U.S. Chamber of Commerce

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U.S. Department of Treasury
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William M. Paul
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Internal Revenue Service
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Re: Previously Taxed Earnings and Profits and Related Basis Adjustments (REG-105479-18)

Dear Ms. Leonard and Mr. Paul:

The U.S. Chamber of Commerce ("Chamber") welcomes the opportunity to comment on the long-awaited proposed regulations under sections 959 and 961 of the Internal Revenue Code regarding previously taxed earnings and profits ("PTEP") of foreign corporations and related basis adjustments.[1] In December 2018, the Department of the Treasury ("Treasury") and Internal Revenue Service ("IRS") released Notice 2019–01,[2] which announced an intent to withdraw proposed regulations issued in 2006 and issue a new notice of proposed rulemaking under sections 959 and 961 to address certain issues arising from the Tax Cuts and Jobs Act ("TCJA"). As explained in that notice, changes made by the TCJA had a significant impact on the role of PTEP and how it functions within the U.S. tax system.

The proposed regulations would provide rules addressing core aspects of the PTEP system, including rules to address longstanding issues under sections 959 and 961, account for new provisions and amendments under the TCJA, and implement IRS notices from 1988 and 2019. As set forth in the enclosed comments, however, the proposed regulations are lacking in several important respects and could benefit from revisions prior to being finalized. In general, taxpayers are unable to rely on the proposed regulations before the taxable year final regulations are published in the *Federal Register*. Additionally, the proposed regulations would add inordinate complexity to controlled foreign corporation ("CFC") share basis tracking by adopting a share-by-share approach that, if finalized, could result in double taxation.

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[1] Previously Taxed Earnings and Profits and Related Basis Adjustments, 89 Fed. Reg. 95362 (proposed Dec. 2, 2024).

[2] 2019-02 I.R.B. 275.

Furthermore, the proposed regulations do not contain any de minimis thresholds for tracking PTEP and basis, despite the obvious impracticability of tracking all U.S. persons' PTEP and basis—regardless of whether any such person is a United States shareholder. The proposed regulations also presume that partnerships will be able to obtain the partner-level information needed to comply therewith. These and other issues are discussed in greater detail in the enclosed comments. Please note, however, that the enclosed comments represent only a subset of the issues raised by our member companies.

The Chamber appreciates the opportunity to comment on the proposed regulations. We urge Treasury and the IRS to engage closely with the business community while reviewing our and other stakeholders' comments. As always, we would welcome the opportunity to discuss our comments with you or your colleagues in further detail and provide whatever additional information you may require. Thank you for your time and attention.

Sincerely,

W. M. McLeish

Watson M. McLeish
Senior Vice President, Tax Policy
U.S. Chamber of Commerce

Enclosure

U.S. Chamber of Commerce
Previously Taxed Earnings and Profits and Related Basis Adjustments (REG-105479-18)

STATUTORY PROVISION	ISSUE(S)	DISCUSSION
N/A	**Ability to Rely on Proposed Regulations** The proposed regulations would generally apply to taxable years of foreign corporations beginning on or after the date the proposed regulations are finalized in a Treasury Decision and to taxable years of persons for which such taxable years of foreign corporations are relevant. Under an "early application option," however, taxpayers would be permitted to choose to apply the proposed regulations in their entirety to taxable years of foreign corporations beginning before the general applicability date provided that those taxable years and all subsequent taxable years remain open. Thus, if the proposed regulations are not finalized relatively quickly, controversies could arise from closed years.	**Recommendation** The application of various provisions covered by the proposed regulations (e.g., section 961(c)) has been a source of debate and controversy among both taxpayers and tax practitioners. To foster greater certainty, Treasury and the IRS should amend the proposed regulations or issue other published guidance to confirm that taxpayers may elect to apply—and rely on—the proposed regulations as issued and in their entirety.

§ 961. Adjustments to basis of stock in controlled foreign corporations and of other property **(c) Basis adjustments in stock held by foreign corporations** Under regulations prescribed by the Secretary, if a United States shareholder is treated under section 958(a)(2) as owning stock in a controlled foreign corporation which is owned by another controlled foreign corporation, then adjustments similar to the adjustments provided by subsections (a) and (b) shall be made to— (1) the basis of such stock, and (2) the basis of stock in any other controlled foreign corporation by reason of which the United States shareholder is considered under section 958(a)(2) as owning the stock described in paragraph (1), but only for the purposes of determining the amount included under section 951 in the gross income of such United States shareholder (or any other United States shareholder who acquires from any person any portion of the interest of such United States shareholder by reason of which such shareholder was treated as owning such stock, but only to the extent of such portion, and subject to such proof of identity of such interest as the Secretary may prescribe by regulations). The preceding sentence shall not apply with respect to any stock to which a basis adjustment applies under subsection (a) or (b).	**Section 961(c) Losses** Prop. Treas. Reg. § 1.961-11(e)(2)(ii) would not allow positive section 961(c) basis to create a loss that reduces amounts included under section 951 in the gross income of the United States shareholder ("U.S. shareholder") of a controlled foreign corporation ("CFC"). For example, if CFC1 sells both CFC2 and CFC3 in the same taxable year, any "section 961(c) loss" with respect to CFC2 could not be used to reduce the U.S. shareholder's gross income generated by the sale of CFC3.	**Recommendation** The final regulations should eliminate this rule and permit section 961(c) basis to create a loss that is allocable to the amount included under section 951 in the U.S. shareholder's gross income. • Such an approach would be consistent with the plain language of section 961(c), which provides for basis adjustments "for the purposes of determining the amount included under section 951 in the gross income of such [U.S.] shareholder." The plain language does not limit losses resulting from positive section 961(c) basis and contradicts the approach taken in the proposed regulations. • Allowing the inclusion of such losses would also be consistent with the approach taken in the proposed corporate alternative minimum tax regulations, which would permit the netting of positive and negative adjusted financial statement income from CFCs. *See generally* Prop. Treas. Reg. § 1.56A-6(b). • There is no discernable policy for not permitting such a loss. The rationale for permitting section 961(c) basis to reduce gain is that the economic income giving rise to such basis has already been subject to U.S. tax, but there is no articulated justification for reducing only gain and not creating a loss.

§ 961. Adjustments to basis of stock in controlled foreign corporations and of other property **(b) Reduction in basis** **(1) In general** Under regulations prescribed by the Secretary, the adjusted basis of stock or other property with respect to which a United States shareholder or a United States person receives an amount which is excluded from gross income under section 959(a) shall be reduced by the amount so excluded. In the case of a United States shareholder who has made an election under section 962 for any prior taxable year, the reduction in basis provided by this paragraph shall not exceed an amount equal to the amount received which is excluded from gross income under section 959(a) after the application of section 962(d). **(2) Amount in excess of basis** To the extent that an amount excluded from gross income under section 959(a) exceeds the adjusted basis of the stock or other property with respect to which it is received, the amount shall be treated as gain from the sale or exchange of property.	**Double Taxation of PTEP – Section 961(b) and Share-by-Share Approach to Basis Adjustments** The proposed regulations would adopt a share-by-share approach for a U.S. shareholder's CFC section 961 basis increases to prevent non-economic losses. And while the proposed regulations would prevent certain instances of non-economic loss recognition, they could still result in gain recognition from routine repatriation transactions where there is no economic gain. This is because distributions would be treated as having been made pro-rata across shares under Prop. Treas. Reg. § 1.961-4(b)(2)(i)-(ii). The following example illustrates how the share-by-share approach adopted in the proposed regulations could result in double taxation. **Year 1:** A U.S. corporation ("USH"), the sole shareholder, owns the 1 outstanding share of stock of a CFC ("Share 1") that has a fair market value of $50. USH's basis in its CFC share is $50. In year 1, CFC earns $50 of subpart F income and has a corresponding income inclusion, resulting in section 959(c)(2) PTEP. Thus, USH increases its adjusted basis in Share 1 to $100 under section 961(a). *Year 2:* In year 2, USH contributes appreciated assets with a FMV of $100 and with a basis of $0 to CFC in exchange for 1 share of CFC stock ("Share 2"), in a tax-free section 351 exchange. USH's basis in Share 2 received in the exchange is $0 under section 358(a)(1). CFC does not recognize any net income in year 2. *Year 3:* CFC makes a distribution to USH of $50 at the end of year 3, which is attributable to CFC's PTEP with respect to USH and treated for U.S. federal income tax purposes as	**Recommendation** The final regulations should include a mechanism to prevent double taxation of PTEP that may arise due to the share-by-share approach adopted by the proposed regulations with respect to section 961(b) basis increases under Prop. Treas. Reg. §§ 1.961-4(b)(2), 1.961-3(d)(2)–(3), (e)(1). • Preventing double taxation of PTEP is recognized in the proposed regulations with respect to section 961(c) basis of lower-tier CFCs. In the preamble to the proposed regulations, Treasury and the IRS explain that "[a]n aggregate approach to applying positive section 961(c) basis allows positive section 961(c) basis of a transferred unit to be applied to a portion of the covered shareholder's share of the covered gain that is recognized with respect to another transferred unit." • In other areas of the Code, mechanisms exist to alleviate similar issues with respect to distributions, such as the "spill-over" rules that exists for S corporation distributions.[1] Accordingly, in the case of an actual or deemed distribution, the final regulations should allow adjusted basis to be available for purposes of section 961(b) across all a U.S. shareholder's shares of stock in the distributing corporation at the time of the distribution. This could be achieved by allowing adjusted basis to move from shares that have excess adjusted basis to those shares that do not have sufficient adjusted basis (i.e., a PTEP basis transfer) to the extent a pro-rata distribution would otherwise cause gain recognition under section 961(b). If the PTEP basis

[1] *See* Treas. Reg. § 1.1367-1(c)(3) ("The basis of a shareholder's share of stock is decreased by an amount equal to the shareholder's pro rata portion of the passthrough items and distributions described in section 1367(a)(2) attributable to that share, determined on a per share, per day basis in accordance with section 1377(a). If the amount attributable to a share exceeds its basis, the excess is applied to reduce (but not below zero) the remaining bases of all other shares of stock in the corporation owned by the shareholder in proportion to the remaining basis of each of those shares.").

	having been made pro rata on each of the 2 shares of CFC stock held by USH. *Result:* The proposed regulations would allocate PTEP basis to specific shares, in other words, on a share-by-share basis. However, dividend distributions are made pro-rata with respect to each share of stock of the foreign corporation owned at the time of the distribution. In this example, a distribution of $50 in year 3 would be allocated pro-rata to each share of stock in the CFC. As described above, Share 1 has $100 of basis and Share 2 has $0 of basis. This distribution would reduce PTEP basis in Share 1 by $25, leaving $75 PTEP basis in Share 1. But, because there is no basis in Share 2, $25 of the distribution would be treated as section 301(c)(3) capital gain. As evidenced by the example, in this circumstance, a routine distribution of cash attributable to PTEP that has already been subject to U.S. tax at 21% would result in incremental U.S. tax for the shareholder—a clear case of double taxation. Paradoxically, if the earnings and profits distributed had not previously been subject to U.S. tax, there would be no U.S. tax imposed on the distribution because the section 245A dividends received deduction would have applied. Furthermore, under the proposed regulations, there would be a non-economic loss of $25 that persists in Share 1 because of the share-by-share approach. As the preceding example demonstrates, the proposed regulations would contravene the purpose of sections 959 and 961, which is to prevent double taxation of PTEP. It would also fail to eliminate the creation of non-economic losses, which is the stated intent of the proposed share-by-share allocation. If, however, the USH had been able to use $25 of the PTEP basis from Share 1 against the $25 distributions of PTEP attributable to Share 2, double taxation would not have resulted.	transfer suggestion is adopted, in the preceding example, the taxpayer would first transfer $25 of the Share 1 adjusted basis to Share 2, before recognizing gain, resulting in zero remaining PTEP in both shares, and zero gain. This rule could be adopted by inserting a step between Prop. Treas. Reg. § 1.961-4(b)(2)(ii) and (iii) to provide for a transfer of basis to the extent necessary to prevent gain recognition. We understand Treasury's concern with transactions that may be structured to achieve non-economic losses by taxpayers. The proposed mechanism of transferring only basis if and when necessary to prevent gain recognition under section 961(b) is intended to mitigate this concern.

§ 964. Miscellaneous provisions	**Positive Section 961(c) Basis and Section 964(e)**	**Recommendation**
(e) Gain on certain stock sales by controlled foreign corporations treated as dividends **(1) In general** If a controlled foreign corporation sells or exchanges stock in any other foreign corporation, gain recognized on such sale or exchange shall be included in the gross income of such controlled foreign corporation as a dividend to the same extent that it would have been so included under section 1248(a) if such controlled foreign corporation were a United States person. For purposes of determining the amount which would have been so includible, the determination of whether such other foreign corporation was a controlled foreign corporation shall be made without regard to the preceding sentence.	The proposed regulations would provide specific rules regarding how positive section 961(c) basis is applied with respect to a covered shareholder. Under the proposed regulations, covered gain on the sale of stock in a foreign corporation by a CFC would be determined on an aggregate basis and assigned to covered shareholders to determine each shareholder's share of covered gain. *See* Prop. Treas. Reg. § 1.961-9(d)(1). The proposed regulations would allow each covered shareholder to apply positive section 961(c) basis to the covered gain and characterize the gain as PTEP with respect to the covered shareholder. Prop. Treas. Reg. § 1.961-9(d)(2).	Treasury and the IRS should retain this approach in the final regulations.

§ 959. Exclusion from gross income of previously taxed earnings and profits **(a) Exclusion from gross income of United States persons** For purposes of this chapter, the earnings and profits of a foreign corporation attributable to amounts which are, or have been, included in the gross income of a United States shareholder under section 951(a) shall not, when— (1) such amounts are distributed to, or (2) such amounts would, but for this subsection, be included under section 951(a)(1)(B) in the gross income of, such shareholder (or any other United States person who acquires from any person any portion of the interest of such United States shareholder in such foreign corporation, but only to the extent of such portion, and subject to such proof of the identity of such interest as the Secretary may by regulations prescribe) directly or indirectly through a chain of ownership described under section 958(a), be again included in the gross income of such United States shareholder (or of such other United States person). The rules of subsection (c) shall apply for purposes of paragraph (1) of this subsection and the rules of subsection (f) shall apply for purposes of paragraph (2) of this subsection.	**Covered Shareholder and Deemed Covered Shareholder** The proposed regulations reference "covered shareholder" and "deemed covered shareholder," and would require the tracking of PTEP with respect to both. Specifically, Prop. Treas. Reg. § 1.959-7(g)(1) provide that PTEP of a covered shareholder would transfer to a non-U.S. shareholder if the covered shareholder sells the stock of the foreign corporation to the non-U.S. shareholder. In addition, if the non-U.S. shareholder sells stock of the foreign corporation to a covered shareholder in the future, the PTEP and any subsequent adjustments would transfer to the covered shareholder. Thus, a deemed covered shareholder would be treated the same as a covered shareholder.	**Recommendation** There should be de minimis thresholds with respect to "covered shareholders." • It is not practical to track every U.S. person regardless of whether such person is a U.S. shareholder. • In addition, the proposed rules for deemed covered shareholders would be extremely burdensome to administer. In a sale and purchase context, it is highly unlikely that a foreign shareholder would know what PTEP is, let alone the amount of PTEP available. Given these issues, Treasury and the IRS should propose "reasonable methods" that a U.S. acquiror could use to calculate PTEP. One such method could be requiring a seller to certify PTEP amounts to the purchaser and separately maintain supporting records.

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<td>N/A</td>
<td>Partnership Reporting and Capital Account Issues
The proposed regulations would adopt a mixed aggregate and entity-level approach with respect to partnerships and partners. Such treatment would make it difficult, if not impracticable, for many partnerships to comply.
For instance, tracking derived basis on a share-by-share and shareholder-by-shareholder basis would be difficult for any partnership without access to how partners report inclusions.
And the general rules for maintaining capital accounts under section 704(b), under which book treatment of an item must follow the tax treatment, would create unintended consequences in cases where partnerships might incorrectly apply the proposed regulations’ reporting and tracking rules.</td>
<td>Recommendation
Treasury and the IRS should revisit and reconsider the treatment of partnerships and partners under the proposed regulations.
At a minimum, Treasury and the IRS should provide coordinating rules to facilitate the maintenance of capital accounts in accordance with section 704(b) and exceptions under which those rules would not be violated in the case of a mistake or a “foot fault” in applying the proposed reporting and tracking rules.
In addition, Treasury and the IRS should provide a de minimis exemption from the derived basis and PTEP reporting requirements. For example, a partner with the lesser of 1% of the capital of the partnership or $1,000,000 of a capital account should be exempt from reporting.</td>
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<td>§ 951. Amounts included in gross income of United States shareholders
(b) United States shareholder defined
For purposes of this title, the term ‘‘United States shareholder’’ means, with respect to any foreign corporation, a United States person (as defined in section 957(c)) who owns (within the meaning of section 958(a)), or is considered as owning by applying the rules of ownership of section 958(b), 10 percent or more of the total combined voting power of all classes of stock entitled to vote of such foreign corporation, or 10 percent or more of the total value of shares of all classes of stock of such foreign corporation.</td>
<td>U.S. Shareholder Partner Determination
The proposed regulations would presume that the partnership or CFC knows whether a direct or indirect partner is a U.S. shareholder with respect to a CFC owned by a partnership.</td>
<td>Recommendation
The final regulations should incorporate a safe harbor provision under which partners must notify the partnership if there are any U.S. shareholders in the ownership chain, similar to Rev. Proc. 2019-40, Section 4. This would help partnerships comply with partnership reporting requirements.</td>
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§ 6241. Definitions and special rules	**BBA Rules and Partnership-Related Items**	**Recommendation**
(2) Partnership adjustment **(B) Partnership-related item** The term “partnership-related item” means— (i) any item or amount with respect to the partnership (without regard to whether or not such item or amount appears on the partnership’s return and including an imputed underpayment and any item or amount relating to any transaction with, basis in, or liability of, the partnership) which is relevant (determined without regard to this subchapter) in determining the tax liability of any person under chapter 1, and (ii) any partner’s distributive share of any item or amount described in clause (i).	Derived basis information would be based on information obtained from U.S. shareholders regarding their inclusion amounts and elections. *See* Prop. Treas. Regs. §§ 1.961-2(d)(2) and 1.961-8. In addition, successor PTEP would be based on information provided by a transferor covered shareholder to the successor covered shareholder. *See* Prop. Treas. Reg. § 1.959-7(b)(1). In general, regulations under section 6241 recognize that partnership-related items do *not* include items that apply at the partner level, such as an item that is limited or determined based on a partner’s facts and circumstances. Treas. Reg. § 301.6241-1(a)(6)(v). But a BBA partnership may be subject to tax and penalties if such items are considered partnership-related items and not properly reported.	Final regulations should confirm that derived basis adjustments and successor PTEP are not partnership-related items subject to BBA reporting and penalties because they are based on a partner’s books and records.