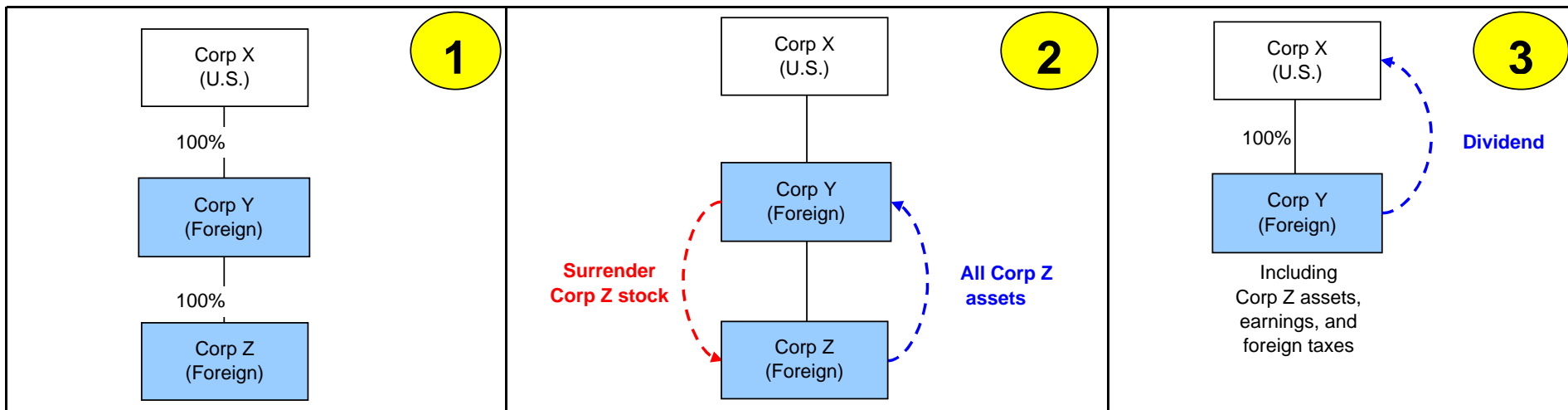


Deemed Paid Credit Impact of Lower-Tier 332 Liquidation

Initial Structure

Lower Tier Liquidation

Dividend



Domestic corporation X owned all the outstanding voting stock of foreign corporation Y which, in turn, owned all the outstanding voting stock of foreign corporation Z. Y acquired all the assets of Z in a distribution in complete liquidation within the meaning of section 332, in which the basis of the assets carried over under section 334(b)(1). The acquisition of the assets of Z by Y is a transaction described in section 381(a)(1). As required by section 367, X obtained a ruling from the IRS before the liquidation that the acquisition of the assets of Z by Y was not in pursuance of a plan having as one of its principal purposes the avoidance of Federal income tax. Subsequent to that acquisition and unrelated thereto, a dividend was paid to X by Y from the accumulated earnings and profits that included earnings and profits Z had accumulated prior to its liquidation. Prior to its complete liquidation Z had paid or accrued taxes to the foreign country in which it was incorporated.

Section 381(c)(2) provides that an acquiring corporation (such as Y) in a transaction to which section 381(a) applies shall succeed to and take into account the earnings and profits of the transferor corporation (such as Z) as of the close of the date of the transfer. See also Reg. 1.381(c)(2)-1.

Since a qualified domestic corporate shareholder may obtain a foreign tax credit under section 902 with respect to distributions from the earnings and profits of a second-tier corporation and since a first-tier corporation may succeed to and take into account under section 381(c)(2) the earnings and profits of a second-tier transferor corporation in a transaction covered by section 381(a)(1), it is proper to allow the first-tier transferee corporation to succeed to and take into account the accumulated profits and foreign income taxes of the second-tier corporation imposed on the income to which the earnings and profits are attributable.

With respect to the dividend paid to X after liquidation of Z out of the accumulated profits of Y and Z for the respective taxable years prior to the date of Z's liquidation, X will be deemed to have paid a proportionate part of the foreign income taxes paid or accrued by both Y and Z on their respective accumulated profits for such taxable years and is entitled to a credit with respect thereto under section 902.