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Department of the Treasury
Washington, DC 20224

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Date:
July 16, 2012

LEGEND

Taxpayer =

X =
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Date 1 =
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Dear :

This is in response to your letter dated December 30, 2011, requesting a ruling granting Taxpayer permission to revoke elections made under Treas. Reg. § 1.954-2(g)(4) and former Treas. Reg. § 1.954-2T(g)(5) with respect to all of its controlled foreign corporations (CFCs).

The ruling contained in this letter is based upon information and representations submitted by Taxpayer, and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of this request for ruling, such material is subject to verification upon examination. The information submitted in the request is substantially as set forth below.

FACTS

Taxpayer is a large corporation headquartered in the United States. Taxpayer employs approximately X people in Y countries around the world.

Taxpayer's initial election to treat all foreign currency gains or losses as foreign personal holding company income (FPHCI) was made on its tax return for the year ended Date 1. At that time, the election was made pursuant to former Treas. Reg. § 1.954-2T(g)(5). The election was made on behalf of all of Taxpayer's CFCs, because the temporary regulations contained a conformity rule making the election effective for all related persons as defined in section 954(d)(3) and the regulations thereunder.

Final regulations adopted in 1995 removed this conformity rule and allowed an election under Treas. Reg. § 1.954-2(g)(4) to be made on a CFC-by-CFC basis. With the exception of the taxable years ending Date 2 and Date 3, Taxpayer made annual elections under Treas. Reg. § 1.954-2(g)(4) on behalf of all new CFCs up through and including its tax return for the year ending Date 4. For the taxable year ending Date 2, Taxpayer made the election under Treas. Reg. § 1.954-2(g)(4) for all newly formed CFCs but failed to make the election for newly acquired CFCs. For the taxable year ending Date 3, Taxpayer did not make the election under Treas. Reg. § 1.954-2(g)(4) for newly formed or acquired CFCs. Despite having omitted certain CFCs from the election for the taxable year ending Date 2 and failing to make the election for newly formed and acquired CFCs for the taxable year ending Date 3, Taxpayer treated all of its CFCs as if the election had been made. For each subsequent year, Taxpayer has consistently treated all of its CFCs as subject to the election.

At the time of Taxpayer's initial election, Taxpayer did not have financial accounting systems conducive to performing the tracing necessary to appropriately track transactions generating foreign currency gain or loss for purposes of the business needs exception under section 954(c)(1)(D). As a result of the election, net foreign currency losses of Taxpayer's CFCs are taken into account to determine each CFC's FPHCI, but net foreign currency gains are not eligible for the business needs exception under section 954(c)(1)(D) and Treas. Reg. § 1.954-2(g)(2) and thus constitute FPHCI.

Because a significant change of circumstances has occurred since its initial election, Taxpayer now wants to revoke the election. Taxpayer implemented a financial accounting system on a global basis and included a general ledger with a common chart of accounts. The chart of accounts includes specific accounts that capture foreign currency gain or loss related to transactions entered into in the normal course of each CFC's trade or business. Taxpayer has now progressed its systems capabilities to the point that it is able to efficiently track foreign currency transactions for purposes of the business needs exception. Taxpayer believes that its enhanced ability to identify

section 988 transactions that are directly related to the business needs of its CFCs will allow the exclusion of such transactions from the calculation of FPHCI.

RULINGS REQUESTED

Taxpayer requests consent to revoke its prior year elections under Treas. Reg. § 1.954-2(g)(4) and former Treas. Reg. § 1.954-2T(g)(5) that it made with respect to its CFCs, effective for the taxable year beginning Date 5.

LAW

Section 951(a) of the Code requires a United States shareholder of a CFC to include in gross income its pro rata share of the CFC's subpart F income for the taxable year.

Section 952(a) defines subpart F income to include, among other things, foreign base company income. Code section 954(a) defines foreign base company income to include FPHCI.

Section 954(c)(1)(D) provides that FPHCI includes the excess of foreign currency gains over foreign currency losses (as defined in section 988(b)) attributable to any section 988 transactions unless the transaction is directly related to the business needs of the CFC.

Section 988(a)(1) provides generally that any foreign currency gain or loss attributable to a section 988 transaction shall be computed separately and treated as ordinary income or loss.

Section 988(b)(1) defines foreign currency gain as any gain from a section 988 transaction to the extent such gain does not exceed gain realized by reason of changes in exchange rates on or after the booking date and before the payment date.

Section 988(b)(2) defines foreign currency loss as any loss from a section 988 transaction to the extent such loss does not exceed the loss realized by reason of changes in exchange rates on or after the booking date and before the payment date.

Treas. Reg. § 1.954-1(c)(1)(ii) provides generally that a net loss in any category of FPHCI may not reduce income in any other category of FPHCI.

Treas. Reg. § 1.954-2(g)(2)(ii) provides that foreign currency gain or loss directly related to the business needs of the CFC is excluded from FPHCI. Generally, foreign currency gain or loss is directly related to the business needs of a CFC if it falls within one of three categories of foreign currency transactions: (1) certain transactions or property related to the business activities of the CFC; (2) certain gains and losses from bona fide

hedging transactions; or (3) transactions in dealer property. Foreign currency gains or losses that fall within the general definition of FPHCI under section 954(c)(1)(D) will be excluded from FPHCI if the business needs exception is met.

Treas. Reg. § 1.954-2(g)(4)(i) provides that the controlling United States shareholders of a CFC can elect to include in the CFC's computation of FPHCI the excess of foreign currency gains over losses or the excess of foreign currency losses over gains attributable to any section 988 transaction (except gains or losses treated as capital gain or loss under section 988(a)(1)(B)). Thus, the general rule of Treas. Reg. § 1.954-1(c)(1)(ii) that net foreign currency losses may not reduce income in any other category of FPHCI would not apply if this election has been made because the regulations specifically provide that the excess of foreign currency losses over foreign currency gains may reduce other categories of FPHCI.

Treas. Reg. § 1.954-2(g)(4)(iii) provides that an election under Treas. Reg. § 1.954-2(g)(4)(i) is effective for the taxable year of the CFC for which it is made and all subsequent taxable years of such CFC unless revoked by or with the consent of the Commissioner.

Former Treas. Reg. § 1.954-2T(g)(5)(i) and (ii), effective for taxable years beginning after December 31, 1986, until final regulations were issued in 1995, provided an election to include in the computation of FPHCI all of a CFC's foreign currency gains or losses attributable to section 988 transactions, except for certain foreign currency gain or loss of a qualified business unit. The election was effective for all related persons as defined in section 954(d)(3) and the regulations thereunder.

ANALYSIS

As a United States shareholder, Taxpayer must include in gross income its pro rata share of each of its CFCs' subpart F income for the taxable year, including FPHCI. Because Taxpayer made elections on behalf of its CFCs under Treas. Reg. § 1.954-2(g)(4) and former Treas. Reg. § 1.954-2T(g)(5), its CFCs are subject to the terms of that election for purposes of calculating their FPHCI. Therefore, in the absence of consent being granted to revoke the elections made by Taxpayer, each CFC must include its net foreign currency gains as FPHCI, without application of any of the exclusions from FPHCI that might otherwise apply.

RULING

Based upon the facts submitted, permission is granted for Taxpayer to revoke its elections under Treas. Reg. § 1.954-2(g)(4) and former Treas. Reg. § 1.954-2T(g)(5), effective for the taxable year beginning Date 5. Additionally, Taxpayer is prohibited from making a new election under Treas. Reg. § 1.954-2(g)(4) until the sixth taxable year following the taxable year for which the revocation is first effective.

No opinion is expressed about whether the business needs exception is satisfied in this case.

This private letter ruling is directed only to the taxpayer who requested it. Code section 6110(k)(3) provides that it may not be used or cited as precedent.

A copy of this letter ruling must be attached to any federal income tax return to which it is relevant.

Sincerely,

Jeffery G. Mitchell
Chief, Branch 2
Office of the Associate Chief Counsel
(International)