Internal Revenue Service

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Department of the Treasury
Washington, DC 20224

Person To Contact:
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April 02, 2004

TY:

Legend

Transferor =

US Holdco =

Corp W =
Corp X =

Corp Y =

Corp Z =

Country C =
Holdco
Business A =
State B =
Country C =
Year 1 =
Year 2 =
Year 3 =
Year 4 =
Year 5 =
Year 6 =
Date 7 =
Date 8 =
Date 9 =

Date 10 =

Dear :

This is in response to a letter dated June 19, 2003, from your authorized representatives, requesting a ruling that the proposed disposition of the stock of Corp X by Transferor will not constitute a disposition within the meaning of Treas. Reg. § 1.884-2T(d)(5). Additional information was submitted in letters dated December 11, 2003, December 15, 2003, and December 16, 2003, and February 17, 2004. The information submitted is summarized below.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for a ruling, it is subject to verification on examination.

Transferor was incorporated over 100 years ago in Country C to engage in Business A. Corp X was incorporated in State B in Year 2 as a wholly owned subsidiary of Transferor. At the time of this ruling request, it was the common parent of an affiliated group of corporations that since Year 4 has filed a consolidated federal income tax return.

Corp Y was incorporated prior to Corp X and is now a wholly owned State B subsidiary of Corp X. Corp Y formerly was a wholly owned subsidiary of Corp Z, a U.S. affiliate of Corp X, and Corp Z in turn was a wholly owned subsidiary of Transferor. As described below, in Year 3, Transferor transferred the stock of Corp Z to Corp X, and in Year 5 Corp Z was merged into Corp Y.

Transferor also conducted operations in the United States through a U.S. branch. Between Year 1 and Year 3, Transferor restructured its branch operations through a series of transactions, so that, thereafter, it no longer conducted any business in the United States other than through subsidiaries. These transactions are described in greater detail below.

Previous Transactions

The Year 1 Transaction

In Year 1, Transferor transferred to Corp Y (either directly or through Corp Z) certain branch assets. By private letter ruling, the Service ruled that the Year 1 indirect transfers of branch assets to Corp Y were treated as back-to-back section 351 transfers

of assets from Transferor to Corp Z and from Corp Z to Corp Y. Transferor and Corp Z made the section 351 earnings and profits election contemplated by Treas. Reg. §1.884-2T(d)(4), and Transferor attached the relevant statement to its timely filed Year 1 federal income tax return.

The Year 2 Transaction

In Year 2, Transferor transferred to Corp X additional assets of its U.S. branch in exchange for additional shares of Corp X stock. Following that transaction, Transferor and Corp X made the section 351 earnings and profits election contemplated by Treas. Reg. §1.884-2T(d)(4) and Transferor attached the relevant statement to its timely filed Year 2 federal income tax return.

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The Year 3 Transactions

In Year 3, Transferor transferred to Corp Y (either directly or through Corp Z) most of the remaining U.S. branch assets. On the same day, Transferor also transferred to Corp Z the remainder of its branch assets. Immediately thereafter, Transferor transferred all the stock of Corp Z to Corp X in exchange for additional shares of Corp X stock.

Favorable rulings were obtained from the IRS regarding the tax-free nature of each of the Year 3 transactions on behalf of Transferor, Corp Z and Corp X and the branch profits tax consequences of the Year 3 transactions. For corporate tax purposes, the first and second transactions were treated as if Transferor had transferred the assets to Corp Z in a transaction that qualified under section 351, and Corp Z had then transferred the assets from Corp Z to Corp Y in a related transaction that qualified under section 351. For corporate tax purposes, the Year 3 stock transfer was treated as if Transferor had transferred certain assets and stock of Corp Z to Corp X in a transaction that qualified under section 351, and Corp X had then transferred those assets to Corp Z. With respect to the branch profits tax, the IRS ruled that the Year 3 transaction would not be treated as a disposition of the Corp Z stock for branch profits tax purposes and that, in essence, the branch profits tax “taint” (i.e., the triggering of a branch profits tax on any disposition of stock by the foreign transferor) would attach to the shares of Corp X stock. More specifically, the IRS ruled as follows:

> (17) Provided that Corp X makes a valid election to increase its earnings and profits by an amount equal to the earnings and profits previously allocated to Corp Z pursuant to elections made previously or made with respect to the transfers described in this letter ruling by Transferor under §1.884-2T(d)(4), and provided that Transferor attaches a statement to its timely filed (including extensions) federal income tax return treating such earnings and profits as if they

had been allocated from Transferor to Corp X pursuant to an election under §1.884-2T(d)(4) of the temporary regulations: (a) Transferor's transfer of the stock of Corp Z to Corp X will not constitute a "disposition" of part or all of the stock of Corp Z within the meaning of §1.884-2T(d)(5)(ii), and (b) Corp Z's earnings and profits will be reduced by an amount equal to the earnings and profits allocated to Corp X.

Corp X made the section 351 earnings and profits election contemplated by Treas. Reg. §1.884-2T(d)(4) and Transferor attached the relevant statement to its timely filed Year 3 federal income tax return.

Transactions For Which Ruling Requested

Transferor requested a ruling pursuant to §1.884-2T(d)(5)(ii) prior to Exchange 1 and Exchange 2.

Exchange 1

On Date 7 in Year 6, Transferor formed U.S. Holdco, a single member limited liability company organized under the laws of Delaware, in order to provide Transferor with a new U.S. holding company that is not engaged in Business A and that it can use to make acquisitions of, and enter into transactions with, non-Business A companies. U.S. Holdco will timely elect under Treas. Reg. § 301.7701-3(a) to be classified as an association, and therefore will be treated as a corporation for federal tax purposes pursuant to Treas. Reg. § 301.7701-2(b)(2). This will allow Transferor to achieve certain Country C tax efficiencies. On Date 9 in Year 6 Transferor transferred all the stock of Corp X to U.S. Holdco, in exchange for the sole equity interest in U.S. Holdco. (Exchange 1).

Exchange 2

On Date 8 in Year 6, Transferor formed a new wholly-owned Country C subsidiary (Country C Holdco) in order to provide Transferor with a Country C corporate structure that will facilitate its ability to borrow funds the interest on which will be fully deductible for Country C tax purposes. On Date 9, Transferor transferred all the stock of U.S. Holdco to Country C Holdco in exchange for shares of Country C Holdco common stock. (Exchange 2) Consequently, Country C Holdco now holds certain of Transferor's high-value assets (namely the stock of Transferor's U.S. subsidiaries).

Immediately following the transactions, Transferor owns 100 percent of the stock of Country C Holdco, Country C Holdco owns the sole equity interest in U.S. Holdco, and U.S. Holdco owns all the stock of Corp X.

Transferor has made the following representations in connection with the proposed transactions:

(1) Exchange 1 will qualify for tax-free treatment under section 351;
(2) Exchange 2 will qualify for tax-free treatment under section 351;
(3) U.S. Holdco will be treated as a corporation for U.S. federal tax purposes and for Country C tax purposes;
(4) Transferor is a qualifying person for purposes of the U.S. –Country C income tax treaty **;**
(5) Country C Holdco will be a qualifying person for purposes of the U.S. –Country C income tax treaty **;**
(6) Transferor does not intend to dispose of Country C Holdco, US Holdco, Corp X or any of its existing U.S. operations outside of Corp W's Country C corporate group .

Transferor requests a ruling that the back-to-back transfers of the Corp X stock by Transferor to US Holdco and then the transfer of the US Holdco stock from Transferor to Country C Holdco will not be treated as dispositions of the Corp X stock under Treas. Reg. § 1.884-2T(d)(5)(i).

Law and Analysis

Under Treas. Reg. §1.884-2T(d)(3), if a foreign corporation engaged in the conduct of a U.S. trade or business makes a transfer under section 351(a) of the Code of all or part of its U.S. assets to a U.S. corporation in exchange for stock or securities in the transferee, the transferor corporation's dividend equivalent amount will be determined without regard to the section 351 transfer, provided the U.S. transferee corporation makes an election under Treas. Reg. §1.884-2T(d)(4) to increase its earnings and profits by an allocable portion of the transferor corporation's effectively connected earnings and profits and non-previously taxed effectively connected accumulated earnings and profits. The transferor must also file a statement agreeing that, upon the disposition of part or all of the stock or securities it owns in the transferee, (or a successor in interest) it will treat as a dividend equivalent amount for the taxable year in which the disposition occurs an amount equal to the lesser of (A) the amount realized upon such disposition or (B) the total amount of the effectively connected earnings and profits and non-previously taxed effectively connected accumulated earnings and profits that was allocated from the transferor corporation to the transferee corporation pursuant to the election under Treas. Reg. §1.884-2T(d)(4)(i). Treas. Reg. §1.884-2T(d)(5)(i).

Pursuant to Treas. Reg. §1.884-2T(d)(5)(ii), a "disposition" does not include a transfer of stock or securities of the transferee corporation by the transferor corporation pursuant to a complete liquidation described in section 332(b) or a transfer pursuant to a reorganization described in section 368(a)(1)(F). Any other transfer of transferee shares that qualifies for non-recognition of gain or loss shall be treated as a disposition for purposes of paragraph (d)(5)(i), unless the Commissioner has determined otherwise "by published guidance or by prior ruling issued to the taxpayer upon its request." The Commissioner has not determined otherwise by published guidance.

Thus, absent the relief requested, any disposition of shares of Corp X stock would trigger a branch profits tax because of the section 884 elections made in connection with prior transfers that qualified under section 351.

Based solely on the information submitted and on the representations set forth above, we rule as follows:

> Assuming that the back-to-back transfers of the Corp X stock by Transferor to US Holdco in Exchange 1 and of US Holdco stock from Transferor to Country C Holdco in Exchange 2 qualify under section 351, and provided that U.S.Holdco makes an election under Treas. Reg. §1.884-2T(d)(4) to increase its earnings and profits by an amount equal to the earnings and profits allocated to Corp X pursuant to elections made previously, that Country C Holdco attaches a statement to its timely filed (including extensions) federal income tax return for Year 6, agreeing that upon disposition of all or part of its interest in US Holdco, Country C Holdco will treat as a dividend equivalent amount for the taxable year in which the disposition occurs an amount equal to the lesser of (a) the amount realized upon such disposition or (b) the total amount of effectively connected earnings and profits and non-previously taxed accumulated earnings and profits that was treated as allocated to US Holdco from Corp X, except to the extent such amount was previously taken into account by Country C Holdco as dividends or dividend equivalent amounts for branch profits tax purposes, then neither Transferor's transfer of the stock of Corp X to US Holdco nor Transferor's transfer of the stock of US Holdco to Country C Holdco will constitute a "disposition" of all or part of the stock of Corp X or US Holdco, within the meaning of §1.884-2T(d)(5)(ii), and Corp X's earnings and profits will be reduced by an amount equal to the earnings and profits allocated to US Holdco.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

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

A copy of this letter must be attached to any income tax return to which it is relevant.

Sincerely,

Elizabeth U. Karzon
Chief, Branch 1
Office of the Associate Chief Counsel
(International)

cc: