Internal Revenue Service

Department of the Treasury

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Person to Contact:

Telephone Number:

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June 18, 2001

Legend:

A =

B =

C =

D =

Country1 =

State1 =

a% =

b% =

c% =

This letter responds to the ruling request dated February 26, 2001, which was submitted by your authorized representative on behalf of A, and which requests rulings under section 897 of the Internal Revenue Code.

FACTS

A, B, and C are corporations established under the laws of Country1. A wholly owns B and B wholly owns C. A does not engage in a trade or business in the United States.

D is a domestic corporation established under the laws of State1. A, B and C each hold a direct interest in D; A holds a%, B holds b%, and C holds c% of the shares of D.

The remaining shares are publicly traded on a major domestic exchange.

Country1 has a comprehensive income tax treaty with the United States which contains an exchange of information provision that meets the requirement set forth in section 1.897-6T(b)(2).

A represents that D is United States Real Property Holding Corporation within the meaning of section 897(c)(2) and that A's direct interest in D constitutes a United States real property interest within the meaning of section 897(c)(1).

A will transfer the shares it holds directly in D, representing an a% interest, to B, in exchange for additional shares of B. A will be the only transferor of property to B. A has represented that A has no intention, after the exchange, to dispose of the new shares in B and that A's transfer is a transfer of property described in section 351.

LAW AND ANALYSIS

Section 897(a) provides that gain or loss of a nonresident alien individual or a foreign corporation from the disposition of a United States real property interest shall be taken into account as if the taxpayer were engaged in a trade or business within the United States during the taxable year and as if such gain or loss were effectively connected with such trade or business. The term "United Sates real property interest" (USRPI) includes an interest in real property (including an interest in a mine, well, or other natural deposit) located in the United States or the Virgin Islands, and any interest (other than an interest solely as a creditor) in any domestic corporation unless the taxpayer establishes (at such time and in such manner as the Secretary by regulations prescribes) that such corporation was at no time a United States real property holding corporation.

The term "United States real property holding corporation" (USRPHC) means any corporation if the fair market value of its United States real property interests equals or exceeds 50 percent of the fair market value of the following: (i) its USRPI, (ii) its interests in real property located outside the United States, and (iii) any other of its assets which are used or held for use in a trade or business. Section 897(c)(2).

With respect to a transaction coming within a nonrecognition provision of the Code, section 897(e)(1) states that such nonrecognition provision will apply to a transaction only in the case of an exchange of a USRPI for an interest the sale of which would be subject to taxation. The term "nonrecognition provision" includes any provision under the Code for not recognizing gain or loss. Section 1.897-6T addresses the application of any nonrecognition provision to a transfer by a foreign person under section 897(e). The regulation states that a nonrecognition provision will apply to a transfer by a foreign person of a USRPI on which gain is realized only to the extent that the transferred interest is exchanged for a USRPI which, immediately following the exchange, would be subject to U.S. taxation upon its disposition, and the transferor complies with the filing requirements

of section 1.897-5T(d)(1)(iii).

However, section 1.897-6T(b)(1) provides an exception to the above rule that a foreign transferor of a USRPI must receive a USRPI to obtain nonrecognition treatment. The exception applies (and the transferor does not recognize gain) when a foreign person transfers a USRPI to a foreign corporation in exchange for stock in a foreign corporation, and 1) the transferee's subsequent disposition of the transferred USRPI would be subject to U.S. taxation as determined in accordance with the provisions of section 1.897-5T(d)(1); 2) the filing requirements of section 1.897-5T(d)(1)(iii) are met; 3) one of the five conditions set forth in section 1.897-6T(b)(2) is met; and 4) one of three forms of exchange set forth in section 1.897-6T(b)(1) takes place.

As set forth in the third requirement above, the exception set forth in section 1.897-6T(b)(1) applies only if one of the following five conditions set forth in section 1.897-6T(b)(2) exists:

1. Each of the interests exchanged or received in a transferor corporation or transferee corporation would not be a USRPI as defined in section 1.897-1(c)(1) if such corporations were domestic corporations; or

2. The transferee corporation (and the transferee corporation's parent in the case of a parenthetical B or C reorganization) is incorporated in a foreign country that maintains an income tax treaty with the United States that contains an information exchange provision; the transfer occurs after May 5, 1988; and the transferee corporation (and the transferee corporation's parent in the case of a parenthetical B or C reorganization) submit a binding waiver of all benefits of the respective income tax treaty (including the opportunity to make an election under section 897(i), which must be attached to each of the transferor and transferee corporation's income tax returns for the year of the transfer; or

3. The transferee foreign corporation (and the transferee corporation's parent in the case of a parenthetical B or C reorganization) is a qualified resident as defined in section 884(e) and any regulations thereunder of the foreign country in which it is incorporated; or

4. The transferee foreign corporation (and the transferee corporation's parent in the case of a parenthetical B or C reorganization) is incorporated in the same foreign country as the transferor foreign corporation; and there is an income tax treaty in force between that foreign country and the United States at the time of the transfer that contains an exchange of information provision; or

5. The transferee foreign corporation is incorporated in the same foreign

country as the transferor foreign corporation; and the transfer is incident to a mere change in identity, form, or place of organization of one corporation under section 368(a)(1)(F).

Further, the fourth requirement set forth in section 1.897-6T(b)(1) is that the exchange of a USRPI to a foreign corporation in exchange for stock in a foreign corporation must come within one of the following forms of exchange:

1. The exchange is made by a foreign corporation pursuant to section 361(a) in a reorganization described in section 368(a)(1)(D) or (F) and there is an exchange of the transferor corporation stock for the transferee corporation stock under section 354(a); or

2. The exchange is made by a foreign corporation pursuant to section 361(a) in a reorganization described in section 368(a)(1)(C); there is an exchange of the transferor corporation stock for the transferee corporation stock (or stock of the transferee corporation's parent in the case of a parenthetical C reorganization) under section 354(a); and the transferor corporation's shareholders own more than fifty percent of the voting stock of the transferee corporation (or stock of the transferee corporation's parent in the case of a parenthetical C reorganization) immediately after the reorganization; or

3. The USRPI exchanged is stock in a USRPHC; the exchange qualifies under section 351(a) or section 354(a) in a reorganization described in section 368(a)(1)(B); and immediately after the exchange, all of the outstanding stock of the transferee corporation (or stock of the transferee corporation's parent in the case of a parenthetical B reorganization) is owned in the same proportions by the same nonresident alien individuals and foreign corporations that, immediately before the exchange, owned the stock of the USRPHC.

Notwithstanding the fact that an exchange may come within section 351(a) and meets the other requirements to obtain nonrecognition treatment for the transfer of the USRPI to a foreign corporation, if the nonresident alien individual or foreign corporation which received stock in the exchange disposes of any of such foreign stock within three years from the date of its receipt, then that individual or corporation must recognize that portion of the gain realized with respect to the stock in the USRPHC for which the foreign stock disposed of was received.

A represents that D is a USRPHC and that its interest in D constitutes a USRPI. Further, A's transfer of the D stock to B is a transfer of property that comes within section 351(a) and is a transfer to which section 897(e) applies. Accordingly, to obtain nonrecognition treatment for the transfer, A must meet the requirements set forth in section 1.897-6T of the regulations. All of the requirements of section 1.897-6T have been

met in this case. After A's transfer to B, a foreign corporation, B will hold an interest that will be subject to taxation under section 1.897-5T(d)(1). Further, as mentioned, A's proposed transfer is a transfer of property described in section 351(a). A has represented that the filing requirements of section 1.897-5T(d)(1)(iii), as modified by Notice 89-57, 1989-1 C.B. 698 will be complied with, and that A's interest in D before and after the proposed transfer will be identical. Finally, the United States has a comprehensive income tax treaty with Country 1 which contains an exchange of information provision.

CONCLUSION

Based solely on the information submitted and on the representations made and provided that the exchange of D stock for B stock qualifies as an exchange under section 351(a) and the filing requirements of section 1.897-5T(d)(1)(iii) as modified by Notice 89-57 are met, we rule that A will not recognize gain on the exchange of D stock for B stock under section 897(e) (section 1.897-6T(b)(1) and (2)).

Except as specifically set forth above, no opinion is expressed as to the federal tax consequences of the transaction described above under any other provision of the Internal Revenue Code. Also, see section 1445 and the regulations thereunder for the withholding responsibilities of A and B.

The rulings contained in this letter are based on facts and representations submitted by the taxpayer under penalties of perjury. The Internal Revenue Service may require verification of this information as part of the audit process.

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Pursuant to the power of attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely yours,
Charles P. Besecky
Chief, Branch 4
Associate Chief Counsel (International)

Enclosures: 2
Copy of this letter
Copy for §6110 purposes