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July 7, 2016

Comments to the Department of the Treasury and Internal Revenue Service on Proposed Regulations to Prevent Earnings Stripping

Re: Proposed Rulemaking on Treatment of Certain Interests in Corporations as Stock or Indebtedness (REG-108060-15)

I am writing in support of the proposed regulations to address earnings stripping under Internal Revenue Code Section 385. Earnings stripping is a type of tax avoidance available to U.S. corporations that are foreign-owned or that use inversions to characterize themselves as foreign-owned.

To take a simple example, an American company could trim its future U.S. profits by ostensibly borrowing from its foreign parent company, which could be based in a country with a much lower corporate tax rate. Often, the American company does not actually borrow any money but just distributes a note and makes interest payments. The American company tells the IRS that it has little income to report because of the interest payments it made to the foreign company that holds the note. This, in effect, shifts its profits out of the United States. The companies involved are all related and acting in reality as one company, so the “debt” between them is merely an accounting gimmick to avoid U.S. taxes.

The Corporate Tax Dodging Prevention Act, which I introduced in the Senate last year, includes a provision that would crack down on earnings stripping and is similar to the one included in the President’s budget proposal. Given Congress’s failure to enact such legislation, the Treasury Department is appropriately working to ensure that, at the very least, existing law is applied using the authority Congress has already provided to address this problem.

The law authorizes the Secretary “to determine whether an interest in a corporation is to be treated for purposes of this title as stock or indebtedness (or as in part stock and in part indebtedness).” The proposed regulations would essentially treat some of the intercompany “debt” in these situations as stock (meaning payments by the American company are dividends, which cannot be deducted, rather than interest payments). The proposed regulations focus only on the most blatant abuses in which the “debt” is clearly an accounting gimmick or unsubstantiated.

I applaud the Treasury Department and encourage it to continue using its untapped authority to address earnings stripping. I look forward to working with the Department in the future to address this and other problems in our tax code.

Sincerely,

A handwritten signature in blue ink, appearing to read "Bernard Sanders". The signature is fluid and cursive, with the first name "Bernard" and last name "Sanders" clearly distinguishable.

Bernard Sanders,
United States Senator