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# Proposed Regulations Regarding the Aggregate Treatment for Pass-Through Owners of PFIC Stock

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On January 25, 2022, the Internal Revenue Service (the "IRS") and the Department of the Treasury ("Treasury") released regulations (the "Final Regulations") finalizing provisions in prior proposed regulations which generally would treat domestic partnerships as *aggregates* of their partners (rather than as entities) for purposes of determining income inclusions under the Subpart F provisions applicable to certain shareholders of controlled foreign corporations.[1] Under the aggregate approach, a partner in a domestic partnership would have a Subpart F inclusion from an underlying CFC only if the partner itself is a US shareholder of the CFC.

The IRS and Treasury also released new proposed regulations (the "Proposed Regulations") which would broaden the aggregation approach to domestic partnerships and S corporations that own stock of passive foreign investment companies ("PFICs"). Under the Proposed Regulations, this aggregation treatment would apply for purposes of making the qualified electing fund ("QEF") election or the PFIC mark-to-market ("MTM") election, recognizing QEF inclusions or MTM amounts, making PFIC purging elections, the CFC overlap rule, and filing Forms 8621. Thus, for example, a domestic partner, rather than the domestic partnership, would make a QEF election (and file Form 8621) in respect of PFIC stock held by the partnership.[2]

The Proposed Regulations would require each electing partner (or S corporation shareholder) to notify the partnership (or S corporation), respectively, of its election in order to assist the partnership (or S corporation) with information reporting and tracking basis in the QEF stock. In addition, each partner (and S corporation shareholder) would include its pro rata share of ordinary earnings and net capital gain attributable to the QEF stock as if such person owned its share of the QEF stock directly, and not as a share of the pass-through entity's income.

Responding to questions regarding the administrability of the aggregate approach, the Treasury Department and the IRS request comments on whether the final regulations should permit a domestic partnership-level (or S corporation-level) QEF election on behalf of its partners (or shareholders). With respect to preexisting QEF elections made by a domestic partnership (or an S corporation), the Proposed Regulations would effectively treat the preexisting QEF election as if it were made by each partner or S corporation shareholder owning an interest in the preexisting QEF.

The Final Regulations apply to tax years of a foreign corporation beginning on or after the date that the regulations are filed with the Federal Register. Domestic partnerships may, however, apply the regulations to tax years of a foreign corporation beginning after 2017, subject to consistency requirements. The Proposed Regulations would apply to tax years beginning on or after the date adopted as final regulations.

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[1] The Subpart F provisions include sections 951 through 965 of the Internal Revenue Code (the "Code"). Note that the aggregate approach does not apply for purposes of Code section 1248 or for determining whether a foreign corporation is a controlled foreign corporation (a "CFC").

[2] The Proposed Regulations also contain certain other changes, generally conforming to the aggregate treatment paradigm, including guidance regarding the determination of the controlling domestic shareholders of foreign corporations, the owner of a controlled foreign corporation or QEF that makes an election under section 1411, the treatment of S corporations with accumulated earnings and profits under the Subpart F provisions, and the determination and inclusion of related person insurance income ("RPII") under Code section 953(c).

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