Internal Revenue Service

Department of the Treasury
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Third Party Communication: None
Date of Communication: Not Applicable
Person To Contact:
, ID No.
Telephone Number:

Refer Reply To:
CC:INTL:B04
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Date:
May 06, 2010

Legend

Individual X =

Entity A =

Entity B =

Entity C =

Entity D =

Entity E =

Country 1 =

Country 2 =

aa =

Dear :

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 the request for rulings, it is subject to verification on examination.

This 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.

FACTS

Individual X is a permanent resident of Country 1, but a citizen of Country 2. He represents that the income tax treaty between Country 1 and the United States applies to the transactions discussed below.

Individual X is the aa% shareholder of Entity A, a domestic corporation. Individual X is also the sole shareholder of Entity B, a domestic corporation. Furthermore, Individual X is the sole member of Entity C, a domestic limited liability company, which is disregarded as an entity separate from its sole owner for U.S. federal income tax purposes. Entity A and Entity B constitute U.S. real property holding corporations, the shares of which are U.S. real property interests pursuant to section 897(c) of the Internal Revenue Code. Entity C also owns U.S. real property interests pursuant to section 897(c) of the Internal Revenue Code.

As part of a restructuring of his business enterprises, Individual X will undertake two separate, but interrelated, transactions. In Transaction 1, Individual X will transfer all of his shares in Entity A and Entity B, as well as all of his interests in Entity C, to newly formed domestic Entity D, in exchange for all the authorized shares of Entity D.

After Transaction 1 is complete, Individual X will immediately undertake Transaction 2. Individual X will transfer all of the shares of Entity D to newly formed Entity E, which will be organized under the laws of Country 1, in exchange for all the shares in Entity E. Simultaneously with this transfer, Entity E will file a notice with the Internal Revenue Service under section 897(i) of the Code, electing to be treated as a domestic corporation for purposes of sections 897, 1445, and 6039C.

The following representations have been made in connection with the proposed transactions:

(1) Entity A and Entity B are United States real property holding corporations within the meaning of section 897(c)(2), and the interests in them constitute United States real property interests as defined in section 897(c)(1).

(2) Immediately after Transaction 1, Entity D will be a United States real property holding corporation within the meaning of section 897(c)(2); its stock will be subject to U.S. taxation upon its disposition; and Individual X will comply with the filing requirements of Treas. Reg. § 1.897-5T(d)(1)(iii), as modified by Notice 89-57, 1989-1 C.B. 698.

(3) Immediately after Transaction 2, Entity E will be a United States real property holding corporation within the meaning of section 897(c)(2); its stock will constitute a United States real property interest as defined in section 897(c)(1) that will be subject to U.S. taxation upon its disposition; and Individual X will comply with the filing requirements of Treas. Reg. § 1.897-5T(d)(1)(iii), as modified by Notice 89-57, 1989-1 C.B. 698.

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 States 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 during the 5-year period ending on the date of disposition of such interest.

Section 897(c)(2) provides that the term "United States real property holding corporation" (USRPHC) means any corporation if the fair market value of its USRPIs equals or exceeds 50 percent of the fair market value of the following: (i) its USRPIs, (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.

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, such as section 351(a). Treas. Reg. § 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 Treas. Reg. § 1.897-5T(d)(1)(iii).

Section 1445(a) provides that, except as otherwise provided in this section, in the case of any disposition of a United States real property interest (as defined in section 897(c)) by a foreign person, the transferee shall be required to deduct and withhold a tax equal to 10 percent of the amount realized on the disposition.

Treas. Reg. § 1.1445-2(d)(2) provides that a transferee shall not be required to withhold under section 1445(a) with respect to the transfer of a USRPI if the following occurs: (A) The transferor notifies the transferee, in the manner described in Treas. Reg. § 1.1445-2(d)(2)(iii), that by reason of the operation of a nonrecognition provision of the Internal Revenue Code or the provisions of any Unites States treaty the transferor is not required to recognize any gain or loss with respect to the transfer; and (B) By the 20th day after the date of the transfer the transferee provides a copy of the transferor's notice to the Internal Revenue Service provided in Treas. Reg. § 1.1445-1(g)(10), together with a cover letter setting forth the name, identifying number, and the home address (in the case of an individual) or office address (in the case of an entity) of the transferee providing the notice to the Service.

Section 897(i) provides that if a foreign corporation holds a United States real property interest, and under any treaty obligation of the United States the foreign corporation is entitled to nondiscriminatory treatment with respect to that interest, then such foreign corporation may make an election to be treated as a domestic corporation for purposes of this section, section 1445, and section 6039C.

Treas. Reg. § 1.897-3 provides, in part, that this section provides rules pursuant to which a foreign corporation may elect under section 897(i) to be treated as a domestic corporation for purposes of section 897, 1445, and 6039C and the regulations thereunder. A foreign corporation with respect to which an election under section 897(i) is in effect is subject to all rules under sections 897 and 1445 that apply to domestic corporations. A foreign corporation that makes an election under section 897(i) shall not be treated as a domestic corporation for purposes of any other provision of the Code or regulations, except to the extent that it is required to consent to such treatment as a condition to making the election. For further information concerning the effect of an election under section 897(i) upon the withholding requirements of section 1445, see Treas. Reg. § 1.1445-7.

Treas. Reg. § 1.1445-7(a) provides that pursuant to section 897(i) a foreign corporation may elect to be treated as a domestic corporation for purposes of sections 897 and 6039C. A foreign corporation that has made such an election shall also be treated as a domestic corporation for purposes of the withholding required under section 1445, in accordance with the provisions of this section.

For Transaction 1 to qualify for nonrecognition treatment, it must satisfy the requirements of section 897(e) and Treas Reg. § 1.897-6T. That is, the interests in Entities A, B, and C must be exchanged for a USRPI which, immediately following the

exchange, would be subject to U.S. taxation upon its disposition, and Individual X must comply with the filing requirements of Treas. Reg. § 1.897-5T(d)(1)(iii), as modified by Notice 89-57, 1989-1 C.B. 698. Individual X represents that Entity A and Entity B are USRPHCs and that his interests in Entities A and B constitute USRPIs. In addition, Individual X, who represents that Entity C has elected to be treated as a disregarded entity for U.S. tax purposes, is treated as directly owning the USRPIs which in turn are owned by Entity C. Individual X also represents that immediately after Transaction 1, Entity D will be a USRPHC and that Individual X will comply with the filing requirements of Treas. Reg. § 1.897-5T(d)(1)(iii), as modified by Notice 89-57, 1989-1 C.B. 698. Transaction 1 will therefore qualify for nonrecognition treatment.

For Transaction 2 to qualify for nonrecognition treatment, it must also satisfy all the requirements of section 897(e) and Treas. Reg. § 1.897-6T. That is, the interests in Entity D must be exchanged for a USRPI which, immediately following the exchange, would be subject to U.S. taxation upon its disposition. Individual X represents that Entity D will be a USRPHC and that Individual X's interest in it will constitute a USRPI. Furthermore, Individual X represents that, immediately after Transaction 2, Individual X's interest in Entity E will constitute a USRPI which will be subject to U.S. taxation upon disposition. Individual X will make an 897(i) election so that Entity E will be treated as a domestic corporation for purposes of sections 897, 1445, and section 6039C. Entity E is eligible for an election under 897(i) because it holds a United States real property interest and is entitled to nondiscriminatory treatment with respect to that interest under the income tax treaty with Country 1. Entity E will be a USRPHC under section 897(c) immediately after the exchange, and Individual X's interest in Entity E will constitute a USRPI. Individual X further represents that he will comply with the filing requirements of Treas. Reg. § 1.897-5T(d)(1)(iii), as modified by Notice 89-57, 1989-1 C.B. 698. Based upon the foregoing, Transaction 2 satisfies the requirements of Treas. Reg. § 1.897-6T and will qualify for nonrecognition treatment under section 897(e).

OTHER REPRESENTATIONS

Transfer 1

1. No stock or securities will be issued for services rendered to or for the benefit of Entity D in connection with the proposed transaction. No stock or securities will be issued for indebtedness of Entity D that is not evidenced by a security or for interest on indebtedness of Entity D which is accrued on or after the beginning of the holding period of Individual X for the debt.

2. Transfer 1 is not the result of the solicitation by a promoter, broker or investment house.

3. Individual X will not retain any rights in the property transferred to Entity D.

4. There is no indebtedness between Entity D and Individual X, and there will be no

indebtedness created in favor of Individual X as a result of Transaction 1.

5. Transaction 1 will occur under a plan agreed upon before the transaction in which the rights of the parties are defined.

6. There is no plan or intention on the part of Entity D to redeem or otherwise reacquire any stock or indebtedness to be issued in Transaction 1.

7. Taking into account any issuance of additional shares of Entity D stock; any issuance of stock for services; the exercise of any Entity D stock rights, warrants, or subscriptions; a public offering of Entity D stock; and the sale, exchange, transfer by gift, or other disposition of any of the stock of Entity D to be received in the exchange, the transferor will be in “control” of Entity D within the meaning of section 368(c) of the Code (Rev. Rul. 2003-51, 2003-1 C.B. 938).

8. Individual X will receive stock, securities, or other property approximately equal in value to the fair market value of the property transferred to Entity D.

9. Entity D will remain in existence and retain use of the property transferred to it in a trade or business.

10. There is no plan or intention by Entity D to dispose of the transferred property other than as proposed in Transaction 2.

11. Each of the parties to Transaction 1 will pay its or his/her own expenses, if any, incurred in connection with Transaction 1.

12. Entity D will not be an investment company within the meaning of section 351(e)(1) of the Code and section 1.351(c)(1)(ii) of the Regulations.

13. Individual X is not under the jurisdiction of a court in a title 11 or similar case (within the meaning of section 368(a)(3)(A)) and the stock or securities received in the exchange will not be used to satisfy the indebtedness of such debtor.

14. Entity D will not be a “personal service corporation” within the meaning of section 269A of the Code.

15. The aggregate fair market value of the assets transferred to Entity D by Individual X will equal or exceed the aggregate adjusted basis of these assets.

Transfer 2

16. No stock or securities will be issued for services rendered to or for the benefit of Entity E in connection with the proposed transaction. No stock or securities will be issued for indebtedness of Entity E that is not evidenced by a security or for interest on indebtedness of Entity E which is accrued on or after the beginning of the holding period of Individual X for the debt.

17. Transfer 2 is not the result of the solicitation by a promoter, broker or investment house.

18. Individual X will not retain any rights in the property transferred to Entity E.

19. There is no indebtedness between Entity E and Individual X, and there will be no indebtedness created in favor of Individual X as a result of Transaction 2.

20. Transaction 2 will occur under a plan agreed upon before the transaction in which the rights of the parties are defined.

21. There is no plan or intention on the part of Entity E to redeem or otherwise reacquire any stock or indebtedness to be issued in Transaction 2.

22. Taking into account any issuance of additional shares of Entity E stock; any issuance of stock for services; the exercise of any Entity E stock rights, warrants, or subscriptions; a public offering of Entity E stock; and the sale, exchange, transfer by gift, or other disposition of any of the stock of Entity E to be received in the exchange, the transferor will be in “control” of Entity E within the meaning of section 368(c) of the Code.

23. Individual X will receive stock, securities, or other property approximately equal in value to the fair market value of the property transferred to Entity E.

24. Entity E will remain in existence and retain use of the property transferred to it in a trade or business.

25. There is no plan or intention by Entity E to dispose of the transferred property.

26. Each of the parties to Transaction 2 will pay its or his/her own expenses, if any, incurred in connection with Transaction 2.

27. Entity E will not be an investment company within the meaning of section 351(e)(1) of the Code and section 1.351(c)(1)(ii) of the Regulations.

28. Individual X is not under the jurisdiction of a court in a title 11 or similar case (within the meaning of section 368(a)(3)(A)) and the stock or securities received

in the exchange will not be used to satisfy the indebtedness of such debtor.

29. Entity E will not be a “personal service corporation” within the meaning of section 269A of the Code.

30. The aggregate fair market value of the assets transferred to Entity E by Individual X will equal or exceed the aggregate adjusted basis of these assets.

CONCLUSION

Based solely on the information submitted and on the representations made, we rule that Transaction 1 and Transaction 2 each qualify as separate exchanges under section 351(a) and that, as long as the filing requirements of Treas. Reg. § 1.897-5T(d)(1)(iii), as modified by Notice 89-57, 1989-1 C.B. 698, are met, Individual X will not recognize gain or loss on Transaction 1 or Transaction 2 under section 897(e)(1). See section 1.897-6T(a)(1).

In regard to the withholding requirements on Transaction 1 and Transaction 2 under section 1445(a), see Treas. Reg. §§ 1.1445-2(d)(2) and 1.1445-7(a).

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 the request for rulings, it is subject to verification on examination.

No opinion is expressed as to the validity of the election by Entity E under section 897(i) of the Code, nor as to the effect on this ruling of any requirement that Entity E might be required to consent to as a condition to making that election.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

This 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.

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

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter ruling.

Sincerely,

Charles P. Besecky
Chief, Branch 4
Office of the Associate Chief Counsel (International)

cc: