

## Section 367.—Foreign Corporations

*26 CFR 1.367(e)-1: Distributions described in section 367(e)(1).*

### T.D. 8834

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

### Treatment of Distributions to Foreign Persons Under Sections 367(e)(1) and 367(e)(2)

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document amends the Income Tax Regulations by removing

temporary regulations on the treatment of distributions to foreign persons under section 367(e) of the Internal Revenue Code and adding final regulations under section 367(e). These final regulations are necessary to implement section 367(e)(1) and (2), as added to the Internal Revenue Code by the Tax Reform Act of 1986, which affects U.S. corporations.

DATES: These regulations are effective August 9, 1999.

FOR FURTHER INFORMATION CONTACT: Guy A. Bracuti, 202-622-3860 (not a toll-free number).

#### SUPPLEMENTARY INFORMATION:

##### *Paperwork Reduction Act*

The collection of information in this final rule has been reviewed and, pending receipt and evaluation of public comments, approved by the Office of Management and Budget (OMB) under 44 U.S.C. 3507 and assigned control number 1545-1487.

The collections of information in this regulation are in §§1.367(e)-1(d)(2), 1.367(e)-1(d)(3), 1.367(e)-2(b)(2), and 1.6038B-1(e). This information is required to obtain certain exemptions from taxation and to satisfy other information

reporting requirements imposed by the Internal Revenue Code (Code). This information will be used by the **Internal Revenue Service** to verify whether a taxpayer is entitled to an exemption from income tax. The likely respondents are large corporations.

Comments on the collections of information should be sent to the **Office of Management and Budget**, Attn: Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Washington, DC 20503, with copies to the **Internal Revenue Service**, Attn: IRS Reports Clearance Officer, OP:FS:FP, Washington, DC 20224. Comments on the collection of information should be received by October 8, 1999.

Comments are specifically requested concerning: Whether the collections of information are necessary for the proper performance of the functions of the IRS, including whether the information will have practical utility; The accuracy of the estimated burden associated with the collection of information (see below); How the quality, utility, and clarity of the information to be collected may be enhanced; How the burden of complying with the collections of information may be minimized, including through the application of automated collection techniques or

other forms of information technology; and Estimates of capital or start-up costs and costs of operation, maintenance, and purchase of services to provide information. The estimated total annual reporting and/or recordkeeping burden is 2,471 hours. The estimated average annual burden hours per respondent and/or recordkeeper is 11 hours. The estimated number of respondents and/or recordkeepers is 217. The estimated annual frequency of responses is once.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a valid control number assigned by the Office of Management and Budget.

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*

Section 367(e)(1) amended the Code by providing regulatory authority to tax gain on a domestic distributing corporation's section 355 distribution of stock or securities to foreign persons. Section 367(e)(2) amended the Code by requiring a liquidating corporation to recognize gain (or loss) attributable to property distributed in a section 332 liquidation to a foreign parent corporation, except to the extent regulations provide otherwise.

On January 16, 1990, temporary regulations under section 367(e)(1) and (2) were published in the **Federal Register** (55 F.R. 1406 [T.D. 8280, 1990-1 C.B. 80]). A cross-referenced Notice of Proposed Rulemaking was published on that same date under RIN 1545-AL35 (55 F.R. 1472 [1990-1 C.B. 678]). The temporary regulations were proposed and issued to implement section 367(e) of the Internal Revenue Code of 1986 (Code), as amended by sections 631(d)(1) and 1810(g) of the Tax Reform Act of 1986 (100 Stat. 2085, 2272, Public Law 99-514 [1986-3 C.B.]). On January 25, 1993, final regulations under section 367(e)(1) were published in the **Federal Register** (58 F.R. 5927 [T.D. 8472, 1993-1 C.B. 51]). RIN 1545-AL35 was thereby closed. The preamble of T.D. 8472 stated that final regulations under

section 367(e)(2) would be promulgated in a separate Treasury decision and that taxpayers could apply the provisions contained in §1.367(e)-2T to distributions occurring on or after January 16, 1993, and prior to the date that is 30 days after final regulations under section 367(e)(2) are published in the **Federal Register**. The final regulations under section 367(e)(1) were removed and replaced with temporary regulations that were published in the **Federal Register** on August 14, 1996 (61 F.R. 42165 [T.D. 8682, 1996-2 C.B. 12]). A cross-referenced Notice of Proposed Rulemaking was published on August 14, 1996 under RIN 1545-AU22 (61 F.R. 42217). A new RIN (RIN 1545-AX30) has been issued under which the section 367(e)(2) proposed regulations will be finalized.

No significant comments were received with respect to the 1996 Notice of Proposed Rulemaking with respect to section 367(e)(1). Comments were received with respect to the 1990 Notice of Proposed Rulemaking with respect to sections 367(e)(1) and 367(e)(2). No hearings were held on either Notice of Proposed Rulemaking.

### *Explanation of Revisions and Summary of Comments*

#### *I. Overview*

These final regulations address the tax consequences of a distribution by a domestic corporation of its subsidiary's stock to foreign shareholders in a transaction described in section 355 (outbound section 355 distribution), a liquidation of a domestic corporation into a foreign parent corporation in a transaction described in section 332 (outbound liquidation), and a liquidation of a foreign corporation into a foreign parent corporation in a transaction described in section 332 (foreign-to-foreign liquidation).

Section 367(e) grants the Secretary authority to provide the extent to which a distributing corporation in an outbound section 355 distribution or liquidation or foreign-to-foreign liquidation may obtain the benefit of nonrecognition treatment when it makes the distribution to a foreign shareholder. The purpose of section 367 is to prevent the inappropriate avoidance of U.S. tax that can arise from the application of nonrecognition provisions in the cross-border context.

#### *A. Outbound section 355 distributions*

Section 367(e)(1) provides that a distribution under section 355 (or so much of section 356 as relates to section 355) by a U.S. corporation to its foreign shareholders is accorded nonrecognition treatment except to the extent provided in regulations. Section 1.367(e)-1 provides the circumstances under which such a distribution is taxable.

The legislative history to section 367(e)(1) provides that "transfers of stock by domestic corporations to foreign persons pursuant to Code section 355 . . . will give rise to the recognition of gain under Code section 367(e), to the extent provided in regulations. The committee expects that the Secretary will carefully consider the extent to which it is appropriate, in view of the purpose of section 367(e), to require the recognition of gain upon the transfer of the stock of a domestic corporation to foreign persons under section 355." H.R. Rep. 426, 99th Cong., 1st Sess. 931 (1985); S. Rep. 313, 99th Cong., 2nd Sess. 950 (1986).

The temporary regulations under section 367(e)(1) provide a general rule that a domestic distributing corporation is taxed on a distribution of controlled stock to foreign shareholders, regardless of whether the controlled corporation is a domestic corporation or a foreign corporation. Several exceptions are provided in the current temporary regulations in the case of an outbound distribution of stock of a domestic controlled corporation.

Consistent with the legislative history above and the temporary regulations, the final regulations continue to provide that an outbound section 355 distribution of a foreign controlled corporation is taxable to the distributing corporation. See also sections 367(b) and 1248(f) of the Code. In the case of an outbound section 355 distribution of a domestic controlled corporation, however, the final regulations amend the temporary regulations by providing that the distributing corporation shall obtain the benefit of nonrecognition treatment. In weighing the administrative burdens to taxpayers and the Government in connection with rules requiring gain recognition agreements and similar arrangements, the IRS and Treasury believe that adequate protections are in place to protect the policies of section

367(e)(1). Specifically, significant protections are provided in sections 355(d) and (e) and the device and continuity of interest requirements of section 355.

## B. *Outbound and foreign-to-foreign liquidations*

Generally, a liquidating corporation does not recognize gain or loss on a distribution in complete liquidation into a parent corporation that meets the ownership requirements of section 332(b). See Section 337(a) of the Code. Section 367(e)(2) provides that a section 332 liquidation into a foreign parent is taxed to the liquidating corporation, except to the extent provided in regulations. Section 1.367(e)-2 provides the circumstances under which gain or loss on assets distributed in a section 332 liquidation into a foreign parent is not currently recognized.

Section 332 was enacted in 1935 to encourage the simplification of corporate structures and was retained in 1986 as an exception to the repeal of the General Utilities doctrine. Consistent with the policies of section 332, the final regulations generally tax the distribution of assets in an outbound liquidation but provide exceptions for assets over which the United States retains adequate taxing jurisdiction. The final regulations retain the exceptions in the proposed regulations for a distribution of assets used in the conduct of a U.S. trade or business and for a distribution of a U.S. real property interest (USRPI). In addition, the final regulations provide a new exception for a distribution of stock of a domestic subsidiary that is 80 percent owned by vote and value directly by the liquidating corporation.

In a foreign-to-foreign liquidation, the final regulations generally adopt the rules provided in the proposed regulations. Thus, the regulations generally provide that the liquidation is not taxable, except to the extent that assets used in a U.S. trade or business are distributed and not used in a U.S. trade or business over the subsequent ten-year period. The ten-year period (which is also used in the U.S. trade or business exception for outbound liquidations) supplements the principles contained in section 864(c)(7). The regulations also tax a distribution of assets that had formerly been used in the conduct of a U.S. trade or business by the liquidating corporation.

## II. *Details of Provisions*

### A. *Outbound section 355 distributions*

The final regulations amend the rule in the temporary regulations and do not require gain recognition on an outbound section 355 distribution of the stock or securities of a domestic corporation. The final regulations continue to require gain recognition on an outbound section 355 distribution of the stock or securities of a foreign corporation.

Where gain recognition is required, the final regulations amend the rules for determining the residency status of distributees of stock or securities in an outbound section 355 distribution. A distributee is presumed to be a person who is not a qualified U.S. person (i.e., a person that is not a U.S. citizen, resident, or corporation), except to the extent that the distributing corporation certifies that the distributee is a qualified U.S. person. A publicly traded distributing corporation may use a reasonable analysis with respect to distributees who are not five percent shareholders of publicly traded stock to demonstrate the number of distributees that are qualified U.S. persons. A reasonable analysis includes a determination of the actual number of distributees that are qualified U.S. persons or a reasonable statistical analysis of shareholder records and other relevant information. The final regulations also broaden the look-through rule in the temporary regulations for determining the identity of the distributees of stock or securities of a controlled corporation received by a partnership, trust or estate to include stock or securities received by a disregarded entity.

Section 1.367(e)-1 is applicable to distributions occurring in taxable years ending after August 8, 1999.

### B. *Outbound and foreign-to-foreign liquidations*

#### 1. *General Rule*

The final regulations under section 367(e)(2) contain two sets of rules, depending upon whether the liquidating corporation is domestic or foreign. The final regulations retain the rules of the proposed regulations with respect to foreign-to-foreign liquidations with only minor modification.

In the case of an outbound liquidation, a domestic liquidating corporation is gen-

erally required to recognize gain (or loss) on the distributed assets. In determining the amount of gain or loss recognized under the general rule, the proposed regulations contain an anti-netting rule and an anti-stuffing rule that limit the domestic liquidating corporation's ability to recognize losses.

Several commentators criticized the anti-netting rule contained in the proposed regulations as overly broad because the rule prohibits the netting of ordinary losses against capital gains. The final regulations take this into account and allow the netting of ordinary or capital losses against ordinary or capital gains to the same extent allowed under general rules of the Code, including section 1211.

Commentators also questioned the propriety of the anti-stuffing rule in the proposed regulations and argued that the anti-stuffing rules contained in section 336(d) and the loss limitation rules of section 382 should sufficiently address loss trafficking concerns. The anti-stuffing rule contained in the proposed regulations disallows the recognition of losses attributable to property acquired in capital contributions, section 332 liquidations, and exchanges under sections 351 and 361 within five years of the distribution.

The IRS and Treasury do not believe that sections 336(d) and 382 alone adequately address the Government's loss trafficking concerns. For example, neither section 336(d) nor 382 would limit a liquidating corporation's ability to recognize a loss that is acquired in a reorganization among affiliates even though the loss could not have been recognized if those corporations were liquidated individually. The anti-stuffing rule in the proposed regulations also does not adequately protect against the use of losses to offset gains where the loss corporation acquires the gain property.

After considering the issue, the Treasury and the IRS have amended the anti-stuffing rule in the final regulations to limit the recognition of built-in gains and losses attributable to property received by the domestic liquidating corporation in a reorganization or liquidation occurring within two years prior to the distribution. Sections 336(d) and 382 also limit loss recognition in applicable circumstances.

Comments also requested clarification on the treatment of a distribution of an in-

terest in a publicly traded partnership (PTP). The final regulations provide that an interest in a PTP that is treated as a corporation under section 7704(a) shall be treated in the same manner as stock.

The final regulations retain the look-through rule for a domestic liquidating corporation's distribution of a partnership interest to its foreign parent. The look-through rule provides that, for purposes of the regulation, a domestic liquidating corporation is treated as distributing its proportionate share of the partnership property. The Treasury and the IRS hereby request comments on the proper method of calculating such gain or loss and reserve a section in the final regulations with respect to this issue. Comments should consider the application of similar rules in other cross-border contexts, such as Treas. Reg. §1.367(a)-1T(c)(3).

## 2. Exceptions to General Rule

The proposed regulations contain exceptions to the general gain recognition rule for the distribution of property used in a U.S. trade or business and the distribution of a USRPI. The final regulations retain the two exceptions with some modifications and add an additional exception for stock of a domestic subsidiary corporation.

Under the proposed regulations, a domestic liquidating corporation does not recognize gain (or loss) on the distribution of property used in a U.S. trade or business, if: (1) the foreign parent is not a controlled foreign corporation; (2) the foreign parent continues to use the property in a U.S. trade or business for a ten-year period following the distribution of such property; and (3) the domestic liquidating corporation and the foreign parent attach a statement to their U.S. income tax returns for the year of distribution. If within the ten-year period following a distribution, the property ceases to be used in the foreign parent's U.S. trade or business other than by a disposition, then the foreign parent is required to file an amended U.S. income tax return on behalf of the domestic liquidating corporation and recognize gain thereon. If the foreign parent disposes of such property, then the foreign parent recognizes gain (or loss) on its U.S. income tax return for the year of disposition in lieu of the domestic liquidating corporation recognizing gain on an

amended return for the year of distribution. Also, under the proposed regulations, gain recognition is not triggered on involuntary conversions of such property under section 1033, like-kind exchanges of such property under section 1031, and the abandonment of obsolete or worthless property.

The final regulations modify the U.S. trade or business property exception in response to comments in several respects. First, the final regulations make the exception available to a domestic liquidating corporation that liquidates into a controlled foreign corporation. Second, the final regulations no longer require that the foreign parent file an amended return on behalf of the liquidating corporation when property ceases to be used in the conduct of a U.S. trade or business (whether by disposition or otherwise), provided that the foreign parent properly recognizes gain (or loss in the case of a disposition) as if the property had been sold for fair market value at the time the property ceases to be used in the conduct of a U.S. trade or business. Third, the final regulations expand the types of dispositions that will not trigger gain recognition. U.S. trade or business property may be transferred to another person without gain recognition, if the transfer is a disposition normally entitled to nonrecognition under the Code and the transferor and transferee satisfy various procedural requirements.

The final regulations retain the exception for a distribution of a USRPI contained in the proposed regulation with only minor modification.

The final regulations add a new exception that allows for nonrecognition of gain on a distribution of stock of a domestic subsidiary that is 80 percent owned (by vote and value) directly by the domestic liquidating corporation, provided that the liquidation does not have as a principal purpose the avoidance of U.S. tax on a subsequent disposition of the domestic subsidiary.

## 3. General Anti-abuse Rule

The final regulations contain a new anti-abuse rule that allows the Commissioner to require the liquidating corporation to recognize gain (or treat the liquidating corporation as if it had recognized loss) on the distribution of property pursuant to the liquidation if a principal pur-

pose of the liquidation is the avoidance of U.S. tax. The rule would apply, for example, if a principal purpose of a liquidation is the distribution of a domestic liquidating corporation's earnings and profits without a U.S. withholding tax. In certain circumstances, the Service is also concerned about a liquidation of a domestic corporation into a U.S. branch of a foreign corporation in a manner that facilitates the avoidance of U.S. tax, including the inappropriate use of attributes such as net operating losses. Liquidations used to facilitate the avoidance of tax may be challenged under existing law. The Treasury and the IRS hereby solicit comments, however, as to other measures that should be taken to adequately address such transactions, including the more specific identification of the conditions under which liquidated property, particularly securities and other financial instruments, may be considered to be used in a U.S. trade or business.

## 4. Effective Date

Section 1.367(e)-2 is applicable to distributions occurring 30 days after August 9, 1999 or, if a taxpayer elects, to distributions in taxable years ending after August 8, 1999. In addition, taxpayers may rely on the principles contained in the temporary regulations issued under section 367(e)(2) on January 16, 1990 for distributions occurring prior to 30 days after August 9, 1999.

## C. Section 6038B

The regulations under section 6038B are also revised to require reporting for transactions described in section 367(e)(1) and (2) in accordance with the final regulations under section 367(e)(1) and (2).

## Special Analyses

It has been determined that these regulations are not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It is hereby certified that the collections of information contained in this regulation 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(e) distributions that require

reporting under these regulations is estimated to be only 400 per year. Moreover, because these regulations will primarily affect large multinational corporations, it is estimated that out of the 400 transactions very few, if any, will involve small entities. Thus, 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, the notice of proposed rulemaking preceding these regulations was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on the impact of the proposed regulations on small business.

#### *Drafting Information*

The principal author of these regulations is Guy A. Bracuti 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 removing the entry for 1.367(e)–1T and by adding entries in numerical order to read in part as follows:

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

Section 1.367(e)–1 also issued under 26 U.S.C. 367(e)(1).

Section 1.367(e)–2 also issued under 26 U.S.C. 367(e)(2). \* \* \*

#### **§1.367(e)–0T through §1.367(e)–2T [Removed]**

Par. 2. Sections 1.367(e)–0T, 1.367(e)–1T, and 1.367(e)–2T are removed.

Par. 3. Sections 1.367(e)–0, 1.367(e)–1, and 1.367(e)–2 are added to read as follows:

#### *§1.367(e)–0 Outline of §§1.367(e)–1 and 1.367(e)–2.*

This section lists captioned paragraphs contained in §§1.367(e)–1 and 1.367(e)–2 as follows:

#### *§1.367(e)–1 Distributions described in section 367(e)(1).*

- (a) Purpose and scope.
- (b) Gain recognition.
- (1) General rule.
- (2) Stock owned through partnerships, disregarded entities, trusts, and estates.
- (3) Gain computation.
- (4) Treatment of distributee.
- (c) Nonrecognition of gain.
- (d) Determining whether distributees are qualified U.S. persons.
- (1) General rule—presumption of foreign status.
- (2) Non-publicly traded distributing corporations.
- (3) Publicly traded distributing corporations.
- (i) Five percent shareholders.
- (ii) Other distributees.
- (4) Qualified exchange or other market.
- (e) Reporting under section 6038B.
- (f) Effective date.

#### *§1.367(e)–2 Distributions described in section 367(e)(2).*

- (a) Purpose and scope.
- (1) In general.
- (2) Nonapplicability of section 367(a).
- (b) Distribution by a domestic corporation.
- (1) General rule.
- (i) Recognition of gain and loss.
- (ii) Operating rules.
- (A) General rule.
- (B) Overall loss limitation.
- (I) Overall loss limitation rule.
- (2) Example.
- (C) Special rules for built-in gains and losses attributable to property received in liquidations and reorganizations.
- (iii) Distribution of partnership interest.
- (A) General rule.
- (B) Gain or loss calculation. [Reserved]
- (C) Basis adjustments.
- (D) Publicly traded partnerships.
- (2) Exceptions.
- (i) Distribution of property used in a U.S. trade or business.
- (A) Conditions for nonrecognition.
- (B) Qualifying property.
- (C) Required statement.
- (I) Declaration and certification.
- (2) Property description.

- (3) Distributee identification.
- (4) Treaty benefits waiver.
- (5) Statute of limitations extension.
- (D) Failure to file statement.
- (E) Operating rules.
- (I) Gain or loss recognition by the foreign distributee corporation.
- (i) Taxable dispositions.
- (ii) Other triggering events.
- (2) Gain recognition by the domestic liquidating corporation.
- (i) General rule.
- (ii) Amended return.
- (iii) Interest.
- (iv) Joint and several liability.
- (3) Schedule for property no longer used in a U.S. trade or business.
- (4) Nontriggering events.
- (i) Conversions, certain exchanges, and abandonment.
- (ii) Amendment to Master Property Description
- (5) Nontriggering transfers to qualified transferees.
- (ii) Distribution of certain U.S. real property interests.
- (iii) Distribution of stock of domestic subsidiary corporations.
- (A) Conditions for nonrecognition.
- (B) Exceptions when the liquidating corporation is a U.S. real property holding corporation.
- (C) Anti-abuse rule.
- (D) Required statement.
- (3) Other consequences.
- (i) Distributee basis in property.
- (ii) Reporting under section 6038B.
- (iii) Other rules.
- (c) Distribution by a foreign corporation.
- (1) General rule—gain and loss not recognized.
- (2) Exceptions.
- (i) Property used in a U.S. trade or business.
- (A) General rule.
- (B) Ten-year active U.S. business exception.
- (C) Required statement.
- (D) Operating rules.
- (ii) Property formerly used in a U.S. trade or business.
- (3) Other consequences.
- (i) Distributee basis in property.
- (ii) Other rules.
- (d) Anti-abuse rule.
- (e) Effective date.

*§1.367(e)-1 Distributions described in section 367(e)(1).*

(a) *Purpose and scope.* This section provides rules for recognition (and non-recognition) of gain by a domestic corporation (distributing corporation) on a distribution of stock or securities of a corporation (controlled corporation) to foreign persons that is described in section 355. Paragraph (b) of this section contains the general rule that gain is recognized on the distribution to the extent stock or securities of controlled are distributed to foreign persons. Paragraph (c) of this section provides an exception to the gain recognition rule for distributions of stock or securities of a domestic corporation. Paragraph (d) of this section contains rules for determining whether distributees of stock or securities in a section 355 distribution are qualified U.S. persons. Paragraph (e) of this section cross-references section 6038B for certain reporting obligations. Finally, paragraph (f) of this section specifies the effective date of this section.

(b) *Gain recognition—(1) General rule.* If a domestic corporation makes a distribution of stock or securities of a corporation that qualifies for nonrecognition under section 355 to a person who is not a qualified U.S. person, then, except as provided in paragraph (c) of this section, the distributing corporation shall recognize gain (but not loss) on the distribution under section 367(e)(1). A distributing corporation shall not recognize gain under this section with respect to a section 355 distribution to a qualified U.S. person. For purposes of this section, a qualified U.S. person is—

(A) A citizen or resident of the United States; or

(B) A domestic corporation.

(2) *Stock owned through partnerships, disregarded entities, trusts, and estates.* For purposes of this section, distributing corporation stock or securities owned by or for a partnership (whether foreign or domestic) are owned proportionately by its partners. A partner's proportionate share of the stock or securities of the distributing corporation shall be equal to the partner's distributive share of the gain that would have been recognized had the partnership sold the stock or securities (at a taxable gain) immediately before the distribution. The partner's distributive

share of gain shall be determined under the rules and principles of sections 701 through 761 and the regulations thereunder. For purposes of this section, stock or securities owned by or for an entity that is disregarded as an entity (disregarded entity) under §1.7701-3(b)(1)(ii) or (b)(2)(i)(C) are owned directly by the owner of such disregarded entity. For purposes of this section, stock or securities owned by or for a trust or estate (whether foreign or domestic) are owned proportionately by the persons who would be treated as owning such stock or securities under section 318(a)(2)(A) and (B). In applying section 318(a)(2)(B)(i), if a trust includes interests that are not actuarially ascertainable, all such interests shall be considered to be owned by foreign persons. In a case where an interest holder in a partnership, a disregarded entity, trust, or estate that (directly or indirectly) owns stock of the distributing corporation is itself a partnership, disregarded entity, trust, or estate, the rules of this paragraph (b)(2) apply to such interest holder.

(3) *Gain computation.* Gain recognized under paragraph (b)(1) of this section shall be equal to the excess of the fair market value of the stock or securities distributed to persons who are not qualified U.S. persons (determined as of the time of the distribution) over the distributing corporation's adjusted basis in the stock or securities distributed to such distributees. For purposes of the preceding sentence, the distributing corporation's adjusted basis in each unit of each class of stock or securities distributed to a distributee shall be equal to the distributing corporation's total adjusted basis in all of the units of the respective class of stock or securities owned immediately before the distribution, divided by the total number of units of the class of stock or securities owned immediately before the distribution.

(4) *Treatment of distributee.* If the distribution otherwise qualifies for nonrecognition under section 355, each distributee shall be considered to have received stock or securities in a distribution qualifying for nonrecognition under section 355, even though the distributing corporation may recognize gain on the distribution under this section. Thus, the distributee shall not be considered to have received a distribution described in section 301 or a distribution in an exchange

described in section 302(b) upon the receipt of the stock or securities of the controlled corporation, and the domestic distributing corporation shall have no withholding responsibilities under section 1441. Except where section 897(e)(1) and the regulations thereunder cause gain to be recognized by the distributee, the basis of the distributed domestic or foreign corporation stock in the hands of the foreign distributee shall be the basis of the distributed stock determined under section 358 without any increase for any gain recognized by the domestic corporation on the distribution.

(c) *Nonrecognition of gain.* A domestic distributing corporation shall not recognize gain under paragraph (b)(1) of this section on the distribution of stock or securities of a domestic corporation.

(d) *Determining whether distributees are qualified U.S. persons—(1) General rule—presumption of foreign status.* Except as provided in paragraphs (d)(2) and (3) of this section, all distributions of stock or securities in a distribution described in paragraph (b)(1) of this section are presumed to be to persons who are not qualified U.S. persons, as defined in paragraph (b)(1) of this section.

(2) *Non-publicly traded distributing corporations.* If the class of stock or securities of the distributing corporation (in respect to which stock or securities of the controlled corporation are distributed) is not regularly traded on a qualified exchange or other market (as defined in paragraph (d)(4) of this section), then the distributing corporation may only rebut the presumption contained in paragraph (d)(1) of this section by identifying the qualified U.S. persons to which controlled corporation stock or securities were distributed and by certifying the amount of stock or securities that were distributed to the qualified U.S. persons.

(3) *Publicly traded distributing corporations.* If the class of stock or securities of the distributing corporation (in respect to which stock or securities of the controlled corporation are distributed) is regularly traded on a qualified exchange or other market (as defined in paragraph (d)(4) of this section), then the distributing corporation may only rebut the presumption contained in paragraph (d)(1) of this section as described in this paragraph (d)(3).

(i) *Five percent shareholders.* A publicly traded distributing corporation may only rebut the presumption contained in paragraph (d)(1) of this section with respect to distributees that are five percent shareholders of the class of stock or securities of the distributing corporation (in respect to which stock or securities of the controlled corporation are distributed) by identifying the qualified U.S. persons to which controlled corporation stock or securities were distributed and by certifying the amount of stock or securities that were distributed to the qualified U.S. persons. A five percent shareholder is a distributee who is required under U.S. securities laws to file with the Securities and Exchange Commission (SEC) a Schedule 13D or 13G under 17 CFR 240.13d-1 or 17 CFR 240.13d-2, and provide a copy of same to the distributing corporation under 17 CFR 240.13d-7.

(ii) *Other distributees.* A distributing corporation that has made a distribution described in paragraph (d)(3) of this section may rebut the presumption contained in paragraph (d)(1) of this section with respect to distributees that are not five percent shareholders (as defined in this paragraph (d)(3)) by relying on and providing a reasonable analysis of shareholder records and other relevant information that demonstrates a number of distributees that are qualified U.S. persons. Taxpayers may rely on such analysis, unless it is subsequently determined that there are actually fewer distributees who are qualified U.S. persons than were demonstrated in the analysis.

(4) *Qualified exchange or other market.* For purposes of paragraph (d) of this section, the term qualified exchange or other market means, for any taxable year—

(i) A national securities exchange which is registered with the SEC or the national market system established pursuant to section 11A of the Securities Exchange Act of 1934 (15 U.S.C. 78f); or

(ii) A foreign securities exchange that is regulated or supervised by a governmental authority of the country in which the market is located and which has the following characteristics—

(A) The exchange has trading volume, listing, financial disclosure, and other requirements designed to prevent fraudulent and manipulative acts and practices, to remove impediments to and perfect the

mechanism of a free and open market, and to protect investors; and the laws of the country in which the exchange is located and the rules of the exchange ensure that such requirements are actually enforced; and

(B) The rules of the exchange ensure active trading of listed stocks.

(e) *Reporting under section 6038B.* See the regulations under section 6038B for reporting requirements for distributions under this section.

(f) *Effective date.* This section shall be applicable to distributions occurring in taxable years ending after August 8, 1999.

#### *§1.367(e)-2 Distributions described in section 367(e)(2).*

(a) *Purpose and scope—(1) In general.* This section provides rules requiring gain and loss recognition by a corporation on its distribution of property to a foreign corporation in a complete liquidation described in section 332. Paragraph (b)(1) of this section contains the general rule that gain and loss are recognized when a domestic corporation makes a distribution of property in complete liquidation under section 332 to a foreign corporation that meets the stock ownership requirements of section 332(b) with respect to stock in the domestic corporation. Paragraph (b)(2) of this section provides the only exceptions to the gain and loss recognition rule of paragraph (b)(1) of this section. Paragraph (b)(3) of this section refers to other consequences of distributions described in paragraphs (b)(1) and (2) of this section. Paragraph (c)(1) of this section contains the general rule that gain and loss are not recognized when a foreign corporation makes a distribution of property in complete liquidation under section 332 to a foreign corporation that meets the stock ownership requirements of section 332(b) with respect to stock in the foreign liquidating corporation. Paragraph (c)(2) of this section provides the only exceptions to the nonrecognition rule of paragraph (c)(1) of this section. Paragraph (c)(3) of this section refers to other consequences of distributions described in paragraphs (c)(1) and (2) of this section. Paragraph (d) of this section contains an anti-abuse rule. Finally, paragraph (e) of this section specifies the effective date for the rules of this section.

The rules of this section are issued pursuant to the authority conferred by section 367(e)(2).

(2) *Nonapplicability of section 367(a).* Section 367(a) shall not apply to a complete liquidation described in section 332 by a domestic liquidating corporation into a foreign corporation that meets the stock ownership requirements of section 332(b).

(b) *Distribution by a domestic corporation—(1) General rule—(i) Recognition of gain and loss.* If a domestic corporation (domestic liquidating) makes a distribution of property in complete liquidation under section 332 to a foreign corporation (foreign distributee) that meets the stock ownership requirements of section 332(b) with respect to stock in the domestic liquidating corporation, then—

(A) Pursuant to section 367(e)(2), section 337(a) and (b)(1) shall not apply; and

(B) The domestic liquidating corporation shall recognize gain or loss on the distribution of property to the foreign distributee, except as provided in paragraph (b)(2) of this section.

(ii) *Operating rules—(A) General rule.* Except as provided in paragraphs (b)(1)-(ii)(B) and (C) of this section, the rules contained in section 336 will apply to the gain and loss recognized pursuant to this section.

(B) *Overall loss limitation—(1) Overall loss limitation rule.* Loss in excess of gain from the distribution shall not be recognized. If realized losses exceed recognized losses, the losses shall be recognized on a pro rata basis with respect to the realized loss attributable to each distributed loss asset in the category of assets (i.e., capital or ordinary) to which the realized but unrecognized loss relates. For additional limitations on the recognition of losses, see, e.g., section 1211.

(2) *Example.* The following example illustrates the overall loss limitation rule, the pro rata loss allocation method, and the general capital loss limitation rule in section 1211(a):

*Example.* F, a foreign corporation, owns all stock of US1, a domestic corporation. US1 owns the following capital assets: Asset A, which has a fair market value of \$100 and an adjusted basis of \$40; Asset B, which has a fair market value of \$60 and an adjusted basis of \$80; and, Asset C, which has a fair market value of \$40 and an adjusted basis of \$100. US1 also owns the following business assets that

will generate ordinary income (or loss) upon disposition: Asset D, which has a fair market value of \$100 and an adjusted basis of \$40; Asset E, which has a fair market value of \$60 and an adjusted basis of \$100; and, Asset F, which has a fair market value of \$40 and an adjusted basis of \$80. US1 liquidates into F and distributes all assets to F in liquidation. None of the assets qualify for nonrecognition under paragraph (b)(2) of this section. US1's total realized capital loss is \$80, but it may only recognize \$60 of that loss. See section 1211(a). US1's total realized ordinary loss is \$80, but it may only recognize \$60 of that loss. See paragraph (b)(1)(ii)(B)(I) of this section. US1 will allocate \$45 ( $60 \times .75$ ) of the recognized capital loss to Asset B and will allocate the remaining \$15 ( $60 \times .25$ ) of recognized capital loss to Asset C. See paragraph (b)(1)(ii)(B)(I) of this section. US1 will allocate \$30 ( $60 \times .50$ ) of the recognized ordinary loss to Asset E and will allocate the remaining \$30 ( $60 \times .50$ ) to Asset F. See paragraph (b)(1)(ii)(B)(I) of this section.

(C) *Special rules for built-in gains and losses attributable to property received in liquidations and reorganizations.* Built-in losses attributable to property received in a transaction described in sections 332 or 361 (during the two-year period ending on the date of the distribution in liquidation covered by this section) shall not offset gain from property not received in the same transaction. Built-in gains attributable to property received in a transaction described in sections 332 or 361 (during the two-year period ending on the date of the distribution in liquidation covered by this section) shall not offset loss from property not received in the same transaction. Built-in gain or loss is that amount of gain or loss on property that existed at the time the domestic liquidating corporation acquired such property. See sections 336(d) and 382 for additional limitations on the recognition of losses.

(iii) *Distribution of partnership interest*—(A) *General rule.* If a domestic corporation distributes a partnership interest (whether foreign or domestic) in a distribution described in paragraph (b)(1)(i) of this section, then for purposes of applying this section the domestic liquidating corporation shall be treated as having distributed a proportionate share of partnership property. Accordingly, the applicability of the recognition rules of paragraphs (b)(1)(i) and (ii) of this section, and of any exception to recognition provided in this section shall be determined with reference to the partnership property, rather than to the partnership interest itself. Where the partnership property includes an interest in a lower-tier partnership, the applicabil-

ity of any exception with respect to the interest in the lower-tier partnership shall be determined with reference to the lower-tier partnership property. In the case of multiple tiers of partnerships, the applicability of an exception shall be determined with reference to the property of each partnership, applying the rule contained in the preceding sentence. A domestic liquidating corporation's proportionate share of partnership property shall be determined under the rules and principles of sections 701 through 761 and the regulations thereunder.

(B) *Gain or loss calculation.* [Reserved]

(C) *Basis adjustments.* The foreign distributee corporation's basis in the distributed partnership interest shall be equal to the domestic liquidating corporation's basis in such partnership interest immediately prior to the distribution, increased by the amount of gain and reduced by the amount of loss recognized by the domestic liquidating corporation on the distribution of the partnership interest. Solely for purposes of sections 743 and 754, the foreign distributee corporation shall be treated as having purchased the partnership interest for an amount equal to the foreign corporation's adjusted basis therein.

(D) *Publicly traded partnerships.* The distribution by a domestic liquidating corporation of an interest in a publicly traded partnership that is treated as a corporation for U.S. income tax purposes under section 7704(a) shall not be subject to the rules of paragraphs (b)(1)(iii)(A) and (B) of this section. Instead, the distribution of such an interest shall be treated in the same manner as a distribution of stock. Thus, a transfer of an interest in a publicly traded partnership that is treated as a U.S. corporation for U.S. income tax purposes shall be treated in the same manner as stock in a domestic corporation, and a transfer of an interest in a publicly traded partnership that is treated as a foreign corporation for U.S. income tax purposes shall be treated in the same manner as stock in a foreign corporation.

(2) *Exceptions*—(i) *Distribution of property used in a U.S. trade or business*—(A) *Conditions for nonrecognition.* A domestic liquidating corporation shall not recognize gain or loss under paragraph (b)(1) of this section on its distribu-

tion of property (including inventory) used by the domestic liquidating corporation in the conduct of a trade or business within United States, if—

(1) The foreign distributee corporation, immediately thereafter and for the ten-year period beginning on the date of the distribution of such property, uses the property in the conduct of a trade or business within the United States;

(2) The domestic liquidating corporation attaches the statement described in paragraph (b)(2)(i)(C) of this section to its U.S. income tax returns for the taxable years that include the distributions in liquidation; and

(3) The foreign distributee corporation attaches a copy of the property description contained in paragraph (b)(2)(i)(C)(2) of this section to its U.S. income tax return for the tax year that includes the date of distribution.

(B) *Qualifying property.* Property is used by the foreign distributee corporation in the conduct of a trade or business in the United States within the meaning of this paragraph (b)(2)(i) only if all income from the use of the property and all income or gain from the sale or exchange of the property would be subject to taxation under section 882(a) as effectively connected income. Also, stock held by a dealer as inventory or for sale in the ordinary course of its trade or business shall be treated as inventory and not as stock in the hands of both the domestic liquidating corporation and the distributee foreign corporation. Notwithstanding the foregoing, the exception provided in this paragraph (b)(2)(i) shall not apply to intangibles described in section 936(h)(3)(B).

(C) *Required statement.* The statement required by paragraph (b)(2)(i)(A) of this section shall be entitled "Required Statement under §1.367(e)-2(b)(2)(i)" and shall be prepared by the domestic liquidating corporation and signed under penalties of perjury by an authorized officer of the domestic liquidating corporation and by an authorized officer of the foreign distributee corporation. The statement shall contain the following items:

(1) *Declaration and certification.* A declaration that the distribution to the foreign distributee corporation is one to which the rules of this paragraph (b)(2)(i) apply and a certification that the domestic liquidating corporation and the foreign



distributee corporation agree to all of the terms and conditions set forth in this paragraph (b)(2)(i).

(2) *Property description.* A description of all property distributed by the domestic liquidating corporation (irrespective of whether the property qualifies for nonrecognition). Such description shall be entitled “Master Property Description” and shall identify the property that continues to be used by the foreign distributee corporation in the conduct of a trade or business within the United States, including the location, adjusted basis, estimated fair market value, a summary of the method (including appraisals if any) used for determining such value, and the date of distribution of such items of property. The description shall also identify the property excepted from gain recognition under paragraphs (b)(2)(ii) and (iii) of this section.

(3) *Distributee identification.* An identification of the foreign distributee corporation, including its name and address, taxpayer identification number, residence, and place of incorporation.

(4) *Treaty benefits waiver.* With respect to property entitled to nonrecognition pursuant to this paragraph (b)(2)(i), a declaration by the foreign distributee corporation that it irrevocably waives any right under any treaty (whether or not currently in force at the time of the liquidation) to sell or exchange any item of such property without U.S. income taxation or at a reduced rate of taxation, or to derive income from the use of any item of such property without U.S. income taxation or at a reduced rate of taxation.

(5) *Statute of limitations extension.* An agreement by the domestic liquidating corporation and the foreign distributee corporation to extend the statute of limitations on assessments and collections (under section 6501) with respect to the domestic liquidating corporation on the distribution of each item of property until three years after the date on which all such items of property have ceased to be used in a trade or business within the United States, but in no event shall the extension be for a period longer than 13 years from the filing of the original U.S. income tax return for the taxable year of the last distribution of any such item of property. The agreement to extend the statute of limitation shall be executed on a

Form 8838, “Consent to Extend the Time to Assess Tax Under Section 367—Gain Recognition Agreement.”

(D) *Failure to file statement.* If a domestic liquidating corporation that would otherwise qualify for nonrecognition on the distribution of property under this paragraph (b)(2)(i) fails to file the statement described in paragraph (b)(2)(i)(C) of this section or files a statement that does not comply with the requirements of paragraph (b)(2)(i)(C) of this section, the Commissioner may treat the domestic liquidating corporation as if it had claimed nonrecognition under this paragraph (b)(2)(i) and met all the requirements of paragraph (b)(2)(i)(C) of this section, if such treatment is necessary to prevent the domestic liquidating corporation or the foreign distributee corporation from otherwise deriving a tax benefit by such failure.

(E) *Operating rules.* By the domestic liquidating corporation’s claiming nonrecognition under this paragraph (b)(2)(i) and filing a statement described in paragraph (b)(2)(i)(C) of this section, the domestic liquidating corporation and the foreign distributee corporation agree to be subject to the rules of this paragraph (b)(2)(i)(E).

(I) *Gain or loss recognition by the foreign distributee corporation—(i) Taxable dispositions.* If, within the ten-year period from the date of a distribution of qualifying property, the foreign distributee corporation disposes of any qualifying property in a transaction subject to tax under section 882(a), then the foreign distributee corporation shall recognize such gain (or loss) and properly report it on a timely filed U.S. income tax return. If the foreign distributee corporation recognizes such gain (or loss) under this paragraph (b)(2)(i)(E)(I)(i) and properly reports such gain (or loss) on its U.S. income tax return, then the domestic liquidating corporation shall not recognize gain attributable to such property under paragraph (b)(2)(i)(E)(2) of this section.

(ii) *Other triggering events.* If, within the ten-year period from the date of distribution, any qualifying property ceases to be used by the foreign distributee corporation in the conduct of a trade or business in the United States (other than by reason of a taxable disposition described in paragraph (b)(2)(i)(E)(I)(i) of this section, a nontriggering event described in para-

graph (b)(2)(i)(E)(4) of this section, or a nontriggering transfer described in paragraph (b)(2)(i)(E)(5) of this section), then the foreign distributee corporation shall recognize gain (but not loss) attributable to such property and properly report it on a timely filed U.S. income tax return. If the foreign distributee corporation properly reports gain under this paragraph (or if such qualified property is not gain property on the date that it ceases to be used in the foreign distributee corporation’s U.S. trade or business), then the domestic liquidating corporation shall not recognize gain attributable to such property under paragraph (b)(2)(i)(E)(2) of this section. The gain recognized under this paragraph (b)(2)(i)(E)(I)(ii) shall be an amount equal to the fair market value of the property on the date it ceases to be used in the foreign distributee corporation’s U.S. trade or business less the foreign distributee corporation’s adjusted basis in such property.

(2) *Gain recognition by the domestic liquidating corporation—(i) General rule.* If, within the ten-year period from the date of distribution, any qualifying property described in paragraph (b)(2)(i)(B) of this section ceases to be used by the foreign distributee corporation (or a qualifying transferee described in paragraph (b)(2)(i)(E)(5) of this section) in the conduct of a trade or business in the United States for any reason (including but not limited to the sale or exchange of such property or the removal of the property from conduct of the trade or business), then, except to the extent gain (or loss) is recognized under paragraph (b)(1)(i)(E)(I) of this section, the domestic liquidating corporation shall recognize the gain (but not loss) realized but not recognized upon the initial distribution of such item of property. The domestic liquidating corporation shall recognize gain pursuant to this paragraph (b)(2)(i)(E)(2)(i) on the amended U.S. income tax return described in paragraph (b)(2)(i)(E)(2)(ii) of this section.

(ii) *Amended return.* If gain recognition is required pursuant to paragraph (b)(2)(i)(E)(2)(i) of this section, the foreign distributee corporation shall file an amended U.S. income tax return on behalf of the domestic liquidating corporation for the year of the distribution of such item of property. On the amended return,

the domestic liquidating corporation may use any losses (or credits) existing in the year of the distribution to offset the gain recognized pursuant to paragraph (b)(2)(i)(E)(2)(i) of this section (or the tax thereon), provided that the losses (or credits) were otherwise available in the year distribution and were not used in another year. The amended return shall be filed no later than the due date (including extensions) for the return of the foreign distributee corporation for the taxable year in which the property ceases to be used by the foreign distributee corporation in the conduct of a trade or business in the United States.

(iii) *Interest.* If the domestic liquidating corporation owes additional tax pursuant to paragraph (b)(2)(i)(E)(2)(i) of this section for the year of liquidation, then interest must be paid on that amount at the rates determined under section 6621. The interest due will be calculated from the due date of the domestic liquidating corporation's U.S. income tax return for the year of the distribution to the date on which the additional tax for that year is paid.

(iv) *Joint and several liability.* The foreign distributee corporation shall be jointly and severally liable for any tax owed by the domestic liquidating corporation as a result of the application of this section, and shall succeed to the domestic liquidating corporation's agreement to extend the statute of limitations on assessments and collections under section 6501.

(3) *Schedule for property no longer used in a U.S. trade or business.* If qualifying property (other than inventory) ceases to be used by the foreign distributee corporation in the conduct of a U.S. trade or business in the ten-year period beginning on the date of distribution of such property from the domestic liquidating corporation to the foreign distributee corporation, then the foreign distributee corporation shall list on a separate schedule (attached to its U.S. income tax return for the year of cessation) all such qualifying property. For purposes of this paragraph (b)(2)(i)(E)(3), property ceases to be used in a U.S. trade or business whenever such property is sold, exchanged, or otherwise removed from the U.S. trade or business, irrespective of whether the domestic liquidating corporation filed an amended return under paragraph

(b)(2)(i)(E)(2) of this section, and irrespective of whether the property ceases to be used in the foreign distributee corporation's U.S. trade or business by virtue of a nontriggering event described in paragraph (b)(2)(i)(E)(4) of this section or a nontriggering transfer described in paragraph (b)(2)(i)(E)(5) of this section.

(4) *Nontriggering events—(i) Conversions, certain exchanges, and abandonment.* Gain (or loss) under this paragraph (b)(2)(i)(E) shall not be triggered if qualifying property described in paragraph (b)(2)(i)(B) of this section is involuntarily converted into, or exchanged for, similar qualifying property used in the conduct of a trade or business in the United States, to the extent such conversion or exchange qualifies for nonrecognition under sections 1033 or 1031. Also, the abandonment or disposal of worthless or obsolete property shall not trigger gain (or loss) under this paragraph (b)(2)(i)(E).

(ii) *Amendment to Master Property Description.* If the foreign distributee corporation acquires replacement property by virtue of a conversion or exchange of the qualifying property under this paragraph (b)(2)(i)(E)(4), then the foreign distributee corporation shall attach to its U.S. income tax return for the year of the acquisition such replacement property a schedule entitled "Amendment to Master Property Description Required by §1.367(e)-2(b)(2)(i)" that lists the replacement property and the property being replaced.

(5) *Nontriggering transfers to qualified transferees.* Gain (or loss) under this paragraph (b)(2)(i)(E) will not be triggered if qualifying property described in paragraph (b)(2)(i)(B) of this section is transferred to another person (qualified transferee) in a transaction qualifying for nonrecognition under the Internal Revenue Code (other than transactions described in paragraphs (b)(2)(i)(E)(4)(i) and (c)(1) of this section), if—

(i) The qualified transferee (and all other subsequent qualified transferees), immediately thereafter and for the ten-year period beginning on the date of the initial distribution of such qualifying property from the domestic liquidating corporation to the foreign distributee corporation, uses the property in the conduct of a trade or business in the United States;

(ii) The foreign distributee corporation (or its successor in interest) prepares and attaches to its U.S. income tax return for the year of transfer a statement entitled "Required Statement under §1.367(e)-2(b)(2)(i)(E)(5) for Property Transferred to a Qualified Transferee" that is signed under penalties of perjury by an authorized officer of the foreign distributee corporation and by a person similarly authorized by the qualified transferee;

(iii) The statement described in paragraph (b)(2)(i)(E)(5)(ii) of this section shall contain a description of all qualifying property transferred by the foreign distributee corporation (or qualified transferee) to the qualified transferee (or subsequent qualified transferee);

(iv) The statement described in paragraph (b)(2)(i)(E)(5)(ii) of this section shall also contain an identification of the qualified transferee (or subsequent qualified transferee), including its name and address, taxpayer identification number, residence, and place of incorporation (if applicable);

(v) The statement described in paragraph (b)(2)(i)(E)(5)(ii) of this section shall also contain a declaration by the qualifying transferee (or subsequent qualifying transferee) that it irrevocably waives any right under any treaty (whether or not currently in force at the time of the liquidation) to sell or exchange any item of such property without U.S. income taxation or at a reduced rate of taxation, or to derive income from the use of any item of such qualifying property without U.S. income taxation or at a reduced rate of taxation; and

(vi) A declaration that the transfer to the qualifying transferee (or subsequent qualifying transferee) is one to which the rules of this paragraph (b)(2)(i)(E)(5) apply and a certification that the foreign distributee corporation (or its successor in interest) and the qualifying transferee (or subsequent qualifying transferee) agree to all of the terms and conditions set forth in paragraph (b)(2)(i)(E)(I) of this section, replacing "foreign distributee corporation" with "qualifying transferee" and replacing references to "section 882(a)" with "section 871(b)" (as the case may be).

(ii) *Distribution of certain U.S. real property interests.* A domestic liquidating corporation shall not recognize gain (or loss) under paragraph (b)(1) of this sec-

tion on the distribution of a U.S. real property interest (other than stock in a former U.S. real property holding corporation that is treated as a U.S. real property interest for five years under section 897(c)(1)(A)(ii)). If property distributed by the domestic liquidating corporation is a U.S. real property interest that qualifies for nonrecognition under this paragraph (b)(2)(ii) in addition to nonrecognition provided by paragraph (b)(2)(i) of this section, then the domestic liquidating corporation shall secure nonrecognition pursuant to this paragraph (b)(2)(ii) and not pursuant to the provisions of paragraph (b)(2)(i) of this section.

(iii) *Distribution of stock of domestic subsidiary corporations*—(A) *Conditions for nonrecognition.* A domestic liquidating corporation shall not recognize gain or loss under paragraph (b)(1) of this section on a distribution of stock of an 80 percent domestic subsidiary corporation, if the domestic liquidating corporation attaches a statement described in paragraph (b)(2)(iii)(D) of this section to its U.S. income tax return for the year of the distribution of such stock. For purposes of this paragraph (b)(2)(iii), a corporation is an 80 percent domestic subsidiary corporation, if—

(I) The subsidiary corporation is a domestic corporation (but not a foreign corporation that has made an election under section 897(i) to be treated as a U.S. corporation for purposes of section 897);

(2) The domestic liquidating corporation owns (directly) at least 80 percent of the total voting power of the stock of such corporation; and

(3) The domestic liquidating corporation owns (directly) at least 80 percent of the total value of all stock of such corporation.

(B) *Exceptions when the liquidating corporation is a U.S. real property holding corporation.* If the domestic liquidating corporation is a U.S. real property holding corporation (as defined in section 897(c)(2)) at the time of liquidation (or was a U.S. real property holding corporation with respect to the foreign distributee corporation during the five year period ending on the date of liquidation), then the exception in paragraph (b)(2)(iii)(A) of this section shall apply only to the distribution of stock of an 80 percent domestic subsidiary corporation that is a U.S.

real property holding corporation (as defined in section 897(c)(2)) at the time of the liquidation and immediately thereafter.

(C) *Anti-abuse rule.* (I) The exception in paragraph (b)(2)(iii)(A) of this section shall not apply, if a principal purpose of the distribution of the 80 percent domestic subsidiary corporation's stock is the avoidance of U.S. tax that would have been imposed on the domestic liquidating corporation's disposition of such stock (directly or indirectly) to an unrelated party. A distribution may have a principal purpose of tax avoidance even though the tax avoidance purpose is outweighed by other purposes (taken together or separately).

(2) For purposes of paragraph (b)(2)(iii)(C)(I) of this section, a distribution of stock of the 80 percent domestic subsidiary corporation will be deemed to have been made pursuant to a plan, one of the principal purposes of which was the avoidance of U.S. tax, if the foreign distributee corporation disposes of any such stock within two years of such distribution. The rule in this paragraph (b)(2)(iii)(C)(2) will not apply if the foreign distributee corporation can demonstrate to the satisfaction of the Commissioner that a principal purpose of the liquidation was not the avoidance of U.S. tax.

(D) *Required statement.* The statement required by paragraph (b)(2)(iii)(A) of this section shall be entitled "Required Statement under §1.367(e)–2(b)(2)(iii) for Stock of 80 Percent Domestic Subsidiary Corporations" and shall be prepared by the domestic liquidating corporation and shall be signed under penalties of perjury by an authorized officer of the domestic liquidating corporation and by an authorized officer of the foreign distributee corporation. The required statement shall contain a certification that states that if the foreign distributee corporation disposes of any stock subject to paragraph (b)(2)(iii)(A) of this section in a transaction described in paragraph (b)(2)(iii)(C) of this section, then the domestic liquidating corporation shall recognize all realized gain attributable to such stock at the time of distribution, and the domestic liquidating corporation (or the foreign distributee corporation on behalf of the domestic liquidating corporation) shall file a U.S. income tax return

(or amended U.S. income tax return, as the case may be) for the year of distribution reporting the gain attributable to such stock.

(3) *Other consequences*—(i) *Distributee basis in property.* The foreign distributee corporation's basis in property subject to this paragraph (b) shall be the same as the domestic liquidating corporation's basis in such property immediately before the liquidation, increased by any gain, or reduced by any loss recognized by the domestic liquidating corporation on such property pursuant to paragraph (b)(1) of this section. In no case, however, will the foreign distributee corporation's adjusted basis in distributed property exceed the fair market value of such property at the time of liquidation.

(ii) *Reporting under section 6038B.* Section 6038B and the regulations thereunder apply to a domestic liquidating corporation's transfer of property to a foreign distributee corporation under section 367(e)(2).

(iii) *Other rules.* For other rules that may be applicable, see sections 1248, 897, and 381.

(c) *Distribution by a foreign corporation*—(1) *General rule—gain and loss not recognized.* If a foreign corporation (foreign liquidating) makes a distribution of property in complete liquidation under section 332 to a foreign corporation (foreign distributee) that meets the stock ownership requirements of section 332(b) with respect to stock in the foreign liquidating corporation, then, except as provided in paragraph (c)(2) of this section, section 337(a) and (b)(1) shall apply and the foreign liquidating corporation shall not recognize gain (or loss) on the distribution under section 367(e)(2). If a foreign liquidating corporation distributes a partnership interest (whether foreign or domestic), then such corporation shall be treated as having distributed a proportionate share of partnership property in accordance with the principles of paragraph (b)(1)(iii) of this section.

(2) *Exceptions*—(i) *Property used in a U.S. trade or business*—(A) *General rule.* A foreign liquidating corporation (including a corporation that has made an effective election under section 897(i)) that makes a distribution described in paragraph (c)(1) of this section shall recognize gain on the distribution of qualified prop-

erty, as described in paragraph (b)(2)-(i)(B) of this section (other than U.S. real property interests), that is used by the foreign liquidating corporation in the conduct of a trade or business within the United States at the time of distribution.

(B) *Ten-year active U.S. business exception.* A foreign liquidating corporation shall not recognize gain under paragraph (c)(2)(i)(A) of this section, if—

(1) The foreign distributee corporation, immediately thereafter and for the ten-year period beginning on the date of the distribution of such property, uses the property in the conduct of a trade or business in the United States;

(2) The foreign distributee corporation is not entitled to benefits under a comprehensive income tax treaty (this requirement shall apply only if the foreign liquidating corporation (or predecessor corporation) was not entitled to benefits under a comprehensive income tax treaty); and

(3) The foreign liquidating corporation and foreign distributee corporation attach the statement described in paragraph (c)(2)(i)(C) of this section to their U.S. income tax returns for their taxable years that include the distribution.

(C) *Required statement.* The statement required by paragraph (c)(2)(i)(B)(3) of this section shall be entitled “Required Statement under §1.367(e)-2(c)(2)(i),” shall be prepared by foreign liquidating corporation, shall be signed under penalties of perjury by an authorized officer of the foreign liquidating corporation and by an authorized officer of the foreign distributee corporation, and shall be identical to the statement described in paragraph (b)(2)(i)(C) of this section, except that “§1.367(e)-2(c)(2)(i)(B)” shall be substituted for references to “§1.367(e)-2(b)(2)(i)” and “foreign liquidating corporation” shall be substituted for “domestic liquidating corporation” each time it appears. References in the rules of paragraph (b)(2)(i)(C) of this section to various rules in paragraph (b) of this section shall be applied as if such references were to this paragraph (c). However, the statement described in this paragraph (c)(2)-(i)(C) shall be modified as follows:

(1) The foreign distributee corporation shall not be required to waive its income tax treaty benefits as required by §1.367(e)-2(b)(2)(i)(C)(4), unless—

(i) The foreign liquidating corporation was required to waive its treaty benefits under paragraph (b)(2)(i)(C)(4) of this section in connection with the distribution of such property in a prior liquidation distribution subject to the provisions of this section; or

(ii) The foreign distributee corporation is entitled benefits under a treaty to which the foreign liquidating corporation was not entitled.

(2) If the foreign distributee is required to waive treaty benefits because of paragraph (c)(2)(i)(C)(1)(ii) of this section, then the foreign distributee shall only be required to waive benefits that were not available to the foreign liquidating corporation (or a predecessor corporation) prior to liquidation.

(3) The property description described in paragraph (b)(2)(i)(C)(2) of this section shall include only the qualified U.S. trade or business property described in paragraph (c)(2)(i) of this section.

(D) *Operating rules.* By the foreign liquidating corporation’s claiming non-recognition under paragraph (c)(2)(i)(B) of this section and filing a statement described in paragraph (c)(2)(i)(C) of this section, the foreign liquidating corporation and the foreign distributee corporation agree to be subject to the rules of paragraph (c)(2)(i) of this section, as well as the rules of paragraphs (b)(2)(i)(D) and (E) of this section. In applying the rules of paragraphs (b)(2)(i)(D) and (E) of this section, “foreign liquidating corporation” shall be used instead of “domestic liquidating corporation” each time it appears. References in the rules of paragraphs (b)(2)(i)(D) and (E) of this section to various rules in paragraph (b) of this section shall be applied as if such references were to this paragraph (c).

(ii) *Property formerly used in a United States trade or business.* A foreign liquidating corporation that makes a distribution described in paragraph (c)(1) of this section shall recognize gain (but not loss) on the distribution of property (other than U.S. real property interests) that had ceased to be used by the foreign liquidating corporation in the conduct of a U.S. trade or business within the ten-year period ending on the date of distribution and that would have been subject to section 864(c)(7) had it been disposed. Section 864(c)(7) shall govern the treatment of

any gain recognized on the distribution of assets described in this paragraph as income effectively connected with the conduct of a trade or business within the United States.

(3) *Other consequences—(i) Distributee basis in property.* The foreign distributee corporation’s basis in property subject to this paragraph (c) shall be the same as the foreign liquidating corporation’s basis in such property immediately before the liquidation, increased by any gain, or reduced by any loss recognized by the foreign liquidating corporation on such property, pursuant to paragraph (c)(2) of this section. In no event, however, will the foreign distributee corporation’s adjusted basis in distributed property exceed the fair market value of such property at the time of liquidation.

(ii) *Other rules.* For other rules that may apply, see sections 367(b) and 381.

(d) *Anti-abuse rule.* The Commissioner may require either a domestic liquidating corporation or a foreign liquidating corporation to recognize gain on a distribution in liquidation described in paragraph (b) or (c) of this section (or treat the liquidating corporation as if it had recognized loss on a distribution in liquidation), if a principal purpose of the liquidation is the avoidance of U.S. tax (including, but not limited to, the distribution of a liquidating corporation’s earnings and profits with a principal purpose of avoiding U.S. tax). A liquidation may have a principal purpose of tax avoidance even though the tax avoidance purpose is outweighed by other purposes (taken together or separately).

(e) *Effective date.* This section shall be applicable to distributions occurring 30 days after August 9, 1999 or, if taxpayer so elects, to distributions in taxable years ending after August 8, 1999.

Par. 4. Section 1.6038B-1 is amended by revising the fourth sentence of paragraph (a), the first sentence of paragraph (b)(1)(i), and paragraphs (d), (e), and (g) to read as follows:

*§1.6038B-1 Reporting of certain transactions to foreign corporations.*

(a) \* \* \* Section 1.6038B-1(e) describes the filing requirements for property transfers described in section 367(e). \* \* \*

(b) *Time and manner of reporting—(1) In general—(i) Reporting procedure.* Ex-

cept for stock or securities qualifying under the special reporting rule of paragraph (b)(2) of this section, or cash, which is subject to special rules contained in paragraph (b)(3) of this section, any U.S. person that makes a transfer described in section 6038B(a)(1)(A), 367(d), or 367(e), is required to report pursuant to section 6038B and the rules of this section and must attach the required information to Form 926, "Return by Transferor of Property to a Foreign Corporation." \* \* \*

\* \* \* \* \*

(d) [Reserved]. For further guidance, see §1.6038B-1T(d).

(e) *Transfers subject to section 367(e)—(1) In general.* If a domestic corporation (distributing corporation) makes a distribution described in section 367(e)(1) or section 367(e)(2), the distributing corporation must comply with the reporting requirements of this paragraph (e). Unless otherwise provided in this section, a distributing corporation making a distribution described in sections 367(e)(1) or 367(e)(2) must file a Form 926, "Return by a U.S. Transferor of Property to a Foreign Corporation (under section 367)," as amended and modified by this section.

(2) *Reporting requirements for section 367(e)(1) distributions of domestic controlled corporations.* A domestic distributing corporation making a distribution of the stock or securities of a domestic corporation under section 355 is not required to file a Form 926, as described in paragraph (e)(1) of this section, and shall have no other reporting requirements under section 6038B.

(3) *Reporting requirements for section 367(e)(1) distributions of foreign controlled corporations.* If the distributing corporation makes a section 355 distribution of the stock or securities of a foreign controlled corporation to distributee shareholders who are not qualified U.S. persons, as defined in §1.367(e)-1(b)(1), then the distributing corporation shall complete Part 1 of the Form 926 and attach a signed copy of such form to its U.S. income tax return for the year of the distribution. The distributing corporation shall also attach to its U.S. income tax return for the year of distribution a statement signed under the penalties of perjury

entitled, "Addendum to Form 926." The addendum shall contain a brief description of the transaction, state the number of shares distributed to distributees who are not qualified U.S. persons (applying the rules contained in §1.367(e)-1(d)), and state the basis and fair market value of the distributed stock or securities (including a list stating the amounts that were distributed to distributees who were not qualified U.S. persons and distributees who were qualified U.S. persons).

(4) *Reporting rules for section 367(e)(2) distributions by domestic liquidating corporations.* If the distributing corporation makes a distribution of property in complete liquidation under section 332 to a foreign distributee corporation that meets the stock ownership requirements of section 332(b) with respect to the stock of the distributing corporation, then the distributing corporation shall complete a Form 926 and attach a signed copy of such form to its U.S. income tax return for the year of the distribution. The property description contained in Part III of the Form 926 shall contain a description of all property distributed by the liquidating corporation (regardless of whether the property qualifies for non-recognition). The description shall also identify the property excepted from gain recognition under §1.367(e)-2(b)(2)(ii) and (iii). If the distributing corporation distributes property that will be used by the foreign distributee corporation in a U.S. trade or business and the distributing corporation does not recognize gain on such distribution under §1.367(e)-2(b)(2)(i), then the distributing corporation may satisfy the requirements of this section by completing Part 1 of the Form 926, noting thereon that the information required by the Form 926 is contained in the statement required by §1.367(e)-2(b)(2)(i)(C)(2), and attaching a signed copy of the Form 926 to its U.S. income tax return for the year of the distribution.

\* \* \* \* \*

(g) *Effective dates.* This section applies to transfers occurring on or after July 20, 1998, except paragraph (e) of this section, which applies to transfers that are subject to §§1.367(e)-1(f) and 1.367(e)-2(e). See §1.6038B-1T for transfers occurring prior to July 20, 1998. See also §1.6038B-1T(e) in effect prior to August

9, 1999, (as contained in 26 CFR part 1 revised April 1, 1999) for transfers described in section 367(e) that are not subject to §§1.367(e)-1(f) and 1.367(e)-2(e).

Par. 5. Section 1.6038B-1T is amended by revising the section heading, revising paragraph (e) and revising the first sentence of paragraph (g), to read as follows.

*§1.6038B-1T Reporting of certain transactions to foreign corporations (temporary).*

\* \* \* \* \*

(e) [Reserved] For further guidance, see §1.6038B-1(e).

\* \* \* \* \*

(g) *Effective date.* This section applies to transfers occurring after December 31, 1984. \* \* \*

PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Par. 6. The authority citation for part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 7. In §602.101, paragraph (b) is amended in the table by removing the entries for 1.367(e)-1T and 1.367(e)-2T, revising the entry for 1.6038B-1, and adding entries in numerical order to read as follows:

*§602.101 OMB Control numbers.*

\* \* \* \* \*

(b) \* \* \*

CFR part or section where identified and described	Current OMB control No.
1.367(e)-1 . . . . .	1545-1487
1.367(e)-2 . . . . .	1545-1487
1.6038B-1 . . . . .	1545-1487 1545-1615

\* \* \* \* \*

Robert E. Wenzel,  
Deputy Commissioner of  
Internal Revenue.

Approved 7/29/1999.

Donald C. Lubbick,  
*Assistant Secretary of  
the Treasury.*

(Filed by the Office of the Federal Register on August 6, 1999, 8:45 a.m., and published in the issue of the Federal Register for August 9, 1999, 64 F.R. 43072)