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FEDERAL EXPRESS

April 20, 1998

Re: Proposed Regulations Relating to Global Dealing Operations

The Honorable Joseph H. Guttentag
Deputy Assistant Secretary - International Tax Affairs
Treasury Department
1500 Pennsylvania Avenue
Washington, DC 20220

Michael Danilack, Esq.
Associate Chief Counsel (International)
Internal Revenue Service
1111 Constitution Avenue, N.W.
Washington, DC 20224

Dear Sirs:

We write to express our strong support for the issuance on March 2 of the proposed regulations relating to global dealing operations and to suggest that these regulations be adopted now as temporary regulations, effective for taxable years beginning on or after the date they are so adopted.^{1/} The purpose would be to provide

^{1/} 63 Fed. Reg. 11177 (March 6, 1998).

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taxpayers with rules that may be relied on in filing returns for taxable years beginning on or before the adoption of final regulations.

Under the proposed regulations, branches maintained by a single corporation in different countries may be treated as separate entities in determining the source (and thus, in the case of a foreign corporation, the taxability) of income from customer transactions in notional principal contracts, foreign currencies and other securities. Income generally will be allocated between branches under the "arm's length" pricing principles that apply under Section 482 of the Internal Revenue Code to transactions between separate legal entities that are commonly controlled. The proposed regulations will apply to taxable years beginning after the date of their adoption as final regulations.

While the proposed regulations will apply, and are important, to both domestic and foreign taxpayers, they fill a particular need in the case of foreign banks that engage in such operations through branches located in the United States. With the exception of foreign banks, most taxpayers may, if they choose, determine income or loss from transactions with related parties under the Section 482 regulations and without seeking an advance pricing agreement from the Internal Revenue Service. Current regulations generally disregard inter-branch transactions and also provide that, if a U.S. branch materially participates in a transaction involving notional principal contracts, all of the income or loss from the transaction is effectively connected with that branch.^{2/} The broad effect of these rules is to

^{2/} Treas. Regs. §§ 1.863-7(a)(1), 1.863-7(b)(3), 1.988-1(a)(10) (general rule) and 1.988-4(c).

preclude reliance on Section 482 and to force a foreign bank to seek an advance pricing agreement if it effects customer transactions in foreign exchange or notional principal contracts in its U.S. branch and it either enters into inter-branch transactions as part of that business or conducts the business in more than one jurisdiction. The problem is compounded because advance pricing agreements are available only pursuant to U.S. tax treaties and there is thus no alternative available to a foreign bank that is not a treaty country resident.

The global dealing operation regulations proposed on March 2 would provide a basis on which foreign banks could, like other taxpayers, determine income or loss on the basis of rules set out in regulations issued under Section 482. We strongly support that result, and we believe it would be appropriate to adopt these regulations now, as temporary regulations, so that they may be relied on by taxpayers prior to their adoption as final regulations. Adopting the proposed regulations now as temporary regulations will not prejudice taxpayers — any taxpayer who objects to the rules will be free, as before, to seek an advance pricing agreement from the Internal Revenue Service that adopts a different method. Nor should it prejudice the Internal Revenue Service — the rules set out in the proposed regulations were developed by the Service and presumably reflect its view as to what is acceptable. Consideration might also be given to permitting taxpayers to elect to apply the temporary regulations to prior open years.

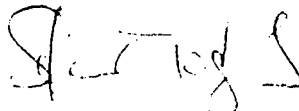
The Honorable Joseph H. Guttentag
Michael Danilak, Esq.

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April 20, 1998

We are not in this letter commenting on the substance of the proposed regulations, but simply on the importance of providing, as soon as practicable, rules that may be relied on by taxpayers who for whatever reason do not want to seek, or who are ineligible for, advance pricing agreements with respect to global dealing operations.

Very truly yours,

A handwritten signature in dark ink, appearing to read "Steven C. Todrys", written over a horizontal line.

Steven C. Todrys,
Chair

cc: The Honorable Donald C. Lubick
Philip R. West, Esq.
Patricia Brown, Esq.

The Honorable Charles O. Rossotti
The Honorable Stuart L. Brown
Ginny Chung, Esq.
Richard Hoge, Esq.