Simplifying cross-border debt cleanup:

Key US tax considerations

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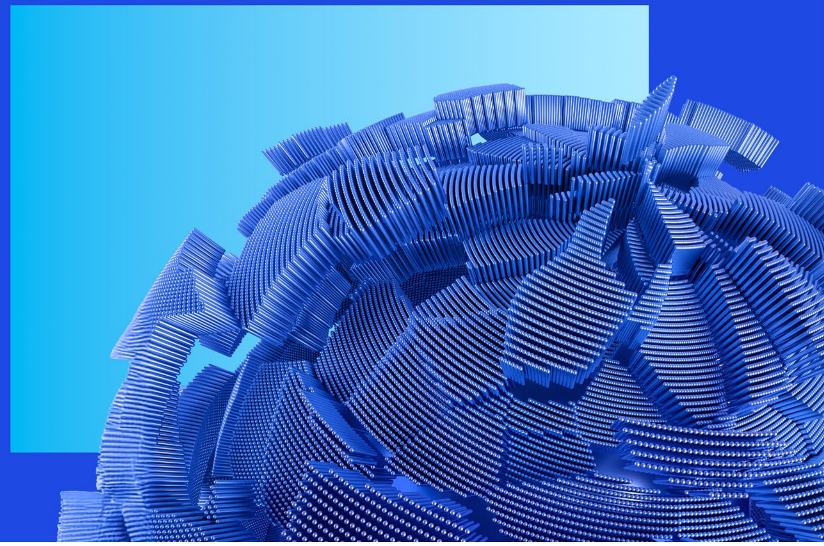


Multinational corporations often face complex challenges when dealing with outstanding debts between their international subsidiaries. Recent regulatory changes, such as the Base Erosion and Anti-abuse Tax (BEAT) and Pillar Two, have prompted companies to simplify their structures and clean up their debt footprint. This process, while necessary, is complicated by various factors, including the need to value debt instruments correctly and navigate foreign currency implications.

Valuation of cross-border instruments: A critical step

When cleaning up intercompany debt across borders, companies must carefully consider several critical aspects. First, determining the proper value of cross-border debt instruments is essential for understanding the tax consequences. This valuation process is complex, as it involves examining the contractual terms of the debt, current market conditions, and the debtor's capacity to support the debt.

For instance, changes in market rates and credit ratings can significantly impact the fair market value of these instruments. Moreover, assessing an entity's debt capacity is vital to determine the appropriate amount of debt it can realistically support.

With the valuation complexities understood, the next critical consideration is how foreign currency fluctuations impact cross-border debt cleanup.

Foreign currency tax implications

The foreign currency tax implications of cross-border debt cleanup are another significant consideration. Companies must navigate two primary types of tax issues: transactions involving foreign currencies and the translation of foreign operations into U.S. dollars. The tax code sections that govern these issues, particularly Sections 988, 986, and 987, play a crucial role in determining how gains and losses from currency fluctuations are handled. Understanding these rules is essential for managing the tax implications of debt cleanup effectively.

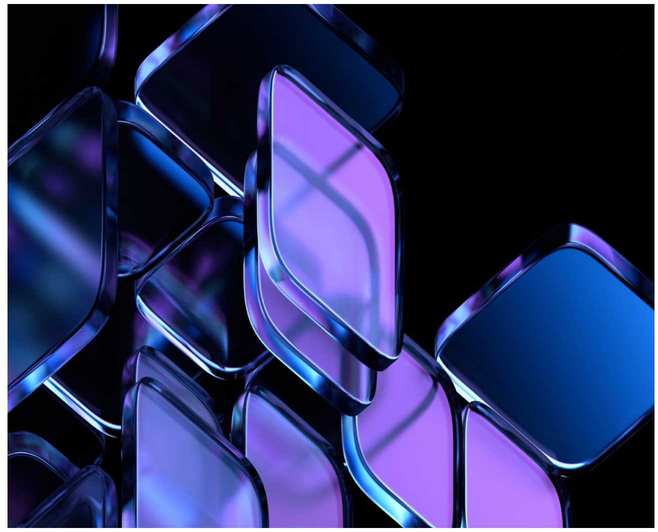
As companies navigate these foreign currency tax implications, they must also consider how they apply in practical scenarios, such as liquidations and intercompany debt cancellations.

Liquidations and intercompany debt: Practical scenarios

The process becomes even more complex when considering specific scenarios, such as the liquidation of a subsidiary or the cancellation of debt between related companies. For example, when a solvent subsidiary is liquidated, the tax implications differ significantly from those of an insolvent subsidiary. Similarly, the gratuitous cancellation of debt between sibling companies introduces its own set of tax considerations. In each case, understanding the recognition of gains and losses, as well as the application of relevant tax code sections, is critical.

Key considerations for tax professionals

To navigate these complexities, tax professionals must focus on several key areas. They must accurately value cross-border instruments, understand the associated transfer pricing considerations, and be well-versed in the foreign currency tax implications. Moreover, maintaining accurate documentation and planning is crucial to minimize tax risks and ensure compliance with relevant tax laws and regulations. By mastering these areas, tax professionals can effectively manage the challenges associated with cross-border intercompany debt cleanup.



Contact us

Megan Fitzsimmons
Principal, M&A Tax
KPMG LLP
E: meganfitzsimmons@kpmg.com

Ashley Marx
Managing Director
M&A Tax
E: amarx@kpmg.com

Blair Gowasack
Senior Manager
M&A Tax
E: bgowasack@kpmg.com

Gloria LaBerge
Senior Manager
Washington National Tax – International Tax
E: glaberge@kpmg.com

Sayantani Ghose
Principal
Washington National Tax – Valuation Services
E: sghose@kpmg.com

Michael Timmerman
Manager
Washington National Tax – International Tax
E: michaeltimmerman@kpmg.com

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