

EFFECTIVE DATE OF 2010 AMENDMENT

Amendment by Pub. L. 111-147 applicable to obligations issued after the date which is 2 years after Mar. 18, 2010, see section 502(f) of Pub. L. 111-147, set out as a note under section 149 of this title.

EFFECTIVE DATE

Section applicable to taxable years ending after July 18, 1984, except as otherwise provided, see section 44 of Pub. L. 98-369, set out as a note under section 1271 of this title.

§ 1288. Treatment of original issue discount on tax-exempt obligations

(a) General rule

Original issue discount on any tax-exempt obligation shall be treated as accruing—

- (1) for purposes of section 163, in the manner provided by section 1272(a) (determined without regard to paragraph (7) thereof), and
- (2) for purposes of determining the adjusted basis of the holder, in the manner provided by section 1272(a) (determined with regard to paragraph (7) thereof).

(b) Definitions and special rules

For purposes of this section—

(1) Original issue discount

The term “original issue discount” has the meaning given to such term by section 1273(a) without regard to paragraph (3) thereof. In applying section 483 or 1274, under regulations prescribed by the Secretary, appropriate adjustments shall be made to the applicable Federal rate to take into account the tax exemption for interest on the obligation.

(2) Tax-exempt obligation

The term “tax-exempt obligation” has the meaning given to such term by section 1275(a)(3).

(3) Short-term obligations

In applying this section to obligations with maturity of 1 year or less, rules similar to the rules of section 1283(b) shall apply.

(Added Pub. L. 98-369, div. A, title I, §41(a), July 18, 1984, 98 Stat. 553; amended Pub. L. 100-647, title I, §1006(u)(3), Nov. 10, 1988, 102 Stat. 3427.)

AMENDMENTS

1988—Subsec. (a). Pub. L. 100-647 substituted “paragraph (7)” for “paragraph (6)” in pars. (1) and (2).

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by Pub. L. 100-647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99-514, to which such amendment relates, see section 1019(a) of Pub. L. 100-647, set out as a note under section 1 of this title.

EFFECTIVE DATE

Section applicable to taxable years ending after July 18, 1984, and applicable to obligations issued after Sept. 3, 1982, and acquired after Mar. 1, 1984, see section 44 of Pub. L. 98-369, set out as a note under section 1271 of this title.

PART VI—TREATMENT OF CERTAIN PASSIVE FOREIGN INVESTMENT COMPANIES

Subpart

- A. Interest on tax deferral.

Subpart

- B. Treatment of qualified electing funds.
- C. Election of mark to market for marketable stock.
- D. General provisions.

AMENDMENTS

1997—Pub. L. 105-34, title XI, §1122(d)(6), Aug. 5, 1997, 111 Stat. 977, added items for subparts C and D and struck out former item for subpart C “General provisions”.

SUBPART A—INTEREST ON TAX DEFERRAL

Sec.

- 1291. Interest on tax deferral.

§ 1291. Interest on tax deferral

(a) Treatment of distributions and stock dispositions

(1) Distributions

If a United States person receives an excess distribution in respect of stock in a passive foreign investment company, then—

- (A) the amount of the excess distribution shall be allocated ratably to each day in the taxpayer’s holding period for the stock,
- (B) with respect to such excess distribution, the taxpayer’s gross income for the current year shall include (as ordinary income) only the amounts allocated under subparagraph (A) to—
 - (i) the current year, or
 - (ii) any period in the taxpayer’s holding period before the 1st day of the 1st taxable year of the company which begins after December 31, 1986, and for which it was a passive foreign investment company, and
- (C) the tax imposed by this chapter for the current year shall be increased by the deferred tax amount (determined under subsection (c)).

(2) Dispositions

If the taxpayer disposes of stock in a passive foreign investment company, then the rules of paragraph (1) shall apply to any gain recognized on such disposition in the same manner as if such gain were an excess distribution.

(3) Definitions

For purposes of this section—

(A) Holding period

- The taxpayer’s holding period shall be determined under section 1223; except that—
 - (i) for purposes of applying this section to an excess distribution, such holding period shall be treated as ending on the date of such distribution, and
 - (ii) if section 1296 applied to such stock with respect to the taxpayer for any prior taxable year, such holding period shall be treated as beginning on the first day of the first taxable year beginning after the last taxable year for which section 1296 so applied.

(B) Current year

The term “current year” means the taxable year in which the excess distribution or disposition occurs.

(b) Excess distribution**(1) In general**

For purposes of this section, the term “excess distribution” means any distribution in respect of stock received during any taxable year to the extent such distribution does not exceed its ratable portion of the total excess distribution (if any) for such taxable year.

(2) Total excess distribution

For purposes of this subsection—

(A) In general

The term “total excess distribution” means the excess (if any) of—

(i) the amount of the distributions in respect of the stock received by the taxpayer during the taxable year, over

(ii) 125 percent of the average amount received in respect of such stock by the taxpayer during the 3 preceding taxable years (or, if shorter, the portion of the taxpayer’s holding period before the taxable year).

For purposes of clause (ii), any excess distribution received during such 3-year period shall be taken into account only to the extent it was included in gross income under subsection (a)(1)(B).

(B) No excess for 1st year

The total excess distributions with respect to any stock shall be zero for the taxable year in which the taxpayer’s holding period in such stock begins.

(3) Adjustments

Under regulations prescribed by the Secretary—

(A) determinations under this subsection shall be made on a share-by-share basis, except that shares with the same holding period may be aggregated,

(B) proper adjustments shall be made for stock splits and stock dividends,

(C) if the taxpayer does not hold the stock during the entire taxable year, distributions received during such year shall be annualized,

(D) if the taxpayer’s holding period includes periods during which the stock was held by another person, distributions received by such other person shall be taken into account as if received by the taxpayer,

(E) if the distributions are received in a foreign currency, determinations under this subsection shall be made in such currency and the amount of any excess distribution determined in such currency shall be translated into dollars,

(F) proper adjustment shall be made for amounts not includible in gross income by reason of section 959(a) or 1293(c), and

(G) if a charitable deduction was allowable under section 642(c) to a trust for any distribution of its income, proper adjustments shall be made for the deduction so allowable to the extent allocable to distributions or gain in respect of stock in a passive foreign investment company.

(c) Deferred tax amount

For purposes of this section—

(1) In general

The term “deferred tax amount” means, with respect to any distribution or disposition to which subsection (a) applies, an amount equal to the sum of—

(A) the aggregate increases in taxes described in paragraph (2), plus

(B) the aggregate amount of interest (determined in the manner provided under paragraph (3)) on such increases in tax.

Any increase in the tax imposed by this chapter for the current year under subsection (a) to the extent attributable to the amount referred to in subparagraph (B) shall be treated as interest paid under section 6601 on the due date for the current year.

(2) Aggregate increases in taxes

For purposes of paragraph (1)(A), the aggregate increases in taxes shall be determined by multiplying each amount allocated under subsection (a)(1)(A) to any taxable year (other than any taxable year referred to in subsection (a)(1)(B)) by the highest rate of tax in effect for such taxable year under section 1 or 11, whichever applies.

(3) Computation of interest**(A) In general**

The amount of interest referred to in paragraph (1)(B) on any increase determined under paragraph (2) for any taxable year shall be determined for the period—

(i) beginning on the due date for such taxable year, and

(ii) ending on the due date for the taxable year with or within which the distribution or disposition occurs,

by using the rates and method applicable under section 6621 for underpayments of tax for such period.

(B) Due date

For purposes of this subsection, the term “due date” means the date prescribed by law (determined without regard to extensions) for filing the return of the tax imposed by this chapter for the taxable year.

(d) Coordination with subparts B and C**(1) In general**

This section shall not apply with respect to any distribution paid by a passive foreign investment company, or any disposition of stock in a passive foreign investment company, if such company is a qualified electing fund with respect to the taxpayer for each of its taxable years—

(A) which begins after December 31, 1986, and for which such company is a passive foreign investment company, and

(B) which includes any portion of the taxpayer’s holding period.

Except as provided in section 1296(j), this section also shall not apply if an election under section 1296(k) is in effect for the taxpayer’s taxable year. In the case of stock which is marked to market under section 475 or any other provision of this chapter, this section shall not apply, except that rules similar to the rules of section 1296(j) shall apply.

(2) Election to recognize gain where company becomes qualified electing fund**(A) In general**

If—

(i) a passive foreign investment company becomes a qualified electing fund with respect to the taxpayer for a taxable year which begins after December 31, 1986,

(ii) the taxpayer holds stock in such company on the first day of such taxable year, and

(iii) the taxpayer establishes to the satisfaction of the Secretary the fair market value of such stock on such first day,

the taxpayer may elect to recognize gain as if he sold such stock on such first day for such fair market value.

(B) Additional election for shareholder of controlled foreign corporations**(i) In general**

If—

(I) a passive foreign investment company becomes a qualified electing fund with respect to the taxpayer for a taxable year which begins after December 31, 1986,

(II) the taxpayer holds stock in such company on the first day of such taxable year, and

(III) such company is a controlled foreign corporation (as defined in section 957(a)),

the taxpayer may elect to include in gross income as a dividend received on such first day an amount equal to the portion of the post-1986 earnings and profits of such company attributable (under regulations prescribed by the Secretary) to the stock in such company held by the taxpayer on such first day. The amount treated as a dividend under the preceding sentence shall be treated as an excess distribution and shall be allocated under subsection (a)(1)(A) only to days during periods taken into account in determining the post-1986 earnings and profits so attributable.

(ii) Post-1986 earnings and profits

For purposes of clause (i), the term “post-1986 earnings and profits” means earnings and profits which were accumulated in taxable years of such company beginning after December 31, 1986, and during the period or periods the stock was held by the taxpayer while the company was a passive foreign investment company.

(iii) Coordination with section 959(e)

For purposes of section 959(e), any amount included in gross income under this subparagraph shall be treated as included in gross income under section 1248(a).

(C) Adjustments

In the case of any stock to which subparagraph (A) or (B) applies—

(i) the adjusted basis of such stock shall be increased by the gain recognized under

subparagraph (A) or the amount treated as a dividend under subparagraph (B), as the case may be, and

(ii) the taxpayer’s holding period in such stock shall be treated as beginning on the first day referred to in such subparagraph.

(e) Certain basis, etc., rules made applicable

Except to the extent inconsistent with the regulations prescribed under subsection (f), rules similar to the rules of subsections (c) and (d) (e),¹ of section 1246 (as in effect on the day before the date of the enactment of the American Jobs Creation Act of 2004) shall apply for purposes of this section; except that—

(1) the reduction under subsection (e) of such section shall be the excess of the basis determined under section 1014 over the adjusted basis of the stock immediately before the decedent’s death, and

(2) such a reduction shall not apply in the case of a decedent who was a nonresident alien at all times during his holding period in the stock.

(f) Recognition of gain

To the extent provided in regulations, in the case of any transfer of stock in a passive foreign investment company where (but for this subsection) there is not full recognition of gain, the excess (if any) of—

- (1) the fair market value of such stock, over
- (2) its adjusted basis,

shall be treated as gain from the sale or exchange of such stock and shall be recognized notwithstanding any provision of law. Proper adjustment shall be made to the basis of any such stock for gain recognized under the preceding sentence.

(g) Coordination with foreign tax credit rules**(1) In general**

If there are creditable foreign taxes with respect to any distribution in respect of stock in a passive foreign investment company—

(A) the amount of such distribution shall be determined for purposes of this section with regard to section 78,

(B) the excess distribution taxes shall be allocated ratably to each day in the taxpayer’s holding period for the stock, and

(C) to the extent—

(i) that such excess distribution taxes are allocated to a taxable year referred to in subsection (a)(1)(B), such taxes shall be taken into account under section 901 for the current year, and

(ii) that such excess distribution taxes are allocated to any other taxable year, such taxes shall reduce (subject to the principles of section 904(d) and not below zero) the increase in tax determined under subsection (c)(2) for such taxable year by reason of such distribution (but such taxes shall not be taken into account under section 901).

(2) Definitions

For purposes of this subsection—

¹ So in original. See 2010 Amendment notes below.

(A) Creditable foreign taxes

The term “creditable foreign taxes” means, with respect to any distribution—

(i) any foreign taxes deemed paid under section 902 with respect to such distribution, and

(ii) any withholding tax imposed with respect to such distribution,

but only if the taxpayer chooses the benefits of section 901 and such taxes are creditable under section 901 (determined without regard to paragraph (1)(C)(ii)).

(B) Excess distribution taxes

The term “excess distribution taxes” means, with respect to any distribution, the portion of the creditable foreign taxes with respect to such distribution which is attributable (on a pro rata basis) to the portion of such distribution which is an excess distribution.

(C) Section 1248 gain

The rules of this subsection also shall apply in the case of any gain which but for this section would be includible in gross income as a dividend under section 1248.

(Added Pub. L. 99-514, title XII, § 1235(a), Oct. 22, 1986, 100 Stat. 2566; amended Pub. L. 100-647, title I, § 1012(p)(1), (3), (6), (7), (9), (12)–(14), (28), (31), (33), title VI, § 6127(b), Nov. 10, 1988, 102 Stat. 3515–3517, 3520, 3521, 3715; Pub. L. 105-34, title XI, § 1122(b), Aug. 5, 1997, 111 Stat. 976; Pub. L. 105-206, title VI, § 6011(c)(2), July 22, 1998, 112 Stat. 818; Pub. L. 107-16, title V, § 542(e)(5)(B), June 7, 2001, 115 Stat. 85; Pub. L. 108-357, title IV, § 413(c)(24), Oct. 22, 2004, 118 Stat. 1509; Pub. L. 111-147, title V, § 521(b), Mar. 18, 2010, 124 Stat. 112; Pub. L. 111-312, title III, § 301(a), Dec. 17, 2010, 124 Stat. 3300.)

REFERENCES IN TEXT

The date of the enactment of the American Jobs Creation Act of 2004, referred to in subsec. (e), is the date of enactment of Pub. L. 108-357, which was approved Oct. 22, 2004.

AMENDMENTS

2010—Subsec. (e). Pub. L. 111-312, which directed that subsec. (e) be amended to read as if amendment by Pub. L. 107-16, § 542(e)(5)(B), had never been enacted, was executed by inserting “(e),” after “subsections (c) and (d)” and substituting “; except that—” and pars. (1) and (2) for the period at end. See 2001 Amendment note below.

Pub. L. 111-147 substituted “and (d)” for “; (d), and (f)”.

2004—Subsec. (b)(3)(F). Pub. L. 108-357, § 413(c)(24)(A), substituted “959(a)” for “551(d), 959(a),”.

Subsec. (e). Pub. L. 108-357, § 413(c)(24)(B), inserted “(as in effect on the day before the date of the enactment of the American Jobs Creation Act of 2004)” after “section 1246” in introductory provisions.

2001—Subsec. (e). Pub. L. 107-16, § 542(e)(5)(B), struck out “(e),” after “subsections (c), (d),” and substituted period at end for “; except that—

“(1) the reduction under subsection (e) of such section shall be the excess of the basis determined under section 1014 over the adjusted basis of the stock immediately before the decedent’s death, and

“(2) such a reduction shall not apply in the case of a decedent who was a nonresident alien at all times during his holding period in the stock.”

1998—Subsec. (d)(1). Pub. L. 105-206 inserted at end “In the case of stock which is marked to market under

section 475 or any other provision of this chapter, this section shall not apply, except that rules similar to the rules of section 1296(j) shall apply.”

1997—Subsec. (a)(3)(A). Pub. L. 105-34, § 1122(b)(3), amended heading and text of subpar. (A) generally. Prior to amendment, text read as follows: “The taxpayer’s holding period shall be determined under section 1223; except that, for purposes of applying this section to an excess distribution, such holding period shall be treated as ending on the date of such distribution.”

Subsec. (d). Pub. L. 105-34, § 1122(b)(2), substituted “subparts B and C” for “subpart B” in heading.

Subsec. (d)(1). Pub. L. 105-34, § 1122(b)(1), inserted concluding provisions.

1988—Subsec. (a)(1)(B)(ii). Pub. L. 100-647, § 1012(p)(12), amended cl. (ii) generally. Prior to amendment, cl. (ii) read as follows: “any period in the taxpayer’s holding period before the 1st day of the 1st taxable year of the company for which it was a passive foreign investment company (or, if later, January 1, 1987), and”.

Subsec. (a)(3)(A). Pub. L. 100-647, § 1012(p)(14), substituted “for purposes of applying this section to” for “in the case of”.

Subsec. (a)(4), (5). Pub. L. 100-647, § 1012(p)(7)(A), struck out par. (4) which related to coordination with section 904, and par. (5) which related to section 902 not applying.

Subsec. (b)(2)(A). Pub. L. 100-647, § 1012(p)(13), inserted at end “For purposes of clause (ii), any excess distribution received during such 3-year period shall be taken into account only to the extent it was included in gross income under subsection (a)(1)(B).”

Subsec. (b)(3)(F). Pub. L. 100-647, § 1012(p)(3), added subpar. (F).

Subsec. (b)(3)(G). Pub. L. 100-647, § 1012(p)(33), added subpar. (G).

Subsec. (c)(1). Pub. L. 100-647, § 1012(p)(31), inserted at end “Any increase in the tax imposed by this chapter for the current year under subsection (a) to the extent attributable to the amount referred to in subparagraph (B) shall be treated as interest paid under section 6601 on the due date for the current year.”

Subsec. (d)(1). Pub. L. 100-647, § 6127(b)(1), inserted “with respect to the taxpayer” after “qualified electing fund”.

Pub. L. 100-647, § 1012(p)(1), amended par. (1) generally. Prior to amendment, par. (1) read as follows: “This section shall not apply with respect to—

“(A) any distribution paid by a passive foreign investment company during a taxable year for which such company is a qualified electing fund, and

“(B) any disposition of stock in a passive foreign investment company if such company is a qualified electing fund for each of its taxable years—

“(i) which begins after December 31, 1986, and for which such company is a passive foreign investment company, and

“(ii) which includes any portion of the taxpayer’s holding period.”

Subsec. (d)(2)(A)(i). Pub. L. 100-647, § 6127(b)(2), inserted “with respect to the taxpayer” after “qualified electing fund”.

Subsec. (d)(2)(B). Pub. L. 100-647, § 1012(p)(28), added subpar. (B) and struck out former subpar. (B) which related to adjustments to basis of stock to which subpar. (A) applies.

Subsec. (d)(2)(B)(i)(I). Pub. L. 100-647, § 6127(b)(2), inserted “with respect to the taxpayer” after “qualified electing fund”.

Subsec. (d)(2)(C). Pub. L. 100-647, § 1012(p)(28), added subpar. (C).

Subsec. (e). Pub. L. 100-647, § 1012(p)(6)(B), substituted “Except to the extent inconsistent with the regulations prescribed under subsection (f), rules similar”.

Subsec. (e)(2). Pub. L. 100-647, § 1012(p)(9), struck out “not” before “a nonresident”.

Subsec. (f). Pub. L. 100-647, § 1012(p)(6)(A), amended subsec. (f) generally. Prior to amendment, subsec. (f), “Nonrecognition provisions”, read as follows: “To the extent provided in regulations, gain shall be recognized

on any disposition of stock in a passive foreign investment company.”

Subsec. (g). Pub. L. 100-647, §1012(p)(7)(B), added subsec. (g).

EFFECTIVE DATE OF 2010 AMENDMENT

Amendment by Pub. L. 111-312 applicable to estates of decedents dying, and transfers made after Dec. 31, 2009, except as otherwise provided, see section 301(e) of Pub. L. 111-312, set out as an Effective and Termination Dates of 2010 Amendment note under section 121 of this title.

Pub. L. 111-147, title V, §521(c), Mar. 18, 2010, 124 Stat. 112, provided that: “The amendments made by this section [amending this section and section 1298 of this title] take effect on the date of the enactment of this Act [Mar. 18, 2010].”

EFFECTIVE DATE OF 2004 AMENDMENT

Amendment by Pub. L. 108-357 applicable to taxable years of foreign corporations beginning after Dec. 31, 2004, and to taxable years of United States shareholders with or within which such taxable years of foreign corporations end, see section 413(d)(1) of Pub. L. 108-357, set out as an Effective and Termination Dates of 2004 Amendments note under section 1 of this title.

EFFECTIVE DATE OF 2001 AMENDMENT

Amendment by Pub. L. 107-16 applicable to estates of decedents dying after Dec. 31, 2009, see section 542(f)(1) of Pub. L. 107-16, set out as a note under section 121 of this title.

EFFECTIVE DATE OF 1998 AMENDMENT

Amendment by Pub. L. 105-206 effective, except as otherwise provided, as if included in the provisions of the Taxpayer Relief Act of 1997, Pub. L. 105-34, to which such amendment relates, see section 6024 of Pub. L. 105-206, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1997 AMENDMENT

Amendment by Pub. L. 105-34 applicable to taxable years of United States persons beginning after Dec. 31, 1997, and to taxable years of foreign corporations ending with or within such taxable years of United States persons, see section 1124 of Pub. L. 105-34, set out as a note under section 532 of this title.

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by section 1012(p)(1), (3), (6), (7), (9), (12)-(14), (28), (31), (33) of Pub. L. 100-647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99-514, to which such amendment relates, see section 1019(a) of Pub. L. 100-647, set out as a note under section 1 of this title.

Amendment by section 6127(b) of Pub. L. 100-647 effective as if included in the amendments made by section 1235 of Pub. L. 99-514, see section 6127(c)(1) of Pub. L. 100-647, set out as a note under section 1295 of this title.

EFFECTIVE DATE

Pub. L. 99-514, title XII, §1235(h), Oct. 22, 1986, 100 Stat. 2576, provided that: “The amendments made by this section [enacting this section and sections 1293 to 1297 of this title and amending sections 532, 542, 551, 851, 904, 951, 1246, and 6503 of this title] shall apply to taxable years of foreign corporations beginning after December 31, 1986.”

SUBPART B—TREATMENT OF QUALIFIED ELECTING FUNDS

Sec.	
1293.	Current taxation of income from qualified electing funds.
1294.	Election to extend time for payment of tax on undistributed earnings.
1295.	Qualified electing fund.

§ 1293. Current taxation of income from qualified electing funds

(a) Inclusion

(1) In general

Every United States person who owns (or is treated under section 1298(a) as owning) stock of a qualified electing fund at any time during the taxable year of such fund shall include in gross income—

(A) as ordinary income, such shareholder's pro rata share of the ordinary earnings of such fund for such year, and

(B) as long-term capital gain, such shareholder's pro rata share of the net capital gain of such fund for such year.

(2) Year of inclusion

The inclusion under paragraph (1) shall be for the taxable year of the shareholder in which or with which the taxable year of the fund ends.

(b) Pro rata share

The pro rata share referred to in subsection (a) in the case of any shareholder is the amount which would have been distributed with respect to the shareholder's stock if, on each day during the taxable year of the fund, the fund had distributed to each shareholder a pro rata share of that day's ratable share of the fund's ordinary earnings and net capital gain for such year. To the extent provided in regulations, if the fund establishes to the satisfaction of the Secretary that it uses a shorter period than the taxable year to determine shareholders' interests in the earnings of such fund, pro rata shares may be determined by using such shorter period.

(c) Previously taxed amounts distributed tax free

If the taxpayer establishes to the satisfaction of the Secretary that any amount distributed by a passive foreign investment company is paid out of earnings and profits of the company which were included under subsection (a) in the income of any United States person, such amount shall be treated, for purposes of this chapter, as a distribution which is not a dividend; except that such distribution shall immediately reduce earnings and profits. If the passive foreign investment company is a controlled foreign corporation (as defined in section 957(a)), the preceding sentence shall not apply to any United States shareholder (as defined in section 951(b)) in such corporation, and, in applying section 959 to any such shareholder, any inclusion under this section shall be treated as an inclusion under section 951(a)(1)(A).

(d) Basis adjustments

The basis of the taxpayer's stock in a passive foreign investment company shall be—

(1) increased by any amount which is included in the income of the taxpayer under subsection (a) with respect to such stock, and

(2) decreased by any amount distributed with respect to such stock which is not includible in the income of the taxpayer by reason of subsection (c).

A similar rule shall apply also in the case of any property if by reason of holding such property the taxpayer is treated under section 1298(a) as owning stock in a qualified electing fund.