

United States Senate  
WASHINGTON, DC 20510

October 11, 2016

The Honorable Shaun Donovan  
Director  
Office of Management and Budget (OMB)  
725 17<sup>th</sup> Street, N.W.  
Washington, DC 20503

Re: Proposed Regulations under Internal Revenue Code Section 385 (REG-108060-15)

Dear Director Donovan:

It is our understanding that the Treasury Department submitted final debt-equity regulations under Internal Revenue Code section 385 to the Office of Management and Budget's Office of Information and Regulatory Affairs (OIRA) for review on September 30, 2016. We are alarmed with the Treasury Department's plan to "move swiftly to finalize" these complex rules, especially when economic growth remains anemic in the U.S. We urge you to delay approving the section 385 rules until the economic impact of these regulations can be fully assessed.

As members of Senate Committee on Finance, we have repeatedly contacted the Treasury Department expressing our deep concerns over the far-reaching impact of the proposed rules under section 385 on job growth, global competitiveness, and capital investment. Since April, we have met with stakeholders, business associations, and small businesses regarding the broad impact these rules would have on jobs and economic growth in our home states, nationally, and abroad. Despite providing ample time to address our concerns, we have yet to receive a substantial response from the Treasury Department on what significant reforms, if any, this agency will implement to fix the proposed rules. Due to the Treasury Department's lack of transparency with respect to these proposed regulations, there remains a great deal of doubt whether Treasury will take into account our concerns.

Additionally, according to some estimates, over ten million intercompany debt-equity transactions would now be subject to documentation requirements, significantly increasing the cost of doing business in the U.S. Per our letter to the Treasury Department on July 1, 2016, as enclosed, we requested an extended comment period along with a thorough review of all stakeholders' comments and concerns. Considering the thousands of pages that have been submitted, we remain concerned whether a thorough vetting has taken place in such a short period of time.

Further, under Executive Order 12866, the proposed regulations were deemed recently to be economically significant, meaning they would have an annual effect of \$100 million or more on

the economy. OMB previously estimated the proposed regulations would impose a cost of almost \$1 billion annually. After extensive conversations with small businesses, multinational companies, and foreign businesses that support numerous jobs across the nation, we believe this number is grossly understated. Additionally, we believe these proposed rules are already creating obstacles to job creation, impeding economic growth and increasing the cost of doing business, given the retroactive nature of these proposed rules.

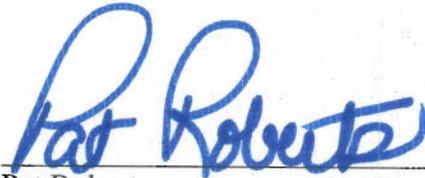
Should your agency decide to approve the section 385 rules, we urge your agency, at a minimum, to exempt cash pooling transactions, foreign-to-foreign transactions and domestic-to-domestic transactions. Additionally, we urge you to exempt industries that are subject to regulatory review. We also urge you to consider the increased cost of compliance to millions of small businesses, both nationally and internationally, who have intercompany loans and cannot meet the burdensome documentation requirements. We also detailed these concerns in the July 1, 2016, letter to the Treasury.

Thank you for your attention to this matter. We respectfully request a response to our concerns, **before you approve the rules or by October 25, 2016.**

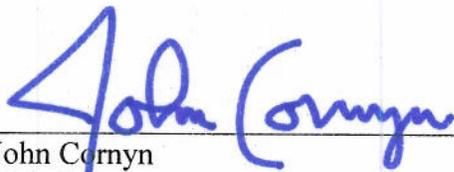
Sincerely,



Dean Heller  
U.S. Senator



Pat Roberts  
U.S. Senator



John Cornyn  
U.S. Senator



Johnny Isakson  
U.S. Senator



Tim Scott  
U.S. Senator



Mike Crapo  
U.S. Senator

CC: The Honorable Jacob Lew, Secretary of the Treasury, U.S. Department of the Treasury

The Honorable Mark J. Mazur, Assistant Secretary for Tax Policy, U.S. Department of the Treasury

Mr. Robert B. Stack, Deputy Assistant Secretary (International Tax Affairs), U.S. Department of the Treasury

Ms. Emily S. McMahon, Deputy Assistant Secretary (Tax Policy), U.S. Department of the Treasury

United States Senate  
WASHINGTON, DC 20510

July 1, 2016

The Honorable Jacob Lew  
Secretary of the Treasury  
U.S. Department of the Treasury  
1500 Pennsylvania Avenue, NW  
Washington, DC 20220

Re: Proposed Regulations under Internal Revenue Code section 385 (REG-108060-15)

Dear Secretary Lew:

As supporters of overhauling our broken tax code, we strongly believe that tax reform, done the right way, can promote job growth and strengthen our nation's global competitiveness. Given our concerns over job growth and global competitiveness, we are deeply concerned with the Treasury Department's proposed debt-equity regulations under Internal Revenue Code section 385 (the "proposed regulations")<sup>1</sup> that were released on April 4, 2016. We write today to detail our concerns over the proposed regulations and request that you work with us to address the series of issues discussed in this letter.

In particular, we ask that you take the following steps:

1. Extend the July 7, 2016, comment period deadline to at least October 5, 2016;
2. Consider the comments and feedback you have received through the extended comment period; and
3. Change the effective date for these rules so that they would apply to debt instruments issued, or deemed issued, no sooner than 90 days after the date the regulations are issued in final form.

Over the past few months, we have heard from numerous stakeholders, including small businesses, business associations, and companies with operations in our home states that would be impacted if the proposed regulations are implemented without

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<sup>1</sup> REG-108060-15, available at: <https://www.regulations.gov/docket?D=IRS-2016-0014>

significant alterations. We respectfully request that, at a minimum, you substantially modify the proposed rules so that ordinary business transactions unrelated to tax avoidance are not adversely affected by the broad scope of these proposed rules. Additionally, we are alarmed with your plan to “move swiftly to finalize” these proposed regulations, which in current form would provide a stark impediment to jobs and capital investment. The Treasury Department’s apparent haste to finalize these complex rules is especially troubling given that economic growth remains anemic. Simply put, we believe finalizing these regulations will create new disincentives to investment in the United States and threaten to further exacerbate our current economic woes.

According to the Preamble of the proposed regulations, the intent of these rules was “motivated in part by the enhanced incentives for related parties to engage in transactions that result in excessive indebtedness in the cross-border context.” While we share your concern regarding erosion of the U.S. tax base, the proposed regulations are far broader than the types of cross-border transactions associated with “earnings stripping.” Unlike the other regulations issued by Treasury on April 4, 2016, that directly relate to corporate tax inversions, the proposed section 385 regulations represent a fundamental shift in how debt and equity are characterized, with far-reaching implications for a wide range of American businesses. Far from the stated intent of addressing abusive tax transactions, we are concerned that the actual effect of these regulations will be to drive investment and capital outside of America’s borders, further eroding the U.S. tax base. In our view, creating obstacles to job creation and impeding economic growth should not be the outcome of any proposed Treasury regulations.

We commend the House Ways and Means Committee for demonstrating bipartisan concern with the proposed rules. In fact, the letter written by Democratic members of the Committee dated June 22, 2016, calls for addressing many of our own concerns because the proposed regulations would “adversely affect ordinary course business transactions between related parties lacking tax avoidance motives.”

Below are just a few of the concerns we have repeatedly heard from stakeholders regarding these regulations. We note this is not an exhaustive list. In addition to the other critical issues that have been raised, we expect to see—at the very least—the following reforms should Treasury decide to finalize the proposed regulations:

- Ensure that S corporations, a critical component of America’s small business community, do not lose their S corporation tax status by virtue of having their

debt re-characterized as equity and are not penalized for their domestic-to-domestic transactions;

- Ensure that non-tax motivated cash management techniques, such as cash pooling or revolving credit arrangements, are exempted;
- Exempt foreign-to-foreign transactions from the scope of the proposed regulations;
- Address the “cascading effect” of the currently drafted regulations, where a single tainted transaction funded with intercompany debt can create a multitude of additional tainted transactions;
- Extend the 30-day deadline for meeting the documentation requirements;
- Expand the \$50 million intercompany debt threshold so that more small businesses will be exempt from these rules;
- Ensure the regulations take into account the global economic and regulatory environment in which regulated financial groups operate; and
- Ensure that local interest deductions for U.S. multinational businesses are not eliminated under the OECD BEPS hybrid transaction concepts.

Given the scope of the proposed rules, we, like businesses large and small across America, are still analyzing the potential impact these rules could have on business operations. As you know, Treasury’s intention to issue such broad-ranging rules under section 385 was not included in the most recent Treasury Priority Guidance Plan, as would normally be the case. As a result, many businesses have only recently become aware of how these far-reaching and complex regulations will impact their daily business activities. Given the broad range of issues that are already disrupting ordinary business operations, we ask that you extend the July 7, 2016, comment period and change the effective date of the proposed debt-equity rules to a date that is 90 days after the regulations are finalized. Additionally, considering your expedited scheduling of the July 14, 2016, public hearing on the proposed regulations, we respectfully request you make a thorough review of any public comments, including those from congressional lawmakers, before finalizing any rules.

Please know we are prepared to work with the Treasury Department in any way to improve America’s global competitiveness and promote more robust job creation. Unfortunately, the proposed regulations, as drafted, appear to head in exactly the opposite direction, imposing unnecessary costs on American businesses at precisely the time when our economy is already overburdened by excessive regulation. While we believe a better approach would be to focus on a more narrowly-tailored effort to target those tax transactions that are actually abusive, we

urge you to—at a minimum—address the concerns raised in this letter should Treasury insist on finalizing the proposed regulations. We respectfully request a response to our concerns by July 15, 2016.

Sincerely,



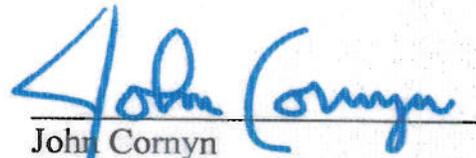
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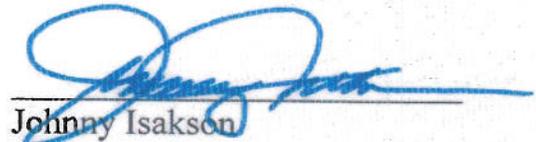
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