

The Form 5471 Series

Episode 5

Subpart F Income

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August 25, 2023

The Form 5471 Series (2023-2024)

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1. What is Subpart F Income?

Where **subpart F** fits into the United States Code

- **Title 26** (mostly means the same thing as the Internal Revenue Code)
- **Subtitle A** (income tax, self-employment tax, net investment income tax, withholding rules, and consolidated returns)
- **Chapter 1** (income tax, or as they call it, “normal taxes and surtaxes”)
 - **Subchapter N** (the international stuff we know and love)
 - **Part III** (income from sources outside the United States)
 - **Subpart F (controlled foreign corporations)**

Subpart F **income** — certain types of foreign corporation income

- **Subpart F income** is an arbitrary definition in the Internal Revenue Code.
- It is the sum of five different types of income earned by a controlled foreign corporation. IRC §952(a).

IRC §951(a)(1) includes subpart F income in the shareholder's income

- (1) *In general.* If a foreign corporation is a controlled foreign corporation at any time during any taxable year, every person who is a United States shareholder (as defined in subsection (b)) of such corporation and who owns (within the meaning of section 958(a)) stock in such corporation on the last day, in such year, on which such corporation is a controlled foreign corporation **shall include in his gross income**, for his taxable year in which or with which such taxable year of the corporation ends—
 - **(A) his pro rata share (determined under paragraph (2)) of the corporation's subpart F income for such year, and**
 - (B) the amount determined under section 956 with respect to such shareholder for such year (but only to the extent not excluded from gross income under section 959(a)(2)).

Other closely-related forced income inclusions

- IRC §951(a)(1). Subpart F income.
- IRC §956. Earnings and profits invested in U.S. assets.
- IRC §965(a). The computed income amount is included in subpart F income.
- **All of the above income inclusion items are forced by IRC §951(a)(1) onto the U.S. shareholder's income tax return.**
- And of course let's not forget . . . IRC §951A. Global Intangible Low-Taxed Income. That's in Episode 6, next month.

Subpart F income vs. Global Intangible Low-Taxed Income

- Form 5471, Schedule I-1 (Dec. 2021)

		Functional Currency	Conversion Rate	U.S. Dollars
1	Gross income (see instructions if cost of goods sold exceed gross receipts)	1		
2	Exclusions (see instructions if cost of goods sold exceed gross receipts)			
	a Effectively connected income	2a		
	b Subpart F income	2b		
	c High tax exception income per section 954(b)(4)	2c		
	d Related party dividends	2d		
	e Foreign oil and gas extraction income	2e		
3	Total exclusions (combine lines 2a through 2e)	3		
4	Gross income less total exclusions (line 1 minus line 3) (see instructions)	4		

The Supreme Court may make all of this irrelevant

- A pending United States Supreme Court challenges the validity of IRC §965: *Moore v. United States*.
- The taxpayer claims that the a tax on accumulated earnings of a foreign corporation violates the 16th Amendment. The Federal power to tax income is limited to income that is “realized.” This principle has been in place since a 1920 Supreme Court case, *Eisner v. Macomber*.
- The taxpayer argues that undistributed foreign corporation earnings are not “realized” by a shareholder, so the IRC §965 transition tax (which forced inclusion of untaxed earnings and profits in shareholder income) was unconstitutionally imposed.

2. Why Does Subpart F Income Exist?

Paper exploits gave taxpayers the keys to the tax-deferral kingdom

- Tax deferral for passive income earned by a foreign corporation but not distributed to the U.S. shareholder as a dividend. The taxpayer controls timing of income recognition, therefore plays the Time Value of Money Game like a pro.
- *Countermeasure: Foreign Personal Holding Company Income.*
- Why should your domestic C corporation collect all of the profit? Why not set up a sales subsidiary in a tax-free country, and take a slice of the profit there? The taxpayer builds up a tax-deferred pool of working capital.
- *Countermeasures: Foreign Base Company Sales Income, Foreign Base Company Services Income, IRC §956 (technically not subpart F income).*

3. All of the Types of Subpart F Income

The five types of subpart F income

- Play games with captive insurance companies - IRC §§952(a)(1), 953
- Foreign Base Company Income - IRC §§952(a)(2), 954
- Participate in boycotts - IRC §§952(a)(3), 999
- Violate the Foreign Corrupt Practices Act - IRC §952(a)(4)
- Do business in enemy countries - IRC §952(a)(5)

Sloppy language is a tell — that's what the government cares about

- Play games with captive insurance companies - IRC §§952(a)(1), 953
- **Foreign Base Company Income** - IRC §§952(a)(2), 954
- Participate in boycotts - IRC §§952(a)(3), 999
- Violate the Foreign Corrupt Practices Act - IRC §952(a)(4)
- Do business in enemy countries - IRC §952(a)(5)

Closely related but technically not subpart F income

- **IRC §956.** When a CFC invests its undistributed earnings and profits in U.S. assets, creates gross income for the U.S. shareholder. Included in gross income of the shareholder by IRC §951(a)(1)(B).
- **IRC §965(a).** The transition tax. “Deferred foreign income” of a “specified foreign corporation” is included in the shareholder’s subpart F income, so it’s like a one-time stealth addition to the definition of subpart F income in IRC §952(a). Subpart F income is included in gross income of the shareholder by IRC §951(a)(1)(A).

Form 5471, Schedule I - where subpart F income happens

Schedule I Summary of Shareholder's Income From Foreign Corporation (see instructions)

If item H on page 1 is completed, a separate Schedule I must be filed for each Category 4, 5a, or 5b filer for whom reporting is furnished on this Form 5471. This Schedule I is being completed for:

Name of U.S. shareholder	Identifying number
1a Section 964(e)(4) subpart F dividend income from the sale of stock of a lower-tier foreign corporation (see instructions)	1a
b Section 245A(e)(2) subpart F income from hybrid dividends of tiered corporations (see instructions)	1b
c Subpart F income from tiered extraordinary disposition amounts not eligible for subpart F exception under section 954(c)(6)	1c
d Subpart F income from tiered extraordinary reduction amounts not eligible for subpart F exception under section 954(c)(6)	1d
e Section 954(c) Subpart F Foreign Personal Holding Company Income (enter result from Worksheet A)	1e
f Section 954(d) Subpart F Foreign Base Company Sales Income (enter result from Worksheet A)	1f
g Section 954(e) Subpart F Foreign Base Company Services Income (enter result from Worksheet A)	1g
h Other subpart F income (enter result from Worksheet A)	1h
2 Earnings invested in U.S. property (enter the result from Worksheet B)	2
3 Reserved for future use	3
4 Factoring income	4
See instructions for reporting amounts on lines 1, 2, and 4 on your income tax return.	
5a Section 245A eligible dividends (see instructions)	5a
b Extraordinary disposition amounts (see instructions)	5b
c Extraordinary reduction amounts (see instructions)	5c
d Section 245A(e) dividends (see instructions).	5d
e Dividends not reported on line 5a, 5b, 5c, or 5d	5e
6 Exchange gain or (loss) on a distribution of previously taxed earnings and profits	6

Foreign Base Company Income - three types

1. Insurance income - IRC §§952(a)(1), 953
2. Foreign Base Company Income - IRC §§952(a)(2), 954
 - 2.1. Foreign Personal Holding Company Income - IRC §954(c)
 - 2.2. Foreign Base Company Sales Income - IRC §954(d)
 - 2.3. Foreign Base Company Services Income - IRC §954(e)
3. Participate in boycotts - IRC §952(a)(3)
4. Violate the Foreign Corrupt Practices Act - IRC §952(a)(4)
5. Do business in enemy countries - IRC §952(a)(5)

Foreign Personal Holding Company Income - eight types

1. Insurance income - IRC §§952(a)(1), 953
2. Foreign Base Company Income - IRC §§952(a)(2), 954
 - 2.1. Foreign Personal Holding Company Income - IRC §954(c)
 - 2.1.1. Dividends, Interest, Rents, Royalties, and Annuities - IRC §954(c)(1)(A)
 - 2.1.2. Gains from Certain Property Transactions - IRC §954(c)(1)(B)
 - 2.1.3. Commodities Transactions - IRC §954(c)(1)(C)
 - 2.1.4. Foreign Currency Gains - IRC §954(c)(1)(D)
 - 2.1.5. Income Equivalent to Interest - IRC §954(c)(1)(E)
 - 2.1.6. Income from Notional Principal Contracts - IRC §954(c)(1)(F)
 - 2.1.7. Payments in lieu of dividends - IRC §954(c)(1)(G)
 - 2.1.8. Income from personal service contracts - IRC §954(c)(1)(H)
 - 2.2. Foreign Base Company Sales Income - IRC §954(d)
 - 2.3. Foreign Base Company Services Income - IRC §954(e)
3. Participate in boycotts - IRC §952(a)(3)
4. Violate the Foreign Corrupt Practices Act - IRC §952(a)(4)
5. Do business in enemy countries - IRC §952(a)(5)

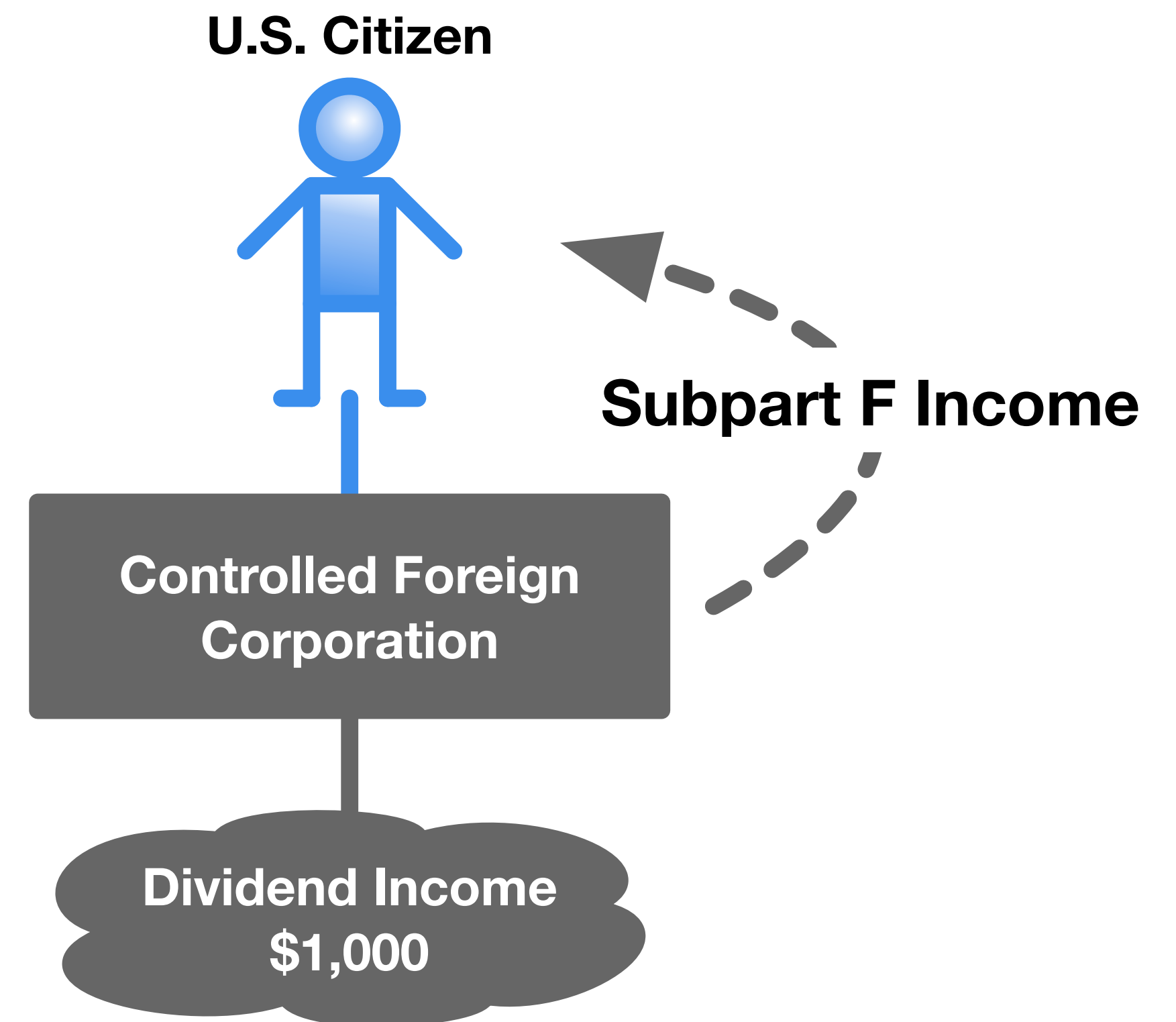
I will use dividend income to demonstrate how subpart F income works

1. Insurance income - IRC §§952(a)(1), 953
2. Foreign Base Company Income - IRC §§952(a)(2), 954
 - 2.1. Foreign Personal Holding Company Income - IRC §954(c)
 - 2.1.1. Dividends, Interest, Rents, Royalties, and Annuities - IRC §954(c)(1)(A)**
 - 2.1.2. Gains from Certain Property Transactions - IRC §954(c)(1)(B)
 - 2.1.3. Commodities Transactions - IRC §954(c)(1)(C)
 - 2.1.4. Foreign Currency Gains - IRC §954(c)(1)(D)
 - 2.1.5. Income Equivalent to Interest - IRC §954(c)(1)(E)
 - 2.1.6. Income from Notional Principal Contracts - IRC §954(c)(1)(F)
 - 2.1.7. Payments in lieu of dividends - IRC §954(c)(1)(G)
 - 2.1.8. Income from personal service contracts - IRC §954(c)(1)(H)
 - 2.2. Foreign Base Company Sales Income - IRC §954(d)
 - 2.3. Foreign Base Company Services Income - IRC §954(e)
3. Participate in boycotts - IRC §952(a)(3)
4. Violate the Foreign Corrupt Practices Act - IRC §952(a)(4)
5. Do business in enemy countries - IRC §952(a)(5)

4. “How it Works” for Subpart F Income, Using a (Very) Simple Example

A demonstration of subpart F income using a (very) simple example

- A U.S. citizen owns 100% of the stock of a foreign corporation.
- The foreign corporation receives \$1,000 of dividend income.
- The foreign corporation pays no tax and has no expenses. It does not pay a dividend to the shareholder.
- Here's what happens on the U.S. citizen shareholder's Form 1040.



Welcome to Worksheet A

Worksheet A

Summary of U.S. Shareholder's Pro Rata Share of Subpart F Income of a CFC (See the Worksheet A instructions, later.) Enter the amounts on lines 1a through 62, 64, 66, and 68 in functional currency.		
1 Gross foreign personal holding company income:		
a Dividends, interest, royalties, rents, and annuities (section 954(c)(1)(A) (excluding amounts described in sections 954(c)(2), (3), and (6))	1a	
b Excess of gains over losses from certain property transactions (section 954(c)(1)(B))	1b	
c Excess of gains over losses from commodity transactions (section 954(c)(1)(C))	1c	
d Excess of foreign currency gains over foreign currency losses (section 954(c)(1)(D))	1d	
e Income equivalent to interest (section 954(c)(1)(E))	1e	
f Net income from a notional principal contract (section 954(c)(1)(F))	1f	
g Payments in lieu of dividends (section 954(c)(1)(G))	1g	
h Certain amounts received for services under personal service contracts (see section 954(c)(1)(H))	1h	
i Certain amounts from sales of partnership interests to which the look-through rule of section 954(c)(4) applies	1i	
2 Gross foreign personal holding company income. Add lines 1a through 1i.		2
3 Gross foreign base company sales income (see section 954(d))		3
4 Gross foreign base company services income (see section 954(e))		4
5 Gross foreign base company income. Add lines 2 through 4		5
6 Gross insurance income (see sections 953 and 954(b)(3)(C) and the instructions for lines 18 and 19)		6
7 Gross foreign base company income and gross insurance income. Add lines 5 and 6		7
8 Enter 5% of total gross income (as computed for income tax purposes)		8
9 Enter 70% of total gross income (as computed for income tax purposes)		9
10 If line 7 is less than line 8 and less than \$1 million, enter -0- on this line and skip lines 11 through 19		10
11 If line 7 is more than line 9, enter total gross income (as computed for income tax purposes)		11
12 Total adjusted gross foreign base company income and insurance income (enter the greater of line 7 or line 11)		12
13 Adjusted net foreign personal holding company income:		
a Enter amount from line 2	13a	
b Expenses directly related to amount on line 2	13b	
c Subtract line 13b from line 13a	13c	
d Related person interest expense (see section 954(b)(5))	13d	
e Other expenses allocated and apportioned to the amount on line 2 under section 954(b)(5)	13e	
f Net foreign personal holding company income. Subtract the sum of lines 13d and 13e from line 13c	13f	
g Net foreign personal holding company income excluded under high-tax exception	13g	
h Subtract line 13g from line 13f		13h
14 Adjusted net foreign base company sales income:		
a Enter amount from line 3	14a	
b Expenses allocated and apportioned to the amount on line 3 under section 954(b)(5)	14b	
c Net foreign base company sales income. Subtract line 14b from line 14a	14c	
d Net foreign base company sales income excluded under high-tax exception	14d	
e Subtract line 14d from line 14c		14e
15 Adjusted net foreign base company services income:		
a Enter amount from line 4	15a	
b Expenses allocated and apportioned to line 4 under section 954(b)(5)	15b	
c Net foreign base company services income. Subtract line 15b from line 15a	15c	
d Net foreign base company services income excluded under high-tax exception	15d	
e Subtract line 15d from line 15c		15e
16 Adjusted net full inclusion foreign base company income:		
a Enter the excess, if any, of line 11 over line 7	16a	
b Expenses allocated and apportioned under section 954(b)(5)	16b	
c Net full inclusion foreign base company income. Subtract line 16b from line 16a	16c	
d Net full inclusion foreign base company income excluded under high-tax exception	16d	
e Subtract line 16d from line 16c		16e

Worksheet A

Worksheet A (continued) (See instructions.)		
17 Adjusted net foreign base company income. Add lines 13h, 14e, 15e, and 16e		17
18 Adjusted net insurance income (other than related person insurance income):		
a Enter amount from line 6 (other than related person insurance income)	18a	
b Expenses allocated and apportioned to the amount on line 18a under section 953	18b	
c Net insurance income. Subtract line 18b from line 18a	18c	
d Net insurance income excluded under high-tax exception	18d	
e Subtract line 18d from line 18c		18e
19 Adjusted net related person insurance income:		
a Enter amount from line 6 that is related person insurance income	19a	
b Expenses allocated and apportioned to the amount on line 19a under section 953	19b	
c Net related person insurance income. Subtract line 19b from line 19a	19c	
d Net related person insurance income excluded under high-tax exception	19d	
e Subtract line 19d from line 19c		19e
20 International boycott income (section 952(a)(3))		20
21 Illegal bribes, kickbacks, and other payments (section 952(a)(4))		21
22 Income described in section 952(a)(5) (see instructions)		22
23 Subpart F income before application of sections 952(b) and (c) and section 959(b). Add lines 17, 18e, 19e, and 20 through 22		23
24 Enter the portion of line 13h that is U.S. source income effectively connected with a U.S. trade or business (section 952(b))	24	
25 Exclusions under section 959(b) that apply to line 13h amount	25	
26 Section 954(c) subpart F Foreign Personal Holding Company Income. Subtract the sum of lines 24 and 25 from line 13h		26
27 Enter the portion of line 14e that is U.S. source income effectively connected with a U.S. trade or business (section 952(b))	27	
28 Exclusions under section 959(b) that apply to line 14e amount	28	
29 Section 954(d) subpart F Foreign Base Company Sales Income. Subtract the sum of lines 27 and 28 from line 14e		29
30 Enter the portion of line 15e that is U.S. source income effectively connected with a U.S. trade or business (section 952(b))	30	
31 Exclusions under section 959(b) that apply to line 15e amount	31	
32 Section 954(e) subpart F Foreign Base Company Services Income. Subtract the sum of lines 30 and 31 from line 15e		32
33 Enter the sum of the portion of lines 16e, 18e, 19e, 20, 21, and 22 that is U.S. source income effectively connected with a U.S. trade or business (section 952(b))	33	
34 Exclusions under section 959(b) that apply to line 16e, 18e, 19e, 20, 21, and 22 amounts	34	
35 Other subpart F income. Subtract the sum of lines 33 and 34 from the sum of lines 16e, 18e, 19e, 20, 21, and 22		35
36 Total subpart F income. Add lines 26, 29, 32, and 35		36
37 Current E&P limitation computation:		
a Current E&P	37a	
b Tested loss (enter as a positive number—see instructions)	37b	
c Total of line 37a and line 37b	37c	
38 Enter the smaller of line 36 or line 37c		38

Worksheet A

Worksheet A (continued) (See instructions.)		
39 If the amount on line 37c is less than the amount on line 36, allocate the subpart F income remaining (after having been limited) to lines 40, 41, 42, and 43 below in the manner prescribed by Regulations section 1.952-1(e). If the amount on line 37c is greater than or equal to the amount on line 36, enter the amount from line 26 onto line 40, enter the amount from line 29 onto line 41, enter the amount from line 32 onto line 42, and enter the amount from line 35 onto line 43.		
40 Section 954(c) subpart F Foreign Personal Holding Company Income subtotal		40
41 Section 954(d) subpart F Foreign Base Company Sales Income subtotal		41
42 Section 954(e) subpart F Foreign Base Company Services Income subtotal		42
43 Other subpart F income subtotal		43
44 Shareholder's pro rata share of line 40	44	
45 Shareholder's pro rata share of export trade income that applies to line 44 amount (see section 970(a))	45	
46 Section 954(c) subpart F Foreign Personal Holding Company Income subtotal. Subtract line 45 from line 44		46
47 Shareholder's pro rata share of line 41	47	
48 Shareholder's pro rata share of export trade income that applies to line 47 amount (see section 970(a))	48	
49 Section 954(d) subpart F Foreign Base Company Sales Income subtotal. Subtract line 48 from line 47		49
50 Shareholder's pro rata share of line 42	50	
51 Shareholder's pro rata share of export trade income that applies to line 50 amount (see section 970(a))	51	
52 Section 954(e) subpart F Foreign Base Company Services Income subtotal. Subtract line 51 from line 50		52
53 Shareholder's pro rata share of line 43	53	
54 Shareholder's pro rata share of export trade income that applies to line 53 amount (see section 970(a))	54	
55 Other subpart F income subtotal. Subtract line 54 from line 53		55
56 Add lines 46, 49, 52, and 55		56
57 Divide the number of days in the tax year that the corporation was a CFC by the number of days in the tax year and multiply the result by line 56	57	
58 Dividends paid to any other person with respect to your stock during the tax year	58	
59 Divide the number of days in the tax year you did not own such stock by the number of days in the tax year and multiply the result by line 56	59	
60 Enter the smaller of line 58 or line 59	60	
61 Shareholder's pro rata share of subpart F income. Subtract line 60 from line 57		61
62 Amount of line 61 that applies to section 954(c) subpart F Foreign Personal Holding Company Income		62
63 Translate the amount on line 62 from functional currency to U.S. dollars at the average exchange rate. See section 989(b). Enter the result here and on Form 5471, Schedule I, line 1e		63
64 Amount of line 61 that applies to section 954(d) subpart F Foreign Base Company Sales Income		64
65 Translate the amount on line 64 from functional currency to U.S. dollars at the average exchange rate. See section 989(b). Enter the result here and on Form 5471, Schedule I, line 1f		65
66 Amount of line 61 that applies to section 954(e) subpart F Foreign Base Company Services Income		66
67 Translate the amount on line 66 from functional currency to U.S. dollars at the average exchange rate. See section 989(b). Enter the result here and on Form 5471, Schedule I, line 1g		67
68 Amount of line 61 that applies to other subpart F income		68
69 Translate the amount on line 68 from functional currency to U.S. dollars at the average exchange rate. See section 989(b). Enter the result here and on Form 5471, Schedule I, line 1h		69

Lines 1, 2: dividend income is foreign personal holding company income

Summary of U.S. Shareholder's Pro Rata Share of Subpart F Income of a CFC (See the Worksheet A instructions, later.) Enter the amounts on lines 1a through 62, 64, 66, and 68 in functional currency.

1	Gross foreign personal holding company income:		
a	Dividends , interest, royalties, rents, and annuities (section 954(c)(1)(A) (excluding amounts described in sections 954(c)(2), (3), and (6))	1a	1,000
b	Excess of gains over losses from certain property transactions (section 954(c)(1)(B))	1b	
c	Excess of gains over losses from commodity transactions (section 954(c)(1)(C))	1c	
d	Excess of foreign currency gains over foreign currency losses (section 954(c)(1)(D))	1d	
e	Income equivalent to interest (section 954(c)(1)(E))	1e	
f	Net income from a notional principal contract (section 954(c)(1)(F))	1f	
g	Payments in lieu of dividends (section 954(c)(1)(G))	1g	
h	Certain amounts received for services under personal service contracts (see section 954(c)(1)(H))	1h	
i	Certain amounts from sales of partnership interests to which the look-through rule of section 954(c)(4) applies	1i	
2	Gross foreign personal holding company income. Add lines 1a through 1i.	2	1,000

Lines 3-12: the “de minimis” and “full inclusion” exceptions

3	Gross foreign base company sales income (see section 954(d))	3	
4	Gross foreign base company services income (see section 954(e))	4	
5	Gross foreign base company income. Add lines 2 through 4	5	1,000
6	Gross insurance income (see sections 953 and 954(b)(3)(C) and the instructions for lines 18 and 19)	6	
7	Gross foreign base company income and gross insurance income. Add lines 5 and 6	7	1,000
8	Enter 5% of total gross income (as computed for income tax purposes)	8	50
9	Enter 70% of total gross income (as computed for income tax purposes)	9	700
10	If line 7 is less than line 8 and less than \$1 million, enter -0- on this line and skip lines 11 through 19	10	0
11	If line 7 is more than line 9, enter total gross income (as computed for income tax purposes)	11	1,000
12	Total adjusted gross foreign base company income and insurance income (enter the greater of line 7 or line 11)	12	1,000

Line 13a-13h: from gross FPHCI to net FPHCI

13 Adjusted net foreign personal holding company income:

- a Enter amount from line 2
- b Expenses directly related to amount on line 2
- c Subtract line 13b from line 13a
- d Related person interest expense (see section 954(b)(5))
- e Other expenses allocated and apportioned to the amount on line 2 under section 954(b)(5)
- f Net foreign personal holding company income. Subtract the sum of lines 13d and 13e from line 13c
- g Net foreign personal holding company income excluded under high-tax exception
- h Subtract line 13g from line 13f

13a	1,000	
13b		
13c		
13d		
13e		
13f		
13g		
13h	1,000	

Lines 17-23: total up all five types of subpart F income

Worksheet A (continued) (See instructions.)

17	Adjusted net foreign base company income. Add lines 13h, 14e, 15e, and 16e	17	1,000
18	Adjusted net insurance income (other than related person insurance income):		
a	Enter amount from line 6 (other than related person insurance income)	18a	
b	Expenses allocated and apportioned to the amount on line 18a under section 953	18b	
c	Net insurance income. Subtract line 18b from line 18a	18c	
d	Net insurance income excluded under high-tax exception	18d	
e	Subtract line 18d from line 18c	18e	
19	Adjusted net related person insurance income:		
a	Enter amount from line 6 that is related person insurance income	19a	
b	Expenses allocated and apportioned to the amount on line 19a under section 953	19b	
c	Net related person insurance income. Subtract line 19b from line 19a	19c	
d	Net related person insurance income excluded under high-tax exception	19d	
e	Subtract line 19d from line 19c	19e	
20	International boycott income (section 952(a)(3))	20	
21	Illegal bribes, kickbacks, and other payments (section 952(a)(4))	21	
22	Income described in section 952(a)(5) (see instructions)	22	
23	Subpart F income before application of sections 952(b) and (c) and section 959(b). Add lines 17, 18e, 19e, and 20 through 22	23	1,000

Line 24: the IRC §954(b) exception for effectively connected FPHCI

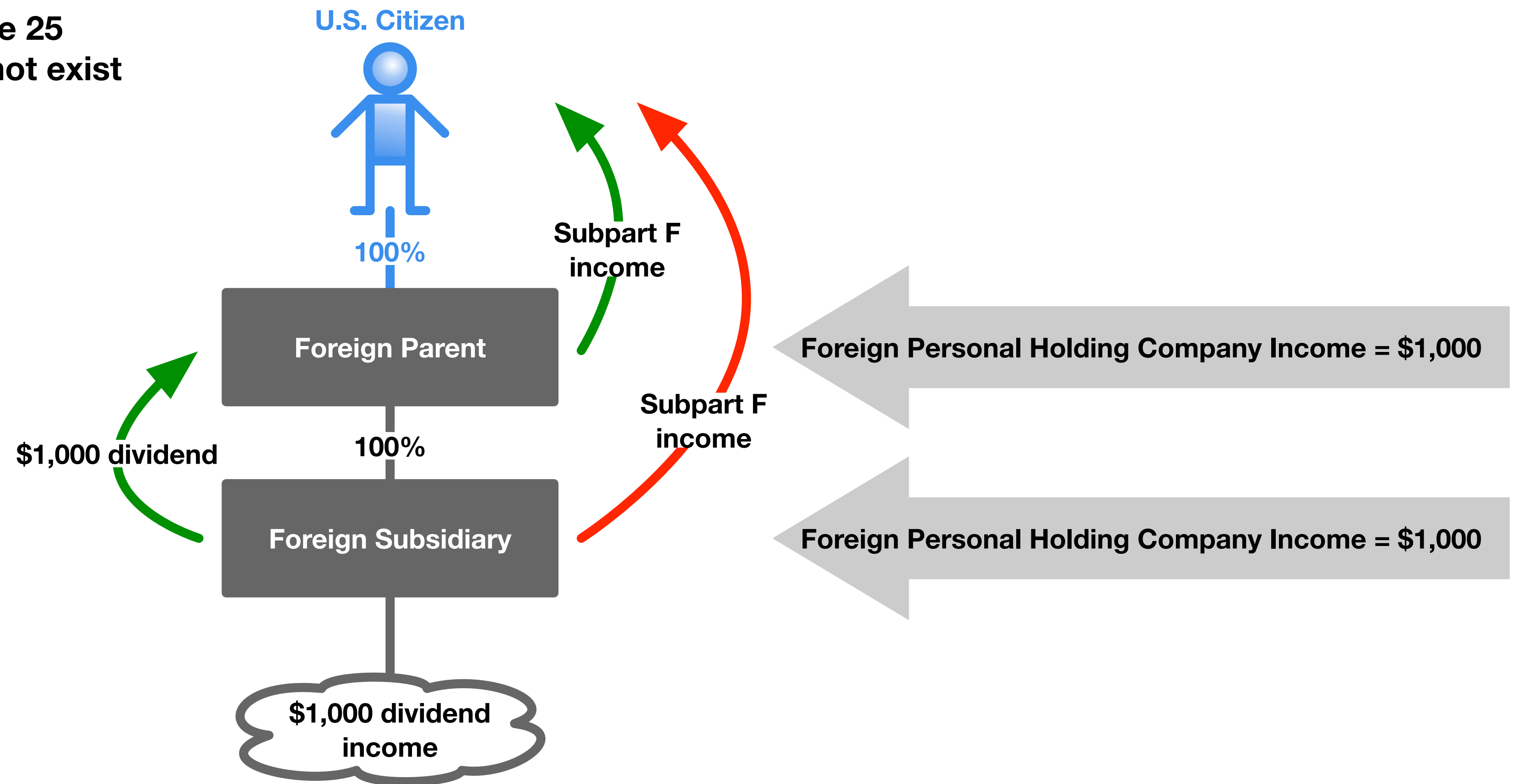
24	Enter the portion of line 13h that is U.S. source income effectively connected with a U.S. trade or business (section 952(b))	24		
25	Exclusions under section 959(b) that apply to line 13h amount	25		
26	Section 954(c) subpart F Foreign Personal Holding Company Income. Subtract the sum of lines 24 and 25 from line 13h	26		1,000

Line 25: IRC §959(b): exclude dividends from subsidiary to parent

24	Enter the portion of line 13h that is U.S. source income effectively connected with a U.S. trade or business (section 952(b))	24		
25	Exclusions under section 959(b) that apply to line 13h amount	25		
26	Section 954(c) subpart F Foreign Personal Holding Company Income. Subtract the sum of lines 24 and 25 from line 13h	26		1,000

If IRC §959(b) exclusion did not exist

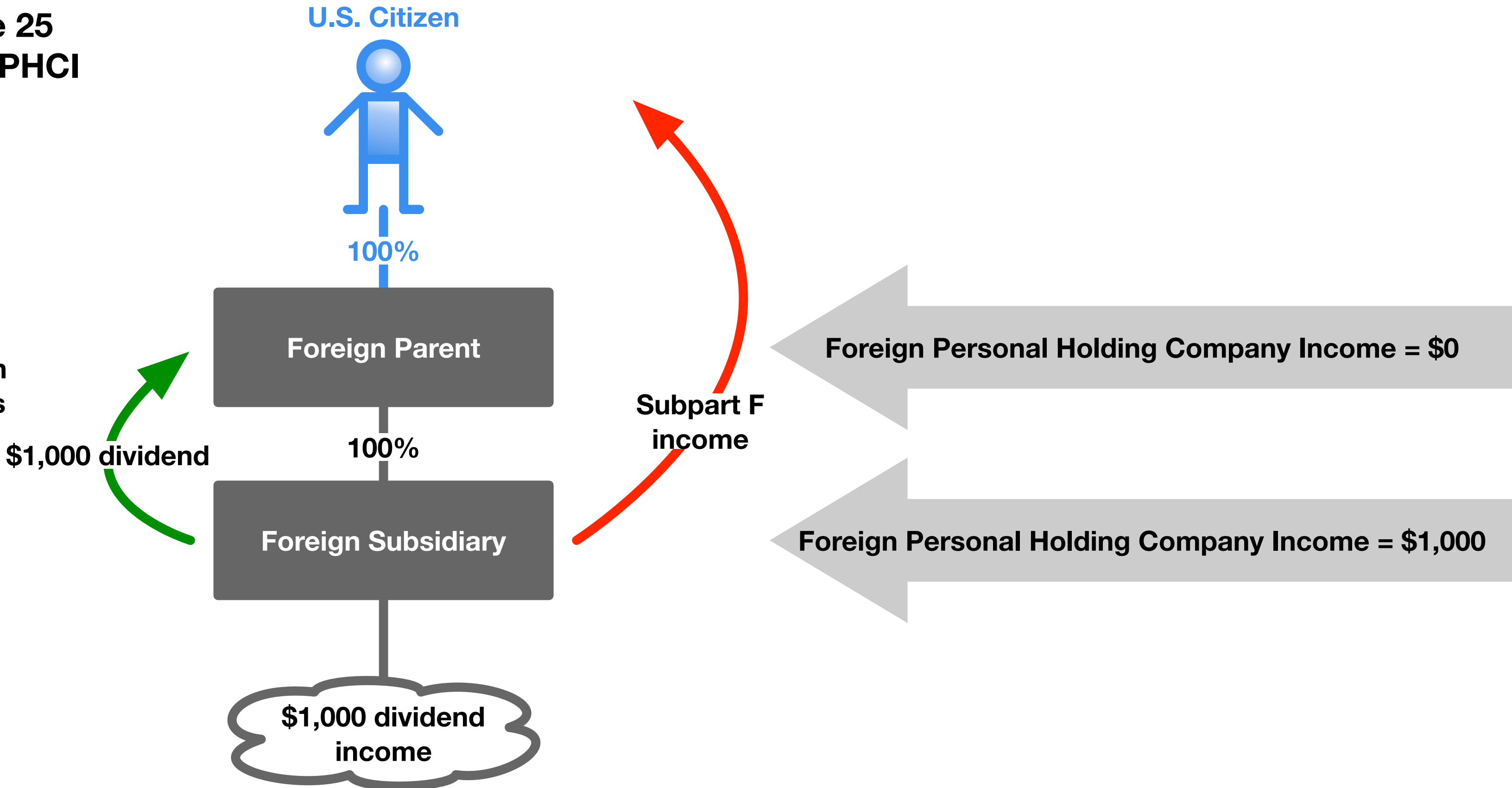
Form 5471, Worksheet A, Line 25
If the IRC §959(b) exclusion did not exist



The IRC §959(b) exception prevents double-counting subpart F income

Form 5471, Worksheet A, Line 25
Eliminate double-inclusion of FPHCI

Exclude the dividend from from Foreign Parent's FPHCI - IRC §959(b). Enter this amount on Line 25



Line 26: FPHCI as computed per IRC §954(c): all special rules applied

24	Enter the portion of line 13h that is U.S. source income effectively connected with a U.S. trade or business (section 952(b))	24			
25	Exclusions under section 959(b) that apply to line 13h amount	25			
26	Section 954(c) subpart F Foreign Personal Holding Company Income. Subtract the sum of lines 24 and 25 from line 13h		26	1,000	

Lines 26-38: apply the current E & P limitation of IRC §952(c)(1)(A)

36	Total subpart F income. Add lines 26, 29, 32, and 35		36	1,000
37	Current E&P limitation computation:			
a	Current E&P	37a		1,000
b	Tested loss (enter as a positive number—see instructions)	37b		
c	Total of line 37a and line 37b	37c		1,000
38	Enter the smaller of line 36 or line 37c		38	1,000

Lines 39-43: application of the E & P limitation; total all subpart F income

Worksheet A (continued) (See instructions.)

39 If the amount on line 37c is less than the amount on line 36, allocate the subpart F income remaining (after having been limited) to lines 40, 41, 42, and 43 below in the manner prescribed by Regulations section 1.952-1(e). **If the amount on line 37c is greater than or equal to the amount on line 36**, enter the amount from **line 26 onto line 40**, enter the amount from line 29 onto line 41, enter the amount from line 32 onto line 42, and enter the amount from line 35 onto line 43.

40	Section 954(c) subpart F Foreign Personal Holding Company Income subtotal	40	1,000
41	Section 954(d) subpart F Foreign Base Company Sales Income subtotal	41	
42	Section 954(e) subpart F Foreign Base Company Services Income subtotal	42	
43	Other subpart F income subtotal	43	Controlled Foreign Corporation

Lines 44-63: Shareholder's subpart F income to go to Schedule I

44	Shareholder's pro rata share of line 40	44	1,000		Shareholder
45	Shareholder's pro rata share of export trade income that applies to line 44 amount (see section 970(a))	45			
46	Section 954(c) subpart F Foreign Personal Holding Company Income subtotal. Subtract line 45 from line 44			46	1,000
47	Shareholder's pro rata share of line 41	47			
48	Shareholder's pro rata share of export trade income that applies to line 47 amount (see section 970(a))	48			
49	Section 954(d) subpart F Foreign Base Company Sales Income subtotal. Subtract line 48 from line 47			49	
50	Shareholder's pro rata share of line 42	50			
51	Shareholder's pro rata share of export trade income that applies to line 50 amount (see section 970(a))	51			
52	Section 954(e) subpart F Foreign Base Company Services Income subtotal. Subtract line 51 from line 50			52	
53	Shareholder's pro rata share of line 43	53			
54	Shareholder's pro rata share of export trade income that applies to line 53 amount (see section 970(a))	54			
55	Other subpart F income subtotal. Subtract line 54 from line 53			55	
56	Add lines 46, 49, 52, and 55			56	1,000
57	Divide the number of days in the tax year that the corporation was a CFC by the number of days in the tax year and multiply the result by line 56	57	1,000		
58	Dividends paid to any other person with respect to your stock during the tax year	58			
59	Divide the number of days in the tax year you did not own such stock by the number of days in the tax year and multiply the result by line 56	59			
60	Enter the smaller of line 58 or line 59	60			
61	Shareholder's pro rata share of subpart F income. Subtract line 60 from line 57			61	1,000
62	Amount of line 61 that applies to section 954(c) subpart F Foreign Personal Holding Company Income			62	1,000
63	Translate the amount on line 62 from functional currency to U.S. dollars at the average exchange rate. See section 989(b). Enter the result here and on Form 5471, Schedule I, line 1e			63	1,000

From Form 5471, Worksheet A to Form 5471, Schedule I

Schedule I Summary of Shareholder's Income From Foreign Corporation (see instructions)

If item H on page 1 is completed, a separate Schedule I must be filed for each Category 4, 5a, or 5b filer for whom reporting is furnished on this Form 5471. This Schedule I is being completed for:

Name of U.S. shareholder	Identifying number
1a Section 964(e)(4) subpart F dividend income from the sale of stock of a lower-tier foreign corporation (see instructions)	1a
b Section 245A(e)(2) subpart F income from hybrid dividends of tiered corporations (see instructions)	1b
c Subpart F income from tiered extraordinary disposition amounts not eligible for subpart F exception under section 954(c)(6)	1c
d Subpart F income from tiered extraordinary reduction amounts not eligible for subpart F exception under section 954(c)(6)	1d
e Section 954(c) Subpart F Foreign Personal Holding Company Income (enter result from Worksheet A)	1e 1,000
f Section 954(d) Subpart F Foreign Base Company Sales Income (enter result from Worksheet A)	1f
g Section 954(e) Subpart F Foreign Base Company Services Income (enter result from Worksheet A)	1g
h Other subpart F income (enter result from Worksheet A)	1h

From Form 5471, Schedule I to Form 1040, Schedule 1

n	Section 951(a) inclusion (see instructions)	8n	1,000	
o	Section 951A(a) inclusion (see instructions)	8o		
p	Section 461(l) excess business loss adjustment	8p		
q	Taxable distributions from an ABLE account (see instructions)	8q		
r	Scholarship and fellowship grants not reported on Form W-2	8r		
s	Nontaxable amount of Medicaid waiver payments included on Form 1040, line 1a or 1d	8s	()	
t	Pension or annuity from a nonqualified deferred compensation plan or a nongovernmental section 457 plan	8t		
u	Wages earned while incarcerated	8u		
z	Other income. List type and amount: _____	8z		
9	Total other income. Add lines 8a through 8z	9		
10	Combine lines 1 through 7 and 9. Enter here and on Form 1040, 1040-SR, or 1040-NR, line 8	10	1,000	

For Paperwork Reduction Act Notice, see your tax return instructions.

Cat. No. 71479F

Schedule 1 (Form 1040) 2022

From Form 1040, Schedule 1 to Form 1040 - included as gross income

separately, \$12,950 • Married filing jointly or Qualifying surviving spouse, \$25,900 • Head of household, \$19,400 • If you checked any box under <i>Standard Deduction</i> , see instructions.	7	Capital gain or (loss). Attach Schedule D if required. If not required, check here <input type="checkbox"/>	7	
	8	Other income from Schedule 1, line 10	8	1,000
	9	Add lines 1z, 2b, 3b, 4b, 5b, 6b, 7, and 8. This is your total income	9	
	10	Adjustments to income from Schedule 1, line 26	10	
	11	Subtract line 10 from line 9. This is your adjusted gross income	11	
	12	Standard deduction or itemized deductions (from Schedule A)	12	
	13	Qualified business income deduction from Form 8995 or Form 8995-A	13	
	14	Add lines 12 and 13	14	
	15	Subtract line 14 from line 11. If zero or less, enter -0-. This is your taxable income	15	

For Disclosure, Privacy Act, and Paperwork Reduction Act Notice, see separate instructions.

Cat. No. 11320B

Form **1040** (2022)

Conclusion: Walkthrough of Worksheet A

- Walking through each line in Worksheet A is an excellent tutorial in the Code's rules for subpart F income.
- The other types of subpart F income work in a similar fashion to what we just reviewed for foreign personal holding company income.

5. Some (Potentially) Useful Exceptions

Again, using foreign personal holding company income as an illustration of what happens generally to subpart F income. As usual, the Code is not uniform and the rules change all over the place.

Some exceptions that apply to FPHCI

- De minimis exception - IRC §954(b)(3)(A).
- Full inclusion exception - IRC §954(c)(3)(B).
- High-tax exception - IRC §954(c)(4).
- Look-through exception - IRC §954(c)(6).
- Same country exception - IRC §954(c)(3)(B).

De Minimis Exception - IRC §954(b)(3)(A)

If only a little bit of a CFC's income is Foreign Base Company Income, then none of it is Foreign Base Company Income.

De Minimis Exception - IRC §954(b)(3)(A)

- If the CFC's foreign base company income + insurance income is under \$1M and 5% or less of the CFC's gross income, then the CFC's foreign base company income is zero.
- This is mandatory. You don't get to choose whether to apply it or not. Reg. §1.954-1(b)(1)(i)(A).
- Functionally, use of this exception converts subpart F income into Global Intangible Low-Taxed Income.
- Worksheet A, line 8.

Subtract subpart F income to get Global Intangible Low-Taxed Income

- Form 5471, Schedule I-1 (Dec. 2021)

		Functional Currency	Conversion Rate	U.S. Dollars
1	Gross income (see instructions if cost of goods sold exceed gross receipts)	1		
2	Exclusions (see instructions if cost of goods sold exceed gross receipts)			
	a Effectively connected income	2a		
	b Subpart F income	2b		
	c High tax exception income per section 954(b)(4)	2c		
	d Related party dividends	2d		
	e Foreign oil and gas extraction income	2e		
3	Total exclusions (combine lines 2a through 2e)	3		
4	Gross income less total exclusions (line 1 minus line 3) (see instructions)	4		

Full Inclusion Exception - IRC §954(b)(3)(B)

If most of a CFC's income is FBCI, then all of it is.

Full inclusion exception - IRC §954(b)(3)(B)

- If 70% or more of a CFC's gross income is Foreign Base Company Income plus insurance income, then 100% of the CFC's gross income is Foreign Base Company Income.
- Mandatory, not optional. Reg. §1.954-1(b)(1)(ii).
- If you want to avoid Global Intangible Low-Taxed Income problems for the CFC, can you make the CFC's gross income be mostly Foreign Base Company Income?
- Worksheet A, line 9.

Use the de maximus exception to eliminate IRC §951A problems

- Form 5471, Schedule I-1 (Dec. 2021)

		Functional Currency	Conversion Rate	U.S. Dollars
1	Gross income (see instructions if cost of goods sold exceed gross receipts)	1		
2	Exclusions (see instructions if cost of goods sold exceed gross receipts)			
	a Effectively connected income	2a		
	b Subpart F income	2b		
	c High tax exception income per section 954(b)(4)	2c		
	d Related party dividends	2d		
	e Foreign oil and gas extraction income	2e		
3	Total exclusions (combine lines 2a through 2e)	3		
4	Gross income less total exclusions (line 1 minus line 3) (see instructions)	4		

High-tax Exception - IRC §954(b)(4)

High-tax exception - IRC §954(b)(4)

- Foreign Base Company Income and insurance income that is taxed in a foreign country at 90% of the U.S. corporate rate is excluded from subpart F income.
- $21\% \times 90\% = 18.9\%$ foreign tax rate.
- Although the Code makes the high-tax exception mandatory (“shall”) the Regulations make this elective. Reg. §1.954-1(d)(1).
- Worksheet A, line 13g.

Look-through Exception - IRC §954(c)(6)

The look-through rule - IRC §954(c)(6)

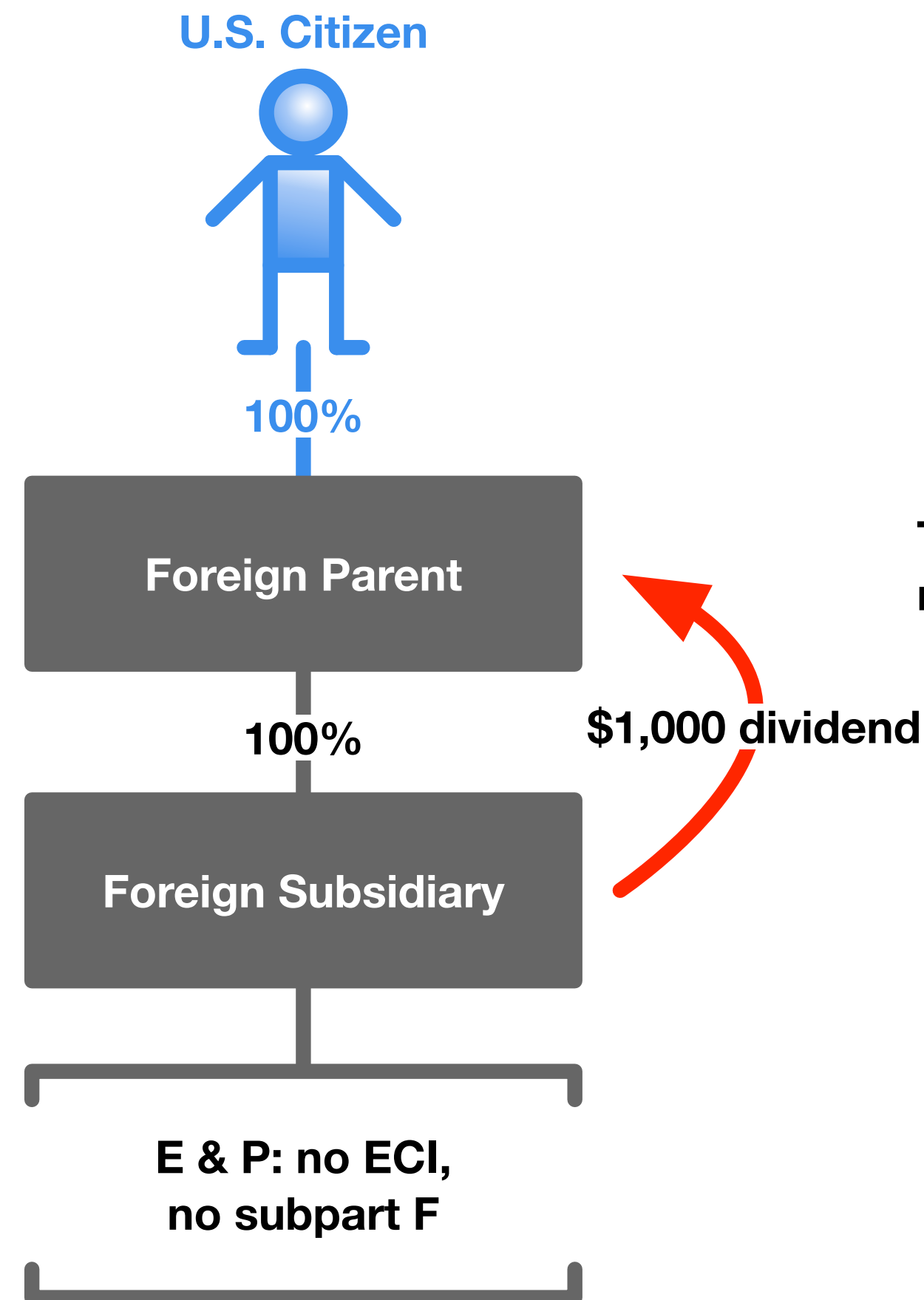
- Dividend, interest, rent, royalty paid from a CFC to a related CFC won't be classified as foreign personal holding company income to the recipient.
- The paying CFC must make the payment out of earnings and profits that are NOT subpart F and are NOT effectively connected income.
- Designed to allow U.S.-owned CFCs to move capital among related party entities without incurring tax liability for the U.S. shareholders.
- Worksheet A, line 1a.

How the look-through exception works (example: dividend)

Form 5471, Worksheet A, Line 1a The Look-Through Rule

Foreign Personal Holding Company Income = \$0

Key: the payor's earnings and profits cannot include ECI or subpart F income. Applies to dividends, interest, rent, royalties. IRC §954(c)(6). Exclude the dividend from total FPHCI entered on Worksheet A, Line 1a.



The CFCs are “related” within the meaning of IRC §954(d)(3)(A) and (B).

The Same-Country Exception - IRC §954(c)(3)

Same-country exception

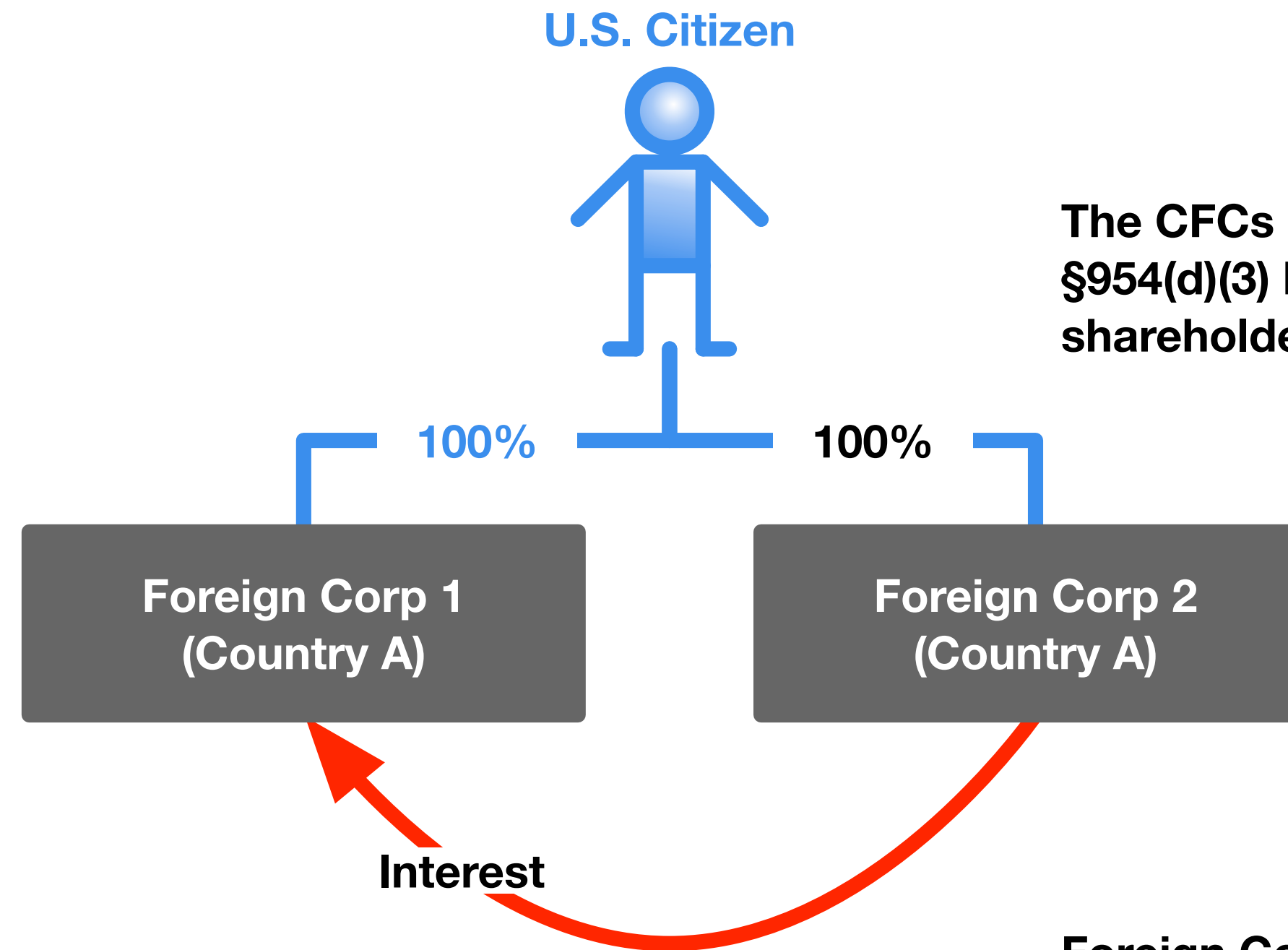
- Focus on the payor: are substantially all of its assets used in an active business in the country?
- Then look at the two CFCs— are they “related”?
- If yes, then the foreign personal holding company income received by the payee will not be included in calculations of its subpart F income.
- Worksheet A, line 1a.

How the same-country exception works: (example: interest)

Form 5471, Worksheet A, Line 1a The Same Country Exception

Foreign Personal Holding Company Income = \$0

Same-country rule: applies to dividends, interest, rents, royalties. Exclude from Foreign Parent's FPHCI - IRC §954(c)(3); exclude the interest income from total FPHCI entered on Worksheet A, Line 1a.



The CFCs are “related” as defined by IRC §954(d)(3) because they have a common shareholder that controls them both.

Foreign Corp 2 “uses a substantial part of its assets in a trade or business” in Country A. Reg. §1.954-2(b)(4)(i)(A)(3).

6. Conclusion

Conclusion

- Before IRC §951A, the mad scramble was to avoid subpart F income to achieve deferral of taxation on a CFC's earnings and profits. That is not the game anymore.
- Subpart F is still as complex as it used to be, and I barely scratched the surface here, using one of the easiest income types as a model for how income flows from a CFC to a U.S. shareholder.
- Worksheet A is your friend. Work through it methodically, line by line and you'll probably do just fine. (Reading the Code and Regulations will take you from “probably” to “definitely”).

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This is not legal advice and I am not your lawyer. Do not rely on this presentation—do your own research to verify that the information is correct and that it applies to you. Or hire someone intelligent to help you.