

Announcement of Amendments to Regulations Under Section 367 of the Internal Revenue Code

Notice 2002-77

The Internal Revenue Service (the “Service”) is publishing Rev. Rul. 2002-85 contemporaneously with the issuance of this Notice. Rev. Rul. 2002-85 holds that an acquiring corporation’s transfer of the target corporation’s assets to a subsidiary controlled by the acquiring corporation pursuant to a plan of reorganization will not prevent a transaction that otherwise qualifies as a reorganization under section 368(a)(1)(D) from so qualifying. This notice announces that the Treasury and the Service will amend the regulations under Treas. Reg. § 1.367(a)-3(d) to provide specifically that a reorganization under section 368(a)(1)(D) followed by the transfer of all or a portion of a target corporation’s assets to a controlled subsidiary pursuant to a plan of reorganization constitutes an indirect transfer of stock or securities for purposes of Treas. Reg. § 1.367(a)-3.

I. BACKGROUND

Section 367(a)(1) requires a U.S. person who transfers property (including stock or securities) to a foreign corporation in connection with an exchange described in section 332, 351, 354, 356, or 361 to recognize gain (but not loss) on the transfer, unless the transfer qualifies for an exception to this general rule. Transfers covered by section 367(a)(1) also include indirect and constructive transfers. Treas. Reg. § 1.367(a)-1T(c)(1).

Treas. Reg. § 1.367(a)-3 contains rules that address transfers of stock or securities by a U.S. person to a foreign corporation in an exchange described in section 367(a). For these purposes, certain transactions that are in form asset transfers are treated as stock transfers. For example, Treas. Reg. § 1.367(a)-3(d)(1)(v) treats as an indirect stock transfer a U.S. person’s exchange of stock or securities of a corporation for voting stock or securities of a foreign acquiring corporation in a reorganization described in section 368(a)(1)(C) in which the acquiring corporation trans-

fers the acquired corporation’s assets to a subsidiary controlled by the acquiring corporation in a transaction described in section 368(a)(2)(C). In the case of a reorganization in which part but not all of the assets of the acquired corporation are transferred pursuant to section 368(a)(2)(C), the transaction is considered to be an indirect transfer of stock or securities only to the extent of the assets so transferred. Treas. Reg. § 1.367(a)-3(d)(1)(v).

In Rev. Rul. 2002-85, pursuant to a plan of reorganization, (i) a corporation (the “target corporation”) transfers all of its assets to another corporation (the “acquiring corporation”) in exchange for consideration consisting of 70 percent acquiring corporation voting stock and 30 percent cash, (ii) the target corporation then liquidates, distributing the acquiring corporation voting stock and cash to its shareholder, and (iii) the acquiring corporation subsequently transfers the target corporation’s assets to a preexisting, wholly owned subsidiary of the acquiring corporation. Rev. Rul. 2002-85 holds that the acquiring corporation’s transfer of the target corporation’s assets to its controlled subsidiary as part of a plan of reorganization will not prevent a transaction that otherwise qualifies as a reorganization under section 368(a)(1)(D) from so qualifying.

II. TREATMENT OF A REORGANIZATION UNDER SECTION 368(a)(1)(D) FOLLOWED BY A TRANSFER OF THE ACQUIRED CORPORATION’S ASSETS TO A CONTROLLED SUBSIDIARY UNDER THE INDIRECT STOCK TRANSFER RULES.

Consistent with the current rules for transactions described in sections 368(a)(1)(C) and (a)(2)(C), the Treasury and the Service will amend the regulations under section 367 to provide specifically that a U.S. person’s exchange of stock or securities of a corporation (the acquired corporation) for stock or securities of a foreign acquiring corporation in a reorganization under section 368(a)(1)(D) in which the foreign acquiring corporation transfers part or all of the acquired corporation’s assets to a subsidiary controlled by the acquiring corporation pursuant to the plan of reorganization constitutes an indirect transfer of stock or securities by the U.S. person to the

foreign acquiring corporation under Treas. Reg. § 1.367(a)-3(d). In the case of a reorganization under section 368(a)(1)(D) in which part but not all of the assets of the acquired corporation are transferred to a subsidiary controlled by the acquiring corporation pursuant to the plan of reorganization, the regulations will provide that the transaction is considered to be an indirect transfer of stock or securities to the extent of the assets so transferred. The amendment to the regulations under section 367 described in this notice will be effective for transfers occurring after **December 9, 2002**. For additional guidance concerning transfers that occurred on or after July 20, 1998 and on or before **December 9, 2002**, see Rev. Rul. 2002-85.

III. DRAFTING INFORMATION AND REQUEST FOR COMMENTS

The principal author of this notice is Richard Osborne of the Office of Associate Chief Counsel (International). However, other personnel from the Service and the Treasury participated in its development. For further information regarding this notice, contact Mr. Osborne at (202) 622-3036 (not a toll-free call).

Written comments concerning this notice may be submitted to the Associate Chief Counsel (International), Attention: Richard Osborne (Notice 2002-77), Room 4573, CC:Intl:Br4, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, DC 20224. Alternatively, taxpayers may submit comments directly to the IRS Internet site at http://www.irs.ustreas.gov/prod/tax_regs/comments.html. Comments will be available for public inspection and copying. The Treasury and the Service request comments by January 15, 2003.
