

paid foreign income taxes of \$10 on the dividend received from C Corporation, B Corporation distributes the balance of \$70 to A Corporation. After having paid foreign income taxes of \$5 on the dividend received from B Corporation, A Corporation distributes the balance of \$65 to N Corporation. The dividend so received by B Corporation, and in turn by A Corporation, is excluded from the gross income of such corporations under section 959(b) and § 1.959-2. Under paragraph (b) of this section N Corporation is not required to include in gross income the \$15 (\$10+\$5) of foreign income taxes which are paid by corporations B and A, respectively, in connection with the dividend so received and which are deemed paid by N Corporation under section 902(a) and paragraphs (b) and (c) of § 1.960-2.

[T.D. 7120, 36 FR 10856, June 4, 1971, as amended by T.D. 7481, 42 FR 20130, Apr. 18, 1977; T.D. 7649, 44 FR 60089, Oct. 18, 1979; T.D. 7843, 47 FR 50484, Nov. 8, 1982]

§ 1.960-4 Additional foreign tax credit in year of receipt of previously taxed earnings and profits.

(a) *Increase in section 904(a) limitation for the taxable year of exclusion*—(1) *In general.* The applicable limitation under section 904(a) for a taxpayer's taxable year (hereinafter in this section referred to as the "taxable year of exclusion") in which he receives an amount which is excluded from gross income under section 959(a)(1) and which is attributable to a controlled foreign corporation's earnings and profits in respect of which an amount was required to be included in the gross income of such taxpayer under section 951(a) for a taxable year (hereinafter in this section referred to as the "taxable year of inclusion") previous to the taxable year of exclusion shall be increased under section 960(b)(1) by the amount described in paragraph (b) of this section if the conditions described in subparagraph (2) of this paragraph are satisfied.

(2) *Conditions under which increase in limitation is allowed for the taxable year of exclusion.* The increase in limitation described in subparagraph (1) of this paragraph for the taxable year of exclusion shall be made only if the taxpayer—

(i) For the taxable year of inclusion either chose to claim a foreign tax credit as provided in section 901 or did

not pay or accrue any foreign income taxes,

(ii) Chooses to claim a foreign tax credit as provided in section 901 for the taxable year of exclusion, and

(iii) For the taxable year of exclusion pays, accrues, or is deemed to have paid foreign income taxes with respect to the amount, described in subparagraph (1) of this paragraph, which is excluded from his gross income for such year under section 959(a)(1).

(b) *Amount of increase in limitation for the taxable year of exclusion.* The amount of increase under section 960(b)(1) in the applicable limitation under section 904(a) for the taxable year of exclusion shall be—

(1) The amount by which the applicable section 904(a) limitation for the taxable year of inclusion was increased, determined as provided in paragraph (c) of this section, by reason of the inclusion of the amount in the taxpayer's income for such year under section 951(a), reduced by

(2) The amount of foreign income taxes allowed as a credit under section 901 for such taxable year of inclusion and which were allowable to such taxpayer solely by reason of the inclusion of such amount in his gross income under section 951(a), as determined under paragraph (d) of this section, and then by

(3) The additional reduction for such taxable year of inclusion arising by reason of increases in limitation under section 960(b)(1) for taxable years intervening between such taxable year of inclusion and such taxable year of exclusion, as determined under paragraph (e) of this section in respect of such inclusion under section 951(a),

except that the amount of increase determined under this paragraph for the taxable year of exclusion shall in no case exceed the amount of foreign income taxes paid, accrued, or deemed to be paid by such taxpayer for such taxable year of exclusion with respect to the amount, described in paragraph (a)(1) of this section, which is excluded from gross income for such year under section 959(a)(1).

(c) *Determination of increase in limitation for the taxable year of inclusion.* The amount of the increase in the applicable limitation under section 904(a) for

the taxable year of inclusion which arises by reason of the inclusion of the amount in gross income under section 951(a) shall be the amount of the applicable limitation under section 904(a) for such year reduced by the amount which would have been the applicable limitation under section 904(a) for such year if the amount had not been included in gross income for such year under section 951(a).

(d) *Determination of foreign income taxes allowed for taxable year of inclusion by reason of section 951(a) amount.* The amount of foreign income taxes allowed as a credit under section 901 for the taxable year of inclusion which were allowable solely by reason of the inclusion of the amount in gross income for such year under section 951(a) shall be the amount of foreign income taxes allowed as a credit under section 901 for such year reduced by the amount of foreign income taxes which would have been allowed as a credit under section 901 for such year if the amount had not been included in gross income for such year under section 951(a). For purposes of this paragraph, the term "foreign income taxes" includes foreign income taxes paid or accrued, and foreign income taxes deemed paid under section 902, section 904(d), and section 960(a), for the taxable year of inclusion.

(e) *Additional reduction for the taxable year of inclusion arising by reason of increases in limitation for intervening years.* The amount of increase in the applicable limitation under section 904(a) for the taxable year of inclusion shall also be reduced, after first deducting the foreign income taxes described in paragraph (b)(2) of this section, by any increases in limitation which arise under section 960(b)(1)—by reason of any earlier exclusions under section 959(a)(1) in respect of the same inclusion under section 951(a) for such taxable year of inclusion—for the first, second, third, fourth, etc., succeeding taxable years of exclusion, in that order, which follow such taxable year of inclusion and precede the taxable year of exclusion in respect of which the increase in limitation under section 960(b)(1) and paragraph (b) of this section is being determined. The amount of any increase in limitation which arises under section

960(b)(1) for any such succeeding taxable year of exclusion shall be the amount of foreign income taxes allowed as a credit under section 901 for each such taxable year reduced by the amount of foreign income taxes which would have been allowed as a credit under section 901 for each such year if the limitation for each such year were not increased under section 960(b)(1). For any such succeeding taxable year of exclusion for which the taxpayer does not choose to claim a foreign tax credit as provided in section 901, the same increase in limitation under section 960(b)(1) shall be treated as having been made, for purposes of this paragraph, which would have been made for such taxable year if the taxpayer had chosen to claim the foreign tax credit for such year.

(f) *Illustrations.* The application of this section may be illustrated by the following examples:

Example 1. Domestic corporation N owns all of the one class of stock of controlled foreign corporation A. Corporation A, after paying foreign income taxes of \$30, has earnings and profits for 1978 of \$70, all of which are attributable to an amount required under section 951(a) to be included in N Corporation's gross income for 1978. Both corporations use the calendar year as the taxable year. For 1979 and 1980, A Corporation has no earnings and profits attributable to an amount required to be included in N Corporation's gross income under section 951(a); for each such year it makes a distribution of \$35 (from its earnings and profits for 1978) from which a foreign income tax of \$6 is withheld. For each of 1978, 1979, and 1980, N Corporation derives taxable income of \$50 from sources within the United States and claims a foreign tax credit under section 901, determined by applying the overall limitation under section 904(a)(2).

The United States tax payable by N Corporation is determined as follows, assuming a corporate tax rate of 48 percent:

1978	
Taxable income of N Corporation:	
U.S. sources	\$50.00
Sources without the U.S.:	
Amount required to be included in N Corporation's gross income under section 951(a)	\$70.00

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	1978	
Foreign income taxes deemed paid by N Corporation under section 960(a)(1) and included in N Corporation's gross income under section 78 (\$30×\$70/\$70)	30.00	100.00
Total taxable income		150.00
U.S. tax payable for 1978:		
U.S. tax before credit (\$150×0.48)		72.00
Credit: Foreign income taxes of \$30, but not to exceed overall limitation of \$48 for 1978 (\$100/\$150×\$72)		30.00
U.S. tax payable		42.00
	1979	
Taxable income of N Corporation, consisting of income from U.S. sources	\$50.00	
U.S. tax before credit (\$50×0.48)		24.00
Section 904(a)(2) overall limitation for 1979:		
Limitation for 1979 before increase under section 960(b)(1) (\$24×\$0/\$50)		0
Plus: Increase in overall limitation for 1979 under section 960(b)(1):		
Amount by which 1978 overall limitation was increased by reason of inclusion in N Corporation's gross income under section 951(a) for 1978 (\$48 - [(\$50×0.48)×\$0/\$50])	\$48.00	
Less: Foreign income taxes allowed as a credit for 1978 which were allowable solely by reason of such section 951(a) inclusion (\$30 - \$0)		30.00
Balance		18.00
But: Such balance not to exceed foreign income taxes paid by N Corporation for 1979 with respect to \$35 distribution excluded under section 959(a)(1) (\$6 tax withheld)	6.00	6.00
Overall limitation for 1979		6.00
U.S. tax payable for 1979:		
U.S. tax before credit (\$50×0.48)		24.00
Credit: Foreign income taxes of \$6, but not to exceed overall limitation of \$6 for 1966		6.00
U.S. tax payable		18.00
	1980	
Taxable income of N Corporation, consisting of income from U.S. sources	\$50.00	
U.S. tax before credit (\$50×0.48)		24.00
Section 904(a)(2) overall limitation for 1980:		
Limitation for 1980 before increase under section 960(b)(1) (\$24×\$0/\$50)		0

	1980	
Plus: Increase in overall limitation for 1980 under section 960(b)(1):		
Amount by which 1978 overall limitation was increased by reason of inclusion in N Corporation's gross income under section 951(a) for 1978 (\$48 - [(\$50×0.48)×\$0/\$50])	\$48.00	
Less: Foreign income taxes allowed as a credit for 1978 which were allowable solely by reason of such section 951(a) inclusion (\$30 - \$0)		30.00
Tentative balance		18.00
Less: Increase in overall limitation under section 960(b)(1) for 1979 by reason of such section 951(a) inclusion		6.00
Balance		12.00
But: Such balance not to exceed foreign income taxes paid by N Corporation for 1980 with respect to \$35 distribution excluded under section 959(a)(1) (\$6 tax withheld)	6.00	6.00
Overall limitation for 1980		6.00
U.S. tax payable for 1980:		
U.S. tax before credit (\$50×0.48)		24.00
Credit: Foreign income taxes of \$6, but not to exceed overall limitation of \$6 for 1967		6.00
U.S. tax payable		18.00

Example 2. The facts for 1978, 1979, and 1980, are the same as in example 1, except that in 1977, to which the section 904(a)(2) overall limitation applies, N Corporation pays \$18 of foreign income taxes in excess of the overall limitation and that such excess is not absorbed as a carryback to 1975 or 1976 under section 904(c). Therefore, there is no increase under section 960(b)(1) in the overall limitation for 1979 or 1980 since the amount (\$48) by which the 1978 overall limitation was increased by reason of the inclusion in N Corporation's gross income for 1978 under section 951(a), less the foreign income taxes (\$48) allowed as a credit which were allowable solely by reason of such inclusion, is zero. The foreign income taxes so allowed as a credit for 1978 which were allowable solely by reason of such section 951(a) inclusion consist of the \$30 of foreign income taxes deemed paid for 1978 under section 960(a)(1) and the \$18 of foreign income taxes for 1977 carried over and deemed paid for 1978 under section 904(c).

Example 3. (a) Domestic corporation N owns all the one class of stock of controlled foreign corporation A, which in turn owns all the one class of stock of controlled foreign corporation B. All corporations use the calendar years as the taxable year. Corporation B, after paying foreign income taxes of \$30, has earnings and profits for 1978 of \$70, all of which is attributable to an amount required under section 951(a) to be included in N Corporation's gross income for 1978, and \$35 of

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which it distributes in such year to A Corporation. For 1978, A Corporation, after paying foreign income taxes of \$5 on such dividend from B Corporation, has total earnings and profits of \$30, all of which it distributes in such year to N Corporation, a foreign income tax of \$3 being withheld therefrom.

(b) For 1979, B Corporation has no earnings and profits, but distributes in such year to A Corporation the \$35 remaining of its earnings and profits for 1965. For 1979, A Corporation, after paying foreign income taxes of \$5 on such dividend from B Corporation, has total earnings and profits of \$30, all of which it distributes to N Corporation, a foreign income tax of \$3 being withheld therefrom.

(c) For each of 1978 and 1979, N Corporation has taxable income of \$100 from United States sources and claims a foreign tax credit under section 901, determined by applying the overall limitation under section 904(a)(2). The United States tax payable by N Corporation is determined as follows, assuming a corporate tax rate of 48 percent:

1978	
Taxable income of N Corporation:	
U.S. sources	\$100
Sources without the U.S.:	
Amount required to be included in N Corporation's gross income under section 951(a) with respect to B Corporation	\$70
Foreign income taxes deemed paid by N Corporation under section 960(a)(1) and included in N Corporation's gross income under section 78 (\$30×\$70/\$70)	30
	100
Total taxable income	200
U.S. tax payable for 1978:	
U.S. tax before credit (\$200×0.48)	96
Credit: Foreign income taxes of \$38 ((\$30×\$70/\$70)+\$3), but not to exceed overall limitation of \$48 (\$96×\$100/\$200)	38
	58
U.S. tax payable	58

1979	
Taxable income of N Corporation, consisting of income from U.S. sources	
	\$100
U.S. tax before credit (\$100×0.48)	48
Section 904(a)(2) overall limitation for 1979:	
Limitation for 1979 before increase under section 960(b)(1) (\$48×\$0/\$100)	0
Plus: Increase in overall limitation for 1979 under section 960(b)(1):	
Amount by which 1978 overall limitation was increased by reason of inclusion in N Corporation's gross income under section 951(a) for 1978 (\$48 - [(\$100×0.48)×\$0/\$100]) ...	\$48
Less: Foreign income taxes allowed as a credit for 1978 which were allowable solely by reason of such section 951(a) inclusion (\$38 - \$0)	38
	10
Balance	10

1979	
But: Such balance not to exceed foreign income taxes paid and deemed paid by N Corporation for 1979 with respect to \$30 distribution excluded under section 959(a)(1) ((\$5×\$30/\$30)+\$3)	
	8
	8
Overall limitation for 1979	8
U.S. tax payable for 1979:	
U.S. tax before credit (\$100×0.48)	48
Credit: Foreign income taxes of \$8 (\$3+\$5), but not to exceed overall limitation of \$8 for 1979	8
	8
U.S. tax payable	40

[T.D. 7120, 36 FR 10859, June 4, 1971, as amended by T.D. 7649, 44 FR 60089, Oct. 18, 1979]

§ 1.960-5 Credit for taxable year of inclusion binding for taxable year of exclusion.

(a) *Taxes not allowed as a deduction for taxable year of exclusion.* In the case of any taxpayer who—

(1) Chooses to claim a foreign tax credit as provided in section 901 for the taxable year for which he is required to include in gross income under section 951(a) an amount attributable to the earnings and profits of a controlled foreign corporation, and

(2) Does not choose to claim a foreign tax credit as provided in section 901 for a taxable year in which he receives an amount which is excluded from gross income under section 959(a)(1) and which is attributable to such earnings and profits of such controlled foreign corporation,

No deduction shall be allowed under section 164 for the taxable year of such exclusion for any foreign income taxes paid or accrued on or with respect to such excluded amount.

(b) *Illustration.* The application of this section may be illustrated by the following example:

Example. Domestic Corporation N owns all the one class of stock of controlled foreign corporation A. Both corporations use the calendar year as the taxable year. All of A Corporation's earnings and profits of \$80 for 1978 (after payment of foreign income taxes of \$20 on its total income of \$100 for such year) are attributable to amount required under section 951(a) to be included in N Corporation's gross income for 1978. For 1978, N Corporation chooses to claim a foreign tax credit for the \$20 of foreign income taxes which for such year are paid by A Corporation and deemed paid by N Corporation