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

Initial Loan (Jan. 1, 1996)  

1  

FP (Country N)  

100%  

Loan of $1 million  

FS (Country T)  

100%  

DS (U.S.)  

FP, a corporation organized in country N, owns all of the stock of FS, a corporation organized in country T, and 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. FS is an entity that is disregarded as an entity separate from its owner under Reg. 301.7701-3.

On January 1, 1996, FP lends $1,000,000 to DS in exchange for a note issued by DS. On January 1, 1997, FP assigns the DS note to FS in exchange for a note issued by FS. After receiving notice of the assignment, DS remits payments due under its note to FS. FS, as a disregarded entity, is a person and therefore may itself be an intermediate entity that is linked by financing transactions to other persons in a financing arrangement. The DS note held by FS and the FS note held by FP are financing transactions and together constitute a financing arrangement.

Fin. Transaction + Fin. Transaction = Fin. Arrangement

FP (Country N)

FS (Country T)

DS (U.S.)

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