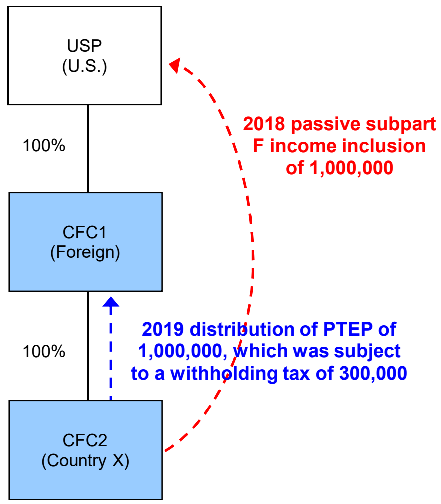
Reg. 1.960-3(e)(1), Example 1

Foreign Income Taxes Deemed Paid Under Sec. 960(b) and Accounting for PTEP



	CFC2	CFC1
Passive subf PTEP at the beginning of 2018	0	0
Increase in passive subf PTEP in 2018 (from subf inclusion)	1,000,000	0
Passive subf PTEP at the end of 2018	1,000,000	0
2019 distribution of passive subf PTEP from CFC2 to CFC1	(1,000,000)	1,000,000
Less dividend withholding taxes		(300,000)
Passive subf PTEP at the end of 2019	0	700,000
PTEP group taxes for passive subf PTEP at the end of 2019	0	300,000

(i) Facts. USP, a domestic corporation, owns all of the stock of CFC1, a controlled foreign corporation. CFC1 owns all of the stock of CFC2, a controlled foreign corporation. USP, CFC1, and CFC2 each use the calendar year as their U.S. taxable year. CFC1 and CFC2 use the “u” as their functional currency. At all relevant times, 1u = $1x. With respect to CFC2, USP includes in gross income a subpart F inclusion of 1,000,000u = $1,000,000x for the taxable year ending December 31, 2018. The inclusion is with respect to passive category income. In its U.S. taxable year ending December 31, 2019, CFC2 distributes 1,000,000u to CFC1. CFC2 has no earnings and profits except for the 1,000,000u of previously taxed earnings and profits resulting from USP's 2018 taxable year subpart F inclusion. CFC2's country of organization, Country X, imposes a withholding tax on CFC1 of 300,000u on CFC2's distribution to CFC1. Under Reg. 1.960-1(d)(3)(ii), CFC1's 300,000u of current year taxes are allocated and apportioned to the PTEP group within the annual PTEP account within the section 904 category to which the 1,000,000u of previously taxed earnings and profits are assigned.

(ii) Analysis—(A) Under Reg. 1.960-3(c)(1), a separate annual PTEP account in the passive category for the 2018 taxable year is established for CFC2 as a result of USP's subpart F inclusion. Under Reg. 1.960-3(c)(2), this account contains one PTEP group, section 951(a)(1)(A) PTEP.

(B) Under Reg. 1.960-3(c)(3), in the 2019 taxable year, the 1,000,000u related to the section 959(b) distribution from CFC2 is added to CFC1's annual PTEP account for the 2018 taxable year in the passive category and to the section 951(a)(1)(A) PTEP within such account. Similarly, CFC2's 2018 taxable year annual PTEP account within the passive category, and the section 951(a)(1)(A) PTEP within such account, is reduced by the amount of the 1,000,000u section 959(b) distribution to CFC1. Additionally, CFC1's annual PTEP account for the 2018 taxable year in the passive category, and the section 951(a)(1)(A) PTEP within such account, is reduced by the 300,000u of withholding tax imposed on CFC1 by Country X. Therefore, CFC1's annual PTEP account for the 2018 taxable year within the passive category and the section 951(a)(1)(A) PTEP within such account is 700,000u.

(C) Under Reg. 1.960-3(d)(1), the 300,000u of withholding tax is translated into U.S. dollars and $300,000x is added to the PTEP group taxes with respect to CFC1's section 951(a)(1)(A) PTEP within the annual PTEP account for the 2018 taxable year within the passive category.