Internal Revenue Service
DEPARTMENT OF THE TREASURY

# LB&I Concept Unit

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|---|---|---|
| **Unit Name** | Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA | |
| **Primary UIL Code** | 9423 | CFC of US Parent |

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| **Shelf** | Business Inbound |
| **Book** | Inbound Financing |
| **Chapter** | Interest Expense Limitation Under IRC 163(j) |

| | |
|---|---|
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## Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA

- IRC 163(j) was first enacted by the Omnibus Act of 1989. This code section and proposed regulations only applied to U.S. corporations or foreign corporations with effectively connected income (ECI) that pay interest to a related person not subject to U.S. tax and was reported on Form 8926. The Tax Cut Jobs Act (TCJA) of 2017 repealed and replaced the prior law effective for tax years beginning after December 31, 2017. The TCJA provision applies to domestic and certain foreign corporations.
- The purpose of the provision is to limit the deductibility of interest. The TCJA IRC 163(j) limits the interest deduction, in general, for all trades or business including those held by individuals, partnerships, corporations and S corporations. The IRC 163(j) limitation is reported on Form 8990 attached to the U.S. tax return  (or attached to Form 5471 for foreign corporations). This Practice Unit will concentrate on the rules as applied to controlled foreign corporations (CFCs).
- The first set of proposed regulations, published in 2018, addressed how to calculate the limitation, what constitutes interest for purposes of the limitation, which taxpayers and trades or businesses are subject to the limitation, and how the limitation generally applies to a consolidated group, partnership, foreign person, and other contexts. Most of the 2018 Proposed Regulations were published as final regulations in 2020 (TD 9905, 85 FR 566806), with some changes made from the 2018 Proposed Regulations. However, most of the international rules, including the rules relating to CFCs, were not finalized in 2020. The 2020 Final Regulations were published in the Federal Register on September 14, 2020, and are generally applicable to tax years beginning on or after November 13, 2020. (Note: An early draft of the 2020 Final Regulations (TD 9905) was released on www.irs.gov in July 2020. But minor changes were made before the regulations were published in the Federal Register. Please refer to the Federal Register version, which is the official version.) In 2020, at the same time that 2020 Final Regulations were published in the Federal Register, new proposed regulations were published. The 2020 Proposed Regulations addressed certain topics not covered in the 2020 Final Regulations, such as certain partnership and international issues. Final regulations, finalizing most of the 2020 Proposed Regulations were published in the Federal Register on January 19, 2021 (TD 9943, 86 FR 5496), although some sections remain in proposed form. The 2021 Final Regulations are generally applicable to tax years beginning on or after March 22, 2021. Relevant sections that remain in proposed form address certain partnership issues under Treas. Reg. 1.163(j)-6, the computation of adjusted taxable income (ATI) by a U.S. shareholder of a CFC under Treas. Reg. 1.163(j)-7, and the application of IRC 163(j) to foreign persons with ECI under Treas. Reg. 1.163(j)-8. (Note: An early draft of the 2021 Final Regulations (TD 9943) was released on www.irs.gov in December 2020. But minor changes were made before the regulations were published in the Federal Register. Please refer to the Federal Register version, which is the official version.)

# General Overview (cont'd-1)

## Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA

- For taxable years beginning after December 31, 2017, and before November 13, 2020:
  - A taxpayer may rely on the 2018 Proposed Regulations. A taxpayer that relies on the 2018 Proposed Regulations must generally follow all of those rules consistently.
  - A taxpayer can choose to apply the 2020 Final Regulations. A taxpayer who chooses to apply the 2020 Final Regulations must generally follow all of those rules consistently.
  - A taxpayer who chooses to apply the 2020 Final Regulations may also rely on the 2020 Proposed Regulations or choose to apply the 2021 Final Regulations, subject to the consistency requirements provided in those regulations.
- For taxable years beginning on or after November 13, 2020, and before March 22, 2021:
  - A taxpayer must apply the 2020 Final Regulations.
  - A taxpayer may rely on the 2020 Proposed Regulations, subject to the consistency requirements provided in the preamble to the 2020 Proposed Regulations.
  - A taxpayer can choose to apply the 2021 Final Regulations, subject to the consistency requirements provided in the 2021 Final Regulations.
- For taxable years beginning on or after March 22, 2021:
  - A taxpayer must apply the 2020 Final Regulations and the 2021 Final Regulations.
  - A taxpayer may rely on the portions of the 2020 Proposed Regulations that have not been finalized, subject to the consistency requirements provided in the preamble to the 2021 Final Regulations.
- There are ordering rules in applying IRC 163(j). It does not apply to interest expense disallowed under IRC 267A and applies after IRC 267(a)(2) and (3). IRC 163(j) will not apply to interest expense properly capitalized under IRC 263A.
- The 2020 Final Regulations allow taxpayers to use any reasonable method for coordinating the interaction of IRCs 163(j) and 250, both of which have a limitation based on taxable income. (The 2018 proposed 163(j) regulations provided an ordering rule under which IRC 250 was taken into account without regard to the IRC 250(a)(2) limitation for purposes of IRC 163(j)).

# General Overview (cont'd-2)

## Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA

- Below is a comparison of the 2018 Proposed Regulations to the 2020 Proposed Regulations and 2021 Final Regulations.

| Change | 2018 | 2020/2021 |
|---|---|---|
| Method of calculation | Aggregates CFC group interest expense and income, reallocates proportional share of net interest expense. Each CFC does a separate IRC 163(j) limitation calculation. Excess taxable income (ETI) tiers-up. | Single IRC 163(j) limitation calculation for CFC group (analogous to consolidated returns approach); eliminates ETI tier-up |
| U.S. shareholder's ATI increase | Yes, through (ETI) tier-up | Yes, through ETI/ATI ratio applied to each CFC's specified deemed inclusions |
| Group election | Two or more CFCs >=80% of the stock by value | Similar, also, stand-alone CFCs; requires formal election on return |
| Election | Irrevocable | Revocable, 60-month waiting period |
| Special sub-groups | Financial services sub-group | No sub-groups |
| CFC group and ECI | No CFCs with ECI can be included in the group | CFC group includes CFCs with ECI but ECI items are placed in a separate "ECI deemed corporation" and such deemed corporation is not part of the CFC group |
| Anti-avoidance | No special rule for CFCs | New principal purpose test |
| Specified period | Majority U.S. shareholder taxable year | Specified group parent taxable year/required year under IRC 898(c)(1) |

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# General Overview (cont'd-3)

## Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA

- Below is a comparison of the 2020 Proposed Regulations to the 2021 Final Regulations.

| Change | 2020 | 2021 |
|---|---|---|
| Foreign taxes | Reduce tentative taxable income | Do not reduce tentative taxable income |
| Anti-abuse rule expanded | Only applies to intragroup transactions that affect ATI | May apply not only to certain intragroup transactions that affect ATI but also to intragroup transactions entered into with a principal purpose of affecting a CFC group or a CFC group member's IRC 163(j) limitation by increasing the CFC group or a CFC group member's business interest income (BII). |
| Safe-harbor | Applies if business interest expense (BIE) does not exceed 30 percent of the lesser of its eligible amount or its qualified tentative taxable income | Expanded the safe harbor to cover applicable CFC's and CFC groups without net BIE (BII => BIE). |

# Relevant Key Factors

| Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA |
|---|
| **Key Factors** |
| ▪ A Form 5471 is filed with the Form 1120 return reporting BIE through Form 8990. |

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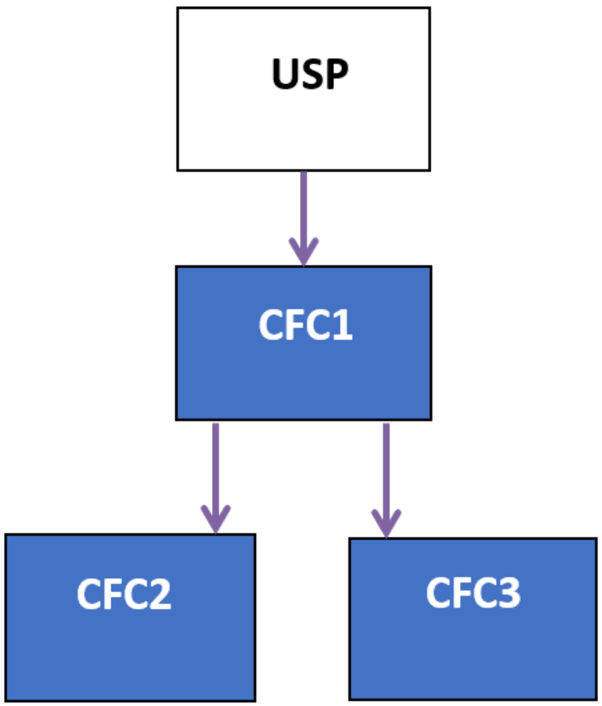
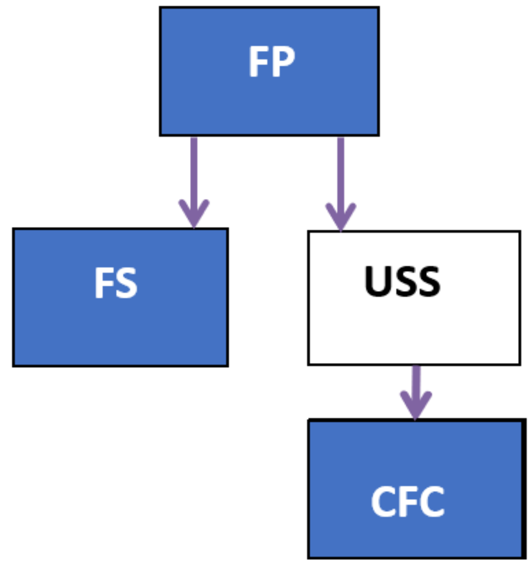
# Diagram of Concept

## Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA

### Diagram of Concept




USP is the U.S. parent corporation and owns three CFCs with Form 5471 filing requirements reporting interest expense. USP and the CFCs are subject to IRC 163(j).

FP is the foreign parent corporation and owns a foreign sub and a U.S. sub, USS. USS owns a CFC with a Form 5471 filing requirements reporting interest expense. USS and CFC are subject to the IRC 163(j) limitation.

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# Detailed Explanation of the Concept

## Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA

The TCJA IRC 163(j) limits the interest deduction, in general, for all trades or business including those owned by individuals, partnerships, corporations and S corporations.

| Analysis | Resources |
|---|---|
| ▪ Treas. Reg. 1.163(j)-7 applies to CFCs and their U.S shareholders, as defined in IRC 951(b). The IRC 163(j) limitation generally applies to CFCs in the same manner as domestic C corporations, with several modifications. The general IRC 163(j) training materials are found in the Virtual Library, in the Issues Affecting Various Return Types Knowledge Base and specifically in the IRC Section 163(j) Business Interest Expense Limitation Book. The resources on this site deal with all issues (outside of CFCs and Effectively Connected Income which are on the CBA KB Virtual Library) such as the definition of BIE, BII, taxable income (TI), ATI, the small business exception, and general exemption elections, etc.<br>▪ The regulation limits the extent to which U.S. shareholders can shift their interest deductions to CFCs in order to reduce their subpart F income and/or Global Intangible Low-Taxed Income (GILTI).<br>▪ Generally, if an exemption or exception does not apply and the CFC has business interest expense, then Form 8990, Limitation on Business Interest Expense Under Section 163(j) must be attached to its Form 5471*, Information Return of U.S. Persons With Respect to Certain Foreign Corporations*.<br>▪ A taxpayer can calculate the limitation separately for each separate CFC or make a CFC group election to calculate one aggregated limitation for all members in the CFC group. | ▪ IRC 163(j) – *Limitation on Deduction For Interest On Certain Indebtedness*<br>▪ Treas. Reg. 1.163(j)-7 - *Application of the Section 163(j) Limitation to Foreign Corporations and United States Shareholders*<br>▪ Treas. Reg. 1.163(j)-7(b) – *General Rule Regarding the Application of Section 163(j) to Relevant Foreign Corporations*<br>▪ IRC 957 – *Controlled Foreign Corporations; United States Persons*<br>▪ IRC 951(b) – *United States Shareholder Defined*<br>▪ Form 8990 – *Limitation on Business Interest Expense Under Section 163(j)*<br>▪ Form 5471 – *Information Return of U.S. Persons With Respect to Certain Foreign Corporations* |

# Detailed Explanation of the Concept (cont'd-1)

<table>
<tr><th colspan="2">Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA</th></tr>
<tr><th>Analysis</th><th>Resources</th></tr>
<tr><td>

- A CFC group means, for a specified period, all CFC group members for their specified taxable years ending with or within the specified period. The duration of the group continues until the CFC group election is revoked or there is no longer a specified period with respect to the specified group. If a CFC group election is in effect and a CFC joins and becomes a specified group member, then it becomes a CFC group member. If a CFC ceases to be a specified group member, the CFC group continues, and the election will terminate solely with respect to the CFC leaving the group.
- The election applies to each specified group member for its entire specified taxable year that ends with or within the specified period. Each designated U.S person must file a CFC group election statement with their return detailing the CFCs included and their specified taxable years. If an election is terminated, then there is a 60-month waiting period to re-elect a new CFC group.
- The designated U.S person with respect to a stand-alone applicable CFC is each controlling domestic shareholder, as defined in Treas. Reg. 1.964-1(c)(5) of the applicable CFC.
- The designated U.S person with respect to a specified group is:
  - The specified group parent, if the specified group parent is a qualified U.S person, or
  - Each controlling domestic shareholder, as defined in Treas. Reg. 1.964-1(c)(5), of the specified group parent, if the specified group parent is an applicable CFC. (Those U.S. shareholders who own in the aggregate more than 50% of the total combined voting power of all classes of the stock of the foreign corporation entitled to vote and who undertake to act on its behalf. If the U.S. shareholders do not own in the aggregate more than 50% as described above, then the controlling U.S. shareholders shall be all those U.S. shareholders who own stock of such corporation within the meaning of IRC 958(a).)

</td><td>

- Treas. Reg. 1.163(j)-7(c) – *Application of Section 163(j) to CFC Group Members of a CFC Group*
- Treas. Reg. 1.163(j)-7(e)(5) – *Manner of Making or Revoking a CFC Group Election*
- Treas. Reg. 1.163(j)-7(k)(12) – *Designated U.S. Person*
- Treas. Reg. 1.964-1(c)(5) – *Controlling Domestic Shareholders*

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# Detailed Explanation of the Concept (cont'd-2)

| Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA | |
|---|---|
| **Analysis** | **Resources** |
| ▪ Specified group member - The rules for who is a member of a CFC group (that is, a specified group for which a CFC group election is made) are found under Treas. Reg. 1.163(j)-7(d). A specified group includes one or more chains of applicable CFCs connected through stock ownership with a specified group parent. An entity must be an applicable CFC to be included. A specified group parent must own 80% of stock by value, directly or indirectly, in one or more applicable CFC. The specified group parent must be either a qualified U.S. person (which excludes partnerships) or an applicable CFC. A consolidated group that files or is required to file a U.S consolidated income tax return is treated as a single qualified U.S. person. Indirect ownership only occurs through a partnership or estate/trust under IRC 318(a)(2)(A) or (B). In addition, 80% of the stock (by value) in each applicable CFC must be directly or indirectly owned by another group member. | ▪ Treas. Reg.1.163(j)-7(d) – *Determination of a Specified Group and Specified Group Members*<br>▪ IRC 318 – *Constructive Ownership of Stock* |
| ▪ Specified period - The specified period will depend on the identity of the specified group parent. If the specified group parent is a qualified U.S person, then the period will be that U.S person's taxable year. If the specified group parent is an applicable CFC, then the period will be the specified group's parent's required taxable year determined under IRC 898(c)(1), without regard to IRC 898(c)(2). IRC 898 deals with the taxable year of foreign corporations and (c)(1) states the required year is the majority U.S. shareholder's year when there is a majority shareholder. (The 2018 proposed regulations defaulted to the majority U.S. shareholder's taxable year.) | ▪ Treas. Reg. 1.163(j)-7(k)(29) – *Specified Period*<br>▪ IRC 898 – *Taxable Year of Certain Foreign Corporations* |

# Detailed Explanation of the Concept (cont'd-3)

| Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA | |
|---|---|
| **Analysis** | **Resources** |
| ▪ A single IRC 163(j) limitation is computed for a specified period of a CFC group. The CFC group's current year BIE, disallowed BIE carryforwards, BII, floor plan financing interest expense, and ATI for a specified period equal the sums of each CFC group member's current year BIE, disallowed BIE carryforwards, BII, floor plan financing interest expense, and ATI for its specified taxable year with respect to the specified period. A CFC group member's current year BIE, disallowed BIE carryforwards, BII, floor plan financing interest expense, and ATI are generally determined on a separate company basis. ATI of a CFC group member may be less than zero, but the ATI of the CFC group may not be less than zero. | ▪ Treas. Reg. 1.163(j)-7(c)(2) – *Calculation of Section 163(j) Limitation for a CFC Group for a Specified Period* |
| ▪ Any transaction between related group members of a CFC group that is entered into with a principal purpose of affecting a CFC group or a CFC group member's IRC 163(j) limitation by increasing or decreasing a CFC group or CFC group member's ATI or BII for a specified taxable year is disregarded for purposes of IRC 163(j). | ▪ Treas. Reg. 1.163(j)-7(c)(2)(ii) – *Certain Transactions Between CFC Group Members Disregarded* |

# Detailed Explanation of the Concept (cont'd-4)

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<tr><th>Analysis</th><th>Resources</th></tr>
<tr><td>

- Current-year business interest expense is deducted in the current taxable year before any disallowed business interest expense carryforwards from a prior taxable year are deducted in that year. Disallowed business interest expense carryforwards are deducted in the order of the taxable years in which they arose, beginning with the earliest taxable year, subject to certain limitations.
- If a CFC group calculates its limitation and the allowable amount is greater than current year BIE plus carryforward(s) of disallowed BIE from prior years, then each group member deducts total BIE without limitation. Members may still be subject to limitation under other provisions of the code.
- If a CFC group calculates its limitation and the allowable amount is greater than current year BIE, but less than current year BIE plus carryforward of disallowed BIE from prior years:
  - Each CFC group member deducts its current year BIE without limitation.
  - The CFC group members deduct (subject to the remaining limitation) BIE carryforwards beginning with the earliest year, allocated pro rata for each year based on each member's relative share of the group's BIE carryforwards for the year.
- If allowable amount is less than current year BIE:
  - Each CFC group member first deducts its current year BIE up to its own BII.
  - Remaining current year BIE deducted (subject to remaining limitation) on a pro rata basis, based on CFC member's relative share of group's remaining current year BIE.

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- Treas. Reg. 1.163(j)-5(b)(2) – *Deduction of Business Interest Expense*

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# Detailed Explanation of the Concept (cont'd-5)

| Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA | |
|---|---|
| **Analysis** | **Resources** |
| ▪ Items of a CFC group member are translated into a single currency for the CFC group and back to the functional currency of the CFC group member using the average exchange rate for the CFC group member's specified taxable year. The single currency for the CFC group may be the U.S. dollar or the functional currency of a plurality of the CFC group members.<br>▪ Only ATI, BII, BIE of an applicable CFC that are not attributable to ECI are included in the CFC group's IRC 163(j) calculations. If a CFC does have ECI, the ECI of the applicable CFC is treated as income of a separate CFC called an "ECI deemed corporation" and such deemed corporation is not included in the CFC group. Disallowed BIE carryforwards retain their character.<br>▪ The rules for foreign persons with ECI are described under Prop. Reg. 1.163(j)-8. | ▪ Treas. Reg. 1.163(j)-7(c)(4) – *Currency Translation*<br>▪ Treas. Reg. 1.163(j)-7(f) – *Treatment of a CFC Group Member That Has ECI*<br>▪ Proposed Treas. Reg. 1.163(j)-8 – *Application of the Section 163(j) Limitation to Foreign Persons with Effectively Connected Income* |

# Detailed Explanation of the Concept (cont'd-6)

| Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA | |
|---|---|
| **Analysis** | **Resources** |
| ▪ Safe harbor election - Taxpayers may make a safe harbor election and if made, no portion of an applicable CFC's BIE is disallowed. The safe harbor election is an annual election made by each designated U.S person for a CFC group or for a stand-alone applicable CFC. The election must be made no later than the due date (including extensions) of the original federal income tax return by attaching an election statement. The election is only available if no group member has pre-group BIE carryforwards.<br>▪ To qualify for the safe harbor, the BIE must be less than BII, or must be less than or equal to 30% of the lesser of qualified tentative taxable income (QTTI) or the eligible amount. The eligible amount is defined as the amount that would be included in gross income by a domestic corporation that wholly owned the stand-alone applicable CFC or the CFC group members under IRCs 951(a) (subpart F) and 951A (GILTI), net of related deductions under IRCs 245A and 250. The eligible amount is determined by only taking into account items attributable to non-excepted trades or businesses. For 2019 and 2020, substitute the 50% for the 30%.<br>▪ For a CFC group, the computation is done on a group-wide basis. | ▪ Treas. Reg. 1.163(j)-7(h) – *Election to Apply Safe Harbor*<br>▪ IRC 952 – *Subpart F Income Defined*<br>▪ IRC 250 – *Foreign-Derived Intangible Income* |

# Detailed Explanation of the Concept (cont'd-7)

| Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA | |
|---|---|
| **Analysis** | **Resources** |
| Special Rules:<br>▪ Foreign Taxes - Under the proposed regulations, foreign taxes reduced tentative taxable income. However, in the final regulations, foreign taxes do not reduce tentative taxable income.<br>▪ Negative ATI - The final regulations clarified that the general rule providing that ATI cannot be negative applies with respect to the ATI of a CFC group, rather than a CFC group member.<br>▪ Special Pre-group BIE carryforward rule in the final regulations - Separate return limitation year (SRLY) - like rules apply for CFCs joining the group with a pre-group disallowed BIE carryforward. Pre-group disallowed BIE carryforwards that are included in any CFC group member's BIE deduction for any specified year may not exceed the aggregate IRC 163(j) limitation for specified periods of the CFC group determined by reference only to the CFC group member's items of income, gain, deduction and loss, and reduced (but not below zero) by the CFC group member's BIE (including disallowed BIE carryforwards) taken into account as a deduction in all specified taxable years in which the CFC group member has continuously been a CFC group member. | ▪ Treas. Regs. 1.163(j)-7(g)(3) – *Treatment of Certain Foreign Income Taxes*<br>▪ Treas. Regs. 1.163(j)-7(c)(2) – *Calculation of Section 163(j) Limitation for a CFC Group for a Specified Period*<br>▪ Treas. Regs. 1.163(j)-7(c)(3)(B)(iv) – *Limitation on Pre-group Disallowed Business Interest Expense Carryforward* |

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# Detailed Explanation of the Concept (cont'd-8)

| Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA | |
|---|---|
| **Analysis** | **Resources** |
| ▪ If a specified group member of a specified group or an applicable partnership (specified lender) includes an amount (payment amount) in income and such amount is attributable to BIE incurred by another specified group member or an applicable partnership of the specified group (specified borrower) during its taxable year, then the ATI of the specified borrower for the taxable year is increased by the ATI adjustment amount if:<br>− The BIE is incurred with a principal purpose of reducing the federal income tax liability of any U.S. shareholder of a specified group member (including over other taxable years);<br>− Absent the application of anti-abuse rule, the effect of the specified borrower treating all or part of the payment amount as disallowed BIE would be to reduce the federal income tax liability of any U.S. shareholder of a specified group member; and<br>− Either no CFC group election is in effect with respect to the specified group or the specified borrower is an applicable partnership. | ▪ Treas. Reg. 1.163(j)-7(g)(4) – *Anti-Abuse Rule* |

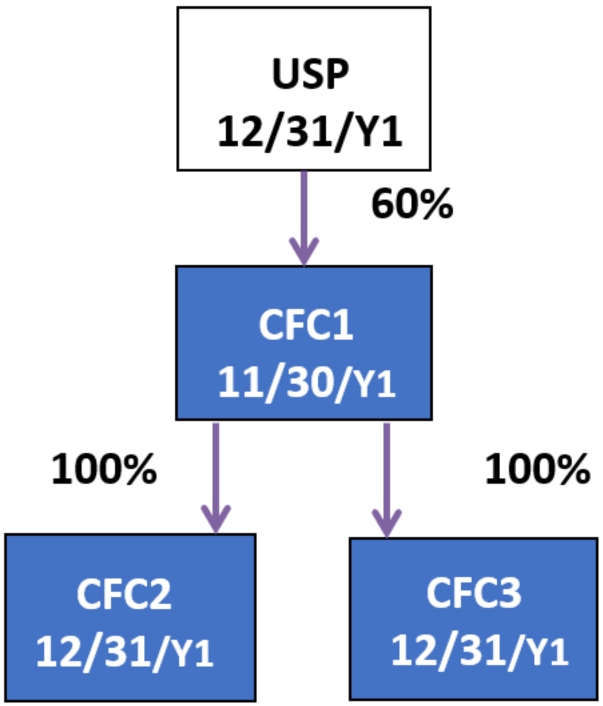
# Detailed Explanation of the Concept (cont'd-9)

| Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA | |
|---|---|
| **Analysis** | **Resources** |
| U.S shareholders' ATI - A U.S shareholder's ATI excludes GILTI inclusion, subpart F inclusion, and the IRC 78 gross-up. Under the 2020 proposed regulations, a portion of the GILTI and subpart F inclusion (but not the IRC 78 gross-up) may be added back. That portion is calculated by applying a CFC's ETI/ATI ratio. The add-back is only available to the U.S. shareholders of stand-alone applicable CFCs and CFC group members if the CFC or CFC group has ETI and with respect to a CFC group member, a CFC group election has been made. To the extent that a CFC group election is not in effect, a U.S. shareholder may not increase its ATI for any portion of its GILTI or subpart F inclusion attributable to a specified group member of a specified group.<br>▪ There is no ATI increase if the safe-harbor election is made.<br>▪ These rules were not finalized as part of the 2021 Final Regulations and remain proposed regulations. | ▪ Treas. Reg. 1.163(j)-1(b)(1)(ii)(G)<br>▪ Proposed Treas. Reg. 1.163(j)-7(j) |

# Examples of the Concept

## Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA

### Examples




Here is an example of how a CFC group election might be made. USP owns 60% of CFC1, which wholly owns CFC2 and CFC3. USP could separately calculate the limitation for each CFC or elect to make a CFC group Election. If it makes a group election, USP still files separate Forms 8990 for each CFC reporting BIE, BII and ATI separately for each CFC but calculates the limitation on a CFC group basis and files a separate Form 8990 for the CFC group under the 2021 Final Regulations. If the CFC group election is made, all three CFCs must be part of the group.

The specified parent will be CFC1 as it owns more than 80% of the value of CFC2 and CFC3.

Next, let's analyze the specified period. USP files on a 12/31 tax year end, and so does CFC2 and CFC3. CFC1 files on an 11/30 year end. Treas. Reg. 1.163-7(k)(29) states that if an applicable CFC is the specified group parent, the specified period is the specified group parent's required year under IRC 898(c)(1), which defaults to the majority U.S shareholder's taxable year. In this case, that is USP. Therefore, the specified period will be its taxable year of 1/1 to 12/31.

# Examples of the Concept (cont'd-1)

**Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA**

**Example 1**

**CF = Carryforward**

| CFC Group | Separate (current year) BIE | Separate BIE CF |
|---|---|---|
| CFC1 | 5 | 10 |
| CFC2 | 15 | 5 |

**Assume the CFC group limitation is $50 and all carryforwards arose in the same year. Below is the proration of the limitation.**

| Item | CFC1 | CFC2 | Total |
|---|---|---|---|
| Separate current year BIE (table above) | $5 | $15 | $20 |
| Allowed current year BIE | $5 | $15 | $20 |
| Remaining limitation | See total | See total | ($50–20) = $30 |
| Separate BIE CF | $10 | $5 | $15 |
| Allowed BIE CF | $10 | $5 | $15 |
| Remaining BIE CF to next year | $0 | $0 | $0 |

# Examples of the Concept (cont'd-2)

**Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA**

**Example 2**

| CFC Group | Separate (current year) BIE | Separate BIE CF |
|---|---|---|
| CFC1 | 5 | 10 |
| CFC2 | 15 | 5 |

**Assume the CFC group limitation is $25 and all carryforwards arose in the same year. Below is the proration of the limitation.**

| Item | CFC1 | CFC2 | Total |
|---|---|---|---|
| Separate current year BIE (table above) | $5 | $15 | $20 |
| Allowed current BIE | $5 | $15 | $20 |
| Remaining limitation | See total | See total | ($25−20) = $5 |
| Separate BIE CF | $10 | $5 | $15 |
| Allowed BIE CF | 5*(10/15)=$3.33 | 5*(5/15)=$1.67 | $5 |
| Separate BIE CF to next year | $6.67 | $3.33 | $10 |

# Examples of the Concept (cont'd-3)

| Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA |
|---|
| Example 3 |

| CFC Group | Separate (current year) BIE | Separate BIE CF |
|---|---|---|
| CFC1 | 5 | 10 |
| CFC2 | 15 | 5 |

**Assume the CFC group limitation is $5, all carryforwards arose in the same year and neither CFC has BII or floor plan financing interest expense. Below is the proration of the limitation.**

| Item | CFC1 | CFC2 | Total |
|---|---|---|---|
| Separate current year BIE (table above) | $5 | $15 | $20>limitation so must allocate |
| Pro-rata limitation | $5*(5/20) = $1.25 | $5*(15/20) = $3.75 | $5 |
| Separate BIE CF to next year | (5−1.25) +10 = $13.75 | (15−3.75) +5 = $16.25 | $30 |

# Examples of the Concept (cont'd-4)

**Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA**

**Example 4**

| CFC Group | Separate (Current year) BIE | BIE CF | BII |
|---|---|---|---|
| CFC1 | 10 | 10 | 5 |
| CFC2 | 15 | 5 | |

**Assume the CFC group limitation is $15 and all carryforwards arose in the same year. Below is the proration of the limitation.**

| Item | CFC1 | CFC2 | Total |
|---|---|---|---|
| Separate current year BIE up to BII | $5 | | $5 |
| Remaining separate current year BIE | $5 | $15 | $20 |
| Additional allowed current year BIE | $10*(5/20) = $2.50 | $10*(15/20) = $7.50 | $10 |
| Total allowed BIE per CFC | $5+2.50 = $7.50 | $7.50 | $15 |
| Separate BIE CF | $10+2.50 = $12.50 | $5+7.50 = $12.50 | $25 |

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# Examples of the Concept (cont'd-5)

| Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA |
|---|
| **Example 5** |

**Example with BIE CFs from Multiple Years**

**Assume neither CFC has BII or floor plan financing interest expense. CFC group limitation is $25.**

**Facts:**

| CFC Group | Separate (current year) BIE | BIE CF Year 1 | BIE CF Year 2 | Total |
|---|---|---|---|---|
| CFC1 | 5 | 10 | 5 | 20 |
| CFC2 | 15 | 5 | 10 | 30 |
| Total | 20 | 15 | 15 | 50 |

# Examples of the Concept (cont'd-6)

**Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA**

**Example 5 (cont'd)**

**Example with BIE CFs from Multiple Years (cont'd)**

**Analysis:**

| Item | CFC1 | CFC2 | Total |
|---|---|---|---|
| Separate current year BIE (above) | $5 | $15 | $20 |
| Allowed current year BIE | $5 | $15 | $20 |
| Remaining limitation | See total | See total | ($25−20) = $5 |
| Separate BIE CF YR1 allocated first | $10 | $5 | $15 |
| Allowed BIE CF | $5*(10⁄15) = $3.33 | $5*(5⁄15) = $1.67 | $5 |
| Disallowed BIE CF (YR1 remaining + all of YR2) | YR1 (10−3.33) + YR2 (5) = $11.67 | YR1 (5−1.67) + YR2 (10) = $13.33 | $25 |

# Examples of the Concept (cont'd-7)

**Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA**

**Example 6**

**U.S. Shareholder's ATI Example**

Assumptions:

- No ECI
- No floor plan financing interest
- No BII
- A CFC group election has been made

- Group ETI = 251*((251*30%)-55)/(251*30%) = 67.67
- Another way of stating group ETI is: ATI-(Net BIE/30%)= ETI or 251-(55/30%) = 67.67
- CFC1 ETI = 67.67*33.86% = 22.92
- CFC2 ETI = 67.67*22.31% = 15.10
- CFC3 ETI = 67.67*43.82% = 29.65

| CFC Group | ATI | ATI% | BIE | ETI | ETI/ATI |
|---|---|---|---|---|---|
| CFC1 | 85.00 | 33.86% | 35.00 | 22.92 | 0.2696 |
| CFC2 | 56.00 | 22.31% | 20.00 | 15.10 | 0.2696 |
| CFC3 | 110.00 | 43.82% | - | 29.65 | 0.2696 |
| Group | 251.00 | 100% | 55.00 | 67.67 | 0.2696 |

# Examples of the Concept (cont'd-8)

**Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA**

**Example 6 (cont'd)**

**U.S. Shareholder's ATI Example (cont'd)**

| CFC Group | ETI/ATI |
|---|---|
| CFC1 | 0.2696 |
| CFC2 | 0.2696 |
| CFC3 | 0.2696 |

| Item | Decreases (specified deemed inclusions) | Increases (related to specified deemed inclusions) |
|---|---|---|
| Sub F | $10 | 10*26.96% = $2.70 |
| GILTI (net of IRC 250 deduction) | $22.50 | 22.50*26.96% = $6.07 |
| 956 | $5 | 5*26.96% = $1.35 |
| 78 gross up | $2.50 | - |
| **Total** | **$40** | **$10.11** |

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# Index of Referenced Resources

| Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA |
|---|
| IRC 163(j) |
| IRC 250 |
| IRC 267 |
| IRC 267A |
| IRC 318 |
| IRC 898 |
| IRC 951 |
| IRC 952 |
| IRC 957 |
| IRC 958 |
| Treas. Reg. 1.163(j) |
| Treas. Reg. 1.964-1(c)(5) |
| Proposed Treas. Reg. 1.163(j) |
| TD 9905, 85 FR 566806 |
| TD 9943, 86 FR 5496 |
| Form 5471 |
| Form 8990 |

# Training and Additional Resources

| Interest Expense Limitation Under IRC 163(j) for Controlled Foreign Corporations Post-TCJA | |
|---|---|
| **Type of Resource** | **Description(s)** |
| Saba Meeting Sessions | ▪ *(CBA) Inbound Financing 163(j) Post-Tax Cut and Jobs Act Part 1* - 2021 Saba Meeting<br>▪ (*CBA) 163(j) In-Depth International Provisions Part 2* - 2021 CPE Saba Meeting |
| Issue Toolkits | ▪ Audit Tool – International Treas. Reg. 1.163(j)-7 Considerations<br>▪ Domestic Tools<br>− 163(j) Issue Guide<br>− 163(j) Risk Tool<br>− 163(j) Worksheet<br>− 163(j) Proforma IDR |
| Other Training Materials | ▪ *IRC 163(j) Limitation on Business Interest Expense-Risking Corporate Returns* – ITM 79319 |

# Glossary of Terms and Acronyms

| Term/Acronym | Definition |
|---|---|
| ATI | Adjusted Taxable Income |
| BIE | Business Interest Expense |
| BII | Business Interest Income |
| CF | Carryforward |
| CFC | Controlled Foreign Corporation |
| ECI | Effectively Connected Income |
| ETI | Excess Taxable Income |
| FDII | Foreign Derived Intangible Income |
| GILTI | Global Intangible Low-Taxed Income |
| QTTI | Qualified Tentative Taxable Income |
| TCJA | Tax Cut and Jobs Act of 2017 |
| TI | Taxable Income |

# Index of Related Practice Units

| Associated UIL(s) | Related Practice Unit |
|---|---|
| 9423 | *Ability to Service and Repay the Debt* |
| 9423 | *Arm's Length Standard under IRC Section 482 for Rate of Interest Charged on Intercompany Debt* |
| 9423 | *Bona Fide Debt Determination* |
| 9423 | *Deductibility of Foreign Related Party Financing Guarantee Fees* |
| 9423 | *Dividend Distribution with a Debt Issuance* |
| 9423 | *The General and Funding Rules of Treasury Regulations Section 1.385-3* |
| 9423 | *Guarantee Fee Pricing Methods* |
| 9423 | *Hybrid Instrument with a Repurchase Agreement* |
| 9423 | *Interest Expense Limitation Computation Under IRC 163(j) – Pre TCJA* |
| 9423 | *Interest Expense Limitation on Related Foreign Party Loans Under IRC 267(a)(3)* |
| 9423 | *IRC 245A(e) – Anti-hybrid Rules* |
| 9423 | *IRC 482 Arm's Length Interest Rate for Intercompany Debt* |
| 9423 | *TCJA Anti-Hybrid Rules of IRC 267A* |