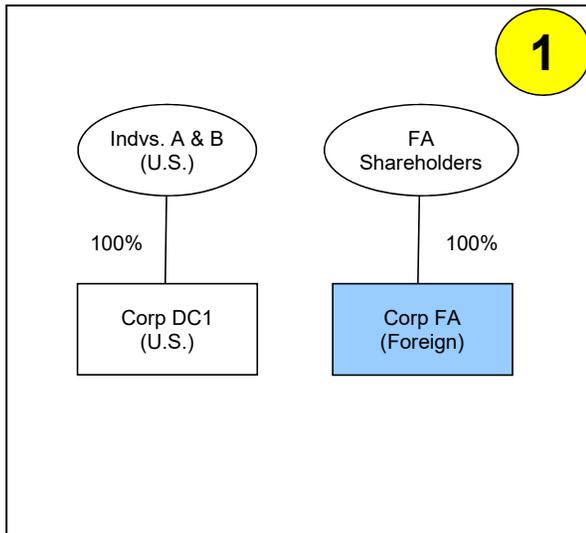
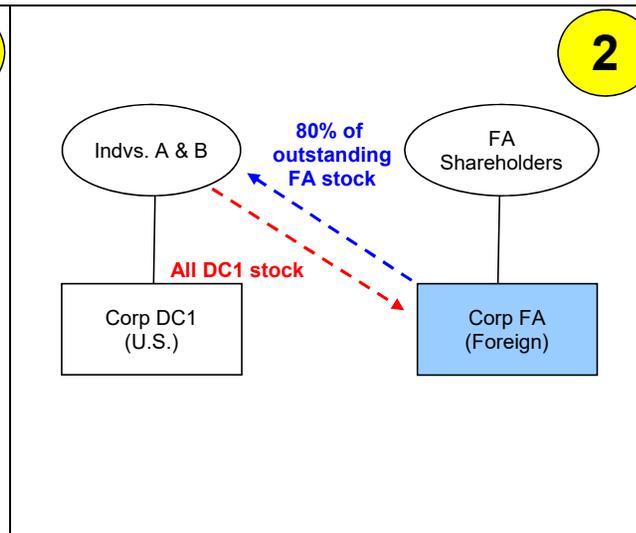


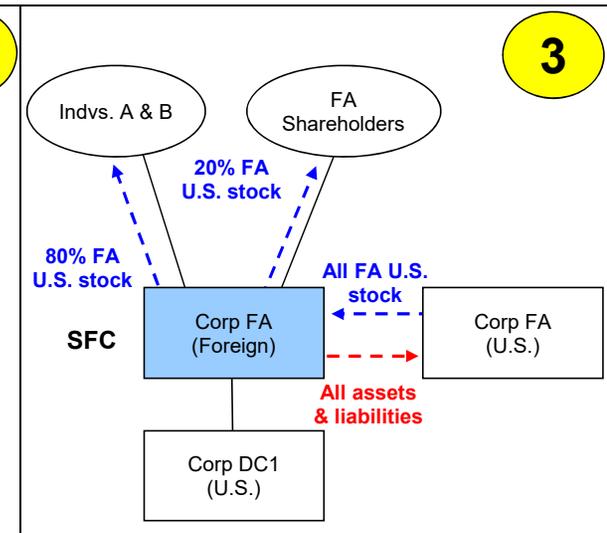
Initial Structure



351 Exchange / B Reorganization



Deemed Inbound F Reorganization



DC1 is a domestic corporation. Individuals A and B are United States persons and equally own DC1. Pursuant to a plan, individuals A and B transfer their DC1 stock to FA, a foreign corporation, in exchange solely for 80% of the outstanding FA stock. After the acquisition, the expanded affiliated group that includes FA does not have substantial business activities in Country A when compared to the total business activities of the expanded affiliated group.

Under Treas. Reg. §1.7874-2(c)(1)(i), for purposes of Code §7874(a)(2)(B)(i), FA is treated as acquiring all of the properties held by DC1 on the date of the stock acquisition. After the acquisition, the former domestic entity shareholders of DC1 own 80% of the stock of FA by reason of holding DC1 stock. Therefore, FA is a surrogate foreign corporation that is treated as a domestic corporation under Code §7874(b). Under Treas. Reg. §1.7874-2(j)(1), except for purposes of determining whether FA is treated as a surrogate foreign corporation, the conversion of FA to a domestic corporation constitutes a reorganization described in Code §368(a)(1)(F) that occurs at the end of the day immediately preceding the date of the stock acquisition. Code §367 applies to the conversion of FA to a domestic corporation. See, for example, Treas. Reg. §§1.367(b)-2 and 1.367(b)-3 for the consequences of the conversion. Under Treas. Reg. §1.7874-2(j)(3), Code §367 does not apply to the transfers of DC1 stock by individuals A and B to FA.

Ending Point

