Internal Revenue Service

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Person To Contact:
, ID No.
Telephone Number:

Refer Reply To:
CC:INTL:B02
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Date:
October 21, 2005

In Re:

Legend

A	=
B	=
C	=
D	=
Business X	=
Date X	=
Date Y	=
Country M	=
Country N	=
Country O	=
Country P	=
Country Q	=

Dear :

This is in response to your letter dated July 26, 2005, requesting a ruling that a foreign subsidiary that recognized gain from selling stock in its 25%-owned subsidiaries before becoming a controlled foreign corporation ("CFC") is treated as selling its proportionate share of the underlying assets of those subsidiaries in determining whether the gain was "passive income" under section 1297(b)(1) of the Internal Revenue Code.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer, and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of this request for ruling, such material is subject to verification upon examination.

FACTS

A, a U.S. corporation, is a wholly-owned, indirect subsidiary of B, a publicly traded, SEC-registered, Country M corporation that is the common parent of a global group of operating companies engaged in business X. A is the holding company for operating companies in Countries N, O, and P.

A owns 100% of the stock of C, a Country Q corporation that currently is a CFC, within the meaning of section 957(a).

On Date X, C sold all the stock of its wholly-owned subsidiary, D, a Country Q corporation that directly or indirectly owned the stock of several European operating companies. At the time of the sale, C had both U.S. and foreign owners and was not a CFC.

A plans to repatriate C's earnings and profits on or before Date Y and reinvest them in the United States in accordance with section 965. Section 965 provides a temporary 85% dividends-received deduction for cash dividends from CFCs that are reinvested in the United States.

To determine whether the repatriation will trigger the application of section 1291, Taxpayer must know whether C is a passive foreign investment company ("PFIC"). Section 1298(b)(1) provides that stock of a corporation held by a taxpayer is stock in a PFIC if, at any time during the taxpayer's holding period, the corporation was a PFIC that was not a QEF. To determine whether C was a PFIC in the year of the sale of D stock, Taxpayer must know whether C's gain from selling D was "passive income" under section 1297(b).

RULING REQUESTED

In determining whether C's gain from selling the stock of D is "passive income" under section 1297(b)(1), C is treated as selling its proportionate share of the underlying assets of D and those subsidiaries of D of which C indirectly owns at least 25%.

LAW AND ANALYSIS

Section 1297(a) defines a PFIC as any foreign corporation if either (1) 75 percent or more of the gross income of such corporation for the taxable year is passive income, or (2) the average percentage of assets held by such corporation during the taxable year which produce passive income or which are held for the production of passive income is at least 50 percent.

Section 1297(b)(1) defines “passive income” as any income which is of a kind which would be foreign personal holding company income (“FPHCI”) under section 954(c). Section 954(c), in turn, defines FPHCI to include certain categories of income and gains from the sale of certain categories of assets. Therefore, whether C’s gain from selling the stock of D is passive income turns on whether the gain falls within a category of FPHCI under section 954(c).

Section 1297(c) provides that if a foreign corporation directly or indirectly owns at least 25 percent of the stock of another corporation (a “25%-owned subsidiary”), for purposes of determining whether the foreign corporation is a PFIC, the foreign corporation is treated as holding its proportionate share of the assets, and receiving directly its proportionate share of the income, of the 25%-owned subsidiary.

Correspondingly, to determine whether gain from the sale of stock of a 25%-owned subsidiary is “passive income” under section 1297(b)(1), the sale of stock should be treated as a sale of the foreign corporation’s proportionate share of the assets of the 25%-owned subsidiary (and lower-tier 25%-owned subsidiaries) that are treated as held by the foreign corporation under section 1297(c).

Based on the information submitted and representations made:

For purposes of determining whether C is a PFIC under section 1297(a), whether C’s gain from selling the stock of D is “passive income,” under section 1297(b)(1), is determined by treating C as if it sold its proportionate share of the underlying assets of D and of those subsidiaries of D of which C indirectly owns (by value) at least 25%.

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

A copy of this ruling must be attached to any tax return to which it is relevant.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to the taxpayer’s first and second representatives.

Sincerely,

Valerie Mark Lippe
Senior Technical Reviewer
(International)

cc: