Reg. 1.7874-2(k), Example 18

## Partnership Interest Treated as Stock of Foreign Corporation

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Corp DC1

(U.S.)

**Initial Structure** Formation of FRS **Ending Point** 2 **Public** Indvs. A & B Indvs. A & B Public Indvs. A & B **Public** Class B **Partnership** Interest Corp FA 100% of FA 100% Cash (Foreign) Class B Partnership Corp FA Interest Corp DC1 Corp DC1 Class A 100% of Corp FA (Foreign) (U.S.) (U.S.) **Partnership** Class A (Foreign) **FPS** Interest Partnership (Foreign) Interest All DC1 100%

Cash

DC1 is a domestic corporation. Individuals A and B equally own DC1. FA, a newly formed foreign corporation, issues stock in a public offering for cash. Individuals A and B and FA organize FPS. FA transfers part of the cash from the public offering to FPS in exchange for a class A partnership interest. FA does not hold any significant assets other than the class A partnership interest. Individuals A and B transfer their DC1 stock to FPS in exchange for class B partnership interests.

**FPS** 

(Foreign)

Stock

The class B partnership interests entitle individuals A and B to cash distributions from FPS approximately equal to any dividend distributions made by FA with respect to its publicly traded stock. In certain circumstances, the class B partnership interests also permit individuals A and B to require FPS to redeem the interests in exchange for cash equal to the value of an amount of FA stock as determined on the redemption date. The class B partnership interests do not provide individuals A or B voting rights with respect to FA.

The non-liquidating distribution rights provided by the class B partnership interests are substantially similar in all material respects to the dividend rights provided by the FA stock. Because FA does not hold any significant assets other than the class A partnership interest, the value of the class B partnership interests held by individuals A and B is approximately equal to a corresponding amount of FA stock. The distribution rights on liquidation (or redemption) provided by the class B partnership interests, therefore, are substantially similar in all material respects to distribution rights on liquidation (or redemption) provided by the FA stock. Thus, the distribution rights provided by the class B partnership interests are substantially similar in all material respects to the distribution rights provided by the publicly traded FA stock. As a result, if treating the class B partnership interests as FA stock would have the effect of treating FA as a surrogate foreign corporation, under Treas. Reg. §1.7874-2(i)(1) the class B partnership interests will be treated as FA stock for purposes of Code §7874.