Understanding New Code Sec. 951B and When It Matters

By Brian Jenn

On July 4, 2025, President Trump signed into law the reconciliation bill known as the "One Big Beautiful Bill Act," now "popularly" known as OB3. The new legislation generally makes permanent the key features and parameters of the U.S. international tax system that was put in place in 2017 through the Tax Cuts and Jobs Act (TCJA) while also making some "clean-up" changes to certain TCJA-introduced provisions about which Congress either immediately or eventually came to have second thoughts. In one of the most significant examples of OB3 back-tracking on a TCJA provision, Congress reinstated former Code Sec. 958(b)(4), which prohibits "downward attribution" under Code Sec. 318(a)(3) constructive ownership rules of stock held by a foreign person to a U.S. person for purposes of determining controlled foreign corporation (CFC)[1] or U.S. shareholder[2] status. The repeal by TCJA of Code Sec. 958(b)(4) for tax years beginning after December 31, 2017, which had resulted in the treatment as CFCs of many foreign corporations that are not directly or indirectly owned by U.S. persons, itself is repealed by OB3 for tax years beginning after December 31, 2025.

As it happens, however, reducing comes with a price—and in this case, the price is more complexity. In particular, to address some of the policy concerns that originally motivated the repeal of downward attribution, OB3 introduces a new Code Sec. 951B, which effectively creates a parallel international tax system for "foreign-controlled U.S. shareholders" ("FCUSSs") of "foreign-controlled foreign corporations" ("FCFCs"). Confusingly, for purposes of determining status as an FCUSS or FCFC, one must ignore the newly reinstated prohibition of downward attribution under Code Sec. 958(b)(4). A particular oddity of these definitions is that even U.S. persons that do not have foreign owners may be considered FCUSSs. Fortunately, in typical fact patterns involving a U.S.-parented multinational group, FCUSS status generally should not result in additional U.S. tax liability under Code Sec. 951B. For foreign-parented groups, Code Sec. 951B would come into play in fact patterns where a foreign corporation owns stock of a U.S. corporation that directly or indirectly owns (under Code Sec. 958(a)) any stock of a foreign corporation that is majority owned by foreign members of the group.

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Although Code Sec. 951B adds little text to the Code, merely providing rules to modify the normal operation of other international tax Code provisions, tracing the effects of Code Sec. 951B on those other Code section s can be arduous. The goal of this note is to orient readers with Code Sec. 951B sufficiently to be able to understand whether Code Sec. 951B is even potentially an issue in a particular fact pattern, and how to assess what the consequences are if it is.

Determining "Foreign-Controlled U.S. Shareholder" Status

Only U.S. persons that are FCUSSs are subject to tax under Code Sec. 951B. Status as an FCUSS is determined under Code Sec. 951B by making modifications to the U.S. shareholder definition under Code Sec. 951(b). Generally, Code Sec. 951(b) provides that a U.S. shareholder means, with respect to a foreign corporation, a U.S. person that owns (within the meaning of Code Sec. 958(a)), or is considered as owning by applying the constructive ownership rules of Code Sec. 958(b), 10 percent of more of the total combined voting power or value of the foreign corporation. In determining FCUSS status, Code Sec. 951B modifies this definition by substituting "more than 50 percent" for "10 percent" and applying Code Sec. 958 without regard to the downward attribution prohibition under Code Sec. 958(b)(4). Consequently, an FCUSS means any U.S. person that has majority ownership of a foreign corporation, taking into account downward attribution as well as the other attribution rules.

As it turns out, it is actually not a definition requirement for an FCUSS to be foreign-controlled. That is, technically, any U.S. person is an FCUSS with respect to a foreign corporation if it has majority ownership of the foreign corporation, taking into account downward attribution. Additionally, there is no overlap rule providing that a U.S. shareholder of a foreign corporation cannot also be an FCUSS with respect to that foreign corporation. Consequently, it will often be the case—particularly in a multinational group—that a U.S. corporation is both a U.S. shareholder and an FCUSS with respect to the same foreign corporation. As discussed further below, however, FCUSS status generally will not have any practical effect within a U.S.-parented multinational enterprise (MNE) group, since Code Sec. 951B can only result in additional tax where the domestic corporation is an FCUSS with respect to an FCFC, a status that does not overlap with CFC status.

Determining "Foreign-Controlled Foreign Corporation" Status

Status as an FCFC is determined by reference to the definition of a CFC in Code Sec. 957. Under Code Sec. 957(a), a CFC generally means any foreign corporation if more than 50 percent of the total combined voting power or value of its stock is owned (within the meaning of Code Sec. 958(a)), or is considered as owned by applying the constructive ownership rules of Code Sec. 958(b), by U.S. shareholders any day during the tax year of the foreign corporation. In defining an FCFC, Code Sec. 951B(c) modifies the Code Sec. 957 definition of a CFC by substituting FCUSS for U.S. shareholders and applying Code Sec. 958 without regard to the downward attribution prohibition under Code Sec. 958(b)(4). Importantly, unlike the rule for defining an FCUSS, Code Sec. 951B(c) also contains an overlap rule providing that a CFC cannot also be an FCFC. Consequently, an FCFC means any foreign corporation, other than a CFC, if more than 50 percent of the combined voting power or value of its stock is owned directly, indirectly, or constructively (including by way of downward attribution) by FCUSSs.

In practice, because of the application of downward attribution rules, it will be relatively common for a non-CFC that is part of an MNE group that includes a domestic partnership or a wholly owned U.S. subsidiary to be treated as owned by the domestic partnership or U.S. subsidiary, resulting in FCFC status for the foreign corporation. Importantly, however, as discussed further below, Code Sec. 951B applies only where an FCUSS directly or indirectly owns stock in the FCFC.

How and When Code Sec. 951B Results in U.S. Tax Liability

Code Sec. 951B applies differently with respect to the parts of Subpart F other than Code Sec. 951A as it does with respect to Code Sec. 951A. Generally, the normal application of Subpart F and the application of Subpart F by reason of Code Sec. 951B apply on a side-by-side basis. That is, for a particular FCUSS with respect to an FCFC, the FCUSS must take into account its *pro rata* share of subpart F income of the FCFC if it directly or indirectly owns any stock in the FCFC. (FCFC stock only owned constructively does not result in any inclusions under Code Sec. 951B-modified Code Sec. 951(a).) The inclusion by the FCUSS under Code Sec. 951(a) with

respect to the FCFC is in addition to any inclusions the FCUSS has with respect to any CFCs with respect to which it is a U.S. shareholder, but the two regimes do not directly interact since there is no overlap in the definitions of CFC and FCFC.

Because Code Sec. 951A involves blending of attributes (tested income and tested loss) at the U.S. shareholder level, Code Sec. 951B also applies with respect to Code Sec. 951A on a blended basis. In particular, Code Sec. 951B provides that a domestic corporation that is an FCUSS with respect to an FCFC and directly or indirectly owns any stock of the FCFC under Code Sec. 958(a) must apply Code Sec. 951A by treating each reference to a U.S. shareholder in Code Sec. 951A as a reference to that domestic corporation and each reference to a CFC in Code Sec. 951A as a reference to that FCFC. Consequently, the domestic corporation takes into account its *pro rata* share of tested income and tested loss from the FCFC together with tested income and loss from any CFCs with respect to which it is a U.S. shareholder for purposes of calculating its Code Sec. 951A inclusion.

In sum, Code Sec. 951B uses a few words to create a complicated regime that in many cases achieves the same result as did the 2017 repeal of Code Sec. 958(b)(4), which is reinstated for tax years beginning after December 31, 2025. So what is gained by introducing Code Sec. 951B while reinstating Code Sec. 958(b)(4)? In at least two key fact patterns, Code Sec. 951B will result in a different outcome than Code Sec. 958(b)(4) did.

First, in the case where a foreign corporation would be a CFC as a result of downward attribution—with all of the consequences that CFC status entails—such a foreign corporation would not be a CFC under Code Sec. 951B. Although it would be an FCFC, it would not be treated as a CFC for purposes of Form 5471 and other reporting requirements, or for purposes of determining "normal" Subpart F income under certain tests (*e.g.* Code Sec. 954(c)(6) look-through rule) that depend on CFC status. Rather, its FCFC status would be relevant for determining consequences only under Code Sec. 951B-modified Subpart F. For example, Code Sec. 954(c)(6) would prevent a Code Sec. 951(a) inclusion on a dividend, interest, rental, or royalty payment from one FCFC to another FCFC.

Second, in cases where less than 50 percent of the stock of a foreign corporation is owned by related parties from whom stock of the foreign corporation can be attributed downward, Code Sec. 951B will not result in a Subpart F or GILTI inclusion from that foreign corporation. Here, it is important to recall that the definition of FCUSS requires that the domestic corporation directly, indirectly, or constructively own more than 50 percent of the stock of an FCFC in order to be an FCUSS with respect to that FCFC and thus have an inclusion by reason of Code Sec. 951B. In contrast, under Code Sec. 958(b)(4) repeal, a foreign corporation in which related parties collectively only held a 10-percent interest would be a CFC and could cause an inclusion for a related domestic corporation that owned any of the foreign corporation stock. The "more than 50 percent" threshold under Code Sec. 951B serves an important role of protecting U.S. individuals and multinational groups that hold a minority stake in a foreign corporation, for instance, as a joint venture or a portfolio investment, from having Subpart F or Code Sec. 951A inclusions with respect to that foreign corporation.

Taking all of that into account, who faces tax consequences under Code Sec. 951B? Individuals and domestic corporations that can be attributed *majority* ownership of a foreign corporation that would not be a CFC but for downward attribution will have inclusions under Code Sec. 951B, as they have since the repeal of Code Sec. 958(b)(4) as part of TCJA. For other taxpayers, reinstatement of Code Sec. 958(b)(4) will put them back in the position that they were in pre-2018 with respect to CFC and U.S. shareholder status.

ENDNOTES

[1] Code Sec. 957.

[2] Code Sec. 951(b).