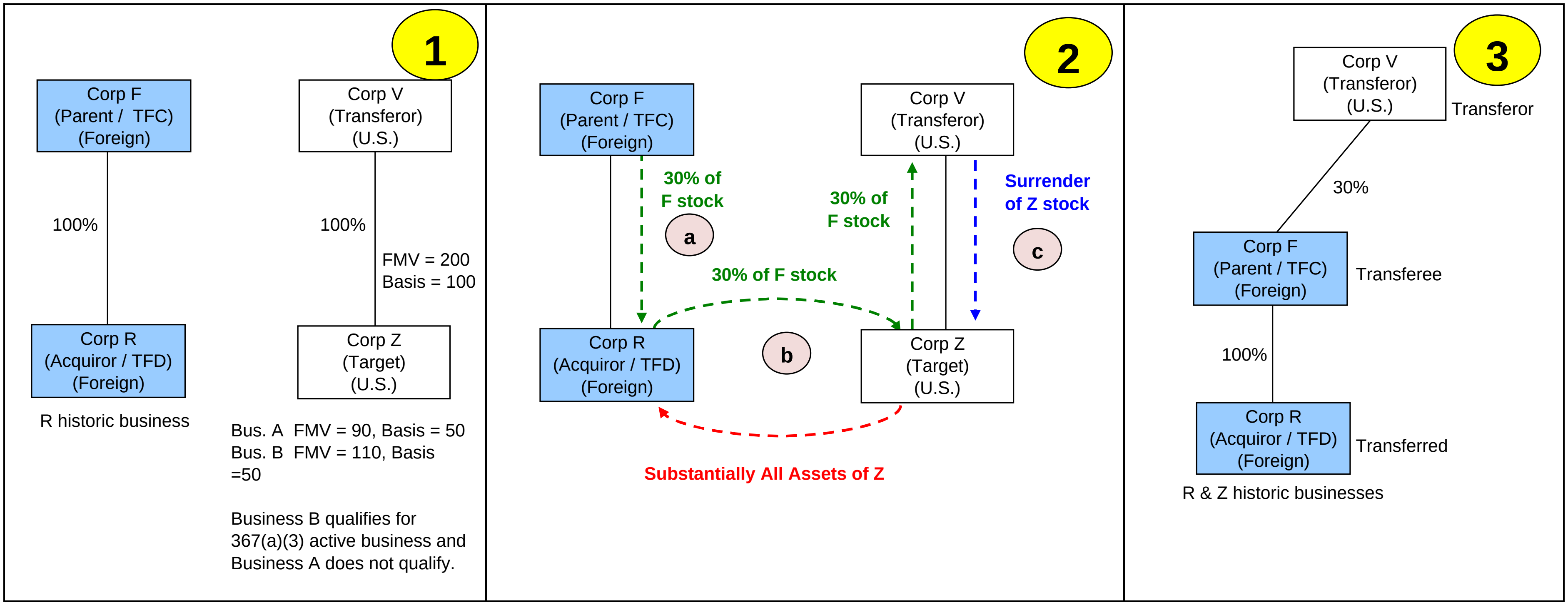
Reg. 1.367(a)-3(d)(3), Example 8A 368(a)(1)(C)
(formerly Example 7A)

Indirect Stock Transfer - Outbound Triangular C Reorg

Initial Structure | **Outbound Triangular C Reorg** | **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 and Z do not file a consolidated return for Federal income tax purposes. The properties of Z consist of Business A assets, with ar adjusted basis of $50 and fair market value of $90, and Business B assets, with an adjusted basis of $50 and a fair market value of $110. Assume that the Business A assets do not qualify for the active trade or business exception under section 367(a)(3), but that the Business B assets do qualify for the exception. V's basis in the Z stock is $100, and the value of such stock is $200.V does not own any of the stock of F (applying the attribution rules of section 318 as modified by section 958(b)). In a triangular reorganization described in section 368(a)(1)(C), R acquires all of the assets of Z, and V receives 30% of the voting stock of F.

The assets of Businesses A and B that are transferred to R must be tested under sections 367(a)(3) and (a)(5) prior to consideration of the indirect stock transfer rules. Thus, Z must recognize $40 of income under section 367(a)(1) on the outbound transfer of Business A assets. Because V and Z do not file a consolidated return, V's basis in its Z stock increases from $100 as a result of Z's $40 gain. V is deemed to transfer the stock of a foreign corporation to F in a section 354 exchange and therefore must enter into a gain recognition agreement in the amount of $60 (the gain realized but not recognized by V in the stock of Z after the $4(basis adjustment). If F sells a portion of its stock in R during the term of the agreement, V will be required to recognize a portion of the $60 gain subject to the agreement. To determine whether R disposes of substantially all of its assets (under §1.367(a)-8T(d)(2)), only the Business B assets will be considered (because the transfer of the Business A assets was taxable to Z under section 367).