¶725 Foreign Tax Credit Limitation Baskets

NEW LAW EXPLAINED

Foreign tax credit limitation basket added.— A new separate foreign tax credit limitation basket is added for foreign branch income (Code Sec. 904(d)(1)(B), as added by the Tax Cuts and Jobs). Foreign branch income means the business profits of a U.S. person that are attributable to one or more qualified business units (QBUs) in one or more foreign countries. A QBU is defined as any separate and clearly identified unit of a trade or business of a taxpayer that maintains separate books and records (Code Sec. 989(b)). The rules for determining the amount of business profits attributable to a QBU will be set forth in regulations (Code Sec. 904(d)(2)(J)(i), as added by the 2017 Tax Cuts Act).

COMMENT

The income of a foreign branch is subject to U.S. tax and a foreign tax credit may be claimed. If the foreign branch is located in a high-tax country, absent the new foreign tax credit limitation basket, those taxes could offset taxes paid in low-tax countries in the general category basket. The addition of the new basket also means that carrybacks and carryforwards of excess foreign tax credits in the foreign branch company basket will be allowed only to the extent of the excess limitation in the basket.

The additional foreign tax credit limitation basket does not apply to income of the foreign branch that is passive category income (Code Sec. 904(d)(2)(J)(ii)). Passive category income includes passive income and specified passive income (Code Sec. 904(d)(2)(A)(i);Reg. §1.904-4(b)(1)). Passive income is generally any type of income that would qualify as subpart F income foreign personal holding company income under Code Sec. 954(c) if the recipient was a controlled foreign corporation (CFC) (e.g., dividends, interest, rents, royalties, and annuities). Specified passive category income includes dividends from a domestic international sales corporation (DISC) or former DISC and distributions from a former foreign sales corporation (FSC) (Code Sec. 904(d)(2)(v); Reg. §1.904-4(b)(3)).

COMMENT

Passive category income is typically low-taxed income that would not be subject to cross-crediting.

A new separate foreign tax credit limitation basket was also added for global intangible low-taxed income (see¶735).

Effective date. The amendments made by this section apply tax years beginning after December 31, 2017 (Act Sec. 14302(c) of the Tax Cuts and Jobs Act).