested income an item that would otherwise be tested income (high-tax exclusion) if the item is subject to an effective rate of foreign tax greater than 90 percent of the maximum rate of tax specified in section 11. *See* § 1.951A-2(c)(7).

Section 960(a) provides that when a domestic corporation includes in gross income any item of income under section 951(a)(1) with respect to a CFC, the domestic corporation is deemed to have paid so much of the CFC's foreign income taxes as are properly attributable to the item of income. Section 960(d)(1) provides that when a domestic corporation has a section 951A inclusion, the domestic corporation is deemed

[2] The statutory citations in part I of this Explanation of Provisions section are to the Code as in effect following the amendments made by the OBBBA. While some of these amendments may not be applicable to a specified foreign corporation's first required year (depending on when that first required year begins), the amendments generally do not affect the proposed regulations implementing the section 898(c) transition rule.

to have paid 90 percent of the product of such domestic corporation's inclusion percentage multiplied by the aggregate tested foreign income taxes paid or accrued by its CFCs. Section 960(d)(3) defines tested foreign income taxes as the foreign income taxes paid or accrued by a CFC which are properly attributable to the tested income of the CFC taken into account by the domestic corporation under section 951A. Therefore, in order for foreign income taxes paid or accrued by a CFC in a taxable year to be deemed paid by a U.S. shareholder, the related subpart F income of the CFC must be included in gross income by the U.S. shareholder under section 951(a)(1), or the related tested income of the CFC must be taken into account in the U.S. shareholder's section 951A inclusion. Section 960(b)(1) provides that a U.S. shareholder of a CFC is deemed to have paid the CFC's foreign income taxes that the U.S. shareholder has not been previously deemed to pay and that are properly attributable to a distribution from the CFC that the U.S. shareholder excludes from its gross income under section 959(a) (a section 959(a) distribution).

Section 1.861-20 provides rules for allocating and apportioning foreign income taxes to statutory and residual groupings for an operative Code section, except as modified under the rules for the operative section. *See also* § 1.861-8(f). These rules apply to attribute foreign income taxes paid or accrued by a CFC to items of income of the CFC in order to determine a CFC's net items of subpart F income and tested income, the effective rate of foreign tax for purposes of the high-tax exception and the high-tax exclusion, and the taxes attributable to the CFC's income groups and PTEP groups (as defined in § 1.960-1(b)). *See* §§ 1.960-1(d), 1.960-2(b)(2) and (c)(4), and 1.960-3(d).

The foreign income taxes taken into account by a CFC in a taxable year are determined under the CFC's method of accounting. For CFCs that use an accrual method of accounting, foreign income taxes accrue in the taxable year in which all the events have occurred that establish the fact of the liability and the amount of the liability can be determined with reasonable accuracy. *See* §§ 1.446-1(c)(1)(ii)(A) and 1.461-4(g)(6)(iii)(B). A foreign income tax determined on the basis of items of income, gain, deduction, and loss that arise in a foreign taxable year (a foreign net income tax) becomes fixed and determinable at the close of the foreign taxable year. *See* § 1.905-1(d)(1)(i). For CFCs that use the cash method of accounting, foreign income taxes are taken into account when paid. *See* §§ 1.905-1(c)(1) and 1.446-1(c)(1)(i). Foreign income taxes are generally considered paid in the taxable year in which the taxes are remitted to the foreign country.

Section 1.901-2(f) provides rules for determining the person considered to have paid or accrued a foreign income tax for foreign tax credit purposes (the section 901 taxpayer). For instance, a partnership is considered the section 901 taxpayer of a foreign income tax imposed at the entity level on the income of the partnership. *See* § 1.901-2(f)(4)(i). Additionally, the person who is treated as owning the assets of a disregarded entity (as described in § 301.7701-2(c)(2)(i)) for Federal income tax purposes is considered the section 901 taxpayer of any foreign income tax imposed at the entity level on the income of the disregarded entity. *See* § 1.901-2(f)(4)(ii). If a partnership, disregarded entity, or corporation undergoes one or more covered events during its foreign taxable year that do not close the foreign taxable year, a foreign income tax, other than a withholding tax described in section 901(k)(1)(B), imposed with respect to that continuing foreign taxable year is allocated to and among the predecessor entities or prior owners under § 1.901-2(f)(5). Section 1.901-2(f)(5)(ii) defines a covered event as a partnership termination under section 708(b)(1), a transfer of a disregarded entity, or a change in entity classification of a disregarded entity or a corporation.

For purposes of determining the amount of the foreign tax credit, foreign income taxes are translated at the rate provided under section 986(a). If the section 901 taxpayer of the foreign income tax takes foreign income taxes into account when accrued, taxes are generally translated using the average exchange rate for the taxable year to which the taxes relate. *See* section 986(a)(1)(A). Section 986(a) provides certain exceptions to the general rule, including for foreign income taxes that are not paid within two years of the close of the U.S. taxable year to which they relate. *See* section 986(a)(1)(B). Section 905(c) provides that, among other things, a change in the amount of foreign income tax accrued and claimed as a credit requires a redetermination of the U.S. tax liability for the year or years affected.

B. *Foreign taxes subject to allocation*

1. Specified Foreign Income Taxes

Section 3.03 of Notice 2025-72 provides that only specified foreign income taxes would be allocated between the first required year and the succeeding taxable year of a specified foreign corporation. Section 3.02(4) of Notice 2025-72 defines a "specified foreign income tax" as a foreign net income tax accrued by an affected corporation in its first required year for which the affected corporation is the section 901 taxpayer. Section 3.02 of Notice 2025-72 defines an affected corporation as a specified foreign corporation (as defined in section 898(b)) that takes into account foreign income taxes under an accrual method of accounting and that, pursuant to section 70352(c) of the OBBBA, is required to change its first taxable year beginning after November 30, 2025. No comments were received on these definitions, and, except as discussed in this part I.B of this Explanation of Provisions section, the proposed regulations would apply to specified foreign income taxes and would define a "specified foreign income tax" and an "affected corporation" consistently with Notice 2025-72. *See* proposed § 1.898(c)-1(b) (clarifying the definition of an affected corporation to require that the specified foreign corporation's first required year end pursuant to section 70352(c)(1) of the OBBBA on the date prescribed by that section) and § 1.898(c)-1(c) (expanding the definition of a specified foreign income tax to include specified distributive shares of creditable foreign tax expenditures if an election is made). Thus, except as discussed in this part I.B of this Explanation of Provisions section, any other foreign tax that is taken into account by a specified foreign corporation in its first required year or its succeeding taxable year would continue to be taken into account in that respective taxable year.

The proposed regulations would allocate specified foreign income taxes between an affected corporation's first required year and its succeeding taxable year to carry out the purposes of section 70352 of the OBBBA. Specified foreign income taxes would generally include foreign net income taxes, which accrue on the last day of a foreign taxable year. As a result of section 70352(c) of the OBBBA, a specified foreign corporation's foreign taxable year may close with or within the specified foreign corporation's first required year. In that case, the foreign net income tax, likely imposed with respect to a full taxable year of foreign law income, accrues in the first required year while only one month of income accrues in that year for Federal income tax purposes. Depending on the amount of the foreign net income tax imposed, this could result in the specified foreign corporation having a loss with respect to a particular income group for the first required year, resulting in foreign income taxes not being deemed paid by the affected corporation's U.S. shareholders under section 960(a) or (d). *See* part I.A of this Explanation of Provisions section.

As under Notice 2025-72, the definition of specified foreign income tax would exclude taxes that are likely to accrue close in time to the related income since any allocation of such tax between the first required year and the succeeding taxable year would create a needless separation of income and tax. For instance, a specified foreign income tax would not include a foreign withholding tax because such a tax accrues close in time to the income to which it relates. Similarly, a specified foreign corporation that uses the cash method of accounting would not be an affected corporation, and foreign net income taxes taken into account by such a specified foreign corporation would not be specified foreign income taxes. A cash-basis specified foreign corporation will generally be required to make monthly or quarterly estimated payments of its foreign income tax liability and, therefore, is unlikely to make a single payment of foreign income tax in its first required year that would result in a loss with respect to a particular income group.

2. Specified Distributive Shares of Creditable Foreign Tax Expenditures

Section 3.03(1) of Notice 2025-72 provides that an affected corporation's distributive share of foreign income taxes paid or accrued by a partnership (creditable foreign tax expenditures or CFTEs, as defined in § 1.704-1(b)(4)(viii)) are not specified foreign income taxes, and therefore, would not be allocated between the affected corporation's first required year and its succeeding taxable year. Section 6 of Notice 2025-72 requested comments on whether an affected corporation's distributive share of CFTEs should be allocated between its first required year and succeeding taxable year when an affected corporation owns an interest in a partnership that is required to change its taxable year because the affected corporation changes its taxable year pursuant to section 70352 of the OBBBA. *See* section 706(b) and § 1.706-1(b). Several comments recommended that distributive shares of CFTEs of such partnerships be allocated between the affected corporation's first required year and succeeding taxable year.

As under Notice 2025-72, the proposed regulations would generally define a specified foreign income tax to exclude an affected corporation's distributive share of CFTEs. This exclusion prevents the separation of income and foreign income tax because the affected corporation will take into account its distributive share of other partnership items based on the partnership's full taxable year at the same time it takes into account its distributive share of CFTEs. *See* section 706(a) and § 1.706-1(a). However, when a partnership is required to change its taxable year because an affected corporation owning an interest in the partnership changes its taxable year pursuant to section 70352 of the OBBBA, the partnership would have a one-month taxable year with outcomes similar to those described in part I.B.1 of this Explanation of Provisions section. Accordingly, the proposed regulations would provide an election to treat all of an affected corporation's distributive shares of certain CFTEs of affected partnerships (specified distributive shares of CFTEs) as specified foreign income taxes. *See* proposed § 1.898(c)-1(c)(2); *see also* part I.E.2 of this Explanation of Provisions section regarding the procedural requirements for making the election.

3. Relevant Succeeding Year Taxes

Section 3.03(1) of Notice 2025-72 provides that foreign income taxes accrued by an affected corporation in its succeeding taxable year are not specified foreign income taxes and, therefore, would not be allocated between the affected corporation's first required year and its succeeding taxable year. Notice 2025-72 explains that while a foreign net income tax accrued in the succeeding taxable year may relate to income accrued in the first required year, the Treasury Department and the IRS expect that the administrative and compliance burdens of allocating a portion of the succeeding year tax to the first required year would exceed the benefits of allocation.

A comment noted that the repeal of section 898(c)(2) could result in a loss of foreign tax credits if the income accrued by an affected corporation in its first required year is different in type than the income accrued by the affected corporation in its succeeding taxable year. For instance, an affected corporation may have a first required year that ends December 31, 2025, and be subject to a foreign income tax with respect to a foreign taxable year that ends on March 31, 2026. The foreign income tax that accrues on March 31, 2026, could be imposed in part on the income that accrued for Federal income tax purposes in the affected corporation's first required year. If the affected corporation does not earn the same type of income in the succeeding taxable year, then a portion of the foreign income tax would not be deemed paid because the affected corporation will not have income in the relevant income group in the succeeding taxable year. The comment also noted that, in some cases, a taxpayer may have the necessary information to allocate the succeeding year taxes before the extended due date of the majority U.S. shareholder's Federal income tax return for the taxable year with which the affected corporation's first required year ends.

The Treasury Department and the IRS continue to be of the view that, in general, the administrative and compliance burdens of allocating a portion of the succeeding year tax to the first required year would exceed the benefits of allocation. Further, maintaining the full amount of foreign income taxes in the succeeding taxable year is appropriate because a full year's worth of foreign income taxes accrue with a full year of income. Accordingly, the proposed regulations would generally provide that foreign income taxes accrued by an affected corporation in its succeeding taxable year are not specified foreign income taxes.

However, the Treasury Department and the IRS agree with the comment that, in some cases, when an affected corporation's foreign taxable year (for example, a March 31 year end) does not align with its succeeding taxable year (for example, a December 31 year end), an allocation of an affected corporation's foreign income taxes accrued in the succeeding taxable year between its first required year and its succeeding taxable year is appropriate to address the concerns described in this part I.B.3 of this Explanation of Provisions section. Accordingly, to address these circumstances, the proposed regulations would provide an irrevocable election to allocate the affected corporation's relevant succeeding year taxes between the affected corporation's first required year and its succeeding taxable year. *See* proposed § 1.898(c)-1(f); *see also* part I.E.2 of this Explanation of Provisions section regarding the procedural requirements for making the election.

C. *Ordering rules*

Section 3.04 of Notice 2025-72 provides that a specified foreign income tax would be allocated between the affected corporation's first required year and its succeeding taxable year and then taken into account in each respective taxable year under certain ordering rules. These ordering rules would coordinate statutory and regulatory provisions related to the computation of an affected corporation's income items under sections 951(a) and 951A and the computation of the foreign taxes deemed paid under section 960(a) and (d) with the allocation of foreign income taxes between the affected corporation's first required year and succeeding taxable year. No comments were received on these ordering rules, and the rules, therefore, are included in the proposed regulations. *See* proposed § 1.898(c)-1(d).

D. *Allocation method*

1. Allocation Percentage

Section 3.05 of Notice 2025-72 provides that a specified foreign income tax would be allocated between an affected corporation's first required year and its succeeding taxable year by determining an allocation percentage for each specified foreign income tax. The allocation percentage would be equal to the portion of an affected corporation's taxable income, as determined under foreign law, that is attributable under the principles of § 1.1502-76(b) to the first required year, divided by the total taxable income, as determined under foreign law, for the foreign taxable year with respect to which the specified foreign income tax is imposed. A comment requested that the proposed regulations allow taxpayers to use any reasonable allocation method that aligns foreign taxes with the income to which those taxes relate, including an allocation of an affected corporation's foreign taxes to its taxable year preceding its first required year.

For the reasons described below, the proposed regulations would require the use of a single prescriptive allocation method to implement the transition rule. *See* proposed § 1.898(c)-1(e). The allocation method would reduce the likelihood that foreign income taxes of a specified foreign corporation in the first required year would not be deemed paid as a consequence of the repeal of section 898(c)(2). Additionally, the allocation method would leverage an existing methodology that is familiar to taxpayers for allocating foreign income taxes, *see, e.g.,* §§ 1.245A-5(e)(3)(i), 1.336-2(g)(3)(ii), 1.338-9(d), and 1.901-2(f)(5), and would use taxable income as determined under foreign law, which is an amount that taxpayers are already required to consider in applying § 1.861-20. Further, the allocation method would better accommodate affected corporations that may earn uneven amounts of income in the first required year, as compared to an allocation method that is based on a set ratio such as months or days. The allocation method would provide flexibility to taxpayers because the principles of § 1.1502-76(b) allow for either a closing of the books method or a ratable allocation method for purposes of determining the portion of taxable income attributable to the first required year. Finally, the method suggested by the comment would not comply with the requirement in section 70352(c) of the OBBBA to allocate foreign taxes between a specified foreign corporation's first taxable year and its succeeding taxable year, and not to an earlier taxable year.

2. Income Group Specific Allocation Percentage

Section 3.05 of Notice 2025-72 provides that a single allocation percentage based on an affected corporation's total taxable income, as determined under foreign law, for the foreign taxable year with respect to which the specified foreign income tax is imposed would apply to the amount of a specified foreign income tax assigned to each income group of the affected corporation. A comment stated that taxpayers generally have the information needed to compute a different allocation percentage for each income group, which may better match the tax allocated to the first required year to the income accrued in that year. By way of example, the comment described a situation in which an affected corporation (AC) with its first required year ending on December 31, 2025, and a foreign taxable year that ends on December 31, 2026, recognizes gain from the sale of stock on December 15, 2025. The gain is foreign personal holding company income described in section 954(c)(1)(B) within the passive category. Under § 1.861-20, as applied in the first required year, the Country X income tax attributable to the stock gain is allocated and apportioned to AC's relevant subpart F income group within the passive category. In its succeeding taxable year, however, AC does not recognize subpart F income in the relevant subpart F income group within the passive category. Any portion of Country X income tax assigned to that income group allocated to the succeeding taxable year under a single allocation percentage would not be deemed paid under section 960(a).

The Treasury Department and the IRS are of the view that, in most cases, determining a different allocation percentage for each income group would require taxpayers to undertake potentially burdensome analyses without providing benefits, and therefore, the proposed regulations would provide, as a general rule, a single allocation percentage that is used for all income groups. However, the Treasury Department and the IRS agree with the comment that in some cases a different allocation percentage for each income group may be appropriate. Accordingly, the proposed regulations would provide an election to apply a specific allocation percentage to the amount of a specified foreign income tax assigned to each income group of an affected corporation. *See* proposed § 1.898(c)-1(e)(3); *see also* part I.E.2 of this Explanation of Provisions section regarding the procedural requirements of the election. The proposed regulations would also provide that the income group specific allocation method is required for allocating a relevant succeeding year tax between an affected corporation's first required year and its succeeding taxable year. *See* proposed § 1.898(c)-1(f)(3). An income group specific allocation percentage is computed by applying the principles of § 1.1502-76(b), using the closing of the books method, separately for each income group to which foreign law income is assigned under § 1.861-20.

3. Election to Not Allocate

Section 3.04 of Notice 2025-72 provides that a specified foreign income tax would be allocated between an affected corporation's first required year and its succeeding taxable year and then would be taken into account in each respective taxable year. A comment requested an election to forgo the allocation rule set forth in the notice and instead apply current accrual rules to specified foreign income taxes in order to allow an affected corporation's controlling domestic shareholders to determine whether these existing rules better serve their interests.

The proposed regulations adopt this comment because the Treasury Department and the IRS believe it would reduce compliance burdens. The proposed regulations would provide an election to not allocate an affected corporation's specified foreign income taxes. If the election is made, the specified foreign income taxes would be taken into account in the affected corporation's first required year. *See* proposed § 1.898(c)-1(e)(4); *see also* part I.E of this Explanation of Provisions section regarding other procedural requirements for making the election. This election would apply to all specified foreign income taxes of an affected corporation. If the election is made, the affected corporation's relevant succeeding year taxes may not be allocated between its first required year and its succeeding taxable year.

E. *Other issues*

1. Sections 905(c) and 986(a)

Section 3.06 of Notice 2025-72 provides that, for purposes of sections 905(c) and 986(a), a specified foreign income tax would accrue in the first required year, regardless of whether a portion of the specified foreign income tax is allocated to the succeeding taxable year. No comments were received on the application of these provisions to specified foreign income taxes, and the proposed regulations would provide that, for purposes of sections 905(c) and 986(a), the first required year is the year to which a specified foreign income tax relates. The proposed regulations would provide similar treatment to relevant succeeding year taxes for purposes of sections 905(c) and 986(a). *See* proposed § 1.898(c)-1(g).

2. Election Procedures

In general, the proposed regulations would provide that the elections described in parts I.B.2 (specified distributive shares of CFTEs), I.B.3 (relevant succeeding year taxes), I.D.2 (income group specific allocation percentage), and I.D.3 (election to not allocate) of this Explanation of Provisions section would be made by an affected corporation's controlling domestic shareholders for its first required year by attaching a statement to their timely filed (including extensions) Federal income tax returns for the years in which or with which the first required year and the succeeding taxable year end. *See* proposed § 1.898(c)-1(h). The election to allocate relevant succeeding year taxes would be irrevocable. *See* proposed § 1.898(c)-1(h)(1).

The proposed regulations would provide that the elections to treat specified distributive shares as specified foreign income taxes and to use the income group specific allocation percentage may be made on an amended Federal income tax return, and except for the election for allocating relevant succeeding year taxes, all of the elections may be revoked on an amended Federal income tax return. An amended Federal income tax return containing an election or revocation must be duly filed within 24 months of the due date (without regard to extensions) of the original Federal income tax return for the year in which or with which the first required year ends. An amended Federal income tax return for the taxable year in which or with which the affected corporation's succeeding taxable year ends must also be filed if needed to reflect a change in election. Permitting a change in election outside of this period could result in changes in amounts of tax due for taxable years that are no longer open for assessment under section 6501 and would increase the administrative burden of the elections. The Treasury Department and the IRS request comments on these election procedures, including the application of this 24-month limitation.

3. Covered Events

Section 3.05(3) of Notice 2025-72 provides rules that would coordinate the allocation of a specified foreign income tax with the covered event rules in § 1.901-2(f)(5) when an affected corporation is the section 901 taxpayer of a portion of the tax due to the application of those rules. *See* part I.A of this Explanation of Provisions section for a description of the covered event rules. A comment requested additional guidance coordinating the covered event rules with the allocation of specified foreign income taxes. Specifically, the comment recommended that the portion of a specified foreign income tax allocated to the succeeding taxable year be further allocated among persons based on the principles of the covered event rules. The comment suggested that the principles of the covered event rules would apply by treating the income earned in the succeeding taxable year as the income to which the specified foreign income tax relates. The comment described cases with respect to which its recommendation would apply.

The Treasury Department and the IRS are of the view that some of the cases discussed in the comment do not involve specified foreign corporations subject to the transition rule and therefore would exceed the authority granted under section 70352(c) of the OBBBA. In other cases, the mismatch of income and foreign income tax was not caused by the repeal of section 898(c)(2) and would likewise be beyond the scope of the transition rule. Finally, the Treasury Department and the IRS do not consider it appropriate to allocate a section 901 taxpayer's foreign income tax to another person. Thus, the proposed regulations do not adopt this comment and would clarify that a specified foreign corporation is an affected corporation if its first taxable year beginning after November 30, 2025, ends pursuant to section 70352(c) of the OBBBA on the date prescribed by that section, which is the last day of the first required year (within the meaning of section 898(c)(1)) ending after November 30, 2025. *See* proposed § 1.898(c)-1(b) (defining affected corporation).

4. Conforming Amendments

The proposed regulations would include conforming amendments to Treasury regulations that refer to the availability of the one-month deferral election or provide special rules when the one-month deferral election is in effect. *See* proposed §§ 1.163(j)-7(k)(29)(i)(B), 1.441-1(b)(2)(ii)(C), 1.442-2(b)(1)(i), and 1.987-11(c)(3)(ii).

II. *Proposed Regulations Implementing the Section 960(d)(4) Foreign Tax Credit Disallowance*

Section 3.01(2) of Notice 2025-77 provides that section 960(d)(4) would apply to foreign income taxes paid or accrued (or deemed paid under section 960(b)(1)) with respect to a section 959(a) distribution to the extent the PTEP results from a section 951A inclusion of a U.S. shareholder in a taxable year ending after June 28, 2025. Section 3.01(3) of Notice 2025-77 provides that the "section 951A PTEP" group set forth in § 1.960-3(c)(2)(viii) would be divided into two groups: (1) PTEP resulting from section 951A inclusions in taxable years of a U.S. shareholder ending on or before June 28, 2025 (pre-06/29/25 section 951A PTEP), and (2) PTEP resulting from section 951A inclusions in taxable years of a U.S. shareholder ending after June 28, 2025 (post-06/28/25 section 951A PTEP). Section 3.01(4) of Notice 2025-77 provides that no credit under section 901 would be allowed for 10 percent of any foreign income taxes paid or accrued (or deemed paid under section 960(b)(1)) with respect to a section 959(a) distribution of post-06/28/25 section 951A PTEP, and those taxes would be allocated and apportioned to post-06/28/25 section 951A PTEP under § 1.861-20. Section 3.01(5) of Notice 2025-77 provides that similar rules would apply to the "reclassified section 951A PTEP" group set forth in § 1.960-3(c)(2)(iv).

No comments were received on Notice 2025-77, and accordingly, the proposed regulations would include these rules. *See* proposed § 1.960-3(b)(6), (c)(2)(iv) and (v), and (c)(2)(ix) and (x). The Treasury Department and the IRS intend to modify the proposed regulations related to PTEP that were published in the **Federal Register** on December 2, 2024, (89 FR 95362) to be consistent with these proposed regulations.

III. *Applicability Dates and Reliance*

The Treasury Department and the IRS expect to finalize the proposed regulations by January 4, 2027. Under section 7805(b)(2), proposed § 1.898(c)-1 is proposed to apply to taxable years of specified foreign corporations beginning after November 30, 2025. *See* proposed § 1.898(c)-1(j). A taxpayer may rely on the proposed regulations regarding section 898(c) for foreign taxes paid or accrued before the date the proposed regulations are published as final regulations in the **Federal Register**, provided the taxpayer applies the proposed regulations regarding section 898(c) in their entirety and in a consistent manner to the first required year and succeeding taxable year of a specified foreign corporation.

Under section 7805(b)(2), proposed § 1.960-3(b)(6) is proposed to apply to foreign income taxes paid or accrued (or deemed paid under section 960(b)(1)) with respect to an amount excluded from gross income under section 959(a) by reason of a section 951A inclusion, to the extent the inclusion occurs in a taxable year of a U.S. shareholder ending after June 28, 2025. The corresponding updates to PTEP groups made by proposed § 1.960-3(c)(2) are proposed to apply to taxable years of foreign corporations ending with or within taxable years of U.S. shareholders ending after June 28, 2025. *See* proposed § 1.960-7(c). A taxpayer may rely on the proposed regulations regarding section 960(d)(4) for taxable years of U.S. shareholders beginning before the date the proposed regulations are published as final regulations in the **Federal Register**, provided the taxpayer follows the proposed regulations regarding section 960(d)(4) in their entirety and in a consistent manner for all applicable taxable years.

Special Analyses

I. *Regulatory Planning and Review -- Economic Analysis*

The Office of Management and Budget's Office of Information and Regulatory Analysis has determined that this proposed regulation is not significant and is not subject to review under section 6(b) of Executive Order 12866. Therefore, a regulatory impact assessment is not required.

II. *Paperwork Reduction Act*

The Paperwork Reduction Act of 1995, 44 U.S.C. 3501-3520 (PRA), 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. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a valid control number assigned by the OMB.

The collections of information in the proposed regulations include reporting, third-party disclosures, and recordkeeping requirements that are necessary for certain individuals and corporations to determine their foreign tax credit under section 901 and related provisions. These collections will be used by IRS for tax compliance purposes.

With respect to section 898(c), the collections in proposed § 1.898(c)-1(h) would provide procedures for making the elections described in parts I.B.2 (specified distributive shares of CFTEs), I.B.3 (relevant succeeding year taxes), I.D.2 (income group specific allocation percentage), and I.D.3 (election to not allocate) of this Explanation of Provisions section. The respondents would be persons who are controlling domestic shareholders of an affected corporation. Pursuant to proposed § 1.898(c)-1(h), respondents would be required to: (1) attach an election statement to an original or amended Federal income tax return (a reporting requirement), and (2) provide any notices required under § 1.964-1(c)(3)(iii) to the persons known to be domestic shareholders of the affected corporation in its first required year and succeeding taxable year (third-party disclosure and recordkeeping requirements).

For purposes of the PRA, the reporting burden associated with proposed § 1.898(c)-1(h) collection requirements will be reflected in the instructions for Form 5471, "Information Return of U.S. Persons With Respect to Certain Foreign Corporations." This revision will be included within the OMB Control Number 1545-0123 for business filers and will be approved by OMB in accordance with the PRA procedures under 5 CFR 1320.10.

III. *Regulatory Flexibility Act*

Pursuant to the Regulatory Flexibility Act (5 U.S.C. chapter 6) (RFA), it is hereby certified that the proposed regulations will not have a significant economic impact on a substantial number of small entities. In general, the proposed regulations would affect U.S. shareholders of foreign corporations, and with respect to proposed § 1.898(c)-1, would affect only U.S. shareholders of foreign corporations that have made the one-month deferral election. The Treasury Department and the IRS do not have adequate data readily available to assess the number of small entities potentially affected by the proposed regulations.

The Treasury Department and the IRS have determined that the proposed regulations will not have a significant economic impact on domestic small business entities. Proposed § 1.898(c)-1 would allow taxpayers to not allocate taxes (*see* part I.D.3 of this Explanation of Provisions section), and therefore, generally would impose neither new requirements nor additional costs on small entities. The only additional costs imposed on a small business entity making an election under proposed § 1.898(c)-1(c)(4) are those associated with the collection of information requirements imposed under proposed § 1.898(c)-1(h). The Treasury Department and the IRS have estimated that the average burden of this collection of information is 1.5 hours per response. The IRS's Research, Applied Analytics, and Statistics division estimates that the appropriate wage rate for taxpayers with less than $25,000,000 in total positive income is between $113.16 and $58.60. Thus, the annual burden from each collection of information requirement for small business entities is at most $169.74, which is a de minimis amount. The proposed regulations regarding section 960(d)(4) would not impose new requirements on small entities but rather would implement the statute by specifying the foreign income taxes with respect to which the foreign tax credit disallowance applies. Accordingly, the proposed regulations are not expected to have a significant economic impact on a substantial number of small entities, and a regulatory flexibility analysis is not required. Notwithstanding this certification, the Treasury Department and the IRS welcome comments on the impact of the proposed regulations on small entities, including the number of small entities that may be impacted and whether that impact would be economically significant.

IV. *Submission to the Small Business Administration*

Pursuant to section 7805(f), the proposed regulations have been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact on small businesses.

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 (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, do not impose substantial direct compliance costs on State and local governments, and do not preempt State law within the meaning of the Executive order.

Comments and Requests for a Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to comments that are submitted timely to the IRS as prescribed in the preamble under the **ADDRESSES** heading. In addition to the comments specifically requested in the Explanation of Provisions section, 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 submits electronic or written comments. Requests for a public hearing are 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**.

Statement of Availability of IRS Documents

Any IRS Revenue Procedures, Revenue Rulings, Notices, or other guidance cited in this document are published in the Internal Revenue Bulletin (or Cumulative Bulletin) and are 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*.

Drafting Information

The principal authors of these regulations are Le Chen and Hayley Rassuchine, Office of Associate Chief Counsel (International). However, other personnel from the IRS and the Treasury Department participated in their development.

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 § 1.898(c)-1 in numerical order to read as follows:

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

* * * * *

Section 1.898(c)-1 also issued under Sec. 70352(c), Pub. L. 119-21, 139 Stat. 72.

* * * * *

Par. 2. Section 1.163(j)-7 is amended by revising paragraph (k)(29)(i)(B) to read as follows:

§ 1.163(j)-7 Application of the section 163(j) limitation to foreign corporations and United States shareholders.

* * * * *

(k) * * *

(29) * * *

(i) * * *

(B) If the specified group parent is an applicable CFC, the period ending on the last day of the specified group parent's required year described in section 898(c)(1) and beginning on the first day after the last day of the specified group's immediately preceding specified period.

* * * * *

Par. 3. Section 1.441-1 is amended by revising paragraph (b)(2)(ii)(C) to read as follows:

§ 1.441-1 Period for computation of taxable income.

* * * * *

(b) * * *

(2) * * *

(ii) * * *

(C) *Specified foreign corporations*. A specified foreign corporation (as defined in section 898(b)) may use a taxable year other than its required taxable year if it elects a 52–53–week taxable year that ends with reference to its required taxable year as provided in paragraph (b)(2)(ii)(A) of this section.

* * * * *

Par. 4. Section 1.441-2 is amended by revising the fourth sentence of paragraph (b)(1)(i) to read as follows:

§ 1.441-2 Election of taxable year consisting of 52–53 weeks.

* * * * *

(b) * * *

(1) * * *

(i) * * * Similarly, a newly-formed specified foreign corporation (as defined in section 898(b)) may adopt a 52–53–week taxable year if such year ends with reference to the taxpayer's required taxable year. * * *

* * * * *

Par. 5. Add § 1.898(c)-1 under the undesignated center heading "*Miscellaneous Provisions*" to read as follows:

§ 1.898(c)-1 Allocation of foreign income taxes of specified foreign corporations affected by the repeal of section 898(c)(2).

(a) *Overview.* This section provides rules for allocating certain foreign taxes paid or accrued by a specified foreign corporation that is required to change its first taxable year beginning after November 30, 2025, pursuant to section 70352(c)(1)(C) of Public Law 119-21, 139 Stat. 72 (July 4, 2025), commonly known as the One, Big, Beautiful Bill Act (OBBBA). Paragraph (b) of this section provides definitions for purposes of this section. Paragraph (c) of this section generally identifies which foreign taxes of an affected corporation are allocated between the affected corporation's first required year and its succeeding taxable year. Paragraph (d) of this section provides ordering rules for allocating a specified foreign income tax under this section. Paragraph (e) of this section provides allocation methods for purposes of determining the amount of a specified foreign income tax allocated to the first required year and the succeeding taxable year and an election to not allocate specified foreign income taxes. Paragraph (f) of this section provides an election to allocate relevant succeeding year taxes between an affected corporation's first required year and its succeeding taxable year. Paragraph (g) of this section provides rules for the treatment of specified foreign income taxes and relevant succeeding year taxes under sections 905(c) and 986(a). Paragraph (h) of this section provides procedures for making the elections provided under paragraphs (c)(2), (e)(3) and (4), and (f) of this section. Paragraph (i) of this section provides examples illustrating the application of this section. Paragraph (j) of this section provides the applicability date.

(b) *Definitions*. The following definitions apply for purposes of this section.

Affected corporation means a specified foreign corporation (as defined in section 898(b)) that takes into account foreign income taxes under an accrual method of accounting and whose first taxable year beginning after November 30, 2025, ends pursuant to section 70352(c) of the OBBBA on the date prescribed by that section.

Affected partnership means a partnership that takes into account foreign income taxes under an accrual method of accounting and whose first taxable year beginning after November 30, 2025, is required to change due to one or more of its partners changing their first taxable year as required by section 70352(c) of the OBBBA.

Allocation percentage has the meaning set forth in paragraph (e)(1) of this section.

Creditable foreign tax expenditure (CFTE) has the meaning set forth in § 1.704-1(b)(4)(viii).

First required year means, with respect to an affected corporation or affected partnership, the first taxable year beginning after November 30, 2025.

Foreign net income tax means a foreign income tax (as defined in § 1.901-2(a)) that is computed based on items of income, gain, deduction, and loss that arise in a foreign taxable year.

Income group specific allocation percentage has the meaning set forth in paragraph (e)(3) of this section.

Relevant succeeding year tax has the meaning set forth in paragraph (f)(1) of this section.

Section 901 taxpayer means the taxpayer described § 1.901-2(f).

Specified distributive share of a CFTE has the meaning set forth in paragraph (c)(2) of this section.

Specified foreign income tax has the meaning set forth in paragraph (c)(1) of this section.

Succeeding taxable year means, with respect to an affected corporation or affected partnership, the taxable year immediately following the first required year.

United States shareholder has the meaning provided in section 951(b).

(c) *Specified foreign income taxes*--(1) *In general*. Except as provided in paragraph (e)(4) of this section, specified foreign income taxes are allocated between an affected corporation's first required year and its succeeding taxable year under this section. A specified foreign income tax is a foreign net income tax accrued without regard to this section by an affected corporation in its first required year for which the affected corporation is the section 901 taxpayer.

(2) *Election to allocate specified distributive shares of CFTEs*. An election may be made under this paragraph (c)(2) pursuant to the procedures of paragraph (h) of this section. If an election is in effect under this paragraph (c)(2), all specified distributive shares of CFTEs of an affected corporation are treated as specified foreign income taxes. A specified distributive share of a CFTE is an affected corporation's distributive share of a CFTE of an affected partnership if--

(i) The affected corporation takes into account its distributive share of the CFTE in its first required year;

(ii) The CFTE is a foreign net income tax; and

(iii) The affected partnership's first required year ends at the same time as the affected corporation's first required year.

(d) *Ordering rules*. The following ordering rules apply for allocating an affected corporation's specified foreign income taxes between the affected corporation's first required year and its succeeding taxable year.

(1) First, specified foreign income taxes are determined.

(2) Second, each specified foreign income tax is allocated and apportioned to income groups pursuant to the rules in this paragraph (d)(2). Section 1.861-20, as modified by § 1.960-1(d)(3)(ii)(B), is applied in the first required year to allocate and apportion the specified foreign income tax to the income groups described in § 1.960-1(d)(2) and the PTEP groups treated as income groups under § 1.960-1(d)(3)(ii)(B) in that year, except that the tentative gross tested income items described in § 1.951A-2(c)(7)(ii) are treated as income groups described in § 1.960-1(d)(2)(ii)(C). Whether any item meets the high-tax exception to foreign base company income in § 1.954-1(d) (high-tax exception) or the high-tax exclusion from tested income in § 1.951A-2(c)(7) (high-tax exclusion) in either the first required year or the succeeding taxable year is determined under paragraph (d)(4) of this section.

(3) Third, the allocation method provided in paragraph (e) of this section is applied to determine the amount of specified foreign income tax in each income group that is allocated to the first required year and the succeeding taxable year.

(4) Fourth, for all purposes of the Internal Revenue Code, except for sections 905(c) and 986(a), the amounts of a specified foreign income tax (assigned to the income groups determined under paragraph (d)(2) of this section) that are allocated to the first required year and the succeeding taxable year under paragraph (d)(3) of this section are treated as accruing in each respective year. Thus, for example, the amounts of a specified foreign income tax allocated to the first required year and the

succeeding taxable year accrue in each respective year for purposes of computing the affected corporation's items of subpart F income and tested income under sections 952 and 951A (including whether any item meets the high-tax exception or the high-tax exclusion), earnings and profits, and taxes deemed paid under section 960(a), (b), or (d). The amount of a specified foreign income tax allocated to the succeeding taxable year is treated as accruing on the first day of the succeeding taxable year and is not allocated among, and considered paid by, two or more persons under § 1.901-2(f) by reason of events that occur in the succeeding taxable year.

(e) *Allocation method*--(1) *In general*. Subject to the special rules provided in paragraph (e)(2) of this section and the elections described in paragraphs (e)(3) and (4) of this section, the amount of a specified foreign income tax assigned to each income group allocated to the first required year is the specified foreign income tax assigned to that income group multiplied by a fraction (the allocation percentage), the numerator of which is the portion of taxable income, as determined under foreign law, that is attributable to the first required year under the principles of § 1.1502-76(b), and the denominator of which is the total taxable income, as determined under foreign law, for the foreign taxable year with respect to which the specified foreign income tax is imposed. The amount of a specified foreign income tax assigned to each income group remaining after the application of the preceding sentence is allocated to the succeeding taxable year.

(2) *Special rules*--(i) *Allocation method for PTEP groups*. The amount of a specified foreign income tax assigned to a PTEP group under paragraph (d)(2) of this section is allocated to the first required year. The numerator and the denominator of the allocation percentage is adjusted to exclude the foreign law taxable income on which that amount of specified foreign income tax is imposed.

(ii) *Allocation method in the case of certain covered events*. If an affected corporation is the section 901 taxpayer of a portion of a specified foreign income tax by reason of the application of § 1.901-2(f)(5), then the allocation percentage is adjusted as follows--

(A) In the case of an affected corporation whose period of existence or ownership (as determined under § 1.901-2(f)(5)) begins on or before the start of the first required year, the denominator of the allocation percentage is the total foreign law taxable income attributable to the affected corporation's period of existence or ownership (as determined under § 1.901-2(f)(5)).

(B) In the case of an affected corporation whose period of ownership (as determined under § 1.901-2(f)(5)) begins after the start of the first required year, the allocation percentage is deemed to be 100 percent.

(3) *Election to apply income group specific allocation method*. An election may be made under this paragraph (e)(3) pursuant to the procedures of paragraph (h) of this section. If an election is in effect under this paragraph (e)(3), the amount of a specified foreign income tax assigned to each income group allocated to the affected corporation's first required year is the amount of specified foreign income tax assigned to that income group multiplied by a fraction (the income group specific allocation percentage), the numerator of which is the portion of foreign taxable income assigned under § 1.861-20 to the income group that is attributable to the first required year under the principles of § 1.1502-76(b) (using the closing of the books method described in § 1.1502-76(b)(2)(i)), and the denominator of which is the total foreign taxable income assigned under § 1.861-20 to the income group. Adjustments similar to the adjustments provided by paragraph (e)(2) of this section are made in the computation of the income group specific allocation percentage. The amount of specified foreign income tax

assigned to each income group remaining after the application of the preceding sentences is allocated to the succeeding taxable year.

(4) *Election to not allocate specified foreign income taxes*. An election may be made under this paragraph (e)(4) pursuant to the procedures of paragraph (h) of this section. If an election is in effect under this paragraph (e)(4), the specified foreign income taxes of an affected corporation are taken into account in the affected corporation's first required year, and the affected corporation's relevant succeeding year taxes cannot be allocated under paragraph (f) of this section.

(f) *Election to allocate relevant succeeding year taxes*--(1) *In general*. An election may be made under this paragraph (f) pursuant to the procedures of paragraph (h) of this section. If an election is in effect under this paragraph (f), the relevant succeeding year taxes of an affected corporation are allocated between the affected corporation's first required year and its succeeding taxable year under this paragraph (f). A relevant succeeding year tax is a foreign net income tax accrued without regard to this section by the affected corporation in its succeeding taxable year for which the affected corporation is the section 901 taxpayer but only if the foreign taxable year with respect to which the tax is imposed begins before the first day of the affected corporation's succeeding taxable year. If the affected corporation is the section 901 taxpayer of a portion of a foreign net income tax by reason of the application of § 1.901-2(f)(5), then the foreign net income tax is a relevant succeeding year tax only if the affected corporation's period of ownership begins before the beginning of its succeeding taxable year. A relevant succeeding year tax includes an affected corporation's distributive share of a CFTE from an affected partnership that the affected corporation takes into account in its succeeding taxable year if the requirements of paragraphs (c)(2)(ii) and (iii) of this section are met and the foreign taxable year with respect to which the CFTE is imposed begins before the last day of the partnership's succeeding taxable year.

(2) *Ordering rules*. The ordering rules described in paragraph (d) of this section apply for allocating a relevant succeeding year tax between an affected corporation's first required year and its succeeding taxable year, except that in applying paragraph (d)(2) of this section, a relevant succeeding year tax is allocated and apportioned to income groups in the succeeding taxable year. A relevant succeeding year tax assigned to a PTEP group under paragraph (d)(2) of this section is allocated to the succeeding taxable year. The amount of a relevant succeeding year tax allocated to the first required year is treated as accruing on the last day of the affected corporation's first required year and is not allocated to and among, and therefore, not considered paid by, two or more persons under § 1.901-2(f) by reason of events that occur in the first required year.

(3) *Allocation method*. The income group specific allocation method described in paragraph (e)(3) of this section applies to determine the amount of a relevant succeeding year tax assigned to each income group allocated between an affected corporation's first required year and its succeeding taxable year.

(g) *Application of sections 905(c) and 986(a)*. For purposes of sections 905(c) and 986(a), a specified foreign income tax accrues in the first required year, and a relevant succeeding year tax accrues in the succeeding taxable year, regardless of the allocation of the tax under this section. Therefore, for purposes of sections 905(c) and 986(a), the first required year is the year to which a specified foreign income tax relates, and the succeeding taxable year is the year to which a relevant succeeding year tax relates. Thus, for example, any change in the liability for a specified foreign income tax results in the following. First, the amount of the specified foreign income tax accrued (without regard to the application of this section) in the first required year is adjusted to reflect the change in liability. Second, the ordering rules of paragraphs (d)(1) through (3) of this section are applied based upon the adjusted amount of the specified foreign income tax. Third, paragraph (d)(4) of this section applies to the adjusted amounts of specified foreign income tax that are treated as accruing in the first required year and the succeeding taxable year by reason of the reapplication of paragraphs (d)(1) through (3) of this section.

(h) *Election procedures*. This paragraph (h) provides rules for making and revoking the elections described in paragraphs (c)(2), (e)(3) and (4), and (f) of this section.

(1) *Persons making the election*. An election is made by the controlling domestic shareholders (as defined in § 1.964-1(c)(5)) of the affected corporation for its first required year. An election made under paragraph (f) of this section is irrevocable.

(2) *Consistency requirement*. If an election is made with respect to an affected corporation, then the election applies to all United States shareholders of the affected corporation for its first required year and its succeeding taxable year.

(3) *Manner*--(i) *In general*. An election under paragraph (c)(2), (e)(3) or (4), or (f) of this section must be made in accordance with this paragraph (h)(3), and as the Secretary of the Treasury or the Secretary's delegate may provide in forms, instructions, publications, or other guidance.

(A) *Election statement requirement*. The controlling domestic shareholders must file the statement required under § 1.964-1(c)(3)(ii) with their timely filed (including extensions) original Federal income tax returns, or in the case of an election under paragraph (c)(2) or (e)(3) of this section, with their amended Federal income tax returns in accordance with paragraph (h)(3)(ii) of this section, for the taxable years of the controlling domestic shareholders in which or with which the affected corporation's first required year and succeeding taxable year end. The statement must be attached to the

Form 5471, *Information Return of U.S. Persons With Respect To Certain Foreign Corporations*, filed with respect to the affected corporation and titled as follows:

(*1*) “Section 898 Specified Distributive Shares of CFTEs Election Statement” for an election under paragraph (c)(2) of this section;

(*2*) “Section 898 Income Group Specific Election Statement” for an election under paragraph (e)(3) of this section;

(*3*) “Section 898 Non-Allocation Election Statement” for an election under paragraph (e)(4) of this section; and

(*4*) “Section 898 Relevant Succeeding Year Tax Election Statement” for an election made under paragraph (f) of this section.

(B) *Notice requirement*. The controlling domestic shareholders making an election must provide any notices required under § 1.964-1(c)(3)(iii). For this purpose, a domestic shareholder under § 1.964-1(c)(3)(iii) includes any person known to be a domestic shareholder in the succeeding taxable year.

(ii) *Election (or revocation) with an amended Federal income tax return*. In the case of an election under paragraph (c)(2) or (e)(3) of this section, or a revocation of an election under paragraph (c)(2), (e)(3) or (4) of this section, made with an amended Federal income tax return--

(A) The election (or revocation) must be made on an amended Federal income tax return duly filed within 24 months of the due date (without regard to extensions) of the original Federal income tax return for the taxable year of each controlling domestic shareholder with or within which the affected corporation’s first required year ends; and

(B) If a Federal income tax return for the taxable year of any controlling domestic shareholder with or within which the affected corporation’s succeeding taxable year ends has already been filed, an amended Federal income tax return for that year must be filed consistent with the election or revocation of the election.

(i) *Examples*. The following examples illustrate the application of this section.

(1) *Assumed facts*. For purposes of the examples in this paragraph (i), unless otherwise indicated, the following facts are assumed:

(i) CFCX is a specified foreign corporation.

(ii) CFCX's first required year is from December 1, 2025, to December 31, 2025.

(iii) CFCX's succeeding taxable year is from January 1, 2026, to December 31, 2026.

(iv) CFCX takes into account foreign income taxes under an accrual method of accounting.

(v) The functional currency of all qualified business units is the u, and all foreign income taxes are denominated in the u.

(2) *Example 1: Specified foreign income taxes*--(i) *Facts*. CFCX is subject to tax in Country X on the basis of its items of income, gain, deduction, and loss for its Country X taxable year, and the Country X tax is a foreign income tax within the meaning of § 1.901-2(a). CFCX's Country X taxable year is the calendar year. CFCX accrues Country X tax of 7,200u in its first required year. An election under paragraph (e)(4) of this section is not in effect.

(ii) *Analysis*. The 7,200u of Country X tax is a specified foreign income tax under paragraph (c)(1) of this section because it is a foreign net income tax that is accrued by CFCX, an affected corporation, in CFCX's first required year, and CFCX is the section 901 taxpayer of the tax. Accordingly, the 7,200u of Country X tax is allocated between CFCX's first required year and its succeeding taxable year under this section.

(3*) Example 2: Specified distributive share of CFTEs*--(i) *Facts*--(A) *Partnership W and Partnership Y*. CFCX owns 40 percent and 60 percent interests, respectively, in the profits and capital of two foreign business entities: Partnership W, an entity classified as a partnership for Federal income tax purposes that is organized and operates in Country W, and Partnership Y, an entity classified as a partnership for Federal income tax purposes that is organized and operates in Country Y. The remaining interests (60 percent and 40 percent, respectively) in the profits and capital of Partnership W and Partnership Y are owned by persons unrelated to CFCX. Partnership W and Partnership Y each take into account foreign income taxes under an accrual method of accounting. Partnership W and Partnership Y are subject to tax in their countries on the basis of their items of income, gain, deduction, and loss for their foreign taxable year. The Country W tax and the Country Y tax are foreign income taxes within the meaning of § 1.901-2(a). Each partnership's foreign taxable year is the calendar year. Partnership W's U.S. taxable year has always been the calendar year.

(B) *Distributive shares of CFTEs*. For its U.S. taxable year beginning on January 1, 2025, and ending on December 31, 2025, Partnership W accrues Country W tax of 10,000u. For its first required year ending on December 31, 2025, CFCX's distributive share of the Country W tax is 4,000u. For its taxable years beginning before November 30, 2025, Partnership Y's U.S. taxable year ended on November 30. Under section 706(b), Partnership Y is required to change its first taxable year beginning after November 30, 2025, due to CFCX changing its first taxable year beginning after November 30, 2025, by reason of the repeal of section 898(c)(2). For its U.S. taxable year ending on December 31, 2025, Partnership Y accrues Country Y tax of 10,000u. For its first required year ending on December 31, 2025, CFCX's distributive share of the Country Y tax is 6,000u. An election under paragraph (c)(2) of this section is in effect.

(ii) *Analysis*--(A) *Country W tax*. CFCX's 4,000u distributive share of Country W tax is not allocated between CFCX's first required year and its succeeding taxable year under this section. CFCX's 4,000u distributive share of Country W tax is not a specified distributive share of a CFTE because Partnership W is not an affected partnership as defined in paragraph (b) of this section. Partnership W is not an affected partnership because Partnership W was not required to change its taxable year under section 706(b) due to one or more of its partners changing their first taxable year beginning after November 30, 2025, by reason of the repeal of section 898(c)(2). Accordingly, even though an election is in effect under paragraph (c)(2) of this section, CFCX's 4,000u distributive share of the Country W tax is not treated as a specified foreign income tax. Therefore, CFCX's 4,000u distributive share of the Country W tax is not allocated under this section and continues to be taken into account in CFCX's first required year.

(B) *Country Y tax*. CFCX's 6,000u distributive share of Country Y tax is allocated between CFCX's first required year and its succeeding taxable year under the rules of this section because it is a specified distributive share of a CFTE, and an election is in effect under paragraph (c)(2) of this section. Partnership Y is an affected partnership under paragraph (b) of this section because it takes into account foreign income taxes under an accrual method of accounting and is required to change its taxable year under section 706(b) due to its partners changing their first taxable year beginning after November 30, 2025, by reason of the repeal of section 898(c)(2). Further, the Country Y tax is a foreign net income tax, CFCX takes into account its distributive share of the Country Y tax in its first required year, and Partnership Y's first required year ends at the same time (December 31, 2025) as CFCX's first required year.

(4) *Example 3: Allocation of relevant succeeding year taxes*--(i) *Facts*. The facts are the same as in paragraph (i)(2)(i) of this section (*Example 1*), except as follows. CFCX accrues 6,000u of Country X tax in its Country X taxable year beginning on January 1, 2026, and ending on December 31, 2026. CFCX also wholly owns DEZ, a disregarded entity that is organized and operated in Country Z. DEZ is subject to tax in Country Z on the basis of its items of income, gain, deduction, and loss for its Country Z

taxable year, and the Country Z tax is a foreign income tax within the meaning of § 1.901-2(a). DEZ's Country Z taxable year begins on April 1, 2025, and ends on March 31, 2026. CFCX accrues 5,000u of Country Z tax in its succeeding taxable year. An election is in effect under paragraph (f) of this section.

(ii) *Analysis*. Because an election is in effect under paragraph (f) of this section, the relevant succeeding year taxes of CFCX are allocated between its first required year and its succeeding taxable year. The 6,000u of Country X tax is not a relevant succeeding year tax under paragraph (f)(1) of this section because the Country X taxable year with respect to which the tax is imposed did not begin before January 1, 2026. The 5,000u of Country Z tax is a relevant succeeding year tax under paragraph (f)(1) of this section because it is a foreign net income tax accrued in CFCX's succeeding taxable year, for which CFCX is the section 901 taxpayer, and the Country Z taxable year with respect to which the 5,000u of Country Z tax is imposed began before January 1, 2026. Accordingly, the 5,000u of Country Z tax is allocated between CFCX's first required year and its succeeding taxable year under paragraph (f) of this section.

(5) *Example 4: § 1.901-2(f)(5) and relevant succeeding year taxes*--(i) *Facts*. The facts are the same as in paragraph (i)(4)(i) of this section (*Example 3*) except as follows. CFCX acquires the interests in DEZ on February 1, 2026. Applying the principles of § 1.1502-76(b), and using the ratable allocation method under § 1.1502-76(b), CFCX is allocated and is treated as paying under § 1.901-2(f)(5), 833u (5,000u x (2 months of foreign law taxable income over 12 months of foreign law taxable income)) of the Country Z tax that accrues on March 31, 2026.

(ii) *Analysis*. The 833u of Country Z tax is not a relevant succeeding year tax. While the Country Z taxable year began before January 1, 2026, CFCX's period of ownership of DEZ did not begin before January 1, 2026. Therefore, no portion of the 833u of Country Z tax is allocated to CFCX's first required year.

(6) *Example 5: Application of § 1.861-20 and allocation of specified foreign income tax*--(i) *Facts*. The facts are the same as in paragraph (i)(2)(i) of this section (*Example 1*). In addition, CFCX's total taxable income under Country X law for the Country X taxable year ending on December 31, 2025, is 45,000u. Applying the principles of § 1.1502-76(b), 3,750u of this income is attributable to CFCX's first required year. Under § 1.861-20, the 7,200u of Country X tax is allocated and apportioned to the income groups under paragraph (d)(2) of this section as follows: 5,400u to general category tentative gross tested income attributable to the CFC tested unit (CFC income group) and 1,800u to the general category foreign base company services income group (FBCServ income group).

(ii) *Analysis*. Pursuant to the ordering rules in paragraph (d) of this section, the 7,200u of Country X tax is allocated and apportioned to the income groups under paragraph (d)(2) of this section before applying the allocation method under paragraph (e)(1) of this section to determine the amount of the Country X tax that is allocated to CFCX's first required year and succeeding taxable year under paragraph (d)(3) of this section. The allocation method applies as follows. The amount of CFCX's taxable income under Country X law that is attributable to the first required year (3,750u) is divided by the total taxable income for the Country X taxable year (45,000u), which results in an allocation percentage of 8.33 percent. The amount of Country X tax in each income group that is allocated to the first required year is determined by applying the allocation percentage to the amount of the specified foreign income tax in each income group. Therefore, the following amounts of the Country X tax are allocated to the first required year: 450u, which is assigned to the CFC income group (8.33 percent of 5,400u); and 150u, which is assigned to the FBCServ income group (8.33 percent of

1,800u). The remaining amount of Country X tax in each income group is allocated to CFCX's succeeding taxable year as follows: 4,950u, assigned to the CFC income group (5,400u-450u) and 1,650u, assigned to the FBCServ income group (1,800u-150u).

(7) *Example 6: Income group specific allocation method*--(i) *Facts*. The facts are the same as in paragraph (i)(6)(i) of this section (*Example 5*), except as follows. An election is made under paragraph (e)(3) of this section to use the income group specific allocation method. In applying § 1.861-20 under paragraph (d)(2) of this section, 33,750u of CFCX's taxable income under Country X law is assigned to the CFC income group, and 11,250u of CFCX's taxable income under Country X law is assigned to the FBCServ income group. Applying the principles of § 1.1502-76(b) and using a closing of the books method under § 1.1502-76(b) to the items of Country X income, gain, deduction, and loss assigned to each income group, 2,250u of CFCX's Country X taxable income assigned to the CFC income group is attributable to the first required year, and 1,125u of CFCX's Country X taxable income assigned to the FBCServ income group is attributable to the first required year.

(ii) *Analysis*--(A) *Tax assigned to the CFC income group*. The income group specific allocation method applies as follows. Under § 1.861-20, 5,400u of the Country X tax is assigned to the CFC income group. The amount of CFCX's Country X taxable income assigned to the CFC income group that is attributable to the first required year (2,250u) is divided by CFCX's total Country X taxable income assigned to that income group for the Country X taxable year (33,750u), which results in a specific income group allocation percentage of 6.66 percent. Therefore, 360u of Country X tax assigned to the CFC income group is allocated to the first required year. The remaining amount of Country X tax assigned to the CFC income group (5,040u) is allocated to the succeeding taxable year.

(B) *Tax assigned to the FBCServ income group*. Under § 1.861-20, 1,800u of Country X tax is assigned to the FBCServ income group. The amount of CFCX's Country X taxable income assigned to this income group that is attributed to the first required year (1,125u) is divided by CFCX's total Country X taxable income assigned to that income group for the Country X taxable year (11,250u), which results in a specific income group allocation percentage of 10 percent. Therefore, 180u of Country X tax assigned to the FBCServ income group is allocated to the first required year. The remaining amount of Country X tax assigned to the FBCServ income group (1,620u) is allocated to the succeeding taxable year.

(8) *Example 7: Application of the high-tax exclusion*--(i) *Facts*. The facts are the same as in paragraph (i)(7)(i) of this section (*Example 6*), except as follows. An election under § 1.951A-2(c)(7)(viii) is in effect with respect to CFCX for the first required year. Under § 1.951A-2(c)(7)(ii), CFCX has two tentative gross tested income items: 3,000u in the CFC income group and 2,000u of general category tentative gross tested income attributable to the DEZ tested unit. CFCX accrues no expenses in its first required year other than the specified foreign income tax.

(ii) *Analysis*. Under paragraph (g) of this section, the portion of the Country X tax allocated to the first required year is treated as the amount of Country X tax accrued in that taxable year for all purposes of the Code except sections 905(c) and 986(a). Therefore, in determining whether any of CFCX's tentative gross tested income items meet the high-tax exclusion, 360u of Country X tax is treated as accrued in the first required year and allocated and apportioned to the CFC income group, the statutory grouping to which 3,000u of gross income is assigned. If an election under § 1.951A-2(c)(7)(viii) is in effect with respect to CFCX for the succeeding taxable year, the 5,040u of Country X tax assigned to the CFC income group would be taken into account in the same manner in that year.

(j) *Applicability date*. This section applies to taxable years of specified foreign corporations beginning after November 30, 2025.

Par. 6. Section 1.901-1 is amended by revising paragraph (b) to read as follows:

§ 1.901-1 Allowance of credit for foreign income taxes.

* * * * *

(b) *Limitations*. Certain Code sections, including sections 245A(d) and (e)(3), 814, 901(e) through (m), 904, 906 through 909, 911, 960(d)(4), 965(g), 999, and 6038, reduce, defer, or otherwise limit the credit against the tax imposed by chapter 1 of the Code for certain amounts of foreign income taxes.

* * * * *

Par. 7. Section 1.960-3 is amended by:

1. Revising the section heading;

2. Revising the first sentence of paragraph (a);

3. Revising the heading of paragraph (b) and the second sentence of paragraph (b)(1);

4. Adding paragraph (b)(6);

5. In paragraph (c)(2)(iii)(B), removing the language "paragraphs (c)(2)(vi) through (ix)" and adding "paragraphs (c)(2)(vii) through (xi)" in its place;

6. Revising paragraph (c)(2)(iv);

7. Redesignating paragraphs (c)(2)(v), (c)(2)(vi), (c)(2)(vii), (c)(2)(viii), (c)(2)(ix), and (c)(2)(x) as paragraphs (c)(2)(vi), (c)(2)(vii), (c)(2)(viii), (c)(2)(ix), (c)(2)(xi), and (c)(2)(xii), respectively, and adding new paragraph (c)(2)(v);

8. In newly redesignated paragraph (c)(2)(vi), removing the language "paragraphs (c)(2)(v)(A)" and adding "paragraphs (c)(2)(vi)(A)" in its place;

9. Revising newly redesignated paragraph (c)(2)(ix);

10. Adding new paragraph (c)(2)(x);

11. In newly redesignated paragraph (c)(2)(xi), removing the language "paragraphs (c)(2)(ix)(A)" and adding "paragraphs (c)(2)(xi)(A)" in its place;

12. In newly redesignated paragraph (c)(2)(xii), removing the language "paragraph (c)(2)(vi) through (ix)" and adding "paragraph (c)(2)(vii) through (xi)" in its place;

13. In paragraph (e)(2), removing the language "section 951A PTEP" wherever it appears and adding "pre-06/29/25 section 951A PTEP" in its place; and

14. Adding paragraphs (e)(3) and (4).

The revisions and additions read as follows:

§ 1.960-3 Foreign income taxes deemed paid under section 960(b) and foreign tax credits disallowed under section 960(d)(4).

(a) * * * Paragraph (b) of this section provides rules for computing the amount of foreign income taxes deemed paid by a domestic corporation that is a United States shareholder of a controlled foreign corporation, or by a controlled foreign corporation, under section 960(b), and for determining the foreign income taxes subject to the credit disallowance under section 960(d)(4). * * *

(b) *Foreign income taxes deemed paid under section 960(b) and foreign tax credits disallowed under section 960(d)(4)*--(1) * * * See paragraph (b)(6) of this section for rules disallowing credits in relation to a distribution of certain previously taxed earnings and profits resulting from the application of section 960(d)(4), and § 1.965-5(c)(1)(iii) for rules disallowing credits in relation to a distribution of certain previously taxed earnings and profits resulting from the application of section 965. * * *

* * * * *

(6) *Foreign tax credits disallowed under section 960(d)(4)*--(i) *In general.* No credit under section 901 is allowed for 10 percent of--

(A) Foreign income taxes attributable to a section 959(a) distribution of post-06/28/25 section 951A PTEP (as defined in paragraph (c)(2)(ix) of this section) or reclassified post-06/28/25 section 951A PTEP (as defined in paragraph (c)(2)(iv) of this section); and

(B) Foreign income taxes deemed paid under paragraph (b)(1) of this section with respect to a section 959(a) distribution of post-06/28/25 section 951A PTEP (as defined in paragraph (c)(2)(ix) of this section) or reclassified post-06/28/25 section 951A PTEP (as defined in paragraph (c)(2)(iv) of this section).

(ii) *Attribution of foreign income taxes.* For purposes of paragraph (b)(6)(i)(A) of this section, foreign income taxes are attributable to a section 959(a) distribution of post-06/28/25 section 951A PTEP or reclassified post-06/28/25 section 951A PTEP if those taxes would be allocated and apportioned to a distribution of those previously taxed earnings and profits under the rules of § 1.861-20, applied by treating the portion of the distribution that is attributable to post-06/28/25 section 951A PTEP and reclassified post-06/28/25 section 951A PTEP as the statutory groupings, and the portion of the distribution that is attributable to other earnings and profits as the residual grouping.

(c) * * *

(2) * * *

(iv) Earnings and profits described in section 959(c)(1)(A) that were initially described in paragraph (c)(2)(ix) of this section (“reclassified post-06/28/25 section 951A PTEP”);

(v) Earnings and profits described in section 959(c)(1)(A) that were initially described in paragraph (c)(2)(x) of this section (“reclassified pre-06/29/25 section 951A PTEP”);

* * * * *

(ix) Earnings and profits described in section 959(c)(2) by reason of section 951A, to the extent that the inclusion under section 951A occurs in a taxable year of a United States shareholder ending after June 28, 2025 ("post-06/28/25 section 951A PTEP");

(x) Earnings and profits described in section 959(c)(2) by reason of section 951A, to the extent not described in paragraph (c)(2)(ix) of this section ("pre-06/29/25 section 951A PTEP");

* * * * *

(e) * * *

(3) *Example 3: Foreign tax credits disallowed under section 960(d)(4)*--(i) *Facts.* USP, a domestic corporation, owns all of the stock of a single foreign corporation (FC1). FC1, a Country X entity that is a controlled foreign corporation, has the U.S. dollar as its functional currency. Both FC1 and USP use the calendar year as their taxable year. FC1 does not have any accumulated earnings and profits as of the beginning of its 2024 taxable year. FC1 earns tested income of $100x for each of its 2024 and 2025 taxable years, and USP has an inclusion under section 951A (section 951A inclusion) of $100x in each of its 2024 and 2025 taxable years. FC1 has no items of income, gain, deduction, or loss in any of its subsequent taxable years. On January 1, 2026, FC1 distributes $150x to USP, which is a section 959(a) distribution and is treated as a distribution of property for both Country X law and Federal income tax purposes. Country X imposes a withholding tax (as defined in section 901(k)(1)(B)) of $30x with respect to the section 959(a) distribution. For its 2026 taxable year, USP claims the foreign tax credit under section 901.

(ii) *Analysis*--(A) *PTEP groups.* FC1 has earnings and profits of $100x within the annual PTEP account in the section 951A category for its 2024 taxable year. Under paragraph (c)(2)(x) of this section, the $100x of previously taxed earnings and profits, which results from a section 951A inclusion of USP in a taxable year of USP ending on or before June 28, 2025, constitutes pre-06/29/25 section 951A PTEP. FC1 also has earnings and profits of $100x within the annual PTEP account in the section 951A category for its 2025 taxable year. Under paragraph (c)(2)(ix) of this section, the $100x of previously taxed earnings and profits, which results from a section 951A inclusion of USP in a taxable year of USP ending after June 28, 2025, constitutes post-06/28/25 section 951A PTEP.

(B) *Attribution of foreign income taxes.* Under section 959(c) and § 1.959-3(b), FC1's $150x distribution on January 1, 2026, constitutes a distribution of $100x of FC's previously taxed earnings and profits for its 2025 taxable year and $50x of FC's previously taxed earnings and profits for its 2024 taxable year. Under paragraph (b)(6)(ii) of this section and § 1.861-20(d)(3)(i)(B), $100x of the foreign gross income related to the $150x distribution is assigned to the statutory grouping for the portion of the distribution attributable to post-06/28/25 section 951A PTEP, and $50x is assigned to the residual grouping for the portion of the distribution attributable to other earnings and profits. Under paragraph (b)(6)(ii) of this section and § 1.861-20(f), $20x of the $30x of Country X withholding tax ($30x x $100x/$150x) is allocated and apportioned to the statutory grouping, and the remaining $10x ($30x x $50x/$150x) is allocated and apportioned to the residual grouping.

(C) *Disallowance of foreign tax credits.* Under section 960(d)(4) and paragraph (b)(6)(i)(A) of this section, $2x (that is, 10 percent) of the $20x of foreign tax credits otherwise allowable to USP under section 901 with respect to the $20x of Country X withholding tax allocated and apportioned to the statutory grouping is disallowed.

(iii) *Alternative facts--Distribution before June 28, 2025*. The facts are the same as in paragraph (e)(3)(i) of this section, except that the $150x distribution occurs on February 1, 2025. The result is the same as in paragraph (e)(3)(ii) of this section.

(4) *Example 4: Foreign tax credit disallowance under section 960(d)(4) for foreign income taxes deemed paid under section 960(b)*--(i) *Facts*. The facts are the same as in paragraph (e)(3)(i) of this section (*Example 3*), except as follows. FC1 owns all the stock of FC2, a Country Y entity that is a controlled foreign corporation and uses the U.S. dollar as its functional currency. FC2 uses the calendar year as its taxable year. As of January 1, 2027, FC1 does not have any accumulated earnings and profits and FC2's accumulated earnings and profits are entirely comprised of $100x of post-06/28/25 section 951A PTEP within the annual PTEP account in the section 951A category for its 2026 taxable year. On January 1, 2027, FC2 distributes $100x to FC1 (distribution 1), which is treated as a distribution of property for both Country Y law and Federal income tax purposes. Country Y imposes a withholding tax (as defined in section 901(k)(1)(B)) of $20x with respect to distribution 1. FC1 subsequently distributes $80x to USP (distribution 2), which is a section 959(a) distribution. Country X does not impose any withholding tax with respect to distribution 2. Neither FC1 nor FC2 has items of income, gain, deduction, or loss for its 2027 taxable year. For its 2027 taxable year, USP claims the foreign tax credit under section 901.

(ii) *Analysis*--(A) *Distribution 1*. Under section 959(c) and § 1.959-3(b), distribution 1 constitutes a distribution of $100x of FC2's previously taxed earnings and profits. Under paragraph (c)(3) of this section, FC1's post-06/28/25 section 951A PTEP within the annual PTEP account in the section 951A category for its 2026 taxable year is increased by $100x but reduced by the $20x of Country Y withholding tax that is allocated and apportioned to the post-06/28/25 section 951A PTEP under § 1.960-1(d)(3)(ii). FC1's PTEP group taxes with respect to its post-06/28/25 section 951A PTEP within the annual PTEP account in the section 951A category for its 2026 taxable year are increased by $20x under paragraph (d) of this section.

(B) *Distribution 2*. Under section 959(c) and § 1.959-3(b), distribution 2 constitutes a distribution of $80x of FC1's previously taxed earnings and profits. Under paragraph (b)(4) of this section, USP's proportionate share of FC1's PTEP group taxes is $20x. Under section 960(d)(4) and paragraph (b)(6)(i)(B) of this section, $2x (that is, 10 percent) of the $20x of foreign tax credits otherwise allowable to USP under section 901 with respect to FC1's $20x of PTEP group taxes deemed paid by USP under section 960(b)(1) is disallowed.

Par. 8. Section 1.960-7 is amended by:

1. In paragraph (a), removing the language "paragraph (b)" and adding "paragraphs (b) and (c)" in its place; and

2. Adding paragraph (c).

The addition reads as follows:

§ 1.960-7 Applicability dates.

* * * * *

(c) Section 1.960-3(b)(6) applies to foreign income taxes paid or accrued (or deemed paid under section 960(b)(1)) with respect to an amount excluded from gross income under section 959(a) by reason of an inclusion in gross income under section 951A(a), to the extent the inclusion occurs in a taxable year of a United States shareholder ending after June 28, 2025. Section 1.960-3(c)(2) applies to taxable years of foreign corporations ending with or within taxable years of United States shareholders ending after June 28, 2025. For taxable years of foreign corporations ending on or after December 4, 2018, and beginning before the taxable year described in the preceding sentence, *see* § 1.960-3(c)(2) as contained in 26 CFR part 1 revised as of April 1, 2026.

Par. 9. Section 1.987-11 is amended by revising paragraph (c)(3)(ii) to read as follows:

§ 1.987-11 Suspended section 987 loss relating to certain elections; loss-to-the-extent-of-gain rule.

* * * * *

(c) * * *

(3) * * *

(ii) *Owner is a CFC*. For purposes of applying paragraph (c)(2) of this section with respect to an owner that is a CFC, suspended section 987 loss and gross income of a member of the owner's controlled group is determined by reference to the member's suspended section 987 loss and gross income for its taxable year ending with or within the owner's required year described in section 898(c)(1).

* * * * *

Frank J. Bisignano,

Chief Executive Officer.

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