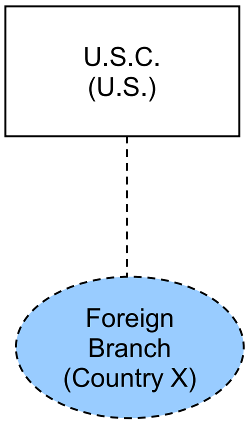
Reg. 1.901-1(c)(4), Example

Foreign Tax Paid in a Credit Year But Relates to a Prior Deduction Year



(i) Facts. U.S.C. is a domestic corporation that is engaged in a trade or business in Country X through a branch. U.S.C. uses the accrual method of accounting and a calendar year for U.S. and Country X tax purposes.
For taxable Years 1 through 3, U.S.C. deducted foreign income taxes accrued in those years. In Years 4 through 6, U.S.C. claimed a credit for foreign income taxes accrued in those years. In Year 6, U.S.C. paid an additional $50x tax to Country X that relates to Year 1 because of the close of a Country X tax audit.

(ii) Analysis. The additional $50x Country X tax paid by U.S.C. in Year 6 that relates to Year 1 cannot be claimed by U.S.C. as a deduction on an amended return for Year 1 because the additional tax accrued in Year 6. See section 461(f) (flush language); Reg. 1.461-1(a)(2)(i) and Reg. 1.461-2(a)(2). In addition, because the additional $50x Country X tax relates to and is considered to accrue in Year 1 for foreign tax credit purposes, U.S.C. cannot claim a credit for the additional $50x Country X tax on its Federal income tax return for Year 6. See Reg. 1.905-1(d)(1). However, pursuant to Reg. 1.901-1(c)(3), U.S.C. can claim a deduction for the additional $50x Country X tax that relates to Year 1 on its Federal income tax return for Year 6, even though it claims a credit for foreign income taxes that accrue in Year 6 and that relate to Year 6.