# COMMITTEE ON WAYS AND MEANS

**U.S. HOUSE OF REPRESENTATIVES**
**WASHINGTON, DC 20515**

August 22, 2016

The Honorable Jacob Lew
United States Treasury Secretary
U.S. Department of the Treasury
1500 Pennsylvania Ave., N.W.
Washington, D.C. 20220

Dear Secretary Lew:

We are writing to continue the discussion about the proposed Section 385 regulations (the "proposed regulations") released by the Treasury Department on April 4, 2016. On June 28, 2016, we sent you a letter expressing our grave concern about the proposed regulations, citing the broad scope of the rules and their negative effect on the ability of companies to engage in normal business activities. Several of our Democrat colleagues sent you a letter in June as well, similarly noting the potential for "unforeseen circumstances in which the regulations could adversely affect ordinary course business transactions between related parties in the absence of tax avoidance motives." On July 6, 2016, Members of both the Committee on Ways and Means and the Senate Committee on Finance discussed our concerns with your tax policy team, highlighting the many ways the regulations as proposed would prevent American businesses from conducting basic, day-to-day operations and transactions. The bottom line is that this proposal ultimately would make it harder for businesses to headquarter and invest in the United States and to hire American workers.

We appreciate the Treasury Department's expressed commitment to making modifications to address some of the identified adverse effects of the proposed regulations. However, based on the information provided by Treasury to date, we are not confident that any such modifications would be sufficient to eliminate the harm that the proposed regulations would inflict on businesses and American workers if they were to be finalized in their current form. Overall, the joint Ways and Means and Finance Committee discussion with your tax policy team reinforced our view that, at a minimum, a complete overhaul of the current proposal would be necessary in order to ensure that any rules in this area appropriately target abusive tax-planning without interfering with normal business financing arrangements. Unfortunately, the clear message from your tax policy team was a single-minded intention to finalize the regulations "swiftly." As we emphasized at the July 6 discussion, the American people deserve a tax system that reflects accuracy and correct policy, not rules that are rushed out without proper vetting and consideration.

During our July 6 discussion, your tax policy team specifically acknowledged several unintended consequences of the proposed regulations that they intend to rectify before the regulations are finalized. The areas where the Treasury Department committed to making changes include:

- Providing an exclusion for cash pooling arrangements;
- Providing exceptions for broader cash management practices including currency and interest-rate hedging;
- Eliminating any adverse impact on S corporation and REIT status;
- Providing exceptions for equity compensation;
- Extending the consolidated group exception to industries such as insurance for which consolidation is restricted; and
- Providing exceptions for regulated industries that are subject to capital and debt requirements

These areas are all complex and it is not clear that your tax policy team has identified specific solutions that would appropriately and fully resolve these fundamental problems with the proposed regulations. We urge you to adopt an open and transparent process, with engagement with stakeholders and the Congressional tax-writing committees. Obtaining and incorporating input from affected stakeholders in order to have confidence that the rules as recrafted would operate properly is too important to risk acting in haste.

In addition, there are multiple areas of concern that the Treasury Department did not adequately address during our July 6 discussion. These issues involve negative unintended consequences for businesses that have no connection to the inversion transactions that Treasury asserts are the intended target of the regulations, including:

- The treatment of longer-term cash and financial management arrangements and transactions;
- The implications for foreign-to-foreign transactions;
- The effect on transactions involving partnerships and disregarded entities; and
- The compliance burden of the documentation requirements.

It is critical that Treasury commit to addressing these areas before the regulations are finalized. This will require thoroughly studying these issues and working with stakeholders and with the Congressional tax-writing committees. Moreover, it must be recognized that this list of negative consequences is by no means exhaustive. Treasury has received hundreds of pages of comments detailing concerns about the proposed regulations and stakeholders continue to identify additional concerns about the sweeping rules in the proposed regulations. Careful consideration of all these comments is essential given what is at stake.

As we stressed during our July 6 discussion, any proposal that would effectuate such a broad change to the U.S. tax law should be analyzed for the potential effects on the American economy before any finalization. In light of the far-reaching effect that the proposed regulations would have on business operations in the United States and abroad, stakeholder input must be a part of such analysis. Moreover, as

you well know, the conduct and submission of an economic cost-benefit analysis is a requirement under the guidelines for major rules outlined in the Congressional Review Act before regulations of this magnitude can be made effective.

In this regard, we note that the regulations purport to comply with the requirements of the Paperwork Reduction Act through the inclusion of estimates of the burden associated with the collection of information under the documentation requirements in Prop. Reg. § 1.385-2(b)(2). According to those estimates, the total annual burden associated with the new documentation requirements contained in the proposed regulations would be 735,000 hours, with an average annual burden of 35 hours per respondent or just under 3 hours per month. Based on our discussions with stakeholders and as reflected in the comment submissions to the Treasury Department, these estimates woefully understate the actual compliance burden the documentation requirements would impose on affected businesses, many of which would be required to document hundreds of transactions on a monthly basis. Of course, the documentation burden represents only one element of the total economic burden these proposed regulations would create. However, even using these low estimates for the documentation burden as a starting point, there would seem to be no doubt that the $100 million threshold for major rules, as defined in the Congressional Review Act, would be met.

We are continuing to coordinate with our Senate Finance Committee colleagues and we share the concerns that Chairman Hatch has communicated regarding the need to follow proper process and procedures with respect to these regulations going forward.

It is essential that we continue the dialogue with you about these important matters. In the meantime, our Committee staff will be following up with your tax policy team on the next steps, including how the Treasury Department intends to address the specific areas identified above and the process Treasury intends to use in conducting the economic analysis required by law.

In closing, we reiterate that the proposed regulations as crafted would interfere inappropriately with businesses' investment and financing decisions. The proposal would have the effect of blocking the ability of businesses to operate effectively and efficiently and to grow and hire new workers. Ultimately, if the proposed regulations are not completely overhauled, they would damage our economy, increase the barriers to investment for American businesses and innovators, and interfere with the growth of the good-paying jobs American workers need and deserve. We cannot allow this to happen.

Sincerely,

Kevin Brady
Chairman

Sam Johnson
U.S. House of Representatives

Devin Nunes
U.S. House of Representatives

Patrick J. Tiberi
U.S. House of Representatives

Dave Reichert
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Kristi Noem
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George Holding
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Jason Smith
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Bob Dold
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Tom Rice
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