

and the selling corporation is engaged within less developed countries, in connection with sales of such property, in continuous operational activities which are substantial in relation to such sales, as evidenced, for example, by the maintenance within less developed countries of a substantial sales or service organization or substantial facilities for the storage, handling, transportation, assembly, packaging, or servicing of such property.

(2) *Production defined.* For purposes of this paragraph, the term "produced" means manufactured, grown, extracted, or constructed and includes a substantial transformation of property purchased for resale or the manufacture of a product when purchased components constitute part of the property which is sold. See paragraph (a)(4)(ii) and (iii) of § 1.954-3 for a statement and illustration of the principles set forth in the preceding sentence.

[T.D. 6683, 28 FR 11183, Oct. 18, 1963, as amended by T.D. 6688, 28 FR 11632, Oct. 31, 1963]

§ 1.955A-1 Shareholder's pro rata share of amount of previously excluded subpart F income withdrawn from investment in foreign base company shipping operations.

(a) *In general.* Section 955 provides rules for determining the amount of a controlled foreign corporation's previously excluded subpart F income which is withdrawn for any taxable year beginning after December 31, 1975, from investment in foreign base company shipping operations. Pursuant to section 951(a)(1)(A)(iii) and the regulations thereunder, a United States shareholder of such controlled foreign corporation must include in his gross income his pro rata share of such amount as determined in accordance with paragraph (c) of this section.

(b) *Amount withdrawn by controlled foreign corporation—(1) In general.* For purposes of sections 951 through 964, the amount of a controlled foreign corporation's previously excluded subpart F income which is withdrawn for any taxable year from investment in foreign base company shipping operations is an amount equal to the decrease for such year in such corporation's qualified investments in foreign base com-

pany shipping operations. Such decrease is, except as provided in § 1.955A-4—

(i) An amount equal to the excess of the amount of its qualified investments in foreign base company shipping operations at the close of the preceding taxable year over the amount of its qualified investments in foreign base company shipping operations at the close of the taxable year, minus

(ii) The amount (if any) by which recognized losses on sales or exchanges by such corporation during the taxable year of qualified investments in foreign base company shipping operations exceed its recognized gains on sales or exchanges during such year of qualified investments in foreign base company shipping operations,

but only to the extent that the net amount so determined does not exceed the limitation determined under subparagraph (2) of this paragraph. See § 1.955A-2 for determining the amount of qualified investments in foreign base company shipping operations.

(2) *Limitation applicable in determining decreases—(i) In general.* The limitation referred to in subparagraph (i) of this paragraph for any taxable year of a controlled foreign corporation shall be the lesser of the following two limitations:

(A) The sum of (1) the controlled foreign corporation's earnings and profits (or deficit in earnings and profits) for the taxable year, computed as of the close of the taxable year without diminution by reason of any distribution made during the taxable year, (2) the sum of its earnings and profits (or deficits in earnings and profits) accumulated for prior taxable years beginning after December 31, 1975, and (3) the amount described in subparagraph (3) of this paragraph; or

(B) The sum of the amounts excluded under section 954(b)(2) (see subparagraph (4) of this paragraph) from the foreign base company income of such corporation for all prior taxable years beginning after December 31, 1975, minus the sum of the amounts (determined under this paragraph) of its previously excluded subpart F income withdrawn from investment in foreign base company shipping operations for all such prior taxable years.

(C) For purposes of the immediately preceding subparagraph (B), the amount excluded under section 954(b)(2) for a taxable year of a controlled foreign corporation (the “first corporation”) includes (1) an amount excluded under section 954(b)(2) by another corporation which is a member of a related group (as defined in § 1.955A-3(b)(1)) attributable to the first corporation’s excess investment (see § 1.955A-3(c)(4)) for a taxable year beginning after December 31, 1983, (2) an amount excluded by a corporation under § 1.954-1(b)(4)(ii)(b) by reason of the application of the carryover rule there set forth, and (3) an amount equal to the first corporation’s pro rata share of a group excess deduction (see § 1.955A-3(c)(2)) of a related group for a taxable year beginning after December 31, 1983 (but not in excess of that portion of such pro rata share which would reduce the first corporation’s foreign base company shipping income to zero). Such amounts will not be treated as excluded under section 954(b)(2) by any other corporation.

(ii) *Certain exclusions from earnings and profits.* For purposes of determining the earnings and profits of a controlled foreign corporation under subdivision (i)(A)(1) and (2) of this subparagraph, such earnings and profits shall be considered not to include any amounts which are attributable to—

(A)(1) Amounts which, for the current taxable year, are included in the gross income of a United States shareholder of such controlled foreign corporation under section 951(a)(1)(A)(i), or

(2) Amounts which, for any prior taxable year, have been included in the gross income of a United States shareholder of such controlled foreign corporation under section 951(a) and have not been distributed; or

(B)(1) Amounts which, for the current taxable year, are included in the gross income of a United States shareholder of such controlled foreign corporation under section 551(b) or would be so included under such section but for the fact that such amounts were distributed to such shareholder during the taxable year, or

(2) Amounts which, for any prior taxable year, have been included in the

gross income of a United States shareholder of such controlled foreign corporation under section 551(b) and have not been distributed.

The rules of this subdivision apply only in determining the limitation on a controlled foreign corporation’s decrease in qualified investments in foreign base company shipping operations. See section 959 and the regulations thereunder for rules relating to the exclusion from gross income of previously taxed earnings and profits.

(3) *Carryover of amounts relating to investments in less developed country shipping companies—(i) In general.* The amount described in this subparagraph for any taxable year of a controlled foreign corporation beginning after December 31, 1975, is the lesser of—

(A) The excess of the amount described in subdivision (ii) of this subparagraph, over the amount described in subdivision (iii) of this subparagraph, or

(B) The limitation determined under subdivision (iv) of this subparagraph.

(ii) *Previously excluded subpart F income invested in less developed country shipping companies.* The amount described in this subdivision for all taxable years of a controlled foreign corporation beginning after December 31, 1975, is the lesser of—

(A) The amount of such corporation’s qualified investments (determined under § 1.955-2 other than paragraph (b)(5) thereof) in less developed country shipping companies described in § 1.955-5(b) at the close of the last taxable year of such corporation beginning before January 1, 1976, or

(B) The limitation determined under § 1.955-1(b)(2)(i)(b) (relating to previously excluded subpart F income) for the first taxable year of such corporation beginning after January 1, 1976.

(iii) *Amounts previously carried over.* The amount described in this subdivision for any taxable year of a controlled foreign corporation shall be the sum of the excesses determined for each prior taxable year beginning after December 31, 1976, of—

(A) The amount (determined under this paragraph) of such corporation’s previously excluded subpart F income withdrawn from investment in foreign

base company shipping operations, over

(B) The sum of the earnings and profits determined under subparagraph (2)(i)(A)(I) and (2) of this paragraph.

(iv) *Extent attributable to accumulated earnings and profits.* The limitation determined under this subdivision for any taxable year of a controlled foreign corporation is the sum of such controlled foreign corporation's earnings and profits (or deficits in earnings and profits) accumulated for taxable years beginning after December 31, 1962, and before January 1, 1976. For purposes of the preceding sentence, earnings and profits shall be determined by excluding the amounts described in subparagraph (2)(ii)(A) and (B) of this paragraph.

(v) *Illustration.* The application of this subparagraph may be illustrated by the following example:

Example. (a) Throughout the period here involved, A is a United States shareholder of controlled foreign corporation M. M is not a foreign personal holding company, and M uses the calendar year as the taxable year.

(b) The amount described in this subparagraph for M's taxable year 1978 with respect to A is determined as follows, based on the facts shown in the following table:

| | |
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| (1) Investment in less developed country shipping companies on December 31, 1975 (subdivision (ii)(A) amount) | \$10,000 |
| (2) § 1.955-1(b)(2)(i)(b) limitation for 1976 (previously excluded subpart F income not withdrawn from investment in less developed countries) (subdivision (ii)(B) amount) | 50,000 |
| (3) Subdivision (ii) amount (lesser of lines (1) and (2)) | 10,000 |
| (4) Subdivision (iii) amount: Excess for 1977 of M's previously excluded subpart F income withdrawn from investment in foreign base country shipping operations, \$3,000, over the sum of the amounts determined under subparagraphs (2)(i)(A)(1) and (2) of this paragraph, \$1,000 | 2,000 |
| (5) Excess of line (3) over line (4) | 8,000 |
| (6) Sum of M's earnings and profits accumulated for 1962 through 1975, determined on December 31, 1978 | 26,000 |
| (7) Amount described in this subparagraph for 1978 (lesser of line (5) and line (6)) | 8,000 |

(c) For 1978, M's earnings and profits (reduced as provided in § 1.955-1(b)(2)(ii)(a)(I)) are \$19,000, and the amount of M's previously excluded subpart F income withdrawn from investment in less developed countries determined under § 1.955-1(b) is \$42,000. Consequently, \$23,000 of M's earnings and profits accumulated for 1962 through 1975 are attributable to such \$42,000 amount, and will

therefore be excluded under subparagraph (2)(ii)(A)(2) of this paragraph from M's earnings and profits accumulated for 1962 through 1975, determined as of December 31, 1979. No other portion of M's earnings and profits accumulated for 1962 through 1975 is distributed or included in the gross income of a United States shareholder in 1978.

(d) The amount described in this subparagraph for M's taxable year 1979 with respect to A is determined as follows, based on the additional facts shown in the following table:

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| (1) Subdivision (ii) amount (line (3) from paragraph (b) of this example) | \$10,000 |
| (2) Subdivision (iii) amount: (i) Excess for 1977 from line (4) of paragraph (b) of this example | 2,000 |
| (ii) Plus: excess for 1978 of M's previously excluded subpart F income withdrawn from investment in foreign base country shipping operations, \$6,000, over the sum of the amounts determined under subparagraphs (2)(i)(A)(1) and (2) of this paragraph, \$25,000 | 0 |
| (iii) Subdivision (ii) amount | 2,000 |
| (3) Excess of line (1) over line (2)(iii) | 8,000 |
| (4) Sum of M's earnings and profits accumulated for 1962 through 1975, determined on December 31, 1979 (\$26,000 minus \$23,000) | 3,000 |
| (5) Amount described in this subparagraph for 1979 (lesser of line (3) and line (4)) | 3,000 |

(4) *Amount excluded.* For purposes of subparagraph (2)(i)(B) of this paragraph, the amount excluded under section 954(b)(2) from the foreign base company income of a controlled foreign corporation for any taxable year beginning after December 31, 1975, is the excess of—

(i) The amount which would have been equal to the subpart F income of such corporation for such taxable year if such corporation had had no increase in qualified investments in foreign base company shipping operations for such taxable year, over

(ii) The subpart F income of such corporation for such taxable year.

(c) *Shareholder's pro rata share of amount withdrawn by controlled foreign corporation—(1) In general.* A United States shareholder's pro rata share of a controlled foreign corporation's previously excluded subpart F income withdrawn for any taxable year from investment in foreign base company shipping operations is his pro rata share of the amount withdrawn for such year by such corporation, as determined under paragraph (b) of this

section. See section 955(a)(3). Such pro rata share shall be determined in accordance with the principles of § 1.195-1(e).

(2) *Special rule.* A United States shareholder's pro rata share of the net amount determined under paragraph (b)(2)(i)(B) of this section with respect to any stock of the controlled foreign corporation owned by such shareholder shall be determined without taking into account any amount attributable to a period prior to the date on which such shareholder acquired such stock. See section 1248 and the regulations thereunder for rules governing treatment of gain from sales or exchanges of stock in certain foreign corporations.

(d) *Illustrations.* The application of this section may be illustrated by the following examples:

Example 1. A, a United States shareholder, owns 60 percent of the only class of stock of M Corporation, a controlled foreign corporation throughout the entire period here involved. Both A and M use the calendar year as a taxable year. The amount of M's previously excluded subpart F income withdrawn for 1978 from investment in foreign base company shipping operations is \$40,000, and A's pro rata share of such amount is \$24,000 determined as follows based on the facts shown in the following table:

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| (a) Qualified investments in foreign base company shipping operations at the close of 1977 | \$125,000 |
| (b) Less: qualified investments in foreign base company shipping operations at the close of 1978 | 75,000 |
| (c) Balance | 50,000 |
| (d) Less: excess of recognized losses (\$15,000) over recognized gains (\$5,000) on sales during 1978 of qualified investments in foreign base company shipping operations ... | 10,000 |
| (e) Tentative decrease in qualified investment in foreign base company shipping operations for 1978 | 40,000 |
| (f) Earnings and profits for 1976, 1977, and 1978 | 45,000 |
| (g) Plus: amount determined under paragraph (b)(3) of this section | 0 |
| (h) Earnings and profits limitation | 45,000 |
| (i) Excess of amount excluded under section 954(b)(2) from foreign base company income for 1976 (\$75,000) over amount of previously excluded subpart F income withdrawn for 1977 from investment in foreign base company shipping operations (\$25,000) | 50,000 |
| (j) M's amount of previously excluded subpart F income withdrawn for 1978 from investment in foreign base company shipping operations (item (e)), but not to exceed the lesser of item (h) or item (i) | 40,000 |

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| (k) A's pro rata share of M Corporation's amount of previously excluded subpart F income withdrawn for 1978 from investment in foreign base company shipping operations (60 percent of \$40,000) | 24,000 |
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Example 2. The facts are the same as in example 1, except that M's earnings and profits (determined under paragraph (b)(2) of this section) for 1976, 1977, and 1978 (item (f)) are \$30,000 instead of \$45,000. M's amount of previously excluded subpart F income withdrawn for 1978 from investment in foreign base company shipping operations is \$30,000. A's pro rata share of such amount is \$18,000 (60 percent of \$30,000).

Example 3. The facts are the same as in example 1, except that the excess of the amount excluded under section 954(b)(2) for 1976 from M Corporation's foreign base company income over the amount of its previously excluded subpart F income withdrawn for 1977 from investment in foreign base company shipping operations (item (i)) is \$20,000 instead of \$50,000. M's amount of previously excluded subpart F income withdrawn for 1978 from investment in foreign base company shipping operations is \$20,000. A's pro rata share of such amount is \$12,000 (60 percent of \$20,000).

[T.D. 7894, 48 FR 22530, May 19, 1983; 48 FR 40888, Sept. 12, 1983]

§ 1.955A-2 Amount of a controlled foreign corporation's qualified investments in foreign base company shipping operations.

(a) *Qualified investments*—(1) *In general.* Under section 955(b), for purposes of sections 951 through 964, a controlled foreign corporation's "qualified investments in foreign base company shipping operations" are investments in—

(i) Any aircraft or vessel, to the extent that such aircraft or vessel is used (or hired or leased for use) in foreign commerce,

(ii) Related shipping assets (within the meaning of paragraph (b) of this section),

(iii) Stock or obligations of a related controlled foreign corporation, to the extent provided in paragraph (c) of this section,

(iv) A partnership, to the extent provided in paragraph (d) of this section, and

(v) Stock or obligations of a less developed country shipping company described in § 1.955-5(b), as provided in paragraph (h) of this section.

(2) *Coordination of provisions.* No amount shall be counted as a qualified