Internal Revenue Service

Department of the Treasury

Washington, DC 20224

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Person to Contact:

Telephone Number:

Refer Reply To:
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Date:
September 27, 2002

Legend

Parent =

Subsidiary =

Partnership X =

Partnership Y =

Business A =

Court =

State B =

Country Z =

Date 1 =

Date 2 =

Year 3 =

Year 4 =

$c =
$d =

Dear :

We respond to your letter dated May 28, 2002, in which you requested a ruling regarding the federal income tax consequences of proposed transactions. Additional information was submitted in subsequent correspondence. The information submitted for consideration is substantially as set forth below.

Parent, or Taxpayer, is a publicly traded State B corporation and the common parent of a consolidated group. Parent and its subsidiaries are engaged in Business A. Their principal operations are in several foreign countries. One of Parent's wholly owned lower tiered domestic corporations, Subsidiary, is a U.S. corporation and a tax resident of Country Z. Subsidiary owns all the stock of several foreign entities that in turn collectively own all of the stock of two Country Z unlimited companies, Partnership X and Partnership Y, that are treated as partnerships for U.S. tax purposes.

On Date 1, Parent filed a petition for bankruptcy under Chapter 11 of the Bankruptcy Code in Court. Taxpayer represents that it will undergo an ownership change within the meaning of § 382 of the Internal Revenue Code on Date 2, the effective date of the plan of reorganization, which is anticipated to be effective in Year 4. Taxpayer proposes to make a closing-of-the-books election under § 1.382-6(b) of the Income Tax Regulations with respect to this ownership change.

Taxpayer estimates a tax loss carryforward of $c that includes a capital loss carryforward of approximately $d from the taxable year ending December 31, Year 3 and a tax loss for Year 4, a portion of which will be allocated to the period before the ownership change. It is also expected that a significant portion of the loss carryforward will be reduced by application of §§ 108(a) and (b) requiring the reduction of tax attributes by the amount of income from cancellation of indebtedness resulting from the restructuring of indebtedness pursuant to the plan of reorganization.

Taxpayer will cause X and Y to elect, under § 301.7701-3 of the Procedure and Administration Regulations, to be classified as associations taxable as corporations for U.S. tax purposes. Both elections will have an effective date within the period before the ownership change. As a result of the entity classification elections, each partnership will be deemed to contribute all of its assets and liabilities to a newly formed Country Z corporation in exchange for stock of the corporation, and to liquidate immediately thereafter by distributing the stock of the new corporation to its partners under § 301.7701-3(g)(1)(i).

Taxpayer represents that these deemed transfers qualify as exchanges subject to § 351. Taxpayer further represents that Taxpayer's consolidated group will have to recognize taxable income in connection with the deemed transfers by reason of the overall foreign loss recapture rules of § 904(f)(3) to the extent the fair market value of the transferred assets exceeds their tax basis; through recapture of dual consolidated losses as a result of a triggering event under § 1.1503-2(g)(2)(iii)(A)(5) after taking into account the rebuttal provision of § 1.1503-2(g)(2)(vii)(B)(1); through recapture of foreign branch losses under § 1.367(a)-6T(b) in an amount equal to previously deducted branch ordinary losses and previously deducted branch capital losses; through gain resulting from an election under § 1.367(d)-1T(g)(2) to treat the transfer of operating intangibles as a sale; and gain under § 357(c) to the extent that liabilities assumed in the transfer exceed the basis of assets transferred.

Taxpayer has submitted the following additional representations in connection with the requested ruling:

(a) The ownership change will not satisfy the requirements of the bankruptcy exception as set forth in § 382(l)(5)(A).

(b) Taxpayer is the common parent of an affiliated group of corporations that file a consolidated federal income tax return and this affiliated group is a "loss group" within the meaning of § 1.1502-91(c)(1).

(c) Taxpayer has not accelerated income into the pre-change period or deferred loss to the post-change period for purposes of avoiding the application of § 382(a).

(d) Taxpayer plans to continue Business A, its historic business, after the effective date of the plan of reorganization and to use its historic business assets in Business A (for at least a two year period from the change date).

(f) All members of the affiliated group will close their books as of the ownership change date pursuant to § 1.382-6(b)(3)(i).

(g) The Partnership X and Partnership Y losses have not been used by any other person in a foreign country.

(h) There have been no special allocations of partnership items of Partnership X and Partnership Y.

(i) There have been no shifts in the ownership of Partnership X and Partnership Y, except for shifts within the U.S. consolidated group incidental to internal restructuring. Such restructurings did not change the

relative ownership of Partnership X and Partnership Y between the U.S. and Country Z affiliates.

Based solely on the information submitted and on the representations set forth above, we hold as follows:

(1) The taxable income that results from the deemed transfers as a result of the entity classification election under § 301.7701-3 is allocable to the pre-change period upon the closing-of-the-books election under § 1.382-6(b) subject to the provision that the income or loss allocated to the pre-change period cannot exceed the taxable income or loss for the taxable year that includes the change date.

(2) In connection with any dual consolidated loss recapture, an interest charge shall be paid as provided in § 1.1503-2(g)(2)(vii)(A)(2).

(3) The taxable income recognized by reason of the overall foreign loss recapture rules of § 904(f)(3) will reduce Taxpayer's overall foreign loss accounts only to the extent the taxable income recognized on the deemed transfers is not reduced by application of a net operating loss or loss carryforward.

Except as specifically set forth above, we express no opinion concerning the tax consequences of the proposed transaction under any other provision of the Code and regulations, or about the tax treatment of any conditions existing at the time of, or effects resulting from, the proposed transaction.

The rulings contained in this letter are predicated upon the facts and representations submitted by the taxpayers and accompanied by a penalties of perjury statement executed by an appropriate party. This office has not verified any of the materials submitted in support of the request for a ruling. Verification of the information, representations, and other data may be required as part of the audit process. See section 12.04 of Rev. Proc. 2002-1, 2002-1 I.R.B. 1, 50, which discusses in greater detail the revocation or modification of ruling letters. However, when the criteria in section 12.05 of Rev. Proc. 2002-1, 2002-1 I.R.B. at 50-51, are satisfied, a ruling is not revoked or modified retroactively except in rare or unusual circumstances.

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

A copy of this letter should be attached to the federal income tax returns of the taxpayers involved for the taxable year in which the transaction covered by this ruling letter is consummated.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to the taxpayer.

Sincerely yours,

Filiz A. Serbes

Filiz A. Serbes
Chief, Branch 3
Office of Associate Chief Counsel
(Corporate)