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The Impact of the Revenue Reconciliation Act of 1993 on International Taxation

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Abstract

The Revenue Reconciliation Act of 1993 introduced numerous modifications to foreign taxation. I have briefly summarized how these code sections appeared and were applied prior to and after these revisions. The objective of my extended research was to determine the impact of the modifications on United States taxpayers, specifically, U.S. multinational corporations. I began my study with a detailed analysis of the tax law prior to the ‘93 Act and proceeded to adjust my knowledge with a similar in depth investigation of the modifications. To determine an overall impact from the tax changes, I interviewed an international tax specialist with both “big six” and “corporate” experience and analyzed numerous articles from specialized periodicals. Primary resources were consulted in every stage and section of my research.
The Impact of the Revenue Reconciliation Act of 1993 on International Taxation

"The Revenue Reconciliation Act of 1993 in encouraging some business owners to take a second look at how they do business," said Ivy F. Zito, CPA, a sole practitioner in Marlborough, Connecticut. Upon enactment of the RRA '93 taxpayers flooded the offices of their tax practitioners seeking explanations and interpretations of yet another change in the tax code. Many were inquiring about possible opportunities available under the new provisions, while others were anxious to discuss new threats the Act exposed them to.

The first goal was to "make the tax code fairer" by taxing the rich. One way to accomplish this goal was to increase the tax rates, and so they did. The top rate was increased to 39%. Second, they wanted to reduce the deficit. In order to reach the middle class, the Administration considered an energy tax, specifically on gas. The tax was to be designed to reach gasoline, a problem for the West, and fuel oil, a problem for the East. Finally, the third goal was to stimulate the economy, and the Administration used an investment tax credit which, as advised by a group of economists, was to accomplish this goal.

International taxation received considerable unfavorable attention by the '93 Act as President Clinton attacked multinationals with a vengeance. Steven Hannes, international tax partner at Deloitte & Touche's Washington office, states, "Clinton's proposals will certainly increase the tax burden on United States subsidiaries of foreign companies." Even though foreign presence in the

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1 Sherr, p. 35
2 CCH, p.8
3 Kranz, p.1
Anti-Abuse & Compliance

The RRA of '93 created four changes that were intended to strengthen anti-abuse rules and improve taxpayer compliance in the international area. The most notable revisions included an expansion of the earnings stripping rules, a stiffening of the penalty for transfer pricing violations, retraction of the portfolio interest exemption for contingent interest, and additional authority on multi-party conduit arrangements.

Earning Stripping Rules

General Rules

Prior to the RRA '93, Section 163(j) was enacted to prevent the following type of activity:

The United States and Italy sign a tax treaty reducing the U.S. withholding tax on interest income for Italy from 30% to 15%. Italian based Corleoni Company subsequently makes a loan to its subsidiary, Smith Company in the U.S. While the interest income received by Corleoni Co. would only be taxed at 15%, Smith Co. would fully deduct the interest expense in computing its U.S. tax liability. This would decrease the tax liability of Smith Co and increase earnings for Corleoni Co.

Congress was convinced that foreign investors in U.S. companies were encouraged by reason of these tax deductible interest payments. The tax avoidance scheme illustrated above is commonly referred to as “earnings stripping”, which occurs when a foreign parent who is not taxed by the U.S., loans money to its U.S. subsidiary who then deducts the interest paid on the debt owed to the parent. Generally, the U.S. imposes a 30% withholding tax on foreign

\[5\] RIA, p.245
U.S. has created many benefits to our economy, including creating jobs for the unemployed, Clinton felt that the tax abuse was “out of hand” and thus pushed for several modifications.

The international tax issues addressed below include additional anti-abuse rules and modifications to the rules relating to controlled foreign corporations and the foreign tax credit. A majority of the tax professionals feel that these laws were unnecessary. Debra Jung, a international tax expert with big six and corporate experience states, “U.S. Multinationals face overlapping tax regimes. It should not be the case. Laws which are established to close every possible loophole result in enormous compliance burdens. Shouldn’t materiality be a factor when these laws are established? Shouldn’t the laws target the appropriate class of taxpayer, rather than all taxpayers? It is sad to think that in this competitive, global economy we waste our resources in such a manner.”

The following section focuses on the changes made to the taxation of corporations by the RRA’93 which first include additional anti-abuse rules with regards to earnings stripping, transfer pricing, and portfolio interest. The second section analyzes the modifications made to the rules relating to controlled foreign corporations. Areas affected by these changes include investments in excess passive assets, foreign investments in U.S. property, and the subpart F provisions. Finally, foreign tax credit changes were made with regards to the allocation of research and development expenditures, working capital for oil, gas and shipping income, and softwood log production.

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4 Debra Jung, interview
companies for any income drawn from their U.S. subsidiaries, unless a treaty with the particular
country eliminates or reduces the tax.

To prevent earnings stripping, Congress enacted Section 163 (j) to disqualify as a deduction
the portion of the interest payment made to a related foreign or tax-exempt organization for
which no U.S. tax was imposed on the corresponding income. This disallowance occurs if the
debt-to-equity ratio of the U.S. company is greater than 1.5 to 1 and the company’s net interest
expense exceeds 50% of its adjusted taxable income. Originally, fixed-term loans issued before
July 1989 were excluded from the scope of Section 163 (j).

Even though it appears as if Section 163 (j) closed a sizable loophole, organizations still
managed to defeat the provision through clever tax avoidance schemes. The Corleoni Company
example continues to illustrate how companies could still “strip their earnings”.

Upon enactment of Section 163 (j), Corleoni Company advises its U.S. subsidiary,
Smith Company, to obtain a loan from Third Party Company instead. Third Party Co., a
tax-exempt organization, loans the money to Smith Co., but only with Corleoni Co.’s
guarantee. Once again, the tax liability for Smith Co. is minimized by interest expense
deductions, causing increased profitability for Smith Co. and additional earnings to Corleoni.

The RRA ‘93 expanded the Section 163 (j) earnings stripping interest deduction limitation to
include guaranteed debt. The definition of “disqualified interest” for purposes of the disallowance
of the interest deduction by a corporation now includes interest paid or accrued on a loan from an
unrelated party that is subject to a disqualified guarantee made by a tax-exempt organization for a
foreign person if there is no gross-basis U.S. income tax imposed on the interest income.

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6 Engle, p. 89
Additionally, the 1993 Act eliminated the exception for fixed-term loans issued before July 11, 1989.\footnote{RRA, p. 2610}

However, there are two exceptions where a guarantee on unrelated party loan, would not disqualify the interest payments for deductibility. Under the first exception, the new rule would not apply if the debtor owns a controlling interest in the guarantor (using Section 267 (C)(1) to define controlling interest). Referring back to the example, if Unrelated Party Co. were to own 80\% of Corleoni Co., the interest payments would be deductible by Smith Company. Under the second exception, a guaranteed loan is not disqualified if the withholding tax would have been posed on the “related guarantor” regardless of whether the loan had passed through a third party. Section 163 (j), as stated prior to RRA ‘93 Act, will only effect those companies with a debt-to-equity ratio of greater than 1.5 to 1 or companies with interest expense greater than 50\% of their adjusted taxable income.\footnote{Engle, p. 89}

**Impact**

The new rules did not spare existing debt arrangements from falling within the scope of the expanded Section 163 (j), for it was enacted to apply to any present and future tax avoidance schemes of this type. Eliminating the fixed-term loan exemption from the pre RRA’93 rule extended Section 183 (j) to nearly eliminate the loop hole, which had a negative impact on foreign investors. Many U.S. economists feared that foreign companies would “pack their bags” and take their business abroad, but the past three years since the enactment reveal no such movement. The biggest impact was a rush to reassess “existing financing structures” in light of the new rules.
Companies needed to refinance existing debt by replacing it with new debt not guaranteed by a foreign related party. It forced them to investigate alternative forms of financing such as insurance or guarantees provided by unrelated parties.

Even though this modification affected many taxpayers, Debra Jung supports her opinion that the new laws are useless and wasteful by stating, "It's unfortunate that these provisions apply to U.S. multinationals. Say that you are a U.S. company and you take a loan from your French subsidiary. Most likely the French subsidiary's income will be subject to U.S. Subpart F tax anyway! Once again, another set of rules to monitor." Depending on the entity being taxed, these provisions apparently have different impacts!

**Transfer Pricing**

The second major revision enacted by Congress to curb taxpayer abuse dealt with the transfer pricing provisions. Section 482 was established to prevent organizations from shifting income to their foreign related parties through transfer pricing schemes. The following example illustrates a typical transfer pricing tax avoidance scheme:

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CD Tunes Corp., based in the United States, manufactures compact discs for recording studios and music companies. Exitos Co., operated in Mexico, is a subsidiary of CD Tunes, and manufacturers cassette tapes for sale in Mexico and the surrounding area. CD Tunes Corp has captured the Mexican market for compact disc sales. If CD Tunes sells directly to the buyers in Mexico, U.S. tax will be imposed on the income. Therefore, to avoid any U.S. tax on sales income, CD Tunes arranges to sell the compact discs to Exitos Corp. at a significantly reduced transfer price, who will then sell them to Mexican buyers. Income will be taxed in Mexico to Exitos Corp. The benefit to parent CD Tunes lies in possible lower tax rates in Mexico, special tax credits on income earned in Mexico, or other tax incentives arranged through treaty.

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Engle, p. 90

Debra Jung, interview

McIntyre, p. 5-3
Prior to RRA '93, Section 482 granted the Internal Revenue Service the authority to allocate income, deductions, and credits between related parties to reflect the actual income of each. The allocation is accomplished through corrections referred to as “correlative adjustments”, which describe the IRS action of adjusting the income of one company, and correspondingly adjusting the income of the related party involved in the transfer price transaction, thereby eliminating any shifting income. Therefore, the IRS would have reallocated the income of both CD Tunes Corporation and Exitos Corporations to reflect their actual income. CD Tunes’ income and tax liability would have increased significantly as a result the correlative adjustment. In addition, CD Tunes might have exposed itself to possible penalties if the valuation misstatements were significant.

Section 482 requires a taxpayer to determine taxable income based upon the transactions with related parties in accordance with the Code’s “arm’s length standard” which is defined in the Treasury Regulations as a transaction, that if entered into with an unrelated party, would have resulted in income. In order to determine if any shifting of income existed, the IRS now must determine if common control exists directly or indirectly by the same interests, and if so, the specific transactions involving transfer prices will be analyzed. The transfer prices should be recomputed using the suggested three pricing methods from the Regulations, which in order of preference are: the comparable uncontrolled price method, the resale price method, and the cost plus method. A fourth residual method, the “any other appropriate method” is also permitted. In applying these methods to the various transaction, the IRS will determine the net transfer price adjustment for the company.

12 Doernberg, p. 149
A net Section 482 transfer price adjustment is the net increase in the taxable income of a commonly controlled taxpayer for the tax year resulting from an adjustment in the price for any property, service, or use of property under Section 482. A net Section 482 transfer price adjustment will not include any portion of the net increase in taxable income that is attributable to redetermination of a price that was in accordance with one of the pricing methods specified above.\textsuperscript{13}

Prior to RRA '93, Section 6662(e) imposed a 20% accuracy related penalty on U.S. companies for understating the tax liability attributable to "\textit{substantial valuation misstatements}" on income tax returns. The penalty was imposed whenever the taxpayer misapplied the arm’s length standard so as to have a Section 482 transfer price adjustment that exceeded the lessor of $10 million or 20% of gross receipts. The 20% penalty would be doubled to 40% if there was a "\textit{gross valuation misstatement}". The 40% penalty was triggered when the transfer price adjustment was greater than lessor of $20 million or 40% of gross receipts.\textsuperscript{14} Both penalties are applied to the amount of the understatement of income, and are in addition to regular tax. However, if the taxpayer, can in good faith, prove that the Section 482 transfer price adjustment would not accurately reflects income, any additional taxes penalties can be avoided.

RRA’93 lowered the thresholds for the valuation penalties, making it easier to impose these penalties on a company. The 20% penalty could now be triggered if the net Section 482 transfer price adjustment that may be a substantial valuation misstatement reaches the lower of $5 million or 10% of the taxpayer’s gross receipts. Similarly, the 40% penalty thresholds have also been reduced to the the lessor of $10 million or 20% of gross receipts.\textsuperscript{15}

\textsuperscript{13} RRA, \\
\textsuperscript{14} RRA, p. 2613 \\
\textsuperscript{15} Engle, p. 147
The House the Senate Bill amendments were identical to each other and expanded the “good faith” requirement to make it more difficult to avoid the transfer price penalty by proving that the transfer prices appropriately reflected income. The RRA ’93 established that in measuring the net Section 482 transfer price adjustment, a net increase in taxable income attributable to a price redetermination will be disregarded under Section 482 if the taxpayer satisfies the following statutory requirements:  

- taxpayer would have to establish that the price it used was determined under a pricing method specified in the Section 482 regulations  
- taxpayer would have to prove that the method was applied reasonably  
- taxpayer would have to establish that there was documentation in existence at the time of the filing of the return which documentation the taxpayer provides to the IRS within 30 days of request.

The original goal of these Section 482 penalties was to encourage adherence to transfer pricing anti-abuse rules. However, many companies found documentation requirements to be excessive, and as a result, they refused to comply. Consequently, the IRS found that the audits regarding transfer pricing became costly as a result of extensive searches for the required documentation. To see how the penalty is computed, the CD Tunes Corporation illustration concludes at the top of the following page.

CD Tunes Corp. managed to avoid any penalties prior to RRA ‘93, and therefore continued to shift income to Exitos Corp through low transfer prices for the compact discs. Realizing the tax benefits of their actions, Exitos begins to sell cassette tapes to CD Tunes at extremely high transfer prices. CD Tunes would sell the cassettes to the unrelated parties. In this case, the tax benefit was derived through an increase in cost of goods, which made for

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16 RR Bill, p. 171
17 Smith, p. 303
smaller gains upon sale and hence less taxable income. Upon enactment of RRA '93, the IRS used the Resale Price Method to determine the “arm’s length” transfer prices for the related parties. The total transfer price adjustment amounted to $12 million. CD Tunes could not prove that their pricing methods were reasonable or documented, and were penalized 40% of the underpayment of tax resulting from the “gross valuation misstatement” in addition to regular U.S. income tax.

Impact

Debra Jung comments on the transfer pricing provision as follows:

"The Tax Reform Act of 1990 introduced sever penalties for abusive transfer pricing practices. The tax Reform Act of 1993 continued the focus on transfer pricing and introduced onerous record keeping requirements as well. The IRS was rightfully concerned that some taxpayers did not give adequate thought and analysis to the transfer prices they had set and had little, if any, documentation to provide auditors. Theoretically the transfer pricing rules (as outlined in Section 482) are correct, but as practical matter, the comparable transactions upon which they are based do not exist for many U.S. Multinationals. This is due to the fact that often the U.S. Multinational A is dealing with its foreign affiliates world-wide, instead of a third party."

The Temporary Regulations provided guidance by detailing how the IRS would test for the reasonableness of pricing methods used in determining which increases in taxable income could be excluded from the net transfer price adjustment.17 The tests are as follows:

- the experience and knowledge of the taxpayer and members of the controlled group.
- The extent to which accurate data was available and that the data was analyzed in a reasonable manner.
- The extent to which the taxpayer followed the requirements in the Section 482 Regulations in applying the method and reasonably relied on an analysis or study done by qualified professionals.

Temp. Reg. 1.6662-6T(d)(2)(iii)(B) and Temp. Reg. 1.6662-6T(d)(2)(iii)(C) explain further the specific forms of documentation required by the Service. Temp. Reg 6662-6T(e) provides computational rules for calculating the net adjustment penalty.

17 Temp. Reg. 1.6662-6T(d)(2)(ii)
A taxpayer could argue that the cost of complying with the Temporary Regulations outweighs the cost of any penalty tax, since it is inevitable anyway. Consider, for example, a company that believes it may be well over the threshold for the penalty. What benefit will documentation provide since the penalty will be imposed with or without the documents? Taxpayers in such a situation might decide to use some simplistic form of transfer price determination, thereby risking exposure to a penalty instead of spending the money to gather data and create the “audit road map with index” required by the IRS.19 The demanding requirements of the regulations disturbed the majority taxpayers affected. Nonetheless, since transfer pricing has proven to be a primary tool for tax avoidance, Congress felt compelled to curtail such abuse.

A procedure available to taxpayers in avoiding problems with the IRS regarding the net transfer adjustment and the related penalties is to enter into an advance pricing agreement (APA) with the IRS. In doing so, the taxpayer specifies in advance the pricing method that will be used, and if the Service agrees with the method there will be no Section 482 adjustment. However, this method also requires significant documentation prior to closing the APA.

The IRS appears to be losing in the courts when it comes to their allocation rights under Section 482. In 1994, The IRS lost three separate cases against Perkin-Elmer Corp, Exxon Corporation, and Seagate Technology.20 In Seagate Technology, the court found that the method used by the IRS to determine the arm’s length transfer price was not reasonable and determined on its own a method they believed to reflect actual income. The court did not believe that Seagate’s transfer prices were at arm’s length, but arrived at income figures that were significantly less than those the IRS determined. Due to the specific circumstances of each case, the rules

19 Smith, p. 307
20 Robbins, p. 33
could be applied differently each time. The courts will remain busy interpreting case-by-case what should be considered a "reasonable transfer pricing methods".

**Portfolio Interest Exemption (Contingency Interest)**

**General Rules**

Nonresident aliens and foreign corporations receive a *portfolio interest* income exemption which, prior to RRA '93, included *contingent interest* income. Interest income is contingent when it is based on uncertainties such as future receipts, sales, cashflows, income, profits, changes in value of property, dividends, and partnership distributions of the debtor or related party. Regarding the portfolio exemption, interest is not deemed contingent when the contingency relates to the timing of interest payments with respect to nonrecourse or limited recourse indebtedness, interest related to currency or interest rate hedging, or interest when determined by reference to changes in the value or yield on actively traded property other than U.S. real property.  

The original provision of Section 871(a) excluded portfolio interest income (including contingent interest) from the 30% withholding tax normally imposed on U.S. income earned by a foreign entity. The exemption applied to income earned on qualifying U.S. bonds and obligations, which are issued with foreign purchase as the main intent. The original provision was specifically enacted in 1984 to expand access of U.S. borrowers to the "Eurobond market" and other international markets. Congress intended to reduce the costs of financing the large federal deficit of the 1980's by allowing these exemptions and facilitating access to the

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*RRA, p.146*
international bond market.\textsuperscript{22} Without Section 871, the U.S. would not be able to trade actively in the international markets because of the 30\% withholding tax. Congress created a tax free trading arena for the U.S. bond market and a heaven for expert tax evaders in the international sector.

The new provision for the exemption benefited the real estate market for foreign companies and non-resident aliens. It allowed the foreign investors to make loans on U.S. real estate ventures and receive not only fixed term interest, but “shared appreciation”, a contingent interest as well. As long as this contingent portion of interest did not too closely resemble a dividend, the 30\% withholding tax would not be imposed according to the original portfolio interest exemption.

Some benefits to the portfolio interest exemption expired upon enactment of RRA’93 when contingent interest was no longer exempt from U.S. tax. Again, this applies to contingent payments from debtors or related persons as defined in Section 267(a). The main purpose of contracting Section 871 was to close a portion of the “tax havens” that were created as a result of allowing foreign corporations to take extreme advantage of the provision. Congress was concerned that the contingent portion of the “participating debt” created a economic result much the same as an equity interest.\textsuperscript{23}

The exact loss in tax revenue resulting from the contingent portfolio interest exemption has never measured due to difficulty in assessing a change so complex. Section 871 provided short-term benefit to the U.S. in 1984, but by 1993 it was time to curtail the abuse by foreigners of the liberal policies of the 1984 Revenue Act. However, the elimination of the contingency interest income exemption does not override any existing treaties.

\textsuperscript{22} McIntyre, p. 248
\textsuperscript{23} Royse, p. 360
There are also special rules that apply to contingent and non-contingent interest subject to estate tax. A proportionate value of such instruments, as determined by the IRS, is treated as property within the United States and is therefore included in the descendant’s gross estate. No rules have been issued which describe a method for determining the proportionate value to include in the estate. However, the Conference Committee has allowed tax payers to use any “reasonable method”, to determine estate value, subject to acceptance by the IRS. This modification to Section 871 to exclude contingent interest from the exemption, is effective for interest received after December 31, 1993, and does not include interest accrued with respect to any indebtedness with a fixed term that was issued before April 8, 1993 or that was issued after April 7, 1993 under a written binding contract in effect on April 7, 1993 and at all time afterwards until the debt is issued.²⁴

**Impact**

Participation financing, commonly referred to an “equity kicker”, was a popular fixed rate mortgage used during the 1980’s that provided shared appreciation (contingent interest). The instrument was given the name “equity kicker” because the borrower would pay back fixed principal plus interest, which included a contingent element of interest based on cash flows or profits from the real estate. The issue of whether the contingent portion of such an instrument should be considered debt or equity was brought up in court in Farley Realty Corp, 279 F. 2d 701 (CA-2 1960) where the court held that a 50% equity kicker was not debt but represented an ownership interest in the underlying property. Prior to RRA ‘93, if the equity kicker was less than 50%, the contingent payment would be considered portfolio interest income and was

²⁴ RIA, p. 244
therefore excludable from income.\textsuperscript{25} Foreign parties structured these realty investments as debt in order to fall within Section 871 and avoid U.S. tax, creating a transaction where economic interest was received but not taxed. Contingent interest income (unless stated otherwise by treaty) received by a foreign person is now fully U.S. taxable, and applies to interest received after 1993. However, participating fixed term debt obligations issued on or before April 7, 1993 are exempt.\textsuperscript{26} Tax planning adapted quickly to changes from RRA'93. Taxpayers intending to use portfolio interest in structuring new debt were asked to consider the statutory exceptions and to make sure the interest could not be classified as contingent, and thus become taxed. Additional tax planning avenues are listed below:

\begin{itemize}
\item provide for an increased fixed portion of interest while decreasing the contingent portion by predicting the contingent independent fact such as cash flows or appreciation.
\item U.S. creditors should obtain loans and financing from those countries where treaties are overriding.
\item Structure all participating debt to be tied to the qualifying factors such as the consumer price index or some other independent index.\textsuperscript{27}
\end{itemize}

**Multi-party Conduit Arrangements**

Code Section 7701 was slightly modified by RRA'93 to include a provision that expanded the IRS's authority regarding multi-party conduit arrangements. The IRS was granted the authority to issue regulations regarding the recharacterization of such arrangements where the IRS believed necessary to prevent tax avoidance. Consider the example below as it describes a typical multi-conduit financing arrangement.

\textsuperscript{25} Royse, p. 361
\textsuperscript{26} Engle, p. 90
\textsuperscript{27} Royse, p. 91
Slovak Corporation in Czechoslovakia is the parent company of both Smith Corporation in the U.S. and Stavros Financing Corporation in Greece. Tax treaties exist between Greece and the U.S. that exempt any interest income payments from the 30% withholding tax. A similar tax treaty exists between Czechoslovakia and Greece. No tax treaty exists between the U.S. and Czechoslovakia. Slovak wants to make a loan to Smith, but the interest payment back to Slovak would be taxed. Instead, Slovak loans the money to Stavros who in turn makes a loan to Smith. Because of the corresponding tax treaties, interest payments from Stavros to Slovak and from the U.S. to Stavros are tax exempt. Essentially the loan from Slovak to Smith was accomplished without any tax impositions.

In the above example, Stavros is considered the “conduit”, a financial intermediary who would not have extended a loan to Smith without the arrangement from Slovak. The courts state that taxation depends upon the substance of a transaction as a whole, and, prior to RRA ‘93, the court recharacterized such multi-party financing arrangements and imposed taxes accordingly. In Commissioner v. Court Holding Co. 324 U.S. 331 (1945) the court ignored the middle party “conduit” and imposed tax as if only the two parties were involved. Using the above example, the same court would have eliminated Stavros as part of the arrangement, and impose tax as if payments were made from Smith to Stavros.

In Aikus Industries Inc. v. Commissioner 56 T.C. 925 (1971), a different type of multi-party financing arrangement named “back-to-back” was attacked by the courts. In a “back-to-back” type of arrangement the intermediary conduit is an unrelated party. Revenue Ruling 87-89 states that a “back-to-back” arrangement should be recharacterized if a creditor would not have otherwise made a loan. In the Aikus Industries case, the court re-characterized the arrangement and gave rise to the 30% withholding tax, since the debts to and from the conduits were identical. After this court case, and prior to RRA ‘93, the IRS took a position even strickeater than the courts by claiming that the loans did not have to exactly match to be recharacterized. Revenue Ruling
84-152 and 84-153 stated that where the conduit does not have control over payments, a reclassification would be considered as is evident above.\textsuperscript{28}

The purpose of the additions to Section 7701 was to give the IRS more authority to issue regulations recharacterizing multi-party financing transactions as a transaction among any two or more such parties. The IRS was also given the authority to issue regulations concerning multi-party transactions involving debt guarantees or equity investments where the IRS believes recharacterization is necessary to prevent tax avoidance.\textsuperscript{29} The provision was effective as of the date of the enactment of RRA '93.

\textsuperscript{28} RR Bill, p. 185
\textsuperscript{29} RRA 93, p. 147
Controlled Foreign Corporations

III.

In addition to strengthening anti-abuse rules and improving taxpayer compliance, the RRA ‘93 also made changes dealing with controlled foreign corporations. The revisions include changes with investment in excess passive assets, a modification to taxation on investment in U.S. property, and a modification to the subpart F.

Investments in Excess Passive Assets

Prior to RRA ‘93, a tax deferral benefit existed for U.S. shareholders (a taxpayer with greater than 10% interest) on a portion of their earnings from investments in Controlled Foreign Corporation’s (CFC) (Bolded terms are subsequently discussed in detail). However, any such advantages were eliminated by the ‘93 Act. Prior to passage of the Act, a U.S. shareholder was required to include in income a pro rata share of the CFC’s subpart F income and the CFC’s increase in earnings invested in U.S. property.30 Now, according to the 1993 revision, a shareholder is also required to include in taxable income a pro rata share of the accumulated earnings of the CFC that were invested in excess passive assets not previously taxed.31

Before 1962 few restrictions existed for U.S. taxpayers who used foreign corporations for tax avoidance purposes. As a result, expert tax evaders took advantage of the liberal policies. In the 1962 legislation, Sections 951 to 964 were enacted to curtail the abuse by placing limitations on the ability of U.S. taxpayers to manipulate foreign corporations solely to defer taxes. These

30 RRA 93, p.25
31 Section 951(a)(1)(C)&(A) as amended by ‘93 Section 13231(a)
sections are contained in subpart F of part III of subchapter N of chapter 1 of the Code, and are commonly referred to as the subpart F provisions.\textsuperscript{32} Prior to the extension of the CFC rules, shareholders only included their pro rata share of any income determined under these subpart F provisions and any earnings invested in U.S. property.

The main purpose of the subpart F provisions was to limit U.S. shareholder ability to defer taxes on income not derived from regular business operations. An initial concern was that placing such restrictions would discourage U.S. persons from investing abroad. Contrary to that belief, it is evident today that foreign investment has expanded. Increased activity in CFC investments brought about clever new tax avoidance schemes, allowing tax evaders to defeat even the subpart F provisions. Consequently, the additional inclusion for U.S. shareholders investing in CFCs was included in the RRA '93.

Many factors must be considered when determining the amount of the new inclusion. The RRA '93 states that the inclusion shall be the \textit{lessor} of (1) the shareholders pro rata share of excess passive assets less any retained earnings previously included in income due to other passive asset provisions, or (2) the shareholders pro rata \textit{applicable earnings} of the CFC, determined after including the shareholders' income from corporate earnings invested in U.S. property.\textsuperscript{33}

\textit{Excessive passive assets} for the shareholder are determined as the pro rata share of the average passive assets held at the close of each quarter during the year over 25% of the total assets held at the close of each quarter for the CFC.\textsuperscript{34} \textit{Previously taxed income} includes earnings or excess passive assets that were previously included in income due to other passive

\textsuperscript{32} McIntyre, p. 126  
\textsuperscript{33} RRA, p. 147  
\textsuperscript{34} Section 956(c)(1)(A)&(B)
Applicable earnings are the sum of (1) E&P accumulated after September 30, 1993 and, (2) current tax year E&P reduced by (1) distributions made during the tax year and, (2) E&P included in gross income of U.S. shareholders on account of investments of the earnings in U.S. property or investment in excess passive assets to the extent accumulated after September 30, 1993. See Figure 1 for a summary of the calculation.

The provision, as amended by the '93 Act, defines a CFC to include all members of a particular group. A CFC group consists of a chain of CFCs, related by stock ownership and connected by a top tier corporation who also is a CFC. To qualify as a CFC group, the top tier corporation must own directly, by vote or value, greater than 50% the stock of at least one of the CFCs. Also, more than 50% of the value or voting stock of the CFC must be owned by each of the CFCs of the other members of the group.

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35 Section 956(a)(1)(B)
36 Section 956(a)(2)
37 Section 956(d)(2)
38 Section956A(d)(2)(A)&(B)
## Figure 1

### I. (1) Average amount of CFC passive assets at the close of each quarter of such year (use adjusted basis)

(2) Average amount of CFC total assets at the close of each quarter of such year (use adjusted basis)

(3) Multiply (2) by 25%

(4) Subtract (3) from (1), if (3) if > (1) enter 0.

(a) Enter your pro rata share in the CFC. (5) (a)

(b) Multiply (4) by (5) (a)  
This is your pro rata share **EXCESS PASSIVE ASSETS.** (5)(b)

### II.

(6) Enter the amount from line (5) (b)

(7) CFC portion of earnings previously included in income because of excess passive assets.

(8) Subtract (1) from (2)

(9) pro rata share of CFC's applicable earnings after including in the pro rata share of the CFC's increase in earnings invested in U.S. property.

(10) Additional Inclusion = Lessor of (8) or (9) 
This is your **INCLUSION AMOUNT**
The following example demonstrates the calculation of an inclusion using the format in figure 1.

U.S. Smith Corporation owns all of the stock of Katkhuda Corporation (a CFC) in Cairo, Egypt. Average adjusted basis of Katkhuda Corp's passive assets is $500. The average adjusted basis of total assets is $1,500. Katkhuda Corp has accumulated earnings at the end of the tax year of $300. None of this income was Subpart F income or previously included in income under a different provision. $150 of the accumulated earnings were earned after September 30, 1993, and were present at the beginning of the current tax year.

**I.**

1. Average amount of CFC passive assets at the close of each quarter of such year (use adjusted basis)  
   (1) 500.00

2. Average amount of CFC total assets at the close of each quarter of such year (use adjusted basis)  
   (2) 1,500.00

3. Multiply (2) by 25%  
   (3) 375.00

4. Subtract (3) from (1), if (3) if > (1) enter 0.  
   (4) 125.00

5. (a) Enter your pro rata share in the CFC.  
   (5) (a) 100%

   (b) Multiply (4) by (5) (a)  
   This is your pro rata share EXCESS PASSIVE ASSETS.  
   (5)(b) 125.00

**II.**

6. Enter the amount from line (5) (b)  
   (6) 125.00

7. CFC portion of earnings previously included in income because of excess passive assets.  
   (7) 0.00

8. Subtract (7) from (6)  
   (8) 125.00

9. pro rata share of CFC's applicable earnings after including in the pro rata share of the CFC's increase in earnings invested in U.S. property.  
   (9) 150.00

10. Additional Inclusion = Lessor of (8) or (9)  
    This is your INCLUSION AMOUNT  
    (10) 125.00

Upon enactment of RRA '93 Smith Corporation must additionally include the $125 in its income for the tax yr.
Impact

Upon enactment of RRA ‘93, CFC investors who were able to escape any inclusions based on the subpart F rules were now required to reconsider the structure of their investments abroad or incurred taxes previously avoided. Tax accountants advised their clients to identify CFC groups and assess the potential impact of the new anti-deferral rules based on projected earnings and asset values of each CFC group. In addition, the U.S. shareholders were advised to review their foreign tax credit positions in order to determine if U.S. tax on the amount deemed distributed under Section 956(a) would be reduced by the excess foreign tax credits of the shareholder. U.S. shareholders were advised to find means to increase active assets through related party transactions for purpose of eliminating the effects of the 25% asset test.39

Investment in U.S. Property

Based upon the new inclusion for excessive passive assets discussed above, the ‘93 Act modified the formula for determining the inclusion for U.S. shareholders on investments by CFCs in U.S. property. Prior to the ‘93 Act, tax was imposed only on the increase in the earnings of the CFC invested in U.S. property from the prior year. For example, shareholders of a CFC in country Y who invested $500,000 in U.S. property in the prior year, and an additional $300,000 in the current tax year would be taxed on their pro rata share of the $300,000 increase in investment. The tax would be limited to an amount that would have been taxable as a dividend

39 Engle, p.86
had it been distributed at the close of the year.\textsuperscript{40} The reasons for modifying this provision are similar to those given for enacting the excess passive asset inclusion. Congress intended to curtail excessive abuse regarding CFCs investments and subpart rules, creating a calculation that was consistent with the methods used under newly-enacted excess passive assets rules.

The inclusion is now determined as follows:

\begin{table}[h]
\centering
\begin{tabular}{|l|}
\hline
\textbf{U.S property investment inclusion as the lessor of...} \\
\hline
(1) U.S. shareholder pro rata average amount of U.S. property held directly or indirectly by the CFC at the close of each quarter, \textit{less} the E&P attributable to amounts that resulted in an inclusion for investment of earnings in U.S. property, \textit{including} those amounts that would have been included but were attributable to earnings that had been previously taxed as subpart F income. \\
(2) U.S. shareholder share of \textit{applicable earnings} of the CFC (as defined for the inclusion for excess passive assets).\textsuperscript{41} \\
\hline
\end{tabular}
\end{table}

U.S. property includes any tangible property located in the United States, any security issued by a U.S. payer, and use of certain intangible property such as patents, copyrights, secret formulas, designs, and another similar property.\textsuperscript{42} Any property purchased by the CFC prior to its first day as a CFC is not considered for purposes of this modified inclusion for investments in U.S. property. However, this exclusion is permitted until the aggregate amount of property disregarded exceeds the portion of the applicable earnings of CFC before its first day as a CFC.

The Secretary was given the authority by Congress to issue regulations regarding this modification. The provision applies to tax years beginning after September 30, 1993.\textsuperscript{43}

\begin{flushright}
\textsuperscript{40} RIA, p.232 \\
\textsuperscript{41} Act Section 13233(A) & Code Section 956(a)(1) \\
\textsuperscript{42} Section 956(B)(2) \\
\textsuperscript{43} RRA, p. 150
\end{flushright}
Modifications to Subpart F Provisions

Similar to the U.S. property modifications, subpart F income provisions were modified in two areas in order to insure that the subpart F provisions were consistent with the new excess passive asset rules. The first modification dealt with eliminating, in certain cases, the same country income exception, and the second adjustment to the subpart F provisions regarded a simplification of Code Section 960(b) which relates to foreign tax credit limitations. Prior to the '93 Act, the activity illustrated in the next example was allowed.

Jeff Johnson, a United States citizen, owns 20% of German based Schwabendorfer Corporation, a CFC whose foreign personal holding company (FPHC) is also located in Duseldorf, Germany. Jeff is required to include in his U.S. taxable income a portion of the FPHC’s income which includes most dividends, interest, royalties, rents, and annuities. The FPHC received dividends from Frauline Gesellschaft, a subsidiary of Schwabendorfer, operating solely in Germany. The “same country exclusion” allows Jeff to exclude from taxable income his portion of the dividend income received by the FPHC from Frauline because it is (1) related to Schwabendorfer, (2) organized under the laws of the same country as Schwabendorfer, the CFC, and (3) has a substantial part of its business assets located in the same country.

A U.S. shareholder (interest greater than 10%) of the CFC generally must include in taxable income any pro-rata share of foreign personal holding company (FPHC) income earned by the CFC. FPHC income includes any dividend received from the CFC. As is evident in the illustration, prior to RRA '93, the tax code provided an exclusion from FPHC income for dividends received from certain corporations which were related to the CFC, organized under the

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44 RIA, p. 256
laws of the same country as the CFC, and had a substantial part of their business assets located in that country.\textsuperscript{45}

The RRA of '93 eliminated the "same country exclusion" for dividend attributable to earnings and profits accumulated during any period during which the recipient CFC did not own the stock, direct or indirectly, with respect to which the dividends paid.\textsuperscript{46} Therefore, if the dividends were distributed from earnings and profits accumulated when the CFC did not own the stock of the subsidiary, then the same country exception will not apply, and the dividends will be included in the income of the U.S. shareholder. In accordance with the precious example, any portion of dividends received by FPHC from Frauline's earnings and profits accumulated when Schwabendorfer did not own stock is included in Jeff's income. Because of the '93 Act, the "same country exclusion" now applies only to dividends that come out of earnings and profits Frauline accumulated while it was a subsidiary of Schwabendorfer. Administrative costs are going to increase because this requires a CFC and shareholder to prove which dividend come from which earnings and profit.

The second modification to the subpart F provisions deals with the effect on the foreign tax credit limitation of the distribution of earnings that were previously taxed under Section 951, the subpart F provision. As mentioned earlier, an example of earnings that were previously taxed are the inclusions for investments in excess passive assets. Therefore, some income, even before it is distributed, is included in the taxable income of the U.S. shareholder of a CFC.

\textsuperscript{45} RIA, p. 255
\textsuperscript{46} Act Section 13233(a)
A foreign tax credit, with limitation, is available for foreign taxes paid by the CFC on earnings and profits. When such previously taxed earnings are finally distributed, a “direct credit” is also available for any additional taxes, such as a withholding tax imposed on the distribution itself rather than the accumulation.47 When the CFC makes a distribution, the shareholder may increase its foreign tax credit limitation in the year of distribution when the following three requirements are met:

- taxpayer elected to claim credit, instead of a deduction, for any taxes paid in the year or accrued in any year the CFC was taxed to the shareholder
- the taxpayer elects to claim credit, instead of deduction, for foreign taxes paid or accrued in year of distribution, and
- foreign taxes are paid or accrued in the year of distribution with respect to the distribution.1

The purpose for allowing an increase in the foreign tax credit is to avoid a situation where a CFC distributes a dividend to a U.S. shareholder not able to claim a credit for foreign taxes paid with respect to the distribution. For example, a foreign country might impose its own withholding tax on “outbound” dividends even when no U.S. withholding tax (30%) is imposed.48

Prior to the ‘93 Act, the amount of the increase in limitation was measured separately for each CFC each year, with separate foreign tax credit limitations. The increase of sequel to: (1) the amount by which, in the year the distributed earnings were earned, the taxpayer’s foreign tax credit limitation was increased on account of the inclusion under the CFC rules, over (2) the

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47 RIA, p. 255
48 RIA, p.233
amount of foreign taxes actually creditable in that earlier year on account of such inclusion of income.\textsuperscript{49}

The '93 Act simplified determination of the amount of increase by first eliminating the need for separate calculations for each CFC. Second, the amount is now determined as the lesser of (1) the amount of foreign income, war profits or excess profits taxes paid, deemed paid or accrued with respect to the distributions, or (2) the amount for the taxpayer's excess limitation account as of the beginning of the taxable year.\textsuperscript{50}

An \textit{excess limitation account} will be maintained for each shareholder who (1) elected to claim a credit for foreign taxes paid or accrued in any taxable year beginning after September 30, 1993, in which he was required to include in income any amounts under the CFC rules, or (2) did not pay or accrue any income, war profits or excess profit taxes paid to any foreign country or U.S. possession in any such year.\textsuperscript{51}

The account is increased by the excess of the amount by which the taxpayer's foreign tax credit limitation for such a year is increased on account of the total amount of the inclusions of income under the CFC, over the amount of taxes actually "creditable" in that earlier year on account of such inclusion in income.\textsuperscript{52} Similarly, this account is decreased to the extent amounts are applied to increase the shareholder's foreign tax credit on account of the portion of distributions previously taxed, and to the extent there is an increase in the foreign tax credit allocable by reason of a carryback, if the increase would not have been allowable but for the

\textsuperscript{49} Engle, p. 148
\textsuperscript{50} Act Section 13233(b)(1)
\textsuperscript{51} Section 960(b)(2)(A)
\textsuperscript{52} Section 960(b)(2)(B)(ii)
inclusion of income of an amount under the CFC rules.\textsuperscript{53} The example below illustrates calculation of the amount of increase in the limitation amount under '93 Act modifications.

\begin{center}
\textbf{Example: Skadarlija Inc., a CFC established during the war in former Yugoslavia is an import/export organization. Miroslav, a Serbian-American, is a U.S. shareholder who owns 40\% of Skadarlija. Miroslav received a distribution from Skadarlija of $10,000 which was taxed by the Serbian government on account of the corporation's "war profiting". In addition, in a prior year, the $10,000 was taxed and included in Miroslav's taxable income because of Skadarlija's investment in excessive passive assets (Subpart F provisions). From last year the excess limitation account had a balance of $1,800. Total tax paid by Miroslav with regards to this year's distribution of $2,500. Miroslav's foreign tax credit limitation is increased by $1,800 the lessor of the amount of taxes paid, deemed paid, or accrued ($2,500) or the amount in the excess limitation account at the beginning of the tax year ($1,800).}
\end{center}

This section was modified primarily to prevent a CFC shareholder from losing foreign tax credits for foreign withholding taxes imposed on distributions of previously taxed income. In the above example, the $10,000 distribution was previously taxed due to subpart F provisions. In addition, the "outbound" distribution was taxed. If this provision did not exist then the shareholder would be taxed twice on the same income without foreign tax credit relief. The '93 Act merely simplified determination of the increase in limitation amount.

\textsuperscript{53} Section 960(b)(2)(B)&(C)
Foreign Tax Credit/Sourcing

III.

The final three modifications made to international corporate taxation by the Revenue Reconciliation Act of 1993 affect the foreign tax credit and sourcing rules. The changes involve the allocation of research and experimental expenditures, the working capital exception for oil, gas, and shipping income, and the treatment of the export of certain softwood logs. The changes made to this section are minor in comparison to the first two parts.

Allocation of R&D Expenditures (effects of foreign tax credit)

General

A U.S. citizen or resident who incurs or pays income taxes to a foreign country on income subject to U.S. tax may be able to claim deductions or credits against U.S. income tax. The more foreign expenditures incurred, the less foreign taxable income realized and foreign taxes paid, but the smaller the foreign tax credit. For this reason, most U.S. taxpayers would prefer to deduct all R&D expenses from U.S. taxable income, thus reducing taxable income in the U.S. and increasing foreign income for which the foreign tax credit would be available anyway. Naturally, the Service does not allow such abuse.

Prior to the '93 Act, qualified R&D, made solely to meet legal requirements imposed by a government for improvement or marketing of specific products or processes which cannot yield income beyond minimal amounts outside government jurisdiction, is allocated only to that source.

54 Sections 27, 164 & 901-905
Therefore, if the R&D expense is a governmental requirement intended to only benefit the particular country, the whole deduction should be allowed against the income applicable. When provisions were initially created in 1977 with regards to R&D allocations, R&D, other than the governmental requirement mentioned above, were 64% attributable to activities conducted in the U.S. and allocated in apportionment to U.S. source income. Similarly, 64% of R&D attributable to activities conducted in a foreign country were allocated and apportioned to foreign source income. Any remaining R&D expense was apportioned on a basis of either gross sales or gross income, and if gross income was used, at least 30% of R&D that would have been allocated if gross sales was used would be allocated to foreign source income. Regulation Section 1.86108 was created in 1977 to provide rules for these allocations.

**Impact**

Up until 1981 Congress enacted many temporary modifications to the above regulation. In 1989, Code Section 864(f) was enacted, which changed the 64% requirement to 50%, and was to apply until June, 1991. In 1992, the IRS issued Revenue Procedure 92-56 which extended the 1989 864(f) section for the last six months of 1991 and through the 1993 tax year. For this twelve year period, Congress, the IRS, and industry representatives studied the R&D allocation rules and the impact of the various changes on the foreign tax credit. They concluded nothing. “No unambiguous recommendation exists on the appropriates of allocating U.S. based research

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expense to U.S. source income either under 1977 Regulations or the 1981 temporary modifications.\textsuperscript{59}

Taxpayers were confused and uncertain as to the future of R&D allocation and how Congress would choose to treat it. They did not know what to expect and thus experience difficulty in planning for such expenditures. Congress noted in the conference report that the uncertainty with regards to this area would not last long, and that they were not ready to make any changes. Thus, the ‘93 Act extended the 864(f) 50% rules for an additional year.\textsuperscript{60} ‘93 Act Section 13234 extended the provisions and granted regulatory authority to the IRS to prescribe Regulations to carry out the rules.

Being that the focus of the RRA ‘93 international taxation changes were not modified in favor of foreign activity, the Treasury hesitated to allow all R&D expense to be deducted from U.S. source income to deter tax avoidance schemes, as stated earlier. A majority of R&D is performed in the U.S. and to allow deductions solely against foreign source income would not make economical sense.\textsuperscript{61}

**Working Capital Exception for Oil, Gas, and Shipping Income**

**Repealed**

Abuse of foreign tax credits for tax avoidance schemes would be prevalent without provisions such as the three mentioned in this section, including the foreign tax credit limitation which is calculated as follows:

\textsuperscript{59} S. Rept, p. 350  
\textsuperscript{60} S. Rept, p. 350  
\textsuperscript{61} Hoffman, p. 9-23
The amount of the limitation can be manipulated in many ways. For example, a U.S. taxpayer that wants to increase his foreign tax credit limitation could obtain income from foreign sources where there is no, or low foreign tax on the income. The Code and the IRS have cushioned themselves against the clever taxpayer.

The foreign tax credit limitation illustrated above is calculation separately for eight specific categories, and items that do not fall into these special categories are included in a general or residual limitation calculation. An example of these special categories is the passive income foreign tax credit limitation calculation which includes income not subject to high levels of foreign tax. Congress included the low taxed income in this category to avoid the manipulation described earlier.

Why have separate FTC limitation calculations? As stated in the conference report, “it prevents crediting high foreign taxes on income in the ‘general category’ against residual U.S. tax on passive income.” Prior to the ‘93 Act, the passive income category included foreign personal holding company income like dividends and interest, but did not include shipping income or foreign oil and gas extraction income. This separate limitation for passive income was enacted in 1986 and replaced what used to be just a separate limitation calculation for passive interest income, which excluded interest on certain types of interest on working capital. The 1986

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62 Section 904(d)

63 Section 904(d)
changes eliminated this passive interest income category and its exclusion, but for the working capital exception which was maintained for oil, gas, and shipping income.

Therefore, the passive income separate calculation still did not include working capital interest for shipping, oil, and gas income. However, Congress wanted fair treatment for people in the foreign shipping, oil and gas industries and therefore included the working capital interest in passive income separate calculation. The '93 Act put certain passive income related to oil, gas, and shipping operations in passive category for the foreign tax credit limit purpose in all instances.

Taxpayers were quick to inquire about new opportunities in the oil and gas industry. "I expect my wealthier clients will be looking at a lot of oil and gas shelters again. I'm sure that going to be coming across my desk in droves. We'll get our saving in little, little bites, more of the gimmicky thing, the timing issue," said Michael J. Knight, CPA of MJK & Co. in Fairfield, Connecticut.

**Treatment of Export of Certain Softwood Logs**

Foreign sales corporations (FSC) may exclude part of foreign trade income from U.S. federal tax. If the income earned by the FSC is determined under special administrative pricing rules, then where there are corporate FSC shareholders, the exempt foreign trade income is 15/23 of the foreign trade income derived from the transaction. A U.S. shareholder is allowed a 100% dividends received deduction for dividend from the FSC out of earnings and profits attributable to foreign trade income, and therefore no tax is imposed on part of the FSC's income from exports.

The foreign trade income on exports includes property:

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64 RIA, p. 267
65 Act Section 13239(a)
• in the hands of any person (whether or not a FSC)
• manufactured, produced, or grown or extracted in the U.S. by a person other than a FSC
• held primarily for sale, lease, or rental, in the ordinary course of trade or business by, or to a FSC for direct use, consumption, or disposition outside the U.S.
• not more than 50% of the fair market value of which is attributable to articles imported in the U.S.

Congress was concerned about the rapid deterioration of the natural forests and thus excluded unprocessed timber (soft wood) from the definition of export property described above. The modification was effective after the date of enactment of the RRA. The actual impact of this change on timber exporters and on the environment will be more accurately determined in the future.

"Since the early 60’s US Multinationals have had to cope with subpart F, an anti-deferral regime. The 86’ Act introduced the Passive Foreign Investment Company (PRICE) rules, yet another anti-deferral regime. The 93’ Act introduced the Excess Passive Asset (EPA) rules, yet another anti-deferral regime. Unfortunately, the Subpart F, PFIC and EPA rules all overlap with respect to U.S. Multinationals. Instead of following one set of rules, they now have to follow three sets of rules," states Debra Jung from Coopers & Lybrand concluding the overall affect of the modifications.
In retrospect, the past three years alone demonstrate how the new provision carved many different tax planning paths for diverse taxpaying entities. Whether or not the international provisions created "overlapping tax regimes" also depends upon the affected party. Some taxpayers needed to undergo major tax planning "re-engineering" while others were merely slapped with additional compliance burdens.

Whether or not Congress accomplished the intended goals of (1) taxing the rich, (2) reducing the deficit, and (3) stimulating the economy, depends upon who you ask or from what angle these goals are approached, and most professional responded negatively with regards to the '93 Act. These tax practitioners and many economists fear that the changes will danger foreign investment, but my research has revealed that instead of bailing out, investors merely devised new schemes to defeat the provisions. How long will it be until Congress pushes through yet another set of modifications? As the international borders between countries continue to fade, and the economy continues to globalize, instead of creating stricter international tax provisions in the future, Congress should consider the long-term affects of not maintaining tax law consistent with the global movement.
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