

T.D. 8178

Treasury Decisions
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DEPARTMENT OF THE TREASURY
Internal Revenue Service

26 CFR Parts 1 and 602

53 FR 6770

Income Taxes; Passive Foreign Investment Companies

T.D. 8178

DATE: March 2, 1988

ACTION: Temporary regulations.

SUMMARY: This document contains temporary income tax regulations that provide guidance to passive foreign investment companies and their shareholders that are United States persons about the time, manner and other requirements for making certain elections. These elections were enacted by the Tax Reform Act of 1986. The text of the temporary regulations set forth in this document also serves as the text of the proposed regulations cross-referenced in the notice of proposed rulemaking in this issue of the Federal Register.

DATES:

DATE: Effective for taxable years beginning after December 31, 1986.

ADDRESSES:

FOR FURTHER INFORMATION CONTACT: Gayle E. Novig of the Office of the Associate Chief Counsel (International), within the Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue NW., Washington, DC 20224 (Attention: CC:LR:T) (CC:INTL-655-87) (202-634-5423, not a toll free number).

SUPPLEMENTARY INFORMATION:

Background

This document contains Temporary Income Tax Regulations (26 CFR Part 1) under sections 1291(d)(2), 1294, 1295, and 1297(b)(1) of the Internal Revenue Code of 1986. These provisions were added to the Internal Revenue Code of 1986 by section 1235 of the Tax Reform Act of 1986 (Pub. L. 99-514). The temporary regulations are effective for taxable years beginning after 1986. However, these regulations are not intended to address comprehensively the issues raised by sections 1291, 1294, 1295, and 1297 of the Code.

Need for Temporary Guidance

The temporary regulations provided by this document will remain in effect until superseded by final regulations on these elections. Passive foreign investment companies and their shareholders wishing to make the elections in this Treasury decision for their first taxable year beginning after 1986 have an immediate need for guidance with respect to the time and manner of making the elections. For this reason, it is impracticable to issue this Treasury decision with notice and public procedure under subsection (b) of section 553 of Title 5 of the United States Code or to issue the decision subject to the effective date limitation of subsection (d) of that section.

Explanation of Provisions

General

The Tax Reform Act of 1986 established special rules for the taxation of U.S. persons that are shareholders of passive foreign investment companies (PFICs). For taxable years beginning after December 31, 1986, a foreign corporation will be classified as a PFIC if either 75 percent or more of its gross income for the taxable year is passive, or 50 percent or more of the average value of its assets for the taxable year produce passive income or are held for the production of passive income. Subject to certain exceptions, passive income for these purposes generally is foreign personal holding company income as defined in section 954(c) of the Internal Revenue Code.

There are two types of PFICs. Absent an election to be treated as a qualified electing fund (QEF), a PFIC is considered a "nonqualified fund." U.S. persons that are shareholders of nonqualified funds are subject to special ordinary income treatment and a deferred tax amount upon disposition of the stock and receipt of certain distributions. If, however, a PFIC makes the election under section 1295 to be a QEF, its shareholders that are U.S. persons will be taxed currently on their respective shares of the QEF's earnings.

Statutory Provisions

Election to be a Qualified Electing Fund

A PFIC may make the election under section 1295 to be a QEF for any taxable year. To be effective for a particular taxable year, the election must be filed with the Internal Revenue Service Center in Philadelphia before the 15th day of the third month of the following taxable year. The election, once made, applies to the year for which first effective and all subsequent taxable years that the electing company is a PFIC. The election may be revoked only with the consent of the Secretary. In addition, to be a QEF, the PFIC must comply with requirements prescribed by the Secretary for determining its ordinary earnings and net capital gain for each taxable year, for reporting the U.S. ownership of its stock, and for other purposes necessary to carry out the objectives of the PFIC provisions.

QEF Shareholder Election to Recognize Gain

U.S. persons that are shareholders of a QEF are taxed under section 1293 on their pro rata shares of the QEF's annual ordinary earnings and net capital gain. If the QEF was a nonqualified fund in a prior taxable year included in the shareholder's holding period, the U.S. person also may be taxable under section 1291 on dispositions of the QEF stock and receipt of certain distributions. To limit the shareholder's taxation to section 1293, the shareholder may make the election under section 1291(d) (2) to mark the stock to market as of the first day of the QEF's first taxable year as a QEF. A U.S. person making this election is deemed to have sold the stock held in the QEF on that day for its fair market value. The deemed sale is taxable as a disposition subject to the special tax rules of section 1291. Gain, but not loss, realized on the deemed sale will be recognized. The shareholder's basis in the stock will be adjusted for any gain recognized, and the shareholder's holding period shall thereafter be treated as beginning on the date of the deemed sale. Thereafter, the shareholder will be taxable only under section 1293 with respect to the subsequent earnings derived from the investment in the QEF.

Election to Extend Time for Payment of Tax

The U.S. investor in a QEF is currently taxed on the undistributed earnings of the QEF; however, section 1294 enables the shareholder to elect annually to defer payment of the tax on those earnings, subject to an interest charge. The electing shareholder may terminate the election at any time by paying the tax and interest due. Otherwise, the election automatically terminates upon the occurrence of an event described in section 1294(c).

Election to Purge Stock of PFIC Taint

If, in a particular taxable year, a shareholder owns stock in a foreign corporation which qualifies as a PFIC under section 1296, the stock will retain its character as PFIC stock in subsequent taxable years unless the PFIC is a QEF for the shareholder's entire holding period. An election is available under section 1297(b)(1), however, which allows a shareholder to purge the PFIC taint attributable to stock of a corporation that was a PFIC but no longer qualifies as such under the passive income or passive

asset test of section 1296 (former PFIC). Unless the election is made, the shareholder will continue to be taxable pursuant to section 1291 even after the corporation ceases to meet the PFIC definitional test of section 1296. The election effects a deemed sale of the stock and only applies in circumstances in which the PFIC was not a qualified electing fund at some time during the electing shareholder's holding period. The electing shareholder is treated as having sold the stock in the former PFIC on the last day of the former PFIC's last taxable year during which it met the PFIC definitional test. The deemed sale is treated as a disposition for purposes of section 1291 and, therefore, is subject to the deferred tax amount defined in section 1291(c).

Explanation of Temporary Regulations

The temporary regulations provide the time, manner and other requirements for making the elections under sections 1291(d)(2), 1294, 1295, and 1297(b)(1).

Election to be a Qualified Electing Fund

Section 1.1295-1T of the temporary regulations prescribes the time and manner for making the QEF election and the requirements for continued QEF qualification. The temporary regulations provide that the PFIC must file its QEF election with the Philadelphia Service Center before the 15th day of the third month following the taxable year for which the election is made. The temporary regulations permit a PFIC whose post-1986 short taxable year ended before December 31, 1987 to make the election any time before March 15, 1988. The QEF election will not be available to PFICs with any bearer shares. As part of the election, the PFIC must provide certain information, including the total ordinary earnings and net capital gain for the year of the election and, in certain cases, the fair market of a share of its stock as of the first day of the election year. However, any PFIC which must file its election statement before May 15, 1988, will be able to amend and supplement the information provided in its election statement as well as extend the time to satisfy the other election requirements in § 1.1295-1T(b) described below by June 15, 1988.

The temporary regulations also require the PFIC to notify its shareholders of the daily amount of ordinary earnings and net capital gain of the PFIC deemed earned on a share of stock during the taxable year. However, if the number of outstanding shares of stock in the PFIC changed at any time during the year, the PFIC must provide the shareholders a schedule of the per share amounts of ordinary earnings and net capital gain of the PFIC for each day during the taxable year. The PFIC must send the shareholder notification and request for certification by the 15th day of the third month following each taxable year to which the election applies. However, the date for sending shareholder notification and request for certification statements is extended until June 15, 1988 for elections filed before March 15, 1988 under § 1.1295-1T(b)(1)(iii) of the temporary regulations.

The shareholder notification and certification statement will require certain shareholders of record that hold the stock for their own benefit to complete the certification statement and return it to the PFIC. The shareholder notification and request for certification statement also will advise certain types of shareholders of record to notify their owners, or the persons on whose behalf they hold the stock, of their pro rata shares of the earnings of the PFIC. These shareholders also must be advised to request the indirect owners to report their status as U.S. persons to the PFIC. Only U.S. persons that are direct or indirect shareholders of the PFIC are required to certify their status to the PFIC. The temporary regulations provide that failure of a shareholder to comply with the request for certification will not invalidate the QEF election.

The temporary regulations require the QEF to provide the Internal Revenue Service, by the 15th day of the ninth month following each taxable year to which the election applies, the names, addresses and taxpayer identification numbers of U.S. persons obtained through certification, and their pro rata shares of the ordinary earnings and net capital gain. For taxable years after the year of the election, this information will be required as part of the annual report to be filed by the QEF by the 15th day of the ninth month following each year to which the election applies. The annual report will be similar to the election statement.

The temporary regulations also require a QEF to amend the earnings information filed with the Internal Revenue Service and sent to its shareholders at any time that a recalculation of the ordinary earnings and net capital gain of the QEF is necessary.

The temporary regulations under § 1.1295-IT(b)(3) require the QEF to appoint a person resident in the United States as the QEF's authorized representative in the United States for tax administrative purposes. Section 1.1295-1T(b)(4) requires the QEF to maintain permanent books of account, records and other documents that are necessary to verify the reported amounts of ordinary income and capital gain, to maintain ledgers of all shareholders of record for each year to which the election applies, to keep copies of such documents in the United States, and to make the documents available for inspection by Internal Revenue Service personnel.

Section 1.1295-IT(b)(9) provides that if the electing corporation was a nonqualified fund during a post-1986 taxable year prior to the taxable year for which the section 1295 election is made, it must determine, for purposes of the shareholder election under section 1291(d)(2), the fair market value of its stock on the first day of its first taxable year as a QEF (the valuation date) according to the rules specified in § 1.1295-IT(b)(9) (i), and (ii). This requirement does not apply to a foreign corporation that makes the election for its first taxable year during which it qualifies as a PFIC. A PFIC required to make the fair market value determination must provide this information to those persons that were its shareholders on the valuation date.

The section 1295 election may be revoked by the PFIC but only with the consent of the Commissioner. The Commissioner's determination will take into account the enactment of technical corrections to the Tax Reform Act of 1986 after the PFIC made the election, as well as provisions of PFIC regulations, published after the PFIC made the election.

QEF Shareholder Election to Recognize Gain.

Section 1.1291-10T specifies the time and manner for making the election under section 1291(d)(2) of the Code to treat the stock of a PFIC as sold on the first day on which the PFIC is a QEF. This election only applies to a U.S. person that held such stock in the QEF when it was a nonqualified fund. The election may be made by a shareholder that may realize either a gain or a loss on the deemed sale (although the loss will not be recognized). Section 1.1291-10T(c) provides that the shareholder may make the election only with respect to the taxable year that includes the first day of the QEF's first taxable year as a QEF. Section 1.1291-10T(d) provides that, in order to make the election under section 1291(d)(2), the shareholder generally must pay the tax arising under section 1291 by the due date (determined without extensions) of the return for the shareholder's taxable year that includes the first day of the QEF's first taxable year as a QEF. If the shareholder files the election after the due date, the electing shareholder will have to pay the tax on the gain included in income, the deferred tax amount, and the interest for the underpayment of tax pursuant to section 6601.

The temporary regulations provide rules for direct shareholders making the election under section 1291(d)(2). Guidance for indirect shareholders wishing to make the election will be provided at a later time.

Election to Extend Time for Payment of Tax

Section 1.1294-1T specifies the time and manner for making the annual election under section 1294 to extend the time for payment of the tax liability which is attributable to the undistributed earnings of the QEF, included in income under section 1293, for the taxable year of the QEF that ended during the taxable year of the shareholder. The tax liability is defined in § 1.1294-1T(f) as the excess of the tax imposed under chapter 1 of the Code for the taxable year over the tax that would be imposed for the taxable year without regard to the inclusion in income under section 1293 of undistributed earnings. The electing shareholder will be required to state in the section 1294 election the amount or ordinary earnings and net capital gain of the QEF included in the income of the shareholder for the year and the amount of the tax liability, payment of which is being deferred by reason of the election under section 1294. An extension of time to pay tax terminates upon the occurrence of any of the events listed in § 1.1294-1T(e). These events include receipt of earnings to which the election is attributable, transfer or pledge of the stock with respect to the stock with respect to which the section 1294 election applies, a loan, pledge or guarantee by the QEF to the electing shareholder or to a person related to the shareholder, cessation of the QEF's status as a QEF or as a PFIC, or a determination by the District Director pursuant to section 1294(c)(3) that collection of the tax is in jeopardy.

83Election to Purge Stock of PFIC Taint

11Section 1.1297-3T provides the time and manner for making the election under section 1297(b)(1) of the Code to treat the PFIC stock as sold on the last day of the last taxable year during which it was a PFIC. Thereafter, the foreign corporation will not be treated as a PFIC in the hands of the shareholder. The shareholder makes the election by filing an amended tax return within three years after the due date, as extended, of the shareholder's tax return for the taxable year that includes the date of the deemed sale. The shareholder must describe in the election the manner in which the former PFIC lost the characteristics of a PFIC. The electing shareholder will be liable for interest for underpayment of tax for the year of the deemed sale.

11The temporary regulations provide rules for direct shareholders making the election under section 1297(b)(1). Guidance for indirect shareholders wishing to make the election will be provided at a later time.

84Special Analyses

11It has been determined that this temporary regulation is not a major rule as defined in Executive Order 12291. Therefore, a Regulatory Impact Analysis is not required. A general notice of proposed rule is not required by 5 U.S.C. 553 for temporary regulations. Accordingly, the temporary regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6).

84Paperwork Reduction Act

11The collection of information requirements contained in this regulation have been submitted to the Office of Management and Budget (OMB) in accordance with the requirements of the Paperwork Reduction Act of 1980. These requirements have been approved by OMB under control number 1545-1028.

Drafting Information

The principal author of these temporary regulations is Gayle E. Novig of the Office of the Associate Chief Counsel (International), within the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, on matters of both substance and style.

List of Subjects

26 CFR 1.1201-1 Through 1.1297-1

Income taxes, Capital gains and losses, Recapture and passive foreign investment companies.

26 CFR Part 602

Reporting and recordkeeping requirements.

Adoption of Amendments to the Regulations

Accordingly, 26 CFR Part 1 is amended as follows:

Income Tax Regulations

Paragraph 1. The authority for 26 CFR Part 1 continues to read in part:

Authority: 26 U.S.C. 7805. * * * Sections 1.1291-10T, 1.1294-1T, 1.1295-1T, and 1.1297-3T also issued, respectively, under the authority of 26 U.S.C. 1291(d)(2), 1294, 1295, and 1297(b)(1).

Par. 2. New §§ 1.1291-0T, 1.1291-0T, 1.1294-1T, 1.1295-1T, and 1.1297-3T are added immediately following § 1.1287-1.

The added sections read as follows:

§ 1.1291-0T Passive Foreign Investment Companies. Table of contents (Temporary).

§ 1.1291-0T Election by a United States person to recognize gain in a qualified electing fund

(a) Purpose and scope

(b) Election to recognize gain

(1) In general

(2) Qualification date

(3) Exception

(c) Time for making the election

(d) Manner of making the election

(1) In general

(2) Information to be included in the election

(e) Adjustment to basis; treatment of holding period

§ 1.1294-1T Election to extend the time for payment of tax on undistributed earnings of a qualified electing fund

(a) Purpose and scope

(b) Election to extend time for payment of tax

(1) In general

(2) Exception

(3) Undistributed earnings

(i) In general

(ii) Effect of loan, pledge or guarantee

(c) Time for making the election

(1) In general

(2) Exception

(d) Manner of making the election

(1) In general

(2) Information to be included in the election

(e) Termination of the extension

(f) Undistributed PFIC earnings tax liability

(g) Authority to require a bond

(h) Annual reporting requirement

§ 1.1295-1T Election by a passive foreign investment company to be a qualified electing fund

(a) In general

(b) Election requirements

(1) Time for making the election

(i) In general

(ii) Exception for elections for post-1986 years ended before 12/31/87

(iii) Curing an election made before 5/15/88

(2) Manner of making the election

(i) In general

(ii) Information to be included in the election statement

(3) Appointment of U.S. agent

(4) Books and records

(5) Annual shareholder notification and request for certification of U.S. ownership

(i) In general

(ii) The notification of PFIC information and request for shareholder certification

(6) Annual reporting by the PFIC to the Internal Revenue Service

(7) Amendment of earnings information

(8) Taxpayer identification number

(9) Fair market value determination by certain companies

(i) Companies other than open-end investment companies

(ii) Open-end investment companies

(c) Revocability of election

(1) In general

(2) Failure to obtain shareholder certification

§ 1.1297-3T Deemed sale election by a United States person that is a shareholder of a passive foreign investment company

(i) In general

(b) Time and manner for making the election

(1) In general

(2) Information to be included in the election

(3) Adjustment to basis; treatment of holding period

§ 1.1291-10T Election by a United States person to recognize gain in a qualified electing fund (Temporary).

(a) *Purpose and scope.* This section provides rules for making the election under section 1291(d)(2). Under that section, a U.S. person may elect to recognize gain with respect to stock in a qualified electing fund (QEF) held on the first day of the QEF's first taxable year during which it is a QEF. In general, a QEF is a foreign corporation that is a passive foreign investment company (PFIC), as defined in section 1296, and that has made the election under section 1295. For rules concerning the election by a PFIC under section 1295, see § 1.1295-1T.

(b) *Election to recognize gain -- (1) In general.* A U.S. person may elect to recognize gain under the provisions of this § 1.1291-10T if such person was a shareholder of a QEF on the qualification date. A person that makes such an election shall be treated as having sold on the qualification date for its fair market value stock of the QEF that the person held on that date. The deemed sale is taxed as a disposition pursuant to section 1291. Under that section, the gain is considered earned pro rata over the shareholder's holding period in the stock, and is taxed as ordinary income. The tax on the gain attributable to post-1986 taxable years during which the corporation is a PFIC is based on the value of tax deferral and includes an interest charge. An election may be made by a shareholder that would realize a loss on the deemed sale. Any loss realized on the deemed sale may not be recognized.

(2) *Qualification date.* The qualification date with respect to any shareholder of a QEF is the first day of the QEF's first taxable year as a QEF.

(3) *Exception.* This election does not pertain to a shareholder that held stock in a PFIC which was a QEF for all of the PFIC's taxable years beginning after 1986 during which it qualified as a PFIC and that are included in whole or in part in the shareholder's holding period. See section 1291(d)(1).

(c) *Time for making the election.* Except as provided below, an election under this § 1.1291-10T must be made with the filing of the electing shareholder's tax return for the taxable year which includes the qualification date. The election may be made by filing an amended tax return within three years of the due date, as extended, for the shareholder's tax return for the taxable year which includes the qualification date.

(d) *Manner of making the election -- (1) In general.* The election shall be made by filing Form 8621 or a statement containing the information and representations required by paragraph (d)(2) of this section, reporting the gain on the income tax return as required by section 1291(a)(2), and by paying the tax on the gain as required by section 1291 (including the payment of the deferred tax amount required under sections 1291(a)(1)(C) and 1291(c)). The electing shareholder that makes the election under this section after the due date of the return (determined without extensions) shall pay interest, pursuant to section 6601, on the underpayment of tax for the taxable year that includes the qualification date.

(2) *Information to be included in the election.* If a statement is used in lieu of Form 8621, the statement should be identified, in a heading, as an election under section 1291(d)(2). The statement must contain the following information and representations:

(i) The name, address and taxpayer identification number of the electing shareholder;

(ii) The name, address and taxpayer identification number of the QEF, the stock of which is the subject of the election;

(iii) A statement that the shareholder is making the election under section 1291(d)(2);

(iv) A representation that the person making the election was a shareholder in the QEF on the qualification date;

(v) The qualification date;

(vi) A schedule of the shares held by the electing shareholder in the QEF on the qualification date, listing the date(s) of acquisition, the number of shares acquired on each date listed, and the electing shareholder's tax basis in each of those shares;

(vii) The fair market value of the stock in the QEF as of the qualification date, as provided to the electing shareholder by the QEF pursuant to § 1.1291-1T(b)(5); and

(viii) A schedule showing the computation of the gain recognized on the deemed sale, and the calculation of the deferred tax amount, as defined in section 1291(c).

(e) *Adjustment to basis; treatment of holding period.* An electing shareholder that recognizes gain on the deemed sale shall increase its adjusted basis in the stock by the amount of gain recognized. An electing shareholder shall not adjust the basis in stock with respect to which the shareholder realized a loss on the deemed sale. An electing shareholder thereafter shall treat its holding period in the stock, for purposes of sections 1291 through 1297, as beginning on the qualification date without regard to whether it recognized gain on the deemed sale; for purposes of section 1223, the holding period in the stock in the QEF shall include the period prior to the deemed sale.

§ 1.1294-1T Election to extend the time for payment of tax on undistributed earnings of a qualified electing fund (Temporary).

(a) *Purpose and scope.* This section provides rules for making the annual election under section 1294. Under that section, a U.S. person that is a shareholder in a qualified electing fund (QEF) may elect to extend the time for payment of its tax liability which is attributable to its share of the undistributed earnings of the QEF. In general, a QEF is a passive foreign investment company (PFIC), as defined in section 1296, that makes the election under section 1295. Under section 1293, a U.S. person that owns, or is treated as owning, stock of a QEF at any time during the taxable year of the QEF shall include in gross income, as ordinary income, its pro rata share of the ordinary earnings of the QEF for the taxable year and, as long-term capital gain, its pro rata share of the net capital gain of the QEF for the taxable year. The shareholder's taxable year in which or with which the taxable year of the QEF ends.

(b) *Election to extend time for payment -- (1) In general.* A U.S. person that is a shareholder of a QEF on the last day of the QEF's taxable year may elect under section 1294 to extend the time for payment of that portion of its tax liability which is attributable to the inclusion in income pursuant to section 1293 of the shareholder's share of the QEF's undistributed earnings. The election under section 1294 may be made only with respect to undistributed earnings, and interest is imposed under section 6601 on the amount of the tax liability which is subject to the extension. This interest must be paid on the termination of the election.

(2) *Exception.* An election under this § 1.1294-1T cannot be made for a taxable year of the shareholder if any portion of the QEF's earnings is includible in the gross income of the shareholder for such year under either section 551 (relating to foreign personal holding companies) or section 951 (relating to controlled foreign corporations).

(3) *Undistributed earnings -- (i) In general.* For purposes of this § 1.1294-1T the term "undistributed earnings" means the excess, if any, of the amount includible in gross income by reason of section 1293 (a) for the shareholder's taxable year (the includible amount) over the sum of (A) the amount of any distribution to the shareholder during the QEF's taxable year and (B) the portion of the includible amount that is attributable to stock in the QEF that the shareholder transferred or otherwise disposed of before the end of the QEF's year. For purposes of this paragraph, a distribution will be treated as made from the most recently accumulated earnings and profits.

(ii) *Effect of a loan, pledge or guarantee.* A loan, pledge, or guarantee described in § 1.1294-1T(e) (2) or (4) will be treated as a distribution of earnings for purposes of paragraph (b)(3)(i)(A). If earnings are treated as distributed in a taxable year by reason of a loan, pledge or guarantee described in § 1.1294-1T(e) (2) or (4), but the amount of the deemed distribution resulting therefrom was less than the amount of the actual loan by the QEF (or the amount of the loan secured by the pledge or guarantee), earnings derived by the QEF in a subsequent taxable year will be treated as distributed in

such subsequent year to the shareholder for purposes of paragraph (b)(3)(i)(A) by virtue of such loan, but only to the extent of the difference between the outstanding principal balance on the loan in such subsequent year and the prior years' deemed distributions resulting from the loan. For this purpose, the outstanding principal balance on a loan in a taxable year shall be treated as equal to the greatest amount of the outstanding balance at any time during such year.

Example (1). (i) *Facts.* FC is a PFIC that made the election under section 1295 to be a QEF for its taxable year beginning January 1, 1987. S owned 500 shares, or 50 percent, of FC throughout the first six months of 1987, but on June 30, 1987 sold 10 percent, or 50 shares, of the FC stock that it held. FC had \$100,000x of ordinary earnings but no net capital gain in 1987. No part of FC's earnings in 1987 is includible in S's income under either section 551 or 951. FC made no distributions to its shareholders in 1987. S's pro rata share of income is determined by attributing FC's income ratably to each day in FC's year. Accordingly, FC's daily earnings are \$274x (\$100,000x/365). S's share of the earnings of FC is \$47,484x, determined as follows.

FC's daily earnings X number of days percentage held by S X percentage of ownership in FC.

Accordingly, S's pro rata share of FC's earnings for the first six months of FC's year deemed earned while S held 50 percent of FC's stock is \$24,797x (\$274x X 181 days X 50%). S's pro rata share of FC's earnings for remainder of FC's year deemed earned while S held 45 percent of FC's stock is \$22,687x (\$274x X 184 days X 45%). Therefore, S's total share of FC's earnings to be included in income under section 1293 is \$47,484x (\$24,797x + \$22,687x).

(ii) *Election.* S intends to make the election under section 1294 to defer the payment of its tax liability that is attributable to the undistributed earnings of FC. The amount of current year undistributed earnings as defined in § 1.1294-1T(b)(3) with respect to which S can make the election is the excess of S's inclusion in gross income under section 1293(a) for the taxable year over the sum of (1) the cash and other property distributed to S during FC's tax year out of earnings included in income pursuant to section 1293(a), and (2) the earnings attributable to stock disposed of during FC's tax year. Because S sold 10 percent, or 50 shares, of the FC stock that it held during the first six months of the year, 10 percent of its share of the earnings for that part of the year, which is \$2,480x (\$24,797x X 10%), is attributable to the shares sold. S therefore cannot make the election under section 1294 to extend the time for payment of its tax liability on that amount. Accordingly, S can make the election under section 1294 with respect to its tax on \$45,004x (\$47,484x less \$2,480x), which is its pro rata share of FC's earnings, reduced by the earnings attributable to the stock disposed of during the year.

Example (2). (i) *Facts.* The facts are the same as in Example (1) with the following exceptions. S did not sell any FC stock during 1987. Therefore, because S held 50 percent of the FC stock throughout 1987, S's pro rata share of FC's ordinary earnings was \$50,000x, no part of which was includible in S's income under either section 551 or 951. There were no actual distributions of earnings to S in 1988. On December 31, 1987, S pledged the FC stock as security for a bank loan of \$75,000x. The pledge is treated as a disposition of the FC stock and therefore a distribution of S's share of the undistributed earnings of FC up to the amount of the loan principal. S's entire share of the undistributed earnings of FC are deemed distributed as a result of the pledge of the FC stock. S therefore cannot make the election under section 1294 to extend the time for payment of its tax liability on its share of FC's earnings for 1987.

(ii) *Deemed distribution.* In 1988, FC has ordinary earnings of \$100,000x but no net capital gain. S's pro rata share of FC's 1988 ordinary earnings was \$50,000x. S's loan remained outstanding throughout 1988; the highest loan balance during 1988 was \$74,000x. Of S's share of the ordinary earnings of FC of \$50,000x, \$24,000x is deemed distributed to S. This is the amount by which the highest loan balance for the year (\$74,000x) exceeds the portion of the undistributed earnings of FC deemed distributed to S in 1987 by reason of the pledge (\$50,000x). S may make the election under section 1294 to extend the time for payment of its tax liability of \$26,000x, which is the amount by which S's includible amount for 1988 exceeds the amount deemed distributed to S during 1988.

(c) *Time for making the election -- (1) In general.* An election under this § 1.1294-1T may be made for any taxable year in which a shareholder reports income pursuant to section 1293. Except as provided

in paragraph (c)(2), the election shall be made by the due date, as extended, of the tax return for the shareholder's taxable year for which the election is made.

(2) *Exception.* An election under this section may be made within 60 days of receipt of notification from the QEF of the shareholder's pro rata share of the ordinary earnings and net capital gain if notification is received after the time for filing the election provided in paragraph (c)(1) (and requires the filing of an amended return to report income pursuant to section 1293). If the notification reports an increase in the shareholder's pro rata share of the earnings previously reported to the shareholder by the QEF, the shareholder may make the election under this paragraph (c)(2) only with respect to the amount of such increase.

(d) *Manner of making the election -- (1) In general.* A shareholder shall make the election by (i) attaching to its return for the year of the election Form 8621 or a statement containing the information and representations required by this section and (ii) filing a copy of Form 8621 or the statement with the Internal Revenue Service Center, P.O. Box 21086, Philadelphia, Pennsylvania 19114.

(2) *Information to be included in the election statement.* If a statement is used in lieu of Form 8621, the statement should be identified, in a heading, as an election under section 1294 of the Code. The statement must include the following information and representations:

(i) The name, address, and taxpayer identification number of the electing shareholder and the taxable year of the shareholder for which the election is being made;

(ii) The name, address and taxpayer identification number of the QEF if provided to the shareholder;

(iii) A statement that the shareholder is making the election under section 1294 of the Code;

(iv) A schedule containing the following information:

(A) The ordinary earnings and net capital gain for the current year included in the shareholder's income under section 1293;

(B) The amount of cash and other property distributed by the QEF during its taxable year with respect to stock held directly or indirectly by the shareholder during that year, identifying the amount of such distributions that is paid out of current earnings and profits and the amount paid out of each prior year's earnings and profits; and

(C) The undistributed PFIC earnings tax liability (as defined in paragraph (f) of this section) for the taxable year, payment of which is being deferred by reason of the election under section 1294;

(v) The number of shares of stock held in the QEF during the QEF's taxable year which gave rise to the section 1293 inclusion and the number of such shares transferred, deemed transferred or otherwise disposed of by the electing shareholder before the end of the QEF's taxable year, and the data of transfer; and

(vi) The representations of the electing shareholder that --

(A) No part of the QEF's earnings for the taxable year is includible in the electing shareholder's gross income under either section 551 or 951 of the Code;

(B) The election is made only with respect to the shareholder's pro rata share of the undistributed earnings of the QEF; and

(C) The electing shareholder, upon termination of the election to extend the date for payment, shall pay the undistributed PFIC earnings tax liability attributable to those earnings to which the termination applies as well as interest on such tax liability pursuant to section 6601. Payment of this tax and interest must be made by the due date (determined without extensions) of the tax return for the taxable year in which the termination occurs.

(e) *Termination of the extension.* The election to extend the date for payment of tax will be terminated

in whole or in part upon the occurrence of any of the following events:

- (1) The QEF's distribution of earnings to which the section 1294 extension to pay tax is attributable; the extension will terminate only with respect to the tax attributable to the earnings that were distributed.
- (2) The electing shareholder's transfer of stock in the QEF (or use thereof as security for a loan) with respect to which an election under this § 1.1294-1T was made. The election will be terminated with respect to the undistributed earnings attributable to the shares of the stock transferred. In the case of a pledge of the stock, the election will be terminated with respect to undistributed earnings equal to the amount of the loan for which the stock is pledged. ings -Folios: 414-146 -Date: 2-29-88 - Subformat:
- (3) Revocation of the QEF's election as a QEF or cessation of the QEF's status as a PFIC. A revocation of the QEF election or cessation of PFIC status will result in the complete termination of the extension.
- (4) A loan of property by the QEF directly or indirectly to the electing shareholder or related person, or a pledge or guarantee by the QEF with respect to a loan made by another party to the electing shareholder or related person. The election will be terminated with respect to undistributed earnings in an amount equal to the amount of the loan, pledge, or guarantee.
- (5) A determination by the District Director pursuant to section 1294(c)(3) that collection of the tax is in jeopardy. The amount of undistributed earnings with respect to which the extension is terminated under this paragraph (d)(5) will be left to the discretion of the District Director.
- (f) *Undistributed PFIC earnings tax liability.* The electing shareholder's tax liability attributable to the ordinary earnings and net capital gain included in gross income under section 1293 shall be the excess of the tax imposed under chapter 1 of the Code for the taxable year over the tax that would be imposed for the taxable year without regard to the inclusion in income under section 1293 of the undistributed earnings as defined in paragraph (b)(3) of this section.

Example. The facts are the same as in § 1.1294-1T (b)(3), *Example (1)*, with the following exceptions. S, a domestic corporation, did not dispose of any FC stock in 1987. Therefore, because S held 50 percent of the FC stock throughout 1987, S's pro rata share of FC's ordinary earnings was \$50,000x. In addition to \$50,000x of ordinary earnings from FC, S had \$12,500x of domestic source income and \$6,000x of expenses (other than interest expense) not definitely related to any gross income. These expenses are apportioned, pursuant to § 1.861-8(c)(2), on a pro rata basis between the domestic and foreign source income -- \$1,200x of expenses, or one-fifth, to domestic source income, and \$4,800x of expenses, or four-fifths, to the section 1293 inclusion. FC paid foreign taxes of \$25,000x in 1987. Accordingly, S is entitled to claim as an indirect foreign tax credit pursuant to section 1293(f) a proportionate amount of the foreign taxes paid by FC, which is \$12,500x (\$25,000x x \$50,000x/\$100,000x). S is taxed in the U.S. at the rate of 34 percent. The amount of tax liability for which S may extend the time for payment is determined as follows:

1987 Tax Liability (With Section 1293 Inclusion)

Source	U.S.	Foreign
Income	12,500x	0
Section 1293	0	50,000x
Expenses	-1,200x	-4,800x
Taxable income	11,300x	45,200x
Total taxable income	56,500x	
U.S. income tax rate	x34%	
Pre-credit U.S. tax	19,210x	
Foreign tax credit	-12,500x	
1987 Tax Liability	6,710x Dx	

1987 Tax Liability (Without Section 1293 Inclusion)

Source	U.S.	Foreign
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Income	12,500x	0
Expenses	-6,000x	
Taxable income	6,500x	
U.S. tax rate	x34%	
U.S. Tax	2,210x	
Foreign tax credit	0	
Hypothetical 1987 Tax Liability	2,210x	

The amount of tax, payment of which *S* may defer pursuant to section 1294, is \$4,500x (\$6,710x less \$2,210x).

(g) *Authority to require a bond.* Pursuant to the authority granted in section 6165 and in the manner provided therein, and subject to notification, the District Director may require the electing shareholder to furnish a bond to secure payment of the tax, the time for payment of which is extended under this section. If the electing shareholder does not furnish the bond within 60 days after receiving a request from the District Director, the election will be revoked.

(h) *Annual reporting requirement.* The electing shareholder must attach Form 8621 or a statement to its income tax return for each year during which an election under this section is outstanding. The statement must contain the following information: (1) The total amount of undistributed earnings as of the end of the taxable year to which the outstanding elections apply; (2) the total amount of the undistributed PFIC earnings tax liability and accrued interest charge as of the end of the year; (3) the total amount of distributions received during the taxable year; and (4) a description of the occurrence of any other termination event described in paragraph (e) of this section that occurred during the taxable year. The electing shareholder also shall file by the due date, as extended, for its return a copy of Form 8621 or the statement with the Philadelphia Service Center, P.O. Box 21086, Philadelphia, Pennsylvania 19114.

§ 1.1295-1T Election by a passive foreign investment company to be a qualified electing fund (Temporary).

(a) *In general.* This section provides rules under which a foreign corporation that qualifies as a passive foreign investment company (PFIC), as defined in section 1296, may make the election under section 1295 to be a qualified electing fund (QEF). U.S. persons that are shareholders of a QEF are taxable annually, pursuant to section 1293, on their pro rata shares of the earnings and profits of the QEF unless the shareholder makes the election under section 1294 to extend the time or payment of tax on undistributed earnings. The election under section 1295 may not be made by a PFIC that issues any of its shares in bearer form or is otherwise unable to identify all of its shareholders of record. The election will be effective with respect to all direct and indirect shareholders of the PFIC. The election may be made for any taxable year of the corporation during which it is a PFIC.

(b) *Election requirements.* An election under section 1295 shall be valid only if the PFIC complies with the following requirements.

(1) *Time for making the election -- (i) In general.* A PFIC must make the election under this section before the fifteenth day of the third month following the taxable year for which it is being made. Pursuant to section 7502 and the regulations thereunder, an election or an amended election under this section that is postmarked by United States mail on or before the due date will be considered timely filed. An election mailed by air, postage prepaid and properly addressed to the Internal Revenue Service Center in Philadelphia, Pennsylvania, and bearing an originating official postmark of a foreign postal authority dated at least 10 calendar days before the due date, will be deemed timely filed.

(ii) *Exception for elections for post-1986 years ended before 12/31/87.* A PFIC whose first post-1986 taxable year ended before December 31, 1987 may file its election under this section any time before March 15, 1988.

(iii) *Curing an election made before 5/15/88.* A PFIC that must file its election under this section before

May 15, 1988 has until June 15, 1988 to satisfy all other requirements of this paragraph (b), provided that the PFIC has filed a statement containing the information specified in paragraphs (b)(2)(ii) (A), (B), and (C) of this section at the address specified in paragraph (b)(2)(i) before the fifteenth day of the third month following the taxable year for which the election is made (or, in the case of any PFIC described in paragraph (b)(1)(ii), before March 15, 1988).

(2) *Manner of making the election -- (i) In general.* A PFIC shall make an election under this section by filing Form 8644 (if available) or a statement, in English, containing the information and representations required by this paragraph (b)(2). The form or statement shall be filed with the Internal Revenue Service Center, P.O. Box 21086, Philadelphia, Pennsylvania 19114 U.S.A. The form or statement shall be signed by a responsible officer of the PFIC who verifies, under penalties of perjury, that the officer is authorized to make the election on behalf of the PFIC and that all the information and representations provided in the form or statement are true, correct, and complete to the best of the officer's knowledge and belief.

(ii) *Information to be included in the election statement.* If a statement is used, the statement should be identified, in a heading, as an election under section 1295. The statement must contain the following information and representations:

(A) The name, address, taxpayer identification number, if any, and country and year of incorporation of the PFIC.

(B) A statement that the PFIC is making the election under section 1295 and the date on which the PFIC is making the election.

(C) The taxable year to which the election under section 1295 applies.

(D) The name and address of the United States resident who has been designated by the PFIC as its U.S. agent pursuant to paragraph (b)(3) of this section.

(E) The PFIC's representation that it will maintain its books of account, records, shareholder ledgers, and other documents in the United States in accordance with paragraph (b)(4) of this section and will make such documents available for inspection in the United States by personnel of the Internal Revenue Service.

(F) The name and address of the person (or persons) having custody of the PFIC's books of account, records, shareholder ledgers, and other documents in the United States.

(G) A description of each class of stock of the PFIC outstanding during the taxable year, and the manner in which the stock was traded; if the stock is traded in an established securities market(s), the name of the market(s).

(H) The total amount of ordinary earnings and net capital gain of the PFIC for the taxable year, as determined under United States federal income tax principles and in accordance with section 1293(e). The computations for this purpose shall be determined in the company's functional currency, as defined in section 985(b), and then translated into U.S. dollars, if necessary, at the weighted average exchange rate for the PFIC's taxable year, as provided in section 989(b), specifying the rate of exchange utilized.

(I) The amount of distributions of U.S. dollars and the fair market value and description of any other property (including foreign currency) distributed during the taxable year of the PFIC to which the election under this section applies.

(J) If the PFIC is required to make the fair market value determination under paragraph (b)(9) of this section, the fair market value of one share of each class of stock in the PFIC as of the first day of the PFIC's first taxable year as a QEF, specifying the manner in which the fair market value of the stock was determined, and the relevant data, including the sources thereof, used in the determination. The PFIC shall notify its shareholders of the value of its stock as provided in paragraph (b)(5) of this section.

(3) *Appointment of U.S. agent.* The PFIC shall appoint a person resident in the United States as its authorized representative in the United States (U.S. agent). The PFIC shall have a U.S. agent at all times after the election under section 1295 is made (or perfected pursuant to paragraph (b)(1)(iii) of this section) and during which it remains in effect. The U.S. agent shall be the PFIC's representative for all purposes relating to the administration and enforcement of the federal income tax laws, including providing the Commissioner or his delegate with such information and documents or access thereto as the Commissioner may require for the administration of sections 1291 through 1297 and the regulations thereunder.

(4) *Books and records.* The PFIC shall maintain for each taxable year to which the election under section 1295 applies permanent books of account, records and such other documents as are necessary to establish its ordinary earnings and net capital gain as provided in section 1293(e) and computed in accordance with U.S. generally accepted accounting principles and federal income tax principles. The PFIC also shall maintain for each taxable year to which the election under section 1295 applies a ledger of all shareholders of record during the taxable year. The PFIC shall keep copies of such books, records, shareholder ledgers and other documents in the United States and shall maintain them so long as the contents thereof may be material to the administration of sections 1291 through 1297, but for not less than 10 years. Such books, records, shareholder ledgers and other documents shall be available for inspection in the United States by authorized Internal Revenue officers or employees.

(5) *Annual shareholder notification and request for certification of U.S. ownership -- (i) In general.* Before the fifteenth day of the third month following each taxable year for which the election is in effect, the PFIC shall send the notification of PFIC information and request for shareholder certification statements, set forth in paragraph (b)(5)(ii) of this section, to all persons that were the shareholders of record of the PFIC at any time during such year.

(ii) *The notification of PFIC information and request for shareholder certification.* The notification of PFIC information and request for shareholder certification statements are described below. The PFIC may modify these statements as it deems necessary provided the information contained in the following statements is transmitted to the PFIC shareholders. The PFIC information to be reported in the notification to shareholders includes information regarding the ordinary earnings and net capital gain of the PFIC. The PFIC may report the daily amount of its ordinary earnings and net capital gain on a per share basis. However, if the number of outstanding shares of the PFIC's stock changed at any time during the taxable year, the PFIC shall provide the shareholders a schedule of the per share amounts of ordinary earnings and net capital gain for each day during the taxable year. Each shareholder will determine its pro rata shares of the ordinary earnings and net capital gain of the PFIC based on the information provided by the PFIC. The information contained in paragraph I(F) of the notification statement, regarding the section 1291(d)(2) election, is not required if the PFIC made the election to be a QEF for its first taxable year during which it qualifies as a PFIC under section 1296.

Important Tax Information: Response Required

Notification of Qualified Electing Fund Status and Request for Certification

I. Notification of Qualified Electing Fund Status

A. Earnings and profits: [*Name of the PFIC*] has elected to be a qualified electing fund for U.S. tax purposes for the taxable year beginning [*first day of the PFIC's taxable year*] and ending [*last day of the PFIC's taxable year*]. As a result of this election, all U.S. persons that are direct or indirect shareholders of [*name of the PFIC*] during any part of that taxable year must include in gross income for U.S. tax purposes their pro rata shares of ordinary earnings and net capital gain earned by [*name of the PFIC*] during the taxable year pursuant to section 293 of the Internal Revenue Code. [*The daily amounts of ordinary earnings and net capital gain per share of stock in [name of the PFIC] for the taxable year ended [last day of the PFIC'S taxable year] are as follows; you are to compute your pro rata shares of ordinary earnings and net capital gain by multiplying the daily, per share amount of each type of income by the number of shares held by you during the year and the number of days held.*] [Attached is a schedule of the per share amounts of ordinary earnings and net capital gain for each day during the taxable year of [*name of the PFIC*]; you are to compute your pro rata shares of ordinary earnings and net capital gain by multiplying each day's per share earnings amounts by the number of shares held on that day and then adding the daily ordinary earnings and net capital gain

amounts.]

Ordinary Earnings: [Daily dollar amount per share of stock] [See attached schedule of the per share dollar amounts, for each day,] of ordinary earnings as determined under section 1293.

Net Capital Gain: [Daily dollar amount per share of stock] [See attached schedule of the per share dollar amounts, for each day,] of net capital gain as determined under section 1293.

B. [Name of the PFIC] distributed \$ in cash and other property to you during its taxable year.

C. [Name of the PFIC] [was] [was not] a controlled foreign corporation within the meaning of section 957 of the Internal Revenue Code during the taxable year. Its subpart F income, as determined under section 951 for the taxable year; is XXXXX .

D. [Name of the PFIC] [was] [was not] a foreign personal holding company within the meaning of section 552 of the Internal Revenue Code during the taxable year. Its undistributed foreign personal holding company income, as determined under section 556, is XXXXX .

E. If any portion of your share of the current year earnings of [name of the PFIC] was not distributed to you during its taxable year and you owned the stock in [name of the PFIC] on [the last day of the PFIC's taxable year], you may be able to extend the time for payment of tax on some or all of this income under section 1294 of the Internal Revenue Code. See IRS Form 8621.

[Paragraph F is not required if the PFIC made the election to be a QEF for its first post-1986 taxable year that it qualifies as a PFIC under section 1296.]

F. If you were a U.S. person that was a direct or indirect shareholder of [name of the PFIC] on [the first day of its first taxable year as QEF], you may make the election under section 1291(d)(2) to recognize gain on a deemed sale of your stock in [name of the PFIC]. The fair market value of your stock interest, divided among the different classes of stock that you owned on that day, is as follows:

[Class of Stock]: \$[fair market value determined in accordance with § 1.1295-1T(b)(9)].

G. The U.S. taxpayer identification number assigned to [name of the PFIC] is XXXXX .

II. Request for Certification

U.S. persons that own stock directly or indirectly in [name of the PFIC] are requested to report to [name of the PFIC] by completing the following certification statement and returning it to the company. If additional space is needed, provide the required information on a separate sheet of paper and attach it to this form.

U.S. persons. If you are a U.S. citizen or individual resident, a U.S. corporation, or an estate, trust (other than a grantor trust, described below) or partnership that is a U.S. person for U.S. tax purposes, please complete the Certification Statement below and return it to [name of the PFIC] by [date].

Foreign persons. If you are a foreign corporation that is a passive foreign investment company, a foreign corporation that has a 50 percent or greater shareholder, or an estate, trust (other than a grantor trust, described below), or partnership that is not a U.S. person for U.S. tax purposes, please send this Notification of Qualified Electing Fund Status and Request for Certification to each of your shareholders (foreign corporations that are not passive foreign investment companies need only send the statement to their 50 percent or greater shareholder(s)), beneficiaries, or partners, indicating on the Notification of Qualified Electing Fund Status the amounts attributable to such person's indirect interest in [name of the PFIC]. (If you are unable to compute the amounts attributable to such person's indirect interest, please indicate the amounts attributable to your own interest in [name of the PFIC].)

Grantor trusts. If you are a trust the income of which is taxed entirely to the grantor or other person considered the owner of the trust under U.S. tax principles, please send the Notification of Qualified

Electing Fund Status and Request for Certification to the grantor/owner of the trust.

Nominees. If you are a U.S. or foreign person holding stock in [name of the PFIC] for the account of another person, please send this Notification of Qualified Electing Fund Status and Request for Certification to that other person, indicating on the Notification of Qualified Electing Fund Status the amounts attributable to such person's indirect interest in [name of the PFIC].

Each indirect shareholder that certifies to the PFIC that (he)(she)(it) is a U.S. person shall state (his)(her)(its) pro rata share of the ordinary earnings and net capital gain of the PFIC and pro rata share of the cash and the fair market value of other property distributed by the PFIC.

Certification Statement

[Name of direct or indirect PFIC shareholder (as reported on the U.S. tax return)] is a U.S. citizen/U.S. individual resident/U.S. corporation/U.S. estate/U.S. trust/U.S. partnership/foreign trust/foreign estate (please circle applicable category) that held stock directly or indirectly in [name of the PFIC] during [name of the PFIC]'s taxable year ending XXXXX . [Name of direct or indirect shareholder]'s address is XXXXX , and United States taxpayer identification number is XXXXX . [Name of direct or indirect PFIC shareholder]'s pro rata share of ordinary earnings is \$ XXXXX , pro rata share of net capital gain is \$ XXXXX , and pro rata share of the cash and the fair market value of other property distributed by [name of the PFIC] is XXXXX . Stock in [name of PFIC] is not registered in the name of [name of indirect PFIC shareholder] because the stock was held through [name(s) of nominee(s) or foreign person(s) through which stock was held indirectly].

Under penalties of perjury, I declare that I have examined this certification and, to the best of my knowledge and belief, it is true, correct, and complete.

[Signature of shareholder/authorized representative of shareholder and title, and date].

(6) *Annual reporting by the PFIC to the Internal Revenue Service.* By the fifteenth day of the ninth month following each taxable year of the PFIC to which the election under this section applies, the PFIC shall send to the Internal Revenue Service Center, P.O. Box 21086, Philadelphia, Pennsylvania 19114:

(i) A schedule containing the following information obtained pursuant to the certification procedure described in § 1.1295-1T(b)(5) from each direct or indirect shareholder that certified its status as a U.S. person: Names, addresses, taxpayer identification numbers, their pro rata shares (determined in the manner described in section 1293(b)) of the ordinary earnings and net capital gain of the PFIC for the taxable year determined in accordance with section 1293(e), and their pro rata shares of cash and fair market value of other property distributed to them or to the persons that held the stock directly or indirectly for their benefit.

(ii) For all taxable years of the PFIC following the year of the election, a Form 8644 (if available) or a statement containing the information described in paragraphs (b)(2)(ii) and (b)(6)(i) relating to information to be included in the election statement.

(7) *Amendment of earnings information.* The QEF shall report to the Internal Revenue Service, at the address specified in paragraph (b)(6) of this section, any amendments to the earnings information required to be provided to the Internal Revenue Service pursuant to paragraphs (b)(2)(ii)(H) and (b)(6) of this section, and notify all its shareholders of any amendments to the earnings information reported to the shareholders pursuant to paragraph (b)(5). The QEF shall recalculate its ordinary earnings and net capital gain at any time that it discovers an error in its previous calculations or its books and records or otherwise makes a necessary adjustment in its books and records. The amended information shall be clearly identified as amending the original report or shareholder notification.

(8) *Taxpayer identification number.* The Internal Revenue Service will assign the PFIC a taxpayer identification number upon the filing of the PFIC's election to be a QEF. The PFIC shall use the assigned number on all forms, statements, notifications and other communications filed with the Internal Revenue Service or provided to its shareholders for purposes of the election under this section.

(9) *Fair market value determination by certain companies.* If a foreign corporation is making the

election to be a QEF for a taxable year other than the first taxable year during which it qualified as a PFIC under section 1296, it must determine the fair market value of its stock on the first day of its first taxable year to which the election under section 1295 applies (the valuation date). A PFIC required to make the fair market value determination shall notify its shareholders of the stock value pursuant to paragraph (b)(5) of this section. This value is to be used by the shareholder in making the election under section 1291(d)(2) to recognize gain on a deemed sale of the PFIC stock held on the valuation date. For purposes of determining the fair market value of the stock in the PFIC, the following rules shall apply.

(i) *Companies other than open-end investment companies.* The fair market value of companies, other than open-end investment companies as defined in paragraph (b)(9)(ii)(B) of this section, shall be determined pursuant to subdivisions (A) through (E) of this paragraph (b)(9)(i).

(A) If the stock of the PFIC was regularly traded on an established securities market on the valuation date, the fair market value of the stock shall be the closing price of the stock on the valuation date. If there were no sales on the valuation date, but there were sales on dates within 30 business days before or after the valuation date, the fair market value shall be the mean of the opening and closing prices on the nearest date before or after the valuation date.

(B) If the stock of the PFIC was regularly traded in more than one established securities market, the price of the stock on a composite listing of all established securities markets in which it is regularly traded must be used, provided such a composite listing is set forth in a generally available listing or publication of general circulation. If such a composite listing is not available, the records of the price in the established securities market in which the stock is principally traded must be used.

(C) In any case in which a dividend is declared on a share of stock before the valuation date but payable to stockholders of record on a date after the valuation date, the amount of the dividend must be added to the ex-dividend quotation in determining the fair market value of the stock as of the valuation date.

(D) If the stock in the PFIC was not traded on an established securities market on the valuation date, or within 30 business days before or after the valuation date, the fair market value of the stock shall be the value determined by applying the guidelines of Rev. Rul. 59-60; 1959-1 C.B. 237, as amplified by Rev. Rul. 77-287, 1977-2 C.B. 319, Rev. Rul. 80-213, 1980-2 C.B. 101, and Rev. Rul. 83-120, 1983-2 C.B. 170.

(E) For purposes of this paragraph, the terms "established securities market" and "regularly traded" shall have the meanings given such terms in § 1.897-1 (m) and (n), respectively. However, stock will not be treated as regularly traded if there was not a sale of the stock within 30 business days before or after the valuation date on an established securities market.

(ii) *Open-end investment companies* -- (A) The fair market value of a share in a PFIC that is an open-end investment company (commonly known as a "mutual fund") shall be its public redemption price (or bid price) on the valuation date. If there is no public redemption price quoted by the PFIC for the valuation date, the fair market value of the mutual fund share is the last public redemption price quoted by the PFIC for the most recent day preceding the valuation date for which there was a quotation. In any case where a dividend is declared on a share in a PFIC that is an open-end investment company before the valuation date, but payable to shareholders of record after the valuation date and the share is quoted "ex-dividend" on the valuation date, the amount of the dividend must be added to the ex-dividend quotation in determining the fair market value of the share as of the valuation date.

(B) The term "open-end investment company" and the term "mutual fund" include only a company that on the applicable valuation date was engaged in offering its shares to the public in the capacity of an open-end investment company. An open-end investment company is an investment company that stands ready to redeem its shares, on demand, at their current net asset value.

(C) The term "public redemption price" and the term "bid" price mean the price (the current net asset value) at which the open-end investment company will redeem its shares.

(c) *Revocability of the election* -- (1) *In general.* The election under section 1295 may be revoked by the PFIC only with the consent of the Commissioner. In addition, the Commissioner may revoke the election for failure of the PFIC to satisfy any requirements set forth in this section within 90 days of the mailing of notification from the Internal Revenue Service of such failure. The revocation will be effective for the taxable year for which the requirement was not satisfied. The PFIC shall notify the U.S. persons that are its shareholders within 90 days of receipt of a notice from the Internal Revenue Service that the election under section 1295 has been revoked.

(2) *Failure to obtain shareholder certification.* The election under section 1295 will not be invalidated or revoked in the event a shareholder of the PFIC fails to provide the certification requested pursuant to paragraph (b)(5) of this section.

§ 1.1297-3T Deemed sale election by a United States person that is a shareholder of a passive foreign investment company (Temporary).

(a) *In general.* Except as indicated below, a shareholder of a foreign corporation that no longer qualifies as a passive foreign investment company (PFIC) shall be treated for tax purposes as holding stock in a PFIC and therefore continue to be subject to taxation under section 1291 unless the shareholder makes the election under section 1297(b)(1). This continuing PFIC taint shall not apply to stock in a PFIC for which an election under section 1295 to be a qualified electing fund (QEF) has been in effect throughout that portion of the shareholder's holding period during which the PFIC qualified as a PFIC. A U.S. person making the election under section 1297(b)(1) shall be treated as having sold its stock in the PFIC on the last day of the last taxable year of the foreign corporation during which it qualified as a PFIC (termination date). The shareholder thereafter shall not be treated as holding stock in a PFIC and shall not be subject to taxation under section 1291. The deemed sale is taxed as a disposition under section 1291. Pursuant to that section, the gain, if any, is considered earned pro rata over the shareholder's holding period in the stock and is taxed as ordinary income. The tax on the gain is based on the value of the tax deferral and includes an interest charge. Any loss realized in the deemed sale may not be recognized. This section provides rules for making the election under section 1297(b)(1). The election is available to a U.S. person that is a shareholder of a foreign corporation if --

- (1) The foreign corporation was a PFIC at any time during the period the U.S. person held the stock;
- (2) At any one time during the U.S. person's holding period, the foreign corporation qualified as a PFIC but was not a QEF; and
- (3) The foreign corporation is no longer a PFIC within the meaning of section 1296.

(b) *Time and manner of making the election* -- (1) *In general.* The shareholder shall make the election under this section and section 1297(b)(1) by filing an amended income tax return for its taxable year that includes the termination date within three years of the due date, as extended, for the shareholder's tax return for such taxable year. The shareholder must attach to the amended tax return either Form 8621 or a statement, prepared in accordance with paragraph (c)(2) of this section, reporting the gain on the deemed sale of the stock as required by section 1291(a)(2) (as if such deemed sale occurred under section 1291(a)(2)), and by paying the tax on the gain as required by section 1291 (including the payment of the deferred tax amount required under sections 1291(a)(1)(C) and 1291(c)). The electing shareholder also shall pay interest, pursuant to section 6601, on the underpayment of tax for the taxable year of termination. An electing shareholder that realizes a loss shall report the loss on Form 8621, but shall not recognize the loss.

(2) *Information to be included in the election.* If a statement is used, the statement should be identified, in a heading, as an election under section 1297(b)(1). The statement must include the following information and representations:

- (i) The name, address and taxpayer identification number of the electing shareholder;
- (ii) The name, address and taxpayer identification number, if any, of the PFIC;
- (iii) A statement that the shareholder is making the election under section 1297(b)(1);

(iv) The period in the electing shareholder's holding period in the stock during which the foreign corporation was a PFIC, the period during which it was a QEF (and whether the shareholder elected under section 1294 to defer payment of its tax liability attributable to any portion of such period), and the termination date;

(v) The manner in which the PFIC lost the characteristics of a PFIC;

(vi) A schedule listing the shares in the PFIC held by the electing shareholder on the termination date, listing the date(s) each share or block of shares was acquired, the number of shares acquired on each date listed, and the tax basis of each share;

(vii) The fair market value of the stock in the PFIC on the termination date; for this purpose, the fair market value of the stock shall be determined according to the rules of § 1.1295-1T(b)(9); and

(viii) A schedule showing the computation of the gain recognized on the deemed sale, and a calculation of the deferred tax amount, as defined in section 1291(c).

(3) *Adjustment to basis; treatment of holding period.* An electing shareholder that recognizes gain on the deemed sale of stock shall increase its adjusted basis in the stock by the amount of gain recognized. An electing shareholder shall not adjust the basis in stock with respect to which the shareholder realized a loss on the deemed sale. An electing shareholder shall thereafter treat its holding period in the stock, for purposes of sections 1291 through 1297, as beginning on the day following the termination date without regard to whether it recognized gain on the deemed sale; for section 1223 purposes, the holding period in the stock in the PFIC shall include the period prior to the deemed sale.

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(26 CFR Part 602)

Par. 3. The authority for Part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

§ 602.101 [Amended]

Par. 4. Section 602.101(c) is amended by inserting in the appropriate places in the table § 1.1291-0T . . . 1545-1028, § 1.1291-10T . . . 1545-1028, § 1.1294-1T . . . 1545-1028, § 1.1295-1T . . . 1545-1028, § 1.1297-3T . . . 1545-1028.

Lawrence B. Gibbs,

Commissioner of Internal Revenue.

Approved: February 23, 1988.

O. Donaldson Chapoton,

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