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IRS Enhances Opportunity for U.S. Multinationals to Access Cash from Controlled Foreign Corporations

On October 3, 2008, the U.S. Internal Revenue Service issued Notice 2008-91, which enhances the ability of a controlled foreign corporation ("CFC") to make short-term loans to its U.S. parent to fund operations without creating an income inclusion for U.S. federal income tax purposes. The Notice applies for a CFC's first two taxable years ending after October 3, 2008. Thus, for a CFC with a calendar taxable year, the Notice applies for calendar years 2008 and 2009.

CURRENT LAW

Generally, under Internal Revenue Code ("Code") section 956, a loan made from a CFC to its U.S. parent is considered to be an investment in U.S. property because the CFC holds an "obligation" of the U.S. parent. Under this Code section, the average amount of the CFC's investment in U.S. property held at the end of each quarter of the taxable year is potentially treated as a "deemed dividend" to the U.S. parent and, thus, taxable on the U.S. parent's federal income tax return.

In some circumstances, however, the U.S. parent can have a loan outstanding from its CFC without triggering any income inclusion. Under Notice 88-108, for example, even if a CFC makes a loan to its U.S. parent that extends over a quarter end, there should be no income inclusion provided that this loan is outstanding less than 30 days. But to the extent the CFC held any number of obligations that would constitute U.S. property for aggregate periods totaling 60 or more days during a taxable year, this 30 day exception would not apply.

NOTICE 2008-91

In Notice 2008-91, the IRS has supplemented Notice 88-108 so that a loan from a CFC to its U.S. parent would only constitute an obligation that results in an income inclusion if the loan is held for more than 60 days from the time it is incurred. Notice 2008-91 further provides that if a CFC holds obligations that would constitute U.S. property for 180 or more days cumulatively during a taxable year, then this 60 day exception would not apply.

Thus, Notice 2008-91 effectively extends the periods within which a taxpayer can hold an obligation without triggering the application of Code section 956. A CFC can apply Notice 2008-91 or Notice 88-108, but not both.

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According to Notice 2008-91, the IRS issued this Notice “to facilitate liquidity in the near term” and to announce its intention to issue regulations under Code section 956(e). In issuing the Notice, the IRS recognizes that current market conditions have made funding operations more difficult for many U.S. multinationals. Therefore, provided that the specified time limits are followed, Notice 2008-91 presents a new and previously unavailable opportunity for a U.S. multinational that needs to finance its operations on a short-term basis.