

(2) in the case of any United States person, the earnings and profits determined under paragraph (1) (when distributed, deemed distributed, or otherwise taken into account under this subtitle) shall (if necessary) be translated into dollars using the appropriate exchange rate.

**(c) Previously taxed earnings and profits**

**(1) In general**

Foreign currency gain or loss with respect to distributions of previously taxed earnings and profits (as described in section 959 or 1293(c)) attributable to movements in exchange rates between the times of deemed and actual distribution shall be recognized and treated as ordinary income or loss from the same source as the associated income inclusion.

**(2) Distributions through tiers**

The Secretary shall prescribe regulations with respect to the treatment of distributions of previously taxed earnings and profits through tiers of foreign corporations.

(Added Pub. L. 99-514, title XII, §1261(a), Oct. 22, 1986, 100 Stat. 2586; amended Pub. L. 100-647, title I, §1012(v)(1)(A), Nov. 10, 1988, 102 Stat. 3528; Pub. L. 105-34, title XI, §1102(a)(1), (b)(1), Aug. 5, 1997, 111 Stat. 963, 965; Pub. L. 108-357, title IV, §408(a), (b), Oct. 22, 2004, 118 Stat. 1499.)

**Editorial Notes**

AMENDMENTS

2004—Subsec. (a)(1)(D). Pub. L. 108-357, §408(a), added subpar. (D). Former subpar. (D) redesignated (E).

Subsec. (a)(1)(E). Pub. L. 108-357, §408(b)(1), added subpar. (E). Former subpar. (E) redesignated (F).

Pub. L. 108-357, §408(a), redesignated subpar. (D) as (E).

Subsec. (a)(1)(F). Pub. L. 108-357, §408(b)(1), redesignated subpar. (E) as (F).

Subsec. (a)(2). Pub. L. 108-357, §408(b)(2), inserted “or (E)” after “subparagraph (A)” in introductory provisions.

1997—Subsec. (a). Pub. L. 105-34, §1102(a)(1), amended subsec. (a) generally. Prior to amendment, subsec. (a) read as follows:

“(a) FOREIGN TAXES.—

“(1) IN GENERAL.—For purposes of determining the amount of the foreign tax credit—

“(A) any foreign income taxes shall be translated into dollars using the exchange rates as of the time such taxes were paid to the foreign country or possession of the United States, and

“(B) any adjustment to the amount of foreign income taxes shall be translated into dollars using—

“(i) except as provided in clause (ii), the exchange rate as of the time when such adjustment is paid to the foreign country or possession, or

“(ii) in the case of any refund or credit of foreign income taxes, using the exchange rate as of the time of original payment of such foreign income taxes.

“(2) FOREIGN INCOME TAXES.—For purposes of paragraph (1), ‘foreign income taxes’ means any income, war profits, or excess profits taxes paid to any foreign country or to any possession of the United States.”

Subsec. (a)(3), (4). Pub. L. 105-34, §1102(b)(1), added par. (3) and redesignated former par. (3) as (4).

1988—Pub. L. 100-647 substituted “foreign taxes and foreign corporation’s earnings and profits” for “foreign corporation’s earnings and profits and foreign taxes” in heading, and revised and restructured the provisions of subsecs. (a) and (b).

**Statutory Notes and Related Subsidiaries**

EFFECTIVE DATE OF 2004 AMENDMENT

Pub. L. 108-357, title IV, §408(c), Oct. 22, 2004, 118 Stat. 1500, provided that: “The amendments made by this section [amending this section] shall apply to taxable years beginning after December 31, 2004.”

EFFECTIVE DATE OF 1997 AMENDMENT

Pub. L. 105-34, title XI, §1102(c)(1), Aug. 5, 1997, 111 Stat. 966, provided that: “The amendments made by subsections (a)(1) and (b) [amending this section and section 989 of this title] shall apply to taxes paid or accrued in taxable years beginning after December 31, 1997.”

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 beginning after Dec. 31, 1986, with certain exceptions and qualifications, see section 1261(e) of Pub. L. 99-514, set out as a note under section 985 of this title.

**§ 987. Branch transactions**

In the case of any taxpayer having 1 or more qualified business units with a functional currency other than the dollar, taxable income of such taxpayer shall be determined—

(1) by computing the taxable income or loss separately for each such unit in its functional currency,

(2) by translating the income or loss separately computed under paragraph (1) at the appropriate exchange rate, and

(3) by making proper adjustments (as prescribed by the Secretary) for transfers of property between qualified business units of the taxpayer having different functional currencies, including—

(A) treating post-1986 remittances from each such unit as made on a pro rata basis out of post-1986 accumulated earnings, and

(B) treating gain or loss determined under this paragraph as ordinary income or loss, respectively, and sourcing such gain or loss by reference to the source of the income giving rise to post-1986 accumulated earnings.

(Added Pub. L. 99-514, title XII, §1261(a), Oct. 22, 1986, 100 Stat. 2586; amended Pub. L. 100-647, title I, §1012(v)(1)(B), Nov. 10, 1988, 102 Stat. 3528.)

**Editorial Notes**

AMENDMENTS

1988—Par. (4). Pub. L. 100-647 struck out par. (4) which provided for translation of foreign income taxes paid by each qualified business unit of the taxpayer in the same manner as provided under section 986(b).

**Statutory Notes and Related Subsidiaries**

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 beginning after Dec. 31, 1986, with certain exceptions and qualifications, see section 1261(e) of Pub. L. 99-514, set out as a note under section 985 of this title.

**§ 988. Treatment of certain foreign currency transactions**

**(a) General rule**

Notwithstanding any other provision of this chapter—

**(1) Treatment as ordinary income or loss**

**(A) In general**

Except as otherwise provided in this section, any foreign currency gain or loss attributable to a section 988 transaction shall be computed separately and treated as ordinary income or loss (as the case may be).

**(B) Special rule for forward contracts, etc.**

Except as provided in regulations, a taxpayer may elect to treat any foreign currency gain or loss attributable to a forward contract, a futures contract, or option described in subsection (c)(1)(B)(iii) which is a capital asset in the hands of the taxpayer and which is not a part of a straddle (within the meaning of section 1092(c), without regard to paragraph (4) thereof) as capital gain or loss (as the case may be) if the taxpayer makes such election and identifies such transaction before the close of the day on which such transaction is entered into (or such earlier time as the Secretary may prescribe).

**(2) Gain or loss treated as interest for certain purposes**

To the extent provided in regulations, any amount treated as ordinary income or loss under paragraph (1) shall be treated as interest income or expense (as the case may be).

**(3) Source**

**(A) In general**

Except as otherwise provided in regulations, in the case of any amount treated as ordinary income or loss under paragraph (1) (without regard to paragraph (1)(B)), the source of such amount shall be determined by reference to the residence of the taxpayer or the qualified business unit of the taxpayer on whose books the asset, liability, or item of income or expense is properly reflected.

**(B) Residence**

For purposes of this subpart—

**(i) In general**

The residence of any person shall be—

(I) in the case of an individual, the country in which such individual's tax home (as defined in section 911(d)(3)) is located,

(II) in the case of any corporation, partnership, trust, or estate which is a United States person (as defined in section 7701(a)(30)), the United States, and

(III) in the case of any corporation, partnership, trust, or estate which is not

a United States person, a country other than the United States.

If an individual does not have a tax home (as so defined), the residence of such individual shall be the United States if such individual is a United States citizen or a resident alien and shall be a country other than the United States if such individual is not a United States citizen or a resident alien.

**(ii) Exception**

In the case of a qualified business unit of any taxpayer (including an individual), the residence of such unit shall be the country in which the principal place of business of such qualified business unit is located.

**(iii) Special rule for partnerships**

To the extent provided in regulations, in the case of a partnership, the determination of residence shall be made at the partner level.

**(C) Special rule for certain related party loans**

Except to the extent provided in regulations, in the case of a loan by a United States person or a related person to a 10-percent owned foreign corporation which is denominated in a currency other than the dollar and bears interest at a rate at least 10 percentage points higher than the Federal mid-term rate (determined under section 1274(d)) at the time such loan is entered into, the following rules shall apply:

(i) For purposes of section 904 only, such loan shall be marked to market on an annual basis.

(ii) Any interest income earned with respect to such loan for the taxable year shall be treated as income from sources within the United States to the extent of any loss attributable to clause (i).

For purposes of this subparagraph, the term "related person" has the meaning given such term by section 954(d)(3), except that such section shall be applied by substituting "United States person" for "controlled foreign corporation" each place such term appears.

**(D) 10-percent owned foreign corporation**

The term "10-percent owned foreign corporation" means any foreign corporation in which the United States person owns directly or indirectly at least 10 percent of the voting stock.

**(b) Foreign currency gain or loss**

For purposes of this section—

**(1) Foreign currency gain**

The term "foreign currency gain" means any gain from a section 988 transaction to the extent such gain does not exceed gain realized by reason of changes in exchange rates on or after the booking date and before the payment date.

**(2) Foreign currency loss**

The term "foreign currency loss" means any loss from a section 988 transaction to the ex-