

**Reg. 1.367(a)-3(d)(3), Example 6A**  
**368(a)(1)(C) & 368(a)(2)(C)**  
 (formerly Example 5A)

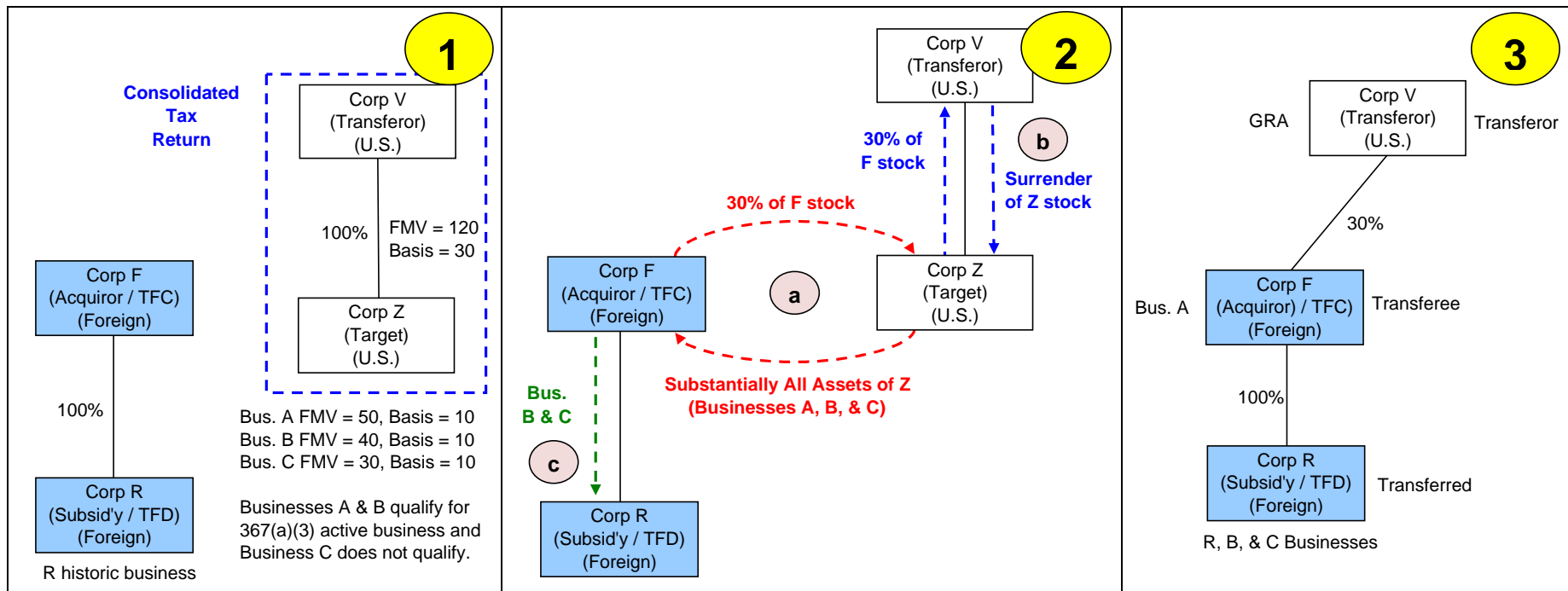
**Indirect Stock Transfer -  
 Outbound C Reorg with Partial Drop**

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**Initial Structure**

**Outbound C Reorg with a Partial Drop**

**Ending Point**



F, a foreign corporation, owns all of the stock of R, a foreign corporation that operates an historical business. V, a domestic corporation, owns all of the stock of Z, also a domestic corporation. V does not own any of the stock of F (applying the attribution rules of section 318 as modified by section 958(b)). Z has 3 businesses: Business A with a basis of \$10 and a value of \$50, Business B with a basis of \$10 and a value of \$40, and Business C with a basis of \$10 and a value of \$30. V and Z file a consolidated Federal income tax return and V has a basis of \$30 in the Z stock, which has a value of \$120. Businesses A and B consist solely of assets that will satisfy the section 367(a)(3) active trade or business exception; none of Business C's assets will satisfy the exception. Z transfers all 3 businesses to F in exchange for 30 percent of the F stock, which Z distributes to V pursuant to a section 368(a)(1)(C) reorganization. F then contributes Businesses B and C to R in a controlled asset transfer.

The transfer of the Business A assets by Z to F does not constitute an indirect stock transfer and, subject to section 367(a)(5), the Business A assets qualify for the section 367(a)(3) active trade or business exception and are not subject to section 367(a). The transfer by Z of the Business B and C assets to F must first be tested under sections 367(a)(1), (3) and (5). Z recognizes \$20 of gain on the outbound transfer of the Business C assets, as such assets do not qualify for an exception to section 367(a)(1). Subject to section 367(a)(5), the Business B assets may qualify for the exception under section 367(a)(3) and §1.367(a)-2T(c)(2) for assets that will be used by R in an active trade or business outside the United States. Under the indirect stock transfer rules V is deemed to transfer the stock of a foreign corporation to F in a section 354 exchange. V must enter into the gain recognition agreement in the amount of \$30 to preserve Z's nonrecognition treatment with respect to its transfer of F is the transferee foreign corporation and R is the transferred corporation.