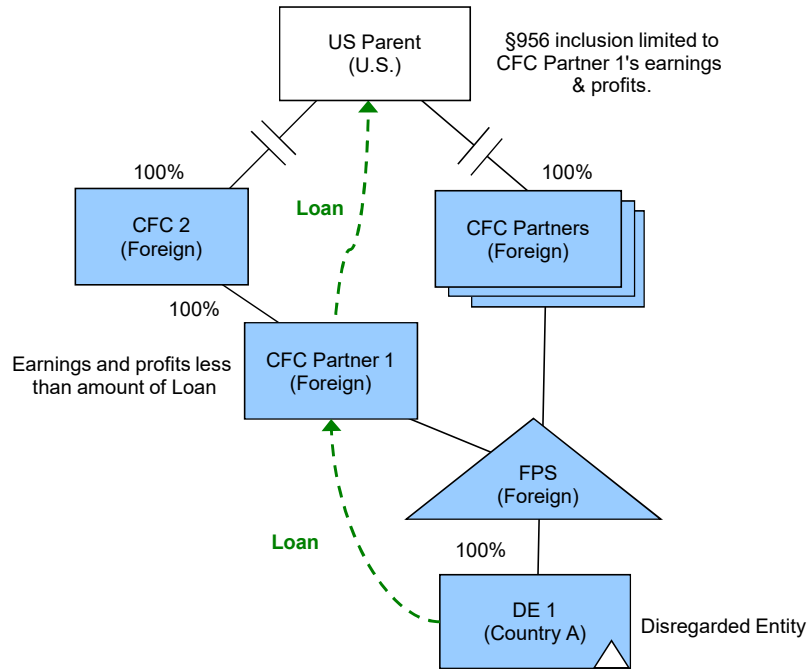
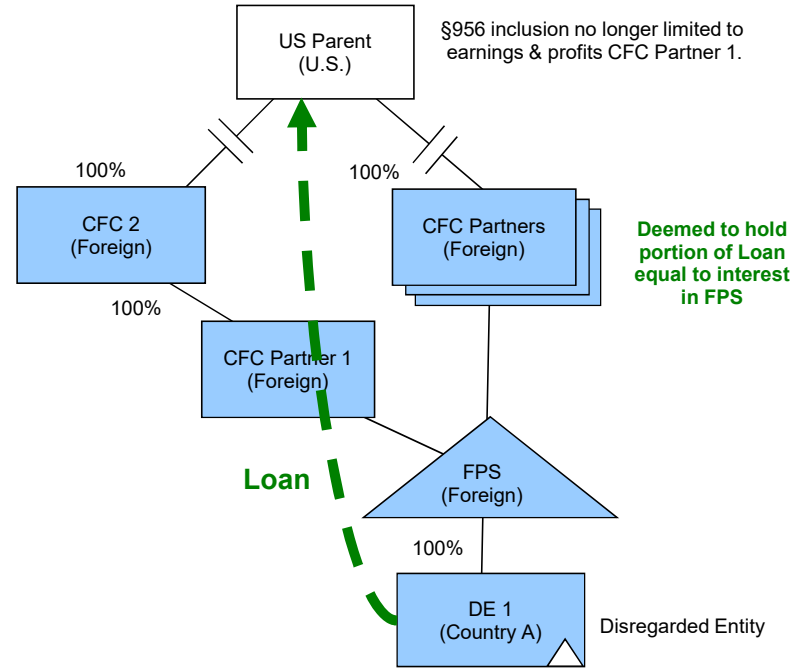


**Back to Back Loans**



**Deemed Transaction**



US Parent indirectly wholly owned CFC Partner 1 and CFC Partners. DE 1, a disregarded entity of FPS, a foreign partnership, made a loan of cash to CFC Partner 1. CFC Partner 1 then loaned that amount to US Parent. US Parent included in its income the Code §956 amount related to the loan from CFC Partner 1. CFC Partner 1 had limited earnings and profits, so the amount of the inclusion was limited to CFC Partner 1's earnings and profits.

Treas. Reg. §1.956-1T(b)(4) provides that:

[A] controlled foreign corporation will be considered to hold indirectly... investments in U.S. property acquired by any other foreign corporation that is controlled by the controlled foreign corporation, if one of the principal purposes for creating, organizing, or funding (through capital contributions or debt) such other foreign corporation is to avoid the application of Code §956 with respect to the controlled foreign corporation. For purposes of this paragraph (b), a foreign corporation will be controlled by the controlled foreign corporation if the foreign corporation and the controlled foreign corporation are related parties under Code §267(b).

Treas. Reg. §1.956-2(a)(3) provides that if a CFC is a partner in a partnership that owns property that would be U.S. property if owned directly by the CFC, the CFC will be treated as holding an interest in the property equal to its interest in the partnership and such interest will be treated as U.S. property.

The IRS argued, among other things: (1) CFC Partner 1 is controlled by the CFC Partners for purposes of Treas. Reg. §1.956-1T(b)(4); (2) CFC Partner 1 was funded by the loan; and (3) a principal purpose of funding CFC Partner 1 was to avoid the application of Code §956 with respect to the CFC Partners. Therefore, CFC Partners were deemed to hold a portion of the loan, and US Parent's Code §956 inclusion was not limited by CFC Partner 1's earnings and profits.