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of §1.963–3) with respect to the distributing corporation and each foreign corporation through which such distribution is made to the United States shareholder, for the taxable year to which the election under section 963 applies; and the foreign income taxes paid by any foreign corporation by reason of such distribution shall, in the application of section 902 and of the special rules of paragraph (c) of §1.963–4, be treated as paid or accrued by such foreign corporation for its taxable year to which such election applies. The distribution shall not count toward a minimum distribution for any other taxable year.

[T.D. 6759, 29 FR 13348, Sept. 25, 1964, as amended by T.D. 6767, 29 FR 14879, Nov. 3, 1964]

§ 1.963–8 Determination of minimum distribution during the surcharge period.

(a) *Taxable years not wholly within the surcharge period.* In the case of a taxable year beginning before the surcharge period and ending within the surcharge period, or beginning within the surcharge period and ending after the surcharge period, or beginning before January 1, 1970, and ending after December 31, 1969, section 963(b) provides the method for determining the required minimum distribution. Under the method prescribed in section 963(b) for such years, the required minimum distribution is an amount equal to the sums of:

(1) That portion of the minimum distribution which would be required if the provisions of section 963(b)(1) were applicable to the taxable year, which the number of days in such taxable year which are within the surcharge period and before January 1, 1970, bears to the total number of days in such taxable year.

(2) That portion of the minimum distribution which would be required if the provisions of section 963(b)(2) were applicable to such taxable year, which the number of days in such taxable year which are within the surcharge period and after December 31, 1969, bears to the total number of days in such taxable year, and

(3) That portion of the minimum distribution which would be required if the provisions of section 963(b)(3) were applicable to such taxable year, which the number of days in such taxable year which are not within the surcharge period bears to the total number of days in such taxable year.

(b) *Calendar year 1970.* For calendar year 1970, the required minimum distribution shall be an amount determined in accordance with the following table:

If the effective foreign tax rate is (percentage)—	The required minimum distribution of earnings and profits is (percentage)—
Under 9	84.983562
9 or over but less than 10	82.967123
10 or over but less than 18	80.983562
18 or over but less than 19	79.471233
19 or over but less than 26	77.487671
26 or over but less than 27	73.958904
27 or over but less than 32	70.487671
32 or over but less than 33	67.463014
33 or over but less than 36	63.991781
36 or over but less than 37	57.942466
37 or over but less than 39	51.991781
39 or over but less than 40	44.934247
40 or over but less than 41	37.495890
41 or over but less than 42	31.446575
42 or over but less than 43	19.446575
43 or over but less than 44	12.893151
44 or over but less than 45	6.446575
45 or over	0

(c) *Surcharge period.* For purposes of this section the term ''surcharge period'' means the period beginning January 1, 1968, and ending June 30, 1970.

(d) *Illustration of principles.* The application of the rules set forth in paragraphs (a), (b), and (c) of this section may be illustrated by the following example. It is assumed that all computations are carried to sufficient accuracy:

Example. (a) M, a domestic corporation, and A, its controlled corporation (the one class of stock of which is wholly owned by M), both have a taxable year beginning December 1, 1969, and ending November 30, 1970. For such taxable year M makes a first-tier election with respect to A corporation. The effective foreign tax rate for such year is 30 percent.

(b) Under section 963(b) and paragraph (b) of this section the surcharge period ends June 30, 1970. Therefore, of the 365 days in the taxable year, 153 days are not within the surcharge period. Of the remaining 212 days, 31 are within the surcharge period and before January 1, 1970 and 181 days are within the surcharge period and after December 31, 1969. If section 963(b)(1) were applicable to the entire taxable year, the required minimum distribution of earnings and profits would be 75

percent. If section 963(b)(2) were applicable to the entire taxable year, the required minimum distribution would be 72 percent. If section 963(b)(3) were applicable to the entire taxable year, the required minimum distribution would be 69 percent.

(c) Under section 963(b) and this section the required minimum distribution of earnings and profits is 71 percent, computed as follows:

$(75\% \times 31 \div 365) + (72\% \times 181 \div 365) + (69\% \times 153 \div 365) = 71\%$.

[T.D. 7100, 36 FR 5336, Mar. 20, 1971]

§ 1.964–1 Determination of the earnings and profits of a foreign corporation.

(a)(1) *In general.* For rules for determining the earnings and profits (or deficit in earnings and profits) of a foreign corporation for taxable years beginning before January 1, 1987, for purposes of sections 951 through 964, *see* 26 CFR 1.964–1(a) (revised as of April 1, 2006). For taxable years beginning after December 31, 1986, except as otherwise provided in the Code and regulations, the earnings and profits (or deficit in earnings and profits) of a foreign corporation for its taxable year shall be computed for all Federal income tax purposes substantially as if such corporation were a domestic corporation by—

(i) Preparing a profit and loss statement with respect to such year from the books of account regularly maintained by the corporation for the purpose of accounting to its shareholders.

(ii) Making the adjustments necessary to conform such statement to the accounting principles described in paragraph (b) of this section; and

(iii) Making the further adjustments necessary to conform such statement to the tax accounting standards described in paragraph (c) of this section.

(2) *Required adjustments.* The computation described in paragraph (a)(1) of this section shall be made in the foreign corporation's functional currency (determined under section 985 and the regulations under that section) and may be made by following the procedures described in paragraphs (a)(1)(i) through (a)(1)(iii) of this section in an order other than the one listed, as long as the result so obtained would be the same. In determining earnings and profits, or the deficit in earnings and profits, of a foreign corporation under section 964, the amount of an illegal bribe, kickback, or other payment (within the meaning of section 162(c), as amended by section 288 of the Tax Equity and Fiscal Responsibility Act of 1982 in the case of payments made after September 3, 1982, and the regulations issued pursuant to section 964) 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 shall not be taken into account to decrease such earnings and profits or to increase such deficit. No adjustment shall be required under paragraph (a)(1)(ii) or (iii) of this section unless it is material. Whether an adjustment is material depends on the facts and circumstances of the particular case, including the amount of the adjustment, its size relative to the general level of the corporation's total assets and annual profit or loss, the consistency with which the practice has been applied, and whether the item to which the adjustment relates is of a recurring or merely a nonrecurring nature. For the treatment of earnings and profits whose distribution is prevented by restrictions and limitations imposed by a foreign government, see section 964(b) and the regulations issued pursuant to section 964.

(3) *Translation into dollars.* In the case of a foreign corporation with a functional currency other than the United States dollar (dollar), see sections 986(b) and 989(b) for rules regarding the time and manner of translating distributions or inclusions of the foreign corporation's earnings and profits into dollars.

(b) *Accounting adjustments*—(1) *In general.* The accounting principles to be applied in making the adjustments required by paragraph (a)(1)(ii) of this section shall be those accounting principles generally accepted in the United States for purposes of reflecting in the financial statements of a domestic corporation the operations of its foreign affiliates, including the following:

(i) *Clear reflection of income.* Any accounting practice designed for purposes other than the clear reflection on a current basis of income and expense for