



[4830-01-p]

## DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[REG-110059-20]

RIN 1545-BP83

Ownership Attribution Under Section 958 for Purposes of Sections 367(a) and 954(c)(6)

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations relating to the modification of section 958(b) of the Internal Revenue Code (“Code”) by the Tax Cuts and Jobs Act, which was enacted on December 22, 2017. The proposed regulations modify the ownership attribution rules applicable to outbound transfers of stock or securities of a domestic corporation under section 367(a). The proposed regulations also narrow the scope of foreign corporations that are treated as controlled foreign corporations for purposes of the look-through rule under section 954(c)(6). The proposed regulations affect United States persons that transfer stock or securities of a domestic corporation to a foreign corporation that are subject to section 367(a), and United States shareholders of foreign corporations.

DATES: Written or electronic comments and requests for a public hearing must be received by November 20, 2020. Requests for a public hearing must be submitted as prescribed in the “**Comments and Requests for a Public Hearing**” section.

ADDRESSES: Commenters are strongly encouraged to submit public comments electronically. Submit electronic submissions via the Federal eRulemaking Portal at [www.regulations.gov](http://www.regulations.gov) (indicate IRS and REG-110059-20) by following the online instructions for submitting comments. Once submitted to the Federal eRulemaking Portal, comments cannot be edited or withdrawn. The IRS expects to have limited personnel available to process public comments that are submitted on paper through mail. Until further notice, any comments submitted on paper will be considered to the extent practicable. The Department of the Treasury (Treasury Department) and the IRS will publish for public availability any comment submitted electronically, and to the extent practicable on paper, to its public docket. Send paper submissions to:

CC:PA:LPD:PR (REG- REG-110059-20), room 5203, Internal Revenue Service, PO Box 7604, Ben Franklin Station, Washington, D.C. 20044.

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, Christina G. Daniels at (202) 317-6934 or Lynlee C. Baker at (202) 317-6937; concerning submissions of comments or requests for a public hearing, Regina Johnson at (202) 317-5177 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

## **Background**

### **I. Sections 318 and 958(b)(4)**

Section 958 provides rules for determining direct, indirect, and constructive stock ownership. Under section 958(a)(1), stock is considered owned by a person if it is owned directly or is owned indirectly through certain foreign entities under section 958(a)(2). Under section 958(b), the constructive stock ownership rules of section 318

apply, with certain modifications, to the extent that the effect is to treat any United States person as a United States shareholder within the meaning of section 951(b) (“U.S. shareholder”) of a foreign corporation, to treat a person as a related person within the meaning of section 954(d)(3), to treat the stock of a domestic corporation as owned by a U.S. shareholder of a controlled foreign corporation within the meaning of section 957 (“CFC”) for purposes of section 956(c)(2), or to treat a foreign corporation as a CFC.

As in effect before repeal, section 958(b)(4) provided that section 318(a)(3)(A), (B), and (C) (providing for so-called “downward attribution”) was not to be applied so as to consider a United States person as owning stock owned by a person who is not a United States person (a “foreign person”). Effective for the last taxable year of foreign corporations beginning before January 1, 2018, and each subsequent year of the foreign corporations, and for the taxable years of U.S. shareholders in which or with which such taxable years of the foreign corporations end, section 958(b)(4) was repealed by section 14213 of the Tax Cuts and Jobs Act, Public Law 115-97 (2017) (the “Act”). As a result of this repeal, stock of a foreign corporation owned by a foreign person can be attributed to a United States person under section 318(a)(3) for various purposes, including for purposes of determining whether a United States person is a U.S. shareholder of the foreign corporation and, therefore, whether the foreign corporation is a CFC. In other words, as a result of the repeal of section 958(b)(4), section 958(b) now provides for downward attribution from a foreign person to a United States person in circumstances in which section 958(b), before the Act, did not so provide. As a result, among other consequences, United States persons that were not

previously treated as U.S. shareholders may be treated as U.S. shareholders, and foreign corporations that were not previously treated as CFCs may be treated as CFCs.

On October 2, 2019, the Treasury Department and the IRS published proposed regulations (REG-104223-18) relating to the repeal of section 958(b)(4) in the **Federal Register** (84 FR 52398) (the “2019 proposed regulations”). The 2019 proposed regulations are issued as final regulations in the Rules and Regulations section of this issue of the **Federal Register**. Consistent with the purpose underlying the 2019 proposed regulations, these proposed regulations propose additional changes that are intended to ensure that certain rules under sections 367(a) and 954(c)(6) apply in the same manner in which they applied before the repeal of section 958(b)(4).

## II. Section 367(a)

Section 367(a)(1) generally provides that if a United States person transfers property to a foreign corporation in connection with an exchange described in section 332, 351, 354, 356, or 361, the foreign corporation will not be treated as a corporation for purposes of determining the extent to which gain is recognized on the transfer.

Section 1.367(a)-3 provides rules regarding the treatment of transfers of stock or securities by a United States person to a foreign corporation in an exchange described in section 367(a)(1) (“outbound transfer”). Section 1.367(a)-3(b)(1) generally requires a United States person to enter into a gain recognition agreement, pursuant to rules under §1.367(a)-8, to obtain nonrecognition treatment on an outbound transfer of stock or securities of a foreign corporation if the United States person owns at least five percent (applying the attribution rules of section 318, as modified by section 958(b)) of the transferee foreign corporation immediately after the transfer. To obtain nonrecognition

treatment on outbound transfers of stock or securities of a domestic corporation (the “U.S. target company”), §1.367(a)-3(c)(1) generally requires the U.S. target company to meet certain reporting requirements and that each of four conditions is satisfied: (1) fifty percent or less of both the total voting power and the total value of the stock of the transferee foreign corporation is received in the transaction, in the aggregate, by U.S. transferors; (2) fifty percent or less of each of the total voting power and the total value of the stock of the transferee foreign corporation is owned, in the aggregate, immediately after the transfer by United States persons that are either officers or directors of the U.S. target company or that are five-percent target shareholders (as defined in §1.367(a)-3(c)(5)(iii)); (3) either the United States person is not a five-percent transferee shareholder (as defined in §1.367(a)-3(c)(5)(ii)), or the United States person enters into a gain recognition agreement as provided in §1.367(a)-8; and (4) the active trade or business test (as defined in §1.367(a)-3(c)(3)) is satisfied. For purposes of applying these tests, §1.367(a)-3(c)(4)(iv) states that, except as otherwise provided, the stock attribution rules of section 318, as modified by section 958(b), apply in determining the ownership or receipt of stock, securities, or other property.

### III. Section 954(c)(6)

Section 954(c)(6)(A) generally provides that for purposes of section 954(c), dividends, interest, rents, and royalties received or accrued by a CFC from a CFC that is a related person are not treated as foreign personal holding company income to the extent attributable or properly allocable (determined under rules similar to the rules of section 904(d)(3)(C) and (D)) to income of the related person that is neither subpart F income nor income treated as effectively connected with the conduct of a trade or

business in the United States (the “section 954(c)(6) exception”). In general, and subject to certain limitations, the section 954(c)(6) exception is intended to make U.S.-based multinational corporations more competitive with foreign-based multinational corporations by allowing U.S.-based multinational corporations to reinvest their active foreign earnings where they are needed without giving rise to immediate additional taxation under the subpart F provisions. See H.R. Rep. No. 109-304 at 45 (2005).

Section 954(c)(6)(A) provides that the Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the provision, including regulations to prevent the abuse of the purposes of the provision. As most recently extended by the Further Consolidated Appropriations Act, Public Law 116–94 (2020), section 954(c)(6) applies to taxable years of foreign corporations beginning after December 31, 2005, and before January 1, 2021, and to taxable years of U.S. shareholders with or within which such taxable years of foreign corporations end.

Notice 2007-9, 2007-5 I.R.B. 401, describes guidance that the Treasury Department and the IRS intend to issue regarding the application of section 954(c)(6), including certain anti-abuse rules. That notice, in section 7(d), provides, in relevant part:

When the use of options or similar interests causes a foreign corporation to become a CFC payor, and a principal purpose for the use of the options or similar interests is to qualify dividends, interest, rents, or royalties paid by the foreign corporation for the section 954(c)(6) exception, the dividends, interest, rents, or royalties received or accrued from such foreign corporation will not be treated as being received or accrued from a CFC payor and, therefore, will not be eligible for the section 954(c)(6) exception.

A rule similar to that in section 7(d) of Notice 2007-9 was included in §1.954-1(f)(2)(iv), T.D. 9883, 84 FR 69107 (2019).

## **Explanation of Provisions**

### **I. Changes in Connection with Section 367(a)**

As discussed in part II of the Background section of this preamble, §1.367(a)-3(c)(4)(iv) states that, except as otherwise provided, the constructive stock ownership rules of section 318, as modified by section 958(b), apply for purposes of determining the ownership or receipt of stock, securities or other property under §1.367(a)-3(c). The repeal of section 958(b)(4) and the resulting application of section 318(a)(3)(A), (B), and (C) to the stock ownership tests under §1.367(a)-3(c)(1) can cause a transfer that previously would have satisfied the conditions set forth in §1.367(a)-3(c)(1) to no longer qualify for the exception to section 367(a)(1) because, for example, more shareholders are now considered to be five-percent target shareholders as a result of downward attribution. The conditions set forth in §1.367(a)-3(c)(1) and the attribution rule in §1.367(a)-3(c)(4)(iv) were promulgated when section 958(b)(4) did not allow for downward attribution from foreign persons.

The Treasury Department and the IRS have determined that, for purposes of applying §1.367(a)-3(c)(1)(i), (ii), and (iv), a United States person's constructive ownership interest should not include an interest that is treated as owned as a result of downward attribution from a foreign person as it would inappropriately treat the United States person as owning an interest it would not have owned under the rules in effect when those regulations were promulgated. The Treasury Department and IRS have determined, however, that the constructive ownership rules as they apply to the condition set forth in §1.367(a)-3(c)(1)(iii) (which requires that either the United States person is not a five-percent transferee shareholder or the United States person must

enter into a gain recognition agreement) should not be modified, and thus will continue to take into account downward attribution. The continued application of downward attribution for purposes of §1.367(a)-3(c)(1)(iii) results in a consistent application of the gain recognition agreement provisions for outbound transfers of stock or securities of domestic and foreign corporations. Although the Act's repeal of section 958(b)(4) may require a United States person to enter into a gain recognition agreement in connection with an outbound transfer of stock or securities of a foreign corporation to obtain nonrecognition treatment when no such agreement would have been required before the Act, no changes are being proposed to §1.367(a)-3(b)(1) because the Treasury Department and the IRS have decided this result is appropriate in light of the policies of section 367(a) and the Act.

Therefore, and in accordance with the regulatory authority provided in section 367(a), the proposed regulations revise §1.367(a)-3(c)(4)(iv) to apply the attribution rules of section 318, as modified by section 958(b) but without applying section 318(a)(3)(A), (B), and (C) to treat a United States person as owning stock that is owned by a foreign person, for all purposes of §1.367(a)-3(c) other than for purposes of determining whether a U.S. person is a five-percent transferee shareholder under §1.367(a)-3(c)(1)(iii).

## II. Changes in Connection with Section 954(c)(6)

As discussed in part III of the Background section of this preamble, Congress enacted section 954(c)(6) to generally allow U.S.-based multinational corporations to reinvest their active foreign earnings (in other words, earnings of CFCs subject to U.S. tax deferral) where they are needed outside the United States without giving rise to

immediate additional taxation under the subpart F provisions. Accordingly, the section 954(c)(6) exception is intended to apply to payments between CFCs of a U.S.-based multinational group that have active foreign earnings that are subject to the subpart F provisions. If a foreign corporation is a CFC solely by reason of downward attribution from a foreign person, however, most or all of that foreign corporation's earnings typically are not under U.S. taxing jurisdiction (that is, subject to the subpart F and GILTI provisions or, in some cases, taxed in the United States when distributed to its owners) and, as a result, amounts paid or accrued by that foreign corporation to another foreign corporation that is a CFC (without regard to downward attribution) should not be eligible for the section 954(c)(6) exception. For example, assume a foreign corporation (FC1) is a CFC (without regard to downward attribution) and a member of a foreign parent multinational group, the common parent of which is not a CFC, and another foreign corporation (FC2) that is also a member of the multinational group is a CFC but solely by reason of downward attribution and does not have any U.S. shareholders that own (within the meaning of section 958(a)) stock in such CFC (a "section 958(a) U.S. shareholder"). FC1 makes a loan to FC2. In the absence of regulations, interest received by FC1 from FC2 would be eligible for the exception under section 954(c)(6) even though the income of FC2 is not taxed by the United States. In comparison, if FC1 made a loan to the foreign parent instead of to FC2, interest received by FC1 from the foreign parent would not be eligible for the exception under section 954(c)(6).

Therefore, in accordance with the regulatory authority provided in section 954(c)(6)(A), the proposed regulations limit the application of the section 954(c)(6) exception to amounts received or accrued from foreign corporations that are CFCs

without applying section 318(a)(3)(A), (B), and (C) to treat a United States person as owning stock that is owned by a foreign person. The modification in these proposed regulations is consistent with the treatment of interest received by FC1 in the example if instead of making the loan to FC2, FC1 made the loan to the foreign parent of the group and with the purposes of the anti-abuse rules set forth in section 7(d) of Notice 2007-9 and §1.954-1(f)(2)(iv).

Comments are requested as to whether, and if so, to what extent, the section 954(c)(6) exception should be available in cases in which a related foreign payor corporation (that is a CFC solely as a result of downward attribution) has section 958(a) U.S. shareholders and therefore is partially under U.S. taxing jurisdiction.

### III. Applicability Dates

The regulations under section 367(a) are proposed to apply to transfers made on or after September 21, 2020.

Subject to special rules for certain entity classification elections and changes in taxable years, the regulations under section 954(c)(6) are proposed to apply to payments or accruals of dividends, interest, rents, and royalties made by a foreign corporation during taxable years of the foreign corporation ending on or after September 21, 2020, and to taxable years of United States shareholders in which or with which such taxable years of the foreign corporation end.

The proposed regulations further provide that taxpayers may choose to apply the rules under section 367 or 954(c)(6), once filed as final regulations in the **Federal Register**, to the last taxable year of a foreign corporation beginning before January 1,

2018, and each subsequent taxable year of the foreign corporation, subject to a consistency requirement. See section 7805(b)(7).

Finally, a taxpayer may rely on the proposed regulations under section 367 or 954(c)(6) with respect to any taxable year before the date that these regulations are published as final regulations in the **Federal Register**, provided that the taxpayer and persons that are related (within the meaning of section 267 or 707) to the taxpayer consistently rely on the proposed regulations under section 367 or 954(c)(6), respectively, with respect to all foreign corporations.

### **Statement of Availability of IRS Documents**

IRS Revenue Procedures, Revenue Rulings, notices, and other guidance cited in this document are published in the Internal Revenue Bulletin and are available from the Superintendent of Documents, U.S. Government Publishing Office, Washington, DC 20402, or by visiting the IRS website at <http://www.irs.gov>.

### **Special Analyses**

These proposed regulations are not subject to review under section 6(b) of Executive Order 12866 pursuant to the Memorandum of Agreement (April 11, 2018) between the Treasury Department and the Office of Management and Budget regarding review of tax regulations.

It is hereby certified that these proposed regulations will not have a significant economic impact on a substantial number of small entities within the meaning of section 601(6) of the Regulatory Flexibility Act (5 U.S.C. chapter 6). The proposed regulations are intended to ensure that certain rules under sections 367(a) and 954(c)(6) apply in the same manner in which they applied before the repeal of section 958(b)(4). The

proposed regulations do not impose any new costs on taxpayers. Consequently, the Treasury Department and the IRS have determined that the proposed regulations will not have a significant economic impact on a substantial number of small entities. Notwithstanding this certification, the Treasury Department and the IRS invite comments on the impacts of these rules on small entities.

Pursuant to section 7805(f), this notice of proposed rulemaking has been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business. The Treasury Department and the IRS request comments on the impact of these proposed regulations on small business entities.

### **Comments and Requests for a Public Hearing**

Before these proposed amendments to the 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**” section. The Treasury Department and the IRS request comments on all aspects of the proposed regulations. Any electronic comments submitted, and to the extent practicable any paper comments submitted, will be made available at [www.regulations.gov](http://www.regulations.gov) or upon request.

As noted in the preamble to the 2019 proposed regulations, the Treasury Department and the IRS intend to update the regulations under section 267 to take into account the changes made to that section by Pub. L. 108-357 in future guidance. The Treasury Department and the IRS also intend to update the regulations under section 163(e) to take into account the changes made to that section by Pub. L. 108-357 in

future guidance. The Treasury Department and the IRS request comments on the appropriate scope of such guidance.

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

Announcement 2020-4, 2020-17 IRB 1, provides that until further notice, public hearings conducted by the IRS will be held telephonically. Any telephonic hearing will be made accessible to people with disabilities.

### **Drafting Information**

The principal authors of the proposed regulations are Karen J. Cate, Christina G. Daniels, and Lynlee C. Baker of the Office of Associate Chief Counsel (International). However, other personnel from the Treasury Department and the IRS participated in the development of the proposed regulations.

### **List of Subjects in 26 CFR Part 1**

Income taxes, Reporting and recordkeeping requirements.

### **Proposed Amendments to the Regulations**

Accordingly, 26 CFR part 1 is proposed to be amended as follows:

#### **PART 1—INCOME TAXES**

Paragraph 1. The authority citation for part 1 is amended by adding an entry for §1.954(c)(6)-2 in numerical order to read in part as follows:

Authority: 26 U.S.C. 7805.

\* \* \* \* \*

Section 1.954(c)(6)-2 issued under 26 U.S.C. 954(c)(6)(A).

\* \* \* \* \*

Par. 2. Section 1.367(a)-3 is amended by revising paragraph (c)(4)(iv) and adding two sentences at the end of paragraph (c)(11)(ii) to read as follows:

§1.367(a)-3 Treatment of transfers of stock or securities to foreign corporations.

\* \* \* \* \*

(c) \* \* \*

(4) \* \* \*

(iv) Attribution rule. Except as otherwise provided in this section, the rules of section 318, as modified by the rules of section 958(b) but without applying section 318(a)(3)(A), (B), and (C) so as to consider a U.S. person as owning stock which is owned by a person who is not a U.S. person, apply for purposes of determining the ownership or receipt of stock, securities, or other property under this paragraph. For purposes of determining whether a U.S. person is a five-percent transferee shareholder under paragraph (c)(1)(iii) of this section, however, the rules of section 318, as modified by the rules of section 958(b) (taking into account section 318(a)(3)(A), (B), and (C) so as to consider a U.S. person as owning stock which is owned by a person who is not a U.S. person), apply.

\* \* \* \* \*

(11) \* \* \*

(ii) \* \* \* Paragraph (c)(4)(iv) of this section applies to transfers occurring on or after September 21, 2020. For transfers occurring before September 21, 2020, a taxpayer may apply paragraph (c)(4)(iv) of this section to transfers occurring during the

last taxable year of a foreign corporation beginning before January 1, 2018, and each subsequent taxable year of the foreign corporation, provided that the taxpayer and persons that are related (within the meaning of section 267 or 707) to the taxpayer consistently apply this paragraph with respect to all transfers to all foreign corporations.

\* \* \* \* \*

Par. 3. Section 1.954(c)(6)-2 is added to read as follows:

§1.954(c)(6)-2 Definition of controlled foreign corporation for purposes of section 954(c)(6).

(a) Controlled foreign corporation. For purposes of section 954(c)(6), the term controlled foreign corporation has the meaning given such term by section 957 (taking into account the special rule for certain captive insurance companies contained in section 953(c)), determined without applying section 318(a)(3)(A), (B), and (C) so as to consider a United States person as owning stock which is owned by a person who is not a United States person.

(b) Applicability dates--(1) In general. Except as provided in paragraph (b)(2) of this section, this section applies to payments or accruals of dividends, interest, rents, and royalties made by a foreign corporation during taxable years of the foreign corporation ending on or after September 21, 2020, and taxable years of United States shareholders in which or with which such taxable years of the foreign corporation end. This section also applies to taxable years of a foreign corporation ending before September 21, 2020, and taxable years of United States shareholders in which or with which such taxable years of the foreign corporation end, resulting from an entity classification election made under §301.7701-3 of this chapter, or resulting from a change in taxable year under section 898, with respect to the foreign corporation that

was effective on or before September 21, 2020, but was filed on or after September 21, 2020.

(2) Special rule. A taxpayer may apply this section to the last taxable year of a foreign corporation beginning before January 1, 2018, and each subsequent taxable year of the foreign corporation ending before September 21, 2020, and to taxable years of United States shareholders in which or with which such taxable years of the foreign corporation end, provided that the taxpayer and persons that are related (within the meaning of section 267 or 707) to the taxpayer consistently apply this section with respect to all foreign corporations.

Sunita Lough,

Deputy Commissioner for Services and Enforcement.

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