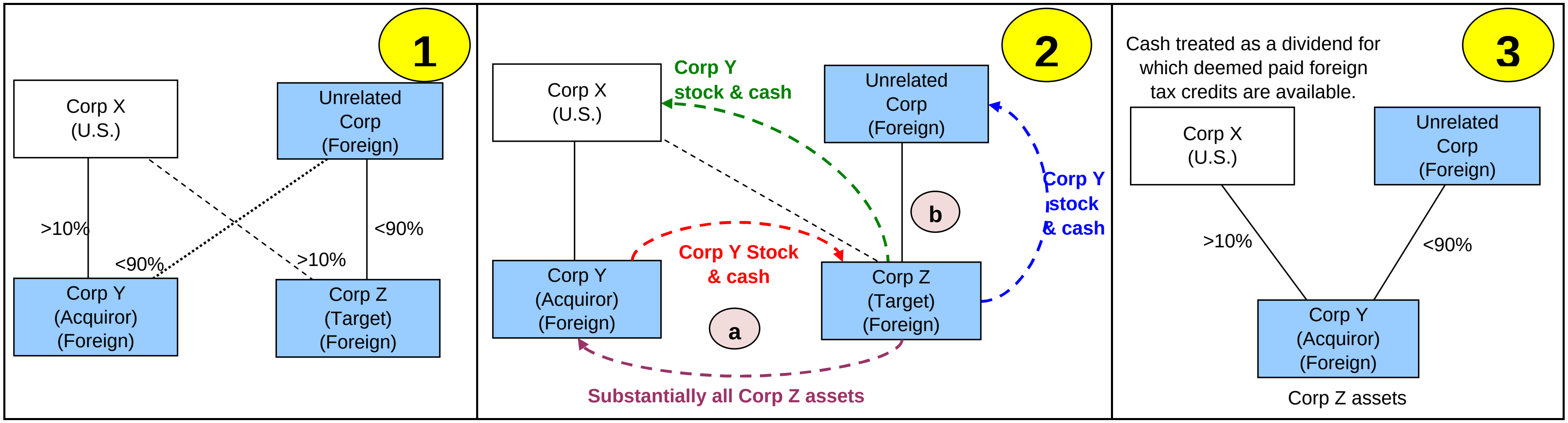
Revenue Ruling 74-387

Section 902 Deemed Paid Credits in D Reorganization With Boot

Initial Structure | **D Reorganization With Boot** | **Ending Point**



X, a domestic corporation, owns directly in excess of 10 percent of the stock of two foreign corporations, Y and Z. The remaining stock of Y and Z is owned by an unrelated foreign corporation. During the taxable year 1973, and after obtaining a favorable ruling from the Commissioner under the provisions of section 367, Y acquired substantially all of the assets of Z solely in exchange for stock of Y and cash. Z then dissolved by distributing the stock of Y and cash to X and the unrelated foreign corporation in exchange for their outstanding stock of Z. The favorable section 367 ruling also held that the transaction qualifies as a reorganization pursuant to section 368(a)(1)(D), and under section 356(a)(1) the gain is recognized to the extent of cash and is treated as a dividend under section 356(a)(2).

Section 902 provides, in general, that where a domestic corporation owns at least 10 percent of the voting stock of a foreign corporation and receives dividends therefrom, the domestic corporation may be entitled to a foreign tax credit under section 901 for a certain portion of the taxes paid by the foreign corporation to a foreign country or United States possession. Treas. Reg. § 1.902-3(f) refers to section 316 for the definition of the term "dividend" for purposes of applying section 902. Section 316 defines the term "dividend" to mean, in general, any distribution of property made by a corporation to its shareholders out of its current and accumulated earnings and profits. The specific issue in the instant case is whether any gain under section 356(a)(1) which X receives in cash during the year of the reorganization, and which is treated as a dividend under section 356(a)(2), is considered a dividend for purposes of the deemed paid foreign tax credit provisions of section 902.

Rev. Rul. 70-240 holds that the gain realized by the exchanging shareholder on a reorganization under section 368(a)(1)(D) and recognized under section 356(a)(1) to the extent of the cash received is treated as a dividend (as defined in section 316) under section 356(a)(2). Since both section 356(a)(2) and Treas. Reg. § 1.902-3(f) use the term "dividend," a dividend under section 356(a)(2) is considered a dividend for purposes of section 902. Accordingly, the cash which is treated as a dividend pursuant to section 356(a)(2) is considered a dividend for purposes of the deemed paid foreign tax credit provided by section 902 to the extent of X's ratable share of Z's accumulated profits.