INTERNAL REVENUE SERVICE

Department of the Treasury

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Taxpayer	=
Sub 1	=
Sub 2	=
Acquired	=
DRE 1	=
DRE 2	=
DRE 3	=
Sub 4	=
Sub 5	=
State V	=
State W	=
Country X	=
Date 1	=
Date 2	=
Date 3	=
Date 4	=
Date 5	=
Date 6	=

$y =

We respond to your June 7, 2001 request for rulings on certain federal income tax consequences of a proposed sale of stock. Additional information was submitted in letters dated August 23, August 30, September 24, September 28, October 11, October 18, and November 20, 2001. The information submitted is summarized below.

Summary of Facts

Taxpayer is a publicly-traded State V corporation that is the common parent of a consolidated group. Prior to the transactions described below, Taxpayer owned all of the issued and outstanding stock of a State W corporation, Sub 1, which owned all of the issued and outstanding stock of DRE 3, a Country X corporation that made a "check-the-box" election to be treated as a branch of Sub 1 for U.S. federal income tax purposes.

Acquired is a Country X corporation that was engaged in two ongoing businesses that are complementary to Taxpayer's businesses. Prior to the transactions described below, Acquired owned all of the stock of Sub 4, a domestic holding corporation that is a dual resident corporation of Country X as well as State W. Sub 4's only significant asset at the time was the stock of Sub 5, a State W corporation engaged in ongoing businesses in the U.S. through subsidiaries.

On Date 1, Taxpayer commenced an all-cash tender offer to acquire all of the stock of Acquired. DRE 1, a Country X corporation, was formed by Sub 1 to effectuate the acquisition. DRE 1 made a check-the-box election to be treated as a disregarded entity for U.S. federal income tax purposes. The tender offer was completed on Date 2, and, as a result of the tender offer, DRE 1 acquired more than 80 percent of the stock of Acquired. On Date 3, Sub 1 created DRE 3 (and made the entity classification election as of that date) and transferred all of the stock of DRE 1 to DRE 3 on Date 5. As a result of subsequent property transfers by other Taxpayer affiliates, DRE 3 still owns the common interest in DRE 1, but the preference interests are owned by the Taxpayer affiliates, and DRE 1 is now treated as a partnership for U.S. federal income tax purposes.

On Date 4, Taxpayer caused Acquired and all of Acquired's non-U.S. subsidiaries to make timely elections under § 338(g). No elections were made for Sub 4 and Sub 5. In addition, Acquired was converted into a Country X private limited company, DRE 2, that elected to be treated as a branch of DRE 1 for U.S. federal income tax purposes. DRE 1, DRE 2, and DRE 3 offset profits and losses and are treated as a single Country X branch for purposes of § 1.1503-2(g)(2)(ii) of the Income Tax Regulations.

As part of a plan to restructure Taxpayer's newly expanded consolidated group, the following steps were taken on Date 6:

(I) DRE 2 transferred all of the stock of Sub 4 to DRE 3.

(II) Sub 4 transferred the stock of Sub 5 to DRE 3 in exchange for DRE 3's note for $y (Sub 4's transfer of Sub 5 stock to DRE 3 in exchange for DRE 3's note may be referred to as "the Transfer"). The note represented the book value of Sub 5 at the time, and Taxpayer represents that the Transfer resulted in an intercompany gain item under § 1.1502-13 of the Income Tax Regulations, which has not been taken into account under the matching rule of § 1.1502-13(c).

(III) Taxpayer contributed all of the stock of Sub 2, a State W corporation, to Sub 1.

(IV) Sub 1 contributed the stock of DRE 3 to Sub 2

Because DRE 3 is a disregarded entity, Sub 2 is treated as owning all of the stock of Sub 4 and Sub 5. After this part of the restructuring, Sub 4 remains a duel resident corporation, but it does not own any operations directly or indirectly.

Proposed Transaction

Taxpayer states that, due to overall market conditions, the value of Sub 5 has declined significantly from the time Acquired/DRE 2 was purchased by DRE 1. Taxpayer currently proposes additional steps in its restructuring, all to be taken pursuant to an overall plan and will occur simultaneously or sequentially on approximately the same day. The restructuring's goal is to allow Taxpayer to dispose of selected parts of Sub 5's business in order to reduce overlap of operations and reduce the debt incurred when Acquired was purchased. Taxpayer also wishes to cancel the $y note and eliminate Sub 4's dual resident status.

Accordingly, Taxpayer has proposed the following transaction:

(i) DRE 3 will form U.S. Newco as a domestic corporation;

(ii) Sub 4 will be merged with and into U.S. Newco (the Sub 4 Merger). Following the merger, U.S. Newco (as successor to Sub 4) will no longer have dual resident status;

(iii) DRE 3 will transfer the stock of Sub 5 to U.S. Newco, DRE 3's note will be cancelled, and Sub 5 will be merged with and into U.S. Newco, with U.S. Newco surviving (the Sub 5 Merger); and

(iv) Sub 2 will sell the U.S. Newco stock to an unrelated purchaser.

At all times during the above transaction, Sub 2 will be considered the owner of Sub 4, Sub 5, and U.S. Newco for U.S. income tax purposes.

Taxpayer represents that:

(a) The Sub 4 Merger will qualify as a reorganization under applicable state law.

(b) The Sub 5 Merger will qualify as a reorganization under applicable state law.

(c) Sub 5 is not and has never been a dual resident corporation.

(d) Sub 5 has not had any dual consolidated losses.

(e) Sub 4 has not had any dual consolidated losses for taxable periods beginning on or after February 1, 1999.

(f) Taxpayer is not covered by the rules of § 1.1503-2(c)(15)(iv).

Taxpayer plans to sell U.S. Newco shortly after step (iii), but, prior to such sale, Taxpayer seeks a ruling that addresses how the netting rule of § 1.1502-20(a)(4) would apply to the sale of U.S. Newco stock at a loss, as is anticipated.

The netting rule of § 1.1502-20(a)(4) allows a loss recognized by one member to be offset by gain recognized by the same or a different member but only if the loss and the gain are with respect to the stock of the same subsidiary having the same material terms and are taken into account as a consequence of the same plan or arrangement. In this case, the intercompany gain item that resulted from the Transfer, which has not yet been taken into account but would be triggered upon the sale of U.S. Newco stock outside of the consolidated group, can offset losses recognized on the sale of U.S. Newco stock.

Accordingly, we rule as follows:

The loss disallowance rule of § 1.1502-20(a)(1) does not apply to disallow any loss, if any, recognized upon the sale of the stock of U.S. Newco to an unrelated third party purchaser to the extent that gain, if any, is taken into account by members of the consolidated group with respect to stock of U.S. Newco having the same material terms.

The regulations further provide that, if the gain to which § 1.1502-20(a)(4) applies is less than the amount of the loss with respect to the disposition of U.S. Newco's stock, the gain is applied to offset loss with respect to each share disposed of in proportion to the amount of the loss deduction that would have been disallowed under § 1.1502-20(a)(1) with respect to such share before the application of § 1.1502-20(a)(4). If the same item of gain could be taken into account more than once in the application of § 1.1502-20(a)(1) and (b)(1), the item is taken into account only once. After the netting rule is applied, the general rules of § 1.1502-20(a)(1) and (c)(1) apply.

We express no opinion about the tax treatment of the proposed transaction under other provisions of the Code and regulations or about the tax treatment of any conditions existing at the time of, or effects resulting from, the proposed transaction that are not specifically covered by the above rulings. In particular, we express no opinion about the Sub 4 Merger or the Sub 5 Merger. See section 3.01(29) of Rev. Proc. 2001-3, 2001-1 I.R.B 79, 114. Further, no rulings were requested and no opinion is expressed concerning the foreign tax treatment of the internal restructurings or

proposed transaction described herein.

The rulings contained in this letter are predicated upon the facts and representations submitted by the taxpayer and accompanied by a penalties of perjury statement executed by an appropriate party. This office has not verified any of the materials submitted in support of the request for a ruling. Verification of the information, representations, and other data may be required as part of the audit process. See section 12.04 of Rev. Proc. 2001-1, 2001-1 I.R.B. 1, 46, which discusses in greater detail the revocation or modification of ruling letters. However, when the criteria in section 12.05 of Rev. Proc. 2001-1, 2001-1 I.R.B. at 47, are satisfied, a ruling is not revoked or modified retroactively except in rare or unusual circumstances.

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

It is important that a copy of this ruling letter be attached to the federal income tax return of each party involved for the taxable year in which the transaction covered by this letter is consummated.

Pursuant to the power of attorney on file in this office, a copy of this letter has been sent to your authorized representative.

Sincerely yours,
Filiz A. Serbes
Chief, Branch 3
Office of Associate Chief Counsel
(Corporate)