

Previously Taxed Earnings and Profits Accounts

Notice 2019-01

SECTION 1. OVERVIEW

This notice announces that the Department of the Treasury (“Treasury Department”) and the Internal Revenue Service (“IRS”) intend to issue regulations addressing certain issues arising from the enactment of the Tax Cuts and Jobs Act, Pub. L. 115-97 (2017) (the “Act”), on December 22, 2017, with respect to foreign corporations with previously taxed earnings and profits (“PTEP”). Section 2 of this notice provides background on section 959 of the Internal Revenue Code (“Code”) and other relevant Code provisions. Section 3 of this notice describes proposed regulations that the Treasury Department and the IRS intend to issue concerning PTEP arising under provisions of the Act (the “forthcoming regulations”). Section 4 of this notice describes the proposed applicability date of the forthcoming regulations. Section 5 of this notice requests comments and provides contact information; as explained in that section, the Treasury Department and the IRS intend to address additional PTEP issues in separate guidance.

SECTION 2. BACKGROUND

The term PTEP refers to earnings and profits (“E&P”) of a foreign corporation attributable to amounts which are, or have been, included in the gross income of a

United States shareholder (as defined under section 951(b)) (“U.S. shareholder”) under section 951(a) or under section 1248(a). See sections 959(a) and (e). Under section 959(a)(1), distributions of PTEP are excluded from the U.S. shareholder’s gross income, or the gross income of any other U.S. person who acquires the U.S. shareholder’s interest (or a portion thereof) in the foreign corporation (such U.S. person, a “successor in interest”). Section 959(a)(2) further excludes PTEP from a U.S. shareholder’s gross income if such E&P would be included in the gross income of the U.S. shareholder or successor in interest under section 951(a)(1)(B) as an amount determined under section 956. Distributions of PTEP to a U.S. shareholder or successor in interest generally are not treated as dividends except that such distributions immediately reduce the E&P of the foreign corporation. Section 959(d).

Section 959(c) ensures that distributions from a foreign corporation are first attributable to PTEP described in section 959(c)(1) (“section 959(c)(1) PTEP”) and then to PTEP described in section 959(c)(2) (“section 959(c)(2) PTEP”), and finally to non-previously taxed E&P (“section 959(c)(3) E&P”). In addition, section 959(f) ensures that, in determining the amount of any inclusion under sections 951(a)(1)(B) and 956 with respect to a foreign corporation, PTEP attributable to section 951(a)(1)(A) inclusions remaining after any distributions during the year are taken into account before non-previously taxed E&P described in section 959(c)(3).

On August 29, 2006, a notice of proposed rulemaking (REG-121509-00) was published in the Federal Register (71 FR 51155) relating to the exclusion from gross income of PTEP and associated basis adjustments, corrections to which were published in the Federal Register on December 8, 2006 (71 FR 71116) (together, the “2006

proposed regulations”). The 2006 proposed regulations were intended to address some of the complexities and open issues regarding the application of sections 959 and 961 that are not specifically addressed in the current final regulations, which were originally published in 1965 and were amended in 1974, 1978, and 1983. See TD 6795 (1965-1 CB 287); TD 7334 (1975-1 CB 246); TD 7545 (1978-1 CB 245); TD 7893 (1983-1 CB 132). The 2006 proposed regulations have not been finalized. The Treasury Department and the IRS intend to withdraw the 2006 proposed regulations and to issue new proposed regulations under sections 959 and 961.

Under proposed §1.959-3(b), shareholders must account for PTEP with respect to their stock in a foreign corporation, and foreign corporations must account for the aggregate amount of PTEP of all shareholders, as well as section 959(c)(3) E&P. Before the Act, annual accounts generally were maintained for each separate category of income described in section 904(d)(1) and segregated between section 959(c)(1) PTEP and section 959(c)(2) PTEP. See Notice 88-71, 1988-2 C.B. 374. Section 959(c)(1) PTEP consisted of E&P previously included in gross income under sections 951(a)(1)(B) and (C), and section 959(c)(2) PTEP consisted of E&P previously included in gross income under section 951(a)(1)(A) or amounts included in gross income as a dividend under section 1248. See §1.959-3(b)(1) and (2); see also proposed §1.959-3(e)(2). Section 959(c)(1) PTEP also included E&P that had been originally classified as section 959(c)(2) PTEP and was reclassified as section 959(c)(1) PTEP because it reduced the amount of an income inclusion under section 951(a)(1)(B) or section 951(a)(1)(C) (before its repeal) pursuant to section 959(a)(2) or section 959(a)(3) (before its repeal). See §1.959-3(b).

Under the provisions of the Act, the portion of a U.S. shareholder's global intangible low-taxed income ("GILTI") included in gross income under section 951A(a) that is allocated to a controlled foreign corporation (as defined in section 957) ("CFC") under section 951A(f)(2) and proposed §1.951A-6(b)(2) is treated as an amount included in the gross income of a U.S. shareholder under section 951(a)(1)(A) for purposes of section 959. Section 951A(f)(1). Likewise, amounts determined under section 965(a), as amended by the Act, with respect to certain foreign corporations are treated as increases to subpart F income, and a U.S. shareholder with respect to such a foreign corporation generally includes in gross income under section 951(a)(1)(A) its pro rata share of such amounts, subject to reduction under section 965(b) for certain deficits attributable to stock in another foreign corporation owned by the U.S. shareholder. Amounts of a U.S. shareholder's inclusions under section 965(a) that are reduced by deficits attributable to stock of another foreign corporation under section 965(b) are treated as amounts included in the shareholder's gross income under section 951(a) for purposes of section 959. Section 965(b)(4)(A). Additionally, section 245A(e)(2) treats certain hybrid dividends received by a CFC as subpart F income for purposes of section 951(a)(1)(A). Finally, section 964(e)(4) treats a certain portion of gain on the disposition of CFC stock as subpart F income of the selling CFC for purposes of section 951(a)(1)(A). Accordingly, after the Act, section 959(c)(2) PTEP may arise from income inclusions under section 951(a)(1)(A) (including by reason of section 245A(e)(2), 951A(f)(1), 959(e), 964(e)(4), or 965(a)) or by reason of the application of section 965(b)(4)(A).

Section 965 and proposed regulations under that section provide special foreign tax credit and deduction rules, and proposed regulations under section 986 provide special foreign currency gain or loss rules, for distributions of PTEP attributable to income inclusions arising from the application of section 965(a) and PTEP attributable to the application of section 965(b)(4)(A) (collectively, “section 965 PTEP”). See proposed §§1.965-5 and 1.986(c)-1. Section 245A(e)(3) applies the disallowance of foreign tax credits in section 245A(d) with respect to any amount included in the income of a U.S. shareholder pursuant to section 245A(e)(2).

In addition, proposed regulations under section 960 establish, for purposes of determining the amount of foreign income taxes deemed paid, a system of accounting for PTEP in annual accounts for each separate category of income as defined in proposed §1.904-5(a)(4)(v) (“section 904 category”) and further segregate each annual account among ten PTEP groups. Proposed §1.960-3(c). The groups correspond to various types of income inclusions under section 951(a) (including amounts treated as giving rise to an income inclusion under section 951(a) for purposes of section 959) and PTEP reclassifications that can arise after the Act.

Finally, certain provisions of the Act provide for a deduction with respect to certain amounts that are included in the income of a domestic corporation and treated as section 951(a)(1)(A) inclusions for purposes of section 959. Sections 245A and 1248(j) generally allow a deduction with respect to gain on the sale of stock of a foreign corporation treated as a dividend under section 1248. In the case of gain treated as a dividend under section 964(e)(1) upon the sale or exchange by a CFC of stock of a lower tier foreign corporation and included in the CFC’s subpart F income under section

964(e)(4), section 964(e)(4) generally allows a deduction under section 245A with respect to a domestic corporation's pro rata share of the subpart F income that it includes in gross income as a dividend pursuant to section 964(e)(4).

SECTION 3. REGULATIONS TO BE ISSUED ADDRESSING PREVIOUSLY TAXED EARNINGS AND PROFITS

.01 Annual Accounts and Groups of Previously Taxed Earnings and Profits

The Act created the need to account for new groups of PTEP because section 959(c)(2) PTEP may arise by reason of income inclusions under section 951(a)(1)(A), 245A(e)(2), 951A(f)(1), 959(e), 964(e)(4), or 965(a) or by reason of the application of section 965(b)(4)(A), and those different groups of PTEP may be subject to different rules under sections 960, 965(g), 245A(e)(3), and 986(c). Additionally, because section 959(c)(2) PTEP may be reclassified as section 959(c)(1) PTEP as a result of sections 956 and 959(a)(2), similar groups for section 959(c)(1) PTEP must be maintained in order to properly apply sections 960, 965(g), 245A(e)(3), and 986(c) when earnings are reclassified. Groups of section 959(c)(1) PTEP must also be maintained with respect to inclusions under section 951(a)(1)(B) and section 951(a)(1)(C) (before its repeal) (in such cases, not by reason of the application of section 959(a)(2) or section 959(a)(3) (before its repeal)).

The Treasury Department and the IRS expect that the forthcoming regulations will provide that an annual account (each an "annual PTEP account") must be maintained and each annual PTEP account must be segregated into the 16 groups described below in each section 904 category (individually, a "PTEP group" and collectively, "PTEP groups"). For rules regarding the year and section 904 category to which an account corresponds, see proposed §1.960-3(c)(1). These 16 groups include

the ten groups identified in proposed §1.960-3(c)(2), which is discussed in section 2 of this notice, and six additional groups.

1. E&P described in section 959(c)(1)(A) that were initially described in section 959(c)(2) by reason of section 965(a) (“reclassified section 965(a) PTEP”);
2. E&P described in section 959(c)(1)(A) that were initially described in section 959(c)(2) by reason of section 965(b)(4)(A) (“reclassified section 965(b) PTEP”);
3. E&P described in section 959(c)(1)(A) by reason of section 951(a)(1)(B) and not by reason of section 959(a)(2) (“section 951(a)(1)(B) PTEP”);
4. E&P described in section 959(c)(1)(A) that were initially described in section 959(c)(2) by reason of section 951A(f)(2) (“reclassified section 951A PTEP”);
5. E&P described in section 959(c)(1)(A) that were initially described in section 959(c)(2) by reason of section 245A(e)(2) (“reclassified section 245A(e)(2) PTEP”);
6. E&P described in section 959(c)(1)(A) that were initially described in section 959(c)(2) by reason of section 959(e) (“reclassified section 959(e) PTEP”);
7. E&P described in section 959(c)(1)(A) that were initially described in section 959(c)(2) by reason of section 964(e)(4) (“reclassified section 964(e)(4) PTEP”);
8. E&P described in section 959(c)(1)(A) that were initially described in section 959(c)(2) by reason of section 951(a)(1)(A) (other than E&P that were initially described in (10) through (15) of this list) (“reclassified section 951(a)(1)(A) PTEP”);
9. E&P described in section 959(c)(1)(B), including by reason of section 959(a)(3) (before its repeal) (“section 956A PTEP”);

10. E&P described in section 959(c)(2) by reason of section 965(a) (“section 965(a) PTEP”);
11. E&P described in section 959(c)(2) by reason of section 965(b)(4)(A) (“section 965(b) PTEP”);
12. E&P described in section 959(c)(2) by reason of section 951A(f)(2) (“section 951A PTEP”);
13. E&P described in section 959(c)(2) by reason of section 245A(e)(2) (“section 245A(e)(2) PTEP”);
14. E&P described in section 959(c)(2) by reason of section 959(e) (“section 959(e) PTEP”);
15. E&P described in section 959(c)(2) by reason of section 964(e)(4) (“section 964(e) PTEP”); and
16. E&P described in section 959(c)(2) by reason of section 951(a)(1)(A) not otherwise described in (10) through (15) of this list (“section 951(a)(1)(A) PTEP”).

Accordingly, after the Act, section 959(c)(1) PTEP will be comprised of PTEP groups described in (1) through (9) of the preceding paragraph, and section 959(c)(2) PTEP will be comprised of PTEP groups described in (10) through (16) of the preceding paragraph. The forthcoming regulations will provide that once PTEP is assigned to a PTEP group within an annual PTEP account for the year of the income inclusion under section 951(a)(1) (including by reason of section 245A(e)(2), 951A(f)(1), 959(e), 964(e)(4), or 965(a)) or the year of application of section 965(b)(4)(A), the PTEP will be maintained in an annual PTEP account with a year that corresponds to the year of the account from which the PTEP originated if PTEP is distributed or reclassified in a

subsequent taxable year. See also proposed §§1.960-3(c)(3) and 1.960-3(c)(4) (providing similar rules for purposes of determining the amount of foreign income taxes deemed paid under section 960(b)).

As discussed in section 2 of this notice, proposed §1.960-3(c) provides that, for purposes of determining the amount of foreign income taxes deemed paid under section 960(b), with respect to a CFC, a separate annual PTEP account is maintained in each relevant section 904 category and the PTEP in each such account is assigned to one or more of the PTEP groups. However, the Treasury Department and the IRS recognize that for purposes of applying the ordering rules described in section 3.02 of this notice, it may be necessary to aggregate amounts across section 904 categories. The Treasury Department and the IRS expect that the forthcoming regulations will provide that, to the extent a CFC has E&P in a PTEP group that is in more than one section 904 category, any distribution out of that PTEP group is made pro rata out of the earnings and profits in each section 904 category. Additionally, the rules in proposed §§1.960-1 and 1.960-3 addressing the types of PTEP groups and their treatment for purposes of applying section 960(b) will be coordinated, as appropriate, with the forthcoming regulations when finalized.

It is expected that forthcoming regulations will provide that dollar basis must be tracked for each annual PTEP account, and, to the extent provided in the forthcoming regulations, separately for each PTEP group within an annual account. The forthcoming regulations will confirm that distributions from any PTEP group reduce the shareholder's stock basis under section 961(b)(1) without regard to how that basis was

originally created, including if the basis was created under section 961(a) due to an inclusion unrelated to the PTEP group being distributed.

It is expected that the forthcoming regulations will provide transition rules for annual PTEP accounts maintained before the applicability date of the regulations. Annual PTEP accounts established for taxable years before the applicability date of the forthcoming regulations will only need to be segregated between the section 951(a)(1)(B) PTEP group, the section 956A PTEP group, and the section 951(a)(1)(A) PTEP group, except for the taxable year to which section 965 applies. For the taxable year to which section 965 applies, annual PTEP accounts must also be segregated between the reclassified section 965(a) PTEP group, the reclassified section 965(b) PTEP group, the section 965(a) PTEP group, and the section 965(b) PTEP group (the “section 965 PTEP groups”). A shareholder that has maintained a multi-year pool instead of annual PTEP accounts for its section 951(a)(1)(B) PTEP, section 956A PTEP, or its section 951(a)(1)(A) PTEP will be permitted to treat the respective pool as a PTEP group in a single annual PTEP account with an average dollar basis, and that annual PTEP account will be considered the annual PTEP account for the last taxable year ending before the applicability date of the proposed regulations. Additionally, a shareholder that has maintained aggregate dollar basis pools to reflect the dollar basis of its total section 959(c)(1) PTEP or its total section 959(c)(2) PTEP (or both) for taxable years before the applicability date of the regulations will be permitted to assign an average dollar basis to the PTEP in each annual account (other than the section 965 PTEP groups), if it maintained annual accounts for section 959(c)(1) PTEP and section 959(c)(2) PTEP.

The forthcoming regulations described herein are intended to allow for the most flexibility in applying the limitations on the creditability of certain foreign income taxes, and the rules under section 986(c) regarding the recognition of foreign currency gain or loss, to the different types of PTEP. Implementing all of the operative provisions relating to PTEP following the Act with complete precision requires maintaining PTEP in 16 PTEP groups across the section 904 categories in annual accounts. The Treasury Department and the IRS recognize the complexity and both the administrative and compliance challenges associated with maintaining such a large number of PTEP groups and are weighing those considerations against the need for precision in applying the related foreign tax credit and foreign currency rules. Some of the proposed PTEP groups, such as reclassified 245A(e) PTEP, reclassified section 959(e) PTEP, reclassified section 964(e)(4) PTEP, section 956A PTEP, section 245A(e) PTEP, section 959(e) PTEP, and section 964(e)(4) PTEP are unlikely to arise on a routine basis. Additionally, because of the one-time nature of section 965, once all of the PTEP in the section 965 PTEP groups are distributed, those groups will be completely eliminated. See section 3.02 of this notice. Furthermore, the Treasury Department and the IRS are considering ways to simplify the rules associated with PTEP by consolidating PTEP groups or grouping accounts into multi-year accounts, or by other methods, and request comments in this regard.

.02 Ordering of Earnings and Profits upon Distribution and Reclassification

Section 959(c) provides that, for purposes of sections 959(a) and (b), section 316(a)(2) (relating to E&P of the taxable year) (“current E&P”) and then section 316(a)(1) (relating to E&P accumulated after February 28, 1913) (“accumulated E&P”) apply first to section 959(c)(1) PTEP, then to section 959(c)(2) PTEP, and finally to

section 959(c)(3) E&P. The reference to section 316 in section 959 indicates that a distribution of PTEP is dependent upon the existence of E&P otherwise sufficient to support a dividend under section 316. The forthcoming regulations will clarify that a distribution will be a distribution of PTEP only to the extent it would have otherwise been a dividend under section 316. For example, if a foreign corporation has no current E&P or accumulated E&P at the end of a taxable year, a distribution from the corporation to a shareholder during the taxable year will be a return of basis or treated as gain from the sale or exchange of property under section 301(c)(2) or (3), respectively, regardless of whether the shareholder has one or more annual PTEP accounts with respect to its stock in the foreign corporation.

Under section 316, distributions are considered first as distributions from current E&P, to the extent thereof, and then as distributions from the most recently accumulated E&P, to the extent thereof. As noted above, PTEP will be maintained in annual PTEP accounts. To facilitate the rule in section 959(c), which incorporates the ordering rule of section 316, the forthcoming regulations will require a “last in, first out” approach to the sourcing of distributions from annual PTEP accounts, subject to the special priority rule for PTEP arising by reason of the application of section 965, as discussed in the following paragraph. Thus, in general, section 959(c)(1) PTEP in the most recent annual PTEP account will be distributed first (with an exception for section 965 PTEP), followed by the next most recent annual PTEP account, and so on, after which the same approach will apply to section 959(c)(2) PTEP. Within each annual PTEP account, the PTEP attributable to each group of PTEP earned in that year will be distributed in the order prescribed in the following paragraphs in this section 3.02.

The forthcoming regulations will provide, under the grants of regulatory authority in sections 965(o) and 7805(a), that PTEP attributable to income inclusions under section 965(a) or by reason of section 965(b)(4)(A) receive priority when determining the group of PTEP from which a distribution is made. This priority will be integrated into the general ordering rule of section 959(c) that sources PTEP first from section 959(c)(1) PTEP and then from section 959(c)(2) PTEP. Thus, starting with section 959(c)(1) PTEP, under the forthcoming regulations, as an exception to the last-in, first-out approach, distributions will be sourced first from the reclassified section 965(a) PTEP and then from the reclassified section 965(b) PTEP. Once those PTEP groups are exhausted, under the last-in, first-out approach, distributions will be sourced pro rata from the remaining section 959(c)(1) PTEP groups in each annual PTEP account, starting from the most recent annual account.

Once the PTEP groups relating to section 959(c)(1) PTEP are exhausted, distributions will be sourced from section 959(c)(2) PTEP. As described in the preceding paragraph, the forthcoming regulations will provide that, as an exception to the last-in, first-out approach, distributions will be sourced first from section 965(a) PTEP and then section 965(b) PTEP. Once those two PTEP groups are exhausted, under the last-in, first-out approach, distributions will be sourced pro rata from the remaining section 959(c)(2) PTEP groups in each annual PTEP account, starting from the most recent annual PTEP account. Finally, once all the PTEP groups have been exhausted, the remaining amount of any distributions will be sourced from section 959(c)(3) E&P, to the extent thereof.

The forthcoming regulations will also provide that reclassifications of PTEP pursuant to the application of section 959(a)(2) will be sourced first from section 965(a) PTEP, then section 965(b) PTEP, and then, under a last-in, first-out approach, pro rata from the remaining section 959(c)(2) PTEP groups in each annual PTEP account, starting from the most recent annual PTEP account.

These ordering rules are expected to simplify PTEP recordkeeping in the future because, once a foreign corporation distributes all of its section 965 PTEP, the foreign corporation and its U.S. shareholder(s) will have reduced the number of PTEP groups that need to be tracked. Absent the ordering rules described in the preceding paragraphs of this section 3.02, the last in, first out approach to PTEP distributions would trap annual PTEP accounts with section 965 PTEP behind subsequent annual PTEP accounts, requiring the section 965 PTEP to be tracked indefinitely. The ordering rules to be provided in forthcoming regulations are illustrated by an example in section 3.04 of this notice.

.03 Adjustments Due to an Income Inclusion in Excess of Current Earnings and Profits

A U.S. shareholder's income inclusion under section 951A is not subject to a limitation based on the E&P of its CFCs for the taxable year. Consequently, in a year in which the portion of a U.S. shareholder's GILTI inclusion amount allocated to a CFC under section 951A(f)(2) and proposed §1.951A-6(b)(2) exceeds the CFC's current E&P, the PTEP resulting by reason of section 951A(f)(1) and proposed §1.951A-6(b)(1) will exceed the CFC's current E&P and, in some cases, may exceed the CFC's accumulated E&P as well. Similarly, an income inclusion under section 951(a)(1)(A) by reason of section 965 is not subject to an E&P limitation. Further, while an inclusion under section 951(a)(1)(A) (other than by reason of section 965) with respect to a CFC

is generally subject to an E&P limitation under section 952(c)(1)(A), a U.S. shareholder's inclusion under section 951(a)(1)(A) with respect to the CFC can exceed its E&P if such CFC has a tested loss. See section 951A(c)(2)(B)(ii) and proposed §1.951A-6(d) (increasing a CFC's E&P by the amount of a tested loss solely for purposes of applying the E&P limitation of section 952(c)(1)(A)).

As noted in section 3.02 of this notice, the aggregate of the amounts of section 959(c)(1) PTEP, section 959(c)(2) PTEP, and section 959(c)(3) E&P of a foreign corporation must equal the amount of E&P of the foreign corporation. The forthcoming regulations under section 959 will provide that current E&P are first classified as section 959(c)(3) E&P and then section 959(c)(3) E&P are reclassified as section 959(c)(1) PTEP or section 959(c)(2) PTEP, as appropriate, in full, which may have the effect of creating or increasing a deficit in section 959(c)(3) E&P. For example, in a case in which the portion of a U.S. shareholder's GILTI inclusion amount allocated to a CFC under section 951A(f)(2) and proposed §1.951A-6(b)(2) exceeds the current E&P of the CFC, section 959(c)(3) E&P will first be increased by the CFC's current E&P and then decreased by the entire amount of the portion of the GILTI inclusion amount allocated to the CFC, possibly below zero, and section 959(c)(2) PTEP will be increased by the same amount. For a similar rule in the case in which a U.S. shareholder's inclusion under section 951(a) by reason of section 965(a) exceeds E&P, see proposed §1.965-2(d)(1).

Finally, in a case where a foreign corporation has a current-year deficit in E&P, that deficit will solely reduce the foreign corporation's section 959(c)(3) E&P without affecting the amount of its section 959(c)(1) PTEP or section 959(c)(2) PTEP.

.04 Examples

The rules described in sections 3.02 and 3.03 of this notice are illustrated in the following examples:

Example 1--(i) Facts. USP, a domestic corporation, wholly owns FC, a foreign corporation that has the U.S. dollar as its functional currency. Both USP and FC use the calendar year as their taxable year. Before 2018, the PTEP of FC was maintained in annual accounts. As of December 31, 2018, FC's \$300x of E&P (before taking into account distributions made or inclusions under section 951(a)(1)(B) in 2018) applicable to USP's interest in FC are classified under section 3.01 of this notice as follows:

Year	Section 959(c)(1)			Section 959(c)(2)				Section 959(c)(3)
	Reclassified Section 965(a) PTEP	Reclassified Section 965(b) PTEP	Section 951(a)(1)(B) PTEP	Section 965(a) PTEP	Section 965(b) PTEP	Section 951A PTEP	Section 951(a)(1)(A) PTEP	
2018						50x	30x	
2017				100x	50x			20x
2016			25x				25x	
Total		25x			255x			20x

In 2018, FC has an amount described in section 956(a) ("section 956(a) amount") of \$125x, without considering the application of section 959(a)(2). In 2019, FC earns \$25x of current E&P, and the amount of USP's income inclusion under section 951A(a) that is allocated to FC under section 951A(f)(2) and proposed §1.951A-6(b)(2) is \$20x. FC also makes a distribution of \$195x in 2019. In 2020, FC earns no current E&P, but FC makes a distribution of \$60x. For all years, the PTEP of FC in each PTEP group is described in a single section 904 category, and all section 959(c)(3) E&P of FC are described in a single section 904 category.

(ii) **Analysis--(A) 2018.** As of December 31, 2018, before considering FC's section 956(a) amount, FC has total section 959(c)(2) PTEP of \$255x. Under section 959(a)(2) and (f)(1), because FC's section 959(c)(2) PTEP exceeds its section 956(a) amount, USP does not include any amount in income under section 951(a)(1)(B). However, under section 959(c)(1)(A), \$125x of FC's section 959(c)(2) earnings must be reclassified as section 959(c)(1) PTEP. Under the rules described in section 3.02 of this notice, the reclassification is sourced first from section 965(a) PTEP and then from section 965(b) PTEP. Under the rules in section 3.01 of this notice, the reclassified PTEP remains in the 2017 annual PTEP account. Thus, in FC's 2017 annual PTEP account, FC's reclassified section 965(a) PTEP is increased by \$100x and its section 965(a) PTEP is decreased by \$100x. Additionally, FC's reclassified section 965(b) PTEP is increased by \$25x and its section 965(b) PTEP is decreased by \$25x. Accordingly, as of December 31, 2018, FC's E&P applicable to USP's interest in FC are classified under section 3.01 of this notice as follows:

Section 959(c)(1)	Section 959(c)(2)	

Year	Reclassified Section 965(a) PTEP	Reclassified Section 965(b) PTEP	Section 951(a)(1)(B) PTEP	Section 965(a) PTEP	Section 965(b) PTEP	Section 951A PTEP	Section 951(a)(1)(A) PTEP	Section 959(c)(3)
2018						50x	30x	20x
2017	100x	25x			25x			
2016			25x				25x	
Total	150x			130x				20x

(B) 2019--(1) Current year adjustments. During 2019, FC earns \$25x of current E&P, and the amount of USP's income inclusion under section 951A(a) that is allocated to FC under section 951A(f)(2) and proposed §1.951A-6(b)(2) is \$20x. Thus, before taking into account USP's income inclusions with respect to FC and any distributions by FC, FC's section 959(c)(3) E&P is initially increased by \$25x. As a result of USP's income inclusion under section 951A, FC's section 951A PTEP increases by \$20x and FC's section 959(c)(3) E&P is decreased by \$20x. Accordingly, as of December 31, 2019, FC's E&P (before taking into account distributions made in 2019) applicable to USP's interest in FC are classified under section 3.01 of this notice as follows:

Year	Section 959(c)(1)			Section 959(c)(2)				Section 959(c)(3)	
	Reclassified Section 965(a) PTEP	Reclassified Section 965(b) PTEP	Section 951(a)(1)(B) PTEP	Section 965(a) PTEP	Section 965(b) PTEP	Section 951A PTEP	Section 951(a)(1)(A) PTEP		
2019						20x		25x	
2018						50x	30x		
2017	100x	25x			25x				
2016			25x				25x		
Total	150x			150x					25x

(2) Distribution. FC's distribution of \$195x is from PTEP because the entire distribution would be a dividend under section 316(a) without regard to section 959 (that is, for purposes of section 316, at the end of 2019, FC has \$325x of E&P (without regard to the distribution), \$25x of which is current E&P). Under section 959(c), the distribution is first treated as attributable to section 959(c)(1) PTEP.

(i) Section 959(c)(1) PTEP. Under the rules described in section 3.02 of this notice, the distribution is first sourced from reclassified section 965(a) PTEP and then from reclassified section 965(b) PTEP, and then pro rata from the remaining PTEP groups that contain section 959(c)(1) PTEP under a last-in, first-out ("LIFO") approach. Thus, in FC's 2017 annual PTEP account, FC's reclassified section 965(a) PTEP is decreased by \$100x and its reclassified section 965(b) PTEP is decreased by \$25x. In FC's 2016 annual PTEP account, FC's section 951(a)(1)(B) PTEP is reduced by \$25x. Thus, of the distribution of \$195x, \$150x is treated as attributable to section 959(c)(1) PTEP (\$100x + \$25x + \$25x).

(ii) Section 959(c)(2) PTEP. After the section 959(c)(1) PTEP is exhausted, the remaining portion of the distribution (\$45x) is treated as attributable to section 959(c)(2) PTEP, to the extent thereof. Under the rules described in section 3.02 of this notice, distributions are first sourced from section 965(a) PTEP and then from section 965(b)

PTEP, and then pro rata from the remaining PTEP groups that contain section 959(c)(2) PTEP under a LIFO approach. Thus, in FC's 2017 annual PTEP account, FC's section 965(b) PTEP is decreased by \$25x. In FC's 2019 annual PTEP account, FC's section 951A PTEP is decreased by \$20x. Because the entire distribution has been accounted for, the remaining PTEP groups that contain section 959(c)(2) PTEP and FC's section 959(c)(3) E&P are not affected. Accordingly, as of December 31, 2019, FC's E&P applicable to USP's interest in FC are classified under section 3.01 of this notice as follows:

Year	Section 959(c)(1)			Section 959(c)(2)				Section 959(c)(3)
	Reclassified Section 965(a) PTEP	Reclassified Section 965(b) PTEP	Section 951(a)(1)(B) PTEP	Section 965(a) PTEP	Section 965(b) PTEP	Section 951A PTEP	Section 951(a)(1)(A) PTEP	
2019								25x
2018						50x	30x	
2017								
2016							25x	
Total						105x		

(C) 2020. FC's distribution of \$60x is from PTEP because the entire distribution would be a dividend under section 316(a) without regard to section 959 (that is, for purposes of section 316, at the end of 2020, FC has \$130x of E&P (without regard to the distribution), all which is accumulated E&P). Under section 959(c), the distribution is first treated as attributable to section 959(c)(1) PTEP; however, FC has no section 959(c)(1) PTEP. Additionally, FC has no section 965(a) PTEP or section 965(b) PTEP. Under the rules described in section 3.02 of this notice, the distribution is sourced pro rata from the remaining PTEP groups that contain section 959(c)(2) PTEP under a LIFO approach. Thus, in FC's 2018 annual PTEP account, FC's section 951A PTEP is decreased by \$37.5x ($\$60x \times \$50x/\$80x$) and its section 951(a)(1)(A) PTEP is decreased by \$22.5x ($\$60x \times \$30x/\$80x$). Because the entire distribution has been accounted for, the remaining PTEP groups that contain section 959(c)(2) PTEP and FC's section 959(c)(3) E&P are not affected. Accordingly, as of December 31, 2020, FC's E&P applicable to USP's interest in FC are classified under section 3.01 of this notice as follows:

Year	Section 959(c)(1)			Section 959(c)(2)				Section 959(c)(3)
	Reclassified Section 965(a) PTEP	Reclassified Section 965(b) PTEP	Section 951(a)(1)(B) PTEP	Section 965(a) PTEP	Section 965(b) PTEP	Section 951A PTEP	Section 951(a)(1)(A) PTEP	
2019								25x
2018						12.5x	7.5x	
2017								
2016							25x	
Total						45x		

Example 2. (i) Facts. USP, a domestic corporation, wholly owns FC, a foreign corporation that has the U.S. dollar as its functional currency. Both USP and FC use the calendar year as their taxable year. At the beginning of Year 1, FC has

accumulated E&P of \$50x, all of which is section 959(c)(3) E&P. In Year 1, FC has \$25x of current E&P and FC makes no distributions. Furthermore, in Year 1, USP's income inclusion under section 951A(a) that is allocated to FC under section 951A(f)(2) and proposed §1.951A-6(b)(2) is \$100x.

(ii) Analysis. Before taking into account USP's income inclusions with respect to FC in Year 1, FC's current E&P for Year 1 increase FC's section 959(c)(3) E&P by \$25x to \$75x (\$50x + \$25x). The \$100x of USP's income inclusion under section 951A(a) allocated to FC results in an increase of \$100x to FC's section 951A PTEP (resulting in a balance of \$100x) and a reduction of \$100x to FC's section 959(c)(3) E&P resulting in a deficit of \$25x (\$75x - \$100x). The sum of the amounts of FC's section 959(c)(1) PTEP (\$0x), section 959(c)(2) PTEP (\$100x), and section 959(c)(3) E&P (deficit of \$25x) equals the amount of FC's E&P (\$75x).

SECTION 4. APPLICABILITY DATE

It is expected that the forthcoming regulations will apply to taxable years of United States shareholders (and successors in interest) ending after December 14, 2018 and to taxable years of foreign corporations ending with or within such taxable years of United States shareholders. See section 7805(b)(1)(C). Before the issuance of the forthcoming regulations, a shareholder may rely on the rules described in section 3 of this notice if the shareholder and each person related to the shareholder under section 267(b) or 707(b) (each such person, a "related shareholder") apply the rules consistently with respect to PTEP of all foreign corporations in which the shareholder or related shareholder, as the case may be, owns stock for all taxable years beginning with the shareholder's or the related shareholder's taxable year that includes the taxable year end of any such foreign corporation to which section 965 applies.

SECTION 5. REQUEST FOR COMMENTS AND CONTACT INFORMATION

The Treasury Department and the IRS request comments on the rules described in this notice, including potential simplification of the rules described in section 3.02 of this notice through the establishment of multi-year PTEP accounts. The Treasury Department and the IRS also request comments concerning the following topics:

1. The extent to which basis created under section 961(c) should be treated as basis for purposes of determining tested income in applying section 951A;
2. The extent to which gain or loss, including foreign currency gain or loss, should be recognized by reason of distributions of PTEP. Additionally, the Treasury Department and the IRS request comments regarding a potential election pursuant to which the shareholder would agree to establish and maintain a multi-year section 951A PTEP group and not apply section 250(a)(2) to the extent such provision would otherwise be relevant in calculating its foreign currency gain or loss on a distribution of section 951A PTEP;
3. The application of sections 959 and 961 to domestic and foreign partnerships; and
4. Other guidance that should be issued under sections 959 and 961, including comments on the 2006 proposed regulations and the extent to which guidance in the 2006 proposed regulations should be incorporated into new proposed regulations.

Comments should be submitted by February 12, 2019. Comments may be submitted electronically via the Federal eRulemaking Portal at **www.regulations.gov** (type IRS-2018-0041 in the search field on the *regulations.gov* homepage to find this notice and submit comments). Written comments may be submitted to the Office of Associate Chief Counsel (International), Attention: Melinda E. Harvey, Internal Revenue Service, IR-4579, 1111 Constitution Avenue, NW, Washington, DC 20224.

Comments will be available for public inspection and copying.

The principal author of this notice is Melinda E. Harvey of the Office of Associate Chief Counsel (International). For further information regarding this notice, contact Ms. Harvey at (202) 317-6934 (not a toll-free number).