Internal Revenue Service

Department of the Treasury

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Person to Contact:

Telephone Number:

Refer Reply To:
CC:INTL:Br.4-PLR-117346-99
Date:
February 28, 2000

Parent =

FS1 =

FS2 =

FS3 =

FS4 =

Year X =

Date Y =

Year Z =

State A =

Country B =

Country C =

Country D =

Dear:

This is in response to your letter, dated October 20, 1999, requesting a private letter ruling providing that the failure to file notices of certain transactions under former Temp. Reg. §7.367(b)-1(c), in effect for the years of the transactions, was due to reasonable cause within the meaning of §7.367(b)-1(c)(3). Additional information was provided in letters dated December 17, 1999, and December 22, 1999.

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.

In Year X, Parent, a State A corporation, owned all the stock of FS1, a Country B corporation. On Date Y, Parent transferred all the stock of FS1 to FS2, a newly-formed wholly-owned Country C subsidiary of Parent, solely in exchange for voting stock of FS2. The purpose of the transaction was to create a holding company for Parent's foreign subsidiaries. After the transaction, FS2 owned all the stock of FS1, and Parent owned all the stock of FS2.

The taxpayer has represented that the transaction qualified as a nontaxable transaction under section 351 and section 368(a)(1)(B) of the Internal Revenue Code (the Code). However, in preparing its federal tax return, Parent reported the transaction as a nonrecognition transaction solely under section 351 of the Code and filed a gain recognition agreement pursuant to Treas. Reg. §1.367(a)-3T(g). For year X, the transfer by a U.S. person of stock of a controlled foreign corporation in an exchange described in both section 351 and section 368(a)(1)(B) is governed by section 367(b) and not section 367(a) and the regulations thereunder. See §1.367(a)-3T(b)(1) and §7.367(b)-4(b). The taxpayer did not identify the transaction as a reorganization under section 368(a)(1)(B) and did not file the notice and required information required under the section 367(b) regulations (see §7.367(b)-1(c)). Although Parent's income tax return was reviewed by a professional international tax accounting firm before the tax return was filed with the Internal Revenue Service, the accounting firm did not discover the error. The taxpayer did file annual certifications pursuant to §1.367(a)-3T for the years following Year X.

In Year Z, an election was made under Treas. Reg. §301.7701-3(a) to disregard FS1 as a separate entity for U.S. income tax purposes. In addition, FS2 transferred all the stock of FS1 to FS3, a wholly owned Country C subsidiary of FS2, solely in exchange for voting stock of FS3. FS3 then transferred all the stock of FS1 to FS4, a Country D corporation and a wholly-owned subsidiary of FS3, as a contribution of capital. The taxpayer reported the transaction on statements attached to its federal income tax return as (i) an acquisition by FS3 of all the assets and liabilities of FS1 in

exchange for voting stock of FS3 in a transaction that qualified as a reorganization under section 368(a)(1)(C) of the Code, followed by (ii) a transfer by FS3 of such assets and liabilities to FS4. The taxpayer represents that the stock of FS1 has not subsequently been disposed of or otherwise exchanged, although it is contemplated that, through a series of transactions, FS4 (along with FS1 as its wholly-owned subsidiary) will become directly owned by Parent.

If the taxpayer's characterization of the Year Z reorganization is followed, then the Year Z reorganization was subject to the requirements of section 367(b) and the regulations promulgated thereunder. However, Parent failed to identify the reorganization as a section 367(b) transaction and, consequently, did not file the notice and requisite information required by §7.367(b)-1(c). Although Parent's tax return was reviewed by a professional international tax accounting firm before the tax return was filed with the Internal Revenue Service, the accounting firm did not discover the error.

The taxpayer's outside counsel recently discovered the reporting errors for Years X and Z, and these errors were brought to the Service's attention before they were discovered by the Service. The statutes of limitations for Years X and Z are open and the examinations for these years have not closed, so that the taxpayer's characterizations of the transactions could be verified.

For tax years X and Z, any person that realizes gain (whether or not recognized) in an exchange to which section 367(b) applies must file a notice of such exchange on or before the last date (including extensions) for filing a federal income tax return for the person's taxable year in which gain was realized. See §7.367(b)-1(c)(1). A person that fails to provide, in a timely manner, information sufficient to apprise the Commissioner of the occurrence and nature of a section 367(b) exchange will be considered to have failed to comply with §§7.367(b)-1 through 7.367(b)-12 only if the person fails to establish reasonable cause for the failure. See §7.367(b)-1(c)(3).

Based solely on the information and representations submitted, and provided that the §7.367(b)-1(c) notice and information reporting requirements are complied with in the manner described below and that any other information reporting requirements under other Code sections in regard to the transactions in years X and Z are met, we hold that Parent had reasonable cause for the failures in Year X and Year Z to comply with the §7.367(b)-1(c) notice and information reporting requirements.

This holding is based, in part, on the fact that Parent reasonably relied upon the review of its tax returns by qualified tax professionals when filing its Year X and Year Z returns, and the tax professionals failed to advise parent to file such notice. Moreover, this holding looks to the fact that Parent informed the Service and attempted to comply with the reporting requirements as soon as practicable after the omissions were discovered by taxpayer's counsel and before the issue was uncovered by an Internal Revenue Service examination. Finally, the holding is also based on the fact that the

Service's interests were not prejudiced by the failure of Parent to comply with section 367(b) notice requirements, provided that the taxpayer amends its returns for Years X and Z and provides a statement which reflects the amount of earnings and profits attributed by reason of §7.367(b)-7(b) and §7.367(b)-9 (see §7.367(b)-1(c)(2)(v)).

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. In particular, no opinion is expressed about any transaction subsequent to the Year Z transaction discussed 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.

Copies of this letter must be attached to disclosures of the Year X and Year Z section 367(b) exchanges that satisfy the §7.367(b)-1(c) notice and information reporting requirements. The disclosure should be filed as soon as practicable with the District Director with whom Parent was originally required to file the §7.367(b)-1(c) notice and information. In addition, Parent should attach a copy of this letter and the disclosure to its federal income tax return for the taxable year in which it receives this letter.

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

Sincerely,

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

cc: