

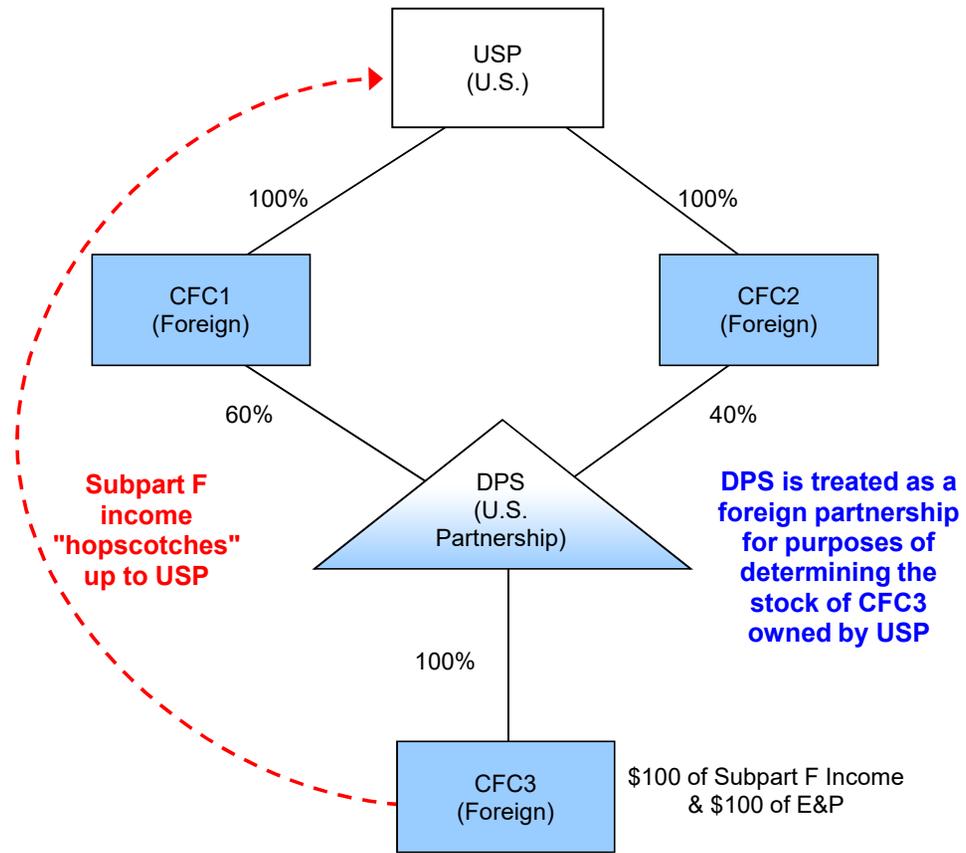
**Prop. Reg. 1.951-1(h)(3),
Example**

Subpart F Income Partnership Blocker

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USP, a domestic corporation, owns all of the stock of CFC1 and CFC2. CFC1 and CFC2 own 60% and 40%, respectively, of the interests in the capital and profits of DPS, a domestic partnership. DPS owns all of the stock of CFC3. Each of CFC1, CFC2, and CFC3 is a controlled foreign corporation. USP, DPS, CFC1, CFC2, and CFC3 all use the calendar year as their taxable year. For Year 1, CFC3 has \$100x of subpart F income (as defined under section 952) and \$100x of earnings and profits.

DPS is a controlled domestic partnership with respect to USP within the meaning of Prop. Reg. 1.951-1(h)(2) because more than 50% of the interests in its capital or profits are owned by persons related to USP within the meaning of section 267(b) (that is, CFC1 and CFC2), and thus DPS is controlled by USP and related persons.



Without regard to Prop. Reg. 1.951-1(h), DPS is a United States shareholder that owns (within the meaning of section 958(a)) stock of CFC3, a controlled foreign corporation. If DPS were treated as foreign, CFC3 would continue to be a controlled foreign corporation, and USP would be treated as owning (within the meaning of section 958(a)) stock in CFC3 through CFC1 and CFC2, which are both partners in DPS. Thus, under Prop. Reg. 1.951-1(h)(1), DPS is treated as a foreign partnership for purposes of determining the stock of CFC3 owned (within the meaning of section 958(a)) by USP. Accordingly, USP's pro rata share of CFC3's subpart F income for Year 1 is \$100x, and USP includes in its gross income \$100x under section 951(a)(1)(A). DPS is not a United States shareholder of CFC3 for purposes of sections 951 through 964.