

**MEMO# 32218**

February 19, 2020

# ICI Submits Comment Letter on Proposed Foreign Tax Credit Regulations

[32218]

February 19, 2020 TO: ICI Members

Management Company Tax Subcommittee SUBJECTS: Tax RE: ICI Submits Comment Letter on Proposed Foreign Tax Credit Regulations

ICI has submitted comments on recently [proposed regulations](#) that would, among other things, amend the definition of “financial services group” (FSG) for purposes of the foreign tax credit rules under section 904. The proposed definition is significantly more limited than the definition under current law and, if adopted, would impact the ability of some affiliated groups to use credits for foreign taxes paid on passive income against other types of income.

Under current law, a “financial services entity” (FSE) as defined in the regulations may treat certain passive income as general category income for foreign tax credit purposes, permitting these entities to offset foreign taxes paid on passive income with other types of income. The current regulations also provide that if a corporation is not an FSE under the regulations but is a member of an affiliated group that as a whole meets the definition of FSE, then such corporation also will be treated as an FSE. Thus, under this special rule, passive income of a corporation that is a member of an affiliated group that meets this definition is categorized as general category income for purposes of section 904.

The proposed regulations would amend the definitions of FSE and FSG for purposes of the foreign tax credit bucketing rules. These changes are intended to promote simplicity and consistency in the Internal Revenue Code. The proposed definition of FSG, however, is narrower than that of the proposed definition of FSE, and would limit the special rule for FSGs to only certain types of FSEs.

The proposed definition of FSE cross-references section 954(h)(2)(B) and generally provides that a taxpayer is an FSE if (i) more than 70 percent of the gross income of the individual or corporation is derived directly from the active and regular conduct of a lending or finance business from transactions with unrelated persons; (ii) it is engaged in the active conduct of a banking business and is licensed to do so in the US; or (iii) it is engaged in the active conduct of a securities business and is registered as a securities broker or dealer under section 15(a) of the Securities Exchange Act of 1934 or is registered as a Government securities broker or dealer under section 15C(a) of such Act.

The proposed definition of FSG, however, only cross-references clause (i) of section 954(h)(2)(B). Therefore, an affiliated group would qualify as an FSG under the proposed regulations only if it satisfied the lending or finance business requirement. Affiliated groups that predominantly are banks or brokers/dealers would not satisfy the proposed FSG requirement.

ICI thus recommends that the Treasury Department and the Internal Revenue Service broaden the definition of FSG to conform with that of FSE. Specifically, the definition of FSG should cross-reference all of section 954(h)(2)(B), not just the first clause. We believe that the limited FSG definition in the proposed regulations was an oversight and making this change would be consistent with the definition of FSE in the proposed regulations and elsewhere in the Internal Revenue Code.

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[Attachment](#)

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