

that appropriate adjustments are made to eliminate duplicate benefits arising from application of 26 CFR 1.904(f)-12T(h) to taxable years that are not open for assessment. In addition, if a taxpayer that is a financial services entity (as defined in §1.904-4(e)(3)) chooses to apply 26 CFR 1.904(f)-12T(h) to taxable years ending before April 7, 2011, then as of the beginning of the taxpayer's first taxable year ending on or after April 7, 2011 any remaining balance in a passive category loss account that is attributable to a loss account in a pre-2007 separate category for high withholding tax interest shall be allocated to the general category or eliminated pursuant to §1.904(f)-12(h)(4), and any remaining balance in a separate limitation loss account with respect to passive category income that is attributable to a loss account with respect to a pre-2007 separate category for high withholding tax interest will be recaptured in such year and subsequent taxable years as general category income or eliminated pursuant to §1.904(f)-12(h)(4).

[T.D. 8306, 55 FR 31381, Aug. 2, 1990, as amended by T.D. 9260, 71 FR 24539, Apr. 25, 2006; T.D. 9368, 72 FR 72591, Dec. 21, 2007; T.D. 9452, 74 FR 27886, June 11, 2009; T.D. 9521, 76 FR 19273, Apr. 7, 2011]

§ 1.904(g)-0 Outline of regulation provisions.

This section lists the headings for §§ 1.904(g)-1 through 1.904(g)-3.

§ 1.904(g)-1 Overall domestic loss and the overall domestic loss account.

- (a) Overview of regulations.
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 - (1) In general.
 - (2) Taxable year in which overall domestic loss is sustained.
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 - (1) Overall domestic loss defined.
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 - (3) Qualified taxable year defined.
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- (d) Additions to overall domestic loss accounts.
 - (1) General rule.
 - (2) Overall domestic loss of another taxpayer.
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- (1) Pre-recapture reduction for amounts allocated to other taxpayers.
- (2) Reduction for amounts recaptured.
- (f) Effective/applicability date.

§ 1.904(g)-2 Recapture of overall domestic losses.

- (a) In general.
- (b) Determination of U.S. source taxable income for purposes of recapture.
- (c) Section 904(g)(1) recapture.
- (d) Effective/applicability date.

§ 1.904(g)-3 Ordering rules for the allocation of net operating losses, net capital losses, U.S. source losses, and separate limitation losses, and for recapture of separate limitation losses, overall foreign losses, and overall domestic losses.

- (a) In general.
- (b) Step One: Allocation of net operating loss and net capital loss carryovers.
 - (1) In general.
 - (2) Full net operating loss carryover.
 - (3) Partial net operating loss carryover.
 - (4) Net capital loss carryovers.
- (c) Step Two: Section 904(b) adjustments.
- (d) Step Three: Allocation of separate limitation losses.
- (e) Step Four: Allocation of U.S. source losses.
- (f) Step Five: Recapture of overall foreign loss accounts.
- (g) Step Six: Recapture of separate limitation loss accounts.
- (h) Step Seven: Recapture of overall domestic loss accounts.
 - (i) [Reserved]
 - (j) Examples.
 - (k) Effective/applicability date.

[T.D. 9371, 72 FR 72599, Dec. 21, 2007, as amended by T.D. 9595, 77 FR 37580, June 22, 2012]

§ 1.904(g)-1 Overall domestic loss and the overall domestic loss account.

(a) *Overview of regulations.* This section provides rules for determining a taxpayer's overall domestic losses, for establishing overall domestic loss accounts, and for making additions to and reducing such accounts for purposes of section 904(g). Section 1.904(g)-2 provides rules for recapturing the balance in any overall domestic loss account under the general recharacterization rule of section 904(g)(1). Section 1.904(g)-3 provides ordering rules for the allocation of net operating losses, net capital losses, U.S. source losses, and separate limitation losses, and the recapture of separate limitation losses,

overall foreign losses and overall domestic losses.

(b) *Overall domestic loss accounts*—(1) *In general.* Any taxpayer that sustains an overall domestic loss under paragraph (c) of this section must establish an overall domestic loss account for such loss with respect to each separate category, as defined in § 1.904(f)-7(b)(1), of the taxpayer in which foreign source income is offset by the domestic loss. The balance in each overall domestic loss account represents the amount of such overall domestic loss subject to recapture in a given taxable year. From year to year, amounts may be added to or subtracted from the balances in such loss accounts as provided in paragraphs (d) and (e) of this section.

(2) *Taxable year in which overall domestic loss is sustained.* When a domestic loss is carried back or carried forward as part of a net operating loss, and offsets foreign source income in a carry-over year, the resulting overall domestic loss is treated as sustained in the later of the year in which the domestic loss was incurred or the year to which the loss was carried. Accordingly, when a taxpayer incurs a domestic loss that is carried back as part of a net operating loss to offset foreign source income in a qualified taxable year, as defined in paragraph (c)(3) of this section, the resulting overall domestic loss is treated as sustained in the later year in which the domestic loss was incurred and not in the earlier year in which the loss offset foreign source income. In addition, when a taxpayer incurs a domestic loss that is carried forward as part of a net operating loss and applied to offset foreign source income in a later taxable year, the resulting overall domestic loss is treated as sustained in the later year in which the domestic loss offsets foreign source income and not in the earlier year in which the loss was incurred. For example, if a taxpayer incurs a domestic loss in the 2007 taxable year that is carried back to the 2006 qualified taxable year and offsets foreign source income in 2006, the resulting overall domestic loss is treated as sustained in the 2007 taxable year. If a taxpayer incurs a domestic loss in a pre-2007 taxable year that is carried forward to a post-2006 quali-

fied taxable year and offsets foreign source income in the post-2006 year, the resulting overall domestic loss is treated as sustained in the post-2006 year. An overall domestic loss account is established, or increased under paragraph (d) of this section, at the end of the taxable year in which the overall domestic loss is treated as sustained and will be recaptured from U.S. source income arising in subsequent taxable years.

(c) *Determination of a taxpayer's overall domestic loss*—(1) *Overall domestic loss defined.* For taxable years beginning after December 31, 2006, a taxpayer sustains an overall domestic loss—

(i) In any qualified taxable year in which its domestic loss for such taxable year offsets foreign source taxable income for the taxable year or for any preceding qualified taxable year by reason of a carryback; and

(ii) In any other taxable year in which the domestic loss for such taxable year offsets foreign source taxable income for any preceding qualified taxable year by reason of a carryback.

(2) *Domestic loss defined.* For purposes of this section and §§ 1.904(g)-2 and 1.904(g)-3, the term *domestic loss* means the amount by which the U.S. source gross income for the taxable year is exceeded by the sum of the expenses, losses, and other deductions properly apportioned or allocated to such income, taking into account any net operating loss carried forward from a prior taxable year, but not any loss carried back. If a taxpayer has any capital gains or losses or qualified dividend income, as defined in section 1(h)(11), the amount of the taxpayer's domestic loss that offsets foreign source income must be determined taking into account adjustments under section 904(b)(2). See § 1.904(g)-1(d)(3) for further guidance.

(3) *Qualified taxable year defined.* For purposes of this section and §§ 1.904(g)-2 and 1.904(g)-3, the term *qualified taxable year* means any taxable year for which the taxpayer chooses the benefits of section 901.

(4) *Method of allocation and apportionment of deductions.* In determining its overall domestic loss, a taxpayer shall allocate and apportion expenses, losses, and other deductions to U.S. source

gross income in accordance with sections 861(b) and 865 and the regulations thereunder, including §§1.861-8 through 1.861-14T.

(d) *Additions to overall domestic loss accounts*—(1) *General rule.* A taxpayer's overall domestic loss as determined under paragraph (c) of this section shall be added to the applicable overall domestic loss account at the end of its taxable year to the extent that the overall domestic loss either reduces foreign source income for the year (but only if such year is a qualified taxable year) or reduces foreign source income for a qualified taxable year to which the loss has been carried back.

(2) *Overall domestic loss of another taxpayer.* If any portion of any overall domestic loss of another taxpayer is allocated to the taxpayer in accordance with §1.1502-9 (relating to consolidated overall domestic losses) the taxpayer shall add such amount to its applicable overall domestic loss account.

(3) *Adjustments for capital gains and losses.* If the taxpayer has capital gains or losses or qualified dividend income, the amount by which a domestic loss is considered to reduce foreign source income in a taxable year shall equal the section 904(f)(5)(D) amount determined under §1.904(b)-1(h)(1)(iii), regardless of the amount of domestic loss that was determined before taking any section 904(b)(2) adjustments into account.

(e) *Reductions of overall domestic loss accounts.* The taxpayer shall subtract the following amounts from its overall domestic loss accounts at the end of its taxable year in the following order, as applicable:

(1) *Pre-recapture reduction for amounts allocated to other taxpayers.* An overall domestic loss account is reduced by the amount of any overall domestic loss which is allocated to another taxpayer in accordance with §1.1502-9 (relating to consolidated overall domestic losses).

(2) *Reduction for amounts recaptured.* An overall domestic loss account is reduced by the amount of any U.S. source income that is recharacterized in accordance with §1.904(g)-2(c) (relating to recapture under section 904(g)(1)).

(f) *Effective/applicability date.* This section applies to taxpayers that sus-

tain an overall domestic loss for a taxable year beginning on or after January 1, 2012. Taxpayers may choose to apply this section to overall domestic losses sustained in other taxable years beginning after December 31, 2006, including periods covered by 26 CFR §1.904(g)-1T (revised as of April 1, 2010).

[T.D. 9595, 77 FR 37580, June 22, 2012]

§ 1.904(g)-2 Recapture of overall domestic losses.

(a) *In general.* A taxpayer shall recapture an overall domestic loss as provided in this section. Recapture is accomplished by treating a portion of the taxpayer's U.S. source taxable income as foreign source income. The recharacterized income is allocated among and increases foreign source income in separate categories in proportion to the balances of the overall domestic loss accounts with respect to those separate categories. As a result, if the taxpayer chooses the benefits of section 901, the taxpayer's foreign tax credit limitation is increased. As provided in §1.904(g)-1(e)(2), the balance in a taxpayer's overall domestic loss account with respect to a separate category is reduced at the end of each taxable year by the amount of loss recaptured during that taxable year. Recapture continues until the amount of U.S. source income recharacterized as foreign source income equals the amount in the overall domestic loss account.

(b) *Determination of U.S. source taxable income for purposes of recapture.* For purposes of determining the amount of an overall domestic loss subject to recapture, the taxpayer's taxable income from U.S. sources shall be computed in accordance with the rules set forth in §1.904(g)-1(c)(4). U.S. source taxable income shall be determined by taking into account adjustments for capital gains and losses and qualified dividend income in a similar manner to the adjustments made to foreign source taxable income under section 904(b)(2) and §1.904(b)-1, following the principles of §1.904(b)-1(h)(1)(i).

(c) *Section 904(g)(1) recapture.* The amount of any U.S. source taxable income subject to recharacterization in a taxable year in which paragraph (a) of this section applies is the lesser of the