Revenue Ruling 87-96

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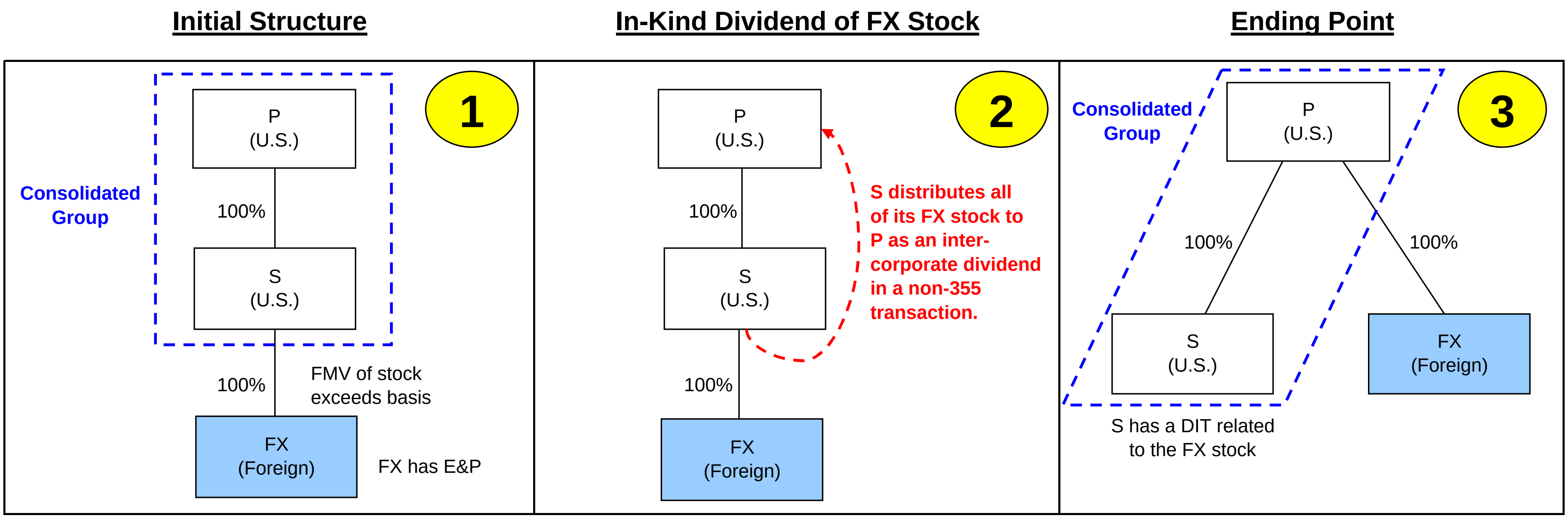
Intercompany Dividend of Foreign Subsidiary Triggers Deferred 311(b) and 1248 Gains



Section 311(b) provides that, if a corporation distributes property to a shareholder in a section 301 transaction and the FMV of the property exceeds it adjusted basis, then gain is recognized by the distributing corporation as if the property had been sold to the distributee at its FMV. Thus, the above transaction will be treated as if S had sold the FX stock to P at its FMV.

Section 1248(a) provides that, if a U.S. person sells stock in a foreign corporation and the ownership requirements of section 1248(a)(2) are satisfied [generally U.S. shareholders of CFCs], the gain recognized on the sale will be included in the seller's gross income <u>as a dividend</u> to the extent of certain E&P of the foreign corporation. Section 1248(a) applies to the gain realized by S on its distribution of FX stock to P.

Reg. 1.1502-14 provides that the inclusion of income of any gain recognized by a distributing corporation in certain intercompany distributions (including any amount treated as gain under section 311) will be deferred until a "triggering event" occurs. Thus, S will defer the section 311(b) gain on its distribution of FX stock to P until the occurrence of a triggering event. [In tax vernacular, there is a deferred intercompany transaction (or "DIT") with regard to the FX stock.]

S will maintain a separate account reflecting the potential section 1248 recharacterization. Distributions from FX to P will reduce the separate account, as will section 956 inclusions. When a triggering event occurs, S will include in its income the amount of deferred gain required by the consolidated return regulations. An amount of that gain equal to any remaining section 1248 recharacterization account will be characterized as a dividend by section 1248(a) at that time.