

## Section 367.—Foreign Corporations

26 CFR 1.367(b)–3T: Repatriation of foreign corporate assets in certain nonrecognition transactions (temporary).

T.D. 8863

### DEPARTMENT OF THE TREASURY Internal Revenue Service 26 CFR Parts 1 and 602

#### Stock Transfer Rules: Supplemental Rules

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Temporary regulations.

SUMMARY: This document contains temporary regulations that provide an election for certain taxpayers engaged in certain exchanges described in section 367(b). These regulations provide guidance for taxpayers that make the specified election in order to determine the extent to which income must be included and certain corresponding adjustments must be made. The text of the temporary regulations also serves as the text of the proposed regulations set forth in the notice of proposed rulemaking on this subject in

REG–116048–99 on page 584.

**DATES:** *Effective Date.* These regulations are effective as of February 23, 2000.

*Applicability Date.* These regulations apply to section 367(b) exchanges that occur on or after February 23, 2000.

FOR FURTHER INFORMATION CONTACT: Mark D. Harris, (202) 622-3860 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

#### Paperwork Reduction Act

These regulations are being issued without prior notice and public procedure pursuant to the Administrative Procedure Act (5 U.S.C. 553). For this reason, the collection of information contained in these regulations has been reviewed and, pending receipt and evaluation of public comments, approved by the Office of Management and Budget under control number 1545-1666. Responses to this collection of information is mandatory.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid OMB control number.

For further information concerning this collection of information, and where to

submit comments on the collection of information and the accuracy of the estimated burden, and suggestions for reducing this burden, please refer to REG–116048–99, page 584, the preamble to the cross-referencing notice of proposed rulemaking published in the Proposed Rules section of this issue of the **Federal Register**.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential, as required by 26 U.S.C. 6103.

#### Background

On December 27, 1977, the IRS and Treasury issued proposed and temporary regulations under section 367(b) of the Internal Revenue Code (Code). Subsequent guidance updated and amended the 1977 temporary regulations (the 1977 regulations) several times over the next 14 years. On August 26, 1991, the IRS and Treasury issued proposed regulations §§1.367(b)–1 through 1.367(b)–6 (the 1991 proposed regulations). Comments to the 1991 proposed regulations were received, and a public hearing was held on November 22, 1991. In June of 1998, the IRS and Treasury issued final regulations

under sections 367(a) and (b) (the 1998 regulations). The 1998 regulations addressed transactions under section 367(b) only to the extent the transactions are also subject to the stock transfer rules of section 367(a). Thus, the 1977 regulations have remained in effect to the extent not superseded by the 1998 regulations. The preamble to the 1998 regulations stated that the IRS and Treasury would issue guidance at a later date to address the portions of the 1991 proposed regulations related to section 367(b) that were not addressed in the 1998 regulations.

The IRS and Treasury adopted §§1.367(b)-1 through 1.367(b)-6 as final regulations under section 367(b) (see T.D. 8862, page 466). These temporary regulations relate to certain provisions of the 1991 proposed regulations not adopted in the final section 367(b) regulations T.D. 8862.

## General Purpose

These temporary regulations address the elimination of an election available to certain taxpayers under the 1991 proposed regulations that was not adopted in the final section 367(b) regulations T.D. 8862.

## Specific Provisions

### *A. §1.367(b)-3T(b)(4): Election of taxable exchange treatment*

Section 1.367(b)-3 of the 1991 proposed regulations addressed transactions in which a foreign corporation transfers assets to a domestic corporation pursuant to a Subchapter C nonrecognition provision. These transactions include a section 332 liquidation of a foreign corporation into a domestic parent corporation and an asset reorganization, such as a C, D or F reorganization, of a foreign corporation into a domestic corporation. The 1991 proposed regulations required a U.S. shareholder of a foreign acquired corporation (or, in certain cases, a foreign subsidiary of the U.S. shareholder) to currently include in income the allocable portion of the foreign acquired corporation's earnings and profits accumulated during the U.S. shareholder's holding period (all earnings and profits amount). The final section 367(b) regulations T.D. 8862 adopted this general rule.

Sections 7.367(b)-5(b) and 7.367(b)-7(c)(2)(ii) of the 1977 regulations and §1.367(b)-3(b)(2)(iii) of the 1991 proposed regulations provided an exception to this rule, which permitted an exchanging shareholder to elect to recognize the gain (but not the loss) that it realizes in the exchange (taxable exchange election), rather than include the all earnings and profits amount in income. To the extent the all earnings and profits amount exceeds a shareholder's stock gain, the 1991 proposed regulations further required the foreign acquired corporation to reduce various tax attributes that would otherwise carry over to the domestic acquiring corporation (attribute reduction regime). The final regulations T.D. 8862 did not adopt the taxable exchange election.

In order to provide taxpayers an opportunity to comment on this change, these temporary regulations provide the taxable exchange election in modified form. The modified election permits an exchanging shareholder to elect to treat a transaction as a taxable exchange, but limits application of the attribute reduction regime to a section 332 liquidation or to an inbound asset reorganization in which the foreign acquired corporation is wholly owned (directly or indirectly) by one U.S. person. These temporary regulations apply to section 367(b) exchanges that occur between February 23, 2000, and February 24, 2001.

## Further Explanation

For a more detailed discussion regarding section 367(b), see T.D. 8862.

## Special Analyses

It has been determined that these Temporary regulations are not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations. Further it is hereby certified pursuant to sections 603(a) and 605(b) of the Regulatory Flexibility Act that the collection of information in these regulations will not have a significant economic impact on a substantial number of small entities. This certification is based upon the fact that the number of section 367(b) exchanges that require reporting under these

regulations is estimated to be only 20 per year. Therefore, a Regulatory Flexibility Analysis under the Regulatory Flexibility Act (5 U.S.C. chapter 6) is not required.

Pursuant to section 7805(f) of the Code, these temporary regulations will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact.

## Drafting Information

The principal author of these regulations is Mark Harris of the Office of Associate Chief Counsel (International). However, other personnel from the IRS and Treasury Department participated in their development.

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## Adoption of Amendments to the Regulations

Accordingly, 26 CFR parts 1 and 602 are amended as follows:

### PART 1—INCOME TAXES

Paragraph 1. The authority citation for part 1 is amended by adding entries in numerical order to read in part as follows:

Authority: 26 U.S.C. 7805 \* \* \*

Section 1.367(b)-3T also issued under 26 U.S.C. 367(a) and (b). \* \* \*

Par. 2. Section 1.367(b)-3T is added to read as follows:

*§1.367(b)-3T Repatriation of foreign corporate assets in certain nonrecognition transactions (temporary).*

(a) through (b)(3). [Reserved]. For further guidance, see §1.367(b)-3(a) through (b)(3).

(4) *Election of taxable exchange treatment—(i) Rules—(A) In general.* In lieu of the treatment prescribed by §1.367(b)-3(b)(3)(i), an exchanging shareholder described in §1.367(b)-3(b)(1) may instead elect to recognize the gain (but not loss) that it realizes in the exchange (taxable exchange election). To make a taxable exchange election, the following requirements must be satisfied—

(1) The exchanging shareholder (and its direct or indirect owners that would be affected by the election, in the case of an exchanging shareholder that is a foreign corporation) reports the exchange in a manner consistent therewith (see, e.g., sections 954(c)(1)(B)(i), 1001 and 1248);

(2) The notification requirements of paragraph (b)(4)(i)(C) of this section are satisfied; and

(3) The adjustments described in paragraph (b)(4)(i)(B) of this section are made when the following circumstances are present—

(i) The transaction is described in section 332 or is an asset acquisition described in section 368(a)(1), with regard to which one U.S. person owns (directly or indirectly) 100 percent of the foreign acquired corporation; and

(ii) The all earnings and profits amount described in §1.367(b)–3(b)(3)(i) with respect to the exchange exceeds the gain recognized by the exchanging shareholder.

(B) *Attribute reduction*—(1) *Reduction of NOL carryovers*. The amount by which the all earnings and profits amount exceeds the gain recognized by the exchanging shareholder (the excess earnings and profits amount) shall be applied to reduce the net operating loss carryovers (if any) of the foreign acquired corporation to which the domestic acquiring corporation would otherwise succeed under section 381(a) and (c)(1). See also Rev. Rul. 72–421 (1972–2 C.B. 166) (see §601.601(d)(2) of this chapter).

(2) *Reduction of capital loss carryovers*. After the application of paragraph (b)(4)(i)(B)(1) of this section, any remaining excess earnings and profits amount shall be applied to reduce the capital loss carryovers (if any) of the foreign acquired corporation to which the domestic acquiring corporation would otherwise succeed under section 381(a) and (c)(3).

(3) *Reduction of basis*. After the application of paragraph (b)(4)(i)(B)(2) of this section, any remaining excess earnings and profits amount shall be applied to re-

duce (but not below zero) the basis of the assets (other than dollar-denominated money) of the foreign acquired corporation that are acquired by the domestic acquiring corporation. Such remaining excess earnings and profits amount shall be applied to reduce the basis of such assets in the following order: first, tangible depreciable or depletable assets, according to their class lives (beginning with those assets with the shortest class life); second, other non-inventory tangible assets; third, intangible assets that are amortizable; and finally, the remaining assets of the foreign acquired corporation that are acquired by the domestic acquiring corporation. Within each of these categories, if the total basis of all assets in the category is greater than the excess earnings and profits amount to be applied against such basis, the taxpayer may choose to which specific assets in the category the basis reduction first applies.

(C) *Notification*. The exchanging shareholder shall elect to apply the rules of this paragraph (b)(4)(i) by attaching a statement of its election to its section 367(b) notice. See §1.367(b)–1(c) for the rules concerning filing a section 367(b) notice.

(D) *Example*. The following example illustrates the rules of this paragraph (b)(4)(i):

*Example*—(i) *Facts*. DC, a domestic corporation, owns all of the outstanding stock of FC, a foreign corporation. The stock of FC has a value of \$100, and DC has a basis of \$80 in such stock. The assets of FC are one parcel of land with a value of \$60 and a basis of \$30, and tangible depreciable assets with a value of \$40 and a basis of \$80. FC has no net operating loss carryovers or capital loss carryovers. The all earnings and profits amount with respect to the FC stock owned by DC is \$30, of which \$19 is described in section 1248(a) and the remaining \$11 is not (for example, because it was earned prior to 1963). In a liquidation described in

section 332, FC distributes all of its property to DC, and the FC stock held by DC is canceled. Rather than including in income as a deemed dividend the all earnings and profits amount of \$30 as provided in §1.367(b)–3(b)(3)(i), DC instead elects taxable exchange treatment under paragraph (b)(4)(i)(A) of this section.

(ii) *Result*. DC recognizes the \$20 of gain it realizes on its stock in FC. Of this \$20 amount, \$19 is included in income by DC as a dividend pursuant to section 1248(a). (For the source of the remaining \$1 of gain recognized by DC, see section 865. For the treatment of the \$1 for purposes of the foreign tax credit limitation, see generally section 904(d)(2)(A)(i).) Because the transaction is described in section 332 and because the all earnings and profits amount with respect to the FC stock held by DC (\$30) exceeds by \$10 the income recognized by DC (\$20), the attribute reduction rules of paragraph (b)(4)(i)(B) of this section apply. Accordingly, the \$10 excess earnings and profits amount is applied to reduce the basis of the tangible depreciable assets of FC, beginning with those assets with the shortest class lives. Under section 337(a) FC does not recognize gain or loss in the assets that it distributes to DC, and under section 334(b) (which is applied taking into account the basis reduction prescribed by paragraph (b)(4)(i)(A)(3) of this section) DC takes a basis of \$30 in the land and \$70 in the tangible depreciable assets that it receives from FC.

(ii) *Effective date*. This paragraph (b)(4) applies for section 367(b) exchanges that occur between February 23, 2000, and February 24, 2001.

(c) and (d) [Reserved]. For further guidance, see §1.367(b)–3(c) through (d).

Par. 3. The authority citation for part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 4. In §602.101, paragraph (b) is amended as follows:

1. Removing the following entries from the table:

§602.101 OMB Control numbers.

\* \* \* \* \*

(b) \* \* \*

2. Adding the following entry in numerical order to the table to read as follows:

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CFR part or section where identified and described

Current OMB control No.

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7.367(b)–1	1545-0026
7.367(b)–3	1545-0026
7.367(b)–7	1545-0026
7.367(b)–9	1545-0026
7.367(b)–10	1545-0026

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§602.101 OMB Control numbers.

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(b) \* \* \*

John M. Dalrymple,  
Acting Deputy Commissioner  
of Internal Revenue.

Approved December 22, 1999.

Jonathan Talisman,  
Acting Assistant Secretary  
of the Treasury.

(Filed by the Office of the Federal Register on January 21, 2000, 8:45 a.m., and published in the issue of the Federal Register for January 24, 2000, 65 F.R. 3586)

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CFR part or section where  
identified and described

Current OMB  
control No.

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1.367(b)-3T .....1545-1666

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