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Overview of corporate alternative minimum tax (CAMT) proposed regulations

Tax Alert

Overview

On September 12, 2024, Treasury and the IRS released proposed regulations (REG-112129-23) which provide guidance on the application of the corporate alternative minimum tax (CAMT) under sections 55, 56A, 59(k) and (l).

Proposed Regulations

The proposed regulations provide definitions and general rules for determining and identifying applicable financial statement income (AFSI). The proposed regulations also address adjustments to AFSI under section 56A and certain tax consolidated return issues. Certain adjustments are not covered in detail in this Tax Alert.

In general, the proposed regulations are proposed to apply to taxable years ending after September 13, 2024 (for example, 2024 tax year for calendar year taxpayers), with certain sections proposed to apply to taxable years ending after the date of publication of final regulations in the Federal Register. Special applicability dates apply in the case of tax consolidated groups. Refer to the **appendix** for more information on reliance on the proposed regulations and applicability dates.

The preamble to the proposed regulations provides that a taxpayer may rely on the interim guidance provided in sections 3 through 7 of Notice 2023–7 (as modified and clarified by Notice 2023–64), sections 3 through 5 of Notice 2023–20, and sections 3 through 14 of Notice 2023–64, for taxable years ending on or before September 13, 2024.

Applicable Corporations and Foreign-Parented Multinational Groups (FPMGs)

Prop. Treas. Reg. § 1.59-2: General Rules for Determining Applicable Corporation Status

- Prop. Treas. Reg. § 1.59-2 provides rules under section 59(k) for purposes of determining whether a corporation is an applicable corporation.
- Corporations that are not members of a FPMG (described below).
  - In general, the rules are consistent with section 59(k), including taking into account AFSI of section 52(a) or (b) group members, and disregarding certain adjustments to AFSI.
  - A corporation that has a different taxable year than a single employer group member includes the AFSI of such member for the taxable year of such member that ends with or within the taxable year of the corporation.
- Passthrough entity considerations with respect to the Status Test.
  - The applicable corporation status test rules in the proposed regulations with respect to partnerships are generally consistent with Notice 2023-64. For example, the proposed regulations confirm that for purposes of the applicable corporation status test ("Status Test"), there is no adjustment to AFSI of a CAMT entity for its distributive share of partnership AFSI under section 56A(c)(2)(D)(i) (that is, the distributive share adjustment rule does not apply for purposes of the Status Test).
  - The proposed regulations provide rules for purposes of the Status Test to prevent "double counting" of income or loss from partnership investments when a partnership is treated as part of an aggregation group with a corporate partner under section 52(b).
  - The proposed regulations also exclude income attributable to non-controlling interests for purposes of the Status Test when a corporation consolidates a partnership but is not related to the partnership under section 52(b).
  - With respect to the application of section 52(b) and what constitutes "trades or businesses under common control," the proposed regulations apply the constructive ownership rules under section 52(b) that are set forth in the current regulations. The proposed regulations do not define a "trade or business" for purposes of applying the single employer rules under section 52(b) (that is, the proposed regulations do not clarify whether a "trade or business" is defined under section 162, 212, or 174 for these purposes).
  - The proposed regulations also provide that, although an S corporation, a RIC, or a REIT is excluded from the definition of an "applicable corporation," the S corporation, RIC, or REIT is not excluded from being treated as a single employer under section 52(a) or (b) for purposes of the Status Test (that is, the AFSI of an S corporation, RIC, or REIT could still potentially cause a C corporation that is part of the same single employer group to be an applicable corporation).
- FPMGs
  - For purposes of the $1 billion test, the proposed regulations provide that:
    - The AFSI taken into account is the AFSI of (i) the FPMG corporation (that is, the entity being tested for applicable corporation status), (ii) all other members of the FPMG, and (iii) any other person that is part of its section 52 group.
    - The corporation being tested for applicable corporation status must be a member of a FPMG on the first or last day of its taxable year.
    - The proposed regulations include the same provisions for different taxable years and partnerships described above.
      - If an entity whose AFSI is taken into account does not have a taxable year for regular tax purposes, its applicable financial statement (AFS, defined below) reporting year is its taxable year.
        - Foreign corporations and non-US persons whose AFSI is taken into account would not make any AFSI adjustment that is dependent on the treatment of an item for regular tax purposes if such entity does not take that item into account for regular tax purposes (for example, depreciation).

    - In general, and in order to prevent duplications of AFSI, the AFSI of a shareholder of a foreign corporation, which is either (i) a corporation that is determining its applicable corporation status or (ii) is a member of a single employer or FPMG group with the shareholder, disregards in certain circumstances any FSI that is attributable to the FSI of the subsidiary corporation (for example, amounts included in FSI under the equity or fair value method of accounting).
  - For purposes of the $100 million test, the proposed regulations provide that:
    - The AFSI taken into account is the AFSI of the FPMG corporation and any person treated as part of a section 52 group with the FPMG corporation.
    - The proposed regulations include the provisions described above for corporations that are not members of a FPMG.
- As discussed above, the definition of Single Employer Groups under the proposed regulations is generally consistent with sections 52(a) and (b) and the related Treasury regulations. The proposed regulations do not define trade or business for purposes of applying section 52(b).
- The proposed regulations provide special rules for applying the average annual AFSI test if persons join or leave a corporation's test group:
  - If an entity whose AFSI is taken into account is only related to the corporation for a portion of the taxable year, then only the AFSI for such portion of the taxable year would be taken into account based on an interim closing of the books.
    - If a corporation experiences a change in ownership that results in the corporation and a person no longer being treated as related, then, for purposes of testing applicable corporation status for the taxable year of the ownership change or a subsequent taxable year, such corporation would not include any AFSI of such related person for any period prior to such ownership change.
    - If a corporation experiences a change in ownership and joins a consolidated group that is an applicable corporation, then such corporation would be treated as an applicable corporation upon joining.
- The proposed regulations generally adopt the simplified method for determining applicable corporation status provided in Notice 2023-7, extending its availability beyond the first taxable year beginning after December 31, 2022.
- The proposed regulations address the termination of status as an applicable corporation providing that corporation status terminates following the taxable year in which the corporation (i) experiences an ownership change with respect to all parents of groups that the corporation was included in (that is, no longer satisfies the relevant relationship criteria), or (ii) does not meet the average annual AFSI test for five consecutive taxable years ending with the taxable year. The proposed regulations include substantiation and reporting requirements as follows:
  - A corporation (other than an S corporation, RIC or REIT) are required to maintain books and records sufficient to demonstrate whether it is an applicable corporation for any taxable year, including relevant section 52 group members or membership in a FPMG.
  - A corporation (other than an S corporation, RIC or REIT) that does not satisfy the simplified method must provide information to demonstrate whether it is an applicable corporation, in such manner as Form 4626, *Alternative Minimum Tax – Corporations,* and the relevant federal income tax return filed require, including their respective instructions.

Prop. Treas. Reg. § 1.59-3: Rules for FPMGs

- Prop. Treas. Reg. § 1.59-2(c)(2) describes the average annual AFSI test applied to a corporation that is a member of an FPMG (described below) for purposes of determining whether such corporation (FPMG corporation) is an applicable corporation. The FPMG corporation is subject to the two-prong average annual AFSI test described in Prop. Treas. Reg. § 1.59-2(c)(2) if it is a member of an FPMG at the beginning or end of its taxable year. Prop. Treas. Reg. § 1.59-2(b)(3).

  - Very generally, the first prong is a test based on global income. Under the first prong, the average annual AFSI of the FPMG corporation for the 3-taxable-year period ending with such taxable year must exceed $1 billion. Prop. Treas. Reg. § 1.59-2(c)(2)(i)(A). For this purpose, the combined AFSI of the FPMG corporation and all relevant aggregation entities (as defined in Prop. Treas. Reg. § 1.59-2(b)(4)) is treated as the AFSI of the FPMG corporation. The relevant aggregation entities for an FPMG corporation are all members of the FPMG, other than the FPMG corporation itself, and any other person that is treated as a single employer with the FPMG corporation under section 52(a) or (b).
  - In general, the second prong is a test based on US nexus income. Under the second prong, the average annual AFSI of an FPMG corporation for the 3-taxable-year period ending with the taxable year must be $100 million or more. Prop. Treas. Reg. § 1.59-2(c)(2)(i)(B). For this purpose, rules similar to those applicable to a corporation that is not a member of an FPMG with respect to aggregating AFSI, disregarding certain specified AFSI adjustments, avoiding the duplication of partnership income, and accounting for adjustments applicable to discharge of indebtedness income with respect to partnership investments, apply.

- Prop. Treas. Reg. § 1.59-3(c) defines a FPMG as two or more entities if: (i) at least one of the entities is a domestic corporation and at least one of the entities is a foreign corporation;[1] (ii) the entities are included in the same AFS for that taxable year; and (iii) one of the entities is a FPMG common parent.
  - Prop. Treas. Reg. § 1.59-3(b)(9) defines an "FPMG common parent" as an "ultimate parent" that is a foreign corporation. Prop. Treas. Reg. § 1.59-3(b)(12) defines an "ultimate parent" as an entity that has a controlling interest in at least one other entity and in which no entity has a controlling interest.
  - Prop. Treas. Reg. § 1.59-3(e) provides that an ultimate parent that is not a corporation is treated as a foreign corporation (a "deemed foreign corporation") if: (i) the ultimate parent directly or indirectly owns (other than through a domestic corporation, excluding a deemed domestic corporation) a foreign trade or business (as defined in Treas. Reg. § 1.989(a)-1(c)); or (ii) the ultimate parent directly or indirectly owns (other than through a domestic corporation, excluding a deemed domestic corporation) any equity interest in a foreign corporation and the ultimate parent has a controlling interest (including through a domestic corporation) in such foreign corporation. Thus, under the proposed regulations, a partnership can be treated as a deemed foreign corporation.
- Generally, the proposed regulations provide that an entity (upper-tier entity) has a "controlling interest" in another entity (lower-tier entity) if the applicable financial accounting standard requires that a consolidated financial statement of the upper-tier entity reflects the assets, liabilities, equity, income, and expenses of the lower-tier entity (regardless of whether or not a consolidated financial statement is or is required to be prepared or is prepared correctly).[2]
- The proposed regulations provide that in determining whether an upper-tier entity has a controlling interest in a lower-tier entity, the applicable financing accounting standard is GAAP, unless an exception applies. Such exceptions can only apply in cases in which there is not a GAAP consolidated financial statement prepared that includes the ultimate parent (determined by treating GAAP as the applicable financing standard). Prop. Treas. Reg. § 1.59-3(h) provides that an FPMG common parent and all entities in which the FPMG common parent has a controlling interest at any time

during the taxable year are treated as included in the same AFS for that taxable year. For this purpose, it is irrelevant whether a consolidated financial statement of the FPMG common parent is prepared, a particular entity is reflected in such consolidated financial statement, or a particular entity would be reflected if a consolidated financial statement of the FPMG common parent were prepared.
- Prop. Treas. Reg. § 1.59-3(i) provides that each entity included in the same AFS as the FPMG common parent for a taxable year is a member of that FPMG (including the FPMG common parent).

Definitions, General Rules, and AFSI Adjustments

Prop. Treas. Reg. § 1.56A-1: Definitions and General Rules for Determining AFSI

- General definitions are provided in Prop. Treas. Reg. § 1.56A-1 that apply to Prop. Treas. Reg. §§ 1.56A-2 through 1.56A-27, 1.59-2 through 1.59-4, 1.1502-53, and 1.1502-56A.
- Key definitions include, but are not limited to:
  - AFSI; adjusted net income or loss; AFS basis; AFS consolidation entries; applicable corporation; AFS; CAMT basis; CAMT entity; change in accounting principle; equity method; fair value method; financial statement income (FSI); impairment loss; impairment loss reversal; modified FSI; purchase accounting; push down accounting; restated AFS; and separate financial statement, among other definitions.
- General rules under section 56A are provided for determining FSI and AFSI including:
  - FSI generally includes all items of income, expense, gain, and loss reflected in the net income or loss of a CAMT entity set forth in the income statement included in the CAMT entity's AFS (for example, excludes retained earnings and other comprehensive income), regardless of tax realization or recognition provisions.
  - For purposes of tax consolidated groups with disregarded entities, if the AFS of each member of a tax consolidated group is not the same consolidated financial statement, then the tax consolidated group combines the financial results of all CAMT entities reflected in the different AFSs of its members to form one consolidated financial statement that is treated as the AFS of the tax consolidated group. Special rules apply for determining AFSI of CAMT entities that own disregarded entities or branches.
  - If a CAMT entity's AFS is a consolidated financial statement (consolidated AFS), the CAMT entity determines the amount of the net income or loss of the financial statement group set forth on the income statement included in the consolidated AFS (consolidated FSI) that is the CAMT entity's FSI. Special rules may apply in calculating FSI of a tax consolidated group. Prop. Treas. Reg. § 1.1502-56A(c). Generally, netting of losses against income within the consolidated AFS is not permitted. Additionally, AFS consolidation entries and elimination items are disregarded.
  - For a CAMT entity with an investment in a partnership or a domestic corporation that is a member of the CAMT entity's financial statement group for which the consolidated AFS is prepared, the income or loss reflected in the FSI of the CAMT entity with respect to the investment and any balance sheet accounts reflected in the CAMT entity's separate books and records with respect to the investment are determined as though the CAMT entity prepared a separate financial statement in which the investment was properly accounted for under the relevant accounting standards.
  - AFS consolidation entries, other than elimination entries, that relate to one or more CAMT entities for which the consolidated AFS is prepared and that are not reflected in the separate books and records of one or more of the CAMT entities are appropriately pushed down to each

  - CAMT entity to which the AFS consolidation entries relate and taken into account in each CAMT entity's FSI.
  - If a CAMT entity's AFS is a consolidated financial statement, and if the CAMT entity's balance sheet accounts or AFS basis in any item are relevant for determining the CAMT entity's AFSI, then the CAMT entity uses the balance sheet accounts or AFS basis reflected in the CAMT entity's separate books and records (including trial balances) used to create the consolidated financial statement and determined without regard to any AFS consolidation entries.
  - A coordination provision indicates that the rules for determining FSI apply before the rules for determining AFSI and other sections of the section 56A regulations, other than Prop. Treas. Reg. § 1.56A-2.
  - Generally, unless an exception applies, the AFSI adjustments described in the section 56A proposed regulations are made for taxable years ending after December 31, 2019. In addition, unless an exception applies, any AFSI adjustment that arises from an event or a transaction that occurs in a taxable year that ends on or before December 31, 2019, is not made in determining AFSI for taxable years ending after December 31, 2019.

Prop. Treas. Reg. § 1.56A-2: Definition of AFS and AFS Priority Rules

- AFS refers to a CAMT entity's financial statement with the highest priority listed in Prop. Treas. Reg. § 1.56A-2(c).
- Priority Listing of AFS, subject to meeting specific requirements:
  - GAAP Statements: Audited financial statement, other than a tax return, that is certified as being prepared in accordance with GAAP, that is (i) filed with the SEC (annual statement to shareholders or Form 10-K); (ii) used for credit purposes, reporting to owners, or any substantial non-tax purposes; or (iii) filed with a federal agency other than the IRS.
  - IFRS Statements: Audited financial statement, other than a tax return, that is certified as being prepared in accordance with IFRS, that is (i) filed with the SEC or with an agency of a foreign government equivalent to the SEC; (ii) used for credit purposes, reporting to owners, or any substantial non-tax purposes; or (iii) filed with a federal agency or foreign agency, other than the SEC, IRS or an agency that is equivalent to the SEC or IRS.
  - Financial statements prepared in accordance with other generally accepted accounting standards: an audited financial statement that is certified as prepared in accordance with accepted accounting standards other than GAAP and IFRS, that is (i) filed with the SEC or an equivalent foreign agency; (ii) used for credit purposes, reporting to owners, or any substantial non-tax purposes; or (iii) filed with a federal agency, foreign agency, or an agency other than the SEC or IRS or a foreign agency that is equivalent to the SEC or IRS.
  - Other Government and Regulatory Statements: Financial statements other than a tax return or a financial statement of higher priority, filed with a federal, state, or foreign government, governmental agency, or self-regulatory organization.
  - Unaudited External Statements: Financial statement other than a tax return or a financial statement of higher priority, that is unaudited (or audited but not certified), and prepared for external non-tax purposes using GAAP, IFRS, or any other accepted accounting standards.
  - Return: Federal income tax return or information return filed with the IRS for a CAMT entity that is not a controlled foreign corporation (CFC), or a Form 5471, *Information Return of U.S. Persons With Respect to Certain Foreign Corporations*, for a CAMT entity that is a CFC.
- Prop. Treas. Reg. § 1.56A-2 clarifies that the term "certified financial statements" means certified by an independent financial statement auditor as fairly presenting the results of operations in conformity with relevant financial accounting standards.

- A restated AFS is prioritized over the original if issued before the federal tax return filing.
- Annual financial statements are prioritized over periodic statements that cover a period of less than 12 months.
- Special rules apply for determining the AFS of a disregarded entity or branch.
- The proposed regulations provide AFS priority rules for consolidated financial statements and consolidated tax returns, most of which are consistent with the Notices, that generally provide:
  - If a CAMT entity's financial results are consolidated with the financial results of one or more other CAMT entities on one or more consolidated financial statements (other than a tax return), then the CAMT entity's AFS is the consolidated financial statement with the highest priority.
  - However, if the CAMT entity's financial results are also reported on one or more separate financial statements that are of equal or higher priority to that highest priority consolidated financial statement, then the CAMT entity's AFS is the separate financial statement with the highest priority.
  - If the tax consolidated group member has only one consolidated financial statement (other than a tax return) that contains the financial results of all members of the tax consolidated group, then a member of the tax consolidated group uses that consolidated financial statement as the AFS, regardless of whether the member's financial results also are reported on (i) a separate financial statement that is of equal or higher priority; or (ii) a consolidated financial statement that contains the financial results of some, but not all, members of the tax consolidated group, and that is of equal or higher priority. Special rules may apply for members of a FPMG.
  - If more than one consolidated financial statement (other than a tax return) contains the financial results of all members of a tax consolidated group, then a member of the tax consolidated group uses the consolidated financial statement (other than a tax return) with the highest priority that contains the financial results of all members of the tax consolidated group, regardless of whether the member's financial results also are reported on (i) a separate financial statement that is of equal or higher priority to that consolidated financial statement; or (ii) a consolidated financial statement that contains the financial results of some, but not all, members of the tax consolidated group, and that is of equal or higher priority to that consolidated financial statement. Special rules may apply for members of an FPMG.
  - If there is only one consolidated financial statement (other than a tax return) that contains the member's financial results and the financial results of at least one other member, but not all members, then the member uses that consolidated financial statement as its AFS, regardless of whether the member's financial results also are reported on a separate financial statement that is of equal or higher priority to that consolidated financial statement. Special rules or exceptions may apply for members of an FPMG and certain other taxpayers.
  - If the tax consolidated group member has more than one consolidated financial statements (other than a tax return) that contains the member's financial results and the financial results of at least one other member of the tax consolidated group, but not all, members of the tax consolidated group, then the member uses as its AFS the consolidated financial statement (other than a tax return) that contains its financial results and the financial results of the greatest number of members of the tax consolidated group, and the one with the highest priority if there is more than one such consolidated financial statement, regardless of whether the member's financial results also are reported on (i) a separate financial statement that is of equal or higher priority to that consolidated financial statement; or (ii) a consolidated financial statement that contains its financial results and the financial results of fewer members of the tax consolidated group, and that is of equal or

higher priority to that consolidated financial statement. Special rules may apply for members of an FPMG and certain other taxpayers.

- The proposed regulations also provide rules for the determination of an AFS for members of an FPMG that are similar to the rules provided in Notice 2023-64, as modified and clarified by Notice 2024-10. Generally, if a CAMT entity is a member of an FPMG, and if the FPMG common parent prepares a consolidated financial statement for a financial statement group that includes the CAMT entity (FPMG consolidated AFS), then the CAMT entity uses the FPMG consolidated AFS as its AFS, regardless of whether the CAMT entity's financial results also are reported on a separate financial statement that is of equal or higher priority to the FPMG consolidated AFS.

Prop. Treas. Reg. § 1.56A-3: AFSI Adjustments for AFS Year and Taxable Year Differences

- In general, if a CAMT entity's AFS period differs from the taxable year, FSI and AFSI is computed as if the financial accounting period were the same as the taxable year by conducting an interim closing of the books.
- For purposes of computing FSI and AFSI under Prop. Treas. Reg. § 1.56A-3, an interim closing of the books is performed at the end of the current and immediately preceding taxable year.

Prop. Treas. Reg. § 1.56A-4: AFSI Adjustments and Basis Determinations with Respect to Foreign Corporations

- Consistent with Notice 2024-10, Prop. Treas. Reg. § 1.56A-4(c)(1) requires a CAMT entity, in calculating AFSI, to disregard any items of income, expense, gain, and loss resulting from ownership of stock of the foreign corporation, including any such items that result from acquiring or transferring such stock, reflected in the CAMT entity's FSI. Additionally, Prop. Treas. Reg. § 1.56A-4(c)(1)(ii) generally requires the CAMT entity to include, in AFSI, any items of income, deduction, gain, and loss for regular tax purposes resulting from ownership of stock of the foreign corporation, including any items that result from acquiring or transferring the stock, other than any items of income, deduction, gain, and loss resulting from the application of sections 78, 250, 951, or 951A.
- Prop. Treas. Reg. § 1.56A-4(e) provides that if a partnership directly owns stock of a foreign corporation, then in determining the AFSI of a CAMT entity that is a partner in the partnership (or an indirect partner, in the case of tiered partnerships), the partner takes into account the tax items described in Prop. Treas. Reg. § 1.56A-4(c)(1)(ii) that are allocated to the partner for regular tax purposes. However, Prop. Treas. Reg. § 1.56A-4(c)(1)(i) (disregarding certain items reflected in FSI) applies at the partnership level because the partnership, as the direct owner of the stock of the foreign corporation, may have reflected certain items resulting from the ownership of stock of the foreign corporation in its FSI.
- Under Prop. Treas. Reg. § 1.56A-4(c)(1)(ii), the AFSI of a CAMT entity that is a shareholder of a passive foreign investment company includes regular tax items resulting from the ownership of the stock of the passive foreign investment company, including any amounts under sections 1291, 1293, and 1296.
- The items described in Prop. Treas. Reg. § 1.56A-4(c)(1)(ii) are determined under regular tax rules, including subchapter C of chapter 1 (subchapter C), taking into account the CAMT entity's basis in the stock of the foreign corporation for regular tax purposes and the foreign corporation's earnings and profits (E&P) for regular tax purposes.
- The proposed regulations include rules for "covered asset transactions." Covered asset transactions include two categories of transactions: (i) a transfer of an asset to, or by, a foreign corporation and (ii) a transfer of stock of a foreign corporation to or by a domestic corporation.

  - Prop. Treas. Reg. § 1.56A-4(c)(2) requires a CAMT entity, in calculating AFSI, to disregard any items of income, expense, gain, and loss with respect to the transferred asset resulting from the covered asset transaction reflected in the CAMT entity's FSI. The proposed regulations also require the CAMT entity to include any items of income, deduction, gain, and loss for regular tax purposes with respect to the transferred asset resulting from the covered asset transaction.
  - Prop. Treas. Reg. § 1.56A-4(d)(1) provides rules for determining the CAMT basis in an asset that is transferred in a covered asset transaction, which generally rely on the principles of the Code for determining basis for regular tax purposes, but use CAMT basis instead of regular tax basis, as applicable.
  - Special rules apply to certain cases in which a CAMT entity receives stock of a foreign corporation in a covered asset transaction and the CAMT entity's basis in the stock of the foreign corporation for regular tax purposes is determined under section 358.
- Prop. Treas. Reg. § 1.56A-4(c)(3) provides adjustments to the AFSI of a foreign corporation, the stock of which is purchased in a transaction where the purchaser makes an election under section 338(g). These adjustments are consistent with the general principles underlying the rules in Prop. Treas. Reg. § 1.56A-4 to follow regular tax rules for foreign stock and transactions involving foreign corporations.
- Prop. Treas. Reg. § 1.56A-1(c)(4)(ii) provides that, except as otherwise provided, any purchase accounting and push down accounting adjustments, as applicable, are required to be reflected in the CAMT entity's AFS basis, balance sheet accounts, and FSI. However, there is an exception to this general rule such that any purchase accounting or push down accounting adjustments, as applicable, with respect to an acquisition of the stock of a foreign corporation by a CAMT entity is disregarded for purposes of determining the CAMT entity's AFSI.

Prop. Treas. Reg. § 1.56A-5: Rules for Determining the AFSI Adjustment for Partner's Distributive Share of Partnership AFSI

- Section 56A(c)(2)(D)(i) provides that if the applicable corporation is a partner in a partnership, the taxpayer's AFSI with respect to the partnership is adjusted to only take into account the taxpayer's "distributive share" of the partnership's AFSI. The proposed regulations provide a "bottom up" approach for determining "distributive share." Under the "bottom up" approach, each partnership, including every partnership in a tiered structure, would calculate its modified FSI and provide the necessary information for a CAMT entity partner to determine its distributive share of the partnership's AFSI using the same multi-step method (the "applicable method") regardless of the applicable corporation's AFS method. Special rules apply if an applicable corporation and a partnership are members of the same financial statement group, if the partnership uses its federal income tax return as its AFS, or if the taxable year of the applicable corporation and the partnership are different.
- Each year, the applicable corporation (or a partnership in a tiered partnership structure that includes the applicable corporation) in conjunction with the partnership must generally determine distributive share of AFSI from the partnership using a mechanical multi-step approach. The proposed regulations provide eight examples, including addressing tiered partnerships, illustrating the applicable method. The applicable method generally includes the following steps:
  - First, the applicable corporation disregards any amount reflected in FSI with respect to the partnership investment from AFSI (including mark-to-market financial statement income under the fair value method).
  - The applicable corporation then determines a "distributive share percentage" that is based on its share of FSI with respect to the applicable corporation's partnership interest (that is, not a percentage

based on section 704(b), section 704(c) or its economic interest for regular tax purposes, as some stakeholders requested).
  - Next, the partnership determines its modified FSI, taking into account certain section 56A adjustments.
  - Then, the applicable corporation multiples its distributive share percentage, as determined above, by the partnership's modified FSI.
  - Finally, the CAMT entity adjusts the amount from the prior step to reflect any separately stated items from the partnership (such as, but not limited to, section 743(b) basis adjustments attributable to section 168 property, or certain deferred gain or loss with respect to property distributed by the partnership, as described below) to arrive at its "distributive share amount."
- FSI amounts resulting from a transfer, sale, or exchange of the applicable corporation's partnership interest are not excluded from the applicable corporation's AFSI under the applicable method. However, these amounts may be adjusted in some instances, including to the extent the applicable corporation's CAMT basis in its partnership interest is different than its AFS basis.
- Both the distributive share percentage and the distributive share amount may be negative. If a CAMT entity's distributive share amount is negative, the proposed regulations (i) limit the allowable negative amount to its CAMT basis (determined using rules similar to the rules under section 705 and beginning the first day of the partnership's taxable year ending after December 31, 2019) in its partnership interest at the end of the partnership's taxable year and (ii) provide for the excess negative amount to be carried forward for subsequent taxable years, subject to the CAMT basis limitation, as described above. Ordering rules similar to the section 704(d) regulations also apply.

Prop. Treas. Reg. § 1.56A-6: AFSI Adjustments with Respect to Controlled Foreign Corporations (CFC)

- The CAMT entity's pro rata share of the adjusted net income or loss of a CFC is determined for the taxable year of the CFC that ends with or within the taxable year of the CAMT entity and is determined under the principles of section 951(a)(2) (including sections 951(a)(2)(A) and (B) and the aggregation rules in Treas. Reg. § 1.958-1(d) (the "Pro Rata Share of CFC Income Rule").[3]
- Solely for purposes of determining AFSI under section 56A (that is, for liability purposes), if an applicable corporation does not claim a foreign tax credit (FTC), the applicable corporation reduces the amount determined under the Pro Rata Share of CFC Income Rule by the applicable corporation's share of "Eligible Taxes," which generally includes foreign income taxes, other than foreign income taxes for which a credit is disallowed or suspended for regular tax purposes under sections 245A(d), 245A(e)(3), 901(e), 901(f), 901(i), 901(j), 901(k), 901(l), 901(m), 907, 908, 909, 965(g), 999, or 6038(c). Such reduction would not be permitted for taxes deemed paid by the applicable corporation on distributions of previously taxed earnings and profits (PTEP) under section 960(b) (PTEP taxes).[4]
- Under the Pro Rata Share of CFC Income Rule, a CAMT entity that is a US shareholder of multiple CFCs includes a single adjustment in determining its AFSI. This means that a net loss of a CFC may offset net income of another CFC in the same taxable year. If the sum of pro rata share of the adjusted net income or loss of each CFC of which the CAMT entity is a US shareholder produces a negative amount, this amount is carried to the succeeding taxable year (such amount is referred to as the CFC adjustment carryover). Specific mechanics are provided as to the ordering of the CFC adjustment carryover.
- The proposed regulations provide that a CFC's adjusted net income or loss is equal to the FSI of the CFC for the taxable year, with certain adjustments.

Specifically, a CFC's adjusted net income or loss is computed by excluding amounts reflected in FSI as a result of owning stock of a foreign corporation and substituting amounts that are recognized for regular tax purposes. The proposed regulations provide that a CFC's adjusted net income or loss excludes any items of income, expense, gain, and loss resulting from ownership of stock of a foreign corporation, including from acquiring or transferring such stock, that is reflected in the CFC's FSI.[5] The proposed regulations also provide that a CFC's adjusted net income or loss includes any items of income, deduction, gain, and loss resulting from the CFC's ownership of stock of a foreign corporation, including from acquiring or transferring such stock, for regular tax purposes, except for the amount of any dividend received from another foreign corporation to the extent the dividend is a "CAMT excluded dividend" (the "Foreign Corporation Stock Ownership Rule").
  - A CAMT excluded dividend is a dividend received by a CFC to the extent the dividend is excluded from:
    - the recipient CFC's gross income under section 959(b) (that is, a distribution of PTEP from a lower-tier CFC to the upper-tier CFC), or
    - the recipient CFC's foreign personal holding company income under section 954(c)(3) (relating to certain income received from related persons – the "same country" exception) **or** section 954(c)(6) (relating to certain amounts received from related persons – the related-party "look-through" exception), **and** the recipient CFC's gross tested income under Treas. Reg. § 1.951A-2(c)(1)(iv).
- The proposed regulations provide that if a CFC is a partner in any partnership or the owner of any disregarded entity, the items taken into account in computing the CFC's adjusted net income or loss generally include the CFC's distributive share amount of modified FSI from any such partnership and the AFSI of any such disregarded entity. The proposed regulations also provide if a partnership directly owns stock of a foreign corporation, then in determining the adjusted net income or loss of a CFC that is a partner in the partnership (or an indirect partner, in the case of tiered partnerships), the partner takes into account the items determined under the Foreign Corporation Stock Ownership Rule discussed above for regular tax purposes.[6]
- The proposed regulations provide that if a CFC is an applicable corporation, the CFC's adjusted net income or loss is reduced by the amount of AFSI of the CFC (with such AFSI determined by taking Prop. Treas. Reg. § 1.56A-7, discussed below, into account which generally provides that a foreign corporation computes its AFSI using effectively connected income (ECI) concepts). Thus, if an amount is subject to CAMT under section 56A(c)(4) and Prop. Treas. Reg. § 1.56A-7 because a CFC is itself an applicable corporation, such amount should be excluded from a US shareholder's adjustment under 56A(c)(3) to prevent double counting of the same income of the CFC.

Prop. Treas. Reg. § 1.56A-7: AFSI Adjustments with Respect to ECI

- Prop. Treas. Reg. § 1.56A-7 provides that, for purposes of section 56A(c)(4), the AFSI of a foreign corporation is adjusted to include only the amounts and items of FSI that would be included in ECI or allowable as a deduction by such corporation for purposes of section 882(c) had such amount or item accrued for regular tax purposes in the taxable year.
- The preamble confirms that section 56A(c)(4) is applied taking into account any income tax treaty obligation of the United States that applies to a taxpayer.[7]

Prop. Treas. Reg. § 1.56A-8: AFSI Adjustments for Certain Federal and Foreign Income Taxes

- Consistent with Notice 2023-64, Prop. Treas. Reg. § 1.56A-8 provides:

- AFSI is appropriately adjusted to disregard any "applicable income taxes" which are defined as federal income taxes and foreign income taxes that are taken into account on the CAMT entity's AFS as current tax expense (or benefit), as deferred tax expense (or benefit), or through increases or decreases to other AFS accounts of the CAMT entity.
- Applicable income taxes are considered taken into account in an AFS if any journal entry has been recorded in the books and records to determine the amounts on the AFS that includes the CAMT entity for any year, or another AFS that includes the CAMT entity, to reflect the taxes, even if the taxes do not increase or decrease the CAMT entity's FSI at the time of the journal entry.
- Applicable income taxes taken into account in a partnership's AFS are also considered taken into account in any AFS of the partnership's partners.

- As defined in Prop. Treas. Reg. § 1.56A-1(b)(18), federal income taxes are taxes imposed by subtitle A of the Code including amounts allowed as credits against taxes imposed by subtitle A and credit amounts that are generated by a partnership and passed through to a partner. Prop. Treas. Reg. § 1.56A-1(b)(23) defines "foreign income tax" as provided in Treas. Reg. § 1.901-2.
- Solely for purposes of determining AFSI under section 56A (that is, for liability purposes), Prop. Treas. Reg. § 1.56A-8(c) provides that an applicable corporation that does not choose to claim a FTC for the taxable year would reduce its AFSI by the amount of foreign income taxes which the applicable corporation deducts for regular tax purposes under section 164 (taking into account all other relevant provisions) for the taxable year, including foreign income taxes of a disregarded entity of which the applicable corporation is the owner for regular tax purposes and creditable foreign tax expenditures (within the meaning of Treas. Reg. § 1.704-1(b)(4)(viii)) allocated to the applicable corporation as a partner or indirect partner in a tiered partnership, and any other foreign income taxes that are allocated to the applicable corporation as an owner of any other type of pass-through entity.

Prop. Treas. Reg. § 1.56A-9: AFSI Adjustments for Owners of Disregarded Entities or Branches

- Prop. Treas. Reg. § 1.56A-9 provides rules under section 56A(c)(6) for determining AFSI of a CAMT entity that owns a disregarded entity ("DRE") or branch.
- Similar to regular tax principles, the CAMT entity that owns a DRE or branch is treated as (i) owning all of the assets and liabilities of the DRE or branch and (ii) directly earning any income, expense, gain, or loss of the DRE or branch.
- Additionally, transactions between the DRE or branch and the CAMT entity (or between DREs or branches with the same CAMT entity owner) and any financial statement accounts that reflect the CAMT entity owner's investment in the DRE or branch are disregarded for CAMT purposes.
- If a DRE or branch is required to determine its own AFS under Prop. Treas. Reg. § 1.56A-2(h) because the financial results of the DRE or branch are not reflected on the CAMT entity owner's AFS, the CAMT entity applies the rules set forth in Prop. Treas. Reg. § 1.56A-9, taking into account the rules where transactions between a CAMT entity owner and a DRE or branch of such owner would be disregarded, by reference to the separate AFS of the DRE or branch.

Prop. Treas. Reg. § 1.56A-12: AFSI Adjustments with Respect to Certain Tax Credits

- Section 56A(c)(9) and Prop. Treas. Reg. § 1.56A-12 provide that AFSI is appropriately adjusted to disregard certain federal income tax credits (that is, follow their treatment for regular tax purposes). The Prop. Treas. Reg. § 1.56A-12 adjustment is made to the extent the amount is not otherwise disregarded under section 56A(c)(5) and Prop. Treas. Reg. § 1.56A-8 (concerning certain federal and foreign income taxes).

- AFSI adjustments are made to disregard the following:
  - Amounts treated as payments against US federal income tax pursuant to an election under section 48D(d) or 6417, including those treated as tax-exempt income for purposes of sections 705 and 1366.
  - Amounts received by a transferor taxpayer as consideration for its transfer of an eligible credit, as defined in section 6418(f)(1)(A), to a transferee taxpayer.
  - For a transferee taxpayer:
    - Amounts paid to acquire the eligible credit; and
    - Increases in the transferee taxpayer's FSI resulting from the utilization of the eligible credit.
  - Decreases in FSI resulting from increases in US federal income tax because of recapture provisions under sections 48D(d)(5), 50(a)(3), 6417(g), and 6418(g)(3).

Prop. Treas. Reg. § 1.56A-15: AFSI Adjustments for Section 168 Property

- Prop. Treas. Reg. § 1.56A-15 reflects two principles:
  - Achieve a result that mimics regular tax treatment of section 168 property as to timing and amount of basis recovery with respect to section 168 property without regard to placed-in-service date, cost recognition for FSI purposes, and whether gain or loss with respect to such property is recognized in FSI; and,
  - Preclude a result for section 168 property that is better for AFSI purposes than for regular tax purposes.
- Section 168 property is defined as MACRS property that is depreciable under section 168, and other property that is qualified property for purposes of bonus depreciation under section 168(k) (for example, computer software, qualified films, and specified plants), determined without regard to whether the taxpayer elects to forgo bonus depreciation. Section 168 property includes only those costs recoverable under section 167 (for example, section 168 property does not include amounts deducted under section 181), and excludes costs that are deducted as incurred for US federal income tax purposes (for example, deductible repair and maintenance expenditures) and property owned by a foreign corporation that is not subject to US federal income tax.
- AFSI is adjusted by the following:
  - Tax depreciation including tax depreciation capitalized under section 263A to inventory, or the basis of property held for sale to customers (tax COGS depreciation), but only to the extent of the amount recovered through COGS or in computing gain or loss on the sale of property held for sale to customers (section 1221(a)(1) property) in computing taxable income for the taxable year.
    - The proposed regulations include two simplifying methods (one for FIFO, one for LIFO) to determine the amount of tax depreciation capitalized into inventory. AFSI is also reduced by depreciation deductions allowed under section 167 with respect to section 168 property (tax depreciation), including tax depreciation that is capitalized and subsequently recovered as a deduction in computing taxable income (deductible tax depreciation).
  - A CAMT entity's book depreciation accounted for in its AFS, including covered book depreciation expense, covered book COGS depreciation (each of which includes other recovery of AFS basis, such as impairment losses), covered book expense (that is, a book expense that reduces FSI and is included in the tax adjusted basis of section 168 property).
  - Tax depreciation section 481(a) adjustment (that is, an adjustment required under section 481(a) for a change in method of accounting that

impacts the timing of taking into account depreciation with respect to section 168 property but not a "tax capitalization method change") taken into account in computing taxable income for the taxable year.
  - Tax capitalization method change AFSI adjustment (that is, the difference between the cumulative amount of AFSI adjustments with respect to costs subject to the tax capitalization method change and cumulative amount of AFSI adjustments that would have been made had the new accounting method been used for those taxable years). The tax capitalization method change AFSI adjustments include only amounts for taxable years beginning after December 31, 2019.
  - Other items as provided in Internal Revenue Bulletin guidance that the IRS may publish.
- For partnerships, AFSI depreciation adjustments with respect to section 734(b) adjustments are taken into account by the partnership, but AFSI depreciation adjustments with respect to section 743(b) adjustments are taken into account by the partner and included in that partner's distributive share amounts. AFSI depreciation adjustments with respect to Treas. Reg. § 1.1017-1(g)(2) adjustments are also taken into account by the partner and included in the partner's distributive share amounts.
- In the taxable year in which section 168 property is disposed of, AFSI is adjusted to take into account gain or loss on such disposition determined with reference to the CAMT basis (that is, the AFS basis of the section 168 property, increased or decreased for the adjustments reflected in computing CAMT—for example, tax depreciation, tax COGS depreciation, covered book expense, covered book depreciation, covered book COGS depreciation, adjustments for attribute reductions, tax credit basis adjustments, etc.).
  - Special rules apply in determining CAMT basis for section 168 property acquired in a covered recognition transaction, for a CAMT entity that satisfies the simplified method, as part of an intercompany transaction within a tax consolidated group, and for section 168 property disposed of by a partnership.
  - AFS basis recovery on section 168 property disposed of is disregarded if it was treated as disposed of for regular tax purposes before AFS purposes.

Prop. Treas. Reg. § 1.56A-16: AFSI Adjustments for Qualified Wireless Spectrum Property

- Qualified wireless spectrum is defined as wireless spectrum (i) used in the trade or business of a wireless telecommunications carrier; (ii) amortizable under section 197; and, (iii) acquired after December 31, 2007, and before August 16, 2022.
- The rules for determining the AFSI adjustments for qualified wireless spectrum are generally consistent with those provided for section 168 property.

Prop. Treas. Reg. § 1.56A-17: AFSI Adjustments to Prevent Duplications or Omissions

- The rules for adjustments to prevent omissions or duplications are generally consistent with the provisions of the Notices. AFSI is adjusted for certain items to prevent duplications or omission of income, expense, gain, or loss that arise from a change in financial accounting principle, an AFS restatement, and an auditor's opinion.
- If a CAMT entity implements, or is treated as implementing, a change in financial accounting principle in its AFS, the CAMT entity's AFSI is adjusted to include the financial accounting principle change amount—equal to the amount of the net cumulative adjustment to beginning retained earnings, adjusted to disregard any portion attributable to taxable years beginning on or before December 31, 2019, and reflect any other AFSI adjustments.

- A financial accounting principle change amount that prevents any net duplication or a net omission that results in an increase to AFSI is included in the CAMT entity's AFSI ratably over four taxable years beginning with the taxable year in which the change in accounting principle is implement in its AFS, unless the CAMT entity can demonstrate that such change is reasonably anticipated to occur over a different period. A net omission that results in a decrease to AFSI is included in the CAMT entity's AFSI in full in the taxable year for which the change in financial accounting principle is implemented in its AFS.
  - A financial accounting principle change also occurs if the priority of a CAMT entity's AFS for one taxable year is different than the priority of its AFS for the immediately preceding taxable year.
- AFSI is adjustment for a CAMT entity's restatement of FSI for the taxable year in which the restated AFS is issued ("AFSI restatement adjustment"). Such adjustment takes into account the cumulative effect on FSI, including any restatement of the CAMT entity's beginning retained earnings (limited to restated retained earnings attributable to taxable years beginning after December 31, 2019). The AFSI restatement adjustment is further adjusted if it relates to another item for which AFSI is adjusted for pursuant to the regulations under section 56A.
  - A CAMT entity is deemed to have issued a restated AFS for a preceding taxable year if—(i) the beginning retained earnings is adjusted to be different than the amount previously-reflected; (ii) such difference is attributable to items that would otherwise be reflected in the CAMT entity's FSI under the relevant accounting standards used to prepare its AFS; and, (iii) a change in accounting principle was not implemented in the CAMT entity's AFS and it was not actually restated.
- AFSI adjustments may be required to take into account amounts disclosed in a financial accounting auditors qualified or adverse opinion if such amounts would have increased the CAMT entity's FSI had the amounts been reported in such entity's AFS.
- AFSI is not adjusted for differences in the period an item is taken into account in FSI and the period the item is taken into account for regular tax purposes.

Prop. Treas. Reg. § 1.56A-18: AFSI, CAMT Basis, and CAMT Retained Earnings Resulting From Certain Corporation Transactions

- Prop. Treas. Reg. § 1.56A-18 provides rules for determining AFSI, CAMT basis, and CAMT earnings consequences resulting from certain distributions, stock sales, and asset sales between a domestic corporation and certain other persons.
  - These rules do not apply to transactions between members of the same tax consolidated group during any period that they are shareholders of other members of the same tax consolidated group or to certain transactions involving foreign corporations described in Prop. Treas. Reg. § 1.56A-4.
- Prop. Treas. Reg. § 1.56A-18(b) provides definitions that apply for purposes of Prop. Treas. Reg. §§ 1.56A-18, 1.56A-19, and 1.56A-21.
- Prop. Treas. Reg. § 1.56A-18(c) provides operating rules that apply for purposes of Prop. Treas. Reg. §§ 1.56A-18, 1.56A-19, and 1.56A-21.
  - Subject to certain exceptions, if a shareholder owns stock of a non-tax consolidated domestic corporation, such shareholder generally disregards the financial accounting consequences of such stock ownership (for example, amounts included in FSI under the equity or fair value method and corresponding adjustments to AFS basis and retained earnings).
  - For certain minority investments in smaller corporations, the shareholder determines the character of any distribution using the corporation's regular tax earnings and profits (as opposed to CAMT earnings).

- For stock acquisitions by a corporation in a covered transaction, purchase accounting or push down accounting adjustments are disregarded.
- For acquisitions of assets of a target corporation by a corporation, (i) in a covered nonrecognition transaction, purchase accounting adjustments are disregarded, and (ii) in a covered recognition transaction, purchase accounting adjustments are regarded.
- Consistent with Notice 2023-7, each component transaction of a larger covered transaction is examined separately for qualification as a covered nonrecognition transaction or a covered recognition transaction for each party.
- A shareholder's initial CAMT stock basis in a non-tax consolidated domestic corporation is equal to its regular tax basis as of the beginning of the first taxable year of the shareholder beginning after 12/31/2019 (if held at such time). Otherwise, such initial CAMT stock basis is determined under Prop. Treas. Reg. §§ 1.56A-18 and -19.

- Prop. Treas. Reg. § 1.56A-18(d) – (h) provide rules for CAMT consequences relating to (i) non-liquidating distributions, (ii) liquidating distributions, (iii) taxable stock sales, and (iv) taxable asset sales.
  - Non-Liquidating Distributions:
    - For distributions of property under section 311, the built-in gain or loss in such property is determined using CAMT basis, with any built-in gains included in AFSI and built-in losses disallowed, and CAMT earnings are adjusted by applying section 312 principles.
    - A shareholder determines its AFSI, CAMT basis in property received, and CAMT earnings from the distribution by applying section 301 and other relevant sections (for example, sections 243, 302, 305, 1059) using the distribution amount reflected on the shareholder's AFS and the CAMT earnings of the distributing corporation.
      - Section 336(e) Elections:
        - If a distributing corporation makes a stock distribution where a section 336(e) election is made:
          - In general, the distributing corporation would not recognize any AFSI with respect to the stock distribution.
          - The controlled or target corporation's AFSI from the deemed sale construct would be determined in accordance with regular tax rules using CAMT asset basis, and such corporation's new CAMT basis would be equal to its basis for regular tax purposes.
  - Liquidating Distributions:
    - Nontaxable Liquidations – Sections 332/337
      - Each of the liquidating corporation and distributee corporation determines its AFSI based on the treatment for regular tax purposes (that is, no AFSI if no gain or loss under section 332(a) or 337(a)).
      - The distributee corporation (i) takes a carryover basis in the property received using CAMT basis, and (ii) succeeds to the liquidating corporation's CAMT attributes (for example, CAMT earnings, financial statement net operating losses (FSNOLs)).
    - Taxable Liquidations – Sections 331/336
      - The liquidating corporation (i) redetermines gain or loss reflected in FSI by using CAMT basis, and (ii) adjusts CAMT retained earnings based on the amount of AFSI recognized.
      - The distributee corporation (i) redetermines gain or loss reflected in FSI by using CAMT basis, (ii) takes a basis in the assets received equal to the AFS basis of such assets, and (iii) adjusts CAMT retained earnings based on the amount of AFSI recognized.
  - Taxable Stock Sales:
    - If a target corporation shareholder transfers target corporation stock to an acquiror corporation in a section 304 or 1001 transaction:

    - Target shareholder (i) redetermines gain or loss reflected in FSI by using CAMT basis, (ii) take a basis in the property received from acquiror equal to its AFS basis, and (iii) adjust its CAMT current earnings by the amount of AFSI recognized.
    - Unless a section 336(e), 338(g), or 338(h)(10) election is made, there would be no CAMT consequences to the target corporation.
      - If such an election is made, the target corporation's AFSI from the deemed sale construct would be determined in accordance with regular tax rules using CAMT asset basis, and such corporation's new CAMT basis would be equal to its basis for regular tax purposes.
      - If a section 336(e) or section 338(h)(10) election is made, the target shareholder's transfer of target stock would be disregarded, and the target shareholder would adjust its CAMT current earnings to take into account the deemed liquidation of the target corporation.
      - The acquiror corporation would redetermine gain or loss reflected in FSI (if any) using CAMT basis, and adjust CAMT current earnings to reflect any such AFSI amount.
      - In general, section 304, including any deemed contribution and redemption construct, would not apply for CAMT purposes.
  - Taxable Asset Sales:
    - The target corporation (i) redetermines gain or loss reflected in FSI by using CAMT basis, (ii) takes a basis in the property received from acquiror equal to its AFS basis, and (iii) adjusts CAMT current earnings to reflect the amount of AFSI recognized.
    - The acquiror corporation (i) redetermines gain or loss reflected in FSI using CAMT basis, (ii) takes a basis in the property received from the target corporation equal to its AFS basis, and (iii) adjusts CAMT current earnings to reflect the amount of AFSI recognized (if any).

Prop. Treas. Reg. § 1.56A-19: AFSI, CAMT Basis, and CAMT Retained Earnings Resulting From Certain Corporate Reorganizations & Organizations

- Prop. Treas. Reg. § 1.56A-19 provides rules for determining AFSI, CAMT basis, and CAMT earnings consequences relating to certain section 368(a) reorganizations, section 355 transactions, and section 351 transactions.
- Prop. Treas. Reg. §§ 1.56A-19(b) through 1.56A-19(g) provides rules regarding the CAMT consequences of the parties to (i) section 368(a)(1)(B) reorganizations (B Reorganizations), (ii) acquisitive reorganizations (for example, reorganizations under sections 368(a)(1)(A), 368(a)(1)(C), and 368(a)(1)(D) (to the extent the requirements of section 354(b)(1)(B) are satisfied)), (iii) section 355 distributions, (iv) section 368(a)(1)(E) reorganizations (E Reorganizations), (v) section 368(a)(1)(F) reorganizations (F Reorganizations), and (vi) section 351 transactions.
- In general, if a transaction is treated as a covered nonrecognition transaction, the rules in each of Prop. Treas. Reg. §§ 1.56A-19(b) through 1.56A-19(g) disregard any gain or loss reflected in FSI and the regular tax rules would govern the treatment of the transactions, but the resulting CAMT consequences would be determined using CAMT basis and CAMT attributes.
  - For example, in a transaction that qualifies as a reorganization under section 368(a)(1)(A), the CAMT consequences to each of the transferor corporation, the acquiror corporation, and the transferor corporation's shareholder generally are as follows:
    - <u>Transferor Corporation:</u> (i) determine AFSI by applying the relevant nonrecognition provision (section 361), (ii) take an exchanged basis in the acquiror corporation stock received equal to its CAMT basis in the assets transferred (section 358), and (iii) adjust CAMT earnings resulting from the transaction by applying section 312.

    - Acquiror Corporation: (i) determine AFSI by applying the relevant nonrecognition provision (section 1032(a)), (ii) take a carryover basis in the transferred assets equal to the transferor corporation's CAMT basis in such assets (section 362), (iii) adjust its CAMT earnings by applying section 312, and (iv) succeed to the transferor corporation's CAMT earnings and other CAMT attributes.
    - Transferor Corporation's Shareholder: (i) determine AFSI by applying the relevant nonrecognition provision (section 354), (ii) take an exchanged basis in the acquiror corporation stock received based on its CAMT basis in the transferor corporation stock surrendered (section 358), and (iv) adjust CAMT earnings under section 312.
        - If the transferor corporation's shareholder receives boot in the exchange, section 356 would apply, based on CAMT stock basis and other attributes.
  - Similar rules apply for B Reorganizations, E Reorganizations, and F Reorganizations.
  - In either a section 355 distribution or a reorganization under sections 368(a)(1)(D) and 355, any gain or loss reflected in FSI is disregarded and the CAMT consequences for each of the distributing corporation, the controlled corporation (for divisive reorganizations only), and the distributing corporation's shareholder generally are the following:
    - Distributing Corporation: (i) determine AFSI by applying the relevant nonrecognition provision (section 355(c) or section 361), (ii) take an exchanged basis in the controlled corporation stock or securities received (section 358 - for divisive reorganizations only) equal to its CAMT basis in the property transferred, and (iii) adjust CAMT earnings by applying section 312.
    - Controlled Corporation: (i) determine AFSI by applying the relevant nonrecognition provision (section 1032(a)), (ii) take a carryover basis in the transferred assets equal to the distributing corporation's CAMT basis in such assets, and (iii) adjust its CAMT earnings by applying section 312.
    - Distributing Corporation's Shareholder / Security Holder: (i) determine AFSI by applying the relevant nonrecognition provision (section 355(a)), (ii) determines CAMT basis in the controlled stock under the relevant Code section, and (iii) adjusts CAMT earnings under section 312.
  - In an exchange of property that qualifies for nonrecognition treatment under section 351(a), any gain or loss reflected in FSI is disregarded and the CAMT consequences for the transferor and the transferee corporation generally are the following:
    - Transferor: (i) determine AFSI by applying the relevant nonrecognition provision (section 351(a)), and (ii) take an exchanged basis in the transferee stock received equal to its CAMT basis in the property transferred (section 358).
    - Transferee Corporation: (i) determine AFSI by applying the relevant nonrecognition provision (section 1032(a)) and (ii) take a carryover basis in the transferred assets equal to the transferor's CAMT basis in such assets (section 362).
    - Special basis redetermination rules would apply if (i) the transferor recognizes gain that would increase the transferee corporation's basis in the transferred assets under section 362, and (ii) other specific criteria are met (for example, the transferor is not an applicable corporation).
- In general, if, in connection with any of the transactions described above, any party recognizes gain or loss, then such transaction would be a covered recognition transaction and such party would (i) redetermine any gain or loss reflected in its FSI using CAMT basis in lieu of AFS basis, (ii) take a basis in the property received equal to the AFS basis for such property, and (iii) adjust CAMT earnings to reflect the amount of AFSI gain or loss taken into account.

- If, in connection with a divisive reorganization, the controlled corporation issues both stock and boot, and the distributing corporation purges all of such boot pursuant to section 361(b), the transaction would not be treated as a covered recognition transaction for the controlled corporation.
- In a section 351 exchange with boot, the special basis redetermination rules described above could apply.

Prop. Treas. Reg. § 1.56A-20: AFSI Adjustments to Apply Certain Subchapter K Principles

- Very generally, under section 56A(c)(15)(B), adjustments are made to the AFSI of a CAMT entity that is a partner in a partnership to include certain principles of subchapter K in connection with partnership contributions and distributions. Unlike Notice 2023-7, the proposed regulations adopt a deferred sale approach, which applies to contributions to or distributions from a partnership of built-in gain or built-in loss property when gain or loss is recognized for AFS purposes.
- Under the deferred sale approach, upon a contribution of built-in gain or built-in loss property to a partnership to which section 721(a) applies (or in the case of a distribution of property to which section 731(b) applies), a CAMT entity must include the amount of any deferred sale gain or loss in its AFSI ratably on a monthly basis, over the applicable period, depending on the type of property contributed. Similar deferred gain or loss rules, as discussed below, also apply in the case of property distributed by a partnership. With respect to the contribution of built-in gain or built-in loss property:
  - The amount of deferred sale gain or loss generally is the amount of gain or loss reflected in the contributor's FSI resulting from the contribution of deferred sale property (subject to certain adjustments to take into account the CAMT basis in the property when the contribution is treated as a sale or exchange for AFS purposes).
  - Different applicable recovery periods apply depending on whether the deferred sale property is section 168 property, depreciable or amortizable property that is not section 168 property, or other property (which is assigned a 15-year recovery period for this purpose).
  - The rules also provide for acceleration events. Specifically, a partial acceleration generally applies if the contributor's distributive share percentage decreases by more than one-third. Full acceleration of any deferred sale gain or loss applies if the partnership sells, distributes, or otherwise disposes of deferred sale property (including in a nonrecognition transaction or even a distribution back to the contributing partner). In these instances, the contributor includes in its AFSI in the taxable year of the disposition the amount of any remaining deferred sale gain or loss.
  - Special rules apply in the case of tiered partnerships.
- A partnership's initial CAMT basis in property contributed by a CAMT entity is the partnership's initial AFS basis in the contributed property at the time of contribution, regardless of whether section 721(a) applies in whole or in part to the contribution. Similarly, a CAMT entity partner's initial CAMT basis in property distributed by a partnership is the partner's initial basis in the property for AFS purposes (determined immediately after the distribution).
- The initial CAMT basis of an interest in a partnership upon a contribution of property to which section 721(a) applies is the contributor's AFS basis, decreased by any deferred sale gain or increased by any deferred sale loss that is required to be included in the contributor's AFSI. With respect to the determination of historic attributes, a CAMT entity's CAMT basis in its partnership investment is equal to the CAMT entity's AFS basis in the partnership investment as of the first day of the partnership's first taxable year ending after December 31, 2019, in which the CAMT entity held its

interest in the partnership, adjusted for each taxable year of the partnership ending after December 31, 2019.

- The treatment of partner and partnership liabilities for purposes of determining a CAMT entity partner's or partnership's AFSI is based on the applicable liability treatment for AFS purposes and not under section 752. As a result, any rules relating to liabilities for regular tax purposes, including the qualified liability rules under section 707(a)(2)(B) and inclusion of liabilities in outside basis for purposes of section 705, do not apply. Thus, transactions that may be nonrecognition transactions for regular tax purposes (for example, contribution of property to a partnership subject to a qualified liability under the section 707(a)(2)(B) regulations, or a debt-financed distribution supported by section 752 basis) may be treated as recognition transactions for CAMT purposes.
- If a transfer of property by a partner to a partnership or by a partnership to a partner does not constitute a nonrecognition transaction in whole or in part (for example, because section 707(a)(2)(B) qualified liability principles and section 752 principles do not apply for CAMT purposes), then the CAMT entity partner or partnership includes in its AFSI or modified FSI, as applicable, a proportionate amount of the FSI associated with the transaction in accordance with a specified formula. This proportionate approach is a change from the partnership transaction rules in Section 3 of Notice 2023-7, which provided a "cliff effect" to AFSI and CAMT basis attributes for part recognition partnership transactions.

Partnership Reporting and Recordkeeping Requirements (Prop. Treas. Reg. §§ 1.56A-5 and 1.56A-20)

- The proposed regulations generally have very expansive reporting and recordkeeping requirements with respect to partnerships (especially in the case of tiered partnerships), including requirements to both request and provide information with respect to the applicable method for distributive share, separately stated items, and information relevant to the application of the deferred sale approach. However, a partnership generally is not required to furnish information to a CAMT entity that is a partner in the partnership until it has notice of a request to provide such information. Once requested, the partnership must continue providing information to a CAMT entity partner due to a request made in a prior taxable year. Penalties under sections 6031(b) and 6722 would apply to the partnership, if applicable.
  - A CAMT entity must generally request CAMT information from partnerships by the 30th day after the close of the taxable year of the partnership to which the request relates. Thus, for calendar tax year partnerships, a CAMT entity will have until January 30, 2025, to request the necessary information from the partnership for the 2024 tax year.
  - In tiered partnership structures, if an upper-tier partnership requires information from a lower-tier partnership to meet its reporting and filing requirements, the upper-tier partnership must request the information from the lower-tier partnership by the later of 30 days after the close of the taxable year of the lower-tier partnership or 14 days after the date the upper-tier partnership receives a request for the information from another upper-tier partnership.
- If a partnership is subject to the centralized partnership audit regime (the BBA), a CAMT entity that is a partner in the partnership must file a notice of inconsistent treatment in accordance with section 6222 if making the required estimate requires the CAMT entity to treat a partnership-related item inconsistent with how the partnership treated the item. In addition, if a BBA partnership previously filed its partnership return for the taxable year and the due date has passed, the BBA partnership must file an AAR in order to adjust any partnership-related items, including as part of furnishing information to a CAMT entity.

Prop. Treas. Reg. § 1.56A-21: AFSI Adjustments for Troubled Companies

- Prop. Treas. Reg. § 1.56A-21 provides rules for determining AFSI with respect to events relating to the bankruptcy or insolvency of a CAMT entity.
- Consistent with Notice 2023-7, Prop. Treas. Reg. § 1.56A-21 includes exclusions from AFSI for FSI relating to the discharge of indebtedness of a CAMT entity in a Title 11 case or that is insolvent (but only to the extent of insolvency).
  - Insolvency is determined under section 108(d)(3) (that is, excess of liabilities over gross fair market value of assets).
  - Disregarded entities would be eligible for these exclusions only if the CAMT entity that is its regarded owner is eligible.
  - For partners in partnership, (i) partnership AFSI excludes FSI from discharge of indebtedness, which is separately stated to the partner, and (ii) eligibility for the exclusions, and any corresponding attribute reduction, is determined at the partner level (taking into account liabilities allocated under section 752).
- Prop. Treas. Reg. § 1.56A-21 requires a CAMT entity to reduce attributes for the amount of excluded FSI in the following order:
  - (i) CAMT basis of covered property (for example, section 168 property and qualified wireless spectrum) but only to the extent the basis of the covered property is reduced under section 108 for regular tax purposes, (ii) FSNOLs, (iii) CFC adjustment carryovers, (iv) CAMT basis of non-covered property that is depreciated or amortized for AFS purposes, (v) CAMT basis of non-covered property that is not depreciated or amortized for AFS purposes, (vi) CAMT foreign tax credits (not dollar-for-dollar), and (vi) any remaining CAMT basis of covered property.
  - Attribute reductions are made after the determination of CAMT liability for the taxable year of the discharge. Attribute reduction does not apply to any discharge that occurs in a taxable year beginning on or before December 31, 2019.
  - CAMT basis reductions are made immediately before the close of the taxable year of the discharge solely with respect to assets that the CAMT entity holds at the beginning of the next taxable year.
- Prop. Treas. Reg. § 1.56A-21 provides for certain AFSI computations for CAMT entities emerging from bankruptcy.
  - Consistent with Notice 2023-7, in general, (i) gain or loss reflected in FSI resulting from a CAMT entity's emergence is disregarded, (ii) any adjustment to AFS basis of assets is disregarded in computing CAMT basis, and (iii) CAMT earnings are adjusted by applying section 312.
  - Clarifies that the discharge of indebtedness provisions take priority over the emergence from bankruptcy provisions for purposes of determining the CAMT consequences of a discharge of indebtedness.
  - CAMT consequences for emergence transactions that are covered transactions are determined by applying Prop. Treas. Reg. §§ 1.56A-18 and -19 (relating to covered recognition transactions and covered nonrecognition transactions, respectively).

Prop. Treas. Reg. § 1.56A-22: AFSI Adjustments for Certain Insurance Companies and Other Specified Industries

- Prop. Treas. Reg. § 1.56A-22(c)(1) provides that Prop. Treas. Reg. §§ 1.56A-4, 1.56A-5, and 1.56A-18 through 1.56A-20 (and, thus, any statutory AFSI adjustments implemented by these provisions) do not apply to exclude from an insurance company's AFSI any gains or losses on assets supporting covered variable contracts, as defined in Prop. Treas. Reg. § 1.56A-22(b)(5), to the extent that (i) the gains and losses result in a change in the amount of the obligations to the contract holders, and (ii) this change is included in the insurance company's FSI.

- Prop. Treas. Reg. § 1.56A-22(b)(5) defines "covered variable contracts" more broadly than Notice 2023-20 which included only specific types of contracts.
  - The term covered variable contract means a contract (i) that is issued by a covered insurance company; (ii) that is regulated as a life insurance or annuity contract in the jurisdiction in which it is issued; and (iii) for which the amount of the covered insurance company's obligations to the contract holder depends in whole or in part (by law, regulation, or the terms of the contract) on the value of the assets that are designated to support the contract. (Prop. Treas. Reg. § 1.56A-22(b)(5)).
- The proposed regulations provide rules for AFSI adjustments with respect to covered reinsurance agreements that are consistent with Notice 2023-20.
- Prop. Treas. Reg. § 1.56A-22(d)(1)(i) provides that the ceding company in a "covered reinsurance agreement" (defined in Prop. Treas. Reg. § 1.56A-22(b)(4)) excludes from AFSI any changes in the amount of the payable to the reinsurer that correspond to the unrealized gains and losses in the withheld assets to the extent the unrealized gains and losses are not included in AFSI.
  - The term covered reinsurance agreement means a funds withheld reinsurance or modified coinsurance agreement and any retrocession of all or part of the risk under either such agreement. Under these agreements, the reinsurance operates like conventional reinsurance, but from a legal title and financial accounting perspective, the ceding company retains the investment assets supporting the obligations to the holders of the underlying contracts (and for modified coinsurance, the ceding company also retains the reserves). The ceding company records a liability to the reinsurer to reflect the assets it has retained. (Prop. Treas. Reg. § 1.56A-22(b)(4)).
- Under Prop. Treas. Reg. § 1.56A-22(d)(1)(ii), the reinsurer in a covered reinsurance agreement excludes from AFSI any changes in the amount of the receivable from the ceding company that correspond to the unrealized gains and losses in the assets withheld by the ceding company.
- Prop. Treas. Reg. § 1.56A-22(d)(3), related to accounting for the reinsurance arrangement at fair value, "turns off" the general rule in Prop. Treas. Reg. § 1.56A-22(d)(1) if the insurance company either (i) makes an election for AFS purposes to account for the covered reinsurance agreement at fair value in its FSI, or (ii) otherwise accounts for both the payable (for the ceding company) or the receivable (for the reinsurer) and the covered reinsurance agreement at fair value in its FSI. Thus, Prop. Treas. Reg. § 1.56A-22(d)(3), applies only if the covered reinsurance agreement is accounted for at fair value in FSI.
- Consistent with Notice 2023-20, under Prop. Treas. Reg. § 1.56A-22(e), for purposes of determining AFSI, the adjusted basis of any asset held by an entity since the date it became fully taxable is determined in accordance with the particular Act that fully subjected the entity to federal taxation. This provision applies to certain Blue Cross or Blue Shield organizations.
- Prop. Treas. Reg. § 1.56A-24 provides certain adjustments to AFSI for an AFSI hedge or the related item. Specifically, under Prop. Treas. Reg. § 1.56A-24(b)(1), an "AFSI hedge" generally includes hedging transactions for regular tax purposes as well as hedging transactions for financial accounting purposes.
- Prop. Treas. Reg. § 1.56A-24(b)(1)(ii)(A) provides an exception for a hedging transaction entered into by an insurance company to hedge obligations to holders of life insurance or annuity contracts that take into account the value of one or more specified assets or indices (for example, variable annuity contracts that have guaranteed minimum benefits), because the amount of the liabilities that corresponds to the hedging transaction is also included in the insurance company's FSI.

Prop. Treas. Reg. § 1.56A-23: AFSI Adjustments for FSNOL and Other Attributes

- Prop. Treas. Reg. § 1.56A-23 provides rules under section 56A(d) for purposes of determining adjustments to AFSI for FSNOLs and built-in losses.
- Consistent with section 56A(d), the proposed regulations provide that (i) an FSNOL is negative AFSI for a taxable year ending after December 31, 2019, (ii) the 80-percent AFSI limitation applies, and (iii) the carryforward period is indefinite.
- In general, Prop. Treas. Reg. § 1.56A-23 implements the guidance set forth in Section 12 of Notice 2023-64 providing that an FSNOL is absorbed to the extent a corporation has positive AFSI in a subsequent taxable year even if such corporation is not an applicable corporation.
- Prop. Treas. Reg. § 1.56A-23 provides new guidance with respect to limitations on the use of FSNOLs and built-in losses.
  - The limitations are based on separate return limitation year (SRLY)-type principles. Notably, section 382 does not apply.
  - These limitations apply where a corporation is acquired pursuant to (i) a section 381(a) transaction, or (ii) a stock acquisition that constitutes an ownership change within the meaning of Prop. Treas. Reg. § 1.59-2(f).[8]
  - In general, Prop. Treas. Reg. § 1.56A-23(e) provides that acquired FSNOLs can only be used to reduce the AFSI of a corporation if the acquired business that generated such FSNOLs is separately tracked in the corporation's books and records. Similar to SRLY rules for regular tax purposes, any such reduction are limited to the amount of AFSI generated by the separately tracked business after the acquisition pursuant to a tracked register (and subject to the 80-percent AFSI limitation).
    - Special rules apply for (i) certain transfers of the acquired business, (ii) integrations of the acquired business with another business, and (iii) multiple separately tracked businesses of the acquired corporation.
    - An example provides that related business assets transferred to a corporation that has FSNOLs and a separately tracked business can be taken into account.
- In general, Prop. Treas. Reg. § 1.56A-23(f) applies the limitation on acquired FSNOLs to the use of built-in losses if the acquired corporation had a CAMT "net unrealized built-in loss" (NUBIL) immediately before the acquisition.
  - A CAMT NUBIL would exist if (i) there is a section 382 ownership change, and there is a NUBIL based on CAMT basis, or (ii) if there is no section 382 ownership change, if there would be a NUBIL on the transaction date taking into account CAMT basis and income, expenses, gains, and losses attributable to periods before the acquisition.
  - The section 382 rule that limits "recognized built-in loss" to the amount of NUBIL would not apply, and thus, the entire unrealized loss would be subject to limitation.
  - The proposed rules for built-in losses also, among other things, provide (i) an ordering rule that built-in losses reduce AFSI before any acquired FSNOLs are allowed to reduce AFSI, and (ii) that disallowed built-in losses would be treated as a separate, pre-acquisition FSNOL carryover.

Prop. Treas. Reg. § 1.56A-24: AFSI Adjustments for Hedging Transactions and Hedged Items

- Prop. Treas. Reg. § 1.56A-24 addresses potential timing differences between hedges and hedged items from an accounting perspective and an accounting/tax perspective.
- A hedge is subject to the proposed regulations if it is an "AFSI Hedge," which is defined as an asset or a liability of a CAMT entity for which there are fair value measurement adjustments and that--
  - (A) is entered into as a hedging transaction, as defined in Treas. Reg. § 1.1221-2(b) (whether or not the character of gain or loss

from the transaction is determined under Treas. Reg. § 1.1221-2), a Treas. Reg. § 1.1275-6 hedge that is part of an integrated transaction subject to Treas. Reg. § 1.1275-6, a section 1256(e) hedging transaction, a section 988(d) hedging transaction that is part of a transaction that is integrated under Treas. Reg. § 1.988-5 or other regulations issued under section 988(d) of the Code (or an advance ruling described in Treas. Reg. § 1.988-5(e)) that govern the character or timing of gain or loss from the transaction, or a position that is a hedge under section 475(c)(2)(F) of the Code;
  - (B) is a hedge that qualifies for, and is properly treated by the CAMT entity as subject to, hedge accounting (for example, under Accounting Standards Codification paragraph 815-20-25-1 or IFRS 9 Chapter 6) and reported on a CAMT entity's AFS; or
  - (C) is described in both paragraphs (A) and (B).
- The proposed regulations attempt to match the timing of gain or loss on the hedging transactions to that of the hedge items (and vice versa) from a financial accounting perspective. The "fair value measurement adjustment" is the financial accounting concept on which these rules are based. Prop. Treas. Reg. § 1.56A-24(c)(2) achieves this result by disregarding any gain or loss on either the hedge or the hedged item if the gain or loss on the other leg is not included in AFSI.
  - Specifically, a fair value measurement adjustment is disregarded by a CAMT entity for purposes of determining its AFSI if either:
    - The CAMT entity marks to market the hedge but not the hedge item for financial accounting purposes, and does not mark either for tax purposes, or
    - The CAMT entity marks to market the hedged item but not the hedge for financial accounting purposes, and does not mark either for tax purposes.
- Prop. Treas. Reg. § 1.56A-24(e)(1) provides operative rules for the inclusion of certain taxable amounts in AFSI for fair value measurement adjustments disregarded from a CAMT entity's AFSI under Prop. Treas. Reg. § 1.56A-24(c)(2). Under Prop. Treas. Reg. § 1.56A-24(e)(1), if the fair value measurement adjustment includes items corresponding to items of income, gain, deduction, or loss for regular tax purposes, such as the accrual of original issue discount on a bond, those items would be taken into account for AFSI purposes.
- Prop. Treas. Reg. § 1.56A-24(e)(2) provides for subsequent adjustments for an AFSI hedge or a hedged item (as applicable) in the taxable year in which there is an AFSI subsequent adjustment date. In general, Prop. Treas. Reg. § 1.56A-24(e)(2) would provide for the inclusion in AFSI of the cumulative fair value measurement adjustments previously disregarded in determining AFSI under Prop. Treas. Reg. § 1.56A-24(c)(2) and for certain adjustments to CAMT basis.
- Prop. Treas. Reg. § 1.56A-24(d) provides rules for net investment hedges.
  - Prop. Treas. Reg. § 1.56A-24(d) states that if an entity marks to market the net investment hedge for tax purposes it would take such tax marked-to-marked gain or loss into account for AFSI purposes.
  - Prop. Treas. Reg. § 1.56A-24(e)(3) provides for subsequent adjustments for a net investment hedge in the taxable year in which a net investment hedge matures or is sold, disposed of, or otherwise terminated, or the asset or liability that was a net investment hedge subject to Prop. Treas. Reg. § 1.56A-24(d) otherwise ceases to constitute a net investment hedge.

Prop. Treas. Reg. § 1.56A-26: AFSI Adjustments for Certain Related-Party Transactions and CAMT Avoidance Transactions

- Prop. Treas. Reg. § 1.56A-26(b) provides that if the AFSI of a CAMT entity reflects a loss resulting from a sale, exchange, or any other disposition of property (including stock) between that CAMT entity and one or more

CAMT entities that are part of that CAMT entity's CAMT-related group, that loss is deferred for AFSI purposes until no member of that CAMT entity's CAMT-related group holds that property (in whole or in part).
- Prop. Treas. Reg. § 1.56A-26(c) provides an anti-abuse rule for arrangements undertaken with a principal purpose of avoiding CAMT, including avoiding treatment as an applicable corporation or reducing or otherwise avoiding a liability under section 55(a). The Commissioner is permitted to disregard or recharacterize such arrangements to the extent necessary to carry out the purposes of CAMT.
- Prop. Treas. Reg. § 1.56A-26(d) provides that any item of income, expense, gain, or loss reflected in the FSI of a CAMT entity with respect to a controlled transaction or controlled transfer (as defined in Treas. Reg. § 1.482-1(i)(8)) between two or more CAMT entities must be adjusted to reflect the principles of section 482 and the regulations under section 482, regardless of whether section 482 otherwise is considered to apply.

Prop. Treas. Reg. § 1.56A-27: AFSI Adjustments for Foreign Governments

- The proposed regulations provide for an adjustment to AFSI of a foreign government for any amount that, if it were properly treated as gross income for regular tax purposes, would be excluded from gross income and exempt from taxation under section 892.

CAMT Foreign Tax Credit (FTC)

Prop. Treas. Reg. § 1.59-4: Rules for Determining the CAMT FTC

- Prop. Treas. Reg. § 1.59-4 provides that a CAMT FTC is available with respect to an Eligible Tax.[9]
- Generally, for an applicable corporation that is a domestic corporation, the amount of the CAMT FTC for the taxable year would equal the sum of two amounts: (i) the lesser of (A) the aggregate of the applicable corporation's pro rata share of taxes of CFCs, as determined under Prop. Treas. Reg. § 1.59-4(d), or (B) the product of the amount of the adjustment under Prop. Treas. Reg. § 1.56-6(b)(1) and the percentage specified in section 55(b)(2)(A)(i) (currently, 15 percent), and (ii) the amount of Eligible Taxes paid by the applicable corporation during the taxable year, to the extent the taxes have been taken into account, within the meaning of Prop. Treas. Reg. § 1.56A-8(d), on the applicable corporation's AFS.
- Generally, under Prop. Treas. Reg. § 1.59-4(d), an applicable corporation's pro rata share of the taxes of a CFC in which the applicable corporation is a US shareholder for the taxable year is the sum of two amounts: (i) the applicable corporation's pro rata share of taxes under section 960(b), and (ii) the applicable corporation's pro rata share of eligible current year taxes, as defined in Treas. Reg. § 1.960-1(b)(5), of the CFC, in each case reduced to reflect the suspensions and disallowances described in the definition of an "Eligible Tax" that apply at the level of the US shareholder.
- Section 59(l)(2) provides that, if an applicable corporation's pro rata shares of foreign income taxes of the CFCs in which it is a US shareholder exceeds 15 percent of the adjustment under section 56A(c)(3) (such excess, "unused CFC taxes"), then the unused CFC taxes are carried forward to any of the first five succeeding taxable years to the extent not absorbed in a prior taxable year. Prop. Treas. Reg. § 1.59-4(e)(3) provides an ordering rule requiring the unused CFC taxes from the fifth preceding taxable year to be absorbed first, followed sequentially by the unused CFC taxes from the fourth, third, second, and first preceding taxable year.
- Generally, a foreign income tax may be claimed as a CAMT FTC in the taxable year in which the tax is paid, within the meaning of Treas. Reg. § 1.901- 2(g)(5), to the extent the taxes have been taken into account, within the meaning of Prop. Treas. Reg. § 1.56A-8(d), in the AFS of the CFC or the applicable corporation, as applicable. In many instances, the timing of

the CAMT FTC will align with the timing of the foreign tax credit for regular tax purposes.

- Prop. Treas. Reg. § 1.59-4(f) provides that foreign income taxes paid or accrued as a result of a foreign tax redetermination are eligible to be claimed as a CAMT FTC only if the domestic corporation is an applicable corporation in the taxable year to which the foreign tax redetermination relates (the relation-back year). A CAMT FTC with respect to such redetermined foreign income taxes may be claimed only in the relation-back year, even if the taxes are reflected in a journal entry of an AFS within a taxable year that is later than the relation-back year.
- Prop. Treas. Reg. § 1.59-4(g) provides that the amount of Eligible Taxes paid or accrued for the taxable year by an applicable corporation (under Prop. Treas. Reg. § 1.59-4(c)(2)) that is a direct or indirect partner in a partnership includes the amount of creditable foreign tax expenditures, within the meaning of Treas. Reg. § 1.704-1(b)(4)(viii), allocated to the applicable corporation for regular tax purposes, reduced by the suspensions and disallowances described in the definition of "Eligible Tax" that apply at the level of the partner.

Consolidated Groups

Prop. Treas. Reg. § 1502-2: Computation of Tax Liability

- Adds the CAMT to the list of taxes that are added together to determine the consolidated group's tax liability for a consolidated return year.

Prop. Treas. Reg. § 1.1502-53: Consolidated Minimum Tax Credit

- Provides rules relating to a consolidated group's determination of its consolidated minimum tax credit and use against the consolidated group's regular tax liability.
- Provides rules (i) limiting the consolidated group's use of a minimum tax credit arising in a separate return year of a member, and (ii) with respect to the allocation of a consolidated minimum tax credit to a member that departs the consolidated group.

Prop. Treas. Reg. § 1.1502-56A: Corporate Alternative Minimum Tax

- Provides rules regarding the computation of AFSI and CAMT liabilities of consolidated groups.
- Generally provides that members of a consolidated group are treated as a single CAMT entity. Any partnership wholly owned by the consolidated group would continue to be treated as a partnership.
- The FSI of a consolidated group is generally determined based on the AFS that includes the consolidated group, which is determined under Prop. Treas. Reg. § 1.56A-1 and -2 and may include non-members.
- Consistent with Notice 2023-64, the proposed rules generally disregard, or take into account, AFS consolidated entries (for example, elimination entries) depending on whether the other party to the transaction is in the same consolidated group.
  - AFS consolidated entries between members are only taken into account if, at the end of the taxable year, (i) each member continues to be a member, and (ii) all relevant property is held by the consolidated group.
  - If the conditions above are not met, then, subject to a whole group acquisition exception, certain AFS consolidation entries generally would cease to be taken into account, and any CAMT consequences would be determined.
- In general, the AFSI of the consolidated group includes gain or loss from one member's sale of stock of another member, using the CAMT basis of the stock.

- The initial CAMT basis of a member's stock that was held by a member on the first day of the first taxable year after December 31, 2019, generally is the regular tax basis as of such time.
  - If stock of a member was not held on such date, the CAMT basis is determined based on the acquisition.
  - In each case, the CAMT basis of the member's stock is subject to adjustments generally in conformity with the basis adjustment rules for regular tax under Treas. Reg. § 1.1502-32.
- Provides rules with respect to regular tax items that replace AFSI items (for example, tax depreciation) and that arise from intercompany transactions between members pursuant to Treas. Reg. § 1.1502-13.
  - In general, any increase or decrease in a regular tax item that results from an intercompany transaction is disregarded.
  - If, however, an AFS consolidation entry relating to the intercompany transaction ceases to be taken into account (for example, a member left the consolidated group), then AFSI would be increased or decreased by the relevant regular tax item that was previously disregarded.
- Provides rules relating to the use of FSNOL carryovers.
  - Generally treats consolidated FSNOL carryovers in a manner similar to the treatment of consolidated net operating loss carryovers for regular tax purposes under Treas. Reg. § 1.1502-21(b), including ordering rules and apportioning consolidated FSNOL carryovers to departing members.
  - The 80-percent AFSI limitation that applies to the use of consolidated FSNOL carryovers applies to consolidated AFSI.
  - Acquired FSNOL are subject to limitations similar to the SRLY rules as set forth in Prop. Treas. Reg. § 1.56A-23(e) (including no section 382 limitation).
- Generally treats consolidated CFC adjustment carryovers in a manner similar to consolidated FSNOL carryovers, but with no 80-percent AFSI limitation and less expansive SRLY-type limitations.
  - Under Prop. Treas. Reg. § 1.1502-56A(h), the use of consolidated CFC adjustment carryovers to reduce the consolidated group's adjustment to AFSI under Prop. Treas. Reg. § 1.56A-6(b)(1) is determined under rules that are based upon the rules in Prop. Treas. Reg. § 1.1502-56A(f), with certain modifications that reflect the rules for CFC adjustment carryovers. For example, the 80-percent limitation in section 56A(d)(1) does not apply to CFC adjustment carryovers and is therefore not included in Prop. Treas. Reg. § 1.1502-56A(h).
- Generally treats consolidated unused CFC taxes in a manner similar to consolidated FSNOL carryovers, including similar SRLY-type rules.
  - Prop. Treas. Reg. § 1.1502-56A(i)(1) generally provides that the amount of consolidated unused CFC taxes of a tax consolidated group that can be used to determine the consolidated tentative minimum tax of the group for any consolidated return year is the aggregate of the group's unused CFC taxes in that year. Prop. Treas. Reg. § 1.1502-56A(i)(2) provides that consolidated unused CFC taxes include both (i) any unused CFC taxes of the consolidated group to the extent available for use under the carryover rules in Prop. Treas. Reg. § 1.59-4(e), and (ii) any unused CFC taxes of the members of the group arising in the respective separate return years of those members to the extent available for use under the carryover rules in Prop. Treas. Reg. § 1.59-4(e). Prop. Treas. Reg. § 1.1502-56A(i)(3) provides rules limiting the use of unused CFC taxes from separate return years of a member. Prop. Treas. Reg. § 1.1502-56A(i)(4) provides rules regarding the amount of unused CFC taxes that can be used in a consolidated return year. Prop. Treas. Reg. § 1.1502-56A(i)(5) provides rules regarding situations in which one or more members deconsolidate from the group.
- Generally allocates CAMT liability to members based on the member's proportionate share of positive AFSI for the taxable year.
- Generally allocates AFSI to a member that leaves the consolidated group for purposes of the applicable corporation determination based on treating the

member as a separate taxpayer for the relevant years (and the AFSI of the consolidated group would not be reduced).

Footnotes

[1] Prop. Treas. Reg. § 1.59-3(d) provides that if a foreign corporation is or is treated as engaged in a US trade or business for purposes of section 882, the US trade or business will be treated as a separate domestic corporation (a "deemed domestic corporation") that is wholly owned by the foreign corporation.
[2] Prop. Treas. Reg. § 1.59-3(f)(1) defines a "controlling interest" based on whether the applicable financial accounting standard requires that a consolidated financial statement of the upper-tier entity reflects the assets, liabilities, equity, income, and expenses of the lower-tier entity (regardless of whether a consolidated financial statement is or is required to be prepared, or is prepared correctly). In addition, special rules are provided which treat an upper-tier entity as having a controlling interest in other entities (notwithstanding that such controlling interest does not exist under the applicable financial accounting standard).
[3] If a CAMT entity's AFS is prepared on the basis of a financial accounting period that differs from the CAMT entity's taxable year, Prop. Treas. Reg. § 1.56A-3(b) provides that the CAMT entity computes FSI and AFSI as if the financial reporting period were the same as the taxable year by conducting an interim closing of the books using the accounting standards the CAMT entity uses to prepare the AFS.
[4] Prop. Treas. Reg. § 1.56A-6(c)(4) provides that the adjustment for foreign income taxes provided in Prop. Treas. Reg. § 1.56A-8(c) does not apply in computing a CFC's adjusted net income or loss.
[5] The proposed regulations provide that adjusted net income or loss of a CFC must be expressed in US dollars using the weighted average rate as defined in Treas. Reg. § 1.989(b)-1 for the CFC's taxable year.
[6] *See* Prop. Treas. Reg. § 1.56A-6(e)(3), Example 3.
[7] The preamble to the proposed regulations notes that the Treasury Department and the IRS are of the view that it is not necessary to make the clarification provided in Section 7.02(5) of Notice 2023-64, because section 894(a) already provides that "the Code is applied with due regard to any income tax treaty obligation of the United States that applies to a taxpayer, and nothing in the IRA changes the normal operation of US income tax treaties in this context."
[8] Generally, where the corporation and its test group parent(s) no longer satisfy the relationship criteria under section 52(a) or (b) or section 59(k)(2)(A) (as applicable), or the acquired corporation joins a tax consolidated group.
[9] The proposed regulations do not apply the limitations under section 960(d) with respect to taxes imposed on tested income of the CFC and the CAMT FTC is not subject to the section 904 limitation.

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