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December 22, 2015

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1111 Constitution Avenue, NW  
Washington, DC 20224

The Honorable William J. Wilkins  
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1111 Constitution Avenue, NW  
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Re: Report No. 1335 on the Operation of Section 956(d) in  
the Context of Multiple Guarantors / Pledgors in Respect  
of a Single Obligation of a U.S. Person

Dear Messrs. Mazur, Koskinen and Wilkins:

I am pleased to submit the attached report of the New York State Bar Association Tax Section. The report makes proposals regarding the treatment under section 956(d) of the Internal Revenue Code of debt obligations of a U.S. person that are supported by a guarantee or pledge of assets of multiple controlled foreign corporations ("CFCs").

Section 956(d) can be read to require each CFC that provides a guarantee or asset pledge in support of an obligation of a U.S. person to be treated as holding the entire obligation for purposes of section 956. Therefore, there is a risk under the

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The Honorable Mark Mazur  
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current rules that a United States shareholder of multiple CFCs could be required to recognize an inclusion under section 956 in an amount greater (in some cases, many times greater) than the amount of the debt obligation supported by the guarantee or asset pledge. This so-called “multiple guarantor problem” thus can give rise to taxable income far in excess of any conceivable economic benefit realized by the taxpayer.

The report recommends the promulgation of regulations under section 956 that would to address situations where multiple CFCs guarantee a single debt obligation. The report refers to these debt obligations as “section 956(d) group obligations.” We recommend that the regulations provide that the total amount taken into account on account of a section 956(d) group obligation under section 956 by a United States with respect to all of its CFCs would be no more than the amount of the obligation.

While there are several potential approaches these regulations could take, we believe the best approach is to cap the amount determined under section 956 for a United States shareholder with respect to any one CFC at:

1. The amount determined under section 956 for United States property other than section 956(d) obligations under the existing rules; plus
2. The CFC’s share of an amount determined by applying the principles of section 956 to a hypothetical combined entity consisting of all the CFCs that are treated as owning the section 956(d) group obligation.

Under the approach proposed in the report, deficits in the earnings and profits of one CFC would not be available to offset positive earnings and profits of another CFC. However, consistent with the general structure and policy of section 956 and section 959, previously taxed income of the guarantor CFCs would be utilized before a United States shareholder is required to recognize taxable income in respect of a section 956(d) group obligation. As explained in the report, we believe that this approach represents the most sensible rule we could identify that would both work well within the larger technical and policy framework of subpart F and avoid the need for what we would consider to be an unduly complex regulatory system.

At the end of the report, we have provided draft regulatory language to illustrate how such a rule might work in detail. As will become apparent from the report, this is truly an area where the “devil is in the details,” and the draft language represents our attempt to help flesh out those details in a concrete way.

The Honorable Mark Mazur  
The Honorable John Koskinen  
The Honorable William J. Wilkins  
December 22, 2015

We appreciate your consideration of our recommendations. If you have any questions or comments regarding this report, please feel free to contact us and we will be glad to discuss or assist in any way.

Respectfully submitted,

David R. Sicular  
Chair

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