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IRS PROPOSED REGULATIONS UNDER INTERNAL REVENUE CODE SECTION 965

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PROPOSED REGULATIONS TO SECTION 965

On August 1, 2018, the Internal Revenue Service (IRS) took the first step in providing significant and detailed guidance on provisions of the Tax Cuts and Jobs Act[1] (TCJA) with the issuance of proposed regulations (the Proposed Regulations) under Section 965 of the Internal Revenue Code of 1986, as amended, or the so-called "Repatriation Tax."[2]

In broad strokes, Section 965 levies a current tax on the previously untaxed post-1986 earnings and profits (E&P) (the greater of the amount calculated on November 2, 2017, or December 31, 2017) of a "specified foreign corporation" (SFC) to 10% US shareholders of the SFC by treating such amounts as additional subpart F income. An SFC is any foreign corporation (that is not a passive foreign investment company) with at least one US corporation that is a 10% US shareholder. In general, foreign earnings not in excess of the foreign cash and cash equivalents (the so-called "cash position") are subject to a 15.5% tax rate and all other untaxed foreign earnings are subject to an 8% tax rate.[3] Taxpayers may elect to pay the Repatriation Tax in eight annual installments on an interest-free basis.[4]

Prior to the issuance of the Proposed Regulations, the IRS had published preliminary guidance on Section 965 through the issuance of several notices and other informal directives.[5] The Proposed Regulations follow and reflect the preliminary guidance in most respects, but also introduce a handful of new and noteworthy provisions.

Nuances of Calculating the Aggregate Foreign Cash Position

The Proposed Regulations largely adopt the prior guidance on the "aggregate foreign cash position." There are, however, several "clarifications" and rejected comments worth noting, as they reflect an expansive view and interpretation of this term.

- The term "accounts payable" remains limited to payables relating to the purchase of goods or receipt of services;[6] the IRS rejected requests to expand the definition to include payables (i) relating to arrangements for the licensing of intellectual property, (ii) owing to employees in the ordinary course of business, and (iii) involving Section 1221(a)(2) property (i.e., depreciable property used in a trade or business).[7]
- A demand feature continues to result in the obligation's treatment as a per se "short-term obligation" that must be included in the foreign cash position;[8] a comment requesting that the presumption be rebuttable based on facts and circumstances was rejected.[9]
- Also rejected were requests to exclude from the definition of a cash position certain assets that might be illiquid, specifically (i) publicly traded stock in a corporation that is actively

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[1] Pub. L. 115-97 § 14103 (Dec. 22, 2017).

[2] 83 Fed. Reg. 39514 (Aug. 9, 2018).

[3] I.R.C. § 965(c).

[4] *See* I.R.C. § 965(h).

[5] *See, e.g.*, (i) Notice 2018-7, 2018-4, I.R.B. 317; (ii) Notice 2018-13, 2018-6, I.R.B. 341; (iii) Publication 5292 (How to Calculate Section 965 Amounts and Elections Available to Taxpayers); (iv) Rev. Proc. 2018-17, 2018-9, I.R.B. 384 (Treatment of deferred foreign income upon transition to participation exemption system of taxation – change in accounting method – automatic approval – procedures); (v) Notice 2018-26, 2018-16, I.R.B. 480; and (vi) IRS FAQ, Questions and Answers about Reporting Related to Section 965 on 2017 Tax Returns (last visited Aug. 7, 2018).

[6] *See* Prop. Treas. Reg. § 1.965-1(f)(5); Notice 2018-13, § 3.04(a); Notice 2018-26, § 3.06.

[7] 83 Fed. Reg. 39523 (Aug. 9, 2018).

[8] *See* Prop. Treas. Reg. § 1.965-1(f)(43).

[9] *See* 83 Fed. Reg. at 39523 (Aug. 9, 2018).

traded on an established financial market in which the SFC holds at least 10% of the stock; (ii) blocked/restricted/segregated cash, cash used for foreign acquisitions, cash held in a fiduciary or a trust capacity, cash required by regulation to be held, and pledged cash; (iii) cash expected to be spent within a specified period of time; (iv) Section 956 loans; and (v) commodities representing inventory or supplies.[10]

- The US Department of the Treasury (Treasury) and the IRS also rejected comments to treat notional pooling arrangements as intercompany loans for Section 965 purposes and therefore possibly qualifying for the exclusion[11] of loans between related SFCs, explaining in the preamble that whether the arrangement is treated as a loan between related parties or between an SFC and a third party is based on federal income tax principles.[12]
- Although the Proposed Regulations allow for certain payables and obligations between related SFCs to be disregarded (to avoid double counting), such treatment is available only to the extent of the lower of the US shareholder's percentage ownership in the two corporations.[13]

Taxpayers should not be surprised if final regulations introduce further developments in this area. The preamble notes that Treasury and the IRS "welcome" additional comments with respect to the definition of cash position, signaling that they continue to study this topic. At the same time, however, taxpayers may wish to temper their expectations about any further relaxation of the rules, as the vast majority of the comments submitted (including those above) were rejected based on a strict reading of the statute.

Foreign Tax Credit Considerations

Section 965 Haircut

Section 965(g)(1) disallows a credit or deduction for the "applicable percentage" of taxes "paid or accrued" with respect to any amount for which a Section 965(c) deduction is allowed. In response to comments, the Proposed Regulations clarify that the disallowance applies broadly to foreign taxes (i) directly paid, (ii) deemed paid under Section 960, (iii) allocated under Treasury Regulations § 1.901-2(f)(4) between two partnerships or between a partnership and a disregarded entity, and (iv) allocated as a partnership item.[14] In practice, this means that the disallowance will apply not only to taxes attributable to amounts included in income under Section 965, but also to any future withholding or net income taxes imposed on distributions of previously taxed Section 965 earnings.[15]

The Proposed Regulations also clarify that the applicable percentage,[16] which determines the disallowed (and, indirectly, the allowed) portion of foreign taxes attributable to amounts included in income under Section 965, must be calculated for each Section 958 US shareholder inclusion year (i.e., each year the US shareholder is required to include an amount in income under Section 965 with respect to an SFC).[17] As a result, a US shareholder with multiple inclusion years could have more than one applicable percentage, and, therefore, a greater disallowance in one year than another. For example, multiple applicable percentages may occur where a US person is a domestic pass-through owner with respect to more than one domestic pass-through entity.

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[10] *See* 83 Fed. Reg. 39538 (Aug. 9, 2018).

[11] *See* Prop. Treas. Reg. § 1.965-3(b)(1); Notice 2018-7, §§ 3.01(b) & (c).

[12] *See* 83 Fed. Reg. 39539 (Aug. 9, 2018).

[13] *See* Prop. Treas. Reg. § 1.965-3(b)(1).

[14] *See* 83 Fed. Reg. 39529 (Aug. 9, 2018).

[15] *See* Prop. Treas. Reg. § 1.965-3(c)(1)(ii).

[16] *See* Prop. Treas. Reg. § 1.965-5(d).

[17] *See* Prop. Treas. Reg. § 1.965-1(f)(34); 83 Fed. Reg. 39529 (Aug. 9, 2018).

The US shareholder also will receive a corresponding haircut on its Section 78 gross-up to align the permitted foreign tax credits (those available post–applicable percentage haircut) and the amount of gross-up included as income.

Section 78 Gross-up

The Proposed Regulations adopt the statutory rules under Section 965(g) governing the treatment of foreign tax credits and the Section 78 gross-up attributable to amounts included in income under Section 965. Under the Section 965(g) rules, foreign tax credits are disallowed, or "haircut" to the extent of the "applicable percentage": the sum of (i) the product of 0.771 and the percentage that the non-cash position is of the amounts included in income under Section 965, and (ii) the product of 0.557 and the percentage that the cash position earnings is of the amounts included in income under Section 965.

Because the 0.771 and 0.557 multiplicands are fixed, the foreign tax credits disallowed under Section 965(g) will (necessarily) be the same for calendar year and fiscal year taxpayers, even though the statutory rate of US tax that each is subject to under Section 11 will be different (i.e., 35% calendar year taxpayers versus something less for fiscal year taxpayers). Given that the intent of the deduction rules in Section 965(c) is to tax a taxpayer, whether calendar year or fiscal year, on the Section 965 inclusion at the same reduced effective tax rate, this treatment makes sense. Since all taxpayers are subject to the same effective tax rate, to provide equal treatment, the amount of the foreign tax credits that are allowed should not differ either.

The question then raised is whether the gross-up should be based on the amount of the allowed foreign taxes even though the statute provides otherwise. Under pre-TCJA thinking, one would expect the corresponding Section 78 gross-up amount to equal the amount of any allowed foreign tax credits. And for calendar year taxpayers, that is indeed the case—the Section 78 gross-up amount will align with the foreign tax credit allowable under Section 965(g). For fiscal year taxpayers, however, under the statutory rule as adopted by the Proposed Regulations, the Section 78 gross-up will exceed the allowable foreign tax credit because it is tied to the amount of the Section 965(a) inclusion in excess of the Section 965(c) deduction, which is a function of the amount of the 8% and 15.5% rate equivalent percentages (i.e., the percentage of the Section 965(a) amount that must be allowed as a deduction under Section 965(c) such that the net amount, when multiplied against the statutory rate, produces an effective rate of 8% or 15.5% on the Section 965(a) amount). For reasons discussed below, the rate equivalent percentages will be lower for fiscal year taxpayers (as compared to calendar year taxpayers), which has the dual effect of reducing the allowable Section 965(c) deduction and increasing the net amount of earnings subject to Section 965(a) taxation, the necessary consequence of which is a greater Section 78 gross-up for fiscal year taxpayers than for calendar year taxpayers.

At first glance, this might seem like an inequitable result that arbitrarily subjects fiscal year taxpayers to additional US taxation. In actuality, the disconnect between the allowable foreign tax credits and the Section 78 gross-up has quite the opposite effect. Similar to the denial of the foreign tax credits under Section 961(g), the gross-up *ensures* that a taxpayer, whether calendar year or fiscal year, pays the *same* overall amount of tax under Section 965. The Section 78 gross-up needs to be greater as the fiscal year taxpayer is subject to a lower statutory rate of tax. In other words, subjecting fiscal year taxpayers to a greater Section 78 gross-up effectively "offsets" the impact of the lower statutory rate that applies to such taxpayers, thereby ensuring that calendar year and fiscal year taxpayers are subject to the same amount of tax overall. The simplified example below, comparing a calendar year taxpayer with a fiscal year taxpayer with a taxable year ending June 30, illustrates that applying the foreign tax credit denial and gross-up rules results in the same overall tax.

	Calendar	Fiscal
Chapter 11 statutory tax rate (a)	35%	28%
Section 965(a) inclusion amount (b)	100	100
Cash Position earnings (15.5%) (c)	0	0
Non-cash Position earnings (8%) (d)	100	100
8% effective rate equivalent percentage (e) (e = 1 – (8%/a))	77.1%	71.4%
Non-cash Participation Deduction (f) (f = d * e)	77.1	71.4
Net Section 965 inclusion (g) (g = b – f)	22.9	28.6
Foreign taxes (h)	20	20
Applicable percentage (i) (i = .771 * (b/(b+c)))	77.1%	77.1%
Disallowed Foreign Tax Credit (FTC) (j) (j = h * i)	15.4	15.4
Allowed FTC (k) (k = h – j)	4.6	4.6
Section 78 gross-up (l) (l = h * (g / b))	4.6	5.7
Net Section 965 inclusion (m) (m = g + l)	27.5	34.3
Section 965 tax liability (n) (n = a * m)	9.6	9.6
Section 965 tax liability after FTC (o) (o = n – k)	5	5

Therefore, the Proposed Regulations' treatment of the denial of the foreign tax credits and the Section 78 gross-up, even though not obvious at first blush, seems clearly correct.

SFCs That Are Not CFCs

Foreign tax credits permitted under Section 960(a)(1) of pre-TCJA law[18] are available only with respect to taxes paid by foreign corporations that are members of a "qualified group" as defined in pre-TCJA Section 902(b), which does not include foreign corporations below the third tier that are not controlled foreign corporations (CFCs).[19] Section 965(e)(2) permits certain non-CFC SFCs to be treated as CFCs solely for purposes of applying Section 965(a). The Proposed Regulations, therefore, confirm that an indirect foreign tax credit is only available for foreign taxes paid or accrued by such SFCs provided that the SFC is a third-tier or higher foreign subsidiary.[20] Thus, 10% US corporate shareholders will not be entitled to indirect foreign tax credits on Section 965 inclusions from SFCs that are treated as CFCs for Section 965 purposes below the third tier. The elimination of the prohibition on the downward attribution rules in Section 958(b)(4), however, may make it more likely that SFCs are CFCs.

Section 960(a)(3) Credits on PTI Distributions

The Proposed Regulations provide that no credit is allowed for net income taxes paid on E&P that is reduced by a deficit and becomes previously taxed income (PTI) under Section 965(b) (Section 965(b) PTI), where such taxes were not taken into account under Section 960 by reason of the Section 965 inclusion.[21] This rule is likely to be the subject of numerous comments, as it does not appear to be justified by either Section 960(a)(3) or policy considerations. Note, however, a foreign tax credit is still allowed for withholding taxes paid on the distribution of both Section 965(a) and 965(b) PTI (or net income taxes on distributions of such PTI between tiers of SFCs), subject to the haircut under Section 965(g) as noted above.

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[18] This is the version of Section 960 relevant to computing credits under Section 965(g) since Section 960, as amended by the TCJA, applies only to taxable years of a foreign corporation beginning after December 31, 2017—years that are not relevant to the Section 965(g) credit.

[19] *See* 83 Fed. Reg. 39531 (Aug. 9, 2018).

[20] Prop. Treas. Reg. § 1.965-1(d).

[21] Although the Proposed Regulations only address PTI distributions under Section 960(a)(3) prior to the changes in Section 960, the preamble indicates that Treasury and the IRS anticipate issuing future regulations that provide similar rules in connection with new Section 960(b).

Section 904 Limitation

Generally, the Proposed Regulations do not alter the normal application of the rules under Sections 861 through 865 that apply to allocate and apportion deductions to the separate foreign tax credit limitation categories under Section 904(d). However, the Proposed Regulations provide that the Section 965(c) deduction allowed with respect to a Section 965(a) inclusion does not cause (i) any portion of the Section 965(a) inclusion to be treated as exempt income within the meaning of Section 864(e)(3) or the regulations thereunder, or (ii) the stock of a deferred foreign income corporation (DFIC) with respect to the Section 965(a) inclusion to be treated as an exempt asset. The Proposed Regulations also provide that neither the Section 965(a) PTI nor the Section 965(b) PTI is treated as giving rise to exempt, excluded, or eliminated income. Thus, a Section 965(a) inclusion and a distribution of Section 965(b) PTI can attract a deduction in the calculation of the US shareholder's foreign source taxable income.

The general Section 904 rules are also not altered but Treasury and the IRS request comments on whether there is a need for additional guidance. At a minimum, it would appear that some guidance is needed for those taxpayers making elections under Section 965(n) on how to apply Section 904(f), and in particular Section 904(f)(5)(D).

Narrow Double-Counting Rules

Notice 2018-7 announced that the Proposed Regulations would include guidance to avoid "double counting" of the post-1986 E&P of an SFC when determining the Section 965 inclusion of a US shareholder.[22] The Proposed Regulations are narrower than expected, in that they only address transactions occurring between SFCs, and only if certain specific requirements are satisfied. The rules do not address transactions, distributions, or deductible payments between an SFC and a US shareholder (or partnerships owned by US shareholders),[23] and comments requesting relief for such transactions were rejected.[24]

Moreover, how these narrow rules that disregard certain distributions between SFCs made between Section 965 E&P measuring dates (i.e., between November 2, 2017, and December 31, 2017)[25] interact with the proposed rules regarding the ordering and characterization of various distributions for purposes of Sections 951, 956, 959, and 965 is unclear. If applied literally, the interplay between the two sets of rules would appear to have the potential for double counting that could be harmful in some cases, but perhaps helpful in others. Taxpayers with distributions between SFCs between measuring dates would be well advised to review their treatment of these transactions.

Consistency of 'Appropriate Basis Adjustments' for Section 965(b) PTI

Section 965(b)(4) treats a deficit absorbed by a DFIC as previously taxed subpart F income. The statute and the TCJA Conference Report reflect Congress's intention to allow an upward adjustment to the stock basis of the DFIC equal to the amount of previously taxed earnings, but say very little as to whether the stock basis of the E&P deficit corporation that surrendered the deficit must also be reduced; the preliminary Section 965 guidance was silent in this regard. Proposed Treasury Regulations § 1.965-2(f)(2) now provides an answer: An elective upward basis adjustment to the stock of a DFIC is allowed only if a corresponding downward adjustment is made to the stock of the E&P deficit corporation. Thus, absent an election by the taxpayer, no basis adjustments are allowed for Section 965(b) PTI. A consistency

[22] Notice 2018-7, 2018-4, I.R.B. 317, § 3.02.

[23] *See* Prop. Treas. Reg. § 1.965-4(f).

[24] *See* 83 Fed. Reg. 39529 (Aug. 9, 2018).

[25] *See* Prop. Treas. Reg. § 1.965-4(f).

requirement applies for US shareholders who are related to each other under either Section 267(b) or 707(b).

If the required downward basis adjustment exceeds the basis in the deficit company stock, gain must be recognized under Section 961(b)(2). Note also that the Proposed Regulations retain the gain reduction rule set forth originally in Notice 2018-7. The gain reduction rule, however, applies to reduce gain attributable to Section 965(a), and reduces gain attributable to Section 965(b) PTI but only if the basis election described above is made. Accordingly, taxpayers need to carefully consider the potential benefits of making the basis election for Section 965(b) PTI.[26]

A Revised 'Anti-Avoidance' Rule

Notice 2018-26 announced that certain transactions, and their attendant consequences, may be disregarded if entered into with a principal purpose of reducing the Section 965 tax liability.[27] The Proposed Regulations retain the "a principal purpose" standard but change the focus of the analysis to whether a transaction was intended to, and would in fact, change any "Section 965 element" of a US shareholder—namely,[28] the US shareholder's (i) Section 965(a) inclusion amount, (ii) aggregate foreign cash position, or (iii) amount of foreign taxes deemed paid under Section 960.[29] Surprisingly, even changes detrimental to a US shareholder—for instance, ones that increase its overall Section 965 tax liability—may nevertheless trigger the anti-avoidance rule and require a transaction to be disregarded. In apparent recognition of this anomalous outcome, the preamble notes that the required "a principal purpose" of changing a Section 965 element may be lacking in such circumstances, in which case the transaction ultimately would not be disregarded.[30] Although comments requested a de minimis exception to this principal purposes rule, none is provided.

The Proposed Regulations identify distributions and transactions that are presumed to be carried out with a principal purpose of changing a Section 965 element, but allow US shareholders to rebut that presumption with clear evidence. However, a narrower subset of these transactions—typically involving related parties and affiliates (only)—are identified as per se avoidance transactions that will be disregarded for purposes of applying Section 965. Examples include the following:

- Distributions by SFCs if and to the extent that, at the time of the distribution, there was a plan or intention for the distributee to transfer any distributed cash or cash equivalents to another SFC of the US shareholder or the distribution is a non–pro rata distribution to a foreign person that is related to the US shareholder.[31]
- A distribution by an SFC to which Section 312(a)(3) applies.[32]

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[26] To the extent a taxpayer makes an election under Proposed Treasury Regulations § 1.965-2(f)(2) to increase the basis of the DFIC shares by the Section 965(b) PTI, the taxpayer must make a corresponding reduction in E&P deficit foreign corporation shares. *See* Prop. Treas. Reg. § 1.965-2(f)(2)(ii)(B). The decrease in basis of the E&P deficit corporation shares is not protected by any sort of gain reduction rule. Thus, if that corresponding basis reduction is in excess of the Section 958(a) US shareholder's basis in the E&P deficit corporation, gain will be triggered. *See* Prop. Treas. Reg. § 1.965-2(h)(3).

[27] *See* Notice 2018-26, § 3.04.

[28] *See* Prop. Treas. Reg. § 1.965-4(b).

[29] *See* Prop. Treas. Reg. § 1.965-4(d).

[30] *See* 83 Fed. Reg. 39528 (Aug. 9, 2018) ("Depending on the facts and circumstances, transactions that do not reduce overall tax liability may not meet the principal purpose test described in proposed § 1.965-4(b)(1)."). But all changes in method of accounting and entity classification elections will be disregarded, regardless of the effect (or lack thereof) on a US shareholder's Section 965 tax liability or taxpayer purpose. *See id.*

[31] Prop. Treas. Reg. § 1.965-4(b)(2)(iii)(B).

[32] Prop. Treas. Reg. § 1.965-4(b)(2)(iv)(B).

- A Section 331 liquidation of an SFC into its US shareholder or a person related to the shareholder.[33]
- "Specified payments": Namely, any amount paid or accrued between November 2, 2017, and December 31, 2017, by a payor SFC to a related payee SFC with a different E&P measurement date that has the effect of reducing the post-1986 E&P of the payor SFC.[34]

Consistent with the statute and Notice 2018-26, the Proposed Regulations also disregard changes in accounting method and entity classifications made or filed after November 2, 2017. The rules are quite strict in this regard—even a change from an impermissible accounting method to a permissible one will be disregarded.

It is important to bear in mind that the scope and reach of these anti-avoidance rules are limited to determining Section 965 elements and a US shareholder's Section 965 tax liability. The rules are not intended to change or otherwise alter the normal operation of other Code sections. However, the Proposed Regulations provide no coordination rules, thus leaving open the possibility of unexpected and unintended tax results from the interactions of the anti-avoidance rules and other Code sections.

Other Noteworthy Provisions of the Proposed Regulations

- Deficits, including hovering deficits, are not taken into account for any purpose other than the determination of post-1986 E&P for purposes of Section 965 (e.g., not taken into account in computing deemed paid foreign tax credits). Additionally, the fact that a hovering deficit is taken into account for Section 965 purposes does not allow any deferred taxes with respect to the deficit to be released in computing foreign tax deemed paid on a Section 965 inclusion.[35]
- The Proposed Regulations adopt the guidance announced in Notice 2018-13 providing that the amount of a deficit of an E&P deficit corporation is determined by taking into account PTI. As a result, the amount of the deficit is reduced.[36] This outcome does not seem consistent with the intent of the rules to allow profits in one specified corporation to be offset with deficits in another, as if both operations had been conducted in a single corporation.
- Post-1986 E&P is determined by backing out only subpart F income as of the relevant measuring date,[37] which could, under the statute and Proposed Regulations, literally be interpreted as requiring a closing of the books at each measuring date to determine the amount of subpart F income that had accrued at that date. Hopefully, final regulations under Section 965 will include some additional guidance and relief similar to the elective calculation rules for determining November 2, 2017 post-1986 E&P.[38]
- The Section 902 fraction cannot be greater than one (also, it is worth noting the Section 902 fraction cannot be less than zero), addressing circumstances in which the numerator of the Section 902 fraction (as defined in Proposed Treasury Regulations § 1.965-6(c)(1)) may be greater than the denominator due to the fact that the Section 965(a) inclusion may be determined on a different date than the measurement date for the post-1986 E&P.[39]

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[33] *Id.*

[34] *See* Prop. Treas. Reg. § 1.965-4(f).

[35] *See* 83 Fed. Reg. 39521 (Aug. 9, 2018).

[36] *See* 83 Fed. Reg. 39516 (Aug. 9, 2018).

[37] *See* Prop. Treas. Reg. § 1.965-1(f)(7).

[38] *See* Prop. Treas. Reg. § 1.965-7(f).

[39] *See* 83 Fed. Reg. 39530 (Aug. 9, 2018).

- Because it has not been included in gross income, Section 986(c) does not apply to Section 965(b) PTI.[40]
- Certain domestic partnerships are treated as foreign partnerships in computing the Section 965 inclusions to avoid issues similar to those that were presented in prior Notice 2010-41,[41] where a domestic partnership owns CFC stock and also has a CFC partner.[42]
- A domestic pass-through entity must allocate its Section 965(c) deduction in the same proportion that its Section 965(a) inclusion is allocated to its domestic owners. These items cannot be separately allocated.[43]
- All members of a consolidated group are treated as a single taxpayer for certain purposes, but, consistent with subpart F computations generally, single taxpayer treatment does not apply for determining (i) any member's income inclusion under Section 951 (including Section 965(a)), (ii) any deduction under Section 965(c), and (iii) any deemed-paid credits under Section 960.[44]
- Despite numerous comments, Treasury and the IRS refused to issue any further guidance addressing the repeal of Section 958(b)(4), explaining that the issue is "beyond the scope of the proposed regulations."[45]
- Treasury and the IRS also rejected comments to allow for alternative E&P measurement for determining an SFC's post-1986 E&P and cash position, such as audited financial statements, in circumstances where the SFC is not a CFC, even though such a corporation does not generally track E&P under US tax principles.[46]
- Comments that requested that the anti-avoidance rule not apply to the extent a reduction in tax liability by reason of Section 965 is offset by an equal amount of tax increase pursuant to a different Code provision were rejected.[47]
- The Proposed Regulations address in detail the Section 965(h) election to pay the transition tax in installments, including providing detailed rules for acceleration events.[48]

Comments Requested by Treasury and the IRS

Finally, specific comments are requested by Treasury and the IRS. These comments, as well as any request for a public hearing, must be received by October 9, 2018. The most significant of these requested comments are set forth below.

- Whether additional rules are needed to address the treatment of hovering deficits that reduce post-1986 E&P of a DFIC; for example, when the hovering deficit creates a specified E&P deficit.[49]

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[40] *See* 83 Fed. Reg. 39537 (Aug. 9, 2018).

[41] Notice 2010-41, 2010-22, I.R.B. 715 (announcing that Treasury and the IRS intended to issue regulations).

[42] *See* 83 Fed. Reg. 39517, 520 (Aug. 9, 2018).

[43] *See* Prop. Treas. Reg. § 1.965-3(g).

[44] *See* 83 Fed. Reg. 39536 (Aug. 9, 2018).

[45] *See* 83 Fed. Reg. 39537 (Aug. 9, 2018).

[46] *See* 83 Fed. Reg. 39521 (Aug. 9, 2018). The proposed regulations do permit an alternative method for calculating post-1986 E&P for SFCs that have 52- to 53-week taxable years. *See* Prop. Treas. Reg. § 1.965-7(f).

[47] 83 Fed. Reg. 39528 (Aug. 9, 2018).

[48] *See* Prop. Treas. Reg. § 1.965-7.

[49] 83 Fed. Reg. 39521 (Aug. 9, 2018).

- The appropriate amount of a basis adjustment with respect to a DFIC with respect to which a Section 962 election is effective.[50]
- As a result of the enactment of Section 965, Treasury and the IRS recognize that the application of Section 965(b)(4)(A) and (B) may warrant the issuance of special rules for the determination of adjusted basis. Furthermore, a different rule may be needed if a taxpayer has made an election under Proposed Treasury Regulations § 1.965-2(f)(2) to adjust its basis to reflect the use of a specified E&P deficit. Treasury and the IRS request comments on what rules may be appropriate, including whether the rules under Treasury Regulations § 1.861-12(c)(2) should be modified.[51]
- Whether more guidance is necessary with respect to the assignment of the Section 965(a) inclusion and the related taxes to a separate category or categories of income.[52]
- Whether additional rules are needed for determining the amount of the increase in the Section 904 limitation with respect to distributions of Section 965(a) previously taxed E&P and Section 965(b) PTI, taking into account the Section 965(c) deduction and the disallowed foreign taxes under Section 965(g).[53]
- The definition of the cash position of an SFC.[54]

Contacts

If you have any questions or would like more information on the issues discussed in this White Paper, please contact any of the following Morgan Lewis lawyers:

Chicago

Michael Liu	+1.312.324.1498	michael.liu@morganlewis.com
Josh Richardson	+1.312.324.1494	joshua.richardson@morganlewis.com
Nelson C. Yates, II	+1.312.324.1489	nelson.yates@morganlewis.com

Philadelphia

Casey August	+1.215.963.4706	casey.august@morganlewis.com

San Francisco/Silicon Valley

Barton Bassett	+1.713.890.5164	barton.bassett@morganlewis.com
John Ryan	+1.650.843.7229	john.ryan@morganlewis.com
Michael Liu	+1.650.843.7505	michael.liu@morganlewis.com

Washington, DC

Peter Daub	+1.202.739.5171	peter.daub@morganlewis.com
Scott Farmer	+1.202.373.6772	scott.farmer@morganlewis.com

[50] 83 Fed. Reg. 39526 (Aug. 9, 2018).

[51] 83 Fed. Reg. 39531-32 (Aug. 9, 2018).

[52] 83 Fed. Reg. 39532 (Aug. 9, 2018).

[53] 83 Fed. Reg. 39532 (Aug. 9, 2018).

[54] 83 Fed. Reg. 39538 (Aug. 9, 2018).

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