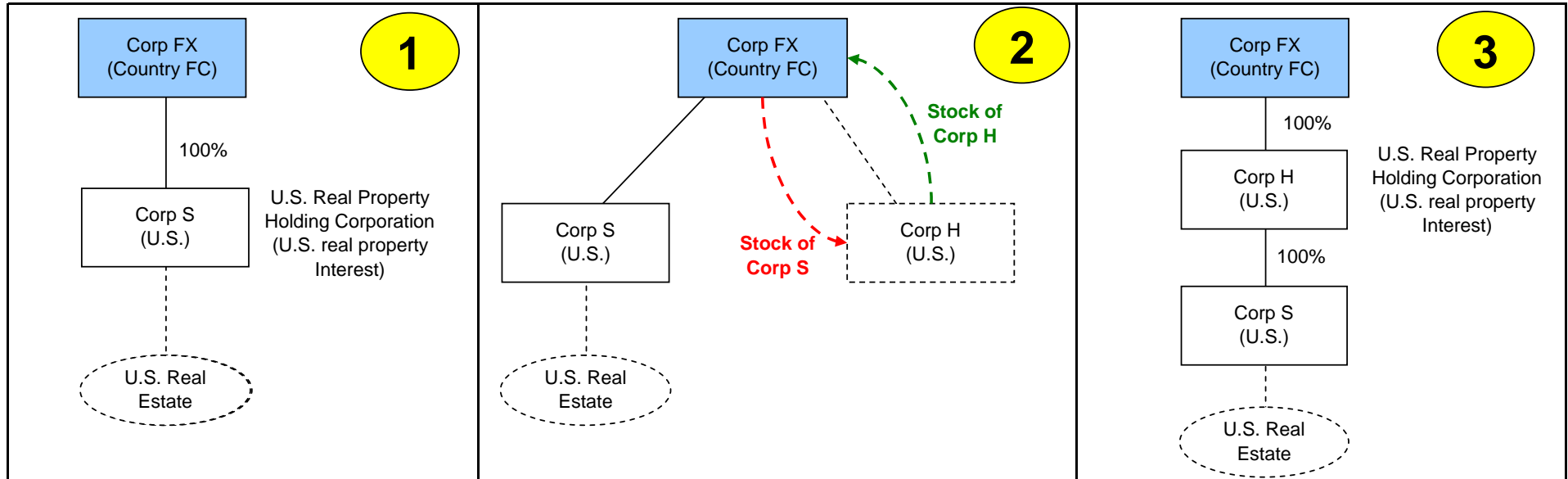


**Section 351 Exchange of
One USRPI for Another USRPI**

Initial Structure

Section 351 Exchange

Ending Point



FX is a corporation organized under the laws of a foreign country (FC), which does not have an income tax treaty with the United States. FX holds 100% of the stock of corporation S, a domestic corporation. S is engaged in real estate development and constitutes a U.S. real property holding corporation as defined in section 897(c)(2). Therefore, the stock of S constitutes a U.S. real property interest pursuant to section 897(c)(1). For business purposes FX wishes to interpose a holding company between itself and S. Therefore, in a transaction qualifying for nonrecognition under section 351, FX transfers all of the shares of S to H, a corporation newly organized in the United States, solely in exchange for the stock of H. Because the shares of S are the only assets of H, H constitutes a U.S. real property holding corporation as defined in section 897(c)(2).

Under section 897(a), a foreign corporation's gain or loss from the disposition of a U.S. real property interest is treated as if the foreign corporation were engaged in a trade or business within the United States and as if the gain or loss were effectively connected with the trade or business. Section 897(e) provides that except to the extent otherwise provided in section 897(d) and section 897(e)(2), any nonrecognition provision shall apply for purposes of section 897 to a transaction **only** in the case of an exchange of a United States real property interest for an interest the sale of which would be subject to U.S. income tax. Section 897(e) is intended to preserve nonrecognition in cases where it is clear that gain inherent in a U.S. real property interest will remain subject to U.S. taxation. In the present case, FX has exchanged, in a transaction qualifying for nonrecognition under section 351, one U.S. real property interest for another U.S. real property interest, the sale of which will be clearly subject to U.S. taxation. Therefore, FX is entitled to receive nonrecognition treatment pursuant to section 897(e).