Internal Revenue
bulletin

Bulletin No. 2009-9
March 2, 2009

HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

T.D. 9444, page 603.
REG–147636–08, page 641.

Final, temporary, and proposed regulations under section 367 of the Code provide rules for the treatment of certain shareholders who transfer stock or securities of controlled corporations to foreign corporations. The regulations also address certain distributions shareholders receive with respect to the stock of controlled foreign corporations.

T.D. 9445, page 635.

Final regulations under section 6103 of the Code relate to administrative review procedures for certain government agencies and other authorized recipients of returns or return information whose receipt of returns and return information may be suspended or terminated because they do not maintain proper safeguards.

T.D. 9446, page 607.

Final regulations under section 367 of the Code provide rules for entering into gain recognition agreements under section 367(a). The regulations clarify the effect that various transactions have on existing gain recognition agreements. Notice 2005–74 obsoleted.

EXEMPT ORGANIZATIONS

Announcement 2009–9, page 643.

A list is provided of organizations now classified as private foundations.

Announcement 2009–10, page 644.

The IRS has revoked its determination that Leszinski Family Support Organization of Atlanta, GA; Kuumba Trust of Pittsburgh, PA; Consumer Debt Management Services of Deerfield Beach, FL; RealtyAmerica.Org, Inc., of Indian Harbour Beach, FL; Consumer Budget Counseling, Inc., of Port Charlotte, FL; Innovative Womens Network, Inc., of Houston, TX; Ellen Stephen Hospice & Home Care of Kyle, SD; Starfish Foundation, Inc., of Richardson, TX; Ronsard Foundation of Statesville, NC; Alternative Care, Inc., of Gainesville, FL; Credit Counseling, Inc., of Sunrise, FL; A New Goal Credit Counseling Agency of San Francisco, CA; Trans-Atlantic Health Organization, Inc., of Gaithersburg, MD; and Ammend Credit Counseling and Debt Consolidation of Cincinnati, OH, qualify as organizations described in sections 501(c)(3) and 170(c)(2) of the Code.

ADMINISTRATIVE

T.D. 9445, page 635.

Final regulations under section 6103 of the Code relate to administrative review procedures for certain government agencies and other authorized recipients of returns or return information whose receipt of returns and return information may be suspended or terminated because they do not maintain proper safeguards.

REG–138326–07, page 638.

Proposed regulations under section 6231 of the Code allow the IRS to convert partnership items to nonpartnership items when the application of the unified partnership audit and litigation procedures of sections 6221 through 6234 with respect to certain tax avoidance transactions interferes with the effective and efficient enforcement of the Internal Revenue laws. A public hearing is scheduled for June 4, 2009.

(Continued on the next page)

Finding Lists begin on page ii.

Department of the Treasury
Internal Revenue Service

Announcement 2009–6, page 643.
New section 6050W of the Code requires information reporting for payment card and third party payment network transactions, effective for returns for calendar years beginning after December 31, 2010. Entities required to report must perform backup withholding if the payee fails to furnish a correct Taxpayer Identification Number ("TIN"). This announcement will alert 6050W filers that they may now participate in the TIN matching program.

The IRS Mission

Provide America's taxpayers top quality service by helping them understand and meet their tax responsibilities and by applying the tax law with integrity and fairness to all.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents are compiled semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1986 Code.
This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1986.

Part II.—Treaties and Tax Legislation.
This part is divided into two subparts as follows: Subpart A, Tax Conventions and Other Related Items, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.
To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts. Also included in this part are Bank Secrecy Act Administrative Rulings. Bank Secrecy Act Administrative Rulings are issued by the Department of the Treasury's Office of the Assistant Secretary (Enforcement).

Part IV.—Items of General Interest.
This part includes notices of proposed rulemakings, disbarment and suspension lists, and announcements.

The last Bulletin for each month includes a cumulative index for the matters published during the preceding months. These monthly indexes are cumulated on a semiannual basis, and are published in the last Bulletin of each semiannual period.

For sale by the Superintendent of Documents, U.S. Government Printing Office, Washington, DC 20402.

Part I. Rulings and Decisions Under the Internal Revenue Code of 1986

Section 367.—Foreign Corporations

26 CFR 1.367(a)–3: Treatment of transfers of stock or securities to foreign corporations.

T.D. 9444

DEPARTMENT OF THE TREASURY
Internal Revenue Service
26 CFR Part 1

Application of Section 367 to a Section 351 Exchange Resulting from a Transaction Described in Section 304(a)(1); Treatment of Gain Recognized Under Section 301(c)(3) for Purposes of Section 1248

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final and temporary regulations.

SUMMARY: This document contains final and temporary regulations under sections 367(a), 367(b) and 1248(a) of the Internal Revenue Code (Code). The final regulations under section 367 revise existing final regulations and add cross-references. The final regulations under section 1248 update an effective/applicability date. The temporary regulations under section 367(a) and (b) revise existing final regulations concerning transfers of stock to a foreign corporation that are described in section 351 by reason of section 304(a)(1). The temporary regulations under section 1248(a) provide that, for purposes of section 1248(a), gain recognized by a shareholder under section 301(c)(3) in connection with the receipt of a distribution of property from a foreign corporation with respect to its stock shall be treated as gain from the sale or exchange of the stock of such foreign corporation. The temporary regulations affect certain persons that transfer stock to a foreign corporation in a transaction described in section 304(a)(1), or certain persons that recognize gain under section 301(c)(3) in connection with the receipt of a distribution of property from a foreign corporation with respect to its stock. The text of the temporary regulations serves as the text of the proposed regulations (REG–147636–08) set forth in the notice of proposed rulemaking on this subject published in this issue of the Bulletin.

DATES: *Effective Date:* These regulations are effective on February 10, 2009.

Applicability Date: These regulations apply to acquisitions of stock occurring on or after February 10, 2009.

FOR FURTHER INFORMATION CONTACT: Sean W. Mullaney, (202) 622–3860 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

Section 367(a)(1) generally provides that if a United States person transfers property to a foreign corporation in an exchange described in section 332, 351, 354, 356, or 361, the foreign corporation shall not be considered a corporation for purposes of determining the extent to which the United States person recognizes gain on such transfer. Exceptions to the general rule are provided by section 367(a)(2) and (3), and the Secretary has broad authority under section 367(a)(6) to promulgate regulations providing exceptions for other transactions.

Section 367(b)(1) provides that in the case of an exchange described in section 332, 351, 354, 355, 356, or 361 in connection with which there is no transfer of property described in section 367(a)(1), a foreign corporation shall be considered to be a corporation except to the extent provided in regulations prescribed by the Secretary which are necessary or appropriate to prevent the avoidance of Federal income taxes. Section 367(b)(2) provides that the regulations prescribed pursuant to section 367(b)(1) shall include (but shall not be limited to) regulations dealing with the sale or exchange of stock or securities in a foreign corporation by a United States person, including regulations providing the circumstances under which gain is recognized, amounts are included in gross income as a dividend, adjustments are made to earnings and profits, or adjustments are made to the basis of stock or securities.

Regulations under section 367(b) generally provide that if the potential application of section 1248 cannot be preserved immediately following the acquisition of the stock or assets of a foreign corporation (foreign acquired corporation) by another foreign corporation in an exchange subject to section 367(b), then certain exchanging shareholders of the foreign acquired corporation must include in income as a dividend the section 1248 amount (as defined in §1.367(b)–2(c)) attributable to the stock of the foreign acquired corporation. See §1.367(b)–4(b).

Section 304(a)(1) generally provides that, for purposes of sections 302 and 303, if one or more persons are in control of each of two corporations and in return for property one of the corporations (the acquiring corporation) acquires stock in the other corporation (the issuing corporation) from the person (or persons) so in control, then such property shall be treated as a distribution in redemption of the stock of the acquiring corporation. To the extent section 301 applies to the distribution, the transferor and the acquiring corporation are treated as if (1) the transferor transferred the stock of the issuing corporation to the acquiring corporation in exchange for stock of the acquiring corporation in a transaction to which section 351(a) applies, and (2) the acquiring corporation then redeemed the stock it is deemed to have issued. Under section 304(b)(2), the determination of the amount of the property distribution that is a dividend (and the source thereof) is made as if the property is distributed by the acquiring corporation to the extent of its earnings and profits, and then by the issuing corporation to the extent of its earnings and profits.

On February 21, 2006, the IRS and Treasury Department issued final regulations (T.D. 9250, 2006–1 C.B. 588) providing that section 367(a) and (b) shall not apply to certain transfers of stock of a foreign or domestic corporation to a foreign acquiring corporation to which section 351 applies (deemed section 351 exchange) by reason of section 304(a)(1) (final 2006 regulations). Specifically, §1.367(a)–3(a) provides that if, pursuant to section 304(a)(1), a United States person is treated as transferring stock of a domestic or foreign corporation to a foreign corporation in exchange for stock of such foreign corporation in a deemed section 351 exchange, the deemed section 351 exchange is not a transfer to a foreign corporation subject to section 367(a). Similarly, §1.367(b)–4(a) provides that if, pursuant to section 304(a)(1), a foreign corporation is treated as acquiring the stock of another foreign corporation in a deemed section 351 exchange, the deemed section 351 exchange is not an acquisition subject to section 367(b).

The preamble to the final 2006 regulations explained that the IRS and Treasury Department determined that the policies underlying section 367(a) and (b) are preserved even if a deemed section 351 exchange is not subject to section 367(a) and (b) because generally the income recognized by the transferor in the transaction (dividend income, capital gain, or both) should equal or exceed the built-in gain in the transferred stock. Comments were received, however, stating that the transferor may not recognize income equal to or greater than the built-in gain in the transferred stock if, under section 301(c)(2), the transferor were permitted to recover the basis of shares of the foreign acquiring corporation held before (and after) the transaction. For example, assume a domestic corporation, P, wholly owns F1 and F2, both foreign corporations. The F1 stock has a $0x basis and $100x fair market value. The F2 stock has a $100x basis and $100x fair market value. Neither F1 nor F2 has current or accumulated earnings and profits. In a transaction subject to section 304(a)(1), P sells the F1 stock to F2 for $100x cash. Under section 304(a)(1), P and F2 are treated as if P transferred the F1 stock to F2 in exchange for F2 stock in a transaction to which section 351 applies, and then F2 redeemed its stock deemed issued to P. Because the redemption of the F2 stock would be described in section 302(d) and therefore subject to section 301, the commentators posited that P may not recognize gain under section 301(c)(3) on the receipt of the $100x cash in redemption of the F2 stock if the basis of both the F2 stock that is received by P in the deemed section 351 exchange ($0x), and of the F2 stock held by P prior to (and after) the transaction ($100x), is available for reduction under section 301(c)(2). If that were the case, P would recognize no gain in the transaction.

The preamble to the final 2006 regulations stated, however, that the IRS and Treasury Department believe current law does not provide for the recovery of basis of any shares of the acquiring corporation other than the shares deemed issued to the transferor and redeemed by the acquiring corporation as provided under section 304(a)(1). Thus, in the example above, P would recognize $100x gain under section 301(c)(3) (the built-in gain on the F1 stock), and the basis of the F2 stock held by P after the transaction would continue to be $100x. The IRS and Treasury Department continue to study the basis recovery issue as part of a larger project and have determined that it is necessary to revise the final 2006 regulations prior to the completion of that project.

Explanation of Provisions

A. *Modified Application of Section 367(a) to Deemed Section 351 Exchanges*

Consistent with the final 2006 regulations, the temporary regulations under section 367(a) generally provide that if, pursuant to section 304(a)(1), a United States person is treated as transferring stock of a domestic or foreign corporation to a foreign corporation in exchange for stock of such foreign corporation in a deemed section 351 exchange, the deemed section 351 exchange is not a transfer to a foreign corporation subject to section 367(a). However, if the distribution received by the United States person in redemption of the foreign acquiring corporation stock received in the deemed section 351 exchange is subject to section 301 (by reason of section 302(d)), the temporary regulations provide an exception to the general rule if the distribution is applied against and reduces (in whole or in part), pursuant to section 301(c)(2), the basis of stock of the foreign acquiring corporation held by the United States person other than the stock deemed issued to the United States person in the deemed section 351 exchange. In such a case, the United States person shall recognize gain under section 367(a)(1) equal to the amount by which the gain realized by the United States person with respect to the transferred stock in the deemed section 351 exchange exceeds the amount of the distribution received by the United States person in redemption of the foreign acquiring corporation stock that is treated as a dividend under section 301(c)(1) and included in gross income by the United States person. Thus, in the hypothetical transaction described above, if any amount of the distribution received by P in redemption of the F2 stock was applied against the basis of the F2 stock held by P before (and after) the transaction, then under the temporary regulations P would recognize $100x gain under section 367(a)(1) in connection with its transfer of the F1 stock to F2 in the deemed section 351 exchange.

The exceptions to the application of section 367(a)(1) for transfers of stock provided in §1.367(a)–3 are not available to transfers covered by the temporary regulations. For example, a United States person cannot avoid gain recognition under the temporary regulations by entering into a gain recognition agreement under §§1.367(a)–3(b)(1)(ii) and 1.367(a)–8 with respect to the deemed section 351 exchange.

The temporary regulations provide rules to coordinate the recognition of gain under the temporary regulations and the corresponding increase to the basis of the stock of the foreign acquiring corporation received by the United States person in the transaction. Under such rules the increase to the basis of the stock of the foreign acquiring corporation by reason of gain recognized by the United States person under the temporary regulations would be taken into account before determining the consequences of the redemption of the shares of the foreign acquiring corporation. For example, in the hypothetical transaction described above, the basis of the F2 stock deemed received by P in exchange for the F1 stock would be increased to $100x under section 358 before determining the consequences of the redemption of such stock under section 301. The gain recognized by P will be treated as recognized with respect to the F1 stock transferred in the deemed section 351 exchange in proportion to the gain realized with respect to the F1 stock.

B. *Modified Application of Section 367(b) to Deemed Section 351 Exchanges*

The temporary regulations make similar revisions to the final 2006 regulations under section 367(b). Specifically, the temporary regulations provide that §1.367(b)–4(b) shall apply to a deemed section 351 exchange to the extent the distribution received by the exchanging shareholder in redemption of the stock deemed issued by the foreign acquiring corporation is applied against and reduces, pursuant to section 301(c)(2), the adjusted basis of stock of the foreign acquiring corporation held by the exchanging shareholder before the transaction.

The temporary regulations provide rules to determine the amount of an income inclusion that is attributable to the shares of stock of the foreign acquired corporation transferred in the deemed section 351 exchange when the income inclusion required under the regulations is less than the aggregate section 1248 amount attributable to all of the shares of stock transferred in the deemed section 351 exchange.

C. *Treatment of Gain Recognized under Section 301(c)(3) for Purposes of Section 1248(a)*

The temporary regulations under section 1248(a) provide that gain recognized under section 301(c)(3) on the receipt of a distribution of property from a foreign corporation shall be treated, for purposes of section 1248(a), as gain from the sale or exchange of the stock of such corporation. The temporary regulations preserve the policies underlying section 367(b), are consistent with the premise of the final 2006 regulations, and ensure that the earnings and profits of lower-tier foreign subsidiaries described in section 1248(c)(2) are taken into account.

D. *Effective Dates*

The temporary regulations apply to transfers or distributions occurring on or after February 10, 2009.

Availability of IRS Documents

IRS notices cited in this preamble are made available by the Superintendent of Documents, U.S. Government Printing Office, Washington, DC 20402.

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. These temporary and final regulations are necessary to ensure that the appropriate amount of income (dividend income, capital gain or both) is recognized currently in the transactions described in the explanation of provisions section in this preamble. Accordingly, good cause is found for dispensing with notice and public comment pursuant to 5 U.S.C. 553(b) and (c) and with a delayed effective date pursuant to 5 U.S.C. 553(d). For applicability of the Regulatory Flexibility Act, see the cross-referenced notice of proposed rulemaking published elsewhere in this **Federal Register**. Pursuant to section 7805(f) of the Code, these regulations have been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Drafting Information

The principal author of these regulations is Sean W. Mullaney of the Office of Associate Chief Counsel (International). However, other personnel from the IRS and the Treasury Department participated in their development.

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Amendments to the Regulations

Accordingly, 26 CFR part 1 is amended as follows:

PART 1—INCOME TAXES

Paragraph. 1. The authority citation for part 1 is amended by adding new entries in numerical order to read as follows:

Authority: 26 U.S.C. 7805 * * *

Section 1.367(a)–9T also issued under 26 U.S.C. 367(a) and (b). * * *

Section 1.367(b)–4T also issued under 26 U.S.C. 367(b). * * *

Par. 2. Section 1.367(a)–3 is amended by revising the third sentence in paragraph (a) to read as follows:

§1.367(a)–3 Treatment of transfers of stock or securities to foreign corporations.

(a) * * * For rules applicable when, pursuant to section 304(a)(1), a United States person is treated as transferring stock of a domestic or foreign corporation to a foreign corporation in exchange for stock of such foreign corporation in a transaction to which section 351(a) applies, see §1.367(a)–9T. * * *

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Par. 3. Section 1.367(a)–9T is added to read as follows:

§1.367(a)–9T Treatment of deemed section 351 exchanges pursuant to section 304(a)(1) (temporary).

(a) *Scope and general rule*. This section applies to the extent that, pursuant to section 304(a)(1), a United States person is treated as transferring stock of a domestic or foreign corporation to a foreign corporation (foreign acquiring corporation) in exchange for stock of the foreign acquiring corporation in a transaction to which section 351(a) applies (deemed section 351 exchange). Except to the extent provided in paragraph (b) of this section, a transfer of stock by a United States person to a foreign acquiring corporation in a deemed section 351 exchange is not subject to section 367(a)(1).

(b) *Special rule*. Notwithstanding paragraph (a) of this section, if the distribution received by the United States person in redemption of the stock of the foreign acquiring corporation deemed issued in the deemed section 351 exchange is applied against and reduces (in whole or in part), pursuant to section 301(c)(2), the basis of stock of the foreign acquiring corporation held by the United States person other than the stock deemed issued in the deemed section 351 exchange, the United States person shall recognize gain pursuant to this paragraph (b). The exceptions described in §1.367(a)–3(b)(1) and (c)(1) shall not apply to a transfer of stock described in paragraph (a) of this section. The amount of gain recognized by a United States person pursuant to this paragraph (b) shall equal the amount, if any, by which—

(1) The gain realized by the United States person with respect to the transferred stock in connection with the deemed section 351 exchange exceeds;

(2) The amount of the distribution received by the United States person in redemption of the stock of the foreign acquiring corporation deemed issued in the deemed section 351 exchange that is treated as a dividend under section 301(c)(1) and included in gross income by the United States person.

(c) *Ordering rule*. For purposes of paragraph (b)(1) of this section, the amount of gain realized by the United States person in connection with the deemed section 351 exchange shall be determined without regard to the amount of gain recognized by the United States person under paragraph (b) of this section.

(d) *Allocation of recognized gain*. Gain recognized by a United States person pursuant to paragraph (b) of this section shall be treated as recognized with respect to the stock transferred in the deemed section 351 exchange in proportion to the amount of gain realized by the United States person with respect to such stock. See §1.367(a)–1T(b)(4) for additional rules on the character, source, and adjustments relating to gain recognized under section 367(a).

(e) *Example*. The following example illustrates the rules of this section:

Example. (i) *Facts*. (A) USP, a domestic corporation, wholly owns FC1 and FC2, each a foreign corporation. USP, FC1 and FC2 use a calendar taxable year. The FC1 stock has a $40x basis and $100x fair market value. The FC2 stock has a $100x basis and $100x fair market value. As of December 31, year 1, FC1 has zero earnings and profits, and FC2 has $20x earnings and profits. On December 31, year 1, in a transaction described in section 304(a)(1), USP sells the FC1 stock to FC2 for $100x cash.

(B) Because USP wholly owns FC1 before the transactions and is treated, under section 318, as indirectly owning 100% of the FC1 stock after the transfer, under section 304(a)(1), USP and FC2 are treated in the same manner as if USP contributed the FC1 stock to FC2 in a deemed section 351 exchange in exchange solely for $100x of FC2 stock, and then FC2 redeemed for $100x cash its stock deemed issued to USP. Because USP wholly owns FC1 before the sale and is treated as owning 100% of FC1 after the sale, section 302(a) does not apply to the redemption. Instead, under section 302(d), the redemption is treated as a distribution to which section 301 applies. Pursuant to section 304(b)(2), $20x of the distribution is treated as a dividend from FC2. With respect to the remaining $80x, USP takes the position that $40x is applied against and reduces the basis of the FC2 stock issued in the deemed section 351 exchange, and $40x is applied against and reduces the basis of the FC2 stock held by USP prior to (and after) the transaction.

(ii) *Analysis*. Under paragraph (b) of this section, USP must recognize gain of $40x on its transfer of the FC1 stock to FC2 in the deemed section 351 exchange (the amount by which the $60x gain realized by USP on the deemed section 351 exchange with respect to the F1 stock exceeds the $20x dividend inclusion). Pursuant to paragraph (b) of this section, the exception under §1.367(a)–3(b) is not available to the transfer of the FC1 stock by USP to FC2 in the deemed section 351 exchange. Thus, USP cannot avoid gain recognition under paragraph (b) of this section by entering into a gain recognition agreement with respect to its transfer of the FC1 stock to FC2 in the deemed section 351 exchange. Under paragraph (d) of this section, the $40x gain recognized is allocated among the shares of FC1 stock transferred to FC2 in the deemed section 351 exchange in proportion to the gain realized by USP on the transfer of such shares. Under paragraph (c) of this section, the application of paragraph (b) of this section is determined prior to taking into account the $40x increase to the basis of the FC1 stock transferred by USP. Under section 362, the basis of the FC1 stock in the hands of FC2 is increased by $40x, the amount of gain recognized by the USP on the transfer of the FC1 stock under paragraph (b) of this section. Under section 358, the basis of the FC2 stock received by USP in the deemed section 351 exchange is similarly increased by $40x. See §1.367(a)–1T(b)(4). The $40x increase to the basis of the FC2 stock is taken into account before determining the consequences of the redemption of such stock under section 304(a)(1).

(f) *Effective/applicability date*. This section applies to transfers occurring on or after February 10, 2009. See §1.367(a)–3(a), as contained in 26 CFR part 1 revised as of April 1, 2008, for transfers occurring on or after February 21, 2006, and before February 10, 2009.

(g) *Expiration date*. This section expires on or before February 10, 2012.

Par. 4. Section 1.367(b)–4 is amended by revising the second sentence in paragraph (a) and adding paragraphs (e), (f) and (g) to read as follows:

§1.367(b)–4 Acquisition of foreign corporate stock or assets by a foreign corporation in certain nonrecognition transactions.

(a) * * * For rules applicable when, pursuant to section 304(a)(1), a foreign acquiring corporation is treated as acquiring the stock of a foreign acquired corporation in a transaction to which section 351(a) applies, see §1.367(b)–4T(e). * * *

* * * * *

(e) [Reserved]. For further guidance, see §1.367(b)–4T(e).

(f) [Reserved]. For further guidance, see §1.367(b)–4T(f).

(g) [Reserved]. For further guidance, see §1.367(b)–4T(g).

Par. 5. Section 1.367(b)–4T is added to read as follows:

§1.367(b)–4T Acquisition of foreign corporate stock or assets by a foreign corporation in certain nonrecognition transactions (temporary).

(a) through (d) [Reserved]. For further guidance, see §1.367(b)–4(a) through (d).

(e) *Application of section 367(b) to transactions described in section 304(a)(1)*— (1) *Scope and general rule*. This section applies to the extent that, pursuant to section 304(a)(1), an exchanging shareholder is treated as transferring the stock of a foreign acquired corporation to a foreign acquiring corporation in a transaction to which section 351(a) applies (deemed section 351 exchange). Except to the extent provided in paragraph (e)(2) of this section, a transfer of stock of a foreign acquired corporation by an exchanging shareholder in a deemed section 351 exchange shall not be subject to paragraph (b) of this section.

(2) *Special rule*. Notwithstanding paragraph (e)(1) of this section, a transfer of stock of a foreign acquired corporation by an exchanging shareholder to a foreign acquiring corporation in a deemed section 351 exchange shall be subject to paragraph (b) of this section to the extent the distribution received by the exchanging shareholder in redemption of the stock of the foreign acquiring corporation is applied against and reduces, pursuant to section 301(c)(2), the basis of stock of the foreign acquiring corporation held by the exchanging shareholder other than the stock deemed issued by the foreign acquiring corporation in the deemed section 351 exchange.

(3) *Allocation of income inclusion*. If the income inclusion resulting from the application of paragraph (e)(2) of this section is less than the section 1248 amount attributable to the shares of stock of the foreign acquired corporation transferred by the exchanging shareholder in the deemed section 351 exchange, the amount of the income inclusion attributable to each share of stock transferred in the deemed section 351 exchange shall be determined by mul-

tiplying the income inclusion by the percentage that the section 1248 amount attributable to such share of stock bears to the aggregate section 1248 amount attributable to all of the shares of stock transferred in the deemed section 351 exchange.

(4) *Example*. The rules of this paragraph (e) are illustrated by the following example:

Example. (i) *Facts*. (A) FP, a foreign corporation, wholly owns USP, a domestic corporation. USP wholly owns CFC1, and CFC1 wholly owns CFC2. CFC2 wholly owns CFC3. CFC1, CFC2 and CFC3 are controlled foreign corporations within the meaning of section 957(a). USP, CFC1, CFC2 and CFC3 use a calendar taxable year. CFC1 owns 30% of the outstanding stock of FS, a foreign corporation. FP owns the remaining 70% of the outstanding stock of FS. The CFC2 stock has a $40x basis and $100x fair market value. The FS stock held by CFC1 has a $60x basis and $100x fair market value. As of December 31, year 1, CFC2 has $20x of section 1248 earnings and profits, CFC3 has $40x of section 1248 earnings and profits, and FS has zero earnings and profits. On December 31, year 1, in a transaction described in section 304(a)(1), CFC1 sells the CFC2 stock to FS for $100x cash. FS is not a controlled foreign corporation (within the meaning section 957(a)) either before or after the sale of the CFC2 stock.

(B) Because CFC1 wholly owns CFC2 before the transaction and is treated, under section 318, as indirectly owning 100% of the CFC2 stock after the transaction, under section 304(a)(1), CFC2 and FS are treated as if CFC1 contributed the CFC2 stock to FS in a deemed section 351 exchange in exchange solely for $100x of FS stock, and then FS redeemed for $100x cash its stock deemed issued to CFC1. Because CFC1 wholly owned CFC2 before the transaction and is treated, under section 318, as indirectly owning 100% of CFC2 after the transaction, section 302(a) does not apply to the redemption. Instead, under section 302(d), the redemption is treated as a distribution to which section 301 applies. Pursuant to section 304(b)(2), $20x of the distribution is treated as a dividend from the earnings and profits of CFC2. With respect to the remaining $80x, CFC1 takes the position that $40x is applied against and reduces the basis of the FS stock deemed issued in the transaction, and $40x is applied against and reduces the basis of the FS stock held by CFC1 prior to (and after) the transaction.

(ii) *Analysis.* Under paragraph (e)(2) of this section, the transfer by CFC1 of the CFC2 stock to FS in the deemed section 351 exchange is subject to paragraph (b) of this section to the extent the distribution received by CFC1 in redemption of the FS stock issued in the deemed section 351 exchange is applied against and reduces, under section 301(c)(2), the basis of the FS stock held by CFC1 before (and after) the transaction. Thus, because $40x of the distribution received by CFC1 from FS in redemption of the FS stock issued in the deemed section 351 exchange is applied against and reduces, under section 301(c)(2), the basis of the FS stock held by CFC1 before (and after) the transaction, under paragraph (b) of this section, CFC1 must include $40x in income as a deemed dividend. See §1.367(b)–2(e) for the treatment of the $40x income inclusion. In total, CFC1 recognizes dividend income of $60x, $20x from the application of section 304(a)(1) to the sale of the CFC2 stock to FS and $40x under paragraph (b) of this section by reason of the application of paragraph (e)(2) of this section.

(f) *Effective/applicability date*. Paragraph (e) of this section applies to transfers occurring on or after February 10, 2009. See §1.367(b)–4, as contained in 26 CFR part 1 revised as of April 1, 2008, for transfers occurring on or after February 21, 2006, and before February 10, 2009.

(g) *Expiration date*. This section expires on or before February 10, 2012.

Par. 6. Section 1.1248–1 is amended by revising paragraphs (b) and (g) and adding paragraph (h) to read as follows:

§1.1248–1 Treatment of gain from certain sales or exchanges of stock in certain foreign corporations.

* * * * *

(b) [Reserved]. For further guidance, see §1.1248–1T(b).

* * * * *

(g) *Effective/applicability date*. (1) The third sentence in paragraph (a)(1), paragraph (a)(4), and paragraph (a)(5), *Example 4*, of this section apply to income inclusions that occur on or after July 30, 2007. A taxpayer may elect to apply paragraph (a)(4) of this section to income inclusions in open taxable years provided that it consistently applies paragraph (a)(4) of this section for income inclusions in the first year for which the election is applicable and in all subsequent years.

(2) [Reserved]. For further guidance, see §1.1248–1T(g)(2).

(h) [Reserved]. For further guidance, see §1.1248–1T(h).

Par. 7. Section 1.1248–1T is added to read as follows:

§1.1248–1T Treatment of gain from certain sales or exchanges of stock in certain foreign corporations (temporary).

(a) [Reserved]. For further guidance, see §1.1248–1(a).

(b) *Sale or exchange*. For purposes of section 1248(a), the term *sale or exchange* includes the receipt of a distribution which is treated as in exchange for stock under section 302(a) (relating to distributions in redemption of stock), section 331(a)(1) (relating to distributions in complete liquidation of a corporation), or section 331(a)(2) (relating to distributions in partial liquidation of a corporation). For purposes of section 1248(a), gain recognized by a shareholder under section 301(c)(3) in connection with a distribution of property by a corporation with respect to its stock shall be treated as gain from the sale or exchange of stock of such corporation.

(c) through (f) [Reserved]. For further guidance, see §1.1248–1(c) through (f).

(g) *Effective/applicability dates*. (1) [Reserved]. For further guidance, see §1.1248–1(g)(1).

(2) Paragraph (b) of this section applies to distributions that occur on or after February 10, 2009.

(h) *Expiration date*. This section expires on or before February 10, 2012.

Linda M. Kroening,
Acting Deputy Commissioner for Services and Enforcement.

Approved January 13, 2009.

Eric Solomon,
Assistant Secretary of the Treasury (Tax Policy).

(Filed by the Office of the Federal Register on February 10, 2009, 8:45 a.m., and published in the issue of the Federal Register for February 11, 2009, 74 F.R. 6824)

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26 CFR 1.367(a)–3: Treatment of transfers of stock or securities to foreign corporations.

T.D. 9446

DEPARTMENT OF THE TREASURY
Internal Revenue Service
26 CFR Parts 1 and 602

Gain Recognition Agreements With Respect to Certain Transfers of Stock or Securities by United States Persons to Foreign Corporations

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations and removal of temporary regulations.

SUMMARY: This document contains final regulations under section 367(a) of the Internal Revenue Code (Code) concerning gain recognition agreements filed by United States persons with respect to transfers of stock or securities to foreign corporations. The regulations finalize temporary regulations published on February 5, 2007 (T.D. 9311, 2007–1 C.B. 635). The regulations primarily affect United States persons that transfer (or have transferred) stock or securities to foreign corporations and that will enter (or have entered) into a gain recognition agreement with respect to such a transfer.

DATES: *Effective Date:* These regulations are effective February 11, 2009.

Applicability Dates: For dates of applicability, see §§1.367(a)–3(g) and 1.367(a)–8(r).

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG–147144–06), room 5203, Internal Revenue Service, PO Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to CC:PA:LPD:PR (REG–147144–06), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, DC, or sent electronically via the Federal eRulemaking Portal at *www.regulations.gov* (IRS REG–147144–06).

FOR FURTHER INFORMATION CONTACT: S. James Hawes, (202) 622–3860 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

The collections of information in these regulations have been reviewed and approved by the office of Management and Budget in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)) under control number 1545–2056.

The collections of information in these final regulations are in §1.367(a)–8(d), (g), (k), and (o). Responses to the collections of information are required to avoid recognizing gain under an existing gain recognition agreement and to facilitate electronic filing. The regulations also require the amount of any gain recognized under a gain recognition agreement and applicable interest due with respect to any additional tax due with respect to such gain to be reflected on a schedule included with the electronically-filed return of the taxpayer.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information, unless the collection of information displays a valid control number.

Books and records relating to these collections of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential, as required by 26 U.S.C. 6103.

Background

On February 5, 2007, the IRS and Treasury Department issued temporary and proposed regulations under section 367(a) concerning the terms and conditions for a gain recognition agreement (GRA) filed by a United States person (the U.S. transferor) in connection with a transfer of stock or securities to a foreign corporation (transferee foreign corporation) and the impact of certain transactions on an existing GRA (the 2007 regulations). 72 F.R. 5184 (T.D. 9311, 2007–1 C.B. 635). No public hearing on the 2007 regulations was requested or held; however, numerous comments were received. After considering the comments received, the IRS and Treasury Department adopt the 2007 regulations, with modifications, as final regulations under section 367(a). This Treasury decision also removes the temporary regulations and revises cross-references where appropriate to reflect the removal and replacement of the temporary regulations with final regulations.

Summary of Comments and Explanation of Revisions

A. *Subsequent Nonrecognition Transfers—In General*

The 2007 regulations provide specific exceptions for certain dispositions or other events that would otherwise require gain to be recognized under an existing GRA (triggering event). The exceptions generally apply to dispositions that qualify for nonrecognition treatment under the Code and require the U.S. transferor to enter into a new GRA with respect to the initial transfer for the remaining term of the existing GRA.

Several commentators asserted that the exceptions provided by the 2007 regulations did not literally apply to various dispositions qualifying for nonrecognition treatment because the entity making the transfer is not described in the relevant exception, thus inappropriately resulting in gain recognition under a GRA. For example, assume that in year 1 a domestic corporation, USP, transfers stock of a foreign corporation, FS1, to another foreign corporation, FS2, pursuant to an exchange to which section 351 applies (the initial transfer). USP files a GRA with respect to the initial transfer. In year 2, FS2 transfers the FS1 stock received from USP in year 1 to another foreign corporation, FS3, solely in exchange for stock of FS3 under section 351. The year 2 transfer of the FS1 stock by FS2 would constitute a triggering event for purposes of the GRA filed by USP with respect to the initial transfer, but the transfer qualifies for an exception under the 2007 regulations. USP complies with the requirements of the 2007 regulations with respect to the GRA filed for the initial transfer. In year 3, FS3 contributes the FS1 stock received from FS2 in year 2 to another foreign corporation, FS4, solely in exchange for stock of FS4 under section 351. The year 3 transfer of the FS1 stock by FS3 is a triggering event with respect to the GRA entered into by USP in connection with the initial transfer.

The 2007 regulations provide an exception for certain subsequent transfers of the transferred stock in a transaction to which section 351 applies (section 351 exchange), but the exception does not clearly apply when the transferor in the section 351 exchange is not the transferee foreign corporation. Commentators expressed similar concerns with respect to other nonrecognition transactions, including liquidations described in section 332 (section 332 liquidation), transactions to which section 355 applies (section 355 transactions), and transactions involving partnerships. The commentators suggested various alternatives for avoiding the inappropriate triggering of a GRA in such cases.

The IRS and Treasury Department agree that certain nonrecognition transactions that may not qualify for an exception under the 2007 regulations should not trigger an existing GRA. Because specific exceptions provide certainty to the relevant transactions, the final regulations retain the exceptions of the 2007 regulations with modifications so that the exceptions apply to transactions involving one or more entities not clearly described in the 2007 regulations. For example, under the final regulations the exception for a section 351 exchange of the transferred stock applies to any transfer of the transferred stock regardless of the identity of the transferor. The final regulations include additional specific exceptions and a general exception for certain transactions that cannot be adequately covered by a specific exception because of the myriad factual permutations.

The general exception provided by the final regulations applies generally to any disposition or other event that would otherwise constitute a triggering event if the disposition is a nonrecognition transaction (as defined in section 7701(a)(45), but including an exchange described in section 351(b) or 356 even if all gain realized is recognized); a U.S. transferor retains a direct or indirect interest in the transferred stock or securities (or the assets of the transferred corporation, such as where the transferred corporation has liquidated in the interim); and the U.S. transferor that retains such direct or indirect interest enters into a new GRA with respect to the initial transfer. However, if, as a result of the disposition or other event, a foreign corporation acquires all or part of the transferred stock or securities (or substantially all the assets of the transferred corporation) the general exception shall apply only if the U.S. transferor owns at least five percent (applying the attribution rules of section 318, as modified by section 958(b)) of the total voting power and the total value of the outstanding stock of such foreign corporation immediately after the disposition or other event. This five percent ownership condition is intended to limit the application of the general exception in transactions where the U.S. transferor retains a minimal interest in the transferred stock or securities (or substantially all the assets of the transferred corporation). The final regulations include examples to illustrate the application of the general exception.

A disposition or other event to which the general exception applies shall be subject to the provisions of the final regulations to the same extent and in the same manner as a disposition or event to which a specific exception applies. For example, even though a specific exception is generally available for a section 351 exchange of the transferred stock by the transferee foreign corporation, the U.S. transferor must still recognize gain under the existing GRA to the extent the transferee foreign corporation would otherwise recognize gain in the exchange under section 351(b). The U.S. transferor must therefore similarly recognize gain in connection with a disposition or other event to which the general exception applies to the extent that the transferee foreign corporation would otherwise recognize gain in the exchange under section 351(b).

A new GRA filed under the general exception is generally subject to the same terms and conditions as the existing GRA, but must also describe the subsequent dispositions that would constitute triggering events (based on the principles of the final regulations, but not including any triggering event otherwise described in the final regulations) and include a statement that the U.S. transferor agrees to treat such dispositions as triggering events. In addition, the final regulations provide that, with respect to a new GRA filed under the general exception, a triggering event shall also include any other disposition or event that is inconsistent with the principles of the triggering event exceptions including, for example, an indirect disposition of the transferred stock or securities or of substantially all of the assets of the transferred corporation. This additional condition is similar to the condition applicable to a GRA filed in connection with an indirect stock transfer described in §1.367(a)–3(d).

One commentator requested that an exception be provided for a securities lending transaction to which section 1058 applies. The final regulations do not provide such an exception.

B. *Dispositions Pursuant to an Intercompany Transaction*

Under the 2007 regulations, a complete or partial disposition by the U.S. transferor of the stock of the transferee foreign corporation received in the initial transfer generally requires the U.S. transferor to recognize gain under the GRA. Exceptions to this general rule are provided for certain nonrecognition transfers to which sections 351, 354, or 721 applies. As described further in part D. of this Preamble, the 2007 regulations provide further that a GRA shall instead terminate (in whole or in part) if the U.S. transferor disposes of all or part of the stock of the transferee foreign corporation received in the initial transfer pursuant to a transaction in which all gain realized is recognized currently and included in taxable income as a result of the disposition, but only if the basis of the stock disposed of (excluding certain adjustments to such basis) is not greater than the basis in the transferred stock or securities at the time of the initial transfer.

If the U.S. transferor disposes of stock of the transferee foreign corporation pursuant to an intercompany transaction (within the meaning of §1.1502–13) that is not described in section 351 or 354, the conditions for terminating the existing GRA (in whole or in part) are not satisfied because, under the provisions of §1.1502–13, the U.S. transferor generally defers taking into account any gain realized and recognized on the disposition. Thus, such a disposition would be a triggering event.

Several commentators asserted that it is inappropriate to require the U.S. transferor to recognize gain under the GRA in such cases because the stock of the transferee foreign corporation remains within the consolidated group of which the U.S. transferor is a member. It is also inappropriate to terminate the GRA because the intercompany item has not been taken into account. Instead, the commentators recommended that the GRA remain in effect for its remaining term. The IRS and Treasury Department agree with this recommendation, and the final regulations provide a specific exception for dispositions of stock of the transferee foreign corporation pursuant to an intercompany transaction (intercompany transaction exception) to which a specific triggering event exception does not apply. If the intercompany transaction exception applies, the U.S. transferor remains subject to the existing GRA. But see the discussion below when the intercompany transaction is a nonrecognition transaction in which an amount of gain is recognized.

The intercompany transaction exception is available if two conditions are satisfied. The first condition is that the basis of the stock of the transferee foreign corporation disposed of in the intercompany transaction is not greater than the sum of the aggregate basis in the transferred stock or securities at the time of the initial transfer, any increase to the basis of the transferred stock or securities by reason of gain recognized by the U.S. transferor in connection with the initial transfer, and any increase to the basis of the stock of the transferee foreign corporation by reason of income inclusions by the U.S. transferor (for example, pursuant to section 961). To satisfy this basis condition, the U.S. transferor can elect to reduce the basis of the stock of the transferee foreign corporation, effective immediately before the intercompany transaction.

The second condition is that the annual certification filed with respect to the existing GRA for the taxable year during which the intercompany transaction occurs includes a complete description of the intercompany transaction and a schedule illustrating how the basis condition is satisfied.

Because the final regulations provide specific exceptions for certain nonrecognition transfers of stock of the transferee foreign corporation (for example, pursuant to a section 351 exchange), the new intercompany transaction exception applies only to the extent the intercompany transaction gives rise to an intercompany item (as defined in §1.1502–13(b)(2)). If the intercompany item is a gain, the existing GRA must be divided into two separate agreements — one that remains with the U.S. transferor (of an amount equal to the intercompany item) and another that moves to the acquiring member (of an amount equal to the remaining amount of the existing GRA amount). For example, assume the amount of the existing GRA is $100x, the intercompany transaction is described in section 351(b), and the U.S. transferor recognizes $20x gain (the intercompany item) in the intercompany transaction. The intercompany transaction exception applies to the extent of the $20x intercompany item, and the exception for section 351 exchanges applies to the remainder of the transfer. Thus, the U.S. transferor remains subject to a $20x GRA (to the extent of the $20x intercompany item), and the acquiring member becomes subject to an $80x GRA. This result is similar to that of a transfer of the stock of the transferee foreign corporation to a domestic acquiring corporation in a section 351 exchange that is not an intercompany transaction but in which the U.S. transferor recognizes gain under section 351(b). In such a case, the amount of the new GRA entered into by the domestic acquiring corporation is reduced by the amount of gain recognized by the U.S. transferor on the transfer under section 351(b). The U.S. transferor does not remain subject to a GRA because the gain recognized under section 351(b) is taken into account. By contrast, if the section 351 exchange were an intercompany transaction, the U.S. transferor must remain subject to a GRA in an amount equal to the gain recognized under section 351(b) because the gain has not been taken into account.

If the intercompany item is a loss, however, the U.S. transferor shall remain subject to the entire GRA. In addition, in such a case, the termination rule that applies to dispositions of the stock of the transferee foreign corporation in which all realized gain is recognized and included in taxable income during the taxable year of the disposition shall not apply.

The final regulations provide rules to coordinate the subsequent inclusion in taxable income of an intercompany item and an amount of gain recognized under the GRA. Generally, under the coordination rule, if subsequent to an intercompany transaction to which the intercompany transaction exception applies, a disposition or other event occurs that requires the U.S. transferor to take into account the intercompany item related to the intercompany transaction (under the provisions of §1.1502–13), the disposition shall not constitute a triggering event. Instead the GRA shall terminate without further effect or the amount of gain subject to the GRA shall be reduced based on the principles of the termination rule that applies to certain dispositions of the stock of the transferee foreign corporation received in the initial transfer. The final regulations include an example illustrating this rule.

C. *Divisive Reorganizations*

The preamble to the 2007 regulations requested comments concerning whether specific exceptions should be provided for divisive reorganizations involving the U.S. transferor, the transferee foreign corporation, or the transferred corporation. No comments were received. However, the final regulations provide a specific exception for divisive reorganizations involving a transfer of the stock of the transferee foreign corporation received in the initial transfer to a domestic corporation (domestic controlled corporation) before the distribution of the stock of the domestic controlled corporation. The specific exception applies if the domestic controlled corporation enters into a new GRA with respect to the initial transfer. The IRS and Treasury Department expect the general exception to apply to other divisive reorganizations, as appropriate. The final regulations include examples illustrating the application of the general exception to divisive reorganizations.

D. *GRA Termination Events*

If certain conditions are met, under the 2007 regulations an existing GRA terminates without further effect (termination rule) if the U.S. transferor (or other specified United States persons) re-acquires the transferred stock or securities, or the U.S. transferor disposes of the stock of the transferee foreign corporation received in the initial transfer. One condition for the application of the termination rule is that, with certain adjustments, the basis of the transferred stock or securities in the hands of the U.S. transferor (or other specified United States person) immediately following the acquisition or the basis of stock of the transferee foreign corporation disposed of by the U.S. transferor, as relevant, must not be greater than the basis of the transferred stock or securities at the time of the initial transfer. To satisfy this basis condition, the 2007 regulations generally permit the U.S. transferor (or other United States person) to reduce the basis of the transferred stock or securities (or the stock of the transferee foreign corporation, as applicable). The 2007 regulations further permit an increase to basis of other stock or securities in the transferred corporation (or stock of the transferee foreign corporation, as applicable) by a corresponding amount, but not in excess of fair market value.

The final regulations retain the termination rule and the conditions for its application, including the option to reduce basis. However, the IRS and Treasury Department have determined that it is inappropriate to permit the shifting of basis to other stock or securities in the case of an election to reduce the basis of stock or securities. The final regulations, therefore, do not permit the U.S. transferor (or other United States person) to increase the basis of other stock or securities of the transferred corporation (or stock of the transferee foreign corporation, as applicable). The general exception, however, may apply allowing the U.S. transferor (or other United States person) to enter into a new GRA in connection with a transaction in which the transferred stock or securities are re-acquired in lieu of reducing the basis of the transferred stock or securities.

One commentator questioned whether the termination rule applies in the case of a downstream asset reorganization of the transferee foreign corporation into the transferred corporation because the U.S. transferor receives newly-issued stock of the transferred corporation in the transaction and not the stock transferred in the initial transfer. The IRS and Treasury Department believe it is appropriate for the termination rule to apply in the case of such downstream asset reorganizations. Accordingly, by revising the location of a rule contained in the 2007 regulations, the final regulations clarify that the term *transferred stock or securities* includes any stock or securities of the transferred corporation with a basis determined, in whole or in part, by reference to the basis of the stock or securities transferred in the initial transfer. Thus, in the case of a downstream asset reorganization, for purposes of the termination rule, the newly-issued stock of the transferred corporation deemed distributed by the transferee foreign corporation to the U.S. transferor under section 361(c) is the stock transferred in the initial transfer.

The 2007 regulations provide an exception for certain expropriation losses that would otherwise constitute triggering events. The final regulations modify the rule to provide instead that the amount of gain subject to a GRA is reduced to the extent a loss is sustained with respect to stock of the transferee foreign corporation, the transferred stock or securities, or substantially all the assets of the transferred corporation by reason of an expropriation of such property by the government of a foreign country, any political subdivision thereof, or any agency or instrumentality of the foregoing.

E. *Transfers by U.S. Transferor Pursuant to an Outbound Asset Reorganization*

The 2007 regulations provide an exception for a transfer of stock of the transferee foreign corporation by the U.S. transferor to a domestic corporation pursuant to an asset reorganization described in section 368(a)(1). See §1.367(a)–8T(e)(3)(i). The preamble to the 2007 regulations requested comments concerning whether an exception should also be provided for an outbound transfer of the stock of the transferee foreign corporation by the U.S. transferor to a foreign corporation pursuant to an asset reorganization described in section 368(a)(1). No comments were received. However, after studying the issue further and considering the principles of the proposed regulations recently issued under sections 367(a)(5), 367(b), and 1248(f) (73 FR 49278), the IRS and Treasury Department have determined that it is appropriate for an exception to apply to such an outbound transfer. The final regulations do not include a specific exception for such outbound transfers, but the IRS and Treasury Department expect the general exception provided by the final regulations to apply to such transfers, as appropriate. The final regulations include an example illustrating the application of the general exception to such a transfer.

F. *Ordering Rule if Triggering Event Affects Multiple GRAs*

The final regulations provide an ordering rule to determine the amount of gain recognized under a GRA when a disposition or other event requires gain to be recognized under more than one GRA. The ordering rule adopts a "first-in-time" approach, providing that gain must first be recognized under the GRA that relates to the earliest initial transfer, then under the GRA that relates to the transfer immediately following the initial transfer, and so forth until the appropriate amount of gain under each GRA has been recognized. This ordering rule clarifies that the gain recognized under a GRA is determined after taking into account any increase to the basis of the transferred stock or securities resulting from gain recognized under another GRA that relates to an earlier initial transfer. The final regulations include an example to illustrate the ordering rule.

G. *Section 301 Distributions*

The 2007 regulations define a disposition as any transfer that would constitute a disposition for any purpose of the Code and the regulations under the Code, but exclude a stock redemption described under section 302(d) (dividend equivalent redemption) to the extent section 301(c)(1) applies. One commentator requested that the final regulations clarify whether the rule for dividend equivalent redemptions applies to redemptions of stock of the transferee foreign corporation, the transferred corporation, or both. The commentator also requested that the final regulations confirm that a distribution of property to which section 301(c)(2) applies (including in the case of a dividend equivalent redemption) does not constitute a disposition of the relevant stock.

The final regulations provide that a disposition generally does not include the receipt of a distribution of property with respect to stock to which section 301 applies, including by reason of section 302(d). The final regulations provide further that a dividend equivalent redemption shall constitute a disposition if the U.S. transferor does not enter into a new GRA that includes appropriate provisions to account for the redemption. The final regulations include an example illustrating this rule and describing the types of appropriate provisions that should be included in the new GRA. The provisions to be included in the GRA are necessary, for example, to account for a dividend equivalent redemption that occurs pursuant to a transaction to which section 304(a)(1) applies and in which the transferor does not retain a direct or indirect interest in the acquiring corporation. In such a case, the GRA would need to provide appropriate provisions to account for indirect dispositions of the transferred stock that should require gain to be recognized under the new GRA.

The final regulations provide that the U.S. transferor must recognize gain under a GRA to the extent gain is recognized under section 301(c)(3) with respect to the transferred stock and that the amount of gain subject to the GRA is reduced to the extent the U.S. transferor recognizes gain under section 301(c)(3) with respect to the stock of the transferee foreign corporation received in the initial transfer.

H. *Elections under Section 338*

One commentator requested that the final regulations provide an exception for a deemed sale of the assets of the transferred corporation or the transferee foreign corporation by reason of an election under section 338(g). The commentator posited a fact pattern where the U.S. transferor entered into a GRA in connection with a transfer of less than 20 percent of the outstanding stock of the transferred corporation to the transferee foreign corporation, and, within the GRA term, the transferee foreign corporation acquires additional stock of the transferred corporation constituting a qualified stock purchase (within the meaning of section 338(d)(3)) and makes an election under section 338(g) with respect to such acquisition. The deemed asset sale that results from the section 338(g) election is a sale for all purposes of the Code (see §1.338–2(c)(6)) and thus, under the 2007 regulations, would require the U.S. transferor to recognize the full amount of gain subject to the GRA. The commentator asserted that providing an exception for such a deemed asset sale was consistent with the policies of the GRA regime because the deemed asset sale is not a monetization of the assets or stock of the transferred corporation.

The IRS and Treasury Department agree with the commentator, and the final regulations provide that a deemed sale of assets of the transferred corporation or the transferee foreign corporation by reason of an election under section 338(g) shall not constitute a triggering event for purposes of the GRA. However, the sale of stock of the target corporation pursuant to the qualified stock purchase shall be taken into account for purposes of a GRA. The sale of stock of the transferred or transferee foreign corporation by the seller should either require gain to be recognized under a GRA or terminate the GRA without further effect if the conditions for the termination rule are satisfied, even if an election under section 338(g) is made.

By contrast, a deemed sale of assets of a domestic corporation by reason of an election under section 338(h)(10) shall continue to be taken into account for purposes of §1.367(a)–8. Thus, for example, if an election under section 338(h)(10) were made with respect to the U.S. transferor, the deemed sale of the stock of the transferee foreign corporation held by the U.S. transferor would constitute a disposition of such stock that either requires gain to be recognized under the GRA or terminates the GRA if the conditions for the termination rule are satisfied.

On August 22, 2008, the IRS and Treasury Department issued proposed regulations under section 336(e) (REG–143544–04, 2008–42 I.R.B. 947) that provide rules generally consistent with the rules that apply to elections under section 338(h)(10). The proposed regulations under section 336(e) shall be applicable to dispositions occurring on or after the proposed regulations are published as final regulations in the **Federal Register**. The proposed regulations do not apply if the selling corporation or the target corporation is foreign. When final regulations under section 336(e) are promulgated, the IRS and Treasury Department anticipate that a deemed asset sale pursuant to a section 336(e) election with respect to a domestic corporation shall be taken into account for purposes of §1.367(a)–8, similar to a deemed asset sale pursuant to an election under section 338(h)(10). Comments are requested in this regard, including what special rules would be required with respect to an existing GRA if an election under section 336(e) were permitted if the selling corporation or the target corporation were foreign.

I. *Expatriation under Section 877A*

The 2007 regulations provide that a GRA shall be triggered immediately before the date on which an individual U.S. transferor loses United States citizenship or ceases to be taxed as a lawful permanent resident (as defined in section 877(e)(2)). This rule applies even if the individual U.S. transferor would have recognized gain with respect to the stock of the transferee foreign corporation under section 877. The final regulations generally retain this rule, modified for the enactment of section 877A. Further, the final regulations make clear that the termination rule that applies in certain cases where the U.S. transferor disposes of the stock of the transferee foreign corporation is not applicable to an individual U.S. transferor that is subject to section 877A.

J. *GRA Content*

Comments were received regarding whether the information required with a GRA could instead be made available by the U.S. transferor "upon request." The final regulations confirm that the information required with a GRA must be included with the GRA as filed with the tax return of the U.S. transferor.

K. *Other Changes*

Under the 2007 regulations, certain dispositions that qualify for an exception nonetheless require the U.S. transferor to recognize gain under the existing GRA. For example, to the extent the transferee foreign corporation would be required to recognize gain under section 351(b) or 356(a)(1) in connection with an exchange of the transferred stock, the U.S. transferor must recognize gain under the GRA notwithstanding that an exception applies to the exchange of the transferred stock. The final regulations retain this rule; however, the final regulations refer to any disposition or event that requires gain to be recognized under a GRA as a "gain recognition event." A gain recognition event includes a triggering event, a disposition that would constitute a triggering event but for the application of an exception (such as the section 351(b) or 356 exchange described above), and a section 301 distribution that would require gain to be recognized under section 301(c)(3) with respect to the transferred stock.

The final regulations clarify the amount of gain subject to a GRA that is filed by a domestic corporate shareholder of a domestic corporation (the U.S. transferor) that transfers stock or securities to the transferee foreign corporation pursuant to an outbound asset reorganization that is subject to section 367(a)(5) and the regulations under that section.

The final regulations clarify that, if a GRA is entered into in connection with a transfer of a partnership interest, a complete or partial disposition of such partnership interest shall constitute a triggering event for purposes of the GRA.

The 2007 regulations provide exceptions for certain dispositions of stock of the transferee foreign corporation or of substantially all the assets of the transferred corporation that are described in section 351, 354 (but only in the case of a reorganization described in section 368(a)(1)(B)), or 721, if, in addition to other requirements, the U.S. transferor complies with requirements similar to those for the exception that applies to similar dispositions of the transferred stock or securities. See §1.367(a)–8T(e)(1)(ii). In response to comments requesting certainty concerning the requirements that must be satisfied, the final regulations identify the specific requirements that must be satisfied with respect to such dispositions.

The 2007 regulations provide that, if the transferred corporation is domestic and at the time of the initial transfer the U.S. transferor owned stock in the transferred corporation satisfying the requirements of section 1504(a)(2), the GRA shall terminate without further effect if the transferred corporation disposes of substantially all of its assets in a transaction in which all gain realized is recognized currently. The final regulations retain this termination rule but add, as an additional condition for its application, that the U.S. transferor and the transferred corporation were members of the same consolidated group on the date of the initial transfer. This change was made because the IRS and Treasury Department expect a lesser degree of inside and outside basis disparity within a consolidated group.

The final regulations provide that, if the initial transfer and one or more dispositions or other events (even if an exception applies) that affect the GRA filed by the U.S. transferor with respect to the initial transfer occur within the same taxable year of such U.S. transferor, or if multiple dispositions or events that affect an existing GRA (even if an exception applies) occur in a taxable year of the U.S. transferor that does not include the initial transfer, the U.S. transferor is only required to enter into a single GRA for such taxable year. The GRA must describe the initial transfer and/or each subsequent disposition or other event that affects the GRA. This rule does not apply, however, if a disposition or other event requires a new GRA to be filed by a United States person that was not the U.S. transferor with respect to the existing GRA.

The final regulations provide that the determination of whether a disposition of substantially all of the assets of the transferred corporation has occurred shall be made on the basis of one or more related transactions. The final regulations provide further that the determination shall be made without regard to a disposition of assets described in section 1221(a)(1) in the ordinary course of business.

Effective/Applicability Dates

The final regulations generally apply to transfers of stock or securities occurring on or after March 13, 2009. The final regulations shall not apply to transfers of stock or securities occurring on or after March 13, 2009 that are entered into pursuant to a contract that was binding before February 11, 2009 (subject to customary conditions) and all times thereafter. However, taxpayers may apply the final regulations to such transfers provided the final regulations are applied consistently to all such transfers. Taxpayers may also apply the rules of the final regulations that were not already effective under §1.367(a)–8 (see 26 CFR part 1, revised April 1, 2006) and §1.367(a)–8T to any gain recognition agreement filed with respect to a transfer of stock or securities occurring on a date that is before March 13, 2009 and during a taxable year for which the period of limitations on assessments under section 6501(a) of the Code has not closed.

Availability of IRS Documents

IRS documents cited in this preamble are made available by the Superintendent of Documents, U.S. Government Printing Office, Washington, DC 20402.

Effect on Other Documents

The following publication is obsolete as of February 11, 2009: Notice 2005–74, 2005–2 C.B. 726.

Special Analyses

It has been determined that this Treasury Decision is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that 5 U.S.C. 553(b) and (d) do not apply to these regulations.

It is hereby certified that the collections of information contained in these regulations will not have a significant economic impact on a substantial number of small entities. Accordingly, a regulatory flexibility analysis is not required. These regulations primarily will affect United States persons that are large corporations engaged in cross-border corporate transactions. Thus, the number of affected small entities—in whichever of the three categories defined in the Regulatory Flexibility Act (small businesses, small organizations, and small governmental jurisdictions)—will not be substantial. The IRS and Treasury Department estimate that small organizations and small governmental jurisdictions are likely to be affected only insofar as they might hold a portfolio interest in stock or securities and in the unlikely event that they transfer such stock or securities to a foreign corporation. While a certain number of small entities may transfer stock or securities to a foreign corporation in connection with an acquisition or reorganization, the IRS and Treasury Department do not anticipate the number to be substantial. Furthermore, the IRS and Treasury Department estimate that those small entities that are affected by the regulations will likely face a burden of approximately two hours at an hourly rate of $200. Considering that the collections of information enable taxpayers to defer the current recognition of gain that is subject to a gain recognition agreement, the IRS and Treasury believe that $400 is not a significant economic impact. Pursuant to section 7805(f) of the Internal Revenue Code, this regulation was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Drafting Information

The principal authors of these regulations are Daniel McCall, formerly of the Office of the Associate Chief Counsel (International), and S. James Hawes, of the Office of the Associate Chief Counsel (International). However, other personnel from the IRS and the Treasury Department participated in their development.

* * * * *

Amendments to the Regulations

Accordingly, 26 CFR parts 1 and 602 are amended as follows:

PART 1—INCOME TAXES

Paragraph 1. The authority citation for part 1 is amended by removing the entries for §§1.367(a)–3T(e) and 1.367(a)–8T to read in part as follows:

Authority: 26 U.S.C. 7805* * *

Par. 2. Section 1.338–1 is amended by adding a new sentence at the end of paragraph (a)(2), to read as follows:

§1.338–1. General principles; status of old target and new target.

(a) * * *

(2) * * * See also §1.367(a)–8(k)(13) for a rule applicable to gain recognition agreements (filed under section §§1.367(a)–3(b)(1)(ii) and 1.367(a)–8) and deemed asset sales as a result of an election under section 338(g).

* * * * *

§1.367(a)–3 [Amended]

Par. 3. For each entry in the table in the "Section" column, remove the language in the "Remove" column and add the language in the "Add" column in its place.

Section	Remove	Add
1.367(a)–3(c)(3)(iii)(B)(*1*)(*i*)(*A*)	1296(b)	1297(b)
1.367(a)–3(d)(2)(iii)	§1.367(a)–8T(b)(3)(i) and (d)	§1.367(a)–8(c)(1)(i)
1.367(a)–3(d)(2)(v)	§1.367(a)–8T(d)(2)	§1.367(a)–8(j)(2)(i)
1.367(a)–3(d)(3), *Example 1*(ii), fourth sentence	§1.367(a)–8T(d)(1)	§1.367(a)–8(j)(1)
1.367(a)–3(d)(3), *Example 1*(ii), fourth sentence	§1.367(a)–8T(b)(1)(vii)	§1.367(a)–8(c)(2)(vi)
1.367(a)–3(d)(3), *Example 1*(ii), fifth sentence	§1.367(a)–8T(b)(1)(vii)	§1.367(a)–8(c)(2)(vi)
1.367(a)–3(d)(3), *Example 1A*(ii), first sentence	§1.367(a)–8T(a)(3)	§1.367(a)–8(d)(3) and (e)(1)(i)
1.367(a)–3(d)(3), *Example 1A*(ii), second sentence	§1.367(a)–8T(d)(4)	§1.367(a)–8(j)(5)
1.367(a)–3(d)(3), *Example 1A*(ii), second sentence	§1.367(a)–8T(e)(8)	§1.367(a)–8(k)(10)
1.367(a)–3(d)(3), *Example 4*(i), first sentence	§1.367(a)–8T(d)(2)	§1.367(a)–8(j)(2)(i)
1.367(a)–3(d)(3), *Example 4*(ii), first sentence	§1.367(a)–8T(d)(2)	§1.367(a)–8(j)(2)
1.367(a)–3(d)(3), *Example 4*(ii), second sentence	§1.367(a)–8T(g)(2)	§1.367(a)–8(o)(4)
1.367(a)–3(d)(3), *Example 5A*(ii), second to last sentence	§1.367(a)–8T(g)(2)	§1.367(a)–8(o)(4)
1.367(a)–3(d)(3), *Example 6*(ii), last sentence	§1.367(a)–8T(d)(2)	§1.367(a)–8(j)(2)(i)
1.367(a)–3(d)(3), *Example 7*(ii), second sentence	§1.367(a)–8T(g)(2)	§1.367(a)–8(o)(4)
1.367(a)–3(d)(3), *Example 7*(ii), third sentence	§1.367(a)–8T(e)(1)(iii)	§1.367(a)–8(k)(4)
1.367(a)–3(d)(3), *Example 7A*(ii), fourth sentence	§1.367(a)–8T(g)(2)	§1.367(a)–8(o)(4)
1.367(a)–3(d)(3), *Example 7A*(ii), last sentence	§1.367(a)–8T(b)(5)	§1.367(a)–8(g)

Section	Remove	Add
1.367(a)–3(d)(3), *Example 7A*(ii), last sentence	§1.367(a)–8T(e)(1)(iii)	§1.367(a)–8(k)(4)
1.367(a)–3(d)(3), *Example 8*(ii), second to last sentence	§1.367(a)–8T(d)(2)	§1.367(a)–8(j)(2)(i)
1.367(a)–3(d)(3), *Example 9*(ii), last sentence	§1.367(a)–8T(d)(2)	§1.367(a)–8(j)(2)(i)
1.367(a)–3(d)(3), *Example 11*(ii), sixth sentence	§1.367(a)–8T(d)(1)	§1.367(a)–8(j)(1)
1.367(a)–3(d)(3), *Example 11*(ii), sixth sentence	§1.367(a)–8T(b)(1)(vii)	§1.367(a)–8(c)(2)(vi)
1.367(a)–3(d)(3), *Example 12*(ii), third sentence	§1.367(a)–3T(e)	§1.367(a)–3(e)
1.367(b)–4(b)(1)(iii), *Example 4*(i), last sentence	§1.367(a)–3T(e)	§1.367(a)–3(e)
1.367(b)–13(a)(2)(iii)	or (iii) or in sections 368(a)(1)(G) and (a)(2)(D)	(iii), or (v)

Par. 4. For each entry in the table, redesignate the paragraph designated in the "Old Paragraph" column as the new paragraph designation in the "New Paragraph" column to read as follows:

§1.367(a)–3(g) [Redesignated]

Section 1.367(a)–3(g) is redesignated as follows:

Old Paragraph	New Paragraph
1.367(a)–3(g)(1)(A)	1.367(a)–3(g)(1)(i)
1.367(a)–3(g)(1)(B)	1.367(a)–3(g)(1)(ii)
1.367(a)–3(g)(1)(B)(*1*)	1.367(a)–3(g)(1)(ii)(A)
1.367(a)–3(g)(1)(B)(*2*)	1.367(a)–3(g)(1)(ii)(B)
1.367(a)–3(g)(1)(B)(*3*)	1.367(a)–3(g)(1)(ii)(C)
1.367(a)–3(g)(1)(B)(*4*)	1.367(a)–3(g)(1)(ii)(D)
1.367(a)–3(g)(1)(B)(*5*)	1.367(a)–3(g)(1)(ii)(E)
1.367(a)–3(g)(1)(B)(*6*)	1.367(a)–3(g)(1)(ii)(F)
1.367(a)–3(g)(1)(C)	1.367(a)–3(g)(1)(iii)
1.367(a)–3(g)(1)(D)	1.367(a)–3(g)(1)(iv)
1.367(a)–3(g)(1)(D)(*1*)	1.367(a)–3(g)(1)(iv)(A)
1.367(a)–3(g)(1)(D)(*2*)	1.367(a)–3(g)(1)(iv)(B)
1.367(a)–3(g)(1)(D)(*3*)	1.367(a)–3(g)(1)(iv)(C)
1.367(a)–3(g)(1)(E)	1.367(a)–3(g)(1)(v)
1.367(a)–3(g)(1)(F)	1.367(a)–3(g)(1)(vi)
1.367(a)–3(g)(2)(G)	1.367(a)–3(g)(1)(vii)

Par. 5. Section 1.367(a)–3 is amended by:

1. In the first sentence of paragraph (b)(1), remove the words "Except as provided in section 367(a)(5)" and add "Except as provided in section 367(a)(5) and paragraph (e) of this section" in their place.
2. In the first sentence of paragraph (c)(1), remove the words "Except as provided in section 367(a)(5)" and add "Except as provided in section 367(a)(5) and paragraph (e) of this section" in their place.
3. Revising paragraphs (d)(2)(iv).
4. Revising the last sentence of paragraph (d)(3), *Example 5*(ii).

5. Removing the last sentence of paragraph (d)(3), *Example 5A*(ii).

6. Revising paragraph (e).

7. Revising and reserving paragraph (f).

8. Revising the heading for paragraph (g) and adding new paragraph (g)(1)(viii).

The revisions and addition read as follows:

§1.367(a)–3 Treatment of transfers of stock or securities to foreign corporations.

* * * * *

(d) * * *

(2) * * *

(iv) *Gain recognition agreements involving multiple parties.* The U.S. person's agreement to recognize gain, as provided in §1.367(a)–8, shall include appropriate provisions consistent with the principles of §1.367(a)–8. See *Examples 5* and *5A* of this section and §1.367(a)–8(j)(9).

* * * * *

(3) * * *

Example 5. * * *

(ii) * * * Under §1.367(a)–8(j)(9), the gain recognition agreement would be triggered if F sold all or a portion of the stock of S.

* * * * *

(e) *Transfers by a domestic corporation to a foreign corporation in a section 361 exchange*—(1) *General rule*. If a domestic corporation (U.S. transferor) transfers stock or securities to a foreign corporation (transferee foreign corporation) in an exchange described in section 361(a) or (b), or in an exchange described in section 351 that is also described in section 361(a) or (b) (collectively, a section 361 exchange), such transfer shall be subject to section 367(a)(1), unless the conditions of paragraphs (e)(1)(i) through (iv) of this section are satisfied.

(i) The conditions set forth in section 367(a)(5) and any regulations under that section have been satisfied including that:

(A) The U.S. transferor is controlled (within the meaning of section 368(c)) by five or fewer (but at least one) domestic corporations (control group members) at the time of the section 361 exchange;

(B) The U.S. transferor recognizes the amount of the gain realized in the section 361 exchange that is allocable to any shareholder that is not a control group member (based on the value of the ownership interest in the U.S. transferor held by the shareholder at the time of the section 361 exchange);

(C) The U.S. transferor recognizes the amount of the gain realized in the section 361 exchange allocable to a control group member that cannot be preserved in the stock received by the control group member in the transaction; and

(D) Appropriate adjustments are made to the basis of the stock received by each control group member in the transaction.

(ii) If the stock or securities transferred in the section 361 exchange are of a domestic corporation, the conditions in paragraphs (c)(1)(i), (ii), and (iv) of this section are satisfied.

(iii) Each control group member that owns five percent or more (applying the attribution rules of section 318, as modified by section 958(b)) of the total voting power or the total fair market value of the stock of the transferee foreign corporation immediately after the transaction enters into a gain recognition agreement as provided in §1.367(a)–8. The amount of gain subject to the gain recognition agreement shall equal the amount of the gain realized by the U.S. transferor on the transfer of the stock or securities in the section 361 exchange that is allocable to such control group member (based on the ownership interest (by value) in the U.S. transferor held by the control group member at the time of the section 361 exchange) reduced by the amount of such allocable gain that is recognized by the U.S. transferor with respect to the control group member. The gain recognition agreement shall designate the control group member as the U.S. transferor for purposes of paragraphs (b) and (c) of this section and §1.367(a)–8.

(iv) Each control group member that enters into a gain recognition agreement pursuant to paragraph (e)(1)(iii) of this section makes the election described in §1.367(a)–8(c)(2)(vi).

(2) *Certain triangular asset reorganizations*. If a transfer of stock or securities described in paragraph (e)(1) of this section is pursuant to a triangular asset reorganization described in §1.358–6(b)(2)(i) through (iii), the gain recognition agreement filed by a control group member pursuant to paragraph (e)(1)(iii) of this section shall include provisions consistent with the principles of §1.367(a)–8 to account for all the parties to the reorganization. See §1.367(a)–8(j)(9).

(3) *Examples*. The following examples illustrate the provisions of paragraph (e)(1) of this section. Except as otherwise indicated, assume US1, US2, USP, and UST are domestic corporations; US1 and US2 are not related; CFC1, CFC2, FA, and FC are foreign corporations; the section 1248 amount attributable to the stock of a foreign corporation is zero; and section 7874 does not apply to the transaction.

Example 1. Outbound asset reorganization. (i) *Facts*. US1 and US2 own 60% and 40%, respectively, of the outstanding stock of UST. UST wholly owns FC. The FC stock held by UST has a $20x basis and a $100x fair market value. UST merges with and into FC in an asset reorganization described in section 368(a)(1)(A). In the section 361 exchange that is part of the reorganization, UST transfers all of its FC stock to FA. UST distributes the FA stock it received in the section 361 exchange to US1 and US2 pursuant to the plan of reorganization. The conditions set forth in the second sentence of section 367(a)(5) and the regulations under that section are satisfied, including adjusting the basis of the FA stock received by US1 and US2 in the reorganization, as appropriate. After the reorganization, US1 and US2 own 6% and 4%, respectively, of the outstanding stock of FA.

(ii) *Result*. If the conditions of paragraph (e)(1)(i) through (iv) of this section are satisfied, the transfer of the FC stock by UST to FA in the section 361 exchange is not subject to section 367(a)(1). Because US1 and US2 complied with the requirements of section 367(a)(5), the requirement of paragraph (e)(1)(i) of this section is satisfied. Paragraph (e)(1)(ii) of this section is not applicable because FC is a foreign corporation. Pursuant to paragraph (e)(1)(iii) of this section, US1 enters into a gain recognition agreement with respect to its share of the gain realized by UST on the transfer of the FC stock to FA in the section 361 exchange ($48x, or 60% of $80x). The amount of gain subject to the gain recognition agreement is $48x because UST did not recognize any amount of such gain under section 367(a)(5) or the regulations under that section with respect to US1. US1 is designated as the U.S. transferor on the gain recognition agreement for purposes of paragraph (b) of this section and §1.367(a)–8. US1 makes the election described in §1.367(a)–8(c)(2)(vi) with respect to the gain recognition agreement. Because US2 owns less than 5% of the stock of FA after the reorganization, US2 is not required to enter into a gain recognition agreement with respect to its share of the gain realized by UST on the transfer of the FC stock to FA in the section 361 exchange.

(iii) *Alternate facts*. The facts are the same as in paragraph (i) of this *Example*, except that, in year 4, FA disposes of 25% of the FC stock in a taxable exchange. Under §1.367(a)–8(c)(1)(i) and (j)(1), the partial disposition of the FC stock requires US1 to include in income 25% of the gain subject to the gain recognition agreement filed in year 1 ($12x, or 25% of $48x) and pay applicable interest on any additional tax due on such inclusion.

(iv) *Alternate facts*. The facts are the same as in paragraph (iii) of this *Example*, except that US1 and US2 are members of a consolidated group of which USP is the common parent. Because US2 is considered to own at least 5% of the stock of FA following the reorganization by reason of the attribution rules of section 318, as modified by section 958(b), a gain recognition agreement must also be entered into on behalf of US2 with respect to the amount of the gain realized but not recognized by UST on the transfer of the FC stock to FA that is allocable to US2 ($32x, or 40% of $80x). Under §1.367(a)–8(d)(3) and §1.1502–77(a)(1), USP enters into the gain recognition agreements on behalf of US1 and US2. In year 4, US1 and US2 must include in income 25% of the amount of gain subject to their respective gain recognition agreement ($12x for US1 and $8x for US2) and pay applicable interest on any additional tax due on such inclusion.

Example 2. *Divisive reorganization*. (i) *Facts*. US1 wholly owns UST. The UST stock has a $120x basis and $150x fair market value. UST wholly owns CFC2. The CFC2 stock has a $20x basis and a $50x fair market value. UST also owns Business A that has a fair market value of $100x. In a divisive reorganization that satisfies the requirements of section 368(a)(1)(D), UST transfers the CFC2 stock to CFC1, a newly-formed corporation, in exchange solely for CFC1 stock. The transfer of the CFC2 stock to CFC1 is a section 361 exchange. UST then distributes the CFC1 stock to US1 in a transaction that qualifies under section 355. Under section 358, the pre-exchange basis in the UST stock ($120x) is allocated between the UST stock and the CFC1 stock based on the relative fair market values of such stock. Therefore, immediately after the transaction, the basis of the UST stock is $80x ($120x multiplied by $100x/$150x), and the basis of the CFC1 stock is $40x ($120x multiplied by $50x/$150x). The conditions set forth in section 367(a)(5) and the regulations under that section are satisfied, including reducing the basis of the CFC1 stock received by US1 in the transaction by $20x so that the $30x built-in gain in the CFC2 stock transferred in the section 361 exchange is preserved in the CFC1 stock received by US1 in the transaction.

(ii) *Result*. Because US1 complied with the requirements of section 367(a)(5) and regulations under that section, the requirement of paragraph (e)(1)(i) of this section is satisfied. Paragraph (e)(1)(ii) of this section is not applicable because CFC2 is a foreign corporation. Pursuant to paragraph (e)(1)(iii) of this section, US1 enters into a gain recognition agreement with respect to its share of the gain realized by UST on the transfer of the CFC2 stock to CFC1 in the section 361 exchange ($30x). The amount of gain subject to the gain recognition agreement is $30x because UST did not recognize any amount of such gain under section 367(a)(5) or the regulations under that section with respect to US1. US1 is designated as the U.S. transferor on the gain recognition agreement for purposes of paragraph (b) of this section and §1.367(a)–8. US1 makes the election described in §1.367(a)–8(c)(2)(vi) with respect to the gain recognition agreement.

(4) *Cross-references*. For other examples that illustrate the application of this paragraph (e), see §1.367(a)–8(q)(2), *Examples 6* and *24*. For rules relating to an acquisition of the stock of a foreign corporation by another foreign corporation in a section 361 exchange, see §1.367(b)–4(b)(1)(iii), *Example 4*. For rules relating to certain distributions of stock of a foreign corporation by a domestic corporation, see section 1248(f) and the regulations under that section.

(f) [Reserved].

(g) *Effective/applicability date* (1) * * *

(viii)(A) Except as provided in this paragraph (g)(1)(viii), the rules of paragraph (e) of this section apply to transfers of stock or securities occurring on or after March 13, 2009. For matters covered in this section for periods before March 13, 2009 but on or after March 7, 2007, the rules of §1.367(a)–3T(e) (see 26 CFR part 1, revised April 1, 2007) apply. For matters covered in this section for periods before March 7, 2007, but on or after July 20, 1998, the rule of §1.367(a)–8(f)(2)(i) (see 26 CFR part 1, revised April 1, 2006) applies.

(B) Taxpayers may apply the rules of §1.367(a)–3(e) to transfers occurring before March 13, 2009 and during a taxable year for which the period of limitations on assessments under section 6501(a) has not closed, if done consistently to all such transfers occurring during each taxable year. A taxpayer applies the rules of §1.367(a)–3(e) to transfers occurring before March 13, 2009 and during a taxable year for which the period of limitations on assessments under section 6501(a) has not closed, by including the gain recognition agreement, annual certification, or other information filing, that is required as a result of the rules of §1.367(a)–3(e) applying to such a transfer, with an amended tax return for the taxable year in which the transfer occurs that is filed on or before August 10, 2009. A taxpayer that wishes to apply the rules of §1.367(a)–3(e) to transfers occurring before March 13, 2009 and during a taxable year for which the period of limitations on assessments under section 6501(a) has not closed but that fails to meet the filing requirement described in the preceding sentence must request relief for reasonable cause for such failure as provided in §1.367(a)–8.

* * * * *

§1.367(a)–3T [Removed]

Par. 6. Section 1.367(a)–3T is removed.

Par. 7. Section 1.367(a)–8 is revised to read as follows:

§1.367(a)–8 Gain recognition agreement requirements.

(a) *Scope*. This section provides the terms and conditions for a gain recognition agreement entered into by a United States person pursuant to §1.367(a)–3(b) through (e) in connection with a transfer of stock or securities to a foreign corporation pursuant to an exchange that would otherwise be subject to section 367(a)(1). Paragraph (b) of this section provides definitions and special rules. Paragraphs (c) through (h) of this section identify the form, content, and other conditions of a gain recognition agreement. Paragraph (i) of this section is reserved. Paragraph (j) of this section identifies certain events that may require gain to be recognized under a gain recognition agreement. Paragraph (k) of this section provides exceptions for certain events that would otherwise require gain to be recognized under a gain recognition agreement. Paragraph (l) of this section is reserved. Paragraph (m) of this section provides rules that require gain to be recognized under a gain recognition agreement in connection with certain events to which an exception under paragraph (k) of this section otherwise applies. Paragraph (n) of this section provides special rules in the case of a distribution of property with respect to stock to which section 301 applies. Paragraph (o) of this section provides rules for certain transactions that terminate or reduce the amount of gain subject to a gain recognition agreement. Paragraph (p) of this section provides relief for reasonable cause for certain failures to comply with the requirements of this section. Paragraph (q) of this section provides examples that illustrate the rules of the section. Paragraph (r) of this section provides effective dates for the provisions of this section.

(b) *Definitions and special rules*. The following definitions and special rules apply for purposes of this section.

(1) *Definitions*—(i) *Asset reorganization*—(A) *General rule*. Except as provided in paragraph (b)(1)(i)(B) of this section, an *asset reorganization* is a reorganization described in section 368(a)(1) that involves an exchange of property described in section 361(a) or (b) (a section 361 exchange).

(B) *Exceptions*. An asset reorganization does not include the following:

(*1*) A reorganization described in section 368(a)(1)(D) or (G) if the requirements of section 354(b)(1)(A) and (B) are not met.

(*2*) For purposes of paragraphs (j)(2)(ii)(B), (k)(6)(ii), and (k)(6)(iii) of this section, a triangular asset reorganization. For rules applicable to a triangular asset reorganization, see paragraph (k)(7) of this section.

(ii) A *consolidated group* has the meaning set forth in §1.1502–1(h).

(iii) *Disposition*. Except as provided in this paragraph (b)(1)(iii), a *disposition* includes any transfer that would constitute a disposition for any purpose of the Internal Revenue Code. A disposition includes an indirect disposition of the stock of the transferred corporation as described in §1.367(a)–3(d). Except as provided in paragraph (n)(1) of this section, a disposition does not include the receipt of a distribution of property with respect to stock to which section 301 applies (including by reason of section 302(d)). See paragraphs (n)(2) and (o)(3) of this section for rules that apply if gain is recognized under section 301(c)(3). A complete or partial disposition by installment sale (under section 453) shall be treated as a disposition in the year of the installment sale.

(iv) A *gain recognition event* is an event described in paragraphs (j) through (o) of this section that requires gain to be recognized under a gain recognition agreement.

(v) The *initial transfer* means a transfer of stock or securities (transferred stock or securities) to a foreign corporation pursuant to an exchange that would otherwise be subject to section 367(a)(1) but with respect to which a gain recognition agreement is entered into by a United States person pursuant to §1.367(a)–3(b) through (e).

(vi) An *intercompany item* has the meaning set forth in §1.1502–13(b)(2).

(vii) An *intercompany transaction* has the meaning set forth in §1.1502–13(b)(1).

(viii) A *nonrecognition transaction* has the meaning set forth in section 7701(a)(45). In addition, a nonrecognition transaction includes an exchange described in section 351(b) or 356 even if all gain realized in the exchange is recognized.

(ix) The terms *P*, *S*, and *T* have the meanings set forth in §1.358–6(b)(1)(i), (ii), and (iii), respectively.

(x) The determination of whether *substantially all* of the assets of the transferred corporation have been disposed of is based on all the facts and circumstances.

(xi) A *timely-filed return* is a Federal income tax return filed by the due date set forth in section 6072(a) or (b), plus any extension of time to file such return granted under section 6081.

(xii) *Transferee foreign corporation*. Except as provided in this paragraph (b)(1)(xii), the *transferee foreign corporation* is the foreign corporation to which the transferred stock or securities are transferred in the initial transfer. In the case of an indirect stock transfer, the transferee foreign corporation has the meaning set forth in §1.367(a)–3(d)(2)(i). The transferee foreign corporation also includes a corporation designated as the transferee foreign corporation in the case of a new gain recognition agreement entered into under this section.

(xiii) *Transferred corporation*. Except as provided in this paragraph (b)(1)(xiii), the *transferred corporation* is the corporation the stock or securities of which are transferred in the initial transfer. In the case of an indirect stock transfer, the transferred corporation has the meaning set forth in §1.367(a)–3(d)(2)(ii). The transferred corporation also includes a corporation designated as the transferred corporation in the case of a new gain recognition agreement entered into under this section.

(xiv) A *triangular asset reorganization* is a reorganization described in §1.358–6(b)(2)(i), (ii), (iii), or (v).

(xv) The *U.S. transferor* is the United States person (as defined in §1.367(a)–1T(d)(1)) that transfers the transferred stock or securities to the transferee foreign corporation in the initial transfer. For purposes of determining the U.S. transferor in the case of a transfer by a partnership, see §1.367(a)–1T(c)(3)(i). The *U.S. transferor* also includes the United States person designated as the U.S. transferor in the case of a new gain recognition agreement entered into under this section including, for example, under paragraph (k)(14) of this section.

(2) *Special rules*—(i) *Stock deemed received or transferred*. References to stock received include stock deemed received (for example, pursuant to section 367(c)(2)). References to a transfer of stock or securities include a deemed transfer of stock or securities.

(ii) *Stock of the transferee foreign corporation*. References to stock of the transferee foreign corporation includes any stock of the transferee foreign corporation the basis of which is determined, in whole or in part, by reference to the basis of the stock of the transferee foreign corporation received by the U.S. transferor in the initial transfer.

(iii) *Transferred stock or securities*. References to transferred stock or securities includes any stock or securities of the transferred corporation the basis of which is determined, in whole or in part, by reference to the basis of the stock or securities transferred in the initial transfer.

(c) *Gain recognition agreement*—(1) *Terms of agreement*—(i) *General rule*. Except as provided in this paragraph (c)(1)(i), if a gain recognition event occurs during the period beginning on the date of the initial transfer and ending as of the close of the fifth full taxable year (not less than 60 months) following the close of the taxable year in which the initial transfer occurs (GRA term), the U.S. transferor must include in income the gain realized but not recognized on the initial transfer by reason of entering into the gain recognition agreement. In the case of a gain recognition event that occurs as a result of a partial disposition of stock, securities, or a partnership interest, as applicable, the U.S. transferor is required to recognize a proportionate amount of the gain subject to the gain recognition agreement, determined based on the fair market value of the stock, securities, or partnership interest, as applicable, disposed of (measured at the time of the partial disposition) as compared to the fair market value of all the stock, securities, or partnership interest, as applicable (measured at the time of the partial disposition). If the U.S. transferor must recognize gain under this paragraph as a result of an event described in paragraph (m) or (n) of this section, see those paragraphs to determine the amount of the gain that must be recognized. The amount of gain subject to the gain recognition agreement shall be reduced by the amount of gain recognized under this paragraph. If the amount of gain subject to the gain recognition agreement is reduced to zero, the gain recognition agreement shall terminate without further effect.

(ii) *Ordering rule for gain recognized under multiple gain recognition agreements*. If a gain recognition event occurs that requires gain to be recognized under multiple gain recognition agreements, gain shall first be recognized under the gain recognition agreement that relates to the earliest initial transfer, then under the gain recognition agreement that relates to the immediately following initial transfer and so forth until the appropriate amount of gain has been recognized under each gain recognition agreement. The amount of gain recognized under a gain recognition agreement shall be determined after taking into account, as appropriate, any increase to basis (including the basis of the transferred stock or securities) under paragraph (c)(4) of this section resulting from gain recognized under another gain recognition agreement. For an illustration of this ordering rule, see paragraph (q)(2) of this section, *Example 6*.

(iii) *Taxable year in which gain is reported*—(A) *Year of initial transfer*. Except as provided in paragraph (c)(1)(iii)(B) of this section, the U.S. transferor must report any gain recognized under paragraph (c)(1)(i) of this section on an amended Federal income tax return for the taxable year of the initial transfer. The amended return must be filed on or before the 90th day following the date on which the gain recognition event occurs.

(B) *Year of gain recognition event*. If an election under paragraph (c)(2)(vi) of this section is made with the gain recognition agreement or if paragraph (c)(5)(ii) of this section applies to the gain recognition agreement, the U.S. transferor must report any gain recognized under paragraph (c)(1)(i) of this section on its Federal income tax return for the taxable year during which the gain recognition event occurs. If an election under paragraph (c)(2)(vi) of this section is made with the gain recognition agreement or if paragraph (c)(5)(ii) of this section applies to the gain recognition agreement but the U.S. transferor does not report the gain recognized on its Federal income tax return for the taxable year during which the gain recognition event occurs, the Commissioner may require the U.S. transferor to report the gain on an amended Federal income tax return for the taxable year during which the initial transfer occurred.

(iv) *Offsets*. No special limitations apply with respect to offsetting gain recognized under paragraph (c)(1)(i) of this section with net operating losses, capital losses, credits against tax, or similar items.

(v) *Payment and reporting of interest*. Interest must be paid on any additional tax due with respect to gain recognized by the U.S. transferor under paragraph (c)(1)(i) of this section. Any interest due shall be determined based on the rates under section 6621 for the period between the date that was prescribed for filing the Federal income tax return of the U.S. transferor for the year of the initial transfer and the date on which the additional tax due is paid. If paragraph (c)(1)(iii)(B) of this section applies, any interest due must be included with the payment of tax due with the Federal income tax return of the U.S. transferor for the taxable year during which the gain recognition event occurs (or should reduce the amount of any refund due to the U.S. transferor for such taxable year). A schedule entitled "Calculation of Section 367 Tax and Interest" that separately identifies and calculates any additional tax and interest due must be included with the Federal income tax return on which any interest due is reported.

(2) *Content of gain recognition agreement*. The gain recognition agreement must be entitled "GAIN RECOGNITION AGREEMENT UNDER §1.367(a)–8" and include the information described in paragraphs (c)(2)(i) through (viii) of this paragraph with the corresponding paragraph numbers. The information required under this paragraph (c)(2) and paragraph (c)(3) of this section must be included in the gain recognition agreement as filed.

(i) A statement that the document constitutes an agreement by the U.S. transferor to recognize gain in accordance with the requirements of this section.

(ii) A description of the transferred stock or securities and other information as required in paragraph (c)(3) of this section.

(iii) A statement that the U.S. transferor agrees to comply with all the conditions and requirements of this section, including to recognize gain under the gain recognition agreement in accordance with paragraph (c)(1)(i) of this section, extend the statute of limitations on assessments of tax as provided in paragraph (f) of this section, and file the certification described in paragraph (g) of this section.

(iv) A statement that arrangements have been made to ensure that the U.S. transferor is informed of any events that affect the gain recognition agreement, including triggering events or other gain recognition events.

(v) In the case of a new gain recognition agreement filed under this section—

(A) A description of the event (such as a triggering event) and the applicable exception, if any, that gave rise to the new gain recognition agreement (such as a triggering event exception), including the date of the event and the name, address, and taxpayer identification number (if any) of each person that is a party to the event;

(B) As applicable, a description of the class, amount, and characteristics of the stock, securities or partnership interest received in the transaction; and

(C) As applicable, a calculation of the amount of gain that remains subject to the new gain recognition agreement as a result of the application of paragraph (m), (n), or (o) of this section.

(vi) A statement whether the U.S. transferor elects to include in income any gain recognized under paragraph (c)(1)(i) of this section in the taxable year during which a gain recognition event occurs. See paragraph (c)(5)(ii) of this section for a rule that requires, in certain cases, for the gain recognized pursuant to a new gain recognition agreement to be included in income during the taxable year in which the gain recognition event occurs.

(vii) A statement whether a gain recognition event has occurred during the taxable year of the initial transfer.

(viii) A statement describing any disposition of assets of the transferred corporation during such taxable year other than in the ordinary course of business.

(3) *Description of transferred stock or securities and other information*. The gain recognition agreement shall include the following:

(i) A description of the transferred stock or securities including—

(A) The type or class, amount, and characteristics of the transferred stock or securities;

(B) A calculation of the amount of the built-in gain in the transferred stock or securities that are subject to the gain recognition agreement, reflecting the basis and fair market value on the date of the initial transfer;

(C) The amount of any gain recognized by the U.S. transferor on the initial transfer; and

(D) The percentage (by voting power and value) that the transferred stock (if any) represents of the total stock outstanding of the transferred corporation on the date of the initial transfer.

(ii) The name, address, place of incorporation, and taxpayer identification number (if any) of the transferred corporation.

(iii) The date on which the U.S. transferor acquired the transferred stock or securities.

(iv) The name, address and place of incorporation of the transferee foreign corporation, and a description of the stock or securities received by the U.S. transferor in the initial transfer, including the percentage of stock (by vote and value) of the transferee foreign corporation received in such exchange.

(v) If the initial transfer is described in §1.367(a)–3(e), a statement that the conditions of section 367(a)(5) and any regulations under that section have been satisfied, and a description of any adjustments to the basis of the stock received in the transaction or other adjustments made pursuant to section 367(a)(5) and any regulations under that section.

(vi) If the transferred corporation is domestic, a statement describing the application of section 7874 to the transaction, and indicating that the requirements of §1.367(a)–3(c)(1) are satisfied.

(vii) If the transferred corporation is foreign, a statement indicating whether the U.S. transferor was a section 1248 shareholder (as defined in §1.367(b)–2(b)) of the transferred corporation immediately before the initial transfer, and whether the U.S. transferor is a section 1248 shareholder with respect to the transferee foreign corporation immediately after the initial transfer, and whether any reporting requirements or other rules contained in regulations under section 367(b) are applicable, and, if so, whether they have been satisfied.

(viii) If the initial transfer involves a transfer by a partnership (see §1.367(a)–1T(c)(3)(i)) or a transfer of a partnership interest (see section 367(a)(4) and §1.367(a)–1T(c)(3)(ii)) a complete description of the transfer, including a description of the partners in the partnership.

(ix) If the transaction involved the transfer of property other than the transferred stock or securities and the transaction was subject to the indirect stock transfer rules of §1.367(a)–3(d), a statement indicating whether—

(A) The reporting requirements under section 6038B have been satisfied with respect to the transfer of such other property;

(B) Whether gain was recognized under section 367(a)(1);

(C) Whether section 367(d) applied to the transfer of such property; and

(D) Whether the other property transferred qualified for the active foreign trade or business exception under section 367(a)(3).

(4) *Basis adjustments for gain recognized.* The following basis adjustments shall be made if gain is recognized under paragraph (c)(1)(i) of this section.

(i) *Stock or securities of transferee foreign corporation.* The basis of the stock or securities, as applicable, of the transferee foreign corporation received by the U.S. transferor in the initial transfer shall be increased as of the date of the initial transfer by the amount of gain recognized.

(ii) *Transferred stock or securities.* The basis of the transferred stock or securities shall be increased as of the date of the initial transfer by the amount of the gain recognized.

(iii) *Other appropriate adjustments.* The basis of other stock, securities, or a partnership interest shall be increased, as appropriate, in accordance with the principles of this paragraph (c)(4). Under no circumstances shall the basis of stock, securities, or of a partnership interest held by a U.S. person that does not recognize gain under paragraph (c)(1)(i) of this section be increased under this paragraph (c)(4). In addition, under no circumstances shall the basis of any property be increased by the amount of any additional tax due or interest paid with respect to such tax, nor shall the basis of the assets of the transferred corporation be increased as a result of gain recognized by the U.S. transferor under paragraph (c)(1)(i) of this section.

(iv) *Cross-reference.* See paragraph (q)(2) of this section, *Examples 1*, *2*, *3*, and *5* for illustrations of the rules of this paragraph (c)(4). See also §1.367(a)–1T(b)(4) for rules that determine the increase to basis of property resulting from the application of section 367(a).

(5) *Terms and conditions of a new gain recognition agreement*—(i) *General rule.* A new gain recognition agreement entered into pursuant to this section shall replace the existing gain recognition agreement, which shall terminate without further effect. The term of the new gain recognition agreement shall be the remaining term of the existing gain recognition agreement. The amount of gain subject to the new gain recognition agreement shall equal the amount of gain subject to the existing gain recognition agreement, reduced by any gain recognized under paragraph (c)(1)(i) of this section with respect to the existing gain recognition agreement by reason of the gain recognition event that gives rise to the new gain recognition agreement. The new gain recognition agreement shall, as applicable, be subject to the conditions and requirements of this section to the same extent as the existing gain recognition agreement. For example, a triggering event with respect to the new gain recognition agreement will generally include a disposition of the transferred stock or securities or of substantially all the assets of the transferred corporation. If, however, the transferred stock is canceled or redeemed pursuant to the disposition or other event that gives rise to the new gain recognition agreement (for example, pursuant to a liquidation where the transferee foreign corporation is the corporate distributee (within the meaning of section 334(b)(2)), or an asset reorganization where the transferee foreign corporation is the acquiring corporation) the transferred stock is not subject to the new gain recognition agreement.

(ii) *Special rule for inclusion of gain.* If the U.S. transferor with respect to the new gain recognition agreement is not the U.S. transferor with respect to the existing gain recognition agreement, or a member of the consolidated group of which the U.S. transferor with respect to the existing gain recognition agreement was a member on the date of the initial transfer, then any gain recognized under paragraph (c)(1)(i) of this section with respect to the new gain recognition agreement must be included in income in the taxable year during which the gain recognition event occurs.

(d) *Filing requirements*—(1) *General rule.* A gain recognition agreement entered into with respect to an initial transfer must be included with the timely-filed return of the U.S. transferor for the taxable year during which the initial transfer occurs.

(2) *Special requirements*—(i) *New gain recognition agreement*. A new gain recognition agreement entered into under this section must be included with the timely-filed return of the U.S. transferor (as identified in the new gain recognition agreement) for the taxable year during which the disposition or event that requires the new gain recognition agreement occurs. If the new gain recognition agreement is entered into by the U.S. transferor that entered into the existing gain recognition agreement, the new gain recognition agreement is in lieu of the annual certification otherwise required for such taxable year under paragraph (g) of this section with respect to the existing gain recognition agreement.

(ii) *Multiple events within a taxable year*. Except as otherwise provided in this paragraph (d)(2)(ii), if the initial transfer and one or more dispositions or other events (even if a triggering event exception applies) that affect the gain recognition agreement entered into by the U.S. transferor with respect to the initial transfer occur within the same taxable year of such U.S. transferor, or if multiple dispositions or other events occur in a taxable year of the U.S. transferor that does not include the initial transfer, only one gain recognition agreement is required to be entered into and included with the timely-filed return of the U.S. transferor for such taxable year. The gain recognition agreement must describe the initial transfer and/or each disposition or other event that affects the gain recognition agreement (even if a triggering event exception applies). This paragraph does not apply, however, if any such disposition or other event requires a new gain recognition agreement to be entered into by a United States person other than the U.S. transferor with respect to the initial transfer or that entered into the existing gain recognition agreement, as applicable.

(3) *Common parent as agent for U.S. transferor*. If the U.S. transferor is a member but not the common parent of a consolidated group, the common parent of the consolidated group is the agent for the U.S. transferor under §1.1502–77(a)(1). Thus, the common parent must file the gain recognition agreement on behalf of the U.S. transferor. References in this section to the timely-filed return of the U.S. transferor include the timely-filed return of the consolidated group of which the U.S. transferor is a member, as applicable.

(e) *Signatory*—(1) *General rule*. The gain recognition agreement must be signed under penalties of perjury by an agent of the U.S. transferor that is authorized to sign under a general or specific power of attorney, or by the appropriate party based on the category of the U.S. transferor described in this paragraph (e)(1).

(i) If the U.S. transferor is a corporation but not a member of a consolidated group, a responsible officer of the U.S. transferor. If the U.S. transferor is a member of a consolidated group, a responsible officer of the common parent of the consolidated group.

(ii) If the U.S. transferor is an individual, the individual.

(iii) If the U.S. transferor is a trust or estate, a trustee, executor, or equivalent fiduciary of the U.S. transferor.

(iv) In a bankruptcy case under Title 11, United States Code, a debtor in possession or trustee.

(2) *Signature requirement*. The inclusion of an unsigned copy of the gain recognition agreement with the timely-filed return of the U.S. transferor shall satisfy the signature requirement of paragraph (e)(1) of this section if the U.S. transferor retains the original signed gain recognition agreement in the manner specified by §1.6001–1(e).

(f) *Extension of period of limitations on assessments of tax*—(1) *General rule*. In connection with the filing of a gain recognition agreement, the U.S. transferor must extend the period of limitations on assessments of tax with respect to the gain realized but not recognized on the initial transfer through the close of the eighth full taxable year following the taxable year during which the initial transfer occurs. The U.S. transferor extends the period of limitations by filing Form 8838 *"Consent to Extend the Time to Assess Tax Under Section 367—Gain Recognition Agreement."* The Form 8838 must be signed by a person authorized to sign the gain recognition agreement under paragraph (e)(1) of this section.

(2) *New gain recognition agreement*. If a new gain recognition agreement is entered into under this section, the U.S. transferor must extend the period of limitations on assessments of tax on the initial transfer through the close of the eighth full taxable year following the taxable year during which the initial transfer occurs, consistent with paragraph (f)(1) of this section, unless the U.S. transferor with respect to the new gain recognition agreement is the U.S. transferor with respect to the existing gain recognition agreement, or a member of the consolidated group of which the U.S. transferor with respect to the existing gain recognition agreement was a member on the date of the initial transfer.

(g) *Annual certification*. Except as provided in paragraph (d)(2)(i) of this section, the U.S. transferor must include with its timely-filed return for each of the five full taxable years following the taxable year of the initial transfer a certification (annual certification) that includes the information described in paragraphs (g)(1) through (3) of this section, as appropriate. The annual certification must be signed by a person authorized under paragraph (e)(1) of this section to sign the gain recognition agreement for the initial transfer. The inclusion of an unsigned copy of the annual certification with the relevant timely-filed return of the U.S. transferor shall satisfy the signature requirement of paragraph (e)(1) of this section provided the U.S. transferor retains the original signed certification in the manner specified by §1.6001–1(e).

(1) A statement of whether a gain recognition event has or has not occurred during such taxable year. If a gain recognition event has occurred during such taxable year, the annual certification must state:

(i) The amount of gain subject to the gain recognition agreement at the time of the gain recognition event;

(ii) The amount of gain recognized under the gain recognition agreement by reason of the gain recognition event; and

(iii) A calculation of the reduction to the amount of gain subject to the gain recognition agreement by reason of the gain recognition event (for example, in the case of a gain recognition event described in paragraph (n)(2) of this section).

(2) A complete description of any event occurring during such taxable year that has terminated or reduced the amount of gain subject to the gain recognition agreement (for example, an event described in paragraph (o) of this section), including a cal-

culation of any reduction to the amount of gain subject to the gain recognition agreement.

(3) A statement describing any disposition of assets of the transferred corporation during the taxable year not in the ordinary course of business.

(h) *Use of security*. The U.S. transferor may be required to furnish a bond or other security that satisfies the requirements of §301.7101–1 if the Area Director, Field Examination, Small Business/Self Employed or the Director of Field Operations, Large and Mid-Size Business (Director) determines that such security is necessary to ensure the payment of any tax on the gain realized, but not recognized, upon the initial transfer. Such bond or security generally will be required only if the transferred stock or securities are a principal asset of the U.S. transferor and the Director has reason to believe that a disposition of the stock or securities may be contemplated.

(i) [Reserved.]

(j) *Triggering events*. Except as provided in this section, if an event described in paragraphs (j)(1) through (10) of this section (triggering event) occurs during the GRA term, the U.S. transferor must recognize gain under the gain recognition agreement in accordance with paragraph (c)(1)(i) of this section. This paragraph (j) generally requires the U.S. transferor to recognize gain (and pay applicable interest with respect to any additional tax due as provided in paragraph (c)(1)(v) of this section) under the gain recognition agreement to the extent the transferred stock or securities are disposed of, directly or indirectly. This paragraph (j) also requires the U.S. transferor to recognize gain under the gain recognition agreement in certain cases where it is not appropriate for the gain recognition agreement to continue. See paragraph (k) of this section for exceptions available for certain events that would otherwise constitute triggering events under this paragraph (j). See paragraph (o) of this section for certain events that terminate or reduce the amount of gain subject to a gain recognition agreement.

(1) *Disposition of transferred stock or securities*. A complete or partial disposition of the transferred stock or securities. See paragraph (q)(2) of this section, *Example 2* for an illustration of the rule of this paragraph (j)(1).

(2) *Disposition of substantially all of the assets of the transferred corporation*—(i) *General rule*. Except as provided in paragraph (j)(2)(ii) of this section, a disposition in one or more related transactions of substantially all of the assets of the transferred corporation (including stock or securities in a subsidiary corporation or a partnership interest). If the transferred corporation is domestic, see paragraph (o)(4) of this section.

(ii) *Exceptions*. For purposes of paragraph (j)(2)(i) of this section, the following dispositions shall be disregarded—

(A) Dispositions of property described in section 1221(a)(1) occurring in the ordinary course of business;

(B) An exchange of stock or securities described in section 354 that is pursuant to an asset reorganization; and

(C) An exchange of stock by a corporate distributee (as defined in section 334(b)(2)) pursuant to a complete liquidation to which section 332 applies.

(3) *Disposition of certain partnership interests*. If the initial transfer occurs by reason of the transfer of a partnership interest, a complete or partial disposition of such partnership interest. See section 367(a)(4) and §1.367(a)–1T(c)(3)(ii).

(4) *Disposition of stock of the transferee foreign corporation*. A complete or partial disposition of the stock of the transferee foreign corporation received by the U.S. transferor in the initial transfer. For purposes of this section, an individual U.S. transferor that loses U.S. citizenship or ceases to be a lawful permanent resident of the United States (within the meaning of section 7701(b)(6)) shall be treated as disposing of all the stock of the transferee foreign corporation received in the initial transfer as of the date before the loss of such status.

(5) *Deconsolidation.* A U.S. transferor that is a member of a consolidated group ceases to be a member of the consolidated group, other than by reason of an acquisition of the assets of the U.S. transferor in a transaction to which section 381(a) applies, or by reason of the U.S. transferor joining another consolidated group as part of the same transaction.

(6) *Consolidation*. A U.S. transferor becomes a member of a consolidated group, including a U.S. transferor that is a member of a consolidated group and that becomes a member of another consolidated group.

(7) *Death of an individual; trust or estate ceases to exist*. A U.S. transferor that is an individual dies, or a U.S. transferor that is a trust or estate ceases to exist.

(8) *Failure to comply*. The U.S. transferor fails to comply in any material respect with any requirement of this section or with the terms of the gain recognition agreement, including failure to file an annual certification under paragraph (g) of this section. If a failure to include information in a gain recognition agreement as filed constitutes a failure to comply in a material respect, the U.S. transferor cannot avoid the application of this paragraph (j)(8) by subsequently making such information available. A material failure under this paragraph (j)(8) shall extend the period of limitations on assessments of tax until the close of the third full taxable year ending after the date on which the Director of Field Operations or Area Director receives actual notice of the failure to comply from the U.S. transferor.

(9) *Gain recognition agreement filed in connection with indirect stock transfers and certain triangular asset reorganizations*. With respect to a gain recognition agreement entered into in connection with an indirect stock transfer (as defined in §1.367(a)–3(d)), or a triangular asset reorganization under §1.367(a)–3(e)(2), an indirect disposition of the transferred stock or securities. For example, in the case of an indirect stock transfer described in §1.367(a)–3(d)(1)(iii)(A), a complete or partial disposition of the stock of the acquiring corporation.

(10) *Gain recognition agreement filed pursuant to paragraph (k)(14) of this section*. In the case of a gain recognition agreement entered into pursuant to paragraph (k)(14) of this section, in addition to any disposition or other event described in paragraphs (j)(1) through (9) of this section,—

(i) Any disposition or other event identified as a triggering event in a new gain recognition agreement as required under paragraph (k)(14)(iii) of this section; and

(ii) Any disposition or other event that is inconsistent with the principles of paragraph (k) of this section including, for example, an indirect disposition of the transferred stock or securities.

(k) *Triggering event exceptions*. Notwithstanding paragraph (j) of this section, a disposition or other event described in paragraphs (k)(1) through (14) of this section shall not constitute a triggering event. This paragraph (k) generally provides exceptions for certain dispositions that constitute nonrecognition transactions but only if, immediately after the disposition, a U.S. transferor retains, as applicable, a direct or indirect interest in the transferred stock or securities, or in the assets of the transferred corporation, and a new gain recognition agreement is entered into with respect to the initial transfer in accordance with this paragraph (k). Notwithstanding the application of this paragraph (k), if a gain recognition event described under paragraphs (m) and (n) of this section occurs during the GRA term the U.S. transferor may be required to recognize gain under the gain recognition agreement in accordance with paragraph (c)(1)(i) of this section. See paragraph (o) of this section which provides that, notwithstanding paragraph (j) of this section, certain dispositions or other events shall instead terminate or reduce the amount of gain subject to a gain recognition agreement.

(1) *Transfers of stock of the transferee foreign corporation to a corporation or partnership*. A disposition of stock of the transferee foreign corporation received in the initial transfer pursuant to an exchange to which section 351, 354 (but only in a reorganization described in section 368(a)(1)(B) that is not a triangular reorganization), 361 (but only in a divisive reorganization to which section 355 applies), or 721 applies, shall not constitute a triggering event if a new gain recognition agreement is entered into in accordance with paragraphs (k)(1)(i) through (iv) of this section, as applicable. In the case of an exchange to which section 354 applies that is pursuant to a triangular reorganization described in section 368(a)(1)(B), see paragraph (k)(14) of this section and paragraph (q)(2) of this section, *Example 4*.

(i) In the case of an exchange to which section 351 or 354 applies in which stock of a foreign acquiring corporation is received, the U.S. transferor includes with the new gain recognition agreement a statement that a complete or partial disposition of the stock of the foreign acquiring corporation received in the exchange shall constitute a triggering event. The principles of paragraph (o)(1)(i) or (ii), as appropriate, shall be applied to determine whether a subsequent complete or partial disposition of the stock of the foreign acquiring corporation received in the exchange shall instead terminate or reduce the amount of the new gain recognition agreement.

(ii) In the case of an exchange to which section 351 or 354 applies in which stock of a domestic acquiring corporation is received, the domestic acquiring corporation enters into the new gain recognition agreement, which must designate the domestic acquiring corporation as the U.S. transferor for purposes of this section. For an illustration of the rule provided by this paragraph (k)(1)(ii), see paragraph (q)(2) of this section, *Example 3*.

(iii) In the case of a section 361 exchange that is pursuant to a divisive reorganization to which section 355 applies and in which stock of a domestic corporation (domestic controlled corporation) is received, the domestic controlled corporation enters into the new gain recognition agreement, which must designate the domestic controlled corporation as the U.S. transferor for purposes of this section. For an illustration of the rule provided by this paragraph (k)(1)(iii), see paragraph (q)(2) of this section, *Example 11*.

(iv) In the case of an exchange to which section 721 applies, the U.S. transferor includes with the new gain recognition agreement a statement that a complete or partial disposition of the partnership interest received in the exchange shall constitute a triggering event for purposes of the new gain recognition agreement.

(2) *Complete liquidation of U.S. transferor under sections 332 and 337*. A distribution by the U.S. transferor of the stock of the transferee foreign corporation received in the initial transfer to which section 337 applies, that is pursuant to a complete liquidation under section 332, shall not constitute a triggering event if the corporate distributee (as defined in section 334(b)(2)) is a domestic corporation (domestic corporate distributee) and the domestic corporate distributee enters into a new gain recognition agreement. The new gain recognition agreement must designate the domestic corporate distributee as the U.S. transferor for purposes of this section.

(3) *Transfers of transferred stock or securities to a corporation or partnership*. A disposition of the transferred stock or securities pursuant to an exchange to which section 351, 354 (but only in a reorganization described in section 368(a)(1)(B)), or 721 applies, shall not constitute a triggering event if the U.S. transferor enters into a new gain recognition agreement that provides that the dispositions described in paragraphs (k)(3)(i) and (ii) of this section shall constitute triggering events for purposes of the new gain recognition.

(i) A complete or partial disposition of the stock, securities, or partnership interest (as applicable) received in exchange for the transferred stock or securities.

(ii) Any other event that is inconsistent with the principles of this paragraph (k), including the indirect disposition of the transferred stock or securities.

(4) *Transfers of substantially all of the assets of the transferred corporation*. A disposition of substantially all of the assets of the transferred corporation pursuant to an exchange to which section 351, 354 (but only in a reorganization described in section 368(a)(1)(B)), or 721 applies, shall not constitute a triggering event if the U.S. transferor enters into a new gain recognition agreement that provides that a complete or partial disposition of the stock, securities, or partnership interest (as applicable) received in exchange for the assets shall constitute a triggering event for purposes of the new gain recognition agreement.

(5) *Recapitalizations and section 1036 exchanges*. A complete or partial disposition of the transferred stock or securities, or of the stock of the transferee foreign corporation received in the initial transfer, pursuant to a reorganization described under section 368(a)(1)(E), or pursuant to a transaction to which section 1036 applies, shall not constitute a triggering event if the U.S. transferor enters into a new gain recognition agreement.

(6) *Certain asset reorganizations*—(i) *Stock of transferee foreign corporation*. If stock of the transferee foreign corporation received in the initial transfer is transferred to a domestic acquiring corporation in a section 361 exchange that is pursuant to an asset reorganization, the exchanges made pursuant to the asset reorganization shall not constitute triggering events if the domestic acquiring corporation enters into a

new gain recognition agreement that designates the domestic acquiring corporation as the U.S. transferor for purposes of this section. For an illustration of the rule provided by this paragraph (k)(6), see paragraph (q)(2) of this section, *Example 5*. If the acquiring corporation is foreign, see paragraph (k)(14) of this section and paragraph (q)(2) of this section, *Example 6*.

(ii) *Transferred stock or securities*. If the transferred stock or securities are transferred to a foreign acquiring corporation in a section 361 exchange that is pursuant to an asset reorganization, the exchanges made pursuant to the asset reorganization shall not constitute triggering events if the U.S. transferor enters into a new gain recognition agreement that designates the foreign acquiring corporation as the transferee foreign corporation for purposes of this section. For an illustration of the rule provided by this paragraph, see paragraph (q)(2) of this section, *Example 7*. If the transfer is to a domestic acquiring corporation, or is pursuant to a triangular asset reorganization, see paragraph (k)(14) or (o)(5) of this section.

(iii) *Assets of transferred corporation*. If substantially all of the assets of the transferred corporation are transferred to a foreign or domestic acquiring corporation in a section 361 exchange that is pursuant to an asset reorganization, the exchanges made pursuant to the asset reorganization shall not constitute triggering events if the U.S. transferor enters into a new gain recognition agreement that, unless the acquiring corporation is the transferee foreign corporation, designates the acquiring corporation as the transferred corporation for purposes of this section. Only the assets of the transferred corporation received by the acquiring corporation shall be treated as assets of the transferred corporation for purposes of this section (for example, only such assets will be taken into account for purposes of paragraph (j)(2) of this section). For an illustration of the rule provided by this paragraph, see paragraph (q)(2) of this section, *Example 8*. If the transferred corporation is domestic, see section 367(a)(1) and (a)(5), and paragraph (o)(4) of this section. If the transfer is pursuant to a triangular asset reorganization, see paragraph (k)(14) of this section.

(7) *Certain triangular reorganizations*—(i) *Transferee foreign corporation*. If substantially all of the assets of the transferee foreign corporation are transferred to a foreign acquiring corporation in a section 361 exchange that is pursuant to a triangular asset reorganization, the exchanges made pursuant to the reorganization shall not constitute triggering events if a new gain recognition agreement is entered into in accordance with paragraphs (k)(7)(i)(A) through (C) of this section. If the acquiring corporation is domestic, see paragraph (k)(14) of this section. For rules that apply to gain recognition agreements entered into as a result of an indirect stock transfer, see §1.367(a)–3(d)(2)(iv) and paragraph (j)(9) of this section.

(A) If P is foreign, the new gain recognition agreement designates P as the transferee foreign corporation and includes a statement that the U.S. transferor agrees to treat a complete or partial disposition of the S stock held by P as a triggering event.

(B) Except as provided in paragraph (k)(7)(i)(C) of this section, if P is domestic, P enters into the new gain recognition agreement that designates P as the U.S. transferor and S as the transferee foreign corporation.

(C) If the triangular asset reorganization is described in section 368(a)(1)(A) by reason of section 368(a)(2)(E) and the transferee foreign corporation is the merged corporation, the U.S. transferor enters into the new gain recognition agreement and designates the surviving corporation as the transferee foreign corporation.

(ii) *Transferred corporation*. If substantially all of the assets of the transferred corporation are transferred in a section 361 exchange pursuant to a triangular asset reorganization, the exchanges made pursuant to the reorganization shall not constitute triggering events if the U.S. transferor enters into a new gain recognition agreement in accordance with paragraph (k)(7)(ii)(A) of this section and, as applicable, paragraph (k)(7)(ii)(B) or (C) of this section.

(A) The new gain recognition agreement includes a statement that the U.S. transferor agrees to treat a complete or partial disposition of the P stock received in the reorganization as a triggering event.

(B) If the triangular asset reorganization is described in section 368(a)(1)(C), or section 368(a)(1)(A) or (G) by reason of section 368(a)(2)(D), the new gain recognition agreement includes a statement that the U.S. transferor agrees to treat a complete or partial disposition of the S stock held by P as a triggering event.

(C) If the triangular asset reorganization is described in section 368(a)(1)(A) by reason of section 368(a)(2)(E) and the transferred corporation is the merged corporation, the new gain recognition agreement includes a statement that the U.S. transferor agrees to treat a complete or partial disposition of the stock of the surviving corporation as a triggering event.

(8) *Complete liquidation of transferred corporation*. A distribution of substantially all of the assets of the transferred corporation to which section 337 applies, and the related exchange of the transferred stock to which section 332 applies, shall not constitute triggering events, if the U.S. transferor enters into a new gain recognition agreement. If the transferred corporation is domestic, see §1.367(e)–2 and paragraph (o)(4) of this section. See paragraph (q)(2) of this section, *Example 9* for an illustration of the rules provided in this paragraph (k)(8).

(9) *Death of U.S. transferor*. The death of a U.S. transferor shall not constitute a triggering event if the person winding up the affairs of the U.S. transferor—

(i) Retains sufficient assets of the U.S. transferor to satisfy any possible Federal tax liability of the U.S. transferor under the gain recognition agreement for the duration of the extended period of limitations on assessments of tax on the gain realized but not recognized in the initial transfer;

(ii) Provides security as required under paragraph (h) of this section for any possible Federal tax liability of the U.S. transferor under the gain recognition agreement; or

(iii) Obtains a ruling from the Internal Revenue Service providing for one or more successors to the U.S. transferor under the gain recognition agreement.

(10) *Deconsolidation*. A deconsolidation of the U.S. transferor shall not constitute a triggering event if the U.S. transferor enters into a new gain recognition agreement.

(11) *Consolidation*. A consolidation of the U.S. transferor shall not constitute a triggering event if the U.S. transferor enters into a new gain recognition agreement. See paragraph (d)(3) of this section.

(12) *Intercompany transactions*—(i) *General rule*. If, pursuant to an inter-

company transaction, the U.S. transferor disposes of stock of the transferee foreign corporation received in the initial transfer, this paragraph (k)(12) applies to such disposition to the extent the intercompany transaction creates an intercompany item that is not taken into account in the taxable year during which the intercompany transaction occurs. To the extent this paragraph (k)(12) applies, the disposition shall not constitute a triggering event, and the U.S. transferor shall remain subject to the gain recognition agreement if the conditions of paragraphs (k)(12)(i)(A) and (B) of this section are satisfied. To the extent the intercompany transaction does not create an intercompany item see, for example, paragraph (k)(1) and paragraph (q)(2) of this section, *Example 20*. See paragraph (o)(6) of this section for the effect on a gain recognition agreement when an intercompany item from an intercompany transaction to which this paragraph (k)(12)(i) applies is taken into account.

(A) At the time of the disposition, the basis of the stock of the transferee foreign corporation received in the initial transfer that is disposed of in the intercompany transaction is not greater than the sum of the amounts described in paragraphs (k)(12)(i)(A)(*1*) through (*3*) of this section. If only a portion of the stock of the transferee foreign corporation received in the initial transfer is disposed of, then the basis of such stock shall be compared with a proportionate amount (measured by value as determined at the time of the disposition) of the amounts described in paragraph (k)(12)(i)(A)(*1*) through (*3*) of this section. To satisfy the basis condition of this paragraph (k)(12)(i)(A), the U.S. transferor may reduce the basis of the stock of the transferee foreign corporation received in the initial transfer that is disposed of in the intercompany transaction in accordance with the principles of paragraph (o)(1)(iii) of this section.

(*1*) The aggregate basis of the transferred stock or securities at the time of the initial transfer;

(*2*) The amount of any increase to the basis of the transferred stock or securities by reason of gain recognized by the U.S. transferor on the initial transfer; and

(*3*) The amount of any increase to the basis of the stock disposed of by reason of an income inclusion by the U.S. transferor with respect to such stock (for example, pursuant to section 961(a)).

(B) The annual certification filed with respect to the existing gain recognition agreement for the taxable year during which the intercompany transaction occurs includes a complete description of the intercompany transaction and a schedule illustrating how the basis condition of paragraph (k)(12)(i)(A) of this section is satisfied.

(ii) *Certain dispositions following intercompany transaction*. A subsequent disposition of stock of the transferee foreign corporation that is transferred in an intercompany transaction to which the exception provided by paragraph (k)(12)(i) of this section applies shall not constitute a triggering event if—

(A) The stock is transferred to a member of the consolidated group that includes the U.S. transferor immediately after the disposition, and

(B) The annual certification filed with respect to the existing gain recognition agreement for the taxable year during which the subsequent disposition occurs includes a complete description of the disposition.

(13) *Deemed asset sales pursuant to section 338(g) elections*. A deemed sale of the assets of the transferred corporation or the transferee foreign corporation as a result of an election under section 338(g) shall not constitute a triggering event. This paragraph does not apply to the sale of the stock of the target corporation (within the meaning of section 338(d)(2)) with respect to which such election is made.

(14) *Other dispositions or events*. A disposition or other event that would constitute a triggering event, without regard to this paragraph (k)(14), shall not constitute a triggering event if the conditions of paragraph (k)(14)(i) through (iii) of this section, as applicable, are satisfied. See paragraph (q)(2), *Examples 4*, *6*, *10*, *12, 17*, *21*, and *23* of this section for illustrations of the rules provided by this paragraph (k)(14).

(i) The disposition qualifies as a nonrecognition transaction.

(ii) Immediately after the disposition or other event, a U.S. transferor retains a direct or indirect interest in the transferred stock or securities or, as applicable, in substantially all of the assets of the transferred corporation (for example, in a case where the transferred corporation has been liquidated pursuant to section 332). If, as a result of the disposition or other event, a foreign corporation acquires the transferred stock or securities or, as applicable, substantially all the assets of the transferred corporation, the condition of this paragraph (k)(14)(ii) shall be satisfied only if the U.S. transferor owns at least five percent (applying the attribution rules of section 318, as modified by section 958(b)) of the total voting power and the total value of the outstanding stock of such foreign corporation.

(iii) A new gain recognition agreement is entered into by the U.S. transferor described in paragraph (k)(14)(ii) of this section that includes—

(A) An explanation of why this paragraph (k)(14) applies to the disposition or other event; and

(B) A description of each subsequent disposition or other event that would constitute a triggering event, other than those described in paragraph (j) of this section, with respect to the new gain recognition agreement based on the principles of paragraphs (j) and (k) of this section including, for example, an indirect disposition of the transferred stock or securities.

(l) [Reserved.]

(m) *Receipt of boot in nonrecognition transactions*—(1) *Dispositions of transferred stock or securities*. Notwithstanding paragraph (k) of this section, if gain is required to be recognized (not including any gain that would be treated as a dividend under section 356(a)(2)) in connection with a disposition of the transferred stock or securities to which an exception under paragraph (k) of this section otherwise applies (triggering event exception), the U.S. transferor shall recognize gain under paragraph (c)(1)(i) of this section equal to the amount of gain required to be recognized in connection with the disposition, but not in excess of the amount of gain subject to the gain recognition agreement. For purposes of this paragraph (m)(1), the amount of gain required to be recognized in connection with the disposition shall be determined before taking into account any increase to the basis of the transferred stock or securities under paragraph (c)(4)(ii) of this section. See paragraph (q)(2) of this section, *Example 13*, for an illustration of the rule provided by this paragraph (m)(1).

(2) *Dispositions of assets of transferred corporation*. If gain is required to be recognized (not including any gain that would be treated as a dividend under section 356(a)(2)) in connection with a disposition of substantially all of the assets of the transferred corporation to which a triggering event exception otherwise applies, the U.S. transferor shall recognize gain under paragraph (c)(1)(i) of this section equal to the amount of gain required to be recognized in connection with the disposition, but not in excess of the amount of gain subject to the gain recognition agreement.

(n) *Special rules for distributions with respect to stock*—(1) *Certain dividend equivalent redemptions treated as dispositions*. A redemption of the transferred stock or of stock of the transferee foreign corporation received in the initial transfer that is treated by reason of section 302(d) as a distribution of property to which section 301 applies shall constitute a disposition for purposes of this section unless the U.S. transferor enters into a new gain recognition agreement that includes appropriate provisions to account for the redemption. For an illustration of the rule of this paragraph (n)(1), see paragraph (q)(2) of this section, *Example 14*.

(2) *Gain recognized under section 301(c)(3)*. If gain is required to be recognized under section 301(c)(3) with respect to the transferred stock, the U.S. transferor shall recognize gain under the gain recognition agreement in accordance with paragraph (c)(1)(i) of this section in an amount equal to the gain required to be recognized under section 301(c)(3), but not in excess of the amount of gain subject to the gain recognition agreement. For this purpose, the amount of gain required to be recognized under section 301(c)(3) shall be determined before taking into account any increase in the basis of the transferred stock under paragraph (c)(4)(ii) of this section.

(o) *Dispositions or other events that terminate or reduce the amount of gain subject to the gain recognition agreement*. Notwithstanding paragraph (j) of this section, the following dispositions or other events shall not constitute triggering events but instead shall terminate or reduce the amount of gain subject to the gain recognition agreement.

(1) *Taxable disposition of stock of the transferee foreign corporation*—(i) *Complete disposition*. Except as otherwise provided in this paragraph (o)(1)(i), if the U.S. transferor disposes of all the stock of the transferee foreign corporation received in the initial transfer in a transaction in which all gain realized is recognized and included in taxable income during the taxable year of the disposition, the gain recognition agreement shall terminate without further effect if, at the time of the disposition, the aggregate basis of such stock is not greater than the sum of the amounts described in paragraphs (o)(1)(i)(A) through (C) of this section. This paragraph shall not apply to a disposition of stock of the transferee foreign corporation pursuant to an intercompany transaction to which paragraph (k)(12) of this section applies. This paragraph shall also not apply to an individual U.S. transferor that loses U.S. citizenship or ceases to be a lawful permanent resident of the United States (within the meaning of section 7701(b)(6)).

(A) The aggregate basis of the transferred stock or securities at the time of the initial transfer;

(B) The amount of any increase to the basis of the transferred stock or securities by reason of gain recognized by the U.S. transferor on the initial transfer; and

(C) The amount of any increase to the basis of the stock disposed of by reason of an income inclusion by the U.S. transferor with respect to such stock (for example, pursuant to section 961(a)).

(ii) *Partial dispositions*. A partial disposition by the U.S. transferor of the stock of the transferee foreign corporation received in the initial transfer in a transaction otherwise described in paragraph (o)(1)(i) of this section shall reduce the amount of gain subject to the gain recognition agreement based on the relative fair market value of the stock disposed of (measured at the time of the disposition) compared to the fair market value of all of the stock of the transferee foreign corporation received in the initial transfer (measured at the time of the disposition). For determining whether the basis condition of paragraph (o)(1)(i) of this section is satisfied in the case of a partial disposition, the aggregate basis of the stock disposed of is compared to a proportionate amount (based on fair market value, as measured at the time of the partial disposition) of the amounts described in paragraphs (o)(1)(i)(A) through (C) of this section. For an illustration of the rules of this paragraph (o)(1)(ii), see paragraph (q)(2), *Example 15*, of this section.

(iii) *Reduction of stock basis*. For purposes of satisfying the basis condition of paragraph (o)(1)(i) or (ii) of this section, the U.S. transferor may reduce the aggregate basis of the stock of the transferee foreign corporation received in the initial transfer, effective immediately before the disposition. For an illustration of the rules of this paragraph (o)(1)(iii), see paragraph (q)(2), *Example 16*, of this section. The U.S. transferor reduces the basis of the stock of the transferee foreign corporation by including a statement with the timely-filed return of the U.S. transferor for the taxable year in which the disposition occurs, entitled "Election to Reduce Stock Basis Under §1.367(a)–8(o)(1)(iii)" and that includes—

(A) A description, including the date, of the disposition;

(B) A description of the stock of the transferee foreign corporation disposed of and the basis adjustments made under this paragraph (o)(1)(iii); and

(C) The fair market value of all the stock of the transferee foreign corporation held by the U.S. transferor at the time of the disposition.

(2) *Gain recognized in connection with certain nonrecognition transactions*. If the U.S. transferor recognizes gain in connection with a complete or partial disposition of stock of the transferee foreign corporation received in the initial transfer that is described in paragraph (k) of this section, and the basis condition of paragraph (o)(1)(i) or (ii) of this section, as applicable, is satisfied with the respect to such disposition, the amount of gain subject to the new gain recognition agreement filed under paragraph (k) of this section as a result of such disposition shall equal the amount of gain subject to the existing gain recognition agreement reduced by the amount of gain recognized by the U.S. transferor on the disposition. If the U.S. transferor recognizes gain in connection with a complete or partial disposition of the stock of the transferee foreign corporation received in the initial transfer that is described in paragraph (k) of this section, and the condition of paragraph (o)(1)(i) or (ii) of this section, as applicable, is satisfied with the respect to the disposition, but a new gain recogni-

tion agreement is not filed with respect to such disposition so that a triggering event exception does not apply to the disposition, the amount of gain required to be recognized by the U.S. transferor under the existing gain recognition agreement shall be reduced by the amount of the gain recognized on the disposition.

(3) *Gain recognized under section 301(c)(3).* If the U.S. transferor recognizes gain under section 301(c)(3) with respect to the stock of the transferee foreign corporation received in the initial transfer, the amount of gain subject to the gain recognition agreement shall be reduced by the amount of such recognized gain.

(4) *Dispositions of substantially all of the assets of a domestic transferred corporation.* Except as otherwise provided in this paragraph (o)(4), the gain recognition agreement shall terminate without further effect if substantially all of the assets of the transferred corporation are disposed of in a transaction in which all gain realized is recognized and included in taxable income during the taxable year of the disposition, but only if, at the time of the initial transfer, the U.S. transferor owned stock in the transferred corporation satisfying the requirements of section 1504(a)(2) and the U.S. transferor and the transferred corporation were members of the same consolidated group. If the initial transfer was part of an indirect stock transfer, the gain recognition agreement shall terminate without further effect if substantially all of the assets of the transferred corporation (taking into account §1.367(a)–3(d)(2)(v)) are disposed of in a transaction in which all gain realized is recognized and included in taxable income during the taxable year of the disposition, but only if at the time of the initial transfer the U.S. transferor owned stock in the transferred corporation satisfying the requirements of section 1504(a)(2) (for example, in the case of a reorganization described in section 368(a)(1)(A) by reason of section 368(a)(2)(E)) and the U.S. transferor and the transferred corporation were members of the same consolidated group.

(5) *Certain distributions or transfers of transferred stock or securities to U.S. persons.* To the extent a distribution or transfer of the transferred stock or securities satisfies the conditions of paragraphs (o)(5)(i) through (iii) of this section, the gain recognition agreement shall terminate without further effect, or the amount of gain subject to the gain recognition agreement shall be reduced, as appropriate.

(i) *Distributions or transfers described in section 337, 355, or 361.* The transferred stock or securities are distributed or transferred pursuant to a transaction described in paragraph (o)(5)(i)(A) through (D) of this section, as appropriate.

(A) A distribution described in section 337 that is pursuant to a complete liquidation described in section 332. See paragraph (q)(2) of this section, *Example 18*, for an illustration of the rule provided by this paragraph (o)(5)(i)(A).

(B) A distribution to which section 355 applies. See paragraph (q)(2) of this section, *Example 19*, for an illustration of the rule provided by this paragraph (o)(5)(i)(B).

(C) A section 361 exchange that is pursuant to an asset reorganization. See paragraph (q)(2) of this section, *Example 22*, for an illustration of the rule provided by this paragraph (o)(5)(i)(C).

(D) A distribution to which section 361(c) applies that is pursuant to an asset reorganization. See paragraph (q)(2) of this section, *Example 22*, for an illustration of the rule provided by this paragraph (o)(5)(i)(D).

(ii) *Qualified recipient.* The recipient of the transferred stock or securities in the relevant transaction described in paragraph (o)(5)(i) of this section (qualified recipient) is—

(A) The U.S. transferor;

(B) A member of the consolidated group that includes the U.S. transferor immediately after the transaction; or

(C) An individual that is a United States person.

(iii) *Basis requirement*—(A) *General rule.* Immediately after the relevant transaction described in paragraph (o)(5)(i) of this section, the aggregate basis of the transferred stock or securities received by the qualified recipient is not greater than the aggregate basis of such stock or securities at the time of the initial transfer (as adjusted for gain recognized by the U.S. transferor on the initial transfer attributable to such stock or securities). For this purpose, the basis of the transferred stock in the hands of the qualified recipient shall be determined without regard to any basis attributable to income inclusions with respect to the stock (for example, under section 961(a)). In the case of a distribution to which section 355 applies, any adjustments to basis under §1.367(b)–5(c) shall be made before determining whether the basis condition of this paragraph is satisfied.

(B) *Election to reduce basis in transferred stock or securities.* If the basis condition of paragraph (o)(5)(iii)(A) of this section is not satisfied, each qualified recipient may reduce the basis of the transferred stock or securities received in the transaction to the extent necessary to satisfy the basis condition. A qualified recipient reduces the basis of the transferred stock or securities by including a statement with its timely-filed return for the taxable year during which the distribution or transfer occurs entitled "Election to Reduce Stock Basis Under §1.367(a)–8(o)(5)(iii)(B)" and that includes—

(*1*) A complete description and the date of the distribution or transfer;

(*2*) The fair market value of the transferred stock or securities received by the qualified recipient in the transaction; and

(*3*) The basis of the transferred stock or securities received by the qualified recipient immediately before and after the basis reduction.

(6) *Dispositions or other event following certain intercompany transactions.* If, subsequent to an intercompany transaction to which paragraph (k)(12) of this section applies, a disposition or other event occurs that requires the U.S. transferor to take into account the intercompany item related to the intercompany transaction (under the provisions of §1.1502–13), the gain recognition agreement shall terminate without further effect or the amount of gain subject to the gain recognition agreement shall be reduced based on the principles of paragraph (o)(1)(i) or (ii) of this section, as appropriate. For an illustration of the rules of this paragraph (o)(6), see paragraph (q)(2) of this section, *Example 20*.

(7) *Expropriations under foreign law.* The amount of gain subject to the gain recognition agreement shall be reduced to the extent the stock or securities of the transferee foreign corporation received in the initial transfer, the transferred stock or securities, or substantially all the assets of the transferred corporation, are expropriated, seized, or subjected to a similar taking of such property by the government

of a foreign country, any political subdivision thereof, or any agency or instrumentality of the foregoing. Principles similar to those of paragraph (o)(1)(i) or (o)(1)(ii) of this paragraph, as relevant, shall be applied to determine the amount of the reduction.

(p) *Relief for reasonable cause for failure to comply*—(1) *Request for relief*. A U.S. transferor that fails to file timely a gain recognition agreement, waiver of period of limitations on assessments of tax, annual certification, or other information required under this section shall be considered to have satisfied the timeliness requirement with respect to such filing, and a failure to comply in any material respect with any requirement of this section or with the terms of the gain recognition agreement that would otherwise constitute a triggering event shall not constitute a triggering event, if a request for relief is filed as provided under paragraph (p)(2) of this section and the U.S. transferor is able to demonstrate to the Area Director, Field Examination, Small Business/Self Employed or the Director of Field Operations, Large and Mid-Size Business (Director) having jurisdiction of the tax return of the U.S. transferor for the taxable year to which the failure relates, that such failure was due to reasonable cause and not willful neglect. Whether the failure was due to reasonable cause and not willful neglect will be determined by the Director after considering all the facts and circumstances. The Director shall notify the U.S. transferor in writing within 120 days if it is determined that the failure was not due to reasonable cause, or if additional time will be needed to make a determination. For this purpose, the 120-day period shall begin on the date the Internal Revenue Service notifies the U.S. transferor in writing that the request for reasonable cause relief has been received and assigned for review. If the U.S. transferor is not again notified before the close of the 120-day period, the U.S. transferor shall be deemed to have established that the failure to file timely or comply was due to reasonable cause and not willful neglect.

(2) *Procedures for filing requests for relief*—(i) *Time of submission*. Requests for relief under paragraph (p)(1) of this section shall be considered only if, as soon as the U.S. transferor becomes aware of the failure to file timely or comply in any material respect with any requirement of this section, an amended return is filed for the taxable year to which the failure relates that includes the information that should have been included with the original return for such taxable year or otherwise complies with the rules of this section and that includes a written statement explaining the reasons for the failure to file timely or comply. The amended return must be filed with the applicable Internal Revenue Service Center with which the U.S. transferor filed its original return for such taxable year.

(ii) *Notice requirement*. In addition to the requirement of paragraph (p)(2)(i) of this section, the U.S. transferor must comply with the requirements of paragraph (p)(2)(ii)(A) or (B) of this section, as applicable.

(A) If any taxable year of the U.S. transferor is under examination when the amended return is filed, a copy of the amended return and any information required to be included with such return must be delivered to the Internal Revenue Service personnel conducting the examination.

(B) If no taxable year of the U.S. transferor is under examination when the amended return is filed, a copy of the amended return and any information required to be included with such return must be delivered to the Director having jurisdiction over the return.

(q) *Examples*—(1) *Presumed facts and references*. For purposes of the examples in paragraph (q)(2) of this section, and except where otherwise indicated, the following is presumed.

(i) UST, USP, and DC are domestic corporations that each use a calendar taxable year.

(ii) USP wholly owns UST and is the common parent of the consolidated group of which UST is a member.

(iii) TFC, TFD, F1, and FA are foreign corporations.

(iv) UST wholly owns TFD.

(v) In a section 351 exchange, UST transfers all of the stock of TFD (TFD stock) to TFC in exchange solely for stock of TFC (the initial transfer).

(vi) Pursuant to §1.367(a)–3(b)(1)(ii) and this section, UST enters into a gain recognition agreement in connection with the initial transfer and makes the election described under paragraph (c)(2)(vi) of this section with respect to the gain recognition agreement.

(vii) As applicable, the section 1248 amount (within the meaning of §1.367(b)–2(c)) or all earnings and profits amount (within the meaning of §1.367(b)–2(d)) attributable to the stock of a foreign corporation is zero.

(viii) All transactions are respected under general principles of tax law, including the step transaction doctrine.

(ix) References to a U.S. transferor entering into a gain recognition agreement mean, where applicable, that the common parent of the consolidated group of which the U.S. transferor is a member has filed the gain recognition agreement on behalf of the U.S. transferor in accordance with paragraph (d)(3) of this section.

(x) Taxable years during the GRA term are referred to, for example, as year 1 and year 2.

(2) *Examples*. The following examples illustrate the application of the rules of this section.

Example 1. Basis adjustments from gain recognized under the gain recognition agreement. (i) *Facts*. TFC wholly owns F1. In year 3, pursuant to a section 351 exchange, TFC transfers all of the TFD stock to F1 in exchange solely for voting stock of F1. UST enters into a new gain recognition agreement with respect to the initial transfer under paragraph (k)(3) of this section, and therefore the transfer by TFC of the TFD stock to F1 is not a triggering event. Under paragraph (c)(5)(i) of this section, the existing gain recognition agreement terminates without further effect. In year 4, in an exchange to which section 721 applies, UST contributes the TFC stock received in the initial transfer to PRS, a domestic partnership, in exchange for a partnership interest. UST enters into a new gain recognition agreement with respect to the initial transfer under paragraph (k)(1) of this section, and therefore the transfer by UST of the TFC stock to PRS is not a triggering event. Under paragraph (c)(5)(i) of this section, the new gain recognition agreement filed by UST in year 3 terminates without further effect. In year 5, TFD disposes of substantially all of its assets in a transaction that constitutes a triggering event under paragraph (j)(2)(i) of this section. Under paragraph (c)(1)(i) of this section, UST recognizes the gain realized but not recognized on the initial transfer by reason of entering into the gain recognition agreement.

(ii) *Result*. Under paragraph (c)(4) of this section, the basis of the PRS interest held by UST, the TFC stock held by PRS that was received from UST in year 4, the F1 stock held by TFC that was received in exchange for the TFD stock in year 3, and the TFD stock held by F1 that was received from TFC in year 3 is increased by the amount of gain recognized by UST (but not by the additional tax or interest paid as result of such gain) with respect to the initial transfer under the gain recognition agreement. However, the basis of the assets of TFD (including the assets disposed of in year 5) is not increased as a result of the gain recognized by UST.

Example 2. *Impact of gain recognition event on computation of income*. (i) *Facts*. At the time of the initial transfer, the TFD stock has a $50x basis, a $100x fair market value, and a $30x section 1248 amount. The amount of gain subject to the gain recognition agreement is $50x. UST did not make an election under paragraph (c)(2)(vi) of this section with respect to the gain recognition agreement. In year 3, TFC disposes of the TFD stock received in the initial transfer in exchange for $120x cash.

(ii) *Result*—(A) *Gain recognition without an election*. The disposition by TFC of the TFD stock in year 3 is a triggering event under paragraph (j)(1) of this section. As a result, under paragraph (c)(1)(i) of this section, UST must recognize and include in income $50x gain under the gain recognition agreement. Under paragraph (c)(1)(iii)(A) of this section, UST must report the $50x gain on an amended return filed for the taxable year of the initial transfer. Under paragraph (c)(1)(v) of this section, UST must pay applicable interest on any additional tax due with respect to the $50x gain recognized. Under section 1248(a), $30x of the gain recognized by UST under the gain recognition agreement is recharacterized as a dividend. Under paragraph (c)(4) of this section, as of the date of the initial transfer, the basis of the TFC stock received by UST in the initial transfer and the TFD stock received by TFC in the initial transfer, respectively, is increased by $50x. After taking into account the increase to the basis of the TFD stock, TFC recognizes $20x gain on the disposition of the TFD stock in year 3.

(B) *Gain recognition with an election*. If UST made an election under paragraph (c)(2)(vi) of this section with the gain recognition agreement filed for the initial transfer, the result would be the same as in paragraph (ii)(A) of this *Example 2*, except that UST must include in income the $50x gain recognized under the gain recognition agreement on its tax return filed for year 3. Any additional tax due with respect to the $50x gain and applicable interest on the additional tax due must be included with such return. The amount, if any, of the $50x gain recognized by UST under the gain recognition agreement that is characterized as a dividend under section 1248(a) is determined in year 3.

Example 3. *Transfer of stock of the transferee foreign corporation to a domestic corporation in a section 351 exchange*. (i) *Facts*. UST wholly owns DC. In year 3, pursuant to a section 351 exchange, UST transfers all of the TFC stock received in the initial transfer to DC in an exchange solely for voting stock of DC.

(ii) *Result*. The year 3 transfer of the TFC stock by UST to DC constitutes a triggering event under paragraph (j)(4) of this section. However, the transfer shall not constitute a triggering event pursuant to paragraph (k)(1)(ii) of this section if DC enters into a new gain recognition agreement with respect to the initial transfer that designates DC as the U.S. transferor for purposes of this section. Pursuant to paragraphs (c)(4)(i) and (ii) of this section, if DC is required to recognize gain under the new gain recognition agreement, the basis of the stock of TFC and TFD would be increased by the amount of gain recognized. However, pursuant to paragraph (c)(4)(iii) of this section, no adjustment would be made to the basis of the DC voting stock received by UST in year 3 as a result of such gain recognition. Alternatively, if the conditions for the application of paragraph (k)(14) of this section are satisfied UST could instead enter into the new gain recognition agreement with respect to the initial transfer.

Example 4. *Transfer of stock of the transferee foreign corporation in a triangular section 368(a)(1)(B) reorganization*. (i) *Facts*. DC wholly owns FA. In year 3, pursuant to a triangular reorganization described in section 368(a)(1)(B), UST transfers all of the TFC stock received in the initial transfer to FA in exchange solely for 20% of the outstanding voting stock of DC. At the time of the reorganization, the TFC stock has a basis in excess of fair market value.

(ii) *Result*. (A) The transfer by UST of the TFC stock to FA is an indirect stock transfer under §1.367(a)–3(d)(1)(iii)(B). Accordingly, to preserve nonrecognition treatment, UST must enter into a separate gain recognition agreement under this section with respect to such transfer.

(B) With respect to the gain recognition agreement filed for the initial transfer of the TFD stock, the transfer by UST of the TFC stock to FA is a triggering event under paragraph (j)(4) of this section. However, the transfer shall not constitute a triggering event if the conditions of the exception provided by paragraph (k)(14) of this section are satisfied.

(*1*) The condition of paragraph (k)(14)(i) of this section is satisfied because the transfer qualifies as a nonrecognition transaction (assuming UST enters into a gain recognition agreement as described in paragraph (ii)(A) of this *Example 4*).

(*2*) The condition of paragraph (k)(14)(ii) of this section is satisfied because immediately after the transfer DC, a domestic corporation that is eligible to be a U.S. transferor, owns at least 5% (applying the attribution rules of section 318, as modified by section 958(b)) of the total voting power and total fair market value of the outstanding stock of FA. As a result, DC is treated as retaining an indirect interest in the TFD stock immediately following the transfer.

(*3*) The condition of paragraph (k)(14)(iii) of this section is satisfied if DC enters into a new gain recognition agreement with respect to the initial transfer of the TFD stock that, based on the principles of paragraph (j) of this section, describes the subsequent dispositions or other events that would constitute triggering events for purposes of the new gain recognition agreement (other than the dispositions and other events described in paragraph (j) of this section). For example, a complete or partial disposition of the stock of FA would constitute a triggering event for purposes of the new gain recognition agreement.

Example 5. *Transfer of stock of the transferee foreign corporation to a domestic corporation pursuant to an asset reorganization*. (i) *Facts*. At the time of the initial transfer the TFD stock has a $50x basis and a $100x fair market value. Therefore, the amount of gain subject to the gain recognition agreement is $50x. In year 3, pursuant to an asset reorganization described in section 368(a)(1)(A), UST transfers its assets to DC in exchange solely for 20% of the outstanding stock of DC. UST distributes the stock of DC to USP pursuant to the plan of reorganization.

(ii) *Result*. The transfer by UST of the TFC stock to DC constitutes a triggering event under paragraph (j)(4) of this section. However, pursuant to paragraph (k)(6)(i) of this section, if DC enters into a new gain recognition agreement with respect to the initial transfer that designates DC as the U.S. transferor, the transfer shall not constitute a triggering event.

Example 6. *Transfer of stock of the transferee foreign corporation to a foreign corporation pursuant to an asset reorganization*. (i) *Facts*. The facts are the same as in *Example 5*, except the acquiring corporation in the asset reorganization is FA, and, at the time of the asset reorganization, the TFC stock transferred by UST to FA has a $50x basis and a $150x fair market value. All of the conditions under section 367(a)(5) and the regulations under that section are satisfied, and no adjustment is required to the basis of the FA stock received by USP in the transaction.

(ii) *Result*. (A) The transfer by UST of the TFC stock to FA is described in section 361(a) and is therefore subject to section 367(a)(5). In general, UST cannot file a gain recognition agreement with respect to such transfer, and the transfer therefore is subject to the general rule of section 367(a)(1). However, if the conditions of §1.367(a)–3(e)(1)(i) through (iv) are satisfied, USP can enter into a gain recognition agreement with respect to the transfer to avoid the recognition of gain by UST on the transfer under section 367(a)(1). If the exception provided by paragraph (k)(14) of this section applies so that the transfer by UST of the TFC stock to FA is not a triggering event with respect to the gain recognition agreement filed for the initial transfer (discussed in paragraph (ii)(B) of this *Example 6*), the amount of gain subject to the gain recognition agreement (if entered into) with respect to the transfer by UST of the TFC stock to FA in the asset reorganization is $100x.

(B) Under paragraph (j)(4) of this section, the transfer of the TFC stock by UST to FA is a triggering event with respect to the gain recognition agreement for the initial transfer. The exception provided by paragraph (k)(6)(i) of this section does not apply to such transfer because FA, the acquiring corporation in the asset reorganization, is foreign. However, the transfer shall not constitute a triggering event if the conditions of the exception provided by paragraph (k)(14) of this section are satisfied.

(*1*) The condition of paragraph (k)(14)(i) of this section is satisfied because the transfer of the TFC stock to FA qualifies as a nonrecognition transaction (assuming USP enters into a gain recognition agreement with respect to such transfer).

(*2*) The condition of paragraph (k)(14)(ii) of this section is satisfied because immediately after the transfer USP, a domestic corporation that is eligible to be a U.S. transferor, owns at least 5% (applying the attribution rules of section 318, as modified by section 958(b)) of the total voting power and total fair market value of the outstanding stock of FA. As a result, USP is treated as retaining an indirect interest in the TFD stock immediately following the transfer.

(*3*) The condition of paragraph (k)(14)(iii) of this section is satisfied if USP enters into a new gain recognition agreement with respect to the initial transfer of the TFD stock that, based on the principles of paragraph (j) of this section, describes the subsequent dispositions or other events that would constitute triggering events for purposes of the new gain recognition agreement, other than those already provided in paragraph (j) of this section. For example, a disposition of the stock of FA would constitute such a triggering event for purposes of the new gain recognition agreement.

(iii) *Alternate facts*. Assume the same facts as in paragraph (i) of this *Example 6*, including that paragraph (k)(14) of this section applies to the year 3 reorganization so that USP enters into a new gain recognition agreement with respect to the initial transfer of the TFD stock that occurred in year 1 (GRA 1), and that under §1.367(a)–3(e) USP enters into a separate gain recognition agreement with respect to the initial transfer of the TFC stock by UST to FA pursuant to the year 3 asset reorganization (GRA 2). Assume further that in year 4 TFC disposes of 10% of the TFD stock pursuant to a transaction that constitutes a triggering event with respect to GRA 1. The disposition of the TFD stock is not a triggering event with respect to GRA 2 because the TFD stock disposed of does not constitute substantially all the assets of TFC. Under paragraphs (j)(1) and (c)(1)(i) of this section, USP must recognize $5x gain (10% of $50x) under GRA 1. Under paragraph (c)(4)(i) and (ii) of this section, as of the date of the initial transfer (with respect to which GRA 1 was filed), the basis of the TFC stock and TFD stock, respectively, is increased by $5x. Under paragraph (c)(1)(i) of this section, the amount of gain subject to GRA 1 is reduced from $50x to $45x. Similarly, because the transferred stock for purposes of GRA 2 is the TFC stock, the amount of gain subject to GRA 2 is reduced from $100x to $95x to reflect the increase to the basis of the TFC stock.

Example 7. Transfer of transferred stock to a foreign corporation pursuant to an asset reorganization. (i) *Facts*. UST wholly owns FA. In year 4, pursuant to a reorganization described in section 368(a)(1)(D), TFC transfers all of the TFD stock to FA in exchange solely for stock of FA. TFC distributes the FA stock to UST pursuant to the plan of reorganization.

(ii) *Analysis*. In general, the year 4 transfer by TFC of the TFD stock to FA and the exchange by UST of the TFC stock for FA stock constitute triggering events under paragraphs (j)(1) and (4) of this section, respectively. However, under paragraph (k)(6)(ii) of this section, the transfers shall not constitute triggering events if UST enters into a new gain recognition agreement with respect to the initial transfer that designates FA as the transferee foreign corporation.

Example 8. Transfer of substantially all the assets of the transferred corporation pursuant to an asset reorganization. (i) *Facts*. In year 4, pursuant to an asset reorganization described in section 368(a)(1)(C), TFD transfers all of its assets to FA in exchange solely for voting stock of FA. TFD distributes the FA voting stock to TFC pursuant to the plan of reorganization.

(ii) *Analysis*. The year 4 transfer by TFD of all its assets to FA and the exchange by TFC of its TFD stock for FA voting stock pursuant to the reorganization constitute triggering events under paragraphs (j)(2) and (j)(1) of this section, respectively. However, under paragraph (k)(6)(iii) of this section, the transfers shall not constitute triggering events if UST enters into a new gain recognition agreement with respect to the initial transfer that designates FA as the transferred corporation. In addition, under paragraph (k)(6)(iii) of this section only the assets of TFD acquired by FA in the asset reorganization shall be treated as assets of the transferred corporation for purposes of the new gain recognition agreement.

Example 9. Complete liquidation of transferred corporation into transferee foreign corporation. (i) *Facts*. UST does not make an election under paragraph (c)(2)(vi) of this section in connection with the gain recognition agreement entered into with respect to the initial transfer. In year 3, TFD distributes all of its assets to TFC pursuant to a complete liquidation to which sections 332 and 337 apply. Under paragraph (k)(8) of this section, UST enters into a new gain recognition agreement with respect to the initial transfer such that the liquidation is not a triggering event. Under paragraph (c)(5)(i) of this section, the new gain recognition agreement is subject to the conditions and requirements of this section to the same extent as the existing gain recognition agreement, except that the transferred stock is no longer subject to the gain recognition agreement because the transferred stock is cancelled by reason of the liquidation. In year 5 TFC disposes of substantially all of the assets received from TFD in the year 3 liquidation.

(ii) *Result*. The year 5 disposition by TFC of substantially all of the assets received from TFD in the year 3 liquidation is a triggering event under paragraph (j)(2) of this section, and therefore UST must recognize the gain subject to the gain recognition agreement. UST must report the gain recognized on an amended return for the taxable year during which the initial transfer occurred. UST must also pay applicable interest on any additional tax due with respect to the gain recognized. Under paragraph (c)(4)(i) of this section, the basis of the TFC stock received by UST in the initial transfer is increased as of the date of the initial transfer by the amount of gain recognized under the gain recognition agreement. The basis of the assets of TFD, however, is not increased.

Example 10. Transfer of transferred stock to foreign corporation in section 351 exchange, followed by a section 332 liquidation of the foreign corporation. (i) *Facts*. In year 3, pursuant to a section 351 exchange, TFC transfers the TFD stock to F1, a newly formed corporation, in exchange solely for voting stock of F1. The transfer by TFC of the TFD stock to F1 is not a triggering event because UST complies with the conditions of paragraph (k)(3) of this section. In year 5, F1 distributes all of its assets to TFC in a complete liquidation to which sections 332 and 337 apply.

(ii) *Result*. The distribution of the TFD stock by F1, and the exchange of F1 stock by TFC pursuant to the year 5 liquidation of F1 constitute triggering events under paragraphs (j)(1) and (k)(3)(i) of this section, respectively. However, if paragraph (k)(14) of this section applies, neither the distribution of the TFD stock by F1, nor the exchange by TFC of the F1 stock, shall constitute a triggering event.

(A) The condition of paragraph (k)(14)(i) of this section is satisfied because the distribution of the TFD stock, and the exchange of F1 stock, both qualify as nonrecognition transactions.

(B) The condition of paragraph (k)(14)(ii) of this section is satisfied because immediately after the distribution UST, a domestic corporation that is eligible to be a U.S. transferor, owns at least 5% (applying the attribution rules of section 318, as modified by section 958(b)) of the stock of TFC. As a result, UST is treated as retaining an indirect interest in the TFD stock following the complete liquidation of F1.

(C) The condition of paragraph (k)(14)(iii) of this section is satisfied if UST enters into a new gain recognition agreement. Because after the complete liquidation of F1, UST wholly owns TFC, which wholly owns TFD, as was the case immediately after the initial transfer, UST is not required to describe, with the new gain recognition agreement, other dispositions or events that would constitute triggering events based on the principles of paragraph (j) of this section, other than the dispositions or events described in paragraph (j) of this section.

Example 11. Disposition of stock of transferee foreign corporation pursuant to a divisive reorganization. (i) *Facts*. In year 3, pursuant to a divisive reorganization described in section 368(a)(1)(D), UST transfers all of the TFC stock to DC, a newly-formed corporation, in exchange solely for stock of DC. UST then distributes all of the DC stock to USP in a transaction to which section 355 applies.

(ii) *Result*. The transfer of the TFC stock by UST to DC constitutes a triggering event under paragraph (j)(4) of this section. However, under paragraph (k)(1)(iii) of this section, the transfer of the TFC stock shall not constitute a triggering event if DC enters into a new gain recognition agreement that designates DC as the U.S. transferor for purposes of this section.

(iii) *Alternate facts*. The facts are the same as in paragraph (i) of this *Example 11*, except that UST transfers only 90% of the TFC stock to DC. Paragraph (k)(1)(iii) of this section applies only with respect to the TFC stock transferred to DC. Thus, the conditions of paragraph (k)(1)(iii) of this section are satisfied if DC enters into a new gain recognition agreement with respect to the TFC stock received from UST. The amount of gain subject to the new gain recognition agreement entered into by DC equals 90% of the amount of gain subject to the gain recognition agreement entered into by UST with respect to the initial transfer. The amount of gain subject to the gain recognition agreement entered into by UST with respect to the initial transfer is reduced by the amount of gain subject to the new gain recognition agreement entered into by DC. The gain recognition agreement entered into by UST with respect to the initial transfer continues to apply to the remaining TFC stock held by UST.

Example 12. Disposition of transferred stock pursuant to a divisive reorganization. (i) *Facts*. In year 3, pursuant to a divisive reorganization described in section 368(a)(1)(D), TFC transfers all of the TFD stock to F1, a newly formed corporation, in exchange solely for all of the outstanding stock of F1. TFC then distributes all of the F1 stock to UST in a transaction to which section 355 applies.

(ii) *Result*. The transfer by TFC of the TFD stock to F1 constitutes a triggering event under paragraph (j)(1) of this section. However, if paragraph (k)(14) of this section applies, neither the transfer of the TFD stock by TFC to F1, nor the distribution of the F1 stock by TFC to UST, shall constitute triggering events.

(A) The condition of paragraph (k)(14)(i) of this section is satisfied because the dispositions of the TFD stock and F1 stock qualify as nonrecognition transactions.

(B) The condition of paragraph (k)(14)(ii) of this section is satisfied because immediately after the transfer UST, an eligible U.S. transferor, owns at least 5% (applying the attribution rules of section 318, as modified by section 958(b)) of the total voting power and the total fair market value of the outstanding stock of F1. As a result, UST is treated as retaining an indirect interest in the TFD stock following the dispositions.

(C) The condition of paragraph (k)(14)(iii) of this section is satisfied if UST enters into a new gain recognition agreement with respect to the initial transfer that describes the subsequent dispositions or other events that would constitute triggering events based on the principles of paragraph (j) of this section, other than those described in paragraph (j) of this section. For example, a complete or partial disposition of the F1 stock would constitute a triggering event for purposes of the new gain recognition agreement (subject to the exceptions provided by paragraph (k) of this section).

Example 13. *Receipt of boot by the transferee foreign corporation in a subsequent section 351 exchange*. (i) *Facts*. At the time of the initial transfer, the TFD stock has a $50x basis and $100x fair market value. The amount of gain subject to the gain recognition agreement is $50x. In year 3, TFC and X, an unrelated foreign corporation, form F1. TFC transfers the TFD stock to F1 in exchange for $35x cash and $65x stock of F1. At the time of the transfer, the TFD stock has a $50x basis and $100x fair market value. The F1 stock received by TFC represents 25% of the outstanding stock of F1. Without regard to the gain recognized under the gain recognition agreement and any adjustments to basis under paragraph (c)(4)(ii) of this section, under section 351(b) TFC would recognize $35x gain in connection with the transfer of the TFD stock to F1. UST complies with the conditions of paragraph (k)(3) of this section, and therefore the disposition by TFC of the TFD stock does not constitute a triggering event.

(ii) *Result*. Under paragraph (m)(1) of this section, UST must recognize $35x gain under the gain recognition agreement as a result of the year 3 disposition by TFC of the TFD stock. Thus, the amount of gain subject to the new gain recognition agreement entered into by UST pursuant to paragraph (k)(3) of this section is $15x. Under paragraph (c)(4)(ii) of this section, as of the date of the initial transfer, the basis of the TFD stock held by TFC is increased by $35x, the amount of the gain recognized by UST under the gain recognition agreement. Under paragraph (c)(4)(i) of this section, the basis of the TFC stock received by UST in the initial transfer is also increased by $35x. After taking into account the increase to the basis of the TFD stock under paragraph (c)(4)(ii) of this section, TFC recognizes $15x gain under section 351(b) in connection with the year 3 transfer of the TFD stock to F1. Under section 362(a), the basis of the TFD stock in the hands of F1 is $100x.

Example 14. *Complete disposition of transferred stock pursuant to a section 304(a)(1) transaction*. (i) *Facts*. UST wholly owns FA. In year 3, in a transaction to which section 304(a)(1) applies, TFC transfers all of the TFD stock to FA in exchange for cash. Under section 304(a)(1), TFC and FA are treated as if TFC transferred the TFD stock to FA in a section 351 exchange in exchange solely for FA stock, and then FA redeemed the FA stock deemed issued in exchange for the cash. Under section 302(d), the redemption of the FA stock deemed issued by FA to TFC under section 304(a)(1) is treated as a distribution to which section 301 applies.

(ii) *Result*. (A) In general, the deemed contribution by TFC of the TFD stock to FA in the section 351 exchange is a triggering event under paragraph (j)(1) of this section. However, under paragraph (k)(3) of this section the deemed contribution shall not be a triggering event if UST enters into a new gain recognition agreement with respect to the initial transfer in which it agrees to treat as a triggering event a complete or partial disposition of the FA stock deemed received by TFC.

(B) Under paragraph (n)(1) of this section, the redemption of the FA stock deemed received by TFC in exchange for the TFD stock shall not constitute a disposition if UST enters into a new gain recognition agreement with respect to the initial transfer that includes appropriate provisions to take into account such redemption. Therefore, under the new gain recognition agreement UST must agree to treat as a triggering event a complete or partial disposition of the stock of FA. Pursuant to paragraph (d)(2)(ii) of this section, UST is permitted to enter into a single new gain recognition agreement in year 3, but the gain recognition agreement must provide a complete description of the section 304(a)(1) transaction including the deemed section 351 exchange and redemption of the FA stock.

Example 15. *Reduction in amount of gain subject to gain recognition agreement, followed by triggering event*. (i) *Facts*. In year 3, UST disposes of 60% of the TFC stock received in the initial transfer in a transaction in which the conditions of paragraph (o)(1)(ii) of this section are satisfied. Thus, the amount of gain subject to the gain recognition agreement is reduced by 60%. In year 5, TFC disposes of 50% of the TFD stock in a transaction that constitutes a triggering event.

(ii) *Result*. As a result of the year 5 disposition by TFC of 50% of the TFD stock, under paragraphs (j)(1) and (c)(1)(i) of this section, UST must recognize and include in income 50% of the gain subject to the gain recognition agreement (because of the year 3 disposition of TFC stock, the amount of gain subject to the gain recognition agreement equals 40% of the gain realized, but not recognized, on the initial transfer). UST must pay applicable interest on any additional tax due with respect to the gain recognized. The amount of gain subject to the gain recognition agreement is reduced by the amount of gain recognized by UST (the remaining gain equals 20% of the gain realized, but not recognized, by UST on the initial transfer).

Example 16. *Taxable sale of stock of transferee foreign corporation and election to reduce stock basis*. (i) *Facts*. UST wholly owns F1 and TFD. The F1 stock has a $100x basis and $90x fair market value, and the TFD stock has a $0x basis and $100x fair market value. UST also owns real property with a $10x basis and $10x fair market value. In year 1, pursuant to a section 351 exchange, UST transfers the real property, the TFD stock, and the F1 stock to TFC in exchange solely for 20 shares of TFC stock. UST enters into a gain recognition agreement with respect to the transfer of the TFD stock. The amount of the gain recognition agreement is $100x. UST takes the position that the basis of each share of TFC stock received in the exchange is $5.5x (a proportionate amount of the $110x aggregate basis of the transferred property). In year 3, UST disposes of all its TFC stock in a transaction in which all gain realized is recognized and included in taxable income.

(ii) *Result*. The year 3 disposition of the TFC stock is a triggering event under paragraph (j)(4) of this section. The disposition does not terminate the gain recognition agreement pursuant to paragraph (o)(1)(i) of this section because the basis of each share of TFC stock received in exchange for the TFD stock in the initial transfer is $5.5x, which exceeds the $0x basis of the TFD stock at time of the initial transfer. However, under paragraph (o)(1)(iii) of this section, to satisfy the basis condition of paragraph (o)(1)(i) of this section, UST can reduce the basis of the 10 shares of the TFC stock received in exchange for the TFD stock to $0x. If UST reduces the basis of the 10 shares of TFC stock to $0x, under paragraph (o)(1)(i) of this section the disposition of the TFC stock shall not constitute a triggering event but instead shall terminate the gain recognition agreement without further effect.

Example 17. *Successive section 351 exchanges, section 301 distributions, and transactions involving partnerships*. (i) *Facts*. UST owns a 40 percent capital and profits interest in a foreign partnership (PRS). PRS wholly owns TFD and other assets with basis equal to fair market value. The TFD stock has a $50x basis and $200x fair market value. TFC wholly owns F1. On day 1 of year 1, in a section 351 exchange, UST transfers its PRS interest to TFC in exchange solely for stock of TFC (initial transfer). On that same day, in a section 351 exchange, TFC transfers the PRS interest received from UST to F1 in exchange solely for stock of F1. In year 3, PRS receives a $150x distribution from TFD to which section 301 applies. Under section 301(c), $25x of the distribution constitutes a dividend, $50x is applied against and reduces the basis of the TFD stock held by PRS, and the remaining $75x is treated as gain from the sale or exchange of property. With respect to the TFD stock deemed transferred by UST in the initial transfer, under section 301(c), $10x (40% of $25x) of the distribution constitutes a dividend, $20x (40% of $50x) is applied against and reduces the basis of TFD stock, and $30x (40% of $75x) is treated as gain from the sale or exchange of property. In year 5, pursuant to a distribution to which section 731 applies, PRS distributes all of the TFD stock to F1.

(ii) *Result*. (A) *Successive section 351 transfers*. Under section 367(a)(4) and §1.367(a)–1T(c)(3)(ii), the transfer of the PRS interest by UST to TFC is treated, for purposes of section 367(a), as a transfer by UST to TFC of its proportionate share of the TFD stock held by PRS (the initial transfer). The initial transfer by UST of the TFD stock to TFC is subject to the general rule of section 367(a)(1), unless UST enters into a gain recognition agreement with respect to such transfer pursuant to §1.367(a)–3(b)(1)(ii) and this section. Under paragraph (c)(3)(viii) of this section, the gain recognition agreement must include a complete description of the transfer, including a description of the partners of PRS. Even if UST enters into a gain recognition agreement with respect to the initial transfer, under paragraph (j)(3) of this section, the subsequent transfer by TFC of the PRS interest to F1 is a triggering event unless UST enters into a new gain recognition agreement with respect to the initial transfer under paragraph (k)(14) that provides that, in addition to the triggering events provided in paragraph (j) of this section, a complete or partial disposition of the F1 stock received by TFC in exchange for the PRS interest shall constitute a triggering event for purposes of the gain recognition agreement. The new gain recognition agreement must also provide that any other disposition that is inconsistent with the principles of paragraph (k), including an indirect disposition of the TFD stock or of substantially all of the assets of TFD, shall constitute a triggering event for purposes of the new gain recognition agreement. Under paragraph (d)(2)(ii) of this section, UST is permitted to enter into a single gain recognition agreement with respect to the initial transfer and the subsequent transfer by TFC of the PRS interest, but the agreement must include a complete description of the initial transfer and the subsequent transfer of the PRS interest.

(B) *Section 301 distribution from TFD to PRS*. Under paragraph (b)(1)(iii) of this section, the section 301 distribution received by PRS from TFD is not a disposition (and therefore does not affect the gain recognition agreement) to the extent it is described in section 301(c)(1) or (2). However, under paragraph (n)(2) of this section, to the extent the distribution is described in section 301(c)(3), UST must recognize gain ($30x) under the gain recognition agreement. For this purpose, the amount of the distribution that is described in section 301(c)(3) is determined before taking into account the increase to the basis of the TFD stock under paragraph (c)(4)(ii) of this section.

(C) *Distribution of TFD stock by PRS to F1*. The year 5 distribution of the TFD stock by PRS to F1 is a triggering event under paragraph (j)(1) of this section, unless paragraph (k)(14) of this section applies.

(*1*) The condition of paragraph (k)(14)(i) of this section is satisfied because the distribution qualifies as a nonrecognition transaction.

(*2*) The condition of paragraph (k)(14)(ii) of this section is satisfied because immediately after the distribution UST, a domestic corporation that is eligible to be a U.S. transferor, owns at least 5% (applying the attribution rules of section 318, as modified by section 958(b)) of the total voting power and total value of the outstanding stock of F1. As a result, UST is treated as retaining an indirect interest in the TFD stock following the distribution.

(*3*) The condition of paragraph (k)(14)(iii) of this section is satisfied if UST enters into a new gain recognition agreement with respect to the initial transfer. The new gain recognition agreement need not describe additional dispositions or other events that would constitute triggering events because, pursuant to paragraph (c)(5) of this section, the dispositions or other events described in paragraph (j) of this section or in the existing gain recognition agreement apply to the new gain recognition agreement.

Example 18. *Complete liquidation of transferee foreign corporation*. (i) *Facts*. TFD has 10 shares of stock outstanding immediately before the initial transfer. On the date of the initial transfer, the TFD stock has a $0x basis and $90x fair market value. In year 2, in exchange for 1 share of TFD stock TFC transfers real estate to TFD with a $10x basis and $10x fair market value. In year 4, TFC distributes the 11 shares of TFD stock to UST in a complete liquidation to which sections 332 and 337 apply.

(ii) *Result*. In determining whether the gain recognition agreement entered into by UST with respect to the initial transfer is terminated under paragraph (o)(5) of this section, or triggered under paragraphs (j)(1) and (j)(4) of this section, only the 10 shares of TFD stock transferred by UST in the initial transfer are considered. Thus, the 1 share of TFD stock received by TFC in exchange for the real estate in year 2 is not taken into account.

Example 19. *Spin-off of transferred corporation*. (i) *Facts*. Before the initial transfer, the TFD stock has an $80x basis and a $100x fair market value, and the TFC stock has a $100x basis and a $100x fair market value. In year 4, TFC distributes all of the TFD stock to UST in a transaction to which section 355 applies. At the time of the distribution, the TFD stock has a $200x fair market value, and the TFC stock (without regard to the value of the TFD stock held by TFC) has a $100x fair market value. At such time, the TFC stock has a $180x basis. As determined under section 358, immediately after the distribution, the TFC stock has a $60x basis, and the TFD stock has a $120x basis.

(ii) *Result*. The distribution of the TFD stock by TFC in year 4 is a triggering event under paragraph (j)(1) of this section. The distribution does not terminate the gain recognition agreement under paragraph (o)(5) of this section because after the distribution, the basis of the TFD stock in the hands of UST ($120x) is greater than the basis of the TFD stock at the time of the initial transfer ($80x). However, if UST reduces the basis of the TFD stock to $80x (as provided under paragraph (o)(5)(iii) of this section) the gain recognition agreement will terminate without further effect. If UST does not elect to reduce the basis of the TFD stock, see paragraph (k)(14) of this section.

Example 20. *Intercompany transaction followed by disposition to nonmember*. (i) *Facts*. At the time of the initial transfer, the TFD stock has a $50x basis and $100x fair market value. The amount of the gain recognition agreement is $50x. In year 3, UST distributes all of the TFC stock to USP in a transaction to which section 301 applies. At the time of the distribution, the TFC stock has a $50x basis and $90x fair market value. Under section 311(b), UST must recognize $40x gain (the intercompany item) on the distribution, but because the distribution is an intercompany transaction, under the provisions of §1.1502–13, the $40x gain is not taken into account in year 3. In year 4, USP sells all of the TFC stock to X, an unrelated corporation. Under the provisions of §1.1502–13, in year 4 UST takes into account the $40x intercompany item as a result of the sale of the TFC stock to X.

(ii) *Result*. (A) The year 3 distribution of the TFC stock by UST to USP does not terminate the gain recognition agreement under paragraph (o)(1) of this section because UST does not include the $40x gain in taxable income during year 3. Under paragraph (j)(4) of this section, the year 3 distribution of the TFC stock by UST to USP is generally a triggering event; however, because the distribution is an intercompany transaction that creates an intercompany item, the distribution shall not constitute a triggering event if the conditions of paragraph (k)(12)(i) of this section are satisfied.

(1) The condition of paragraph (k)(12)(i)(A) of this section is satisfied because the aggregate basis of the TFC stock distributed ($50x) is not greater than the sum of the aggregate basis of the TFD stock at the time of the initial transfer ($50x).

(2) The condition of paragraph (k)(12)(i)(B) of this section is satisfied if the next annual certification for the existing gain recognition agreement includes a complete description of the intercompany transaction and an explanation of how the basis condition of paragraph (k)(12)(i)(A) of this section is satisfied.

(B) Under paragraph (o)(6) of this section and the principles of paragraph (o)(1)(i) of this section, because the year 4 sale of the TFC stock to X requires UST to take into account the $40x gain (the intercompany item) from the year 3 distribution, the year 4 sale terminates the gain recognition agreement. If, alternatively, in year 4 USP had sold only 30% of the TFC stock, then under paragraph (o)(6) of this section and the principles of paragraph (o)(1)(ii) of this section the amount of gain subject to the gain recognition agreement would be reduced by 30%.

(iii) *Alternate facts*. *Intercompany transaction followed by sale of transferee foreign corporation to member*. Assume the same facts as in paragraph (i) of this *Example 20*, except that, instead of USP selling the TFC stock to X, in year 4 USP sells the TFC stock to USS in exchange for $90x cash. UST and USS are members of the USP consolidated group immediately after the sale. The results of the year 3 distribution of the TFC stock by UST to USP are the same as in paragraph (ii) of this *Example 20*. In addition, under paragraph (k)(12)(ii) of this section, the year 4 sale by USP of the TFC stock to USS is not a triggering event, provided UST includes a complete description of the sale with the annual certification filed for the gain recognition agreement in year 4.

(iv) *Alternate facts*. *Intercompany transaction followed by complete liquidation of transferee foreign corporation*. Assume the same facts as in paragraph (i) of this *Example 20*, except that, instead of USP selling the TFC stock to X, in year 4 TFC distributes all of its assets to USP in a complete liquidation to which sections 332 and 337 apply. The result is the same as in paragraph (ii) of this *Example 20* because, under the provisions of §1.1502–13, in year 4 UST takes into account the $40x gain (the intercompany item) from the year 3 distribution.

(v) *Alternate facts*. *Intercompany transaction followed by triggering event*. Assume the same facts as in paragraph (i) of this *Example 20*, except that instead of USP selling the TFC stock to X, in year 4 TFC disposes of all of the TFD stock in a transaction that constitutes a triggering event under paragraph (j)(1) of this section. Under paragraph (c)(1)(i) of this section UST must recognize $50x gain under the gain recognition agreement. Under paragraphs (c)(4)(i) and (ii) of this section, as of the date of the initial transfer the basis of the TFC stock and TFD stock, respectively, is increased by $50x.

(vi) *Alternate facts*. *Intercompany transaction followed by section 351 transfer to member*. The facts are the same as in paragraph (i) of this *Example 20*, except that, in year 3, in a section 351 exchange UST transfers all of the TFC stock to USS in exchange for $10x cash and $80x of stock of USS. USS is a member of the USP consolidated group immediately after the exchange. The transfer of the TFC stock by UST to USS is an intercompany transaction. Under section 351(b), UST must generally recognize $10x gain (intercompany item) in connection with the transfer; however, under the provisions of §1.1502–13, UST does not take the $10x gain into account in year 3. Under paragraph (k)(12) of this section, as result of the intercompany transaction creating an intercompany item ($10x gain), the existing gain recognition agreement ($50x gain) must be divided between UST and USS. UST shall remain subject to a gain recognition agreement of $10x (equal to the amount of the intercompany item). The amount of the gain recognition agreement entered into by USS under paragraph (k)(1) of this section is $40x (equal to the amount of the existing gain recognition agreement, reduced by the amount of the of the gain recognition agreement to which UST remains subject).

Example 21. *Transfer of transferred stock to United States person other than U.S. transferor*. (i) *Facts*. An individual (A) that is a United States citizen wholly owns TFD, TFC, and DC. A transfers the TFD stock to TFC in a section 351 exchange and enters into a gain recognition agreement with respect to such transfer. In year 5, pursuant to an asset reorganization, TFC transfers all of its assets to DC in exchange solely for DC stock. TFC distributes the DC stock to A pursuant to the plan of reorganization.

(ii) *Result*. The transfer by TFC of the TFD stock to DC and the exchange by A of the TFC stock for DC stock pursuant to the asset reorganization are triggering events under paragraphs (j)(1) and (j)(4) of this section, respectively. The gain recognition agreement does not terminate under paragraph (o)(5) of this section because DC is neither the U.S. transferor, nor an individual that is a United States person, nor a member of the same consolidated group of which the U.S. transferor is a member. However, if paragraph (k)(14) of this section applies the exchanges shall not constitute triggering events.

(A) The condition of paragraph (k)(14)(i) of this section is satisfied because the transfer of the TFD stock to DC qualifies as a nonrecognition transaction.

(B) The condition of paragraph (k)(14)(ii) of this section is satisfied because immediately after the transfer DC, a domestic corporation that is eligible to be a U.S. transferor, retains a direct interest in the TFD stock following the transfer.

(C) The condition of paragraph (k)(14)(iii) of this section is satisfied if DC enters into a new gain recognition agreement with respect to the initial transfer. Under paragraph (k)(14)(iii)(B) of this section, DC is not required to describe any subsequent dispositions or other events that (based on the principles of paragraph (j) of this section) would constitute triggering events for purposes of the new gain recognition agreement, other than the dispositions or other events described in paragraph (j) of this section, because DC holds a direct interest in TFD after the asset reorganization.

Example 22. *Transfer of transferred stock to consolidated group member*. (i) *Facts*. UST wholly owns DC, a member of the USP consolidated group that includes UST. In year 5, pursuant to an asset reorganization described in section 368(a)(1)(A) TFC merges with and into DC. Immediately after the asset reorganization, DC wholly owns TFD, and the basis of the TFD stock is not greater than the aggregate basis of such stock at the time of the initial transfer.

(ii) *Result*. The gain recognition agreement filed by UST with respect to the initial transfer terminates without further effect if the conditions of paragraph (o)(5) of this section are satisfied.

(A) The condition of paragraph (o)(5)(i) of this section is satisfied because the transfer of the TFD stock is a section 361 exchange.

(B) The condition of paragraph (o)(5)(ii) of this section is satisfied because DC is a member of the consolidated group that includes UST immediately after the section 361 exchange.

(C) The condition of paragraph (o)(5)(iii) of this section is satisfied because the aggregate basis of the TFD stock immediately after the section 361 exchange is not greater than the aggregate basis of the TFD stock at the time of the initial transfer (as adjusted for any gain recognized by UST on such transfer). If the basis condition of paragraph (o)(5)(iii) were not satisfied, under paragraph (o)(5)(iii) of this section, DC could reduce the basis of the TFD stock received in the reorganization. Alternatively, a new gain recognition agreement could be entered into if paragraph (k)(14) of this section applied to the disposition of the TFD stock pursuant to the section 361 exchange.

(iii) *Alternate facts*. The facts are the same as in paragraph (i) of this *Example 22*, except that instead of TFC merging into DC, TFC merges into TFD in a reorganization described in section 368(a)(1)(A). The gain recognition agreement terminates without further effect if the conditions of paragraph (o)(5) of this section are satisfied.

(A) The condition of paragraph (o)(5)(i) of this section is satisfied because the TFD stock issued by TFD to TFC in the reorganization, which is treated as transferred stock under paragraph (b)(2)(iii) of this section, is distributed by TFC to UST pursuant to section 361(c).

(B) The condition of paragraph (o)(5)(ii) of this section is satisfied because UST is the U.S. transferor.

(C) The condition of paragraph (o)(5)(iii) of this section is satisfied if the aggregate basis of the TFD stock received by UST from TFC is not greater than the aggregate basis of the TFD stock at the time of the initial transfer (as adjusted for any gain recognized by UST on such transfer). If the basis condition of paragraph (o)(5)(iii) were not satisfied, under paragraph (o)(5)(iii) of this section, UST could reduce the basis of the TFD stock received in the reorganization.

Example 23. *Split-off of transferred stock*. (i) *Facts*. X, a domestic corporation that is unrelated to USP and UST, wholly owns TFC. Pursuant to a reorganization described in section 368(a)(1)(B), UST transfers all of the TFD stock to TFC in exchange for 50% of the outstanding voting stock of TFC. UST enters into a gain recognition agreement with respect to such transfer. In year 4, in a split-off transaction to which section 355 applies, TFC distributes all of the TFD stock to X in exchange for all the TFC stock held by X.

(ii) *Result*. Under paragraph (j)(1) of this section, the year 4 distribution of the TFD stock to X constitutes a triggering event. However, the distribution shall not constitute a triggering event if paragraph (k)(14) of this section applies. The gain recognition agreement does not terminate under paragraph (o)(5) of this section because X is not a recipient described in paragraph (o)(5)(ii) of this section.

(A) The condition of paragraph (k)(14)(i) of this section is satisfied because the distribution of the TFD stock qualifies as a nonrecognition transaction.

(B) The condition of paragraph (k)(14)(ii) of this section is satisfied because immediately after the distribution X, a domestic corporation that is eligible to be a U.S. transferor, retains a direct interest in the TFD stock.

(C) The condition of paragraph (k)(14)(iii) of this section is satisfied if X enters into a new gain recognition agreement with respect to the initial transfer. Under paragraph (k)(14)(iii)(B) of this section, X is not required to describe, with the new gain recognition agreement, any subsequent dispositions or other events that (based on the principles of paragraph (j) of this section) would constitute triggering events, other than the dispositions described in paragraph (j) of this section, because X directly owns TFD after the distribution.

(D) If X were a United States citizen, the gain recognition agreement would terminate if the condition of paragraph (o)(5)(iii) of this section were satisfied. Alternatively, the gain recognition agreement would continue for its remaining term if the conditions for the application of paragraph (k)(14) of this section were satisfied.

(iii) *Alternate facts*. *Distribution to unrelated foreign corporation*. The facts are the same as in paragraph (i) of this *Example 23*, except that X is a foreign corporation wholly owned by DC. DC is unrelated to UST. The results are the same as in paragraph (ii) of this *Example 23*, except as follows.

(A) The condition of paragraph (k)(14)(ii) of this section is satisfied because immediately after the distribution DC, a domestic corporation that is eligible to be a U.S. transferor, owns at least 5% (applying the attribution rules of section 318, as modified by section 958(b)) of the total voting power and total value of the outstanding stock of X. As a result, DC is treated as retaining an indirect interest in the TFD stock immediately following the distribution.

(B) The condition of paragraph (k)(14)(iii) of this section is satisfied if DC enters into a new gain recognition agreement with respect to the initial transfer. Under paragraph (k)(14)(iii)(B) of this section, DC must, in addition to the dispositions described in paragraph (j) of this section, include as a triggering event a complete or partial disposition of the stock of X.

(iv) *Alternate facts*. *Distribution to nonresident alien individual*. The facts are the same as in paragraph (i) of this *Example 23*, except that X is a nonresident alien individual. Paragraph (k)(14) of this section does not apply to the distribution because the conditions of paragraph (k)(14)(ii) and (iii) of this section cannot be satisfied. Therefore, the distribution is a triggering event, and UST will recognize gain under the gain recognition agreement as required under paragraphs (c)(1)(i) and (v) of this section. The result would be the same if X were a foreign corporation and, immediately after the distribution, no United States person owned at least 5% (applying the attribution rules of section 318, as modified by section 958(b)) of the total voting power and value of the outstanding stock of X.

Example 24. *Applicability of this section to gain recognition agreements filed before* March 13, 2009. (i) *Facts*. The facts are the same as in paragraph (i) of *Example 6*, except that the initial transfer occurred on March 7, 2007, and the asset reorganization occurred on July 1, 2008.

(ii) *Result*. Under paragraph (r)(1)(ii) of this section, the rules of §1.367(a)–8T (see 26 CFR part 1, revised April 1, 2007) apply to the transfers pursuant to the asset reorganization because the initial transfer occurred on March 7, 2007. As a result of the disposition of the TFC stock pursuant to the asset reorganization, under §1.367(a)–8T(d), USP is required to recognize the gain subject to the gain recognition agreement and pay applicable interest on any additional tax due with respect to such gain. Because the acquiring corporation in the asset reorganization is foreign, an exception under §1.367(a)–8T(e) is not available for the exchange of TFC stock by USP. However, pursuant to paragraph (r)(2)(i) of this section, because the exception provided by paragraph (k)(14) of this section is not included in §1.367(a)–8T, USP may apply paragraph (k)(14) of this section to such exchange (provided the conditions of paragraph (k)(14) of this section are satisfied), if the statute of limitations on assessments of tax for the 2007 tax year has not closed. If USP applies paragraph (k)(14) of this section to its exchange of the TFC stock pursuant to the asset reorganization, under paragraph (r)(2)(ii) of this section USP must include the new gain recognition agreement required under paragraph (k)(14)(iii) of this section with an amended Federal income tax return for its 2008 tax year that is filed before August 10, 2009.

Example 25. Applicability of this section to gain recognition agreements filed before March 13, 2009. (i) *Facts*. The initial transfer occurs in 2004. In 2005, pursuant to a section 351 exchange, TFC transfers the TFD stock to F1 in exchange solely for F1 voting stock. UST does not file a new gain recognition agreement under §1.367(a)–8(g)(2) with respect to the exchange.

(ii) *Result*. Under paragraph (r)(1)(ii) of this section, the rules of §1.367(a)–8 (see 26 CFR part 1, revised April 1, 2006) apply to the year 2005 disposition of the TFD stock because UST filed the gain recognition agreement after July 20, 1998, but before March 7, 2007. Under §1.367(a)–8(e) (see 26 CFR part 1, revised April 1, 2006), as a result of the disposition of the TFD stock by TFC, UST must recognize the amount of gain subject to the gain recognition agreement. Paragraph (r)(2)(i) of this section does not apply because the rule provided by paragraph (k)(3) of this section was included in §1.367(a)–8(g)(2) (see 26 CFR part 1, revised April 1, 2006). However, UST may request relief for reasonable cause under §1.367(a)–8(c)(2) (see 26 CFR part 1, revised April 1, 2006) to file a new gain recognition agreement with respect to the disposition of the TFD stock by TFC in 2005.

(r) *Effective/applicability date*—(1) *General rule*—(i) *Transfers occurring on or after* March 13, 2009. The rules of this section apply to gain recognition agreements filed with respect to transfers of stock or securities occurring on or after March 13, 2009. However, the rules of this section do not apply to gain recognition agreements filed with respect to any such transfer occurring on or after March 13, 2009, if such transfer was entered into pursuant to a written agreement that was (subject to customary conditions) binding before February 11, 2009, and at all times thereafter. Solely for purposes of this paragraph (r), a transfer described in the preceding sentence shall be deemed to be a transfer occurring before March 13, 2009 to which the rules of §1.367(a)–8 (see 26 CFR part 1, revised April 1, 2006) apply. See paragraph (r)(2)(iii) of this section for the ability to apply the rules of this section with respect to gain recognition agreements filed for taxable years ending before March 13, 2009.

(ii) *Transfers occurring before March 13, 2009*. For matters covered in this section for periods before March 13, 2009 but on or after March 7, 2007, the corresponding rules of §1.367(a)–8T (see 26 CFR part 1, revised April 1, 2007) apply. For matters covered in this section for periods before March 7, 2007 but on or after July 20, 1998, the corresponding rules of §1.367(a)–8 (see 26 CFR part 1, revised April 1, 2006) apply. For matters covered in this section for periods before July 20, 1998, the corresponding rules of §1.367(a)–3T(g) (see 26 CFR part 1, revised April 1, 1998) and Notice 87–85, 1987–2 C.B. 395 apply. In addition, if a U.S. transferor entered into a gain recognition agreement for transfers before July 20, 1998, then the rules of §1.367(a)–3T(g) (see 26 CFR part 1, revised April 1, 1998) continue to apply in lieu of this section in the event of any direct or indirect nonrecognition transfer of the same property. See also, §1.367(a)–3(h).

(2) *Applicability to gain recognition agreements filed before March 13, 2009*—(i) *General rule*. Taxpayers may apply the rules of this regulation §1.367(a)–8 that were not included in §1.367(a)–8T (see 26 CFR part 1, revised April 1, 2007), to gain recognition agreements filed with respect to transfers of stock or securities for all open taxable years, if done consistently to all transfers. A U.S. transferor subject to section 877 and §1.367(a)–8T(d)(6) shall not apply the rules of this regulation to reach a contrary result. A taxpayer that failed to file a gain recognition agreement for a transfer, or to comply materially with any requirement of this section with respect to an existing gain recognition agreement, must obtain relief for reasonable cause for such failure under §1.367(a)–8T(e)(10) before applying the rules of this regulation §1.367(a)–8 that were not included in §1.367(a)–8T as permitted by this paragraph (r)(2). See paragraph (q)(2) of this section, *Examples 24* and *25* for illustrations of the rule provided by this paragraph (r)(2)(i).

(ii) *Taxable years ending before March 13, 2009*. Notwithstanding the requirements of §1.367(a)–8(d), any gain recognition agreement or other filing required by reason of electing to apply the rules of this regulation §1.367(a)–8 that were not included in §1.367(a)–8T, as permitted by this paragraph (r)(2), for a taxable year ending before March 13, 2009 shall be considered filed in accordance with the requirements of §1.367(a)–8(d), provided the gain recognition agreement or other filing is attached to an original or amended return for such taxable year. An amended return required to be filed by reason of electing to apply the rules of this regulation §1.367(a)–8 that were not included in §1.367(a)–8T, as permitted by this paragraph (r)(2), must be filed on or before August 10, 2009. A taxpayer that wishes to apply the rules of this regulation §1.367(a)–8 that were not included in §1.367(a)–8T, as permitted by this paragraph (r)(2), but that fails to meet the filing requirement described in the preceding sentence must request relief for reasonable cause under paragraph (p) of this section.

(iii) *Taxable years ending after effective date*. A taxpayer that entered into a gain recognition agreement to which §1.367(a)–8T (see 26 CFR part 1, revised April 1, 2007) applies may apply the rules of this section in a tax year ending on or after March 13, 2009 by attaching the agreement, certification, or other information related to such gain recognition agreement that the rules of this section require in accordance with the rules of this section and with the time and manner rules provided in §1.367(a)–8(d).

§1.367(a)–8T [Removed]

Par. 8. Section 1.367(a)–8T is removed.

PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Par. 9. The authority citation for part 602 continues to read as follows:

Authority: 26 U.S.C. 7805 * * *

Par. 10. In §602.101, paragraph (b) is amended by removing an entry for §1.367(a)–8T from the table and adding an entry for §1.367(a)–8 to the table in numerical order to read as follows:

§602.101 OMB Control numbers.

* * * * *

(b) * * *

CFR part or section where identified and described		Current OMB Control No.
* * * * *		
1.367(a)–8	. . . .	1545–2056
* * * * *		

Linda E. Stiff,
Deputy Commissioner for Services and Enforcement.

Approved January 16, 2009.

Eric Solomon,
Assistant Secretary of the Treasury (Tax Policy).

(Filed by the Office of the Federal Register on February 9, 2009, 11:15 a.m., and published in the issue of the Federal Register for February 11, 2009, 74 F.R. 6951)

Section 3406.—Backup Withholding

Entities required to report under section 6050W must perform backup withholding if the payee fails to furnish a correct Taxpayer Identification Number ("TIN"). This announcement alerts 6050W filers that they may now partificipate in the TIN matching program. See Announcement 2009-6, page 643.

Section 6050W.—Returns Relating to Payments Made in Settlement of Payment Card and Third Party Network Transactions

Entities required to report under section 6050W must perform backup withholding if the payee fails to furnish a correct Taxpayer Identification Number ("TIN"). This announcement alerts 6050W filers that they may now partificipate in the TIN matching program. See Announcement 2009-6, page 643.

Section 6103.—Confidentiality and Disclosure of Returns and Return Information

26 CFR 301.6103(p)(7)–1: Procedures for administrative review of a determination that an authorized recipient has failed to safeguard returns or return information.

T.D. 9445

DEPARTMENT OF THE TREASURY
Internal Revenue Service
26 CFR Part 301

Procedures for Administrative Review of a Determination That an Authorized Recipient Has Failed to Safeguard Tax Returns or Return Information

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations and removal of temporary regulations.

SUMMARY: This document contains final regulations regarding administrative review procedures for certain government agencies and other authorized recipients of returns or return information whose receipt of returns and return information may be suspended or terminated because they do not maintain proper safeguards. The regulations provide guidance to responsible IRS personnel and authorized recipients as to these administrative procedures.

DATES: *Effective Date:* These regulations are effective on February 11, 2009.

Applicability Date: These regulations apply to all authorized recipients of returns and return information that are subject to the safeguard requirements set forth in section 6103(p)(4) on or after February 11, 2009.

FOR FURTHER INFORMATION CONTACT: Wendy L. Kribell, (202) 622–4570 (not a toll-free number).

Background

This document contains final regulations amending the Procedure and Administration Regulations (26 CFR Part 301) under section 6103(p)(4), (p)(7), and (q) of the Internal Revenue Code (Code). Section 6103 protects returns and return information from disclosure except to certain government agencies and other authorized recipients, including State tax agencies as provided in section 6103(d). Section 6103(p)(4) provides that certain authorized recipients must establish procedures satisfactory to the IRS for safeguarding the returns and return information. The IRS reviews, on a regular basis, safeguards established by these authorized recipients. If the IRS determines that an authorized recipient has failed to maintain adequate safeguards or has made any unauthorized inspections or disclosures of returns or return information, section 6103(p)(4) authorizes the IRS to terminate or suspend disclosure of returns and return information to the authorized recipient until the IRS is satisfied that adequate steps have been taken to ensure adequate safeguards or prevent additional unauthorized inspections or disclosures.

Section 6103(p)(7) requires the Secretary to prescribe regulations providing for administrative review of an IRS determination that a State tax agency has failed to meet the safeguarding requirements. Former §301.6103(p)(7)–1 contained procedures to allow State tax agencies, prior to a suspension or termination of disclosure, to appeal a preliminary finding by the IRS of inadequate safeguards or unauthorized disclosure, or to establish that the agency had taken steps to prevent a recurrence of the violation. Section 6103(q) further authorizes the Secretary to prescribe such other regulations as are necessary to carry out the provisions of section 6103 generally.

On February 24, 2006, the Treasury Department and IRS published in the **Federal Register** proposed regulations (REG–157271–05, 2006–1 C.B. 652 [71 FR 9487]) and temporary regulations (T.D. 9252, 2006–1 C.B. 633 [71 FR 9449]) to extend the administrative review procedure for State tax agencies to "any" authorized recipient specified in section 6103(p)(4), and to include unauthorized inspection within the IRS's scope of review (in addition to inadequate safeguards and unauthorized disclosure). Two written comments were received, and no public hearing was requested or held. After consideration of the comments received, the proposed regulations are adopted as final regulations, and the corresponding temporary regulations are removed. See §601.601(d)(2)(ii)(*b*).

Explanation and Summary of Comments

The first commentator suggested that the final regulations expressly provide that the IRS may give written notice of its intention to terminate or suspend disclosure via facsimile or electronic mail. This suggestion was not adopted because nothing in the regulations precludes a written notice from being delivered electronically. Not specifying the means by which written notice is conveyed would also afford greater flexibility in providing notice as other means might evolve.

The second commentator suggested that the proposed regulations would legalize the misuse of returns and return information and thereby discourage taxpayers from seeking tax advice. This suggestion is unwarranted. Section 6103 protects returns and return information from disclosure except to authorized recipients. Section 6103(p)(4) requires certain authorized recipients to establish procedures for safeguarding returns and return information. If the authorized recipient fails to maintain adequate safeguards or has made any unauthorized inspections or disclosures, additional disclosures to that recipient may be suspended or terminated until the IRS is satisfied that adequate steps have been taken to ensure adequate safeguards or prevent additional unauthorized inspections or disclosures. Prior to these final regulations, procedures were available pursuant to section 6103(p)(7) to allow State tax agencies, prior to a suspension or termination of disclosure, to appeal a preliminary finding of inadequate safeguards or unauthorized disclosure, or to establish that the agency had taken steps to prevent a recurrence of the violation. The purpose of these final regulations is to extend these administrative review procedures from State tax agencies to all authorized recipients described in section 6103(p)(4) and to include a preliminary finding of unauthorized inspection within the scope of review. The extension of these provisions to all authorized recipients enhances the protections afforded to returns and return information.

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations. Because the regulations do not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant to section 7805(f) of the Internal Revenue Code, the notice of proposed rulemaking preceding these regulations was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small businesses.

Drafting Information

The principal author of these regulations is Wendy L. Kribell, Office of the Associate Chief Counsel (Procedure & Administration).

* * * * *

Adoption of Amendments to the Regulations

Accordingly, 26 CFR Part 301 is amended as follows:

PART 301—PROCEDURE AND ADMINISTRATION

Paragraph 1. The authority citation for part 301 continues to read in part as follows:

Authority: 26 U.S.C. 7805 * * *

Par. 2. Section 301.6103(p)(4)–1 is added to read as follows:

§301.6103(p)(4)–1 Procedures relating to safeguards for returns or return information.

For security guidelines and other safeguards for protecting returns and return information, see guidance published by the Internal Revenue Service. For procedures for administrative review of a determination that an authorized recipient has failed to safeguard returns or return information, see §301.6103(p)(7)–1.

§301.6103(p)(4)–1T [Removed]

Par. 3. Section 301.6103(p)(4)–1T is removed.

Par. 4. Section 301.6103(p)(7)–1 is added to read as follows:

§301.6103(p)(7)–1 Procedures for administrative review of a determination that an authorized recipient has failed to safeguard returns or return information.

(a) *In general*. Notwithstanding any section of the Internal Revenue Code (Code), the Internal Revenue Service (IRS) may terminate or suspend disclosure of returns and return information to any authorized recipient specified in section (p)(4) of section 6103, if the IRS determines that:

(1) The authorized recipient has allowed an unauthorized inspection or disclosure of returns or return information and that the authorized recipient has not taken adequate corrective action to prevent the recurrence of an unauthorized inspection or disclosure; or

(2) The authorized recipient does not satisfactorily maintain the safeguards prescribed by section 6103(p)(4), and has made no adequate plan to improve its system to maintain the safeguards satisfactorily.

(b) *Notice of IRS's intention to terminate or suspend disclosure*. Prior to terminating or suspending authorized disclosures, the IRS will notify the authorized recipient in writing of the IRS's preliminary determination and of the IRS's intention to discontinue disclosure of returns and return information to the authorized recipient. Upon so notifying the authorized recipient, the IRS, if it determines that tax administration otherwise would be seriously impaired, may suspend further disclosures of returns and return information to the authorized recipient pending a final determination by the Commissioner or a Deputy Commissioner described in paragraph (d)(2) of this section.

(c) *Authorized recipient's right to appeal*. An authorized recipient shall have 30 days from the date of receipt of a notice described in paragraph (b) of this section to appeal the preliminary determination described in paragraph (b) of this section. The appeal shall be made directly to the Commissioner.

(d) *Procedures for administrative review*. (1) To appeal a preliminary determination described in paragraph (b) of this section, the authorized recipient shall send a written request for a conference to: Commissioner of Internal Revenue (Attention: SE:S:CLD:GLD), 1111 Constitution Avenue, NW, Washington, DC 20224. The request must include a complete description of the authorized recipient's present system of safeguarding returns or return information received by the authorized recipient (and its authorized contractors or agents, if any). The request must state the reason or reasons the authorized recipient believes that such system or practice (including improvements, if any, to such system or practice expected to be made in the near future) is or will be adequate to safeguard returns or return information.

(2) Within 45 days of the receipt of the request made in accordance with the provisions of paragraph (d)(1) of this section, the Commissioner or Deputy Commissioner personally shall hold a conference with representatives of the authorized recipient, after which the Commissioner or Deputy Commissioner shall make a final determination with respect to the appeal.

(e) *Effective/applicability date*. This section applies to all authorized recipients of returns and return information that are subject to the safeguard requirements set forth in section 6103(p)(4) on or after February 11, 2009.

§301.6103(p)(7)–1T [Removed]

Par. 5. Section 301.6103(p)(7)–1T is removed.

Linda E. Stiff,
Deputy Commissioner for Services and Enforcement.

Approved January 13, 2009.

Eric Solomon,
Assistant Secretary of the Treasury (Tax Policy).

(Filed by the Office of the Federal Register on February 10, 2009, 8:45 a.m., and published in the issue of the Federal Register for February 11, 2009, 74 F.R. 6829)

Section 6109.—Identifying Numbers

Entities required to report under section 6050W must perform backup withholding if the payee fails to furnish a correct Taxpayer Identification Number ("TIN"). This announcement alerts 6050W filers that they may now partificipate in the TIN matching program. See Announcement 2009-6, page 643.

Part IV. Items of General Interest

Notice of Proposed Rulemaking and Notice of Public Hearing

Tax Avoidance Transactions

REG–138326–07

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking and notice of public hearing.

SUMMARY: This document contains proposed regulations under section 6231 of the Internal Revenue Code that allow the IRS to convert partnership items to nonpartnership items when the application of the unified partnership audit and litigation procedures of sections 6221 through 6234 (TEFRA partnership procedures) with respect to certain tax avoidance transactions interferes with the effective and efficient enforcement of the internal revenue laws. The regulations affect taxpayers who have engaged in a listed transaction through an entity subject to the TEFRA partnership procedures. This document also provides notice of a public hearing on these proposed regulations.

DATES: Written or electronic comments must be received by May 14, 2009. Outlines of topics to be discussed at the public hearing scheduled for June 4, 2009, at 10 a.m. must be received by May 15, 2009.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG–138326–07), room 5205, Internal Revenue Service, PO Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand delivered Monday through Friday between the hours of 8 a. m. and 4 p.m. to: CC:PA:LPD:PR (REG–138326–07), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, DC 20224, or sent electronically via the Federal eRulemaking Portal at *http://www.regulations.gov* (IRS REG–138326–07). The public hearing will be held in the Auditorium, Internal Revenue Service Building, 1111 Constitution Avenue, N.W., Washington, DC.

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, Robert T. Wearing at (202) 622–4570; concerning submissions of comments, the hearing, or to be placed on the building access list to attend the hearing, *Richard.A.Hurst@irscounsel.treas.gov* of the Publications and Regulations Branch at (202) 622–7180 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background

This document contains proposed amendments to the Procedure and Administration Regulations (26 CFR Part 301) under section 6231(c) of the Internal Revenue Code. Section 402 of the Tax Equity and Fiscal Responsibility Act of 1982, Public Law 97–248 (96 Stat. 324) added sections 6221 through 6231 to the Internal Revenue Code to provide unified audit and litigation procedures for determining the tax treatment of partnership items at the partnership level rather than at the partner level. Sections 6233 and 6234 were subsequently added by section 714(p)(1) of the Tax Reform Act of 1984, Public Law 98–369 (98 Stat. 494) and section 1231(a) of the Taxpayer Relief Act of 1997, Public Law 105–34 (11 Stat. 788), respectively.

Ordinarily, under the TEFRA partnership procedures, the IRS must adjust a partner's treatment of partnership items only through partnership-level proceedings. There are several exceptions that allow adjustments to be made through partner-level proceedings. The small partnership exception set forth in section 6231(a)(1)(B) provides that partnerships having ten or fewer partners, each of whom is an individual, a C corporation, or an estate, are not subject to the TEFRA partnership procedures. Section 6231(b) provides that items cease to be partnership items subject to the TEFRA partnership procedures in several different situations. Section 6231(c) allows the Treasury Department and the IRS to determine and provide by regulations that treating items as partnership items in areas that present special enforcement considerations will interfere with the effective and efficient enforcement of the internal revenue laws and that, consequently, the items shall be treated as nonpartnership items. Section 6231(c) also allows the Treasury Department and the IRS to prescribe by regulations rules necessary to achieve the purposes of the TEFRA partnership procedures with respect to special enforcement areas. Section 6231(c) lists several specific special enforcement areas, including criminal investigations and indirect methods of proof of income, and provides that the Treasury Department and the IRS may determine others. The Treasury Department and the IRS previously have determined and provided by regulations that bankruptcy, receivership, and prompt assessment requests interfere with the effective and efficient enforcement of the internal revenue laws and designated them as special enforcement areas. See §§301.6231(c)–7 and –8 of the Procedure and Administration Regulations.

Explanation of Provisions

One of the principal purposes behind the enactment of the TEFRA partnership procedures was to provide for the more efficient use of the IRS's resources by reducing multiple proceedings with respect to partnership items. The abusive tax shelters of the 1970s often used a single partnership to generate tax benefits for dozens, if not hundreds, of investors. Before the enactment of the TEFRA partnership procedures, the partnership items of each investor were subject to separate partner-level proceedings. The TEFRA partnership procedures effectively brought the partnership item components of these proceedings together in a single proceeding. Unlike the tax shelters of the 1970s, however, the recent generation of tax avoidance transactions often uses combinations of trusts, S corporations, limited liability companies, partnerships, and other entities, many times arranged in tiers, for the tax benefit of a single investor or a small group of investors. The application of the TEFRA partnership procedures to these tax avoidance transactions often results in multiple proceedings that complicate the ultimate determination of the investors' tax liabilities and consume significant administrative resources.

For example, in a typical transaction described in Notice 2000–44, 2000–2 C.B. 255, (September 5, 2000), see §601.601(d)(2)(ii)(*b*), in which the ultimate noneconomic loss or deduction is taken at the partner level by a single individual, the IRS first needs to initiate timely partnership-level proceedings to determine, among other things, whether the partnership is a sham and the amount and character of contributions and partnership liabilities. Following the partnership-level proceedings, the IRS often still must issue an affected items notice of deficiency to disallow the noneconomic loss or deduction at the partner level. Conducting both entity-level and partner-level proceedings in these cases to determine the tax liabilities of only a single individual or small group of related persons places an unnecessary burden on taxpayers, the IRS, and the federal courts.

Other tax avoidance transactions use multiple tiers of partnerships making coordinated partnership elections for the benefit of a single individual. Two or more separate partnership proceedings, as well as a partner-level proceeding, may need to take place before an assessment can be made against the individual. Again, conducting entity-level proceedings in these and similar cases in which a single individual or small group of related persons control multiple entities and receive all the tax benefits is inefficient and imposes a significant administrative burden.

The need to conduct partnership-level proceedings to determine the tax liabilities of a single individual or small group of related persons also generates complex and burdensome procedural issues that do not contribute to the determination of the individuals' tax liabilities. For example, the application of the TEFRA partnership procedures may raise complicated issues concerning the segregation and aggregation of partnership items, affected items, and nonpartnership items. Often, the TEFRA partnership procedures make the identification and examination of the transactions more complicated and difficult. As a result, the Treasury Department and the IRS have determined that special enforcement considerations, within the meaning of section 6231(c)(1)(E), are present in the case of transactions that the Treasury Department and the IRS have publicly identified as tax avoidance transactions. Specifically, the Treasury Department and the IRS have determined that treating items related to listed transactions within the meaning of §1.6011–4(b)(2) of the Income Tax Regulations as partnership items interferes with the effective and efficient enforcement of the internal revenue laws.

The proposed regulations are limited to tax avoidance transactions that are publicly identified by the Treasury Department and the IRS as listed transactions under §1.6011–4(b)(2) of the Income Tax Regulations. Under the proposed regulations, the transaction must be a listed transaction on the date the IRS sends written notification to the partner that the partner's partnership items will be treated as nonpartnership items. Accordingly, the fact that a transaction becomes a listed transaction after the date on which the taxpayer engages in the transaction does not preclude the conversion of items under the proposed regulations. This limitation promotes taxpayer awareness of the transactions that can subject their partnership items to removal from the TEFRA partnership procedures. The Treasury Department and the IRS also have determined that the limitation will provide for the more efficient use of the IRS's resources.

Under the proposed regulations, the IRS will make determinations regarding whether to convert partnership items to nonpartnership items on a partnership-by-partnership and partner-by-partner basis. Thus, if a taxpayer is a partner in two partnerships with partnership items related to listed transactions and a third partnership that has no partnership items related to listed transactions, the IRS could convert the taxpayer's partnership items in either or both of the first two partnerships but could not convert the taxpayer's partnership items in the third partnership. Similarly, if a taxpayer engages in a listed transaction through a tier of TEFRA entities, the IRS could convert the taxpayer's partnership items in any or all of the tier entities with partnership items related to the listed transaction.

Although, consistent with section 6231(c)(2), the Secretary has determined that treating items related to listed transactions as partnership items will interfere with the effective and efficient enforcement of the internal revenue laws and has so provided in the proposed regulations, the proposed regulations further provide that the partnership items related to listed transactions remain subject to the TEFRA partnership procedures unless and until the IRS sends written notification to the partner that the items will be treated as nonpartnership items. In this regard, the proposed regulations are consistent with the rules that are already in place with respect to sending notices under section 301.6231(c)–5 of the Procedure and Administration Regulations relating to partners under criminal investigation. See *Phillips v. Commissioner*, 272 F.3d 1172, 1176 (9th Cir. 2001). Specifically, the IRS will send written notification under the circumstances described in the proposed regulations using procedures similar to the procedures used under §301.6231(c)–5 of the Procedure and Administration Regulations, and will make conforming changes to the Internal Revenue Manual and Delegation Order 4–19, as necessary.

If the IRS concludes that a particular partner's partnership items should be treated as nonpartnership items under the circumstances described in the proposed regulations, the IRS will send written notification to the partner identifying each partnership for which the partner's partnership items will be treated as nonpartnership items. In the case of an indirect partner (as defined in section 6231(a)(10)) having an interest in a partnership through one or more pass-thru partners (as defined in section 6231(a)(9)), the IRS may send a written notification to the indirect partner identifying only the lower-tier partnership and not the pass-thru partners. In those circumstances, the partnership items attributable to the lower-tier partnership that flow through to the indirect partners will convert to nonpartnership items of the notified partner, even though the pass-thru partners were not identified in the written notification. Any partnership items originating with the pass-thru partners, that is, partnership items that are not attributable to the lower-tier partnership, will not convert to nonpartnership items unless the IRS identifies the pass-thru partner in the written notification (in which case all the partnership items directly attributable to the pass-thru partner also will convert to nonpartnership items of the notified partner).

As of the date that the IRS sends written notification of the conversion to the partner, all of the partner's partnership items attributable to the identified partnership will be treated as nonpartnership items for all of the identified partnership's taxable years that (1) ended on or before the date written notification is sent by the IRS to the partner and (2) for which the partner has items attributable to that partnership that are related to the listed transaction. The deficiency procedures in subchapter B of chapter 63 will apply, pursuant to section 6230(a)(2)(A)(ii), as of the date of the notice.

The proposed regulations incorporate existing rules under §301.6231(c)–3 of the Procedure and Administration Regulations, which provide that the partnership items of a partnership may not be converted if a notice of final partnership administrative adjustment (FPAA) with respect to those partnership items has been mailed to the tax matters partner of the partnership and either (1) the period for bringing an action with respect to the FPAA has expired and no judicial action has been brought or (2) the decision of the court in an action brought with respect to the FPAA has become final. This rule allows the IRS to send notification converting partnership items to nonpartnership items after the commencement of a judicial proceeding related to the converted partnership items. The Treasury Department and the IRS recognize, however, that it is not in the best interest of taxpayers, the Treasury Department, the IRS, or the courts to unnecessarily delay conversion of partnership items to nonpartnership items. Consistent with its existing practices under section 6231(c), the IRS intends to make a decision regarding whether to convert partnership items to nonpartnership items before the commencement of any judicial proceeding, although on isolated and unusual occasions changed circumstances may require the IRS to revisit that decision after the commencement of a judicial proceeding. In addition, judicial doctrines such as collateral estoppel and res judicata may preclude litigating issues in a partner-level proceeding that were previously litigated in a partnership-level proceeding prior to conversion of partnership items to nonpartnership items. Finally, the partnership items of any partners to whom the IRS does not send written notification will not convert to nonpartnership items.

Proposed Effective Date

The regulations, when finalized, are proposed to apply to any taxable period ending on or after the date of publication of these rules as proposed regulations in the **Federal Register**.

Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It has also been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations, and, because these regulations do not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant to section 7805(f) of the Internal Revenue Code, this notice of proposed rulemaking has been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Comments and Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written (a signed original and eight (8) copies) or electronic comments that are submitted timely to the IRS. The Treasury Department and the IRS request comments on the clarity of the proposed rules and how they can be made easier to understand. The Treasury Department and the IRS also request comments that identify additional transactions or activities that present appropriate grounds for converting partnership items to nonpartnership items. All comments will be made available for public inspection and copying.

A public hearing has been scheduled for June 4, 2009, beginning at 10 a.m. in the Auditorium of the Internal Revenue Service Building, 1111 Constitution Avenue, N.W., Washington, DC. Due to building security procedures, visitors must enter at the Constitution Avenue entrance. In addition, all visitors must present photo identification to enter the building. Because of access restrictions, visitors will not be admitted beyond the immediate entrance area more than 30 minutes before the hearing starts. For information about having your name placed on the building access list to attend the hearing, see the "FOR FURTHER INFORMATION CONTACT" section of this preamble.

The rules of 26 CFR 601.601(a)(3) apply to the hearing. Persons who wish to present oral comments at the hearing must submit written or electronic comments and an outline of the topics to be discussed and the time to be devoted to each topic (signed original and eight (8) copies) by May 15, 2009. A period of 10 minutes will be allotted to each person for making comments. An agenda showing the scheduling of the speakers will be prepared after the deadline for receiving outlines has passed. Copies of the agenda will be available free of charge at the hearing.

Drafting Information

The principal author of these regulations is Robert T. Wearing of the Office of the Associate Chief Counsel (Procedure and Administration).

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Proposed Amendments to the Regulations

Accordingly, 26 CFR Part 301 is proposed to be amended as follows:

PART 301—PROCEDURE AND ADMINISTRATION

Paragraph 1. The authority citation for part 301 is amended by adding the entry in numerical order to read in part as follows:

Authority: 26 U.S.C. 7805 * * *

Section 301.6231(c)–9 is also issued under 26 U.S.C. 6230(k) and 6231(c)(1) and (c)(3). * * *

Par. 2. Section 301.6231(c)–3 is amended by revising paragraphs (a) introductory text, and (b) to read as follows:

§301.6231(c)–3 Limitation on applicability of §§301.6231(c)–4 through 301.6231(c)–9.

(a) *In general.* A provision of §§301.6231(c)–4 through 301.6231(c)–9 shall not apply with respect to partnership items arising in a partnership taxable year if, as of the date on which those items would otherwise begin to be treated as nonpartnership items under that provision—

* * * * *

(b) *Effective/applicability date*. The rules of this section, when adopted as final regulations in the **Federal Register**, will apply to partner taxable years ending on or after the date of publication of these proposed regulations in the **Federal Register**.

Par. 3. Section 301.6231(c)–9 is added to read as follows: *§301.6231(c)–9 Tax avoidance transactions.*

(a) *In general*. The treatment of items that relate to a listed transaction, as defined in §1.6011–4, as partnership items will interfere with the effective and efficient enforcement of the internal revenue laws. Accordingly, if a partner has partnership items that relate to a listed transaction and are attributable to a partnership that is identified in a written notification described in this paragraph, the partner's partnership items that are attributable to the identified partnership shall be treated as nonpartnership items as of the date on which the written notification is sent by the Internal Revenue Service to the partner. The determination whether to treat the partnership items of a partner as nonpartnership items shall be made by the Internal Revenue Service on a partnership-by-partnership and partner-by-partner basis. The partnership items of a partner shall not be treated as nonpartnership items under this section unless and until the Internal Revenue Service sends the partner written notification that the partner's partnership items attributable to the identified partnership will be treated as nonpartnership items. The written notification shall identify each partnership in which the partner holds an interest, directly or indirectly, with respect to which all the partner's partnership items will be treated as nonpartnership items. All partnership items of a partner that are attributable to a partnership that is identified in a written notification shall be treated as nonpartnership items for all taxable years of the identified partnership ending on or before the date the Internal Revenue Service sends written notification to the partner in which the partner has partnership items attributable to the identified partnership that relate to the listed transaction. Partnership items of a partner that are attributable to a partnership that is not identified in a written notification sent by the Internal Revenue Service to that partner shall not be treated as nonpartnership items of the notified partner, except that if the notified partner holds an interest in the identified partnership through one or more pass-thru partners (as defined in section 6231(a)(9)), the partnership items attributable to the identified partnership that flow through the pass-thru partners to the indirect partners (as defined in section 6231(a)(10)), will be treated as nonpartnership items of the notified partner even if the written notification does not identify the pass-thru partners.

(b) *Examples*. The provisions of this section may be illustrated by the following examples:

Example 1. PS1 and PS2 are unrelated partnerships subject to the provisions of subchapter C, chapter 63 of the Internal Revenue Code. A is one of the partners of PS1 and one of the partners of PS2. PS1 and PS2 have partnership items that relate to a listed transaction, as defined in §1.6011–4(b)(2). The IRS sends written notification to A that his partnership items in PS1 will be treated as nonpartnership items, but the IRS does not send written notification to A that his partnership items in PS2 will be treated as nonpartnership items. As a result, A's partnership items in PS1 are treated as nonpartnership items as of the date that the IRS sent written notification of the conversion to A, and A's partnership items in PS2 remain as partnership items.

Example 2. PS3 and PS4 are partnerships subject to the provisions of subchapter C, chapter 63 of the Internal Revenue Code. B is one of the partners of PS3 and PS3 is one of the partners of PS4. B is an indirect partner in PS4 within the meaning of section 6231(a)(10). Both PS3 and PS4 have partnership items related to a listed transaction, as defined in §1.6011–4(b)(2). The IRS sends written notification to B that his partnership items in PS4 will be treated as nonpartnership items. As a result, all of B's partnership items flowing from PS4 are treated as nonpartnership items of B as of the date that the IRS sent written notification of the conversion to B. However, since the IRS did not send written notification to B that his partnership items in PS3 will be treated as nonpartnership items, B's partnership items in PS3 that are not attributable to PS4 will remain partnership items.

(c) *Effective/applicability date*. The rules of this section, when adopted as final regulations in the **Federal Register**, will apply to partner taxable years ending on or after the date of publication of these proposed regulations in the **Federal Register**.

Linda M. Kroening,
Deputy Commissioner for Services and Enforcement.

(Filed by the Office of the Federal Register on February 12, 2009, 8:45 a.m., and published in the issue of the Federal Register for February 13, 2009, 74 F.R. 7205)

Notice of Proposed Rulemaking by Cross-Reference to Temporary Regulations

Application of Section 367 to a Section 351 Exchange Resulting from a Transaction Described in Section 304(a)(1); Treatment of Gain Recognized Under Section 301(c)(3) for Purposes of Section 1248

REG–147636–08

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking by cross-reference to temporary regulations.

SUMMARY: In this issue of the Bulletin, the IRS and Treasury Department are issuing temporary regulations (T.D. 9444) under sections 304 and 1248 of the Internal Revenue Code (Code). The temporary regulations provide rules under section 367(a) and (b) that apply to certain transfers of stock by a United States person to a foreign corporation described in section 304(a)(1). The temporary regulations under section 1248(a) provide that, for purposes of section 1248(a), gain recognized by a shareholder under section 301(c)(3) in connection with the receipt of a distribution of property from a foreign corporation with respect to its stock shall be treated as gain from the sale or exchange of the stock of such foreign corporation. The temporary regulations affect certain shareholders that transfer stock in a corporation to a foreign corporation in a transaction to which section 304(a)(1) applies, or that receive a distribution from a foreign corporation described in section 301(c)(3). The text of the temporary regulations also serves as the text of these proposed regulations. The preamble to the temporary regulations explains the temporary regulations and these proposed regulations.

DATES: Written or electronic comments and requests for a public hearing must be received by May 11, 2009.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG–147636–08), room 5205, Internal Revenue Service, PO Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to CC:PA:LPD:PR (REG–147636–08), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, DC, or sent electronically via the Federal eRulemaking Portal at *www.regulations.gov* (IRS REG–147636–08).

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, Sean W. Mullaney, (202) 622–3860; concerning submissions of comments or requests for a public hearing, *Richard.A.Hurst@irscounsel.treas.gov*; at (202) 622–7180 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background and Explanation of Provisions

Temporary regulations in this issue of the Bulletin amend the Income Tax Regulations (26 CFR part 1) relating to sections 304 and 1248 of the Code. The text of those regulations also serves as the text of these proposed regulations. The preamble to the temporary regulations explains the temporary regulations and these proposed regulations.

Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. These regulations are necessary to ensure that the appropriate amount of income (dividend income, capital gain or both) is recognized currently in the transactions described in the explanation of provisions section in this preamble. Accordingly, good cause is found for dispensing with notice and public comment pursuant to 5 U.S.C. 553(b) and (c) and with a delayed effective date pursuant to 5 U.S.C. 553(d). For applicability of the Regulatory Flexibility Act, see the cross-referenced notice of proposed rulemaking published elsewhere in this **Federal Register**. Pursuant to section 7805(f) of the Code, these regulations have been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Comments and Requests for a Public Hearing

Comments are also requested regarding whether IRS and Treasury Department should exercise the regulatory authority under section 304(b)(6) to permit an increase to the basis of the transferred stock in a section 304(a)(1) transaction to the extent the distribution in redemption of the shares deemed issued by the acquiring corporation is treated as a dividend from the earnings and profits of the issuing corporation.

Before these proposed regulations are adopted as final regulations, consideration will be given to any written comments (a signed original and eight (8) copies) or electronic comments that are submitted timely to the IRS. The IRS and Treasury Department specifically request comments on the clarity of the proposed rules and how they can be made easier to understand. All comments will be available for public inspection and copying. A public hearing will be scheduled if requested in writing by any person that timely submits written comments. If a public hearing is scheduled, notice of the date, time, and place for the public hearing will be published in the **Federal Register**.

Drafting Information

The principal author of these proposed regulations is Sean W. Mullaney of the Office of Associate Chief Counsel (International). However, other personnel from the IRS and the Treasury Department participated in their development.

* * * * *

Proposed Amendments to the Regulations

Accordingly, 26 CFR part 1 is proposed to be amended as follows:

PART 1—INCOME TAXES

Paragraph 1. The authority citation for part 1 is amended by adding an entry to read as follows:

Authority: 26 U.S.C. 7805* * *

Section 1.367(a)–9 also issued under 26 U.S.C. 367(a) and (b).* * *

Par. 2. Section 1.367(a)–9 is added to read as follows:

§1.367(a)–9 Treatment of deemed section 351 exchanges pursuant to section 304(a)(1).

[The text of proposed §1.367(a)–9 is the same as the text of §1.367(a)–9T published elsewhere in this issue of the Bulletin].

Par. 3. Section 1.367(b)–4 is amended by revising paragraphs (e), (f) and (g) to read as follows:

§1.367(b)–4 Acquisition of foreign corporate stock or assets by a foreign corporation in certain nonrecognition transactions.

* * * * *

(e) [The text of proposed §1.367(b)–4(e) is the same as the text of §1.367(b)–4T(e) published elsewhere in this issue of the Bulletin].

(f) [The text of proposed §1.367(b)–4(f) is the same as the text of §1.367(b)–4T(f) published elsewhere in this issue of the Bulletin].

(g) [The text of proposed §1.367(b)–4(g) is the same as the text of §1.367(b)–4T(g) published elsewhere in this issue of the Bulletin].

Par. 4. Section 1.1248–1 is amended by revising paragraphs (b) and (g) to read as follows:

§1.1248–1 Treatment of gain from certain sales or exchanges of stock in certain foreign corporations.

* * * * *

(b) [The text of proposed §1.1248–1(b) is the same as the text of §1.1248–1T(b) published elsewhere in this issue of the Bulletin].

* * * * *

(g) [The text of proposed §1.1248–1(g) is the same as the text of §1.1248–1T(g) published elsewhere in this issue of the Bulletin].

Linda M. Kroening,
Acting Deputy Commissioner for Services and Enforcement.

(Filed by the Office of the Federal Register on February 10, 2009, 8:45 a.m., and published in the issue of the Federal Register for February 11, 2009, 74 F.R. 6840)

Taxpayer Identification Number ("TIN") Matching Program Is Available to Persons Required to Make Returns Under New Section 6050W of the Internal Revenue Code

Announcement 2009–6

The Housing Assistance Tax Act of 2008, Div. C of Pub. L. No. 110–289, 122 Stat. 2653 (the "Act"), enacted on July 30, 2008, added section 6050W to the Internal Revenue Code. This new section requires information returns to be made for each calendar year by merchant acquiring entities and third party settlement organizations with respect to payment card transactions and third party payment network transactions occurring in that calendar year. This requirement to make information returns applies to returns for calendar years beginning after December 31, 2010.

Section 3406(a)(1) requires certain payors to perform backup withholding by deducting and withholding income tax from a reportable payment if the payee fails to furnish the payee's taxpayer identification number ("TIN") to the payor on a required return, or if the Secretary notifies the payor that the TIN furnished by the payee is incorrect. The Act amended section 3406(b)(3) by expanding the meaning of "other reportable payments" that are subject to backup withholding to include payments that are required to be shown on an information return under section 6050W. Backup withholding for amounts reportable under section 6050W applies to amounts paid after December 31, 2011. The Act also amended section 6724(d) by adding returns required by section 6050W to the definition of information returns for purposes of penalties for failure to comply with certain information reporting requirements.

The Act further provides that, solely for purposes of carrying out TIN matching under section 3406, section 6050W is effective on the date of enactment, July 30, 2008. The TIN matching program described in Rev. Proc. 2003–9, 2003–1 C.B. 516, permits program participants to verify the payee TINs required to be reported on information returns and payee statements. Prior to making an information return, a participant may check the TIN furnished by the payee against the name/TIN combination contained in the IRS's database maintained for the program, and the IRS will inform the participant whether or not the name/TIN combination furnished by the payee matches a name/TIN combination in the database. The matching information provided to participants will help avoid TIN errors and reduce the number of backup withholding notices required under section 3406(a)(1)(B) of the Code. A verified TIN/name match will also provide participants with reasonable cause relief from penalties under section 6724(a).

Accordingly, persons who will be required to make returns under section 6050W may now match TINs under the procedures established by Rev. Proc. 2003–9.

The principal author of this announcement is Barbara M. Pettoni of the Office of Associate Chief Counsel (Procedure & Administration). For further information regarding this announcement, please contact Barbara M. Pettoni at (202) 622–4910 (not a toll-free call). For technical information about, or problems with, the TIN matching program, please call 1–866–255–0654.

Foundations Status of Certain Organizations

Announcement 2009–9

The following organizations have failed to establish or have been unable to maintain their status as public charities or as operating foundations. Accordingly, grantors and contributors may not, after this date, rely on previous rulings or designations in the Cumulative List of Organizations (Publication 78), or on the presumption arising from the filing of notices under section 508(b) of the Code. This listing does *not* indicate that the organizations have lost their status as organizations described in section 501(c)(3), eligible to receive deductible contributions.

Former Public Charities. The following organizations (which have been treated as organizations that are not private foundations described in section 509(a) of the Code) are now classified as private foundations:

Alta Housing Corporation, Granbury, TX
American Healthcare Foundation, Newport Beach, CA
Arrowhead Center for the Arts, Eveleth, MN
Bethel Baptist Economic Development, Inc., Montgomery, AL
Bexar County Youth in Action, San Antonio, TX
California State Youth Empowerment, Inc., Vacaville, CA
Caring Community, Inc., Burlington, IA
Ceeatta's Housing, Inc., Richmond, VA
Charros La Esperanza, Inc., San Marcos, CA
City of Marion Recreation Association, Marion, SC
Computer Homework Center, Ferndale, MI
Cortez Hill Interfaith Housing Corporation, Lemon Grove, CA
Educate for Life, Spring Valley, CA
Evolve Project a Nonprofit Public Benefit Corporation, Los Angeles, CA
First Family, Inc., Baltimore, MD
Freedom in Christ Ministries, Brooksville, FL
Future Executives, Inc., Brooklyn, NY
Glory Ministries, Inc., Romulus, MI
God's Unique Angels Righteously Designed, Inc., Arlington, TX
Good Neighbor Food Service, Paulden, AZ
Heal America, Richmond Heights, OH
In His Name, Justice, Education, and Social Services, Washington, DC
Jehovah Adult Daycare, Spartanburg, SC
J E W Ministries, Lake City, SC
Mawus Mothers and Childrens Home Carson, CA
Men In & Out of Schools, Inc., Riverdale, GA
Multiple District 19 Lions Service & Leadership Development Foundation, Bellington, WA
National Land & Wildlife Preservation, Inc., Gilmanton, NH

Nora's Vision NFP, Chicago, IL
Philanthropy International, Clarement, CA
R & N Adult Daycare & Youth Center, Hollandale, MS
River City Small Business Connection, Sacramento, CA
Schoolbox Foundation Corp., Atlanta, GA
Serena Bailey Foundation, Inc., Lakeland, FL
Shannon's Place, Inc., Non for Profit, Chicago, IL
Sturgeon Bay Breakfast Rotary Charitable Tr, Irving, TX
Successful Living Services, Westland, MI
Transition Network, Stafford, TX
Vida Support Services Parent & Youth Counseling Organization, Whittier, CA
Viet Vets Foundation, Inc., Houston, TX
Zhinga-Wee-Thay, Inc., Irving, TX

If an organization listed above submits information that warrants the renewal of its classification as a public charity or as a private operating foundation, the Internal Revenue Service will issue a ruling or determination letter with the revised classification as to foundation status. Grantors and contributors may thereafter rely upon such ruling or determination letter as provided in section 1.509(a)–7 of the Income Tax Regulations. It is not the practice of the Service to announce such revised classification of foundation status in the Internal Revenue Bulletin.

Deletions From Cumulative List of Organizations Contributions to Which are Deductible Under Section 170 of the Code

Announcement 2009–10

The Internal Revenue Service has revoked its determination that the organizations listed below qualify as organizations described in sections 501(c)(3) and 170(c)(2) of the Internal Revenue Code of 1986.

Generally, the Service will not disallow deductions for contributions made to a listed organization on or before the date of announcement in the Internal Revenue Bulletin that an organization no longer qualifies. However, the Service is not precluded from disallowing a deduction for any contributions made after an organization ceases to qualify under section 170(c)(2) if the organization has not timely filed a suit for declaratory judgment under section 7428 and if the contributor (1) had knowledge of the revocation of the ruling or determination letter, (2) was aware that such revocation was imminent, or (3) was in part responsible for or was aware of the activities or omissions of the organization that brought about this revocation.

If on the other hand a suit for declaratory judgment has been timely filed, contributions from individuals and organizations described in section 170(c)(2) that are otherwise allowable will continue to be deductible. Protection under section 7428(c) would begin on March 2, 2009, and would end on the date the court first determines that the organization is not described in section 170(c)(2) as more particularly set forth in section 7428(c)(1). For individual contributors, the maximum deduction protected is $1,000, with a husband and wife treated as one contributor. This benefit is not extended to any individual, in whole or in part, for the acts or omissions of the organization that were the basis for revocation.

Leszinski Family Support Organization
Atlanta, GA
Kuumba Trust
Pittsburgh, PA
Consumer Debt Management Services
Deerfield Beach, FL
RealtyAmerica.Org, Inc.
Indian Harbour Beach, FL
Consumer Budget Counseling, Inc.
Port Charlotte, FL
Innovative Womens Network, Inc.
Houston, TX
Ellen Stephen Hospice & Home Care
Kyle, SD
Starfish Foundation, Inc.
Richardson, TX
Ronsard Foundation
Statesville, NC
Alternative Care, Inc.
Gainesville, FL
Credit Counseling, Inc.
Sunrise, FL
A New Goal Credit Counseling Agency
San Francisco, CA
Trans-Atlantic Health Organization, Inc.
Gaithersburg, MD
Ammend Credit Counseling and Debt Consolidation
Cincinnati, OH

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified*, below).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in laws or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in a new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1986 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified* and *superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case, the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statement of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D. —Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z —Corporation.

Numerical Finding List[1]

Bulletins 2009–1 through 2009–9

[1] A cumulative list of all revenue rulings, revenue procedures, Treasury decisions, etc., published in Internal Revenue Bulletins 2008–27 through 2008–52 is in Internal Revenue Bulletin 2008–52, dated December 29, 2008.

Finding List of Current Actions on Previously Published Items[1]

Bulletins 2009–1 through 2009–9

Notices:

99-35
Obsoleted by
Notice 2009-15, 2009-6 I.R.B. *449*

2001-55
Modified by
Notice 2009-1, 2009-2 I.R.B. *250*

2002-27
Modified by
Notice 2009-9, 2009-5 I.R.B. *419*

2005-74
Obsoleted by
T.D. 9446, 2009-9 I.R.B. *607*

2007-26
Modified by
Notice 2009-15, 2009-6 I.R.B. *449*

2007-54
Obsoleted by
T.D. 9436, 2009-3 I.R.B. *268*

2008-11
Obsoleted by
T.D. 9436, 2009-3 I.R.B. *268*

2008-12
Obsoleted by
T.D. 9436, 2009-3 I.R.B. *268*
Rev. Proc. 2009-11, 2009-3 I.R.B. *313*

2008-13
Obsoleted by
T.D. 9436, 2009-3 I.R.B. *268*
List of forms modified and superseded by
Rev. Proc. 2009-11, 2009-3 I.R.B. *313*
Modified and clarified by
Notice 2009-5, 2009-3 I.R.B. *309*

2008-46
Obsoleted by
T.D. 9436, 2009-3 I.R.B. *268*
Rev. Proc. 2009-11, 2009-3 I.R.B. *313*

2008-100
Amplified and superseded by
Notice 2009-14, 2009-7 I.R.B. *516*

Proposed Regulations:

REG-149519-03
Withdrawn by
Ann. 2009-4, 2009-8 I.R.B. *597*

Revenue Procedures:

2007-17
Superseded by
Rev. Proc. 2009-14, 2009-3 I.R.B. *324*

2007-68
Superseded by
Rev. Proc. 2009-17, 2009-7 I.R.B. *517*

2007-71
Modified by
Notice 2009-3, 2009-2 I.R.B. *250*

2008-1
Superseded by
Rev. Proc. 2009-1, 2009-1 I.R.B. *1*

2008-2
Superseded by
Rev. Proc. 2009-2, 2009-1 I.R.B. *87*

2008-3
Superseded by
Rev. Proc. 2009-3, 2009-1 I.R.B. *107*

2008-4
Superseded by
Rev. Proc. 2009-4, 2009-1 I.R.B. *118*

2008-5
Superseded by
Rev. Proc. 2009-5, 2009-1 I.R.B. *161*

2008-6
Superseded by
Rev. Proc. 2009-6, 2009-1 I.R.B. *189*

2008-7
Superseded by
Rev. Proc. 2009-7, 2009-1 I.R.B. *226*

2008-8
Superseded by
Rev. Proc. 2009-8, 2009-1 I.R.B. *229*

2008-9
Superseded by
Rev. Proc. 2009-9, 2009-2 I.R.B. *256*

2008-61
Superseded by
Rev. Proc. 2009-3, 2009-1 I.R.B. *107*

2008-65
Amplified and supplemented by
Rev. Proc. 2009-16, 2009-6 I.R.B. *449*

2008-68
Amplified and superseded by
Rev. Proc. 2009-15, 2009-4 I.R.B. *356*

Revenue Rulings:

65-286
Obsoleted by
T.D. 9435, 2009-4 I.R.B. *333*

Revenue Rulings— Continued:

76-54
Obsoleted by
T.D. 9435, 2009-4 I.R.B. *333*

92-19
Supplemented by
Rev. Rul. 2009-3, 2009-5 I.R.B. *382*

2008-19
Modified by
Rev. Rul. 2009-3, 2009-5 I.R.B. *382*

[1] A cumulative list of current actions on previously published items in Internal Revenue Bulletins 2008–27 through 2008–52 is in Internal Revenue Bulletin 2008–52, dated December 29, 2008.

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