JULIA SKUBIS WEBER is a Partner in the Chicago office of Baker & McKenzie, LLP.

STEWART R. LIPELES is a Partner in the Palo Alto office of Baker & McKenzie, LLP.

ETHAN S. KROLL is an Associate in the Los Angeles office of Baker & McKenzie, LLP.

International Tax Watch

The Surprisingly Dubious Fate of Code Sec. 965 PTI

By Julia Skubis Weber, Stewart R. Lipeles, and Ethan S. Kroll

The Ways and Means Committee's "Unified Framework for Fixing Our Broken Tax Code" introduced the broad strokes of tax reform with a four-pronged mandate from President Trump: to simplify the Code, cut taxes for American workers, level the playing field of global tax competition, and, finally, to "bring back trillions of dollars that are currently kept offshore to reinvest in the American economy."[1]

The goal could not have been clearer. Congress intended for the new tax rules to incentivize and enable U.S. multinationals to repatriate foreign earnings. Consistent with this intent, the Tax Cuts and Jobs Act ("TCJA") included provisions that exempt future foreign dividends from U.S. taxation, and subject past foreign earnings to a transition tax (at reduced rates) under new Code Sec. 965.

The transition tax has presented a number of areas of uncertainty, some of which IRS and Treasury have begun to address through notices of impending regulations.[2] In this column, we focus on a particular issue of pressing concern, now that tax and treasury groups at U.S. companies are eagerly eyeing a vast pot of earnings treated as previously taxed income ("PTI") by virtue of Code Sec. 965. As practitioners hammer out plans to distribute cash from foreign groups, they are confronted by an unexpected question: is all of this PTI accompanied by sufficient basis to make its distribution truly tax-free? As we discuss below, the statutory language is unclear, but there is compelling support for providing basis for distributions of all Code Sec. 965-related PTI. Treasury should issue guidance confirming this result, so that taxpayers can repatriate these earnings without fear of taxation.

The Code Sec. 965 Transition Tax and Two Kinds of PTI

First, we describe some of the mechanics of the Code Sec. 965 transition tax that give rise to the uncertain status of deemed-repatriated PTI. Code Sec. 965(a) achieves deemed repatriation of untaxed foreign earnings by increasing a foreign subsidiary's Subpart F income (thereby resulting in an inclusion in a U.S. shareholder's income) to the extent of the subsidiary's "accumulated post-1986 deferred foreign income." In the event that one or more foreign subsidiaries have E & P deficits, the E & P deficits are allocated to and offset the positive E & P balances of affiliated foreign subsidiaries. Accordingly, the E & P deficits reduce the aggregate amount of accumulated post-1986 deferred foreign income.[3]

A U.S. shareholder of a deferred foreign income corporation (a "DFIC") must include in its income an amount equal to the DFIC's accumulated post-1986 deferred foreign income measured as of either November 2, 2017, or December 31, 2017 (whichever is greater).[4] The inclusion itself occurs with respect to the "last taxable year of a deferred foreign income corporation which begins before January 1, 2018."[5] For purposes of this provision, a DFIC is defined as any "specified foreign corporation" (or "SFC") of a U.S. shareholder which has accumulated post-1986 deferred foreign income (as of the applicable measurement date) greater than zero.[6] An SFC is any CFC or any foreign corporation with respect to which one or more domestic corporations is a U.S. shareholder.[7] "Accumulated post-1986 deferred foreign income" means "post-1986 earnings and profits," except to the extent such earnings are attributable to either ECI or PTI.[8] The inclusion is subject to a participation exemption under which the U.S. shareholder pays a reduced effective rate of 15.5 or eight percent, depending on the "aggregate foreign cash position" of such U.S. shareholder,[9] and is entitled to deemed-paid credits under Code Sec. 960, but with a haircut to mirror the reduced tax rates applied pursuant to the participation exemption.[10]

Thus, the increase to Subpart F income under Code Sec. 965(a) produces an inclusion at the U.S. shareholder level that results in PTI ("Included PTI"), pursuant to the usual mechanics of Code Sec. 959, with respect to each DFIC that has accumulated post-1986 deferred foreign income. Similarly, Code Sec. 965(b)(4)(A) provides that PTI arises to the extent of the amount by which allocated deficits shielded some or all of the DFIC's accumulated post-1986 deferred foreign income from inclusion ("Shielded PTI"). In this way, most U.S. multinational groups will have large amounts of PTI in their systems as of the relevant inclusion date under Code Sec. 965, comprising some combination of these two types of PTI. The PTI profile of a particular U.S. shareholder will depend on whether the PTI relates to E & P that were actually included under Code Sec. 951(a) by reason of Code Sec. 965(a) (Included PTI), or whether it arose due to the application of E & P deficits that reduced (or eliminated) the net Code Sec. 965 toll charge (Shielded PTI).

PTI and the Prevention of Double Taxation

As mentioned above, the immediate question that tax departments are receiving from their treasury groups is how soon the cash can be brought home. Historically, the matter of distributing PTI has been fairly straight forward, and, for the most part, the TCJA has not altered these mechanics. Upon an income inclusion under Code Sec. 951(a), the U.S. shareholder increases its basis in the stock of the CFC whose income gave rise to the inclusion and the PTI.[11] The ordering rules dictate that PTI is distributed first, before any untaxed E & P.[12] A PTI distribution is not a "dividend" to the receiving U.S. shareholder,[13] and the PTI distributed is not again included in the gross income of such U.S. shareholder,[14] but it does reduce stock basis.[15] If the amount of PTI distributed exceeds the stock basis, the excess is treated as gain from the sale or exchange of property.[16] Foreign currency gain or loss must be determined from the time of the inclusion to the time of the distribution.[17]

By orchestrating these mechanics, Code Secs. 959 and 961 work together to prevent the double taxation of PTI. Under Code Sec. 959, the PTI is protected from being again included in the U.S. shareholder's income. The basis increase Code Sec. 961 provides prevents double taxation of the earnings that gave rise to the CFC's inclusion, even if those earnings are not distributed. The preamble to 2006 regulations proposed under Code Sec. 961 articulates how Code Secs. 959 and 961, *in tandem*, fulfill this purpose of preventing double taxation:

> Section 959 was enacted so that PTI is excluded from gross income and, thus, not taxed again when distributed by the foreign corporation … Accordingly, as a result of its section 951(a)(1) inclusion, a United States shareholder is made whole by receiving, without further U.S. tax, PTI attributable to its stock in a foreign corporation before it receives any taxable distributions from the foreign corporation. Section 961, which adjusts basis in the stock in a foreign corporation for PTI attributable to such stock, also ensures that PTI is not taxed twice if the stock in the foreign corporation is sold before the PTI is distributed.[18]

A sale of the relevant CFC's stock would be for consideration that includes the value of the undistributed (but already taxed) earnings. Absent an increase to stock basis, the selling U.S. shareholder would effectively be taxed twice on the same income.[19] When PTI is distributed to the U.S. shareholder prior to the U.S. shareholder's sale of the CFC stock, the value of the distributing CFC is decreased, and the issue of double taxation is no longer relevant, and the distribution reduces basis accordingly. If the basis relating to PTI has somehow already been benefited, and the PTI distributed exceeds stock basis, this gain is effectively recaptured under Code Sec. 961(b)(2) to the extent of the excess, notwithstanding the exclusion of the amount distributed, itself, from income under Code Sec. 959(a).

Plenty of PTI—But Can It Come Home?

The PTI created as the result of the Code Sec. 965 transition tax seems, initially, to be indistinguishable from the PTI that arose from ordinary Subpart F inclusions pre-2018. This is certainly true with respect to Included PTI, as the actual income inclusion under Code Sec. 965(a) is, by its terms, an ordinary Subpart F inclusion. Thus, the creation of Included PTI should trigger a corresponding increase to basis per Code Sec. 961(a). It would seem to follow, then, that the U.S. shareholder's stock basis with respect to a DFIC would likewise be increased for Shielded PTI. But a peculiarity in the wording of the provision on Shielded PTI has raised doubts as to whether this is the case. Code Sec. 965(b)(4)(A) provides that: "*For purposes of applying section 959* … an amount equal to such shareholder's reduction under [section 965(b)(1)] which is allocated to such deferred foreign income corporation under this subsection shall be treated as an amount which was included in the gross income of such United States shareholder under section 951(a)."[20]

Rather than expressly providing that this deemed Code Sec. 951(a) inclusion treatment is for the purposes of Code Secs. 959 *and* 961, the statute only refers to Code Sec. 959. Given the above-described purpose of Code Secs. 959 and 961 working *in tandem* to ensure the non-taxation of PTI, it would seem logical that Subpart F inclusion treatment for purposes of Code Sec. 959 would automatically give rise to a Code Sec. 961 basis adjustment. But the purpose of Code Secs. 959 and 961, arguably, is not to prevent taxation of PTI, *per se*—rather, it is to prevent the subsequent taxation of income that has already been taxed once. This is the case for Included PTI, but it is not technically true for Shielded PTI. As mentioned, Code Sec. 959(a) provides that E & P of a foreign corporation attributable to amounts that have already been included under Code Sec. 951(a) "shall not … be *again* included" in the gross income of the U.S. shareholder that already included the income.[21] Thus, when Code Sec. 965(b)(4)(A) provides that Shielded PTI is PTI for purposes Code Sec. 959, is it effectively imputing that character of having already been included, so that Shielded PTI is prevented from being included in income "again"?

Additionally, Code Sec. 961(a) states that the basis "shall be increased by the amount required to be included in [the United States shareholder's] gross income under section 951(a) with respect to such stock or with respect to such property, as the case may be, but only to the extent to which such amount was included in the gross income of such United States shareholder." Had Code Sec. 965(b)(4)(A) stated that the Code Sec. 951(a) inclusion treatment were effective for Code Secs. 959 and 961, it would have been clear that such deemed inclusion would trigger the basis increase under Code Sec. 961(a). Absent a reference to Code Sec. 961 in Code Sec. 965(b)(4)(A) (and considering the absence of cross-references to each other in Code Secs. 959(a) and 961(a)), there is a potential reading that the Shielded PTI could be treated as PTI only for purposes of ultimate exclusion of the PTI itself upon distribution, as provided under Code Sec. 959. In other words, nothing in Code Sec. 959 tells us that the distribution of an amount that is, itself, excluded cannot trigger gain with respect to some other asset (*i.e.*, stock). In fact, Code Sec. 961(b) tells us specifically that a distribution of an amount excluded under Code Sec. 959(a) constitutes gain if such excluded amount exceeds the available basis in the stock.

On the other hand, the same interpretive question with respect to Code Sec. 965(b)(4)(A)'s designation of PTI status "for purposes of applying section 959" arises when interpreting Code Sec. 961(a), which requires an increase in basis "to the extent to which such amount was included in the gross income of such United States shareholder." If PTI treatment "for purposes of applying section 959" means that we treat Shielded PTI as income that has already been included once in the U.S. shareholder's income, then this alone could be sufficient to trigger the basis increase under Code Sec. 961(a), lack of explicit cross-references notwithstanding. This reading makes sense. After all, it would defeat the purpose of non-taxation if PTI "excluded" from the U.S. shareholder's income ultimately triggers taxable gain when distributed due to insufficient basis.

Perhaps we can look elsewhere in Code Sec. 965 and to the legislative history for clues. Code Sec. 965(b)(4)(B) provides for an "increase" to the U.S. shareholder's *pro rata* share of E & P of the E & P deficit foreign corporation, to the extent that the corporation's deficit has reduced the Code Sec. 965(a) inclusion. In addition, Code Sec. 965(o)(1) provides the Secretary with the authority to issue "regulations or other guidance to provide appropriate basis adjustments." The Conference Report devotes a paragraph to this authorization and hints that the omission of Code Sec. 961 from Code Sec. 965(b)(4)(A) may have been intentional, leaving the matter of basis adjustments to Treasury. The report provides:

> The conferees recognize that basis adjustments (increases or decreases) may be necessary with respect to both the stock of the deferred foreign income corporation and the E&P deficit foreign corporation and authorizes the Secretary to provide for such basis adjustments or other adjustments, as may be appropriate. *For example, with respect to the stock of the deferred foreign income corporation, the Secretary may determine that a basis increase is appropriate in the taxable year of the section 951A [sic] inclusion or, alternatively, the Secretary may modify the application of section 961(b)(1) with respect to such stock.* Moreover, with respect to the stock of the E&P deficit corporation, the Secretary may require *a reduction in basis* for the taxable year in which the U.S. shareholder's pro rata share of the earnings of the E&P deficit corporation are increased.[22]

The first emphasized passage appears to refer to the Code Sec. 961(a) basis increase that arises from Included PTI and, specifically, the timing with respect to which such increase occurs (" … in the taxable year of the section [951(a)] inclusion … "). The final sentence certainly addresses the allocation of deficits under Code Sec. 965(b), although here the Report is referring to an adjustment to the basis of the stock of the E & P deficit corporation itself, rather than any adjustment to the stock of the DFIC to which such deficit was allocated and which received Shielded PTI as a result.

The guidance issued since the enactment of the TCJA suggests that, with respect to the reference to whether a basis increase is appropriate in the taxable year of the Code Sec. 951(a) inclusion, IRS and Treasury interpreted this mandate in the Conference Report to mean that they needed to provide rules regarding the timing of the Code Sec. 961(a) basis increase with respect to Included PTI, particularly when the PTI is distributed before the end of the taxable year in which the Code Sec. 965(a) inclusion occurred. Both Notice 2018-7 and Notice 2018-13 address PTI distributions, but the guidance alluded to in these Notices is limited, in both instances, to distributions (1) occurring during the inclusion year (*i.e.*, the last taxable year of the relevant SFC beginning before January 1, 2018), and (2) attributable to PTI described in Code Sec. 959(c)(2) *by reason of section 965(a)* (*i.e.*, Included PTI, not Shielded PTI). The "fix" the Notices provide consists of a new "gain-reduction rule," so that an inclusion-year distribution of Included PTI that triggers gain under Code Sec. 961(b)(2) will be granted a reduction of that gain to the extent of the Code Sec. 965(a) inclusion with respect to the distributing SFC. Thus, any positive stock basis adjustment under Code Sec. 961(a) that would result from an actual inclusion under Code Sec. 965(a) would not be effective for purposes of mid-year distributions during the inclusion year.[23] The Notices do not, however, address stock basis adjustments when PTI is created as the result of deficit allocations under Code Sec. 965(b)(4)(A), in spite of the Conference Report's insinuations as to what the Secretary "may" require in this regard.

At least one commenting body has requested further guidance from IRS and Treasury with respect to precisely how Shielded PTI should be addressed. The New York State Bar Association ("NYSBA") Tax Section issued a report exploring the persisting ambiguities created in Code Sec. 965 and recommending, among other things, that the Secretary take further steps to give taxpayers certainty regarding distributions of PTI post-deemed repatriation.[24] The Tax Section describes the problem posed by the potential lack of an accompanying basis increase with the creation of Shielded PTI, noting that this "may have the effect of creating PTI in DFICs that is not matched by corresponding basis adjustments."

Two examples illustrate the potential bad result of such a mismatch. In the first example, a CFC with zero stock basis makes a mid-inclusion year dividend distribution that the U.S. shareholder later discovers (upon the enactment of the TCJA) was actually a distribution of PTI. Because of the allocation of deficits for purposes of the Code Sec. 965 inclusion, the CFC is treated as having distributed $100 of PTI ($50 of Included PTI and $50 of Shielded PTI) but, because the distribution is made before any Code Sec. 961(a) basis materializes, there is no available basis. The gain reduction rule as described in the Notices kicks in, but only reduces the U.S. shareholder's gain by the $50 that U.S. shareholder actually included in income under Code Sec. 965(a). The remaining $50 is taxable gain.

In the second example, the CFC does not make a distribution during the inclusion year. As of January 1, 2018, the CFC has $50 of Included PTI and $50 of Shielded PTI. By this point, the U.S. shareholder's Code Sec. 961(a) basis increase has crystallized, but unfortunately, due to the literal language of Code Sec. 965(b)(4)(A), this increase produces only $50 of basis.

The NYSBA Tax Section acknowledges that creating unmatched PTI "will impede the repatriation of deferred E&P as well as future earnings in many cases," and recommends parity between Included and Shielded PTI. But it then suggests that "adopting [matching basis adjustments] could potentially be viewed as overly generous." The report goes on to describe a possible approach where deficit corporations and DFICs are treated as actually combining into a single corporation. This would, presumably, provide the DFIC with access to the deficit corporation's basis in much the same way as it obtained access to the allocated deficit. Another way to accomplish this result would be to simply make the stock basis of an E & P deficit foreign corporation available for a Shielded PTI distribution:

> One alternative for addressing these issues that we recommend Treasury and the Service consider would be providing rules that permit taxpayers to appropriately utilize basis in the stock of E&P deficit foreign corporations in order to offset section 961(b)(2) gain resulting from distributions of section 965 PTI. For example, the gain-reduction rule could be expanded so that it also operates to reduce section 961(b)(2) gain by the basis in the stock of an E&P deficit foreign corporation to the extent a deficit of such E&P deficit foreign corporation was allocated to reduce the taxpayer's section 951(a)(1) inclusion in respect of the relevant DFIC.

The NYSBA Tax Section's suggestion and the hints in the Conference Report certainly point in the right direction by providing a basis increase to the DFIC and a basis reduction to the E & P deficit corporation. The consumption of a deficit entails a cost to the taxpayer. The sacrifice of an attribute that could otherwise have reduced U.S. tax liability on distributions (at least to the extent of basis, and before Code Sec. 245A provided an exemption for distributions of untaxed foreign E & P) is, effectively, the mirror image of including the E & P that consumes this attribute in the U.S. shareholder's income. Therefore, as this E & P actually "eats up" the attribute, and Congress designates it as PTI, regulations should correctly reflect that the deemed transactions under Code Sec. 965 that consume losses are economically equivalent to the inclusion of the E & P in the gross income of the U.S. shareholder.[25] Thus, a basis increase should accompany the creation of PTI upon either the inclusion of income under Code Sec. 951(a) *or* the consumption of a deficit, and a basis decrease should correspond to the distribution of PTI.

While this approach could alleviate some of the pain caused by the PTI-basis mismatch, there is no assurance, of course, that an E & P deficit foreign corporation would have sufficient stock basis to offset all Shielded PTI. But to say that providing basis to the full extent of Shielded PTI is "overly generous" implies that Congress meant to insert PTI status without accompanying basis as a roundabout way of ensuring that taxpayers have no way to distribute E & P to the extent of allocated deficits, absent preexisting basis. This interpretation is unpersuasive, as Congress could have achieved this less-generous result simply by providing that E & P deficits eliminate positive untaxed E & P. In this scenario, any cash associated with the eliminated E & P would require existing stock basis for tax-free distribution. If Congress intended this result, why did it bother categorizing E & P offset by deficits as "PTI"? Given the ample evidence that the transition tax was meant to wipe the E & P slate clean and remove the roadblocks to repatriating foreign cash, it seems far more likely that Congress intended for Shielded PTI and Included PTI to enjoy the same tax-free treatment on distribution.

When and How to Bring Back Those Trillions?

The ambiguities described above, alone, may be enough to create significant uncertainty with respect to repatriating foreign E & P that was protected from inclusion *via* deficits, so much so that U.S. multinational groups may be stuck waiting until guidance is published (hopefully before the end of 2018) to know what, exactly, happens to Shielded PTI, and whether SFCs can distribute it without trigging tax. If encouraging the immediate distribution of foreign E & P were Congress's goal, it would seem that yanking a tax-free repatriation path for deemed-repatriated earnings accomplishes the opposite. It is a twisted policy posture to permit taxpayers to access real economic losses when determining the net amount subject to tax under Code Sec. 965, and then to slap distributions of those amounts with a 21-percent tax on the resulting gain. It should be noted as well that a distribution of Shielded PTI from a lower-tier CFC to its CFC parent could also trigger subpart F income if there is insufficient basis, taxable at 21 percent. This outcome seems well outside the intent of Code Sec. 965, and an appropriate regulatory response would be to provide rules clarifying that Shielded PTI is accorded the same treatment under Code Sec. 961(a) as Included PTI.

In the meantime, taxpayers may consider alternative approaches to bring back the cash associated with Shielded PTI. For example, while the treatment of PTI upon inbound liquidations is somewhat uncertain and Treasury reserved on this issue in the Code Sec. 367 regulations (other than with respect to currency gain or loss), one option could be simply liquidating a cash-rich top-tier CFC, possibly eliminating the need for Code Sec. 961 basis at all.[26] Related-corporation stock sales under Code Sec. 304 have historically provided a reliable way to shift CFC attributes, including stock basis. Taxpayers should be watchful of regulations in this area, but there could be planning opportunities to use Code Sec. 304 in the post-TCJA environment for the purpose of relocating basis to where it can serve as a bridge for Shielded PTI. Additionally, as Code Sec. 956 has mysteriously remained in the Code, it also remains in the playbook, and could prove useful in accessing the cash that might otherwise be trapped with Shielded PTI. Loans have their own associated costs and limitations. Among other things, Code Sec. 163(j) may apply to the borrower, interest payments could shift income from the U.S. to higher-tax jurisdictions, and the specter of the base erosion anti-avoidance tax looms whenever deductible payments are made by a U.S. corporation.

Other, related, issues spring up after the initial question of the presence or absence of Code Sec. 961(a) basis. For example, is there any kind of ordering or priority with respect to what kind of PTI gets distributed first? The most sensible answer is that, if Shielded PTI is still just "PTI" for purposes of Code Sec. 959, whether distributed PTI is Included or Shielded, it is treated *pari passu* and distributions simply reduce stock basis as they occur chronologically. The NYSBA Tax Section noted in its Report that the gain-reduction rule as described in Notice 2018-13 only applies to distributions "that are attributable to" a U.S. shareholder's PTI that arose under Code Sec. 965, and that therefore it is necessary for taxpayers to be able to tell the difference between Code Sec. 965 PTI and "regular" PTI in distributions.[27] The Tax Section suggests that Code Sec. 965 PTI should be given priority over other PTI, to "achieve the section 965 policy objective of encouraging U.S. multinationals to repatriate untaxed foreign earnings."

Additionally, while Code Sec. 961(a) unambiguously requires a basis increase when the U.S. shareholder owns the stock of the CFC whose income gave rise to the Code Sec. 951(a) inclusion, when the CFC is at a lower tier, any basis adjustments that "tier up" as the PTI is distributed up the chain must rely on the unfulfilled regulatory mandate prescribed under Code Sec. 961(c). In general, the specific grant of regulatory authority, combined with the proposed regulations under Code Sec. 961(c), should provide comfort that these basis adjustments are available (especially if the regulations have remained proposed for 12 years). The description in Notice 2018-13 regarding the application of the gain-reduction rule to lower-tier CFC distributions strongly suggests that IRS and Treasury view Code Sec. 961(c) to be self-executing. But the absence of final rules for how to apply the basis tiering does add another layer of attenuation, given the already uncertain statutory link between Code Secs. 965(b)(4)(A) and 961(a).

Conclusion

This year, tax practitioners seem to be thinking about PTI more than ever before, and with U.S. multinationals impatiently waiting on their foreign cash, the need for guidance on the mechanics for PTI distributions becomes more pressing with every day. Now, IRS and Treasury must decipher whether the silence in Code Sec. 965(b)(4)(A) regarding Code Sec. 961 reflects Congress's intent to deny tax-free treatment to the repatriation of foreign earnings that were already offset by foreign losses. If the regulations do not provide all PTI with accompanying basis, taxpayers may be in for a cruel shock—the earnings that could have been deemed repatriated at the reduced tax rates of 15.5 and eight percent may, because they were offset by deficit allocations, be *actually* repatriated at a 21-percent tax rate. With no deemed-paid foreign tax credits to accompany these earnings, the combined U.S. and foreign effective tax rate on income that becomes Shielded PTI could be well above 21 percent.

ENDNOTES

1 "Unified Framework for Fixing Our Broken Tax Code," available online at *https://waysandmeansforms.house.gov/uploadedfiles/tax_framework.pdf* (Sept. 27, 2017).

2 Some examples of these areas of uncertainty include the treatment of foreign taxes for the inclusion year of fiscal year taxpayers and the treatment of foreign taxes associated with E & P deficit foreign corporations. The IRS and Treasury have begun to outline the regulations taxpayers can expect *via* notices. *See* Notice 2018-7, IRB 2018-4, 317 (Dec. 29, 2017); Notice 2018-13, IRB 2018-6, 341 (Jan. 19, 2018); Notice 2018-26, IRB 2018-16, 480 (Apr. 2, 2018). As of the writing of this column, Treasury officials have stated that the plan is to issue 25 to 30 pieces of guidance by August 15, 2018. *Kautter: Not Every Proposed Regulation Will Get a Notice First*, Tax Analysts Doc. 2018-20415.

3 Code Sec. 965(b).

4 Code Sec. 965(a).

5 *Id.*

6 Code Sec. 965(d)(1). Notice 2018-13 describes regulations that will clarify the determination of DFIC status.

7 Code Sec. 965(e).

8 Code Sec. 965(d)(2).

9 Code Sec. 965(c).

10 Code Sec. 965(g).

11 Code Sec. 961(a).

12 Code Sec. 959(c).

13 Code Sec. 959(d).

14 Code Sec. 959(a).

15 Code Sec. 961(b)(1).

16 Code Sec. 961(b)(2).

17 Code Sec. 986(c).

18 Notice of Proposed Rulemaking, Fed. Reg. Vol. 71, No. 167A, at 51155 (Aug. 29, 2006).

19 *See* Committee Report ¶9611.97 Controlled foreign corporations. (Taxpayer Relief Act of 1997, P.L. 105-34, Aug. 5, 1997) (adding Code Sec. 961(c) to provide regulatory authority for preventing the same issue of double taxation upon a CFC's sale of stock in a lower-tier CFC).

20 Emphasis added.

21 Emphasis added.

22 Joint Explanatory Statement of the Committee of Conference at 492 (emphasis added).

23 Reg. §1.961-1(a)(1) ("[T]he basis of a United States shareholder's stock in a controlled foreign corporation … shall be increased under section 961(a), as of the last day in the taxable year of such corporation on which it is a controlled foreign corporation, by the amount required to be included with respect to such stock … in such shareholder's gross income under section 951(a) for his taxable year in which or with which such taxable year of such corporation ends.").

24 *NYSBA Tax Section Submits Report on New CFC Provision*, 2018 TNT 26-15 (Feb. 6, 2018).

25 This would be consistent with other regimes under the Code that provide basis increases for income inclusions and reductions for distributions. Consider, for example, the investment adjustment rules in the consolidated return regulations under Code Sec. 1502, and the provisions in Subchapters

K and S governing basis increase on the flow-through of income and decrease for distributions and the flow-through of losses. *See* Reg. §1.1502-32; Code Secs. 705 and 1367.

[26] *See* Reg. §1.367(b)-3(f)(2); T.D. 9273, IRB 2006-37, 394 (Aug. 8, 2006) ("After studying the interaction of section 367(b) and the PTI rules, the Treasury Department and the IRS determined that more guidance under section 959 would be useful before issuing regulations to address PTI issues that arise under section 367(b). Accordingly, the Treasury Department and the IRS have opened a separate regulations project under section 959 and expect to issue regulations that address PTI issues under section 959 in the future. Because this project is still ongoing, these final regulations reserve on section 367(b) issues related to PTI. Guidance in this area will come in a separate project.").

[27] *See* NYSBA Report, *supra* note 24.