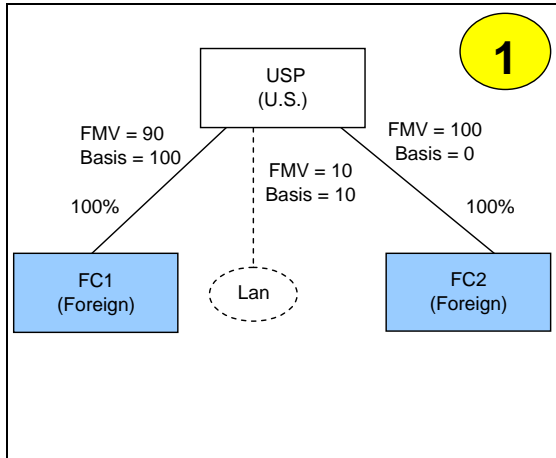
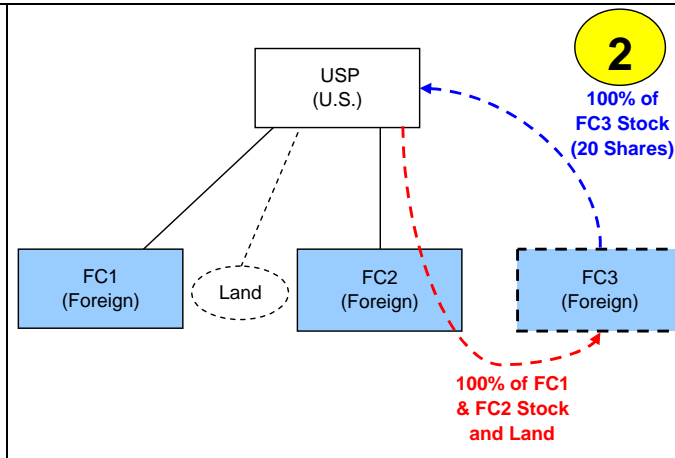


Outbound 351 & Sale of Transferee

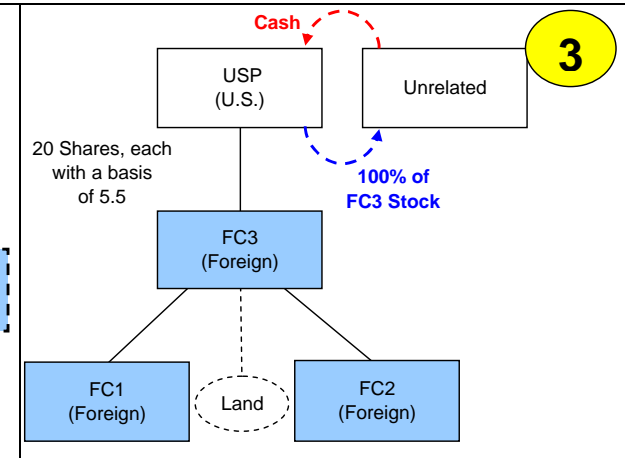
Initial Structure



Outbound 351 Exchange (Year 1)

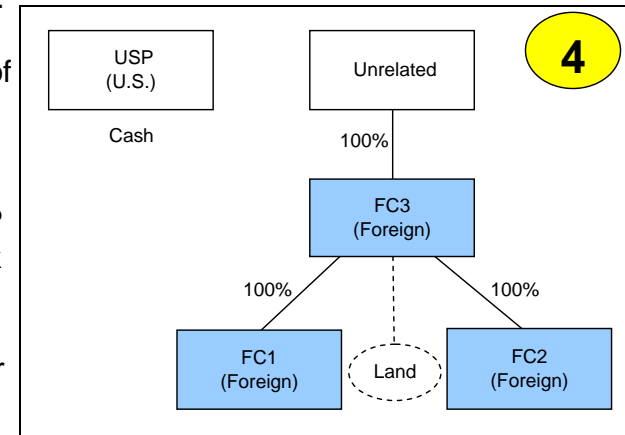


Sale of Transferred Stock (Year 3)



USP, a domestic corporation, owns 100% of the stock of two foreign corporations, FC1 and FC2. The basis and fair market value of the FC1 stock is \$100 and \$90, respectively. The basis and fair market value of the FC2 stock is \$0 and \$100, respectively. USP also owns land that has a basis and fair market value of \$10. In year 1, USP transfers 100% of the stock of FC1 and FC2 and the land to FC3, a newly formed foreign corporation, in exchange for 20 shares of FC3 stock. The transfer of the stock of FC1 and FC2 qualifies under section 351 and section 368(a)(1)(B). The transfer of the land qualifies under section 351. The transfer of the FC2 stock is subject to both section 367(a) and (b). USP enters into a gain recognition agreement with respect to the \$100 of gain in the FC2 stock and complies with the notice requirement under §1.367(b)-1(c). USP takes the position that its basis in each of the 20 shares of FC3 stock received in the transfer equals \$5.5 $((\$100 + \$0 + 10) / 20)$. In year 3, USP sells 100% of its FC3 stock to an unrelated person for cash.

Ending Point



The disposition of the FC3 stock is a triggering event. The disposition does not terminate the gain recognition agreement because USP takes the position that the basis of each of the 10 shares of FC3 stock it received in exchange for the FC2 stock in the initial transfer equals \$5.5. Thus, the total basis in the 10 shares received for the FC2 stock equals \$55, which exceeds the \$0 basis USP had in the FC2 stock it transferred to FC3 in the initial transfer. USP may, however, elect to reduce its basis in 10 of the FC3 shares it disposes of from \$5.5 to \$0, and increase its basis in its remaining 10 shares of FC2 stock by \$5.5. As a result, the disposition would not be a triggering event, and the gain recognition would terminate without further effect.