**Office of Chief Counsel**
**Internal Revenue Service**
# Memorandum

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subject: Foreign Tax Redeterminations With Respect to Pre-1987 Accumulated Profits

This Chief Counsel Advice responds to your request for assistance. This advice may not be used or cited as precedent.

LEGEND

ForParent =
USParent =
EIN =
USGroup =
ForCorp1 =
ForCorp2 =
ForCorp3 =
ForCorp4 =
YGroup =
ForCountry W =
ForCountry X =
ForCountry Y =
ForCountry Z =
Y State 1 =

Y State 2 =
Y State 3 =
Y Tax Agency =
Date 1 =
Business A =

## ISSUE

Whether an additional amount of foreign tax paid in a post-1986 taxable year with respect to pre-1987 accumulated profits of ForCorp4 should be accounted for by adjusting ForCorp4's relevant annual layers of pre-1987 accumulated profits and pre-1987 foreign income taxes or ForCorp4's pools of post-1986 undistributed earnings and post-1986 foreign income taxes?

## CONCLUSION

Under the provisions of I.R.C. section 902(c)(6) and Treas. Reg. §§1.902-1(a)(10), 1.902-1(a)(13), and 1.905-5T prior to its expiration on November 5, 2010, a foreign tax redetermination with respect to a taxable year prior to the first taxable year taken into account in computing the post-1986 undistributed earnings and post-1986 foreign income taxes of ForCorp4 is not taken into account by adjusting the corporation's pools of post-1986 foreign income taxes and post-1986 undistributed earnings. Instead, the additional foreign taxes paid must be accounted for by adjusting ForCorp4's annual layers of pre-1987 accumulated profits and pre-1987 foreign income taxes.

## FACTS

ForParent is an entity incorporated in ForCountry W and resident for tax purposes in ForCountry X. ForParent operates in the United States through USParent (EIN), the U.S. parent company of a U.S. affiliated group (USGroup). It also operates in ForCountry Y through ForCorp1, the ForCountry Y parent company for YGroup. Prior to Date 1, 2009, ForCorp1 and its subsidiaries were not relevant for U.S. tax purposes because ForCorp1 was owned by ForCorp2, a ForCountry Z corporation and indirect subsidiary (through other ForCountry Z entities) of ForParent. On Date 1, 2009, USParent acquired 100 percent of ForCorp1 as part of a series of transactions. As a result of being acquired by USParent, ForCorp1 and the other members of YGroup became controlled foreign corporations (CFCs) in 2009. ForCorp1 directly owns 100 percent of ForCorp3, a ForCountry Y corporation, which in turn owns 100 percent of ForCorp4, a ForCountry Y corporation that is the primary ForCountry Y operating company, whose taxes are at issue.

USParent recognized a section 951(a)(l)(B) inclusion in 2010 relating to a section 956 investment in U.S. property (the purchase of certain U.S. trade receivables from a member of the USGroup) by ForCorp4, and computed an amount of foreign taxes

deemed paid under section 960 with respect to that inclusion. All relevant entities use the calendar year as their U.S. and foreign taxable years.

FOREIGN TAX ASSESSMENTS

Between 2008 and 2011, ForCorp4 was assessed additional tax and interest by the Y Tax Agency and the Y States 1, 2, and 3 tax authorities with respect to its taxable years 1994 through 2008. Although ForCorp4 is contesting certain of the ForCountry Y and Y States 1, 2, and 3 tax assessments, it was required to pay 50 percent of the total assessments of tax and interest, pending resolution of the issues. These amounts, together with the full amounts of tax and interest due with respect to certain agreed adjustments with respect to taxable years 1994 through 2008, were paid in 2008 through 2011.

USParent and Exam agree that ForCorp4's pools of post-1986 undistributed earnings and post-1986 foreign income taxes were established beginning on January 1, 2009, the first year for which ForCorp4 had a domestic corporate shareholder entitled to compute an amount of foreign taxes deemed paid. USParent takes the position that all of the additional creditable tax payments that were made by ForCorp4 to Country Y and to the Y States in 2009 through 2011 (but not in 2008) with respect to taxable years 1994 through 2008 are added in the year paid to ForCorp4's pool of post-1986 foreign income taxes, even though none of the earnings to which the taxes for 1994 through 2008 relate are included in ForCorp4's post-1986 undistributed earnings pool.

LEGAL AUTHORITY

A. Foreign Tax Credit

Section 901(a) provides that, if the taxpayer chooses to have the benefits of Subpart A – Foreign Tax Credit, the tax imposed by Chapter 1 shall, subject to the limitation of section 904, be credited with the amounts provided in the applicable paragraph of subsection (b) plus, in the case of a corporation, the taxes deemed to have been paid under sections 902 and 960.

Section 901(b) states that, subject to the limitation of section 904, a domestic corporation is allowed to claim a credit under section 901(a) for the amount of any income, war profits, and excess profits taxes paid or accrued during the taxable year to any foreign country or to any possession of the United States.

Under section 902(a), a domestic corporation which owns 10 percent or more of the voting stock of a foreign corporation from which it receives dividends in any taxable year shall be deemed to have paid the same proportion of such foreign corporation's post-1986 foreign income taxes as the amount of such dividends (determined without regard to section 78), bears to such foreign corporation's post-1986 undistributed earnings.

Section 960(a) provides that, if there is included under section 951(a) in the gross income of a domestic corporation any amount attributable to earnings and profits of a foreign corporation which is a member of a qualified group (as defined in section 902 (b)) with respect to the domestic corporation, then, except to the extent provided in regulations, section 902 shall be applied as if the amount so included were a dividend paid by such foreign corporation.

Under section 902(c)(1), the term "post-1986 undistributed earnings" means the amount of the earnings and profits of the foreign corporation (computed in accordance with sections 964(a) and 986) accumulated in taxable years beginning after December 31, 1986, as of the close of the taxable year of the foreign corporation in which the dividend is distributed, and without diminution by reason of dividends distributed during such taxable year.

Section 902(c)(2) provides that the term "post-1986 foreign income taxes" means the sum of the foreign income taxes with respect to the taxable year of the foreign corporation in which the dividend is distributed, and the foreign income taxes with respect to prior taxable years beginning after December 31, 1986, to the extent such foreign taxes were not attributable to dividends distributed by the foreign corporation in prior taxable years.

However, under section 902(c)(3)(A), if the first day on which the requirements of section 902(c)(3)(B) are met with respect to any foreign corporation is in a taxable year of such corporation beginning after December 31, 1986, the post-1986 undistributed earnings and the post-1986 foreign income taxes of such foreign corporation shall be determined by taking into account only periods beginning on and after the first day of the first taxable year in which such requirements are met. Section 902(c)(3)(B) provides that the requirements of section 902(c)(3)(B) are met with respect to any foreign corporation if 10 percent or more of the voting stock of such foreign corporation is owned by a domestic corporation, or the requirements of section 902(b)(2) (relating to the inclusion of the foreign corporation in a chain of foreign corporations constituting a qualified group) are met with respect to such foreign corporation. See also Treas. Reg. §§1.902-1(a)(8), 1.902-1(a)(9), 1.902-1(a)(10), and 1.902-1(a)(13), defining post-1986 foreign income taxes and post-1986 undistributed earnings with reference to the special effective date provisions of section 902(c)(3).

Section 902(c)(6) provides rules with respect to the treatment of distributions out of earnings accumulated in taxable years beginning before 1987 and in post-1986 taxable years before the requirements of section 902(c)(3)(B) are met with respect to the foreign corporation. Section 902(c)(6)(A) provides that, in the case of any dividend paid by a foreign corporation out of accumulated profits (as defined in section 902 as in effect on the day before the date of the enactment of the Tax Reform Act of 1986) for taxable years beginning before the first taxable year taken into account in determining the post-1986 undistributed earnings of such corporation, section 902 (as amended by the Tax Reform Act of 1986) shall not apply, but section 902 (as in effect on the day before the

date of the enactment of such Act) shall apply. Section 902(c)(6)(B) and Treas. Reg. §1.902-1(b)(2)(i) provide that dividends paid in post-1986 taxable years shall be treated as made first out of post-1986 undistributed earnings to the extent thereof. Under Treas. Reg. §1.902-1(b)(2)(ii), consistent with the law in effect prior to the Tax Reform Act of 1986 and Treas. Reg. §1.902-3, any dividend in excess of post-1986 undistributed earnings is attributable to pre-1987 accumulated profits for a taxable year to the extent thereof, on a last-in, first-out basis. Under section 902(c)(6)(A) and Treas. Reg. §1.902-1(b)(3), foreign taxes deemed paid with respect to dividends paid out of pre-1987 accumulated profits are computed under section 902 and the regulations thereunder as in effect prior to the effective date of the Tax Reform Act of 1986.

Treas. Reg. §1.902-1(a)(10)(i) provides that the term "pre-1987 accumulated profits" means the amount of the earnings and profits of a foreign corporation computed in accordance with section 902 and attributable to its taxable years beginning before January 1, 1987. However, consistent with section 902(c)(6), if the special effective date of section 902(c)(3) and Treas. Reg. §1.902-1(a)(13) applies, pre-1987 accumulated profits also includes any earnings and profits (computed in accordance with sections 964(a) and 986) attributable to the foreign corporation's taxable years beginning after December 31, 1986, but before the first day of the first taxable year of the foreign corporation in which the ownership requirements of section 902(c)(3)(B) and Treas. Reg. §1.902-1(a)(1) through (4) are met with respect to that corporation. Id. Under section 902(c)(6)(A) and Treas. Reg. §1.902-1(a)(10)(ii), the amount of a distribution out of pre-1987 accumulated profits, and the amount of foreign income taxes deemed paid under section 902 with respect thereto, shall be determined and translated into United States dollars by applying the law as in effect prior to the effective date of the Tax Reform Act of 1986.

Treas. Reg. §1.902-1(a)(10)(iii) provides that the term "pre-1987 foreign income taxes" means any foreign income taxes paid, accrued, or deemed paid by a foreign corporation on or with respect to its pre-1987 accumulated profits. Pre-1987 accumulated profits and pre-1987 foreign income taxes are computed and maintained in annual layers in accordance with Treas. Reg. §1.902-3. See Treas. Reg. §§1.902-3(b)(2), (e), and (f).

B. Foreign Tax Redeterminations

Section 905(c)(1) provides that, in general, if (A) accrued taxes when paid differ from the amounts claimed as credits by the taxpayer, (B) accrued taxes are not paid before the date 2 years after the close of the taxable year to which such taxes relate, or (C) any tax paid is refunded in whole or in part, the taxpayer shall notify the Secretary, who shall redetermine the amount of the tax for the year or years affected. Section 905(c)(1) also provides that the Secretary may prescribe adjustments to the pools of post-1986 foreign income taxes and the pools of post-1986 undistributed earnings under sections 902 and 960 in lieu of the redetermination of U.S. tax required under the preceding sentence. Section 989(c)(4) also authorizes regulations providing for alternative

adjustments to the application of section 905(c) that are necessary or appropriate to carry out the purposes of subpart J, relating to transactions in foreign currency.

Section 905(c)(2)(A) provides additional rules for taxes not paid within two years. In general, except as provided in section 905(c)(2)(B), in making the redetermination under section 905(c)(1), no credit is allowed for accrued taxes not paid before the date two years after the close of the taxable year to which such taxes relate. Under section 905(c)(2)(B)(i)(I) and (II), any such taxes if subsequently paid are taken into account, in the case of taxes deemed paid under section 902 or section 960, for the taxable year in which paid (and no redetermination shall be made under section 905 by reason of such payment), and, in any other case, for the taxable year to which such taxes relate.

Section 905(c) was amended and sections 905(c)(1) and 905(c)(2) were added by the Taxpayer Relief Act of 1997 (P.L. 105-34, §1102(a)(2)), effective for taxes which relate to tax years beginning after December 31, 1997. However, under section 902(c)(6) and Treas. Reg. §§1.902-1(a)(10), 1.902-1(b)(2)(ii), and 1.902-1(b)(3), the amount of a distribution out of pre-1987 accumulated profits, and the amount of foreign income taxes deemed paid under section 902 with respect to such a distribution, is determined by applying the law in effect prior to the effective date of the Tax Reform Act of 1986, which did not include the provisions of sections 905(c)(1)(B) and 905(c)(2)(B)(i)(I).

Temporary and proposed regulations published under section 905(c) in 1988, and amended in part in 2007, generally provide that foreign tax redeterminations with respect to post-1986 undistributed earnings are taken into account through prospective adjustments to post-1986 undistributed earnings and post-1986 foreign income taxes, rather than by redetermining the foreign taxes deemed paid and the U.S. tax liability of the foreign corporation's domestic corporate shareholders. See Treas. Reg. §§1.905-3T(a)(2) and 1.905-3T(d)(2)(i). Section 905(c)(2)(B) codified this rule with respect to additional payments of creditable foreign taxes that relate to tax years beginning after December 31, 1997.

Treas. Reg. §1.905-5T provides rules governing the application of section 905(c) to foreign tax redeterminations occurring in taxable years beginning prior to January 1, 1987, and to foreign tax redeterminations occurring after December 31, 1986, with respect to foreign tax deemed paid under section 902 or section 960 with respect to pre-1987 accumulated profits (as defined in Treas. Reg. §1.902-1(a)(10)(i) to include both taxable years beginning before 1987 and post-1986 taxable years beginning before the foreign corporation first had a domestic corporate shareholder eligible to compute foreign taxes deemed paid).

Under Treas. Reg. §1.905-5T(c), the term "foreign tax redetermination" is defined in Treas. Reg. §1.905-3T(c) as a change in foreign tax liability that may affect a taxpayer's foreign tax credit, including additional payments of creditable foreign tax. Section 1.905-5T(d) states that a redetermination of United States tax liability is required with respect to any foreign tax redetermination subject to Treas. Reg. §1.905-5T.

The proposed and temporary regulations under section 905(c) at Treas. Reg. §§1.905-3T, 1.905-4T, and 1.905-5T were published on June 22, 1988, and amended in part by temporary regulations made effective for taxes paid or accrued in taxable years of United States taxpayers beginning on or after November 7, 2007, and taxes paid or accrued by a foreign corporation in its taxable years ending with or within such taxable years of its domestic corporate shareholder. Because the 2007 amendments were not finalized by November 5, 2010, those temporary regulations expired on November 5, 2010. See Treas. Reg. §§1.905-3T(f), 1.905-4T(f)(3), and 1.905-5T(g).

C. Contested Taxes

Treas. Reg. §1.446-1(c)(1)(ii) provides that, in general, under an accrual method, a liability is incurred, and generally is taken into account for Federal income tax purposes, in the taxable year in which all the events have occurred that establish the fact of the liability, the amount of the liability can be determined with reasonable accuracy, and economic performance has occurred with respect to the liability (all events test). Treas. Reg. §1.461-4(g)(6)(i) generally provides that economic performance with respect to tax liabilities occurs as the tax is paid to the governmental authority that imposed the tax. However, Treas. Reg. §1.461-4(g)(6)(iii)(B) provides that certain foreign taxes are excepted from the economic performance (payment) prong of the all events test. That provision states that, if the liability of a taxpayer is to pay an income, war profits, or excess profits tax that is imposed by the authority of any foreign country and is creditable under section 901, economic performance occurs when the requirements of the all events test other than economic performance are met, whether or not the taxpayer elects to credit such taxes under section 901(a).

In Dixie Pine Products Company v. Commissioner (Dixie Pine), 320 U.S. 516 (1944), the Supreme Court considered whether an accrual basis taxpayer could deduct a Mississippi gasoline tax when the taxpayer simultaneously contested the liability. The court considered the all events test and held that this requirement could not be satisfied "where the liability is contingent and is contested by the taxpayer." Id. at 519. The Court concluded that a deduction may be obtained "only for the taxable year in which [the] liability for the tax was finally adjudicated." Id. When applying the contested tax doctrine to a creditable foreign income tax, the court in The Cuba Railroad Company v. United States (Cuba Railroad), 124 F. Supp. 182 (S.D.N.Y., 1954), adopted the Supreme Court's line of reasoning that a contested liability does not accrue until the contest is resolved. However, the district court concluded that section 905(c) modifies the application of the all events test for foreign tax credits. It held that, if a contest involves a foreign tax liability, when the contest is resolved, section 905(c) applies to relate the accrued tax back to, and treat it as having accrued in, the earlier year to which the tax relates. Thus, in Cuba Railroad, taxes paid to Cuba constitute a proper accrual for the purpose of the foreign tax credit for the year to which the taxes relate, although the contested liability was not resolved, and the taxes were not paid, until a later year.

Revenue Rulings 58-55, 1958-1 C.B. 266; 70-290, 1970-1 C.B. 160; and 84-125, 1984-2 C.B. 125, (the Cuba Railroad rulings) provide further guidance with respect to the accrual, relation back, and crediting of contested foreign income taxes. After discussing sections 901(a) and 905(a), Rev. Rul. 58-55 states that the basic purpose of the allowance of a foreign tax credit is to provide a credit against United States income tax on specific income from foreign sources for foreign taxes paid on such income and in this manner to substantially avoid double taxation on the income when earned. The alternative provisions of section 905(a), providing taxpayers using the cash method of accounting a one-time election to claim credits for foreign taxes in the year accrued, demonstrate the special nature of the credit. Allowing a cash basis taxpayer to take the credit in the year in which the foreign tax accrued permits the taxpayer to offset the foreign tax against U.S. income tax due on the same income, thereby relieving double taxation.

Under the all-events test for accrual, contested taxes cannot accrue until the liability is finally determined, but Rev. Rul. 58-55 states that, under the principles stated in Cuba Railroad, and in view of the special nature of the foreign tax credit, as evidenced by its legislative history and concept, the accrual will relate back to the taxable year for which the foreign tax is in dispute. The ruling holds that the "contested tax doctrine," as expressed in Dixie Pine, is not applicable to the accrual of foreign taxes for the purpose of the credit provided in section 901. A foreign tax is accruable for the purpose of such credit for the taxable year to which it relates, even though the taxpayer contests the liability and such tax is not paid until a later year. However, such accrual cannot be made until the contested liability is finally determined. When the contest is resolved, the accrual relates back and credit may be claimed against U.S. tax in the relation-back year.

In Rev. Rul. 70-290, the taxpayer, a domestic corporation, had income from a foreign country in 1967 and 1968 and was assessed an income tax by the government of that foreign country. The tax assessed was paid by the taxpayer. However, the taxpayer was not certain that the amount assessed was its true tax liability, and filed claims for refunds of overassessments of tax for both years. The ruling provides that, to the extent the taxpayer substantiates as provided in section 905(b) that it has actually paid a tax liability it is contesting, the taxpayer may claim a credit under section 901 against its U.S. income tax on foreign source income for the taxable years involved. The ruling notes that, if the protest by the taxpayers against the original assessment prevails and the contested tax is refunded, the amount of the foreign tax credit will be redetermined under section 905(c).

Rev. Rul. 58-55 was amplified by, and Rev. Rul. 70-290 was clarified by, Rev. Rul. 84-125, which illustrates and refines the relation-back doctrine. Under the facts of the ruling, in 1973 foreign country FC asserted that X was liable for 100x dollars of additional FC income tax with respect to X's FC 1971 tax year. X contested the assessment of any such additional liability. Although contesting the assessment of additional taxes and without admitting that any additional amount was due, X in 1973

paid 5x dollars of the asserted deficiency. In 1978, it was finally determined that X was liable for 20x dollars of additional 1971 FC income tax, and in 1978 X paid the remaining 15x dollars of the taxes in satisfaction of the 1978 determination. Rev. Rul. 84-125 addresses the question of to what extent and in what taxable year should an accrual method taxpayer that contests the assessment of additional income tax by a foreign government be allowed a foreign tax credit under section 901 for the contested tax.

Rev. Rul. 84-125 summarized Rev. Rul. 70-290, stating that the latter ruling holds that the provisions of section 905(c) contemplate that credit is to be given for the taxes paid to a foreign government, and that a redetermination of the credit is to be made in the event of a refund of such taxes to the taxpayer by the foreign government. Thus, the portion of contested foreign tax that is actually paid by the taxpayer is accruable for the taxable year to which the foreign tax liability relates, as provided in section 905(a), and such accrual can be made at the time of payment, even though the amount of the tax liability is not finally determined at the time of payment.

Rev. Rul. 84-125 accordingly provides that in 1973 X may claim a credit of 5x dollars against its 1971 U.S. tax for the amount of the additional foreign tax assessment that was contested but actually paid by X in 1973, which is considered to accrue for the taxable year 1971 pursuant to section 905(a). In 1978, subsequent to the final determination of X's additional foreign tax liability, X may claim a foreign tax credit of 15x dollars which relates back and accrues for the taxable year 1971, representing the difference between the portion of the final foreign tax assessment for which X is finally determined to be liable (20x dollars) and the amount previously paid and claimed as a credit by X in 1973 (5x).

ANALYSIS

Because ForCorp4 first became a CFC on Date 1, 2009, when USParent met the requirements of a domestic shareholder under section 902(c)(3)(B) and Treas. Reg. §1.902-1(a)(1), ForCorp4's pools of post-1986 undistributed earnings and post-1986 foreign income taxes include only earnings and taxes for taxable years beginning on and after January 1, 2009, the first day of ForCorp4's first taxable year in which USParent met such ownership requirements. Section 902(c)(3); Treas. Reg. §1.902-1(a)(13).

Earnings and profits accumulated by ForCorp4 prior to January 1, 2009, are pre-1987 accumulated profits attributable to ForCorp4's taxable years beginning before the first day of its first taxable year in which the ownership requirements were met by USParent with respect to ForCorp4. Treas. Reg. §1.902-1(a)(10)(i) and (13). Foreign income taxes paid, accrued, or deemed paid by ForCorp4 on or with respect to its pre-1987 accumulated profits are pre-1987 foreign income taxes. Treas. Reg. §1.902-1(a)(10)(iii). Accordingly, additional amounts of creditable foreign taxes paid by ForCorp4 in 2008 through 2011 with respect to its pre-1987 accumulated profits for its

1994-2008 taxable years are pre-1987 foreign income taxes. These amounts are definitionally excluded from, and so may not be included in, ForCorp4's pool of post-1986 foreign income taxes. Treas. Reg. §§1.902-1(a)(8)(i), 1.902-1(a)(10)(iii), and 1.902-1(a)(13)(i).

Where actual or deemed dividends are attributable to both post-1986 undistributed earnings and pre-1987 accumulated profits, such dividends will be deemed to be paid first out of post-1986 undistributed earnings, to the extent thereof, after which the remainder is attributable to pre-1987 accumulated profits to the extent thereof. Treas. Reg. §1.902-1(b)(2). If a portion of the dividend is paid out of pre-1987 accumulated profits, deemed paid foreign tax credits are determined under section 902 and the regulations thereunder as in effect prior to the effective date of the Tax Reform Act of 1986 (even though such pre-pooling years may include years that are chronologically after 1986). Treas. Reg. §1.902-1(b)(3). The pre-1987 version of section 902 used a year-by-year approach, rather than the multi-year pooling approach used for post-1986 foreign income taxes, to the computation of deemed paid taxes. That is, under pre-1987 law, a separate section 902 computation is made for each taxable year from which earnings are distributed or deemed distributed. For this purpose, distributions are deemed made out of annual accounts of pre-1987 accumulated profits on a last-in, first-out basis. Treas. Reg. §§1.902-1(b)(2)(ii), 1.902-1(b)(3), 1.902-3.

Thus, to the extent that ForCorp4 pays an actual or deemed dividend, Treas. Reg. §1.902-1(b)(2) provides that the dividend is paid first out of post-1986 undistributed earnings, and Treas. Reg. §1.902-1(a)(8)(i) requires that the pool of post-1986 foreign income taxes be reduced by the amount of taxes deemed paid. Under Treas. Reg. §§1.902-1(b)(2)(ii) and 1.902-1(a)(10)(iii), any dividend in excess of post-1986 undistributed earnings is attributable to pre-1987 accumulated profits, and the pre-1987 foreign income taxes of a particular year are reduced by the amount of taxes paid or deemed paid by the foreign corporation on or with respect to the amounts distributed or otherwise included in income from pre-1987 accumulated profits of that taxable year.

As detailed in the Facts portion of this memorandum, ForCorp4 was assessed additional taxes, and therefore had foreign tax redeterminations, with respect to its pre-1987 accumulated profits for 1994 through 2008. ForCorp4 is contesting certain of the tax assessments from the Y Tax Agency and Y States 1, 2, and 3. However, ForCorp4 was required to, and did, pay 50 percent of the assessments pending resolution of the issue. Under the contested tax doctrine, as set out in Cuba Railroad and Revenue Rulings 58-55, 70-290, and 84-125, a contested tax may be accrued while the contest is ongoing, but only to the extent that it has been paid to the foreign government.

In the instant case, under the authority of the revenue rulings, ForCorp4 may include the amount of contested taxes that were paid to Country Y in the appropriate annual layer of pre-1987 foreign income taxes for 1994 through 2008, because those taxes have been paid to the foreign country and ForCorp4 is contesting its liability for such taxes. Therefore, USGroup may be entitled to claim a foreign tax credit with respect to these

taxes, as well as additional amounts of uncontested taxes for those years that were properly accrued and paid by ForCorp4, to the extent they are deemed paid by USParent with respect to a distribution or inclusion of ForCorp4's pre-1987 accumulated profits for the same taxable year. Additional assessments of tax paid with respect to ForCorp4's 2009 and later taxable years are properly accounted for under section 905(c) and Treas. Reg. §1.905-3T by adjusting ForCorp4's post-1986 undistributed earnings and post-1986 foreign income taxes pools in the year those taxes are paid.

USParent argues that, under section 905(c)(2)(B)(i)(I) and Treas. Reg. §1.905-3T(c), foreign taxes deemed paid under section 902 or 960 that are paid more than two years after the year to which the taxes relate must be taken into account in the year the tax is paid. Thus, USParent argues that, for example, under section 905(c)(2)(B)(i)(I), an additional tax assessment with respect to 2002 that ForCorp4 paid in 2009 should decrease ForCorp4's pool of post-1986 undistributed earnings and increase ForCorp4's pool of post-1986 foreign income taxes in 2009 (because 2009 is more than two years after 2002), instead of adjusting ForCorp4's annual layer of pre-1987 accumulated profits and pre-1987 foreign income taxes for 2002.

USParent's position finds no support in the Code, the regulations or sound tax policy. Section 905(c)(2)(B)(i)(I) and Treas. Reg. §1.905-3T(d) do not apply to section 902 computations, including the effect of foreign tax redeterminations on the amount of foreign taxes deemed paid, with respect to pre-1987 accumulated profits. Instead, those computations are governed by the law in effect prior to the Tax Reform Act of 1986. Section 902(c)(6) and Treas. Reg. §1.905-5T.

USParent acknowledges that earnings and profits accumulated by ForCorp4 in taxable years beginning before January 1, 2009, are pre-1987 accumulated profits. Under Treas. Reg. §§1.902-1(a)(10)(iii) and 1.902-3(e) and (f), any foreign income taxes of ForCorp4 that are attributable to pre-1987 accumulated profits, including but not limited to the additional foreign tax assessments paid in 2008 through 2011 with respect to taxable years 1994 through 2008, are pre-1987 foreign income taxes. Under sections 902(c)(3) and 902(c)(6), such pre-1987 foreign income taxes must be taken into account under the annual layering rules of Treas. Reg. §1.902-3 and are definitionally excluded from ForCorp4's pool of post-1986 foreign income taxes. Under section 902(c)(3) and Treas. Reg. §1.902-1(a)(10)(ii), the amount of a distribution out of any pre-1987 accumulated profits, and the amount of foreign income taxes deemed paid under section 902 with respect to such a distribution, is determined by applying the law as in effect prior to the effective date of the Tax Reform Act of 1986.

The regulations under section 905(c) similarly confirm that foreign tax redeterminations with respect to pre-1987 accumulated profits, regardless of when made, are accounted for by adjusting the foreign corporation's pre-1987 accumulated profits and pre-1987 foreign income taxes for the year or years affected, and not by adjusting the corporation's post-1986 undistributed earnings and post-1986 foreign income taxes pools. Treas. Reg. §1.905-3T(a)(2) specifically limits the application of the prospective

pooling adjustment rules of §1.905-3T(d) to foreign tax redeterminations with respect to post-1986 undistributed earnings. As provided in Treas. Reg. §1.905-5T(a), the rules of Treas. Reg. §1.905-5T(d), rather than the rules of Treas. Reg. §1.905-3T(d), apply to foreign tax redeterminations with respect to pre-1987 accumulated profits. As amended in 2007, the section 905(c) temporary regulations were in effect for 2008, 2009, and for almost all of 2010, the years in which ForCorp4 was assessed and paid most of the additional taxes with respect to its pre-1987 accumulated profits for taxable years 1994 through 2008. Under Mayo Foundation for Medical Education & Research v. United States, 131 S. Ct. 704 (2011), these regulations had the force of law until they expired on November 5, 2010. By their terms, the regulations plainly preclude the inclusion in ForCorp4's post-1986 foreign income taxes pool of any additional tax paid with respect to ForCorp4's pre-1987 accumulated profits for its taxable years 1994 through 2008. But in any event, as described in detail above, the plain language of sections 902(c)(3) and 902(c)(6) and the final regulations under those sections mandate the same result.

USParent's attempt to rely on section 905(c)(2)(B)(i)(I) to support a position expressly contradicted by the rules in Treas. Reg. §§1.905-3T and -5T cited above would fail even if the contrary position set out in those regulations and mandated by section 902(c) and the regulations under that section were disregarded. Section 905(c)(2)(B)(i)(I) provides only that additional payments of tax paid by a foreign corporation shall be taken into account in the taxable year in which paid, and no redetermination of U.S. tax shall be made under section 905(c) by reason of such payment. It does not mandate inclusion of pre-1987 foreign income taxes in the post-1986 foreign income taxes pool. Instead, it simply provides that such taxes can only be deemed paid in the year paid or subsequent years, and are not taken into account by redetermining foreign taxes deemed paid (and the U.S. shareholder's U.S. tax) for prior years, including and subsequent to the year or years to which the taxes relate. Here, the required adjustment to the appropriate annual layer of ForCorp4's pre-1987 accumulated profits and pre-1987 foreign income taxes will not require a redetermination of U.S. tax under section 905(c) and Treas. Reg. §1.905-5T, because no portion of ForCorp4's pre-1987 accumulated profits have yet been distributed or otherwise included in USParent's income, and no portion of ForCorp4's pre-1987 foreign income taxes have ever been deemed paid. The required adjustments to ForCorp4's pre-1987 foreign income taxes paid with respect to its pre-1987 accumulated profits for taxable years 1994-2008 will be taken into account in computing USParent's foreign taxes deemed paid only in connection with distributions or inclusions of ForCorp4's pre-1987 accumulated profits in years subsequent to the year in which the additional taxes were paid. Accordingly, even if section 905(c)(2)(B)(i)(I) applied to the additional assessments, (which under sections 902(c)(3) and 902(c)(6), the regulations under those sections, and Treas. Reg. §§1.905-3T and -5T it clearly does not) USParent would still be precluded from including any pre-1987 foreign income taxes of ForCorp4 in its post-1986 foreign income taxes pool.[1]

[1]We note that section 905(c)(2)(B)(i)(I) is effective for taxes that relate to tax years beginning after December 31, 1997. Therefore, in addition to the dispositive reasons

Finally, the conclusion that foreign tax redeterminations with respect to pre-1987 accumulated profits must be taken into account by adjusting the appropriate annual layers of pre-1987 accumulated profits and pre-1987 foreign income taxes is entirely consistent with the purpose of the foreign tax credit to alleviate double taxation of foreign source income. USParent seeks to claim a deemed-paid foreign tax credit for taxes paid with respect to earnings of ForCorp4 that have not been, and may never be, distributed or deemed distributed and subject to tax in the United States. The result USParent seeks, in addition to being squarely contradicted by the statutory and regulatory regime, is flatly inconsistent with the Congressional policy underlying the matching regime established by section 902. See H.H. Robertson v. Commissioner, 59 T.C. 53, 78-79 (1972) (in computing the deemed paid foreign tax credit, accumulated profits of each year must be matched with foreign taxes paid for that year).

Accordingly, any uncontested foreign tax redetermination with respect to its taxable years 1994 through 2008 must be taken into account in ForCorp4's annual layer of pre-1987 foreign income taxes for the appropriate year. Similarly, pending the resolution of the foreign contests, the contested taxes ForCorp4 paid in 2008 through 2011 with respect to taxable years 1994 through 2008 may provisionally be added to ForCorp4's annual layer of pre-1987 foreign income taxes for the appropriate year. None of these taxes may be added to ForCorp4's post-1986 foreign income taxes pool in the year paid. Only taxes paid with respect to ForCorp4's 2009 and later taxable years are properly included in ForCorp4's post-1986 foreign income taxes pool.

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laid out above, USParent cannot rely on that section as support for including taxes paid by ForCorp4 with respect to its pre-1987 accumulated profits for its 1994-1997 taxable years in its post-1986 foreign income taxes pool.