INTERNAL REVENUE SERVICE
NATIONAL OFFICE TECHNICAL ADVICE MEMORANDUM

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Date of Communication: Not Applicable

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Index (UIL) No.: 368.04-00
CASE-MIS No.: TAM-122241-13

Taxpayer's Name:
Taxpayer's Address:

Taxpayer's Identification No
Year(s) Involved:
Date of Conference:

LEGEND:

Parent =

Sub 1 =

Sub 2 =

Sub 3 =

Sub 4	=
US Holdco:	=
DRE 1	=
DRE 2	=
DRE 3	=
DRE 4	=
DRE 5	=
DRE 6	=
DRE 7	=
DRE 8	=
DRE 9	=
Foreign Holdco	=
CFC 1	=
FC	=

Date 1	=
Date 2	=
Date 3	=
Date 4	=
Date 5	=
Date 6	=
Date 7	=
Date 8	=
Date 9	=
Date 10	=
<u>aa</u>	=
<u>bb</u>	=
<u>cc</u>	=
<u>dd</u>	=
<u>ee</u>	=
<u>ff</u>	=
<u>gg</u>	=
<u>hh</u>	=
<u>ii</u>	=
<u>jj</u>	=
<u>kk</u>	=

<u>ll</u>	=	
<u>mm</u>	=	
<u>nn</u>	=	
<u>oo</u>	=	
<u>pp</u>	=	
<u>qq</u>	=	
<u>rr</u>	=	
<u>ss</u>	=	
State A	=	
Foreign Holdco Debt Instruments	=	
DRE 9 Debt Instruments	=	
Sub 1 Debt Instrument	=	

ISSUE(S):

1) Whether the Cross-Chain Sale (defined below) qualifies as a reorganization under section 368(a)(1)(D) (a “D Reorganization”)?

2) Assuming the Cross-Chain Sale qualifies as a D reorganization, whether US Holdco’s basis in Foreign Holdco should be reallocated to and included in the taxpayer’s basis in its CFC 1 stock?

3) Whether the taxpayer is barred by the duty of consistency from re-characterizing the Cross-Chain Sale as a D reorganization, after having reported the transaction as a taxable sale in earlier tax returns.

CONCLUSION(S):

1) The Cross-Chain Sale does not constitute a D reorganization: neither the transferor corporation nor its shareholder was in control of the transferee corporation, and the transferor corporation neither received nor distributed stock in the transferee corporation or distributed its other properties pursuant to a plan of reorganization as required by sections 354(b)(1)(B) and 368(a)(1)(D).

2) Even if the Cross-Chain Sale is assumed to have constituted a D reorganization, US Holdco's basis in Foreign Holdco cannot be reallocated to or included in the taxpayer's basis in its CFC 1 stock: the Cross-Chain Sale predates the effective date of the relevant regulations under sections 358 and 368(a)(1)(D), the taxpayer's proposed reallocation is not permitted under those regulations or other authorities, there is no unrecovered basis to reallocate, and the taxpayer's attempt to appropriate and recover US Holdco's basis in Foreign Holdco is an effort to claim a double tax benefit that is precluded by the *Ilfeld* doctrine.

3) The taxpayer is barred from re-characterizing the Cross-Chain Sale as a D reorganization because it characterized the transaction differently on a prior return, the IRS relied on that prior characterization, and the statute of limitations on correcting the prior return is now closed, to the detriment of the IRS.

FACTS:

During the relevant taxable years, Parent was the parent of an affiliated group of domestic corporations that filed a consolidated return for U.S. federal income tax purposes (the "Parent Group"). Prior to Date 2, the relevant organizational structure was as follows: Parent indirectly owned Sub 1. In one corporate ownership chain, Sub 1 owned all of the common stock in US Holdco, which owned DRE 1, which owned DRE 2, which owned Foreign Holdco, which owned aa percent (less than 50 percent) of the sole outstanding class of stock in FC (the remaining FC stock was publicly traded). US Holdco had a class of preferred stock outstanding, all of which was owned by one or more unrelated persons. In a second corporate ownership chain, (a) Sub 1 owned Sub 2 and Sub 3, (b) Sub 3 owned DRE 3 and Sub 4, (c) Sub 2, Sub 3, Sub 4, and DRE 3 collectively owned CFC 1,[1] and (d) CFC 1 owned DRE 4, which owned DRE 5, which owned DRE 6, which owned DRE 7, which owned DRE 8, which owned DRE 9.

Sub 1, Sub 2, Sub 3, and Sub 4 were subsidiaries (within the meaning of Treas. Reg. § 1.1502-1(b)) of the Parent Group. US Holdco, a domestic corporation, was not a

[1] It is possible that all of CFC 1's stock might have been directly owned by Sub 3 at the time of the Cross-Chain Sale, rather than as stated in the facts. This does not in any way alter the conclusions stated herein.

member of the Parent Group. Foreign Holdco, an entity classified as a corporation under Treas. Reg. §§ 301.7701-1, *et seq.* (the "entity classification regulations"), was a "controlled foreign corporation" within the meaning of section 957(a)(1) ("CFC"), as to which US Holdco was a "United States shareholder" within the meaning of section 951(b) ("US Shareholder"). CFC 1, an entity classified as a corporation under the entity classification regulations, was a CFC as to which Parent Group members were US Shareholders. FC was a foreign entity classified as a corporation under the entity classification regulations.

DRE 1 and DRE 2 were classified as entities disregarded as separate from their owner under the entity classification regulations ("disregarded entities"), and thus were treated as branches or divisions of US Holdco. DRE 3 was a disregarded entity, and thus was treated as a branch or division of Sub 3. DRE 4, DRE 5, DRE 6, DRE 7, DRE 8, and DRE 9 were disregarded entities, and thus were treated as branches or divisions of CFC 1.

Original Acquisition of FC

Parent indirectly acquired shares in FC during its taxable year ending on Date 1. In that taxable year, Sub 1 incorporated and transferred bb to US Holdco in exchange for all of US Holdco's common stock, and unrelated persons transferred cc to US Holdco in exchange for all of its single class of preferred stock. At that time, US Holdco's preferred stock represented dd percent, and its common stock represented ee percent (less than 80 percent), of the total value of all classes of its stock. US Holdco's preferred stock represented ff percent, and its common stock represented gg percent (less than 80 percent), of the total voting power of all classes of its stock. US Holdco was not a member of the Parent Group nor was it included in the Parent Group's consolidated return.

US Holdco (acting through disregarded entities) formed Foreign Holdco and transferred hh to it in exchange for all of its stock. CFC 1 received ii from unrelated persons in exchange for the issuance of the Foreign Holdco Debt Instruments, and it purchased its FC stock in exchange for jj (approximately equal to the sum of hh and ii).

Cross-Chain Sale of FC Stock

Prior to Date 2, Parent decided to acquire additional shares of FC stock, and to hold all of its FC share ownership through DRE 9. At that time, the value of the FC stock owned by Foreign Holdco was substantially less than what Foreign Holdco had paid for it. US Holdco, DRE 1, DRE 2, and Foreign Holdco were all holding companies, and the FC stock was by far the most meaningful asset in that chain of entities. Thus, there was a corresponding decline in the value of Foreign Holdco's stock and in S2's common stock. As of Date 2 and Date 3, the US Holdco common stock continued to represent gg percent of the total voting power of all classes of its stock; however, its value had declined to kk percent of the total value of all classes of its stock (the US Holdco preferred stock, which had retained its value, had come to represent ll percent of the total value of all classes of US Holdco's stock).

On Date 2, US Holdco adopted a plan of dissolution and liquidation. Consistent with the plan, the following steps were implemented. On Date 3, Foreign Holdco transferred (the "Cross-Chain Sale") all of its shares of FC stock to DRE 9 in exchange for mm, consisting of nn in the form of the DRE 9 Debt Instruments issued by DRE 9 and oo in the form of the Sub 1 Debt Instrument. The amount paid (mm) represented a premium over the trading price of the FC stock, due to the effective control provided by the aa percent block of FC stock. On that same day, Foreign Holdco distributed the Sub 1 Debt Instrument to US Holdco (through disregarded entities) in redemption of a portion of its outstanding shares. On Date 4, US Holdco filed its plan of dissolution with the relevant authority for State A. The day following Date 4, US Holdco collected pp on the Sub 1 Debt Instrument, made a liquidating distribution of almost all of its cash to its preferred shareholders in cancellation of its preferred shares, settled its liabilities with its creditors, and distributed its remaining assets (including its stock in Foreign Holdco, through disregarded entities) to Sub 1. On Date 5, the relevant authority for State A certified that the US Holdco certificate of dissolution had been filed.

The Parent Group filed a consolidated U.S. Corporation Income Tax Return (Form 1120) for the taxable year ending on Date 6 (the "Year 6 Return"), a taxable year that included Date 2, Date 3, Date 4, and Date 5 (Dates 2 through 6 occurred in the same calendar month). On the Year 6 Return, US Holdco's distribution of the Sub 1 Debt Instrument in partial redemption of its stock was treated as a distribution in part payment in exchange for its stock under section 302(a), the dissolution of US Holdco was reported as a taxable liquidation based on section 331, and the Parent Group claimed a capital loss of qq on the liquidation of US Holdco. The Service accepted the Parent Group's Year 6 Return and did not challenge the claimed capital loss. The statute of limitations has run on the Year 6 Return.

As part of its Year 6 Tax Return, US Holdco filed a Form 5471 with respect to its ownership in Foreign Holdco. The Form 5471 reported that US Holdco had redeemed some of its common stock in Foreign Holdco and accordingly reduced the basis in Foreign Holdco to rr. Schedule C of the Form 5471 also showed that Foreign Holdco recorded a loss of ss on its sale of FC. However, Foreign Holdco did not record any net adjustment to earnings and profits on Schedule H on account of the loss.

Events Subsequent to the Sale of FC Stock

On Date 7 (which was in a taxable year subsequent to Date 6), DRE 9 transferred nn to Foreign Holdco in satisfaction of the DRE 9 Debt Instruments, and Foreign Holdco used the proceeds to retire the Foreign Holdco Debt Instruments.

On Date 8 (which was in a taxable year subsequent to Date 7), Sub 1 contributed its interest in DRE 1 (and, indirectly, DRE 2 and Foreign Holdco) to Sub 3, and Sub 3 contributed DRE 1 (thus, indirectly, DRE 2 and Foreign Holdco) to CFC 1. The Parent Group filed a consolidated U.S. Corporation Income Tax Return (Form 1120) for its taxable year ending on Date 8 (the "Year 8 Return"). In its Year 8 Return, the Parent Group filed a statement in accordance with Treas. Reg. § 1.351-3, in which it reported the transfers as nonrecognition exchanges under section 351, and claimed that at the time of the exchanges Sub 1's basis in Foreign Holdco was rr, an amount equal to US Holdco's basis in Foreign Holdco immediately prior to Foreign Holdco's sale of the FC stock to DRE 9, as adjusted to reflect how it treated Foreign Holdco's transfer of the Sub 1 Debt Instrument in partial redemption of its stock.

During its taxable year ending on Date 9, Sub 3 sold the stock of CFC 1 to one or more unrelated persons. The Parent Group filed a consolidated U.S. Corporation Income Tax Return (Form 1120) for the taxable year ending on Date 9 (the "Year 9 Return"). On the Year 9 Return, the Parent Group reported the sale of CFC 1 stock; for purposes of calculating its gain on the sale of CFC 1, the Parent Group claimed that its basis in the CFC 1 stock included rr, based on the Date 8 transfers.

During the examination of the Parent Group's Year 9 Return, the Parent Group admitted that the Treas. Reg. § 1.351-3 statement reporting the Date 8 transfers was erroneous and that the Date 8 transfers had not increased the stock basis in CFC 1. However, the Parent Group claimed for the first time that the Cross-Chain Sale (together with the other contemporaneous steps described above) had qualified as a D reorganization, and that as a result, US Holdco's unrecovered basis in the stock of Foreign Holdco had been reallocated to the basis in shares of CFC 1 held by members of the Parent Group.

LAW AND ANALYSIS:

A. Qualification of Transaction as a Non-Divisive D Reorganization[2]

Section 368(a)(1)(D) defines a D reorganization as a transfer by a corporation of all or a part of its assets to another corporation if immediately after the transfer, the transferor or one of its shareholders, or any combination thereof is in control of the corporation to which the assets are transferred but only if, in pursuance of the plan, stock or securities of the corporation to which the assets are transferred are distributed in accordance with sections 354, 355 or 356.

[2] This memorandum only discusses certain requirements applicable to a non-divisive D reorganization; other applicable requirements are not addressed herein.

Section 368(a)(2)(H) provides that for purposes of determining whether a transaction qualifies as a non-divisive D reorganization, the term “control” has the meaning given such term in section 304(c).

Section 304(c)(1) provides that “control” means the ownership of stock possessing at least 50 percent of the total combined voting power of all classes of stock entitled to vote or at least 50 percent of the total value of shares of all classes of stock.

Section 304(c)(3) provides that the constructive ownership rules of section 318, with certain modifications, apply for purposes of determining control under section 304.

Section 318(a)(2)(C), as modified in its application by section 304(c)(3)(B), provides that if five percent or more in value of the stock in a corporation is owned, directly or indirectly, by or for any person, such person shall be considered as owning the stock owned, directly or indirectly, by or for such corporation, in that proportion which the value of the stock which such person so owns bears to the value of all the stock in such corporation.

Section 318(a)(3)(C), as modified in its application by section 304(c)(3), provides that if five percent or more in value of the stock in a corporation is owned, directly or indirectly, by or for any person, such corporation shall be considered as owning the stock owned, directly or indirectly, by or for such person.

Section 318(a)(5)(A), in general, provides that stock constructively owned by a person by reason of the application of section 318(a)(2)(C) or section 318(a)(3)(C) shall, for purposes of applying such provisions, be considered as actually owned by such person.

Section 354(a) provides that no gain or loss is recognized if the stock of a corporation that is a party to a reorganization is, in pursuance of a plan of reorganization, exchanged solely for stock in another corporation that is a party to the reorganization.

Section 368(b)(2) provides that “a party to the reorganization” includes both corporations, in the case of a reorganization resulting from the acquisition by one corporation of stock or property of the other.

Section 354(b) provides that the nonrecognition rule of section 354(a) does not apply with respect to a non-divisive D reorganization unless the corporation to which the assets are transferred acquires substantially all of the assets of the transferor, and the stock, securities or other properties received by the transferor as well as the other properties of the transferor, are distributed in pursuance of the plan of reorganization.

Section 356(c) provides that if section 354 would apply to an exchange but for the fact that the property received in the exchange consists not only of property permitted by section 354 but also of other property or money, then no loss from the exchange shall be recognized.

1. Control requirement

In a D reorganization, the asset transferor or its shareholder(s) or any combination thereof must own or be considered to own stock in the transferee corporation possessing at least 50 percent of the total combined voting power or 50 percent of the value of all shares of stock. Sections 368(a)(1)(D), 368(a)(2)(H)(i), 304(c).

Neither Foreign Holdco (the transferor corporation) nor US Holdco (its shareholder) actually owned any stock in CFC 1 (the transferee corporation). However, Foreign Holdco and US Holdco are considered to have owned some stock in CFC 1 under the attribution rules.

Sub 2, Sub 3 (directly and through a disregarded entity), and Sub 4, collectively, actually owned all of the outstanding stock in CFC 1. Sub 3 owned all of the stock of Sub 4, and by reason of section 318(a)(2)(C) Sub 3 is considered to have owned all of the stock in CFC 1 that Sub 4 actually owned. Sub 1 directly owned all of the stock in Sub 2 and Sub 3, and by reason of section 318(a)(2)(C) and (a)(5)(A), Sub 1 is considered to have owned all of the stock in CFC 1 actually or constructively owned by Sub 2 and Sub 3 (*i.e.*, 100 percent of CFC 1).

As of Date 2 and Date 3, the common stock in US Holdco owned by Sub 1 represented kk percent (more than five percent but less than 50 percent) of the total value of all of the outstanding US Holdco stock. By reason of section 318(a)(3)(C) (as modified in its application by section 304(c)(3)(B)) and section 318(a)(5)(A), US Holdco is considered to have owned kk percent of the CFC 1 stock constructively owned by Sub 1. US Holdco (through disregarded entities) owned all of the stock of Foreign Holdco; thus, by reason of section 318(a)(2)(C) and (a)(5)(A), Foreign Holdco is considered to have owned 100 percent of the CFC 1 stock constructively owned by US Holdco. Thus, US Holdco and Foreign Holdco each are considered to have owned kk percent of CFC 1's stock (kk percent of 100 percent of CFC 1's stock). The CFC 1 stock constructively owned by Foreign Holdco and US Holdco represented less than 50 percent of the total combined voting power and less than 50 percent of the value of all shares of stock in CFC 1 at the time of the Cross-Chain Sale. As a result, the transaction did not satisfy the control requirement of section 368(a)(1)(D).

The taxpayer proffers the following three theories by which Foreign Holdco and/or US Holdco nonetheless should be considered to have been in control of CFC 1:

a. Step Transaction Doctrine Argument

The taxpayer asserts that for purposes of applying the control requirement of section 368(a)(1)(D), the US Holdco preferred stock should be treated as having been redeemed (or otherwise should be ignored) under the step transaction doctrine because the US Holdco preferred stock was redeemed as part of the same plan.

First, the taxpayer makes this argument notwithstanding its reliance on the US Holdco preferred stock throughout US Holdco's entire corporate existence (i) to exclude US Holdco from the Parent Group's consolidated return, and (ii) to claim a stock loss under sections 331(a) and 165(a) on the US Holdco common stock cancelled in the US Holdco dissolution.[3] The taxpayer asserts that the "planned cash redemption of the [US Holdco preferred stock] can and should be taken into account for the limited purpose of testing control under section 368(a)(1)(D)," even though, at the same time, authorities such as Rev. Rul. 70-106, 1970-1 C.B. 70, prohibit disregarding the US Holdco preferred stock for purposes of section 331.[4] For purposes of this memorandum, we will assume, *arguendo*, that the US Holdco preferred stock can be respected for certain purposes and simultaneously can be disregarded for other purposes.[5]

The step transaction doctrine treats a series of formally separate steps as a single transaction if the steps are integrated and interdependent. Penrod v. Commissioner, 88 T.C. 1415, 1428 (1987). "The existence of an overall plan does not alone . . . justify application of the step-transaction doctrine." Esmark v. Commissioner, 90 T.C. 171, 195 (1988), aff'd, 886 F.2d 1318 (7th Cir. 1989). Although the step transaction doctrine can be used to eliminate meaningless steps in a transaction that serve no purpose other than tax avoidance, it cannot be used simply to ignore economically meaningful transactions. Id.

The taxpayer largely bases its argument on two cases. In Ericsson Screw Machine Products Co. v. Commissioner, 14 T.C. 757 (1950), one corporation (Ecla) transferred its assets to another (Patents) in exchange for all of Patent's stock.

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[3] In addition, had there been no preferred stock, US Holdco would not have been in any position to recognize a loss under section 336(a) upon its liquidating distribution of Foreign Holdco stock to Sub 1 as part of its dissolution.

[4] In Rev. Rul. 70-196, corporation Y owned 75 percent of corporation X, and caused X to redeem the shares held by its minority shareholders, and thereafter adopt a formal plan of liquidation. The ruling held that the plan of liquidation had been adopted at the time the minority shareholders had agreed to be redeemed, and thus the liquidation did not qualify for tax-free treatment under section 332.

[5] The taxpayer does not cite any authority that respected outstanding, non-transitory stock for purposes of section 331 while simultaneously treating that stock as having been redeemed for purposes of section 368, nor does the taxpayer address whether, if the preferred stock should be treated as having been redeemed for purposes of the control requirement, such stock should not also be treated as having been redeemed for purposes of determining whether US Holdco was affiliated with the Parent Group for purposes of sections 1501, *et seq.*

Thereafter and as part of the same plan, Patents consolidated with another corporation (Old Ericsson) to form New Ericsson, and Ecla received stock in New Ericsson in exchange for its Patents stock.[6] As part of the same plan, Ecla gave an option to the former Old Ericsson shareholders to purchase for cash Ecla's stock in New Ericsson, and the option was exercised. The parties had agreed that the former Old Ericsson shareholders would acquire all of the New Ericsson stock, and that Ecla was not to own any of it when the transactions were complete. The court integrated the steps in determining that the transaction was a taxable sale by Ecla of its assets rather than a reorganization under the statutory antecedent to section 368(a)(1)(D).[7]

In Turner Construction Co. v. U.S., 364 F.2d 525 (2d Cir. 1966), one corporation (Old Spencer) transferred cash, furniture and fixtures, and prepaid insurance to a new corporation (New Spencer) in exchange for stock common and preferred stock in New Spencer.[8] Ten days later, Old Spencer transferred its plant and equipment to New Spencer in exchange for cash and a short-term note.[9] The court applied the mutual interdependence formulation of the step transaction doctrine to integrate an initial contribution with a putative sale a handful of days later, and stated that the integrated transactions could have constituted a reorganization within the meaning of a statutory antecedent to section 368(a)(1)(D). Moreover, the court noted that on remand, the trial court was to determine whether New Spencer's subsequent issuance of additional shares to certain of its employees should be integrated with the prior steps, in which case the transaction might not have constituted a reorganization for failure to satisfy the control requirement.[10]

The taxpayer notes that in Ericsson, the transferor (Ecla) and other parties had planned a disposition of the acquiring corporation's stock, whereas here US Holdco and other persons planned for a secondary transfer of cash received. The taxpayer asserts that the underlying legal principle is the same, and that the overall plan of reorganization must be evaluated by taking into account such secondary transfers of consideration received when they are an essential and inseparable step toward the desired result. The taxpayer contends that Turner applies this same general principle.

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[6] The court stated that Patents was "organized and used solely for the convenience of the parties in these particular transaction," and appears to have disregarded Patents. 14 T.C. at 763, citing Gregory v. Helvering, 293 U.S. 465 (1935).

[7] The court held that New Ericsson's basis in the assets formerly held by Ecla for purposes of its depreciation deductions was based on the cost to New Ericsson, and not on the basis of those assets in the hands of Ecla.

[8] Like Ericsson, Turner involved a determination of the taxpayer's basis in depreciable assets.

[9] New Spencer repaid the short term note, and there was evidence that on the day New Spencer satisfied the note it also issued new preferred shares in the approximate amount to Old Spencer.

[10] Turner Construction Co., 364 F.2d at 537. On remand, the trial court found that the integrated transaction had constituted a reorganization, based in part on factual stipulations. Prentis v. U.S., 273 F.Supp. 460 (S.D. NY 1967).

In general, courts have applied step transaction in evaluating whether a transaction is a reorganization; this assertion is unremarkable, but the question of how the overall steps might be viewed, what steps can be integrated, and what constituted the plan of reorganization must be considered. What the taxpayer overlooks is that US Holdco's dissolution was pursuant to a plan to liquidate US Holdco and not pursuant to a plan to reorganize Foreign Holdco, and that even if all of the contemporaneous steps are integrated and treated as a plan to reorganize Foreign Holdco (and if, as taxpayer contends, Foreign Holdco is treated as having *de facto* liquidated), then the control requirement remains unfulfilled.[11]

Section 368(a)(1)(D) looks to the stock ownership – actual or constructive – of the transferor corporation (Foreign Holdco) or its shareholder (US Holdco), in the transferee corporation (CFC 1). Step transaction doctrine cannot give US Holdco additional constructive stock ownership in CFC 1 (the transferee corporation) that it never constructively owned – after all, when all of the contemporaneous steps had been implemented, US Holdco had dissolved (leaving no successor) and all of its stock had been cancelled (leaving it with no shareholders), thus it could not have constructively owned any CFC 1 stock at all under section 318(a)(3)(C). Step transaction doctrine cannot bootstrap Sub 1 into a shareholder of Foreign Holdco, while simultaneously treating Foreign Holdco as having reorganized into CFC 1. At the time the Cross-Chain Sale was effected, US Holdco was Foreign Holdco's sole shareholder, and had been at all times from Foreign Holdco's inception. US Holdco had adopted a plan of dissolution, but it had neither filed its plan with the relevant State A authority nor had it made any liquidating distribution.[12] Foreign Holdco distributed the Sub 1 Debt Instrument to US Holdco (through disregarded entities) and US Holdco made a liquidating distribution of the proceeds thereon to unrelated persons in cancellation of the US Holdco preferred stock; the consideration CFC 1 paid to Foreign Holdco in the Cross-Chain Sale was not distributed to Sub 1. Had Foreign Holdco reorganized, it should have been an empty corporate shell, without assets, prior to the point in time that US Holdco transferred legal ownership of that entity to Sub 1 in a liquidating distribution. Treating Foreign Holdco as

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[11] While the Cross-Chain Sale and the US Holdco dissolution were generally contemporaneous and were all referenced in the US Holdco plan of dissolution, and were all part of an overall plan in a generic sense, the taxpayer does not assert any reason why US Holdco's dissolution should be viewed as contractually binding at the time of the Cross-Chain Sale or as mutually interdependent with, or as an end result of, a plan to reorganize Foreign Holdco. See Esmark, Inc., 90 T.C. at 195; Turner Broadcasting v. Commissioner, 111 T.C. 315, 327 (1998); American Bantam Car Co. v. Commissioner, 11 T.C. 397, 406-407 (1948), aff'd, 177 F.2d 513 (3d Cir. 1949), cert. denied, 339 U.S. 920 (1950). Without additional factual development, we are unable to fully analyze whether the step transaction doctrine would apply as the taxpayer claims.

[12] Moreover, US Holdco's plan of dissolution expressly provided that at any time prior to the effectiveness of a certificate of dissolution, US Holdco's board of directors could abandon the plan without any further action by the shareholders, and could amend the plan in any manner not materially adverse to the holders of any class of its stock without their approval.

having reorganized is not consistent with treating Sub 1 as Foreign Holdco's direct shareholder. Step transaction cannot give the transferor corporation Foreign Holdco additional constructive stock ownership in CFC 1 because Foreign Holdco's shareholder (US Holdco) dissolved, cancelling the US Holdco common stock and thus the attributive link between Foreign Holdco and CFC 1 that existed at the time of the Cross-Chain Sale, and as noted above Sub 1 cannot be considered to have been Foreign Holdco's shareholder nor its successor. The steps cannot be integrated to treat Sub 1 as having engaged in a section 354 or section 356 exchange with CFC 1 (or Foreign Holdco), or otherwise to treat Sub 1 as a shareholder (let alone the majority shareholder) in CFC 1, because due to Sub 1's status as a minority shareholder of US Holdco, the issuance of CFC 1 stock was not a meaningless gesture.

The net effect of what happened, from Sub 1's perspective, is that its economic position in US Holdco had become that of a minority shareholder. A step transaction approach cannot alter this fact. Sub 1 had engineered and implemented a specific structure to acquire its FC stock investment, and as part of that structure it arranged for US Holdco to issue voting preferred stock instead of debt, which had the effect of excluding US Holdco from the Parent Group.[13] In order to acquire full economic ownership of the FC stock, Sub 1 arranged to economically purchase the interest of US Holdco's majority shareholders (which, at that time, the preferred stock represented), and to do so in a manner that allowed it to crystallize and claim a significant stock loss on its investment through the US Holdco dissolution. The taxpayer now seeks to have these steps viewed differently, as part of an attempt to claim a double tax benefit for a single economic loss. However viewed, at the conclusion of all of the contemporaneous steps, assuming that there had otherwise been a reorganization of Foreign Holdco, the very thing that section 368(a)(1)(D) requires – that Foreign Holdco (the transferor) or US Holdco (its shareholder) be in control of CFC 1 – was not present.

The taxpayer, in effect, seeks to disregard the US Holdco preferred shares or the fact that those shares were held by unrelated persons and had come to represent the majority interest (by value) in US Holdco. Those shares were not transitory – the shares were outstanding throughout US Holdco's entire corporate existence, were issued along with the common stock on the same day and as part of the same plan and were cancelled along with the common stock on the same day and as part of the same plan, and were held by unrelated persons through the entire time they were outstanding. The US Holdco preferred shares bore substantial economic rights, which were respected when in its dissolution US Holdco distributed pp in cash to the preferred shareholders.[14] In addition, the preferred shares entitled holders to ff percent of the

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[13] See Commissioner v. National Alfalfa Dehydrating and Milling Co., 417 U.S. 134, 148 (1974) ("a transaction is to be given its tax effect in accord with what actually occurred and not in accord with what might have occurred.").

[14] In Commissioner v. Spaulding Bakeries, 252 F.2d 693 (2d Cir. 1958), the same shareholder held all of the common and preferred stock in a subsidiary corporation that was liquidated. The court respected the preferred stock because the terms of the preferred stock gave the preferred shareholders the rights to all

total voting power of all classes of US Holdco stock. The taxpayer does not contend that these economic or voting rights were illusory, and in fact the taxpayer relied on these rights to exclude US Holdco from the Parent Group and to claim a capital loss on US Holdco's dissolution.

Finally, there is another, inescapable fact – all of US Holdco's stock, both common and preferred, was issued at the same time, and subsequently was canceled as part of the same plan of liquidation, on the same day, after US Holdco's plan of liquidation had been filed with the relevant State A authority. The taxpayer presents no argument to justify disregarding the preferred stock while simultaneously respecting the common stock, especially since both were outstanding at all times during US Holdco's existence, both had substantial economic value and voting rights at all relevant times, and the preferred stock was held by unrelated persons.

The cases that the taxpayer relies upon are inapposite. It was a relatively straightforward matter to determine who owned those shares in those cases, and the relevant stock ownership in the transferee corporation was direct. In contrast, here Foreign Holdco's and US Holdco's underlying stock ownership in CFC 1 was constructive. The relevant section 318(a)(2)(C) attributive link ran through US Holdco. There was no plan to reorganize US Holdco; rather, the plan was to dissolve US Holdco in a liquidation that was specifically structured to ensure that Sub 1 could claim a capital loss on its US Holdco stock. Immediately after US Holdco's dissolution, all of its stock had been cancelled, no person owned any US Holdco stock, and the relevant section 318(a)(2)(C) attributive linkage was severed. The cases cited by the taxpayer involved the direct stock ownership context; here, the multiple tiers of ownership present key, distinguishable facts.

b. Option to Purchase

Section 318(a)(4) provides that, for the purpose of the constructive ownership rules, any person that has the option to acquire stock should be treated as a shareholder.

The taxpayer contends that US Holdco's preferred stock should be ignored in determining control because once its plan of dissolution had been adopted, US Holdco had a unilateral right (and thus had an option) to purchase its outstanding preferred stock. An option is a "promise which meets the requirements for the formation of a contract and limits the promisor's power to revoke an offer." Restatement (Second) of Contracts § 25 (1981) (cited in Saviano v. Commissioner, 80 T.C. 955, 970 fn. 20 (1983), aff'd, 765 F.2d 643 (7th Cir. 1985)). The US Holdco plan of dissolution was adopted by US Holdco's board of directors and approved by the shareholders, but it

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of the proceeds of the corporation upon dissolution. See also H.K. Porter Co., Inc. v. Commissioner, 87 T.C. 689 (1986).

lacked the essential requirements of a contract. By its own terms, the US Holdco plan of dissolution could be abandoned or modified by US Holdco's board of directors without shareholder approval. It did not create enforceable contractual rights for the shareholders, and thus did not meet the definition of an option. US Holdco simply had board approval to redeem preferred shareholders, not an actual option.

Additionally, even assuming US Holdco held an option on its own preferred stock, Rev. Rul. 69-562, 1969 C.B. 48, would not allow such an option to be used to treat Sub 1 as the owner of those shares for purposes of section 318(a). In Rev. Rul. 69-562, the Service stated that it would be meaningless to attribute ownership of a corporation's stock to itself because "the corporation does not acquire voting or other rights as a shareholder by acquiring its own stock through exercise of an option." Similarly, the ruling's logic makes it clear that such an option would not be deemed exercised (and thus no longer outstanding) for purposes of determining the quantum of ownership represented by US Holdco's common stock held by Sub 1. Therefore, US Holdco and Foreign Holdco's constructive interest in CFC 1 would not change, even if US Holdco were considered to have had an option on its own preferred stock.

c. "Any Combination Thereof" Argument

The taxpayer claims that Foreign Holdco and US Holdco, based on their cumulative interests, were in control of CFC 1 under the constructive ownership rules. Under section 368(a)(1)(D), "immediately after the transfer the transferor, or one or more of its shareholders . . . **or any combination thereof**" (emphasis added) must control the transferee. The taxpayer looks to the interest of transferee constructively held by Foreign Holdco (*i.e.*, kk percent), and the interest constructively held by US Holdco (*i.e.*, kk percent), and adds these interests together to determine the "combined" interest of transferor and its shareholder. By combining the interests in this way, the taxpayer determines that the two parties combined own more than 50 percent of CFC 1, which would have satisfied the control requirement.

This argument is unconvincing. First, the taxpayer is unable to cite any authority that supports multiple inclusion of the same stock ownership for purposes of attribution. Second, the argument interprets section 368(a)(1)(D) in a manner that would lead to nonsensical results – if the same stock could be counted twice, why not more than twice?[15] Third, implicitly recognizing the absurdity (and, depending on context, the potential unfairness) of duplicative inclusions, Treas. Reg. § 1.318-1(b)(2) states that in applying section 318(a) to determine the stock ownership of any person, if the amount of stock owned by any person may be included in the computation more than one time, such stock shall be included only once. US Holdco and Foreign Holdco do not hold any

[15] "An interpretation of a statute leading to an absurd result is to be avoided where reasonably possible." Atchison T. & S.F. Ry. Co. v. United States, 295 U.S. 193, 208 (1935), citing United States v. Katz, 271 U.S. 354, 357 (1926) and Territory of Hawaii v. Mankichi, 190 U.S. 197, 212 (1903).

actual interest in CFC 1 and only hold a constructive interest in CFC 1 based on section 318(a). Each corporation's constructive interest is based on the same actual stock held by Sub 2, Sub 3 (directly and through a disregarded entity), and Sub 4, attributed to both Foreign Holdco and US Holdco through Sub 1's ownership of US Holdco's common stock. In determining the combined interest of Foreign Holdco and US Holdco, the actual stock held by Sub 2, Sub 3 and Sub 4 can only be considered once. By combining Sub 1 and CFC 1's constructive interest, the taxpayer is impermissibly including the same stock in the calculation of attribution under section 318(a).[16]

When the actual stock attributable to Foreign Holdco and US Holdco is considered only once in determining constructive ownership, the result is that Foreign Holdco and US Holdco's constructive interest in CFC 1 is only kk percent, which does not constitute control.

d. Conclusion as to Control

Neither the transferor corporation (Foreign Holdco) nor its shareholder (US Holdco) was in control of the transferee corporation (CFC 1), for purposes of section 368(a)(1)(D). This is not surprising – at the time of the Cross-Chain Sale, the Parent Group had come to economically own only an indirect kk percent interest in the underlying FC stock. The US Holdco preferred shareholders – unrelated to the Parent Group – indirectly owned ll percent (more than 50 percent) of the FC stock held by Foreign Holdco, through what had economically become the majority interest in US Holdco. By means of the Cross-Chain Sale and US Holdco's dissolution, the Parent Group in essence purchased from the US Holdco preferred shareholders their economic interest in the FC stock, structured in a way that allowed the Parent Group to claim a capital loss on the US Holdco stock but that did not give Foreign Holdco or US Holdco control of CFC 1. As a result of the absence of control, the Cross-Chain Sale did not qualify as a D reorganization.

2. Distribution Requirement

Section 368(a)(1)(D) states that a transaction can qualify as a D reorganization "only if, in pursuance of the plan, stock or securities of the [acquiring] corporation are distributed in a transaction that qualifies under section 354, 355, or 356."

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[16] The impermissibility of attributing the same stock to two persons for the sake of determining control is further explained by analogy to section 958. Section 958 provides the attribution rules for determining whether a foreign corporation is controlled by a domestic corporation. Section 958(b) explicitly makes section 318(a) applicable, *inter alia*, for purposes of determining whether a corporation is a controlled foreign corporation. An example in the regulations under section 958 demonstrates that constructive interest based on the same stock can only be considered once. See Treas. Reg. § 1.958-2(f)(2), ex. 1(b). The example demonstrates that if a person constructively owns stock through another person, combining the two persons' interests improperly duplicates the same stock interest.

Section 354(b)(1)(B) provides that section 354 does not apply to a D reorganization unless "the stock, securities, and other properties received by [the target], as well as the other properties of such [target], are distributed in pursuance of the plan of reorganization." See also Treas. Reg. § 1.368-2(l)(1) (applicable to transactions occurring on or after Dec. 18, 2009).

a. Requirement that Transferor's Stock be Distributed

As part of a D reorganization, the asset transferor must distribute the stock that it received from transferee. However, in the Cross-Chain Sale, CFC 1 did not issue any stock, Foreign Holdco did not receive any stock from CFC 1, and Foreign Holdco did not distribute any stock CFC 1 stock to its shareholder. In addition, the taxpayer asserts that CFC 1 paid full value in the Cross-Chain Sale; thus, there is no basis to treat CFC 1 as having constructively issued shares in the transaction to account for any shortfall in the consideration paid.[17]

In certain circumstances, an actual issuance by transferee and distribution of that stock by transferor is not required, where the issuance would have been a meaningless gesture. In the most basic case, the stock distribution requirement is met when the stock of the transferor and transferee are directly owned by the same shareholders in the same proportions. In Rev. Rul. 70-240, 1970-1 C.B. 81, shareholder B owned all of the stock of both X corporation and Y corporation. X sold its operating assets for full value to Y in exchange for a cash payment. X paid its debts, and transferred its remaining assets to B in a liquidating distribution. The Service ruled that even though X had not distributed any shares of Y stock to B, nonetheless B would be treated as having received Y stock (thus satisfying the distribution requirement) since B already owned all the stock of Y. Where the same shareholders own a proportionate share of transferor and transferee, the issuance and distribution of stock is a meaningless gesture because it does not change the shareholders' proprietary interest in the assets. James Armour, Inc. v. Commissioner, 43 T.C. 295, 307 (1964). See also Commissioner v. Morgan, 288 F.2d 676, 679-680 (3d Cir. 1961), cert. denied, 368 U.S. 836 (1961); Davant v. Commissioner, 366 F.2d 874 (5th Cir. 1966), cert. denied, 386 U.S. 1022 (1967). In all of these cases, the shareholders of the transferor corporation had preserved their proprietary interest in the underlying business, albeit in the form of a different corporate entity. This is merely a change in form of ownership rather than a change in shareholders' economic position with respect to the underlying business. Therefore, there is no need to issue and distribute stock where the transferor corporation's shareholders' interest is preserved even absent the issuance of stock.

[17] See Treas. Reg. § 1.368-2(l)(2)(i) (generally applicable to transactions occurring on or after December 18, 2009) (by reason of the second sentence, an acquiring corporation is deemed to have constructively issued its shares where the consideration it paid is less than the value of the target corporation's assets).

Under a similar rationale, some courts have even found D reorganizations in the absence of actual stock distributions where the same shareholders held the stock of the transferor and the transferee in similar but non-identical proportions and the shareholders substituted their interest in the transferor corporation for substantially the same interest in the transferee corporation. In one case, Moffatt v. Commissioner, 42 T.C. 558 (1964), aff'd 363 F.2d 262 (9th Cir. 1966), cert. denied, 386 U.S. 1016 (1967), the three primary shareholders of a corporation wanted to add a long-time employee as a shareholder, so they formed a new corporation where the employee held a 10 percent share. The old corporation sold all of its assets to the new corporation and liquidated. The new corporation purchased all of the assets of the old corporation and hired all the staff of the old corporation. The shareholders for the liquidating corporation claimed a capital gain, claiming that the transaction qualified as a taxable distribution, but the court found that this transaction qualified as a D reorganization and the shareholders received boot in the D reorganization. Even though the shareholders of the old corporation only held 90 percent of the stock in the transferee corporation, their interest in the underlying business was substantially preserved and they received boot with respect to their remaining interest. The court looked at the entire transaction and found the transaction to be a D reorganization because the same operations continued in the form of a new transferee corporation. The underlying business existed in a different corporate entity, but the shareholders' interest in the underlying business was substantially the same. The formal issuance and transfer of stock was not required to preserve the shareholders' interest in the underlying business. Similarly, the District Court in Breech v. Commissioner, 23 A.F.T.R. 2d 69-489, 1968 WL 14578 (C.D. Cal.), aff'd on other grounds, 439 F.2d 409 (9th Cir. 1971), found that the "Los Angeles Transaction" qualified as a D reorganization (as well as a reorganization within the meaning of section 368(a)(1)(F)) where three shareholders who owned all of the transferor corporation's stock held 90 percent of the transferee corporation's stock. In the transaction, two shareholders of the old corporation sold their stock to a third shareholder. The same shareholders formed a new corporation with two other shareholders. The court found this to be a stock-for-stock exchange because the consideration that the shareholders received for their old stock was based on their proportionate share of the underlying assets in the new corporation.

Other cases that the taxpayer cites for the proposition that stock need not be issued and distributed in a D reorganization involved taxable years that pre-date the 1954 enactment of the distribution requirement. Pebble Springs Distill. Co. v. Commissioner, 23 T.C. 196 (1954), aff'd, 231 F.2d 288 (7th Cir. 1956); Liddon v. Commissioner, 22 T.C. 1220 (1954), rev'd on other grounds, 230 F.2d 304 (6th Cir. 1956); Heller v Commisioner, 2 T.C. 371, 383-384 aff'd 147 F.2d 376 (9th Cir. 1945), cert. denied, 325 U.S. 868). In each of these cases, a group of shareholders had control of (or at least a near-controlling interest in) both the transferor and transferee corporation, and the shareholders of the old corporation held substantially the same economic interest in the new corporation.

In Pebble Springs, the focus of the inquiry was to determine whether the old corporation could claim a loss on the sale of its assets. The old corporation had sold all of its operating assets to a new corporation, and dissolved. Persons who collectively owned 75.9 percent of the transferor corporation owned 87.5 percent of the transferee corporation. The court held that the transaction met all the requirements of 1939 Code's predecessor to section 368(a)(1)(D); the court found that the shareholders of the old corporation owned stock in the new corporation that constituted control (as that term was defined under the law then in effect), hence the literal requirements of that earlier version of the D reorganization were met. In addition, the court held that the steps, added together, constituted a clear plan of reorganization. In Liddon, the tax court was trying to determine whether shareholders were entitled to treat proceeds from the liquidation of a corporation as capital gain. The taxpayers that owned 80 percent of the stock in the transferor corporation owned more than 99 percent of the stock in the transferee corporation. Again, the transferor corporation sold its assets to the transferee corporation, but neither received nor distributed any transferor corporation stock to its shareholders. The court reasoned that when viewing all of the transactions as a whole, the shareholders had in effect exchanged their old stock for a combination of new stock and money. Therefore, they did not receive capital gain treatment and any proceeds that they received were taxed as a boot dividend. In Heller, a group of three shareholders held all of the stock in the transferor and transferee corporations, although in somewhat different proportions. The court found that the shareholders had substituted their interest in the old corporation for substantially the same interest in the new corporation, and that the net effect of all the steps taken was that the three shareholders exchanged their stock in one corporation for stock in the other pursuant to a plan of reorganization.

In each of these and other cases, the courts evaluated the transactions in their entirety, and concluded that the shareholders of the transferor corporation had in substance exchanged their shares for stock in the transferee corporation, as part of a plan to reorganize the transferor corporation. As stated in Morgan v. Commissioner, "although there was not a direct exchange of stock in the old corporation for stock in the new, plus 'other property or money,' that was the net effect of what was done." 288 F.2d at 680, (quoting Liddon, 230 F.2d at 306-307). These cases are all notable because stock was considered to have been issued and exchanged and the shareholders' interest in the transferor corporation's stock was preserved in transferee corporation stock.

The application of the meaningless gesture doctrine, however, has generally been limited to situations in which there is identical shareholder identity and proportionality of interest, T.D. 9303. 71 Fed. Reg. 75879, 75880 (Dec. 19, 2006), or at least a substantial similarity. Where there are significant disparities in ownership between the transferor and transferee corporations, an issuance and distribution of the transferee corporation's stock is not a meaningless gesture because a share of the transferor corporation imbues very different economic interest to its shareholder with respect to the underlying assets than a share of the transferee corporation. This is illustrated in Warsaw Photographic Assocs., Inc. v. Commissioner, 84 T.C. 21 (1985), where the Tax Court found that the distribution requirement was not satisfied when the same 10 shareholders that held 100 percent of the transferee corporation held only 20 percent of the transferor corporation's stock. The Tax Court found that the transaction did not qualify as a D reorganization when the largest shareholder of the old corporation was not a shareholder in the new corporation. In Warsaw Photographic, the Tax Court stated that where stock ownership in the transferor and transferee corporations is identical, an actual distribution would be a mere formality and the statute may be satisfied without it. 84 T.C. at 37 (citations and quotation marks omitted). However, the court held that the meaningless gesture did not apply due to the significant variation in stock ownership. The court also found that the substance of the transaction at issue there pointed toward a sale at least as much as toward a reorganization. 84 T.C. at 40.

In this case, US Holdco wholly owned Foreign Holdco, the transferor corporation, but constructively held kk (less than 50) percent of CFC 1, the transferee corporation. This ownership disproportionality is far closer to the Warsaw Photographic than Moffatt or Breech. In this case, the interest of US Holdco (the transferor's shareholder) in the underlying assets fundamentally changed after the Cross-Chain sale. Prior to the Cross-Chain sale, US Holdco indirectly owned 100 percent of the FC stock held by Foreign Holdco. After the Cross-Chain Sale, US Holdco's indirect interest in the FC stock was replaced with debt instruments (although US Holdco continued to own constructively, but not economically, a kk percent interest in CFC 1, and thus the FC stock). In short, the economic position of Foreign Holdco's shareholder with respect to Foreign Holdco's underlying assets had substantially changed. Courts have overlooked the distribution requirement when shareholders' interests in the underlying assets are preserved. However, when the shareholders' interests vary so widely, the statutory requirements are not waived and stock must be issued and distributed.

Treas. Reg. § 1.368-2(l)(2) does not apply to deem the issuance of a nominal share of CFC 1 stock in the Cross-Chain Sale. First, as discussed below, the Cross-Chain Sale predates the effective date of the regulation, and the taxpayer is not allowed to retroactively apply the regulation under the circumstances. Second, the same person or persons do not own the stock of the transferor (Foreign Holdco) and transferee (CFC 1) corporations in identical proportions, as required by Treas. Reg. § 1.368-2(l)(2)(i). Rather, Sub 1 constructively owned a minority (by value) interest in Foreign Holdco and 100 percent of CFC 1, whereas unrelated persons owned a majority (by value) interest in Foreign Holdco and no stock whatsoever in CFC 1. The US Holdco stock has significant voting rights, so it is not described in section 1504(a)(4) and thus must be taken into account for purposes of the regulation. See Treas. Reg. § 1.368-2(l)(2)(iii). Treas. Reg. § 1.368-2(l)(2)(iii) tempers the exact identity and proportionality requirement of Treas. Reg. § 1.368-2(l)(2)(i) and applies the meaningless gesture doctrine if there is a *de minimis* variation in shareholder identity or proportionality of ownership. The variation here, however, is substantial, far exceeding anything that might be considered *de minimis*.

b. Requirement that Transferee's Other Properties be Distributed

Under Section 354(b)(1)(B), the transferor must distribute not only the stock, securities, and other properties that it received from the transferee, but also all of its other properties, in pursuance of the plan of organization.

The taxpayer states that Foreign Holdco *de facto* dissolved in Year 6, and thereby satisfied this requirement. However, based on the returns as filed, Foreign Holdco continued to hold more "other properties" after the Cross-Chain Sale. In the Cross-Chain Sale, Foreign Holdco received the DRE 9 Debt Instruments, which represented more than half (by value) of the consideration it received for its FC stock. Foreign Holdco did not distribute the DRE 9 Debt Instruments; rather, Foreign Holdco retained the DRE 9 Debt Instruments until their retirement on Date 7, which was in a subsequent tax year. Foreign Holdco also continued to have "going concern" financial statements prepared by its public accounting firm, and Foreign Holdco's US shareholders continued to file returns (Forms 5471) for Foreign Holdco on a going concern basis and reporting assets and liabilities, until at least Date 9. Foreign Holdco did not distribute all of its assets in Year 6, the year of the Cross-Chain Sale. Accordingly, the transaction fails to meet the distribution requirement.

c. Conclusion as to the Distribution Requirement

Foreign Holdco neither distributed stock or securities of the transferee corporation nor its other properties pursuant to a plan of reorganization, and the stock distribution requirement cannot be treated as having been satisfied either under the meaningless gesture authorities or regulations. As a result, the Cross-Chain Sale did not qualify as a D reorganization.

B. Reallocation of Shareholder's Basis in its Stock in the Transferor Corporation

Section 358(a)(1) provides, in part, that in the case of an exchange to which section 354 or 356 applies, an exchanging shareholder's basis in the stock of the acquiring corporation received in the exchange is the same as its basis in the stock of the target corporation surrendered in the exchange, (A) decreased by the fair market value of any other property and by the amount of money received, and (B) increased by the amount of such money or property that was treated as a dividend and the amount of gain recognized by the shareholder on the exchange.

Treas. Reg. § 1.368-2(l)(2)(i) provides that in certain situations where the same persons directly or indirectly own stock in a transferor and transferee corporation in identical proportions, for purposes of the distribution requirement applicable to a D reorganization the transferee corporation is deemed to issue a nominal share of its stock, which is then deemed to be distributed by the transferor corporation to its shareholders. Where appropriate, the nominal share is deemed to be further transferred through chains of ownership to the extent necessary to reflect the actual ownership of stock in the issuing corporation.

Treas. Reg. § 1.358-2T(a)(2)(iii)(C) provides that if an actual shareholder of an issuing corporation is deemed to receive a nominal share of stock of the issuing corporation described in Treas. Reg. § 1.368-2(l), the shareholder must, after adjusting the basis in the nominal share for any transfers described in Treas. Reg. § 1.368-2(l), designate the share of stock in the issuing corporation to which the basis, if any, of the nominal share will attach.

Section 334(a) provides that if property is received in a distribution in complete liquidation, and if gain or loss is recognized on the receipt of the property, then the basis of the property in the hands of the distributee shall be the property's fair market value at the time of the distribution.

Assuming, *arguendo*, that the Cross-Chain Sale qualified as a D reorganization, the taxpayer argues that US Holdco's basis in Foreign Holdco must be preserved, and that the taxpayer can choose the share of stock to which the basis is reallocated. The taxpayer bases its argument on caselaw and on Treas. Reg. § 1.358-2.

1. Preservation of Basis

The taxpayer proffers a general theory of basis preservation based on the Davant case, discussed above. That case involved a situation where the court found that the transaction qualified as a D reorganization notwithstanding that no transferee corporation stock had been issued to the transferor corporation. In a footnote, the court noted that the shareholders' bases in their transferor stock should be added to their bases in the transferee stock, in order to account for their economic interests in the transferor. 366 F.2d at 887, n. 26. The taxpayer further advocates a theory of basis preservation by analogy to the redemption regulations. In Example 2 of Treas. Reg. § 1.302-2(c), a husband and wife each own 50 percent of the stock in a corporation. The husband's shares are redeemed by the corporation but the distribution is deemed equivalent to a dividend because of his wife's continued interest in the corporation. The example states that the husband's basis is preserved in the wife's shares.

As a threshold matter, US Holdco's basis in Foreign Holdco would have been preserved in any CFC 1 stock it might be deemed to have received (or in the Foreign Holdco stock it owned). At the time of the Cross-Chain Sale, US Holdco had already adopted its plan of dissolution, and its liquidating distribution of such CFC 1 stock (or of the Foreign Holdco stock it actually owned) would have been a recognition event to US Holdco under section 336(a). Basis would have been preserved and recovered, if at all, by US Holdco in its final return.

The cases the taxpayer cites do not support its argument. In Davant, there was a common identity of ownership between the transferor and transferee, and the ownership was direct. The Davant court's articulation is instructive:

> It follows logically from what we have said that the basis formerly belonging to petitioners' Warehouse stock must now be added to the basis of their Water stock. Had the assets of Warehouse been transferred to Water for Water's stock, as they would have been if this transaction had actually been cast as reorganization, the Water stock would have received the basis of petitioners' Warehouse stock when Warehouse was liquidated. See Treasury Reg. 1.358-1. A different result should not be obtained just because petitioners received no new stock but merely allowed their existing stock to appreciate in value. Cf. Treasury Reg. 1.302-2(c).

366 F.2d at 887, n. 26 (emphasis added). Davant expressly grounded this point on ensuring that the shareholders' results would mirror those that would have happened had there been an actual issuance of stock. And where shareholder directly owns both transferor and transferee stock, as in Davant, it is a simple matter to reallocate basis from one to the other.[18]

Where the transaction occurs among lower-tier entities and the stock ownership is indirect, such as in the case under consideration, had shares actually been issued the basis results would differ due to the need to transfer such shares through the ownership chains to the actual owner.[19] Here, Sub 2, Sub 3 (directly and through a disregarded entity), and Sub 4, collectively, were the sole shareholders of CFC 1 at all relevant

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[18] Similarly, in U.S. v. Davis, 397 U.S. 301 (1970), a shareholder directly owned a corporation's common and preferred stock, and his preferred stock was redeemed in a transaction held to be essentially equivalent to a dividend. The Court indicated that the shareholder's basis in the redeemed preferred stock would be applied to his basis in the common stock he continued to own. 397 U.S. at 307, fn. 9.

[19] The taxpayer has not cited any case involving a lower-tier transaction in which basis has been reallocated as it seeks.

times. Had CFC 1 actually issued stock to Foreign Holdco in the Cross-Chain Sale, and had Sub 2, Sub 3 and Sub 4 continued to maintain their complete direct ownership of CFC 1, then somehow that CFC 1 stock would have had to have been distributed up the chain from Foreign Holdco to US Holdco to Sub 1, and then contributed down the ownership chain to Sub 2, Sub 3, and Sub 4. Had those steps actually occurred, US Holdco would have had to have distributed the stock in a liquidating distribution, because it had already adopted its plan of dissolution. In that dissolution, US Holdco would have recognized loss (and recovered its stock basis) under section 336(a), if at all, and Sub 1 would have taken a basis in that stock equal to its fair market value on the date of dissolution by reason of section 334(a). To paraphrase the Davant rationale, "a different result should not be obtained just because [the taxpayer] received no new stock [in CFC 1] but merely allowed [its] existing stock to appreciate in value." Given that CFC 1 paid full value for the FC stock, any actual stock CFC 1 might have issued to Foreign Holdco would have to have had a *de minimis* value. And if, as taxpayer asserts, CFC 1 should be treated as having issued a nominal share, such share would have a $0 value. And in either case, the mechanical basis rules would have allowed US Holdco to recover its basis, and Sub 1's basis would have been set to equal the date-of-distribution value (and would not have had any relation to anyone else's basis in that stock). After that point, the date-of-distribution-value basis would have been transferred by Sub 1 down the ownership chain, with the result that the basis in CFC 1 would have increased, at most, by a *de minimis* amount. This is consistent with Example 16 in Treas. Reg. § 1.358-2T(c) and Example 4 in Treas. Reg. § 1.1502-13(f)(7)(i).

The taxpayer also invokes Example 2 of Treas. Reg. § 1.302-2(c). That example, which occurs in the context of a redemption transaction and illustrates the rule in Treas. Reg. § 1.302-2(c), which provides that "proper adjustment" of the basis of the remaining stock will be made with respect to the stock redeemed. That example shows what the "proper adjustment" would be with respect to its facts. Here, the facts are materially different, because there is no unrecovered basis. In addition, a "proper adjustment" would not cause the stock basis in CFC 1 to increase. As discussed below, any adjustment increasing the basis in CFC 1 stock would allow the Parent Group to claim a duplicative tax benefit for a single economic loss, a result which is precluded under the Ilfeld doctrine.

The Davant rationale is sound. Prior to the Cross-Chain Sale, US Holdco had adopted a plan of dissolution, and the taxpayer treated US Holdco's dissolution as a taxable liquidation under section 331. Had any actual CFC 1 shares been issued, Sub 1's basis in those shares would have been set to equal value, and here there was no value. The taxpayer should not get a different answer just because it chose not to cause CFC 1 to issue its stock in the transaction.

2. Duplicative Tax Benefits for a Single Economic Loss

In Charles Ilfeld, Co. v. Hernandez, 292 U.S. 62, 68 (1934), the Supreme Court stated that, absent a clear declaration of intent by Congress, taxpayers are not allowed to deduct the same economic loss more than once. In that case, the Supreme Court determined that the parent of a consolidated group was not able to deduct losses on the dissolution of its subsidiaries because the losses mirrored the economic losses which the consolidated group had taken in prior years. Therefore, it would be inappropriate to deduct the same economic loss twice. Ilfeld is controlling, and precludes the basis reallocation the taxpayer seeks.

To determine whether the same expense constitutes the same economic loss, courts look to what each of the costs represent. In Thrifty Oil Co. v. Commissioner, 139 T.C. 198 (2011), the taxpayer claimed a capital loss on the sale of a subsidiary that had substantial environmental liabilities. In a subsequent year, the taxpayer claimed a further deduction for expenditures made to clean up the property held by the subsidiary that it sold. The court determined that both the capital loss and the environmental clean up expenses represented the actual cost of cleaning up the property. Therefore, this constituted a double deduction on the same economic loss. The court disallowed the clean up expense deduction.

In the present case, the Parent Group (through Sub 1) contributed bb to US Holdco in a section 351 contribution, to fund an indirect investment in the FC stock. Under section 358, the Parent Group (through Sub 1) took a bb basis in US Holdco's stock. When US Holdco liquidated in a taxable liquidation, the Parent Group (through Sub 1) realized and recognized its economic loss on its stock in US Holdco (and, correspondingly, its economic loss on its indirect investment in FC stock). The basis that the taxpayer seeks to reallocated to CFC 1 duplicates Sub 1's initial bb contribution, and represents the potential for the Parent Group to claim a second tax benefit with respect to the pre-Cross-Chain Sale diminution in the value of the FC stock. No statute or other applicable rule clearly or definitely requires or authorizes a double tax benefit in this circumstance. Under the Ilfeld doctrine, the taxpayer is not allowed to include this basis in CFC 1 stock since it would constitute an impermissible double deduction.

3. The "All-Cash D" regulations

The taxpayer argues that regulations issued in 2009 allow it to designate the share of CFC 1 stock to which US Holdco's basis in Foreign Holdco would attach. However, the Cross-Chain Sale occurred prior to the effective date of the regulations, and in any event the regulations do not apply as the taxpayer demands.

In 2006, temporary regulations were issued[20] under section 368(a)(1)(D) to address the distribution requirement (the "2006 regulations"). The 2006 regulations provided that the distribution requirement would be treated as having been satisfied

[20] T.D. 9303, 71 Fed. Reg. 75879 (Dec. 19, 2006).

notwithstanding the absence of a stock issuance if the same person or persons owned, directly or indirectly, all of the stock of the transferor and transferee corporations in identical proportions. In such a case, the transferee corporation would be deemed to have issued a nominal share of its stock to the transferor corporation in addition to the actual consideration exchanged. Temp. Treas. Reg. § 1.368-2T(l)(2)(i) (2006). For this purpose, *de minimis* variations in stock ownership and preferred stock described in section 1504(a)(4) were not to be taken into account. Temp. Treas. Reg. § 1.368-2T(l)(2)(iii) (2006).

In 2009, final regulations[21] replaced the 2006 regulations. The 2009 regulations retained the nominal share construct. The 2009 regulations contained corresponding modifications to the regulations under sections 358 and 1502. The section 358 provisions allowed shareholders in the nominal share context to designate the share of transferee stock to which the basis of the surrendered stock would attach.

In 2011, temporary regulations were issued[22] under section 358 to clarify the basis consequences resulting from the nominal share construct.

First, these regulations do not apply to the Cross-Chain Sale. The 2006 regulations applied only to transactions occurring after March 18, 2007 and before Dec. 19, 2009. Temp. Treas. Reg. § 1.368-2T(l)(4)(i) (2006). The 2009 regulations apply only to transactions occurring on or after Dec. 18, 2009. Treas. Reg. § 1.368-2(l)(4)(i). The Cross-Chain Sale predates all of these effective dates. The 2006 and 2009 regulations provide that in general, a taxpayer may apply the regulations to transactions occurring prior to the effective date of the regulations provided <u>all</u> of “the transferor corporation, the transferee corporation . . . and any shareholder of the transferor or transferee corporation” apply the provisions of the regulations. Treas. Reg. § 1.368-2(l)(4)(ii). The taxpayer cannot satisfy this latter requirement, because, among other reasons, Foreign Holdco has dissolved, and its final return is time-barred. In addition, at this point in time, the taxpayer neither directly or indirectly has any ownership interest in either Foreign Holdco or CFC 1. If those entities continue to exist, they are beyond the taxpayer’s control, and we have no indication that those entities (or any US Shareholders of those entities) have agreed to apply the provisions of the regulations.

Second the provision in the 2009 regulations that would have allowed reallocation of basis only applied where a shareholder was deemed to have received a nominal share under Treas. Reg. § 1.368-2(l). Treas. Reg. § 1.358-2(a)(iii)(C) (2009). As noted above, no such nominal share construct applies here because the Cross-Chain Sale predates the relevant regulations, and because the stock of Foreign Holdco (transferor) and CFC 1 (transferee) was not held in identical proportions. The US Holdco preferred stock possessed significant, non-transitory voting rights and thus do

[21] T.D. 9475, 74 Fed. Reg. 67053 (Dec. 18, 2009).

[22] T.D. 9558, 76 Fed. Reg. 71878 (Nov. 21, 2011).

not qualify for the section 1504(a)(4) exclusion; these shares would count for purposes of determining proportional ownership.

Finally, assuming *arguendo* that the 2009 regulations somehow applied, the regulations do not permit the taxpayer to reallocate US Holdco's stock basis in Foreign Holdco in the manner it seeks. The 2006 regulations provided that the nominal share of transferee corporation stock deemed to have been issued to the transferor corporation "will then be deemed distributed by the transferor corporation to its shareholders and, where appropriate, further transferred through chains of ownership to the extent necessary to reflect the actual ownership of the transferor and transferee corporations." Temp. Treas. Reg. § 1.368-2(l)(2)(i) (2006). This was explained in the preamble to the 2006 regulations, and illustrated in Ex. 3 of Temp. Treas. Reg. § 1.368-2(l)(3) (2006).

The 2009 regulations continued the nominal share construct, with language substantially similar to that employed in the 2006 regulations. Treas. Reg. § 1.368-2(l)(2)(i). The preamble noted that the nominal share construct was preferable to an approach that simply deemed the distribution requirement to have been satisfied, because the nominal share provided a useful mechanism with respect to stock basis consequences to the exchanging shareholder, preserved remaining basis, if any, and facilitated future stock gain or loss recognition by the appropriate shareholder. T.D. 9475, 74 Fed. Reg. at 67055. The preamble also specifically noted that giving significance to the nominal share for purposes beyond the distribution requirement is consistent with the fundamental premise underlying the intercompany transaction deferral system, which is to preserve the location of gain and loss within a consolidated group. Locational integrity was preserved through the notion that the nominal share is deemed to have been transferred through the chains of ownership prior to any reallocation. The 2009 regulations also added an example to the consolidated return regulations which clearly illustrated the operation of this basis construct. In that example (which involved a transaction among lower-tier members), the shareholder (M) of the transferor corporation (S) is deemed to have received a nominal share of stock in the transferee corporation (B), and adjustments to M's basis in the nominal B share resulted in an excess loss account. Thereafter, M is deemed under Treas. Reg. § 1.368-2(l) to have distributed that nominal share to its shareholder, which resulted in an intercompany gain under section 311(b). Treas. Reg. § 1.1502-13(f)(7)(i), Ex. 4(b). If the taxpayer's approach were to prevail, then M would be able to reallocate the excess loss account to another member's stock in B, thus avoiding the section 311(b) gain recognition. That is not, however, what happens in the example.

The 2009 regulations also amended Treas. Reg. § 1.358-2(a)(2)(iii) (2009), to allow for reallocation of a shareholder's basis in the nominal share. The preamble stated that "this approach is the most consistent with current law regarding basis determination as a similar result would occur under § 1.358-2 if stock was actually issued in the transaction." This approach, of course, sounds like the principle annunciated in the Davant footnote. As discussed above, had CFC 1 actually issued stock to Foreign Holdco in the transaction, the basis would have been recovered, if at all, by US Holdco upon its liquidating distribution to Sub 1. Any reallocation of that basis would have been quite inconsistent with the then-current law regarding basis determination.

The preamble to the 2011 regulations noted that some were contending that the 2009 regulations could be interpreted to allow an inappropriate reallocation of basis in a nominal share by persons who do not actually own stock in the issuing corporation to shares in the issuing corporation actually owned by another person, before the nominal share is deemed to have been transferred through the relevant chains of ownership. The preamble makes clear that such an approach is not supportable:

> The IRS and Treasury did not intend for the [2009] regulations to allow such an inappropriate allocation of basis <u>and do not believe the [2009] regulations support such an allocation</u>.

T.D. 9558, 76 Fed. Reg. at 71878 (emphasis added). The 2011 regulations added Temp. Treas. Reg. § 1.358-2T(a)(2)(iii) in place of its 2009 counterpart, to clarify this point. Example 16 of Treas. Reg. § 1.358-2T(c), added in the 2011 regulations, largely mirrors the transaction in this case and explains how the nominal share takes a fair market value as it is distributed through the chain of ownership to reflect actual ownership. In the example, corporation P wholly owns corporation X and corporation Y. Corporation X wholly owns corporation T. Corporation T sells all of its assets to corporation Y for cash in a transaction that qualifies as an all cash D reorganization under Treas. Reg. § 1.368-2(l). The example notes that when the nominal share of Y stock is deemed distributed to P, P's basis in the stock will equal fair market value under section 301(d).[23]

The taxpayer's position relies on Treas. Reg. § 1.358-2(a)(2)(iii), as added by the 2009 regulations, even though that provision was clarified, removed, and replaced with Temp. Treas. Reg. § 1.358-2T(a)(2)(iii). The taxpayer contends that the latter regulation was made prospectively effective (Treas. Reg. § 1.358-2T(d)), thus indicating that it reflected a major policy shift and change in the law rather than a mere clarification. Therefore, the taxpayer wants to rely on the regulation as issued in 2009 and argues, based on its interpretation of the 2009 regulation, that it can assign the basis of the nominal share to a pre-existing share of CFC 1.

The 2011 regulations clarify that if stock is issued to a lower-tier subsidiary, the basis in the nominal share must be adjusted to fair market value upon distribution of the

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[23] There is no meaningful difference in P taking a fair market value basis under section 301(d) in the case of a non-liquidating distribution, or under section 334(a) in the case of a liquidating distribution. Either way, P's basis is equal to the date of distribution value, without any derivation from the distributor's basis.

nominal share up through the chain of ownership. The preamble to the 2011 regulations specifically referred to the 2011 modification as a "clarification," and expressly stated that the position the taxpayer asserts here was neither intended nor was allowed by the 2009 regulations. T.D. 9558, 76 Fed. Reg. at 71878.

The 2009 regulations cannot reasonably be interpreted to give taxpayer the reallocation it seeks. The preamble to the 2009 regulations stated the regulations were "consistent with current law [at the time of the issuance of the 2009 regulations] regarding basis determination as a similar result would occur under § 1.358-2 if stock was actually issued in the transaction." T.D. 9475. Under the general rules of section 358 and the Davant principle, the basis in the nominal share would have been reset to its value upon US Holdco's post-adoption-of-plan-of-dissolution distribution to Sub 1. Moreover, the preamble to the 2009 regulation also discussed, and included an example, how the regulations applied in the consolidated context. The discussion and example (mirrored in Treas. Reg. § 1.1502-13(f)(7)(i), Ex. 4) demonstrate that any nominal share issued to a lower-tier subsidiary will be deemed distributed to its parent, and the distribution will be treated as a section 301 distribution, in order to preserve locational integrity. The 2011 clarification, including example 16 in Treas. Reg. § 1.358-2T(c) referred to above, is consistent with – not some vast departure from – the policy underlying the 2009 regulations and the pre-existing section 358 rules.

C. Taxpayer's Duty of Consistency

The taxpayer is barred by the duty of consistency from characterizing the Cross-Chain Sale of FC stock as a D reorganization because it reported the transaction on its Year 6 Return as a taxable sale followed by cascading section 351 contributions of Foreign Holdco stock to CFC 1. Such a change in position, after the statute of limitations has closed on the Year 6 Return, would allow the taxpayer to benefit at the expense of the Service by effectively claiming twice what is a single economic loss.

The duty of consistency is a judicial doctrine holding that a taxpayer may not, after taking a position on a given fact or transaction in one year, take a contrary position with respect to that same fact or transaction in a subsequent year when correction of the prior year is time barred. Estate of Ashman v. Commissioner, 231 F.3d 541, 543 (9th Cir. 2000). When such a fact or transaction affects another year, the doctrine holds, there is a duty of consistency with respect to the consequences of that fact or transaction, regardless of whether all the technical elements of estoppel are present. Id. (citing Orange Sec. Corp. v. Commissioner, 131 F.2d 662, 663 (5th Cir. 1942)). The Ninth Circuit has identified three elements that are required for the duty of consistency to apply: (1) a representation by the taxpayer in a given tax year; (2) reliance on that representation by the Service; and (3) an attempt by the taxpayer to change its previous representation, to the detriment of the Service, after the statute of limitations has closed on the prior tax year. Janis v. Commissioner, 461 F.3d 1080, 1085 (9th Cir. 2006); Van Alen v. Commissioner, T.C. Memo. 2013-235. Because all three of these requirements are satisfied by the facts present in this matter, the duty of consistency binds the taxpayer to its initial characterization of the reported transaction.

1. Representation by the Taxpayer

On its Year 6 Return, the Parent Group reported the dissolution of US Holdco as a section 331 taxable liquidation, and claimed a resulting capital loss of qq. CFC 1's Form 5471 treated the Cross-Chain Sale as a taxable purchase, and reported a cost basis (rather than a large built-in loss) in the FC stock. The Cross-Chain Sale was also reported as a taxable sale on the Form 5471 filed for Foreign Holdco for Year 6, and Forms 5471 for Foreign Holdco were prepared and filed on a going concern basis until at least Date 9. The filing of such returns, rather than the abbreviated returns properly filed by a dormant entity under Rev. Proc. 92-70, effectively represented that CFC 1 continued to exist and to own the assets and liabilities reported on the return, and that CFC 1 was not liquidated (either *de facto or de jure*) until at least Date 9 CFC 1.

2. Reliance by the IRS

The Service accepted the Parent Group's Year 6 Return and allowed the qq capital loss resulting from the taxable liquidation of US Holdco. Inherent in accepting the taxpayer's position that the liquidation of US Holdco qualified as a taxable liquidation under section 331, the Service relied upon taxpayer's representations that third parties owned US Holdco voting preferred stock at the time of US Holdco's liquidation, that the preferred stock represented more than 20 percent of the vote and/or value of US Holdco stock, and that US Holdco was not affiliated (and thus not to be consolidated) with the Parent Group. If no voting preferred shares in Sub 2 were held by third parties at the time of the liquidation, as the taxpayer now contends, the Service might not have accepted the taxpayer's claimed capital loss. Given what would have been a latent potential for duplicative tax benefits had the Cross-Chain Sale been reported as a D reorganization, the Service might have been motivated to challenge the loss on Ilfeld or other grounds. Moreover, returns for Foreign Holdco continued to be filed on a going concern basis until Date 9. The taxpayer did not file abbreviated returns under Rev. Proc. 92-70 that would show that Foreign Holdco was a dormant entity, but it represented that Foreign Holdco was a continuing entity with some activity that that held some amount of assets and owned some amount of liabilities. Additionally, CFC 1's Form 5471 reported a cost basis (rather than a large built-in loss) in the FC stock. The Service accepted these representations.

3. Attempt to Change Position

At present, the taxpayer acknowledges that it erred in its prior treatment of the Cross-Chain Sale, and asserts that it should have reported the transaction as a D reorganization on its Year 6 Return. In particular, it asserts that its basis in the CFC 1 stock should be increased by the basis US Holdco had in Foreign Holdco. This position is inconsistent with the way the transaction was reported on the Year 6 return. As we noted above, following a taxable liquidation of US Holdco under a plan of dissolution adopted prior to the Cross-Chain Sale, the correct basis Sub 1 would have taken in the assets distributed to it by US Holdco (including any shares in Foreign Holdco, or any deemed or a nominal share in CFC 1) was equal to the fair market value on the date of distribution fair market value (*i.e.*, zero with respect to the stock in Foreign Holdco or any nominal or constructive share in CFC 1). Therefore, if a nominal or constructive share in CFC 1 is somehow treated as having been owned by Sub 1 or contributed by it to Sub 2, Sub 3, and Sub 4, the taxpayer's basis in CFC 2 would not increase.

Additionally, the taxpayer now states that Foreign Holdco effectively dissolved in Year 6, the year of the Cross-Chain Sale. However, for a number of years after Year 6, Forms 5471 were filed for Foreign Holdco on a going concern basis, and those forms represented that Foreign Holdco owned some amount of assets and owed some amount of liabilities. Now, the taxpayer argues that Foreign Holdco had *de facto* liquidated in Year 6 for purposes of the distribution requirement in sections 354(b)(1)(B) and 368(a)(1)(D). The Service accepted the taxpayer's representations that Foreign Holdco was an ongoing business entity with some activity, that owned assets and owed liabilities, in Year 6 and a number of years thereafter. The Service cannot now audit Foreign Holdco to determine if it continued as a going concern, or determine the quantum or quality of assets and liabilities through these years. Therefore, the effects of this transaction must reflect the representations that the taxpayer made about Foreign Holdco not being liquidated (either *de facto or de jure*) until at least Date 9.

We do not agree with the taxpayer's contention that it engaged in a D reorganization. If the taxpayer *had* engaged in a D reorganization and the Service agreed that the preferred stock should be considered to be redeemed, the Service should have evaluated whether to challenge the capital loss of gg that it reported on its Year 6 return on Ilfeld or other grounds, in order to avoid the potential for duplicative tax benefits derived from a single economic loss. However, the statute of limitations is now closed as to the Year 6 Return and the Service can no longer disallow the gg capital loss. The taxpayer's change in position would effectively allow set it up to benefit twice from the single economic loss it suffered as a result of its investment in FC: first, as a capital loss resulting from the liquidation of US Holdco in Year 6, and then as a loss on the sale of CFC 1 in Year 9. The taxpayer reported on its Year 6 return that it engaged in a taxable subsidiary liquidation. The Service relied on that representation in allowing the taxpayer a gg loss in Year 6. Now that Year 6 is closed to adjustment, the duty of consistency precludes the taxpayer from recharacterizing the Cross-Chain Sale as a tax-free reorganization and effectively duplicating its loss.

CAVEAT(S):

A copy of this technical advice memorandum is to be given to the taxpayer. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.