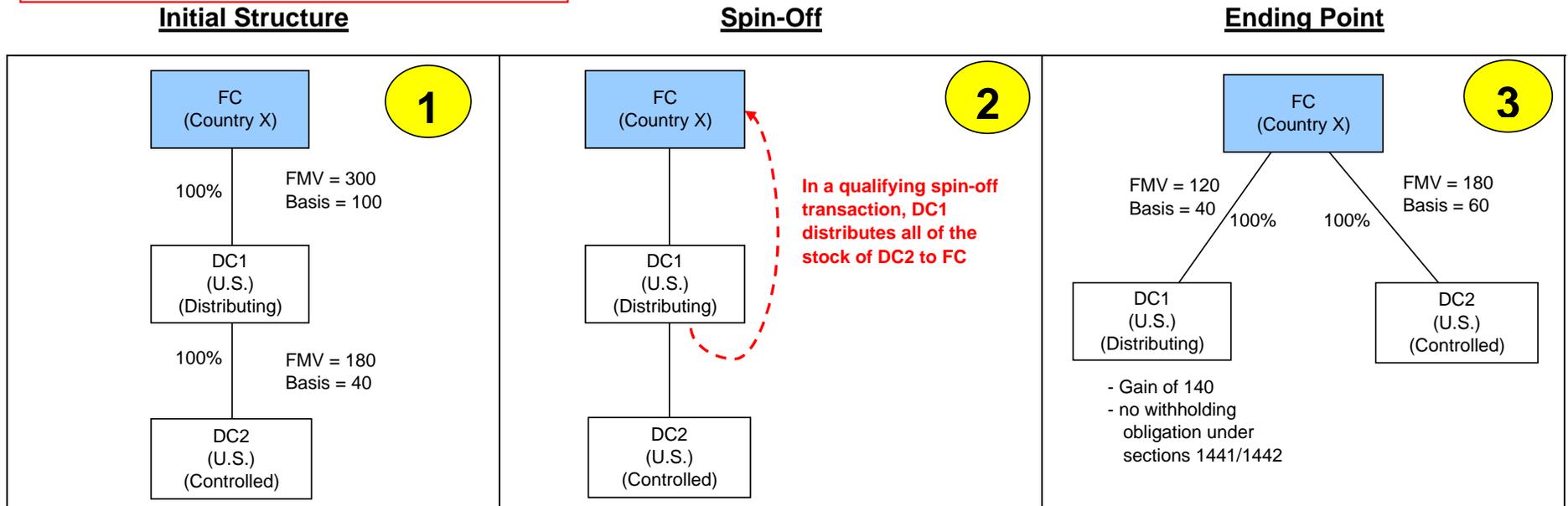


Reg. 1.367(e)-1

**Superseded by T.D. 8834.
See Treas. Reg. § 1.367(e)-1(c)**

**Outbound Spin-Off:
Gain to "Distributing"**

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FC, a Country X corporation, owns all of the outstanding stock of DC1, a domestic corporation. DC1 owns all of the outstanding stock of DC2, another domestic corporation. The fair market value of the DC1 stock is 300x, and FC has a 100x basis in the DC1 stock. The fair market value of the DC2 stock is 180x, and DC1 has a 40x basis in the DC2 stock. Neither DC1 nor DC2 is a U.S. real property holding corporation. Country X does not maintain an income tax treaty with the United States.

In a transaction qualifying for nonrecognition under section 355(a), DC1 distributes all of the stock of DC2 to FC. After the distribution, the DC1 stock has a fair market value of 120x. DC1 recognizes gain of 140x, which is the difference between the fair market value (180x) and the basis (40x) of the stock distributed. FC takes a basis of 40x in the DC1 stock, and a basis of 60x in the DC2 stock.

Even though DC1 must recognize gain on the distribution, FC is considered to have received stock in a distribution qualifying for nonrecognition under section 355. Thus, FC is not be considered to have received a distribution described in section 301 or a distribution in an exchange described in section 302(b), and DC1 has no withholding responsibilities under sections 1441/1442. [The facts of this example are taken from Temp. Reg. 1.367(e)-1T(e), Example 1. Although the temporary regulation does not apply to transactions after August 7, 1999, the results for this example are the same under the final regulations.]