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February 11, 2005

The Honorable Mark W. Everson
Commissioner
Internal Revenue Service
Room 3000 IR
1111 Constitution Avenue, N.W.
Washington, D.C. 20224

Dear Commissioner Everson:

I am pleased to submit the New York State Bar Association Tax Section's Report No. 1079 addressing the proposed Treasury regulations (REG-129771-04) (the "Proposed Regulations") issued by the Internal Revenue Service and the Treasury Department on August 6, 2004 regarding the determination of a United States shareholder's pro rata share of subpart F income under Section 951 of the Internal Revenue Code of 1986, as amended (the "Code").

The Proposed Regulations provide clarification of the operation and scope of the pro rata share determination under Section 951 to ensure that allocations of subpart F income reflect shareholders' economic interests in controlled foreign corporations ("CFCs"). In general, we endorse the policy rationale underlying the Proposed Regulations. The Report identifies several areas, however, where we believe that the Proposed Regulations should be modified or strengthened.

In general, the Proposed Regulations respond to specific fact patterns involving potentially artificial allocations of subpart F income: (i) those where the allocation of earnings and profits among multiple classes of stock depends on the discretion of the governing body of the CFC (referred to in the Report as "Discretionary Stock") and (ii) those where the allocation of earnings and profits among multiple classes of stock is subject to a restriction

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or limitation (referred to in the Report as “Blocked Stock”). Our comments primarily relate to these core provisions.

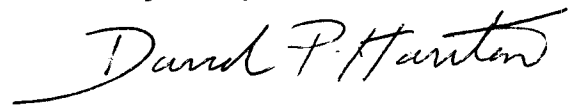
We agree that the rules in the existing regulations for Discretionary Stock are outdated and need to be revised. We are concerned, however, that the proposed valuation rule with respect to Discretionary Stock may prove difficult to administer in practice given the difficulty in applying valuation techniques to a class of stock where the timing of a return on invested capital is subject to the discretion of the governing body of the CFC. We recommend that the IRS and Treasury consider adopting a “facts and circumstances” test in its place.

We endorse the proposal relating to Blocked Stock. We also believe that the IRS and Treasury should expand the proposed rules to cover the effect that certain dividend rights may have on the allocation of earnings and profits in an effort to ensure that such allocations are made in a manner consistent with the shareholders’ economic interests in the CFC. At the same time, we have some concerns that the proposal relating to the treatment of redemptions may be overbroad.

Finally, we have pointed out several instances where we believe that the application of the Proposed Regulations could be clarified and have identified several technical issues with the manner in which the Proposed Regulations would operate in connection with other sections of the Code.

As always, we would be pleased to provide assistance in any way we can.

Respectfully submitted,

A handwritten signature in black ink that reads "David P. Hariton". The signature is written in a cursive style with a long, sweeping underline that extends to the left.

David P. Hariton
Chair

cc: Eric Solomon, Acting Deputy Assistant Secretary (Tax Policy)
Deputy Assistant Secretary (Regulatory Affairs)
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Department of the Treasury
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