

## IRS Issues Guidance Related to the Filing Obligations Resulting from the New CFC Downward Attribution Rules

As discussed in our previous Client Bulletin [U.S. Tax Reform: Key Considerations for Non-U.S. Families with Connections to the United States](#), the Tax Cuts and Jobs Act (the "Act") changed the stock attribution rules that are used to determine whether a non-U.S. corporation is a "controlled foreign corporation" (or "CFC") and whether a U.S. person is a "United States shareholder" of the CFC for U.S. federal income tax purposes. Among the changes made by the Act, was the elimination of a previous limitation on so-called "downward attribution". Prior to the Act, any shares in a non-U.S. corporation that were owned by a non-U.S. person were not attributed down to any U.S. partnership, corporation, trust or estate in which such non-U.S. person held an interest. The Act has eliminated this limitation on "downward attribution." As a result, a U.S. partnership, corporation, trust or estate will be deemed to own any stock in a non-U.S. corporation that is owned by a non-U.S. partner, shareholder or beneficiary, respectively.

Classification as a CFC can (and often does) expose the U.S. shareholder(s) of the CFC to adverse U.S. tax consequences, including additional U.S. tax and reporting obligations. For example, U.S. shareholders of a CFC are generally required to annually file a Form 5471 (Information Return of U.S. Persons With Respect To Certain Foreign Corporations). The Instructions for Form 5471 clarify that a U.S. shareholder who owns stock in a non-U.S. corporation that is a CFC for an uninterrupted period of 30 days or more during any tax year of the non-U.S. corporation, and who owned that

stock on the last day of that year, is a so-called "Category 5 Filer" that must file Form 5471.

The Internal Revenue Service ("IRS") has issued guidance in connection with the expanded downward attribution rules. Among other things, Notice 2018-13 states that the IRS intends to amend the Instructions for Form 5471 to provide an exception from Category 5 filing for a U.S. person that is a U.S. shareholder with respect to a CFC if (i) no U.S. shareholder (including such U.S. person) owns stock in such CFC directly or indirectly (as opposed to constructively, e.g., via the downward attribution rules), and (ii) the non-U.S. corporation is a CFC solely because such U.S. person is considered to own the stock of the CFC owned by a non-U.S. person under the downward attribution rules set forth in Section 318(a)(3) of the Internal Revenue Code. Until the IRS so amends the Instructions for Form 5471, the Notice provides that taxpayers may rely on the exception described in the Notice.

The full text of Notice 2018-13 can be found at <https://www.irs.gov/pub/irs-drop/n-18-13.pdf>.

All client structures should be carefully reviewed in light of the new downward attribution rules to determine whether any non-U.S. corporations should now be properly classified as CFCs, and to ensure compliance with any applicable reporting and/or tax obligations associated with such classifications. The new guidance is helpful in that it may alleviate some onerous filing requirements that could have arisen for certain structures because of the new downward attribution rules.

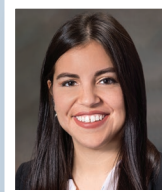
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