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Proposed regulations: Passive foreign investment companies (PFICs) and PFIC insurance exception (text of regulations)

The U.S. Treasury Department and IRS today released for publication in the Federal Register proposed regulations (REG-105474-18) concerning passive foreign investment companies (PFICs) and specifically concerning legislative changes made by the 2017 U.S. tax law with regard to the "PFIC insurance exception" (described below).

Regulations were proposed in 2015 to provide guidance regarding the extent to which a foreign corporation's investment income and the assets producing that income are excluded from passive income and passive assets for purposes of the passive income and passive asset tests in section 1297(a).

Today's **proposed regulations** [PDF 515 KB] (42 pages) withdraw the regulations that were proposed in 2015, and new regulations are proposed with respect to the insurance exception as amended by the U.S. 2017 tax law.

As noted in the preamble to today's proposed regulations:

- Guidance is provided regarding the determination of ownership in a passive foreign investment company (PFIC) within the meaning of section 1297(a) and the treatment of certain income received or accrued by a foreign corporation and assets held by a foreign corporation for purposes of section 1297.

- Guidance is provided regarding when a foreign corporation is a qualifying insurance corporation (QIC) under section 1297(f) and the amounts of income and assets that a QIC excludes from passive income and assets pursuant to section 1297(b)(2)(B)—the "PFIC insurance exception"—for purposes of section 1297(a).

- The application and scope of certain rules are clarified for purposes of determining whether a United States person that directly or indirectly holds stock in a PFIC is treated as a shareholder of the PFIC, and whether a foreign corporation is a PFIC

The proposed regulations will appear in the Federal Register on July 11, 2019. Comments and requests for a public hearing must be received by a date that is 60 days after July 11, 2019.

PFIC insurance exception

The tax law enacted in December 2017 (Pub. L. No. 115-97)—the law that is at times referred to as the "Tax Cuts and Jobs Act" (TCJA)—modified an exception from passive income that prevented certain investment income derived from the active conduct of an insurance business from causing a foreign corporation to be a passive foreign investment company (PFIC). The 2017 tax law amended this exception in the PFIC rules to apply only to a foreign corporation whose applicable insurance liabilities constitute more than 25% of its total assets as reported on the corporation's applicable financial statement for the last year ending with or within the tax year.

As explained by the preamble to the proposed regulations, the 2017 tax law modified the PFIC insurance exception to provide that passive income does not include investment income derived in the active conduct of an insurance business by a QIC. Thus, for tax years beginning after December 31, 2017, the PFIC insurance exception provides that a foreign corporation's income attributable to an insurance business will not be passive income if three requirements are met.

- First, the foreign corporation must be a QIC as defined in section 1297(f).
- Second, the foreign corporation must be engaged in an "insurance business."
- Third, the income must be derived from the "active conduct" of that insurance business.

The purpose of this report is to provide text of today's proposed regulations.

Direct comments, including requests for subscriptions, to Washington National Tax. For more information, contact KPMG's Federal Tax Legislative and Regulatory Services Group at + 1 202.533.4366, 1801 K Street NW, Washington, DC 20006-1301.