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March 16, 2026

Treasury announces simplifying elections in forthcoming Proposed IRC Section 987 Regulations (Notice 2026-17)

On February 25, 2026, the Internal Revenue Service (“IRS”) and the U.S. Department of the Treasury released IRS Notice 2026-17, previewing proposed regulations under Internal Revenue Code Section 987. The Notice aims to simplify the foreign currency rules applicable to Section 987 qualified business units (“QBUs”), reduce administrative complexity, and provide more practical compliance outcomes for multinational taxpayers.

Under Section IRC Section 987, taxpayers must determine the taxable income of a QBU in its functional currency and translate that amount into U.S. dollars using the average exchange rate for the taxable year, while also accounting for transfers of property between a QBU and its owner. Final regulations issued in December 2024 under Treasury Decision 10016 established a comprehensive framework for these calculations, generally requiring the use of the foreign exchange exposure pool (“FEEP”) method.

IRS Notice 2026-17 introduces several proposed measures intended to streamline these rules and provide greater administrative flexibility.

IRC Section 987 Framework: Key Considerations

- The Notice introduces an equity and basis pool method, broadly consistent with the 1991 proposed regulations, as an alternative computational approach for taxpayers that have made a current rate election under IRC Section 987. Under this method, each item of income, gain, deduction, or loss attributable to a QBU is computed in the QBU's functional currency and translated into the owner's functional currency using the average exchange rate for the taxable year.
- Net unrecognized IRC Section 987 gain or loss is determined by comparing the equity pool, measured in the QBU's functional currency and translated at the spot exchange rate on the last day of the tax year (or termination date), with the basis pool maintained in the owner's functional currency. Adjustments may be required to reflect the impact of IRC Section 987 hedging transactions.
- Recognized IRC Section 987 gain or loss is generally determined by multiplying the owner's net unrecognized IRC Section 987 gain or loss by the remittance proportion. The remittance proportion generally equals the amount of the remittance divided by the sum of (i) the equity pool, (ii) the QBU's liabilities, and (iii) the remittance amount, each measured in the QBU's functional currency. If a taxpayer makes an annual recognition election, the remittance proportion equals one, resulting in full recognition of IRC Section 987 gain or loss for the year. The election is subject to the consistency requirements of the final regulations and is generally made by attaching a statement to a timely filed tax return, without requiring prior IRS consent. The election does not apply to QBUs owned through partnerships or S corporations, although similar approaches may qualify as reasonable methods under the regulations.
- The Notice also proposes refinements to the loss suspension rules under the final Section 987 regulations. Currently, losses may be suspended to prevent selective recognition of large currency losses. Under the proposed approach, loss suspension would apply only when (i) the remittance proportion exceeds five percent or (ii) the total amount of unrecognized or deferred IRC Section 987 losses exceeds \$5 million, thereby significantly narrowing the scope of the existing rules.

- The Notice further simplifies the recognition grouping rules that apply to the loss-to-the-extent-of-gain limitation. For domestic corporate owners, all IRC Section 987 gains and losses would generally be treated as belonging to a single recognition group, allowing suspended losses to be recognized against gains across different foreign tax credit categories. For controlled foreign corporations (“CFCs”), recognition groupings remain limited to tentative tested income, subpart F income, income described in Section 952(b), and other income.
- In addition, it clarifies the deferral rules applicable when a QBU terminates and its assets are transferred to another QBU within the same controlled group. Deferral of IRC Section 987 gain or loss would apply only where a successor deferral QBU reflects a “significant portion” of the operating assets of the terminated QBU. Under the existing regulatory framework, more than 30 percent of operating assets will constitute a significant portion in all cases, while less than 10 percent will not, with determinations between those thresholds based on the facts and circumstances.
- It expands the definition of IRC Section 987 hedging transactions. Certain hedges that do not meet U.S. GAAP hedge accounting requirements may nevertheless qualify if they are primarily entered into to manage exchange rate risk associated with an interest in the QBU that would be treated as debt or stock if the QBU were a separate corporation. For hedges entered into before April 26, 2026, transitional relief permits taxpayers to treat hedges as timely identified if they are properly designated under the regulations before that date and substantially all hedges related to the QBU for the tax year are identified as IRC Section 987 hedging transactions.

Anticipated Regulations for CFCs (Section - 5)

The Notice also outlines anticipated regulations that would allow CFCs to elect out of recognizing foreign currency gain or loss under Internal Revenue Code Section 987.

If the election is made, any previously unrecognized Section 987(3) gains or losses arising before the election would generally be recognized ratably over 120 months. The proposed framework also contemplates special rules for inbound reorganizations or liquidations involving a CFC, including the possibility of a Section 987 basis increase reflecting currency-related adjustments.

Applicability and Public Comment

Taxpayers may rely immediately on the rules described in Sections 3 and 4 of IRS Notice 2026-17, provided that the rules are applied consistently across the taxpayer's Section 987 electing group. Reliance on the proposed CFC election rules will be permitted once additional guidance is issued.

The IRS and Treasury have invited public comments by April 26, 2026, particularly with respect to the methodology for determining the proposed Section 987 basis increase and whether the rules should apply to partnerships with CFC partners.

Key Takeaways

Multinational groups should consider evaluating whether the equity and basis pool method aligns with their current compliance approach, assessing the impact of the revised loss suspension thresholds, and reviewing existing hedging arrangements in light of the expanded definition of qualifying hedges.

Organizations may also wish to monitor forthcoming guidance regarding the proposed CFC election and consider providing comments on the proposed framework. Early evaluation of these developments may help taxpayers position themselves to benefit from potential simplifications under the evolving Section 987 regulatory regime.



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