



DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[REG-113839-22]

RIN 1545-BQ51

Single-Entity Treatment of Consolidated Groups for Specific Purposes

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations that treat members of a consolidated group as a single United States shareholder in certain cases for purposes of section 951(a)(2)(B) of the Internal Revenue Code (the “Code”). The proposed regulations affect consolidated groups that own stock of foreign corporations.

DATES: Written or electronic comments and requests for a public hearing must be received by January 18, 2023. 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 (indicate IRS and REG-113839-22) by following the online instructions for submitting comments. Once submitted to the Federal eRulemaking Portal, comments cannot be edited or withdrawn. The Department of the Treasury (“Treasury Department”) and the IRS will publish for public availability any comment submitted electronically or on paper to its public docket. Send paper submissions to: CC:PA:LPD:PR (REG-113839-22), room 5203, Internal Revenue Service, PO Box 7604, Ben Franklin Station, Washington, D.C. 20044.

FOR FURTHER INFORMATION CONTACT: Austin Diamond-Jones, (202) 317-5085

(Corporate) and Julie T. Wang, (202) 317-6975 (Corporate) regarding section 1502 and the proposed amendments to §1.1502-80, and Joshua P. Roffenbender, (202) 317-6934 (International) regarding sections 951, 951A, and 959; concerning submissions of comments and requests for a public hearing, Vivian Hayes at (202) 317-6901 (not toll-free numbers) or by email to publichearings@irs.gov (preferred).

SUPPLEMENTARY INFORMATION:

Background

I. Overview

This document contains proposed amendments to 26 CFR part 1 under sections 1502 and 7805(a) of the Code (the “proposed regulations”).

II. Sections 1501 and 1502

Pursuant to section 1501, an affiliated group of corporations may elect to file a U.S. Federal income tax (“U.S. tax”) return on a consolidated basis (such return, a “consolidated return”). Groups electing to file consolidated returns include all members’ income items on a single return, in lieu of filing separate returns for each member.

Section 1502 authorizes the Secretary of the Treasury or their delegate (“Secretary”) to prescribe regulations for an affiliated group of corporations that join in filing (or that are required to join in filing) a consolidated return (such a group, a “consolidated group,” as defined in §1.1502-1(h)) to clearly reflect the U.S. tax liability of the consolidated group and to prevent avoidance of such tax liability. For purposes of carrying out those objectives, section 1502 also permits the Secretary to prescribe rules that may be different from the provisions of chapter 1 of subtitle A of the Code that would apply if the corporations composing the consolidated group filed separate returns. Terms used in the consolidated return regulations generally are defined in §1.1502-1.

III. Sections 951(a)(1)(A), 951A(a), and 959

Sections 951(a)(1)(A) and 951A(a) subject each United States shareholder

(within the meaning of section 951(b) or section 953(c)(1)(A), if applicable) (each shareholder, a “U.S. shareholder”) of a controlled foreign corporation (within the meaning of section 957 or section 953(c)(1)(B), if applicable) (a “CFC”) to U.S. tax on certain income of the CFC, regardless of whether the CFC distributes the earnings and profits (“E&P”) attributable to such income. To avoid double taxation, a corresponding amount of the CFC’s E&P is designated as previously taxed earnings and profits (“PTEP”) under section 959 and generally is not subject to U.S. tax at the U.S. shareholder level when distributed, whether to a U.S. shareholder or to an upper-tier CFC (such a distribution to a U.S. shareholder or an upper-tier CFC, a “section 959(a) distribution” or a “section 959(b) distribution,” respectively). See section 959. Generally, PTEP is treated as distributed before E&P that is not PTEP (“non-PTEP”), and a section 959(a) distribution is treated as not a dividend. See section 959(c) and (d).

Under section 951(a)(1)(A), a U.S. shareholder of a CFC must include in gross income its pro rata share of the CFC’s subpart F income (as defined in section 952) if the U.S. shareholder owns (within the meaning of section 958(a)) stock of the CFC on the last day of the CFC’s taxable year on which it is a CFC (the “last relevant day”). Ownership of stock within the meaning of section 958(a) means stock owned directly and stock owned indirectly through foreign corporations and other foreign entities (including certain domestic entities to the extent treated as foreign entities under §1.958-1(d)(1)). For purposes of the remainder of this preamble, a reference to stock ownership means stock owned within the meaning of section 958(a).

A U.S. shareholder’s pro rata share of a CFC’s subpart F income for a taxable year of the CFC is calculated by first determining the amount described in section 951(a)(2)(A). This amount, which is determined based on the U.S. shareholder’s proportionate share of a hypothetical distribution by the CFC, represents subpart F

income (unreduced by distributions during the taxable year) allocable to stock of the CFC that the U.S. shareholder owns on the last relevant day. See section 951(a)(2)(A); §1.951-1(b) and (e). That amount is then reduced by the amount described in section 951(a)(2)(B) to arrive at the U.S. shareholder's pro rata share of the CFC's subpart F income. For a discussion of section 951(a)(2)(B), see part IV of this Background section.

Section 951A(a) requires a U.S. shareholder of a CFC to include in gross income its GILTI inclusion amount. See §1.951A-1(b). A U.S. shareholder's GILTI inclusion amount is determined by taking into account the U.S. shareholder's pro rata share of tested items (as defined in §1.951A-1(f)(5)) of certain CFCs in which the U.S. shareholder owns stock, such as tested income, tested loss, and qualified business asset investment. A U.S. shareholder's pro rata share of a CFC's tested items is determined in the same manner as a U.S. shareholder's pro rata share of a CFC's subpart F income under section 951(a)(2), subject to certain modifications. See section 951A(e)(1) and §1.951A-1(d).

In many cases, a significant portion of a CFC's income has been (or will be) subject to U.S. tax under section 951(a)(1)(A) or 951A(a), including by reason of the transition tax imposed under section 965, which taxed non-PTEP of certain foreign corporations under section 951(a)(1)(A). As a result, there is (and will continue to be) a substantial amount of PTEP in the U.S. tax system.

IV. Section 951(a)(2)(B)

Section 951(a)(2)(B) addresses cases in which stock of a CFC owned by a U.S. shareholder on the last relevant day was acquired by the U.S. shareholder during the CFC's taxable year. In these cases, section 951(a)(2)(B) generally reduces the U.S. shareholder's pro rata share of the CFC's subpart F income or tested income by the amount of distributions received by any other person during the taxable year as a

dividend with respect to the acquired stock. However, the reduction is limited to the amount of the dividend that would have been received with respect to the acquired stock if the CFC had distributed an amount equal to its subpart F income for the taxable year multiplied by a fraction, the numerator of which is the number of days during the taxable year on which the U.S. shareholder did not own the acquired stock, and the denominator of which is the number of days during the taxable year (such fraction, the “section 951(a)(2)(B) fraction”).

The reduction, as so limited, represents an amount of distributed income of the CFC on which the U.S. shareholder otherwise would be subject to U.S. tax under section 951(a)(1)(A) or 951A(a) by reason of owning the acquired stock on the last relevant day, but that is not allocable to the period during which the U.S. shareholder owned the acquired stock. The reduction is intended to prevent double taxation of subpart F income or tested income of the CFC that is distributed during the taxable year. In turn, the limitation on the reduction is intended to ensure that income allocable to the U.S. shareholder’s ownership period with respect to the acquired stock is included in the U.S. shareholder’s pro rata share. See generally Technical Explanation of the Revenue Act of 1962, S. Rep. No. 87-1881, at 239 (1962).

V. Application of Sections 951(a)(1)(A) and 951A(a) to Consolidated Groups

A consolidated group member’s inclusion under section 951(a)(1)(A) is determined at the member level in the same manner as the inclusion is determined for any domestic corporation that is a U.S. shareholder of a foreign corporation.

A member’s GILTI inclusion amount is determined by taking into account the aggregate of its pro rata share of the tested income of each tested income CFC (as defined in §1.951A-2(b)(1)) and its allocable share of the group’s aggregate amount of other tested items. See §1.1502-51. As explained in the preamble to the final regulations in §1.1502-51, determining a member’s GILTI inclusion amount entirely on a

separate-entity basis would undermine the clear reflection of the U.S. tax liability of the consolidated group as a whole. In contrast, the adopted approach creates “consistent results regardless of which member of a consolidated group owns the stock of the CFCs[,] . . . removes incentives for inappropriate planning, and also eliminates traps for the unwary.” See TD 9866, 84 Fed. Reg. 29288, 29318.

Explanation of Provisions

I. In General

The Treasury Department and the IRS are aware that some consolidated groups are taking the position that the group’s aggregate inclusions under sections 951(a)(1)(A) and 951A(a) are reduced by changing the location of ownership of stock of a CFC within the group. Specifically, taxpayers are taking the position that a group’s aggregate pro rata share of a lower-tier CFC’s subpart F income or tested income is reduced under section 951(a)(2)(B) by reason of a section 959(b) distribution made by the lower-tier CFC, together with a direct or indirect acquisition of stock of the lower-tier CFC by a member from another member. Given the substantial amount of PTEP in the U.S. tax system following the enactment of sections 951A and 965, the Treasury Department and the IRS understand that taxpayers are taking this position with increasing frequency in an attempt to significantly reduce their income inclusions under sections 951(a)(1)(A) and 951A(a).

For example, assume that M1 and M2 are members of a consolidated group (the “P group”). M1 directly owns all the stock of an upper-tier CFC (“CFC1”), which directly owns all the stock of a lower-tier CFC (“CFC2”). M2 directly owns all the stock of another CFC (“CFC3”). During a taxable year of CFC2, CFC2 makes a section 959(b) distribution to CFC1. On a day other than the last day of the same taxable year, CFC1 transfers all the stock of CFC2 to CFC3 in a transaction that qualifies as a reorganization described in section 368(a)(1)(B). As a result, M2 indirectly acquires

stock of CFC2, which M2 continues to own throughout the rest of the taxable year.

The Treasury Department and the IRS understand that some consolidated groups are taking the position that section 951(a)(2)(B) reduces M2's pro rata share of CFC2's subpart F income or tested income. This position is based in part on the assertion that, for purposes of the section 951(a)(2)(B) fraction, M2 is not treated as owning stock of CFC2 on days on which the stock is owned by M1 (or another member of the group).

This position does not clearly reflect a consolidated group's U.S. tax liability. The group's aggregate pro rata shares of subpart F income and tested income of a CFC – and thus the group's aggregate inclusions under sections 951(a)(1)(A) and 951A(a), respectively – should not be affected when ownership of stock of the CFC moves within the group.

In addition, this position is inconsistent with section 951(a)(2)(B) and the purposes of that provision. The amount described in section 951(a)(2)(B) represents certain distributed income of a CFC on which a U.S. shareholder otherwise would be subject to U.S. tax under section 951(a)(1)(A) or 951A(a) by reason of owning stock of the CFC on the last relevant day. E&P that already has been subject to U.S. tax, such as E&P comprising a section 959(b) distribution, cannot represent such income. A position treating such E&P as giving rise to a section 951(a)(2)(B) reduction inappropriately reduces U.S. taxation of a CFC's subpart F income or tested income. Furthermore, the reduction to U.S. tax could be permanent to the extent that a deduction under section 245A(a) is allowed when E&P corresponding to the untaxed income ultimately is distributed to a U.S. shareholder.

To address the inappropriate outcomes claimed under this position and to clearly reflect a consolidated group's U.S. tax liability, the proposed regulations treat members of a consolidated group as a single U.S. shareholder for certain purposes, as described

in part II of this Explanation of Provisions section. As described in part IV of this Explanation of Provisions, the Treasury Department and the IRS are further considering the interaction of sections 951(a)(2)(B) and 959(b).

II. Consolidated Groups Treated as a Single U.S. Shareholder for Purposes of Applying Section 951(a)(2)(B) with Respect to Section 959(b) Distributions

The proposed regulations treat members of a consolidated group as a single U.S. shareholder for purposes of applying section 951(a)(2)(B) in the context of section 959(b) distributions. See proposed §1.1502-80(j)(1). When members are treated as a single U.S. shareholder, direct or indirect acquisitions of stock of a CFC by one member from another member do not give rise to a section 951(a)(2)(B) reduction, because the numerator of the section 951(a)(2)(B) fraction reflects the period that both members owned stock of the CFC. As a result, the group's aggregate inclusions under sections 951(a)(1)(A) and 951A(a) with respect to a CFC are not reduced under section 951(a)(2)(B) by reason of a section 959(b) distribution made by the CFC and changes in the location of ownership of stock of the CFC within the group. See proposed §1.1502-80(j)(2), Example 1 and Example 2. The Treasury Department and the IRS have determined that this outcome facilitates the clear reflection of the U.S. tax liability of a consolidated group.

The proposed regulations do not apply in the context of dividends composed of non-PTEP. When such a dividend gives rise to a reduction under section 951(a)(2)(B), other rules may result in the dividend being (directly or indirectly) included in the gross income of a U.S. shareholder. See, e.g., §1.245A-5 (limiting the deduction under section 245A(a) and the look-through exception to subpart F income under section 954(c)(6)).

In addition to the proposed regulations, other authorities or common law doctrines may apply to recast a transaction or otherwise affect the tax treatment of a transaction. See, e.g., sections 482 and 7701(o) and §§1.701-2 and 1.1502-13(h).

III. Applicability Date

The proposed regulations are proposed to apply to taxable years for which the original consolidated return is due (without extensions) after the date of publication in the **Federal Register** of a Treasury Decision adopting these rules as final regulations. See section 1503(a).

IV. No Inference

No inference is intended with regard to the treatment of transactions involving a consolidated group before the applicability date of the proposed regulations, including under §1.1502-13. Additionally, no inference is intended with regard to the treatment of similar transactions not involving a consolidated group, or with regard to whether section 959(b) distributions are taken into account under section 951(a)(2)(B). The Treasury Department and the IRS are further considering the interaction of sections 951(a)(2)(B) and 959(b), and any additional guidance issued relating to those sections, including guidance to prevent abuse, may be retroactive.

Special Analyses

I. Regulatory Planning and Review -- Economic Analysis

The Administrator of the Office of Information and Regulatory Affairs (“OIRA”), Office of Management and Budget, has determined that this proposed rule is not a significant regulatory action, as that term is defined in section 3(f) of Executive Order 12866. Therefore, OIRA has not reviewed this proposed rule pursuant to section 6(a)(3)(A) of Executive Order 12866 and the April 11, 2018, Memorandum of Agreement between the Treasury Department and the Office of Management and Budget (“OMB”).

II. Regulatory Flexibility Act

Pursuant to the Regulatory Flexibility Act (5 U.S.C. chapter 6), it is hereby certified that these proposed regulations will not have a significant economic impact on

a substantial number of small entities. This certification is based on the fact that these proposed regulations apply only to corporations that file consolidated Federal income tax returns, and that such corporations almost exclusively consist of larger businesses. Specifically, based on data available to the IRS, corporations that file consolidated Federal income tax returns represent only approximately two percent of all filers of Forms 1120 (U.S. Corporation Income Tax Return). However, these consolidated Federal income tax returns account for approximately 95 percent of the aggregate amount of receipts provided on all Forms 1120. Therefore, these proposed regulations would not create additional obligations for, or impose an economic impact on, small entities. Accordingly, the Secretary certifies that the proposed regulations will not have a significant economic impact on a substantial number of small entities.

III. Section 7805(f)

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.

IV. Unfunded Mandates Reform Act

Section 202 of the Unfunded Mandates Reform Act of 1995 requires that agencies assess anticipated costs and benefits and take certain other actions before issuing a final rule that includes any Federal mandate that may result in expenditures in any one year by a state, local, or tribal government, in the aggregate, or by the private sector, of \$100 million in 1995 dollars, updated annually for inflation. In 2022, that threshold is approximately \$165 million. These proposed regulations do not include any Federal mandate that may result in expenditures by state, local, or tribal governments, or by the private sector in excess of that threshold.

V. Executive Order 13132: Federalism

Executive Order 13132 (entitled “Federalism”) prohibits an agency from

publishing any rule that has federalism implications if the rule either imposes substantial, direct compliance costs on state and local governments, and is not required by statute, or preempts state law, unless the agency meets the consultation and funding requirements of section 6 of the Executive Order. These proposed regulations do not have federalism implications and do not impose substantial direct compliance costs on State and local governments or preempt State law within the meaning of the Executive Order.

Comments and Requests for a Public Hearing

Before the proposed regulations are adopted as final regulations, consideration will be given to comments that are submitted timely to the IRS as prescribed in the preamble under the “**ADDRESSES**” section. The Treasury Department and the IRS request comments on all aspects of the proposed regulations. In addition, the Treasury Department and the IRS continue to study different applications of section 951(a)(2)(B) when CFC interests have been transferred in intercompany transactions and request comments on the interaction of section 951(a)(2)(B) and §1.1502-13. Any comments submitted will be made available at www.regulations.gov or upon request.

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 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.

Statement of Availability of IRS Documents

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

Bulletin) and are available from the Superintendent of Documents, U.S. Government Publishing Office, Washington, DC 20402, or by visiting the IRS website at www.irs.gov.

Drafting Information

The principal authors of these regulations are Joshua P. Roffenbender, Office of Associate Chief Counsel (International), and Jeremy Aron-Dine and Gregory J. Galvin, Office of Associate Chief Counsel (Corporate). However, other personnel from the IRS and the Treasury Department participated in their development.

List of Subjects in 26 CFR Part 1

Income Taxes, Reporting and recordkeeping requirements.

Proposed Amendments to the Regulations

Accordingly, the Treasury Department and the IRS propose to amend 26 CFR part 1 as follows:

PART 1--INCOME TAXES

Paragraph 1. The authority citation for part 1 continues to read in part as follows:

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

Par. 2. In §1.1502-80, paragraphs (i) and (j) are added to read as follows:

§1.1502-80 Applicability of other provisions of law.

* * * * *

(i) [Reserved]

(j) *Special rules for application of section 951(a)(2)(B) to distributions to which section 959(b) applies--(1) Single United States shareholder treatment.* In determining the amount described in section 951(a)(2)(B) that is attributable to distributions to which section 959(b) applies, members of a group are treated as a single United States shareholder (within the meaning of section 951(b) (or section 953(c)(1)(A), if applicable)) for purposes of determining the part of the year during which such

shareholder did not own (within the meaning of section 958(a)) the stock described in section 951(a)(2)(A). The purpose of this paragraph (j) is to facilitate the clear reflection of income of a consolidated group by ensuring that the location of ownership of stock of a foreign corporation within the group does not affect the amount of the group's income by reason of sections 951(a)(1)(A) and 951A(a).

(2) *Examples.* The following examples illustrate the application of paragraph (j)(1) of this section. For purposes of the examples in this paragraph (j)(2): M1 and M2 are members of a consolidated group of which P is the common parent (P group); each of CFC1, CFC2, and CFC3 is a controlled foreign corporation (within the meaning of section 957(a)) with the U.S. dollar as its functional currency (within the meaning of section 985); the taxable year of all entities is the calendar year for Federal income tax purposes; and a reference to stock owned means stock owned within the meaning of section 958(a). These examples do not address common law doctrines or other authorities that might apply to recast a transaction or to otherwise affect the tax treatment of a transaction.

(i) *Example 1. Intercompany transfer of stock of a controlled foreign corporation--*
(A) *Facts.* Throughout Year 1, M1 directly owns all the stock of CFC1, which directly owns all the stock of CFC2. In Year 1, CFC2 has \$100x of subpart F income (as defined in section 952). M1's pro rata share of CFC2's subpart F income for Year 1 is \$100x, which M1 includes in its gross income under section 951(a)(1)(A). In Year 2, CFC2 has \$80x of subpart F income and distributes \$80x to CFC1 (the CFC2 Distribution). Section 959(b) applies to the entire CFC2 Distribution. On December 29, Year 2, M1 transfers all of its CFC1 stock to M2 in an exchange described in section 351(a). As a result, on December 31, Year 2 (the last day of Year 2 on which CFC2 is a controlled foreign corporation), M2 owns 100% of the stock of CFC1, which owns 100% of the stock of CFC2.

(B) *Analysis.* Under paragraph (j)(1) of this section, in determining the amount described in section 951(a)(2)(B) that is attributable to the CFC2 Distribution, all members of the P group are treated as a single United States shareholder for purposes of determining the part of Year 2 during which such shareholder did not own the stock of CFC2. Thus, the ratio of the number of days in Year 2 that such United States shareholder did not own the stock of CFC2 to the total number of days in Year 2 is 0/365. The amount described in section 951(a)(2)(B) is \$0, M2's pro rata share of CFC2's subpart F income for Year 2 is \$80x (\$80x - \$0), and M2 must include \$80x in its gross income under section 951(a)(1)(A).

(ii) *Example 2. Transfer of stock of a controlled foreign corporation between controlled foreign corporations--(A) Facts.* The facts are the same as the facts of Example 1, except that M1 does not transfer its CFC1 stock to M2. Additionally, throughout Year 1 and from January 1, Year 2, to December 29, Year 2, M2 directly owns all 90 shares of the only class of stock of CFC3. Further, on December 29, Year 2, CFC3 acquires all the CFC2 stock from CFC1 in exchange for 10 newly issued shares of the same class of CFC3 stock in a transaction described in section 368(a)(1)(B). As a result, on December 31, Year 2, M1 owns 10% of the stock of CFC2, and M2 owns 90% of the stock of CFC2.

(B) *Analysis.* Under paragraph (j)(1) of this section, in determining the amount described in section 951(a)(2)(B) that is attributable to the portion of the CFC2 Distribution with respect to each of the CFC2 stock that M1 owns on December 31, Year 2, and the CFC2 stock that M2 owns on that day, all members of the P group are treated as a single United States shareholder for purposes of determining the part of Year 2 during which such shareholder did not own such stock. In each case, the ratio of the number of days in Year 2 that such United States shareholder did not own such stock to the total number of days in Year 2 is 0/365, and the amount described in

section 951(a)(2)(B) is \$0. M1's and M2's pro rata shares of CFC2's subpart F income for Year 2 are \$8x (\$8x - \$0) and \$72x (\$72x - \$0), respectively, and M1 and M2 must include \$8x and \$72x in gross income under section 951(a)(1)(A), respectively.

(3) *Applicability date.* This paragraph (j) applies to taxable years for which the original consolidated Federal income tax return is due (without extensions) after the date a Treasury decision adopting these rules as final regulations is published in the *Federal Register*.

Melanie R. Krause,

Acting Deputy Commissioner for Services and Enforcement.

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