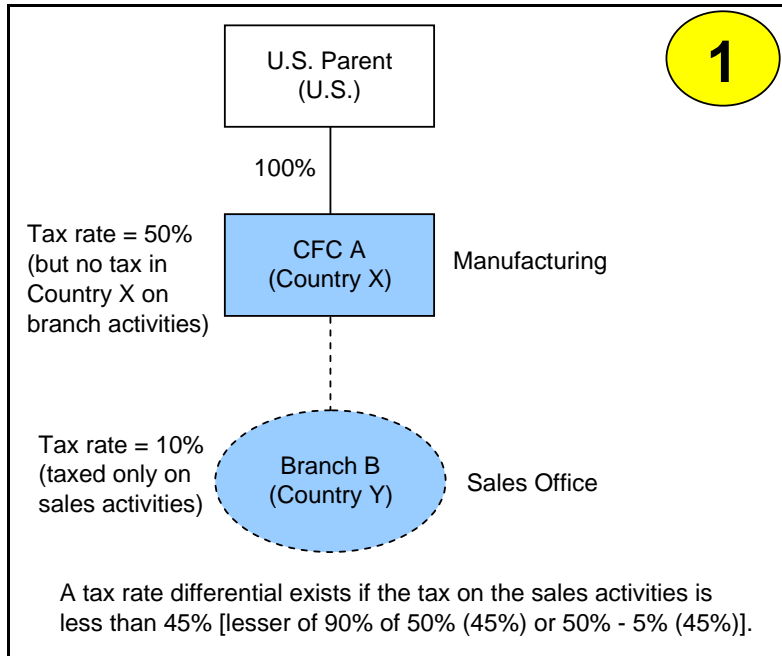
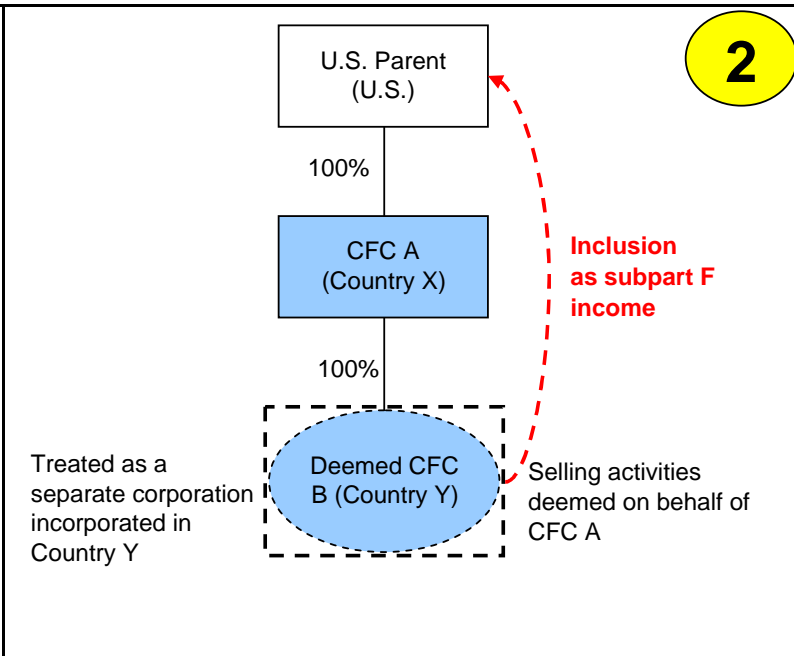


Sales Branch with Tax Rate Differential

Initial Structure



Subpart F Income under the Branch Rule



Controlled foreign corporation A, incorporated under the laws of foreign country X, is engaged in the manufacturing business in such country. Corporation A negotiates sales of its products for use outside of country X through a sales office, branch B, maintained in foreign country Y. These activities constitute the only activities of A Corporation. Country X levies an income tax at an effective rate of 50% on the income of A Corporation derived by the manufacturing plant in country X but does not tax the sales of income of A Corporation derived by branch B in country Y. Country Y levies an income tax at an effective rate of 10% on the sales income derived by branch B but does not tax the income of A Corporation derived by the manufacturing plant in country X. If the sales income derived by branch B were, under the laws of country X, derived from sources within country X by A Corporation, such income would be taxed by such country at an effective rate of 50%. In determining foreign base company sales income of A Corporation, branch B is treated as a separate wholly owned subsidiary corporation of A Corporation, the 10% rate of tax on branch B's income being less than 90% of, and at least 5 percentage points less than, the 50% rate. Income derived by branch B, treated as a separate corporation, from the sale by or through it for use, consumption, or disposition outside country Y of the personal property produced in country X is treated as income from the sale of personal property on behalf of A Corporation, a related person, and constitutes foreign base company sales income. The remainder of A Corporation, treated as a separate corporation, derives no foreign base company sales income since it produces the product which is sold.