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Internal Revenue Service

Index Numbers: 367.00-00; 367.01-00

Department of the Treasury

Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:
CC:INTL:4--PLR-114902-99
Date:
JAN 12 2000

The Company =

Exchange1 =

FC1 =

Type A =

Country A =

Exchange2 =

DC1 =

DC2 =

DC3 =

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FC2 =

Country B =

Type B =

Date 1 =

FC3 =

Country C =

FC4 =

Date 2 =

FC5 =

Country D =

Country E =

Type C =

Date 3 =

Dear

This letter is in reply to your letter dated September 7, 1999, on behalf of The Company, requesting a ruling as to the federal income tax consequences of a proposed transaction under § 367(a) of the Internal Revenue Code and temporary Treasury Regulation §1.367(a)-3T(g)(7). Additional information was submitted on January 3, 6, and 7. 2000.

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The ruling contained in this letter is predicated upon the facts and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. This office has not verified any of the material submitted in support of the ruling request. Verification of the factual information and representations may be required as part of the audit process.

Facts

The Company is a domestic corporation whose stock is publicly held and traded on Exchange1 The Company owns 100% of DC1, a domestic corporation. DC1 has various wholly owned subsidiaries, including the following corporations: DC2, a domestic corporation; DC3, a domestic corporation; and FC2, a Country B Type B company that has elected to be treated as corporation and that is a controlled foreign corporation within the meaning of § 957(a). DC1, DC2. and DC3 join in the filing of The Company's consolidated return. Additionally, prior to Date 1, DC2, DC3, and FC2 owned all of the stock of FC3, a foreign corporation formed in Country C.

FCI is a Type A company organized in Country A and classified as a foreign corporation for U.S. tax purposes. FC1's stock is publicly held and traded on Exchange2. On Date1, DC2, DC3, and FC2, transferred all of their FC3 stock to FC1 in exchange for cash and shares of FC1 stock representing 20% of the outstanding stock of FC1. At the same time and as part of the same plan, FC4, a publicly held foreign corporation, transferred property to FC1 in exchange for 80% of the outstanding stock of FC1. On Date 2, FC4 distributed its FC1 shares to FC4's shareholders, including members of The Company's affiliated group. The Company represents that FC1 has been a controlled foreign corporation within the meaning of § 957(a) from Date 1 until the present time.

The Company represents that the transfer of the FC3 shares to FC1 in exchange for cash and FC1 shares constituted an exchange governed by §§ 304 and 351, and that The Company timely filed on behalf of DC2 and DC3 ten-year gain recognition agreements (collectively GRA1) under § 1.367(a)-3T(g) with its 1998 tax return in connection with the Date 1 transfer of the FC3 shares to FC1.

The Company now proposes that FC5, a foreign corporation formed in Country D, acquire FC1 in a transaction intended to qualify as a reorganization within the meaning of § 368(a)(l)(D). The assets and liabilities of FC1, including the stock of FC3, will be owned by FC5 through a Country E Type C company that FC5 formed on Date 3, and that will elect to be treated as a disregarded entity under § 301.7701-3 effective as of Date 3. The reorganization will be effectuated by means of an integrated

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plan consisting of an arrangement whereby: (1) FC1 will become a wholly owned subsidiary of FC5 (through FC5's Country E disregarded entity); (2) FC1 will convert into a Type C company; and (3) FC1 will distribute all of its assets and liabilities to FC5 in complete liquidation and cancellation of its shares. FC1's shareholders will receive, in exchange for their FC1 shares, cash and common stock of FC5.

The Company represents that after FC1 converts into a Type C company its default classification will be corporate status. See § 301.7701-3(b)(2). The Company also represents that the cash portion will not exceed 30% of the total consideration received in the exchange, and that immediately after the exchange, the former shareholders of FC1 will be in "control" of FC5 within the meaning of § 368(a)(2)(H). Additionally, it is represented that the basis of the assets of FC1 acquired by FC5 will exceed the amount of the liabilities assumed by FC5.

Analvsis

Because the initial transfer of FC3 stock occurred prior to July 20, 1998, Temp Reg. §1.367(a)-3T(g), rather than §1.367(a)-8 of the Final regulations, applies to the initial transfer that necessitated the filing of GRA1, as well as to all subsequent transfers relating to GRA1. See § 1.367(a)-8(i).

Under § 1.367(a)-3T(g)(3)(i), a U.S. transferor entering into a gain recognition agreement must agree to file an amended return for the year of the transfer and to recognize the gain realized but not recognized on the transfer if, prior to the close of the fifth or tenth tax year following the tax year of the transfer (as the case may be), the transferee foreign corporation disposes of the transferred stock in any manner (other than in a liquidation of the transferred corporation).

Accordingly, when DC2 and DC3 entered into GRA1, they agreed to recognize the gain they realized upon the transfer of their FC3 stock to FC1 if FC1 disposed of the FC3 stock prior to the close of the tenth tax year following the tax year of the transfer.

Notwithstanding § 1.367(a)-3T(g)(3)(i), if during the period an agreement is in force the transferee foreign corporation disposes of the stock of the transferred corporation in a transaction on which gain or loss would not be required to be recognized under U.S. income tax principles, the U.S. transferor will not be required to recognize gain under § 1.367(a)-3T(g)(3)(i), provided that the U.S. transferor complies with the requirements of § 1.367(a)-3T(g)(7)(i), (ii), and (iii).

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In the instant case, during the period GRA1 is in force, the transferee foreign corporation, FC1, will dispose of the stock of the transferred corporation, FC3, in a transaction on which gain or loss would not be required to be recognized under U.S. income tax principles. Therefore, DC2 and DC3 will not be required to recognize gain under § 1.367(a)-3T(g)(3)(i) if they comply with the requirements of § 1.367(a)-3T(g)(7)(i), (ii), and (iii). Pursuant to § 1.367(a)-3T(g)(7)(ii), DC2 and DC3 must therefore agree to recognize gain if prior to the close of the tenth tax year following the tax year of the initial transfer FC5 disposes of the FC3 stock (other than in a disposition that itself qualities under the rules of § 1.367(a)-3T(g)(7)).

The Company is concerned that, although it can satisfy the regulations under § 1.367(a)-3T(g)(7) with respect to FCl's transfer of the stock of FC3 to FC5 under § 361 (a), it may be unable to satisfy the regulations under § 1.367(a)-3T(g)(7) with respect to FCl's distribution of the stock of FC5 to FCl's public shareholders under § 361(c).

Based solely on the information submitted and on the representations set forth within this letter, it is held that no gain will be recognized under the current gain recognition agreement (GRA1) because of the proposed transaction, provided that the proposed transaction, including the distribution of the FC5 stock to the FCl's shareholders by FC1, qualifies as a nonrecognition transaction, and that a new gain recognition agreement that satisfies the requirements of § 1.367(a)-3T(g) is filed with The Company's consolidated income tax return for the tax year that includes the proposed transaction. The term of the new agreement will be for the remaining period of GRA1.

No opinion was requested and none is expressed regarding whether the proposed transaction qualifies as a nonrecognition transaction. Also, no opinion is expressed about the tax treatment of the proposed transaction under any other provisions of the Code or the regulations, or about the tax treatment of any conditions existing at the time of, or effects resulting from, the transaction that are not specifically covered by this ruling.

This ruling is directed only to the taxpayer that requested it. Section 6110(k)(3) provides that this ruling may not be used or cited as precedent.

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A copy of this letter and the new gain recognition agreement, as described above, must be attached to The Company's consolidated federal income tax return for the tax year in which the transaction that is the subject of this ruling is consummated.

Sincerely,

Philip L. Tretiak
Senior Technical Reviewer, Branch 4
Office of the Associate Chief
Counsel (international)

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