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shares of class B stock. Each class of the outstanding stock is entitled to participate on a share for share basis in any dividend distributions by S Corporation. The owners of a majority of the class A stock are entitled to elect 7 of the 10 corporate directors, and the owners of a majority of the class B stock are entitled to elect the other 3 of the 10 directors. Thus, the class A stock (as a class) possesses 70 percent of the total combined voting power of all classes of stock entitled to vote of S Corporation, and the class B stock (as a class) possesses 30 percent of such voting power. D, a United States person, owns 31 shares of the class A stock and thus owns 36,167 percent (31/60 × 70 percent) of the total combined voting power of all classes of stock entitled to vote of S Corporation. By reason of the ownership of such voting power, D is a United States shareholder of S Corporation under section 951(b). For purposes of section 957, S Corporation is a controlled foreign corporation by reason of D's ownership of a majority of the class A stock, as illustrated in example 2 of paragraph (c) of §1.957–1. E, a United States person, owns eight shares of the class A stock and thus owns 9.333 percent (8/60 × 70 percent) of the total combined voting power of all classes of stock entitled to vote of S Corporation. Since E owns only 9.333 percent of such voting power and less than 20 percent of the number of shares of the class A stock, he is not a United States shareholder of S Corporation under section 951(b). F, a United States person, owns 14 shares of the class B stock and thus owns 10.5 percent (14/40 × 30 percent) of the total combined voting power of all classes of stock entitled to vote of S Corporation. By reason of the ownership of such voting power, F is a United States shareholder of S Corporation under section 951(b).

Example 2. Foreign corporation R has three classes of stock outstanding, consisting of 10 shares of class A stock, 20 shares of class B stock, and 300 shares of class C stock. Each class of the outstanding stock is entitled to participate on a share for share basis in any distribution by R Corporation. The owners of a majority of the class A stock are entitled to elect 6 of the 10 corporate directors, and the owners of a majority of the class B stock are entitled to elect the other 4 of the 10 directors. The class C stock is not entitled to vote. D, E, and F, United States persons, each own 2 shares of the class A stock and 100 shares of the class C stock. As owners of a majority of the class A stock, D, E, and F elect 6 members of the board of directors. D, E, and F are United States shareholders of R Corporation under section 951(b) since each owns 20 percent of the total number of shares of the class A stock which possesses the power to elect a majority of the board of directors of R Corporation. For purposes of section 957, R Corporation is a controlled foreign corporation by reason of the ownership by D, E, and F of a majority of the class A stock, as illustrated in example 2 of paragraph (c) of §1.957–1.

[T.D. 6795, 30 FR 935, Jan. 29, 1965, as amended by T.D. 7893, 48 FR 22507, May 19, 1983; T.D. 9222, 70 FR 49866, Aug. 25, 2005; 70 FR 67906, Nov. 9, 2005; T.D. 9251, 71 FR 8944, Feb. 22, 2006]

§ 1.951–2 Coordination of subpart F with election of a foreign investment company to distribute income.

A United States shareholder who for his taxable year is a qualified shareholder (within the meaning of section 1247(c)) of a foreign investment company with respect to which an election under section 1247(a) and the regulations thereunder is in effect for the taxable year of such company which ends with or within such taxable year of such shareholder shall not be required to include any amount in his gross income for his taxable year under paragraph (a) of §1.951–1 with respect to such company for that taxable year of such company.

[T.D. 6795, 30 FR 937, Jan. 29, 1965]

§ 1.951–3 Coordination of subpart F with foreign personal holding company provisions.

A United States shareholder (as defined in section 951(b)) who is required under section 551(b) to include in his gross income for his taxable year his share of the undistributed foreign personal holding company income for the taxable year of a foreign personal holding company (as defined in section 552) which for that taxable year is a controlled foreign corporation (as defined in section 957) shall not be required to include in his gross income for his taxable year under section 951(a) and paragraph (a) of §1.951–1 any amount attributable to the earnings and profits of such corporation for that taxable year of such corporation. If a foreign corporation is both a foreign personal holding company and a controlled foreign corporation for the same period which is only a part of its taxable year, then, for purposes of applying the immediately preceding sentence, such corporation shall be deemed to be, for such part of such year, a foreign personal holding company and not a controlled foreign corporation and the

earnings and profits of such corporation for the taxable year shall be deemed to be that amount which bears the same ratio to its earnings and profits for the taxable year as such part of the taxable year bears to the entire taxable year. The application of this section may be illustrated by the following examples:

Example 1. A, a United States shareholder, owns 100 percent of the only class of stock of controlled foreign corporation M which, in turn, owns 100 percent of the only class of stock of controlled foreign corporation N. A and Corporations M and N use the calendar year as a taxable year. During 1963, N Corporation derives $40,000 of gross income all of which is foreign personal holding company income within the meaning of section 553; thus, N Corporation is a foreign personal holding company for such year within the meaning of section 552(a). For 1963, N Corporation has undistributed foreign personal holding company income (as defined in section 556(a)) of $30,000, derives $25,000 of subpart F income, and has earnings and profits of $32,000. During 1963, M Corporation derives $100,000 of gross income (including as a dividend under section 555(c)(2) the $30,000 of N Corporation's undistributed foreign personal holding company income), 65 percent of which is foreign personal holding company income within the meaning of section 553. Therefore, M Corporation is a foreign personal holding company for such year. For 1963, M Corporation has undistributed foreign personal holding company income (as defined in section 556(a)) of $90,000, determined by taking into account under section 552(c)(1) N Corporation's $30,000 of undistributed foreign personal holding company income for such year; in addition, M Corporation derives $50,000 of subpart F income and has earnings and profits of $92,000. Neither M Corporation nor N Corporation makes any actual distributions during 1963. A is required under section 551(b) to include in his gross income for 1963 as a dividend the $90,000 of M Corporation's undistributed foreign personal holding company income for such year. For 1963, A is not required to include in his gross income under section 951(a) any of the $50,000 subpart F income of M Corporation or of the $25,000 subpart F income of N Corporation.

Example 2. The facts are the same as in example 1, except that only 45 percent of M Corporation's gross income (determined by including under section 555(c)(2) the $30,000 of N Corporation's undistributed foreign personal holding company income) is foreign personal holding company income within the meaning of section 553; accordingly, M Corporation is not a foreign personal holding company for 1963. Since for such year M Corporation is not a foreign personal holding company, the undistributed foreign personal holding company income ($30,000) of N Corporation is not required under section 555(b) to be included in the gross income of M Corporation for 1963; as a result, such income is not required under section 551(b) to be included in the gross income of A for such year even though N Corporation is a foreign personal holding company for that year. For 1963, A is required to include $75,000 in his gross income under section 951(a)(1)(A)(i) and paragraph (a) of §1.951–1, consisting of the $50,000 subpart F income of M Corporation and the $25,000 subpart F income of N Corporation.

Example 3. The facts are the same as in example 1, except that in 1963 N Corporation actually distributes $30,000 to M Corporation and M Corporation, in turn, actually distributes $90,000 to A. Under section 556 the undistributed foreign personal holding company income of both M corporation and N Corporation is thus reduced to zero; accordingly, no amount is included in the gross income of A under section 551(b) by reason of his interest in corporations M and N. A must include $75,000 in his gross income for 1963 under section 951(a)(1)(A)(i) and paragraph (a) of §1.951–1, consisting of the $50,000 subpart F income of M Corporation and the $25,000 subpart F income of N Corporation. Of the $90,000 distribution received by A from M Corporation, $75,000 is excludable from his gross income under section 959(a)(1) as previously taxed earnings and profits; the remaining $15,000 is includible in his gross income for 1963 as a dividend.

Example 4. (a) A, a United States shareholder, owns 100 percent of the only class of stock of controlled foreign corporation P, organized on January 1, 1963. Both A and P Corporation use the calendar year as a taxable year. During 1963, 1964, and 1965, P Corporation is not a foreign personal holding company as defined in section 552(a); in each of such years, P Corporation derives dividend income of $10,000 which constitutes foreign personal holding company income (within the meaning of §1.954–2) but under 26 CFR 1.954–1(b)(1) (Revised as of April 1, 1975) excludes such amounts from foreign base company income as dividends received from, and reinvested in, qualified investments in less developed countries. Corporation P's earnings and profits accumulated for 1963, 1964, and 1965 and determined under paragraph (b)(2) of §1.955–1 are $40,000. For 1966, P Corporation is a foreign personal holding company, has predistribution earnings and profits of $10,000, derives $10,000 of income which is both foreign personal holding company income within the meaning of section 553 and subpart F income within the meaning of section 952, distributes $8,000 to A, and has undistributed foreign personal holding company income of $2,000 within the meaning of

section 556. In addition, for 1966 P Corporation has a withdrawal (determined under section 955(a) as in effect before the enactment of the Tax Reduction Act of 1975 but without regard to its earnings and profits for such year) of $25,000 of previously excluded subpart F income from investment in less developed countries. A is required under section 551(b) to include in his gross income for 1966 as a dividend the $2,000 undistributed foreign personal holding company income. The $8,000 distribution is includible in A's gross income for 1966 under sections 61(a)(7) and 301 as a distribution to which section 316(a)(2) applies. Corporation P's $25,000 withdrawal of previously excluded subpart F income from investment in less developed countries is includible in A's gross income for 1966 under section 951(a)(1)(A)(ii) and paragraph (a)(2) of §1.951–1.

(b) If P Corporation's earnings and profits accumulated for 1963, 1964, and 1965 were $15,000, instead of $40,000, the result would be the same as in paragraph (a) of this example, except that a withdrawal of only $15,000 of previously excluded subpart F income from investment in less developed countries would be includible in A's gross income for 1966 under section 951(a)(1)(A)(ii) and paragraph (a)(2) of §1.951–1.

(c) The principles of this example also apply to withdrawals (determined under section 955(a), as in effect before the enactment of the Tax Reduction Act of 1975) of previously excluded subpart F income from investment in less developed countries effected after the effective date of such Act, and to withdrawals (determined under section 955(a), as amended by such Act) of previously excluded subpart F income from investment in foreign base company shipping operations.

Example 5. (a) The facts are the same as in paragraph (a) of example 4, except that, instead of having a $25,000 decrease in qualified investments in less developed countries for 1966, P Corporation invests $20,000 in tangible property (not described in section 956(b)(2)) located in the United States and such investment constitutes an increase (determined under section 956(a) but without regard to the earnings and profits of P Corporation for 1966) in earnings invested in United States property. Corporation P's earnings and profits accumulated for 1963, 1964, and 1965 and determined under paragraph (b)(1) of §1.956–1 are $22,000. The result is the same as in paragraph (a) of example 4, except that instead of including the $25,000 withdrawal, A must include $20,000 in his gross income for 1966 under section 951(a)(1)(B) and paragraph (a)(2)(iv) of §1.951–1 as an investment of earnings in United States property.

(b) If P Corporation's earnings and profits accumulated for 1963, 1964, and 1965 were $9,000 instead of $22,000, the result would be the same as in paragraph (a) of this example, except that only $9,000 would be includible in A's gross income for 1966 under section 951(a)(1)(B) and paragraph (a)(2)(iv) of §1.951–1 as an investment of earnings in United States property.

[T.D. 6795, 30 FR 937, Jan. 29, 1965, as amended by T.D. 7893, 48 FR 22508, May 19, 1983]

§ 1.952–1 Subpart F income defined.

(a) *In general.* For purposes of sections 951 through 964, a controlled foreign corporation's subpart F income for any taxable year shall, except as provided in paragraph (b) of this section and subject to the limitations of paragraphs (c) and (d) of this section, consist of the sum of—

(1) The income derived by such corporation for such year from the insurance of United States risks (determined in accordance with the provisions of section 953 and §§1.953–1 through 1.953–6),

(2) The income derived by such corporation for such year which constitutes foreign base company income (determined in accordance with the provisions of section 954 and §§1.954–1 through 1.954–8),

(3)(i) An amount equal to the product of—

(A) The income of such corporation other than income which—

(*1*) Is attributable to earnings and profits of the foreign corporation included in the gross income of a United States person under section 951 (other than by reason of this paragraph) (determined in accordance with the provisions of section 951 and §1.951–1), or

(*2*) Is described in section 952(b),

multiplied by

(B) The international boycott factor determined in accordance with the provisions of section 999(c)(1), or

(ii) In lieu of the amount determined under paragraph (a)(3)(i) of this section, the amount described under section 999(c)(2) of such international boycott income, and

(4) The sum of the amount of any illegal bribes, kickbacks, or other payments paid after November 3, 1976, by or on behalf of the corporation during the taxable year of the corporation directly or indirectly to an official, employee, or agent in fact of a government. An amount is paid by a controlled foreign corporation where it is paid by an officer, director, employee,