NATIONAL FOREIGN TRADE COUNCIL, INC.

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April 29, 2011

U.S. Department of Treasury
1500 Pennsylvania Ave., N.W.
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In re: Comments of the National Foreign Trade Council, Inc. on "Improving Regulation and Regulatory Overview" Set Forth in the Executive Order 13563 on January 18, 2011

The National Foreign Trade Council ("NFTC") appreciates the opportunity to provide comments under Executive Order 13563 "Improving Regulation and Regulatory Review" on Treasury Regulations that should be modified expanded, streamlined or repealed. The NFTC's comments seek to promote changes to regulations which will streamline the regulatory process for all multinational enterprises.

I. The National Foreign Trade Council, Inc.

The NFTC, organized in 1914, is an association of some 300 U.S. business enterprises engaged in all aspects of international trade and investment. Our membership covers the full spectrum of industrial, commercial, financial, and service activities, and the NFTC therefore seeks to foster an environment in which U.S. companies can be dynamic and effective competitors in the international business arena. The NFTC's emphasis is to encourage policies that will expand U.S. exports and enhance the competitiveness of U.S. companies by eliminating major tax inequities in the treatment of U.S. companies operating abroad. To achieve this goal, American businesses must be able to participate fully in business activities throughout the world, through the export of goods, services, technology, and entertainment, and through direct investment in facilities abroad. Foreign trade is fundamental to the economic growth of U.S. companies.

II. General Comments

1. Proposed Treasury Regulation for Section 987 (56 FR 48457-01, 1991-2 C.B. 1032, 1991 WL 188392 (F.R.) should be modified. While conceptually compelling, the 2006 proposed regulations and the foreign exchange exposure pool method are exceedingly complex and impose a significant record keeping and compliance burden on taxpayers. We believe that certain modifications may help to reduce that complexity and compliance burden without significantly compromising the desired results (i.e., only recognition of economic foreign exchange gains and losses and the preservation of U.S. dollar asset bases).

As stated in the Preamble, the new "proposed regulations are designed to prescribe more precisely foreign currency gain and loss that is economically realized, while minimizing or eliminating the realization of non-economic currency gain and loss." To that end, the new proposed regulations adopt a balance sheet approach to determine exchange gain or loss of a section 987 QBU. The lynchpin of this balance sheet approach is the distinction made between "section 987 marked items" (i.e., financial assets and liabilities that give rise to section 987 gain or loss) and "section 987 historic items" (i.e., non-financial assets and liabilities that do not give rise to section 987 gain or loss).

Under the balance sheet approach/seven step calculation of Prop. Treas. Reg. Sec. 1.987-4, the basis (or amount, in the case of a liability) of each section 987 marked item is translated into the owner's functional currency at the spot rate on the last day of the taxable year; section 987 historic items are translated into the owner's functional currency at the historic exchange rate.

Much of the complexity and compliance/administrative burden associated with this balance sheet approach/seven step calculation is the required tracking of section 987 historic items (and the related historic exchange rates).

The cost associated with the development of database software to track numerous historic items and numerous exchange rates should not be underestimated. In addition, other costs will increase significantly (e.g., costs to conduct internal audits, to comply with Sarbanes Oxley, record retention costs, disaster recovery costs, etc.). Like all additional compliance costs, the NFTC believes that the costs associated with the implementation and maintenance of systems and processes necessary to comply with the 2006 proposed regulations will prejudice the global competitiveness of American worldwide corporations.

2. Treasury Regulations 1.482-1(a)(3) should be modified. It provides authority for a taxpayer to report results from related party transactions different from the prices actually charged, in order to reflect an arm's length result. This ability to make adjustments to pricing on a tax return is crucial, since it allows a taxpayer to incorporate new information and correct any mistakes made in the original transfer pricing. However, this authorization only extends to timely filed returns. A taxpayer is not permitted to file an amended return that decreases taxable income with respect to related party transactions. (A taxpayer is allowed to increase taxable income on an amended return.) So any new information or any discovery of errors after the taxpayer has already filed its return cannot be reflected on an amended return and, in fact, the taxpayer has no means of compelling the IRS to make any adjustments on audit reducing taxable income--even if an arm's length result clearly required such an adjustment.

For example, assume a transaction in 2009 between related parties in the US and UK that was priced in accordance with the information available at the time. Also assume that in 2010, further information became available that indicated that the 2009 pricing was incorrect, that the US entity should have had decreased taxable income and the UK entity should have had increased taxable income to clearly reflect income in the appropriate jurisdictions. If this information came to light prior to the US entity filing its timely 2009 return, the correct pricing could be reflected on this return. However, if the information came to light one day after the filing date, the US entity would have no means to correct the original pricing.

3. Treasury Regulations for Dual Consolidated Losses, Section 1503(d), should be repealed. The application of the DCL rules to the foreign operations of U.S. multinationals can have the effect of discouraging taxpayers from taking available measures to minimize foreign tax costs. This in turn has the long-term consequence of reducing U.S. tax revenues because the incremental foreign taxes can be applied as credits to reduce U.S. tax liability. The NFTC questions whether the policy objectives underlying the enactment of the DCL rules ever justified the creation of this incentive to increase foreign tax payments at the expense of the U.S. fisc. The withdrawal of Notice 98-11, and the ratification by the regulations of double-dip strategies involving the use of disregarded loans, strongly suggests that the exploitation of inconsistencies between U.S. and foreign tax rules to achieve foreign tax savings is no longer thought to raise significant tax policy concerns. The NFTC recognizes that the compatibility with U.S. tax policy of the DCL rules ultimately raises issues that must be addressed by Congress. The NFTC hopes, however, that the Treasury Department's review of regulations will provide an appropriate framework for a broader reevaluation of the DCL rules from a tax policy perspective.

4. Proposed Regulations under new Section 909 Foreign Tax Credit Splitters should be issued. Notice 2010-92 addressed some of the issues under the new provision, but further guidance is necessary for taxpayers to comply with the new provision. The Splitter Rules were not intended to be a total reworking of the previously existing foreign tax credit provisions. The JCT Technical Explanation of the Splitter Rules and the Senate Finance Summary to H.R. 4213, dated June 23, 2010, strongly suggest that the Splitter Rules target only abusive techniques. Furthermore, while the Splitter Rules were enacted against the backdrop of an intense debate about a broad international taxation and foreign tax credit reform, they were never considered to be a part of that effort. Finally, the grant of regulatory authority to the IRS to provide appropriate exceptions from the statute indicates that the purpose of the Splitter Rules was to prevent abuse, and not to rework completely the computational rules.

Consistent with this legislative purpose, the Splitter Rules should be limited to identified abusive transactions that artificially separate income from the foreign taxes imposed on such income. Drawing any other lines would be difficult conceptually and burdensome to administer from a practical standpoint. In defining abusive transactions, the guidance specifically should ensure that the Splitter Rules do not extend indiscriminately to the huge number of ordinary business transactions that may be treated differently under the foreign tax law and the U.S. tax law. To accomplish these goals, we recommend creating a list of prohibited splitter transactions (such as those specified in Notice 2010-92) that would be updated from time to time. If felt to be necessary, the listed transaction approach could be supplemented by a more general "principal purpose to split taxes" anti-abuse rule.

Further, to insure the Splitter Rules are as practical to implement as possible, we suggest that the scope of the Splitter Rules should be determined only after fully addressing the mechanics of dealing with the collateral issues, such as the calculation, tracing and distribution of related income and the interactions between the Splitter Rules and other relevant tax provisions.

Thank you again for the opportunity to provide this submission. The NFTC and its interested members look forward to continuing discussions on these and other matters.

Sincerely,

Catherine Schultz
Vice President for Tax Policy