

[4830-01-p]

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[TD 9522]

RIN 1545-BG94

Clarification of Controlled Group Qualification Rules

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulation.

SUMMARY: This document contains a final regulation that applies to a controlled group of corporations. The regulation clarifies that a corporation that satisfies the controlled group rules for stock ownership and qualification is a member of such group, without regard to its status as a component member.

DATES: Effective Date: This regulation is effective on **[INSERT DATE OF PUBLICATION OF THIS DOCUMENT IN THE FEDERAL REGISTER]**.

Applicability Date: For date of applicability, see §1.1563-1(e).

FOR FURTHER INFORMATION CONTACT: Grid Glycer (202) 622-7930 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background and Explanation of Provisions

This document contains an amendment to 26 CFR Part 1. On September 29, 2009, a notice of proposed rulemaking (NPRM) regarding the controlled group

qualification rules under §1.1563-1 was published in the **Federal Register** (REG-135005-07; 74 FR 49829). The NPRM proposed to amend §1.1563-1 to clarify that a corporation described in section 1563(b) as an excluded member of a controlled group of corporations is nevertheless a member of the group. The NPRM further proposed to add an example demonstrating that a controlled group of corporations can consist solely of excluded members.

One comment was received and no public hearing was requested or held. The public comment concerned the treatment of gross receipts between members of a controlled group of corporations for purposes of section 41, which provides a tax credit to taxpayers for increasing their research activities. In particular, the comment refers to CCA 200233011, dated May 1, 2002. In that CCA, the IRS Office of Chief Counsel concluded first that a domestic corporation and its majority-owned foreign subsidiaries should be treated as a single taxpayer for purposes of sections 41(f)(1)(A)(i), 41(f)(5) and 1563(a) because they were members of the same controlled group of corporations even though the foreign subsidiaries were treated as excluded members of the group.

Second, the IRS Office of Chief Counsel concluded that, given the particular facts and circumstances of that case, the taxpayer should exclude sales to its majority-owned foreign subsidiaries when computing gross receipts for purposes of determining its base amount under section 41(c). The commenter requested guidance on the facts and circumstances that caused the IRS Office of Chief Counsel to exclude such sales in computing gross receipts. The IRS and the Treasury Department believe that the requested guidance is outside the scope of the NPRM, which only involves the first

issue addressed in the CCA, and is consistent with the conclusion of the CCA on that issue.

However, the final regulation makes one clarifying change. Paragraph (a)(1)(ii) of the proposed regulation states that in determining whether a corporation is included in a controlled group of corporations, section 1563(b) shall not be taken into account. Section 1563(b) defines a component member, including an excluded member and an additional member. Paragraph (a)(1)(ii) as now revised will also provide that the underlying regulation, §1.1563-1(b), which defines a component member, shall not be taken into account in determining the members of a controlled group.

Special Analyses

It has been determined that this regulation is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to this regulation and because this regulation does not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant to section 7805(f) this regulation has been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Drafting Information

The principal author of this regulation is Grid Glycer of the Office of Associate Chief Counsel (Corporate). However, other personnel from the IRS and the Treasury Department participated in its development.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 1 is amended as follows:

PART 1--INCOME TAXES

Paragraph 1. The authority citation for part 1 continues to read in part as follows:

Authority: 26 U.S.C. 7805 * * *

Par. 2. Section 1.1563-1 is amended by:

1. Redesignating paragraph (a)(1)(ii) as paragraph (a)(1)(iii) and adding new paragraph (a)(1)(ii).
2. Adding Example 4 to paragraph (b)(4).
3. Adding a sentence at the end of paragraph (e).

The additions read as follows:

§1.1563-1 Definition of controlled group of corporations and component members and related concepts.

(a) * * *

(1) * * *

(ii) Special rules. In determining whether a corporation is included in a controlled group of corporations, section 1563(b) and paragraph (b) of this section shall not be taken into account. For rules defining a component member of a controlled group of corporations, including rules defining an excluded member and an additional member,

see section 1563(b) and paragraph (b) of this section.

* * * * *

(b) * * *

(4) * * *

Example 4. Individual A owns all of the stock of corporations X, Y and Z. Each of these corporations is an S corporation. X, Y, and Z are each members of a brother-sister controlled group, even though each such corporation is treated as an excluded member of such group. See §1.1563-1(b)(2)(ii)(C).

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(e) Effective/Applicability date. * * * Paragraph (a)(1)(ii) of this section applies to taxable years beginning on or after **[INSERT DATE OF PUBLICATION OF THIS DOCUMENT IN THE FEDERAL REGISTER]**.

Steven T. Miller
Deputy Commissioner for Services and Enforcement.

Approved: April 4, 2011

Michael Mundaca
Assistant Secretary of the Treasury (Tax Policy).

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