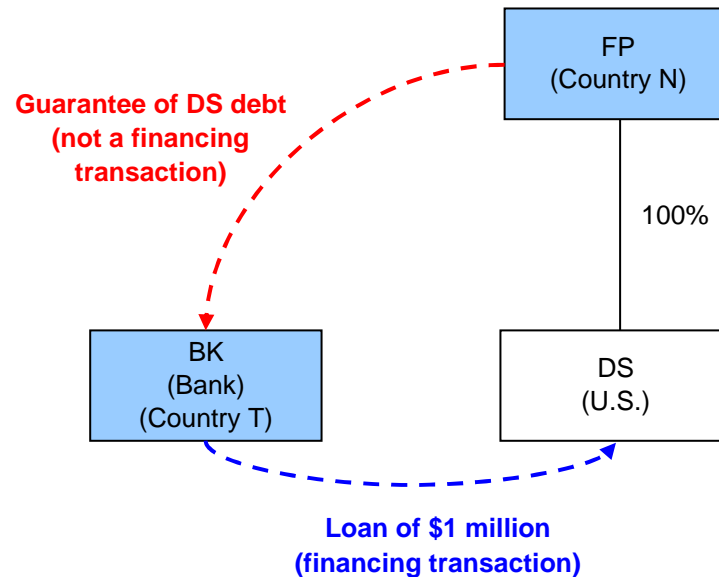


Reg. 1.881-3(e), Example 1 (Conduit Financing Arrangements)

Guarantee of Bank Debt Does Not Create A Financing Arrangement

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FP, a corporation organized in country N, owns all of the stock of DS, a corporation organized in the United States. Country T, but not country N, has an income tax treaty with the United States. The treaty exempts interest, rents and royalties paid by a resident of one state (the source state) to a resident of the other state from tax in the source state.

BK, a bank organized in country T, lends \$1,000,000 to DS in exchange for a note issued by DS. FP guarantees to BK that DS will satisfy its repayment obligation on the loan. There are no other transactions between FP and BK. BK's loan to DS is a "financing transaction". FP's guarantee of DS's repayment obligation is not a financing transaction. Therefore, these transactions do not constitute a financing arrangement.

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