February 26, 2019

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The Honorable David J. Kautter
Assistant Secretary (Tax Policy)
Department of the Treasury
1500 Pennsylvania Ave., N.W.
Washington, D.C. 20220

The Honorable Charles Rettig
Commissioner
Internal Revenue Service
1111 Constitution Ave., N.W.
Washington, D.C. 20224

The Honorable William Paul
Principal Deputy Chief Counsel and Deputy Chief Counsel
Internal Revenue Service
1111 Constitution Ave., N.W.
Washington, D.C. 202224

Re: Proposed Anti-Hybrid Regulations (104352-18)

Dear Sirs:

On behalf of the National Foreign Trade Council ("NFTC"), I would like to express our appreciation to the U.S. Department of the Treasury ("Treasury") and the Internal Revenue Service ("Service") for your efforts in developing the recently issued proposed regulations under Code sections 245A(e) and 267A (the "Proposed Anti-Hybrid Regulations").

The NFTC, organized in 1914, is an association of approximately 250 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.

The Proposed Anti-Hybrid Regulations are highly complex and would have a very significant impact on U.S. income tax administration and compliance. In light of that complexity, and the significant number of issues that we have with the Proposed Anti-Hybrid Regulations, we urge the Treasury and the Service to revise the regulations as discussed below.

Prop. Treas. Reg. Sec. 1.245A(e)-1(d)(2)

The broad language of Prop. Treas. Reg. Sec. 1.245A(e)-1(d) could treat group relief payments between related CFCs that are tax residents of the same country as hybrid dividends to the extent such payments result in deemed distributions.

Recommendation

Treasury should clarify that payments between related CFCs for the purpose of sharing tax liability under a tax consolidation, fiscal unity, group relief, loss sharing, or any similar regime are not hybrid dividends.

Prop. Reg. Sec. 1.245A(e)-1(d)(2)(B); Prop. Reg. Sec. 1-267A-5(b)

Notional Interest Deductions ("NIDs")

The treatment of NIDs as "hybrid deductions" in Prop. Treas. Reg. 1.245A(e)(1) and Proposed Treas. Reg. 1.267A-4(b) is beyond the intended scope of the Code and puts the U.S. at odds with the treatment of such deductions for purposes of anti-hybrid legislation in OECD jurisdicitons. NIDs are neither hybrid entities, nor hybrid transactions, which are the focus of section 267A. NIDs generally are incentivized by tax policy decisions in the taxing jurisdiction—they eliminate distinctions between debt and equity and encourage equity investment. In this regard, an NID is similar to a 100 percent deduction for investments in depreciable assets, such as the deduction allowed under section 168(k). It reflects a tax policy decision that is designed to encourage investment in the taxing jurisdiction.

It is significant that in most cases an NID is available without regard to whether any payment is made by the taxpayer to its shareholders. The proposed regulations recognize that section 267A applies to amounts paid or accrued pursuant to a hybrid transaction. Where an NID is available without regard to any payment, the section 267A should not be implicated. To draft the regulations broader in scope goes beyond the statutory rule.

Recommendation

The regulations should be amended to reflect that NIDs are not "hybrid deductions" for purposes of section 245A or the imported mismatch rules of section 267A. If the rule is to be

retained, it should only apply in the case of NIDs that are dependent on the entity making a payment or distribution to its shareholders. Only in that case is the hybridity, which is central to the application of the rules, arguably present. If the regulations continue to apply to NIDs, existing debt instruments should be grandfathered and it should only apply to debt instruments issued after the date the regulations are finalized.

Prop. Treas. Reg. Sec. 1.267A-3(b)

Prop. Treas. Reg. Sec. 1.267A-3(b) excludes payments that are accounted for as subpart F income or GILTI tested income by the recipient from the the definition of a disqualified hybrid amount because such amounts are already subject to U.S. federal income tax.

Recommendation

The final anti-hybrid regulations should continue this exception, as amounts that constitute subpart F income or GILTI tested income are subject to U.S. federal income tax. Denying a deduction for these amounts would lead to double taxation.

Prop. Treas. Reg. Sec. 1.267A-4

Prop. Treas. Reg. Sec. 1.267A-4 also denies a deduction for interest and royalty payments made to a related party if the payment (an imported mismatch payment) directly or indirectly funds a hybrid deduction. A hybrid deduction, in turn, is directly funded if the payee of the imported mismatch payment (an imported mismatch payee) incurs the hybrid deduction, irrespective of whether the hybrid deduction and the imported mismatch payment are factually related. A hybrid deduction is indirectly funded if (i) a hybrid deduction is incurred by a party other than the imported mismatch payee, and (ii)(A) the imported mismatch payee makes a deductible, non-hybrid payment (a funded taxable payment) to the party that incurred the hybrid deduction, or (B) a chain of funded taxable payments exists connecting the imported mismatch payee, each intermediary party, and the party incurring the hybrid deduction. In every case, whether a directly funded scenario or an indirectly funded scenario, the rules as currently written deny a deduction for an imported mismatch payment regardless of whether there is a factual connection between the imported mismatch payment and the relevant hybrid deduction and/or funded taxable payment. This imposes a requirement to search for potential funding transactions globally which have no relationship whatsoever to any hybrid deduction (which deduction may simply be created as a matter of local law). Such an approach, especially related to indirect funding scenarios, is not only burdensome but inadministrable for both taxpayers and the IRS when doing audits.

Recommendation

One potential approach would be for Treasury to replace the per se approach of the set-off rules and the funding rules in Prop. Treas. Reg. Sec. 1.267A-4(c) with a facts and

circumstances rebuttable presumption test that only disqualifies imported mismatch amounts to the extent that any relevant imported mismatch payment is factually connected to any hybrid deductions and/or funded taxable payments. In this regard, we recommend an approach similar to the rebuttable presumption in Section 355(e), as interpreted through the plan and non-plan factors of Treas. Reg. Sec. 1.355-7(b). A rebuttable presumption would place the evidentiary burden on the taxpayer, while improving administrability by providing a framework for company management to limit the scope of its review to transactions implicating plan factors. We would also be open to the use of other approaches in order to reduce the incredible complexity to comply with the 1.267A-4 imported mismatch funding rules.

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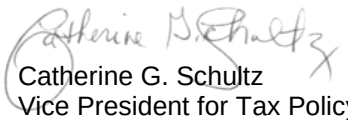
Again, thank you very much for the opportunity to provide these comments. Please do not hesitate to contact me should you have any questions on the above. We would be glad to meet with you to discuss these comments more fully and hereby formally request a public hearing to present our oral comments on the Proposed Anti-Hybrid Regulations.

Sincerely,



Catherine G. Schultz
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