Reg. 1.367(b)-4(b)(1)(iii), Example 3

Foreign to Foreign Triangular C Reorganization: Section 367(a) & (b) Overlap

Initial Structure

1

FP (Foreign)
>80%

DC (U.S.)
100%
1248 amount = 20

CFC

FC1 (Foreign) (Acquiror)

FC2 (Foreign) (Target)

Triangular C Reorganization

2

FP (Foreign)

DC (U.S.)

Surrender FC2 Stock

Solely FP Voting Stock

Solely FP Voting Stock

FC1 (Foreign) (Acquiror)

FC2 (Foreign) (Target)

FC1 (Foreign) (Acquiror)

FC2 (Foreign) (Target)

All Assets & Liabilities

Ending Point

3

DC (U.S.)

If >50% then no deemed dividend and gain recognition agreement must be for entire gain.

If <50% then deemed dividend of 20 and gain recognition agreement is the gain realized less the 20 deemed dividend.

FC1 is a foreign corporation that is controlled (within the meaning of section 368(c)) by FP, a foreign corporation. DC is a domestic corporation that is unrelated to FC1. DC owns all of the outstanding stock of FC2, a foreign corporation. Thus, DC is a section 1248 shareholder with respect to FC2, and FC2 is a controlled foreign corporation. The section 1248 amount attributable to the stock of FC2 held by DC is $20. In a triangular section 368(a)(1)(C) reorganization, FC1 acquires all of the assets and assumes all of the liabilities of FC2 in exchange for FP voting stock. FC2 distributes the FP stock to DC, and the FC2 stock held by DC is canceled.

The transfer of FC2 assets to the lower tier entity FC1 is an indirect stock transfer subject to section 367(a). Accordingly, DC's exchange of FC2 stock for FP stock under section 354 will be taxable (and section 1248 will be applicable) unless DC enters into a gain recognition agreement ("GRA"). If DC enters into a GRA and FP and FC1 are CFCs with DC as a section 1248 shareholder, then there is no deemed dividend to DC. If DC enters into a GRA and FP or FC1 is not a CFC (or DC is not a section 1248 shareholder of the CFC), then DC must include in income, as a deemed dividend from FC2, the section 1248 amount ($20) attributable to the FC2 stock that DC exchanged.

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