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November 24, 2014

The Honorable Mark Mazur
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The Honorable John Koskinen
Commissioner
Internal Revenue Service
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Washington, DC 20224

The Honorable William J. Wilkins
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Internal Revenue Service
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Re: **Report on Treaty Resourcing of Income Provisions**

Dear Messrs. Mazur, Koskinen and Wilkins:

I am pleased to submit the attached report relating to resourcing provisions found in U.S. income tax treaties (the "Report"). The Report provides a general overview of the various types of resourcing rules found in U.S. income tax treaties, conveys the Tax Section's support for the use of a blanket resourcing rule and recommends that the Internal Revenue Service (the "Service") and the United States Department of the Treasury (the "Treasury") issue guidance clarifying the application of the sourcing rules found in certain treaties.

By way of background, U.S. income tax treaties generally provide that the United States will grant a U.S. taxpayer a credit against U.S. tax for taxes paid or accrued to the treaty partner in accordance with the terms of the treaty. However, the grant of a credit against U.S. tax is generally made in accordance with and subject to the law of the United States, and U.S. law includes a variety of rules and limitations relating to foreign tax credits, including rules designed to limit the foreign tax credit to taxes paid on income that is treated as foreign source. Where a U.S. income tax treaty allows the treaty partner to tax income that U.S. domestic law treats as U.S. source, a U.S. taxpayer that pays income tax to the treaty partner on such income may not be able to claim a foreign tax credit unless the income is treated as foreign source under the treaty.

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Mr. Mazur
Mr. Koskinen
Mr. Wilkins
November 24, 2014

As described in detail in the Report, U.S. income tax treaties have over time taken various approaches to resourcing income that a treaty partner is permitted to tax. The Tax Section strongly supports the approach of the current U.S. Model Income Tax Convention, providing for a blanket resourcing of all income of a U.S. resident that a treaty partner is authorized to tax under a bilateral income tax treaty. However, a number of treaties currently in force do not have a blank resourcing rule and the scope of the resourcing rule in some of these treaties is not entirely clear. Many of the issues raised by these treaties could be solved through the publication of guidance (which could take the form of a revenue ruling, revenue procedure or notice) explaining how the United States will interpret the treaties. Such guidance could be directed at the interpretation of specific, individual treaties (or groups of identified treaties with identical or similar language) where the application of the source rules for purposes of claiming a foreign tax credit is unclear and it is determined that the intent of the treaty (when combined with the application of the Code) is to allow the sourcing required for a foreign tax credit. Alternatively, for some treaties broader guidance could be issued, providing that income which the treaty allows the foreign treaty partner to tax shall be treated for Section 904 purposes as “arising from sources outside the United States” (and therefore as sourced to the relevant treaty partner country, subject to the other limitations of Section 904). As a further alternative, guidance interpreting various treaties could be issued in the form of regulations under Section 894 or possibly under Section 904(d)(6)(C).

We appreciate your consideration of our recommendations.

Respectfully submitted,



David H. Schnabel
Chair

Attachment

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November 24, 2014

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