



**BDO Seidman, LLP**  
Accountants and Consultants

# InternationalTaxAlert

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## ISSUE:

### INSOLVENT CFC'S CAN TRIGGER ORDINARY WORTHLESS STOCK DEDUCTION

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## DATE:

*Immediate action may be necessary for calendar year taxpayers.*

## DETAILS:

A planning opportunity may exist for certain U.S. companies that own worthless controlled foreign corporation ("CFC") shares. If the worthlessness can be documented to have occurred during 2003, immediate action may be required to trigger the loss for calendar year taxpayers. Generally, some of the indicia of worthlessness include (but are not limited to): if the CFC became insolvent during 2003 (liabilities in excess of the FMV of the assets -- including intangibles and going concern, etc.), continual funding of CFC losses by owner, and no prospects for future earnings, etc. Establishing and documenting the timing of the worthlessness through a third party valuation is strongly recommended (for practical purposes a preliminary valuation should be performed now, followed by a formal valuation completed before the 2003 tax return filing).

Lastly, making the "check-the-box" election is required to trigger the loss. Afterwards, the foreign subsidiary would be a flow-through entity for U.S. tax purposes. The election itself and the flow-through effects have other potentially significant tax ramifications that must be considered prior to taking any action.

According to Revenue Ruling 2003-125, the deemed liquidation that occurs as a result of the "check-the-box" election is an "identifiable event" that fixes the parent's loss (if any) with respect to the subsidiary stock. With certain exceptions, this could be an ordinary loss deduction equal to the basis in the subsidiary.

The "check-the-box" election needs to be made on Form 8832 on or before March 15, 2004 if it is to be effective for December 31, 2003.

## RECOMMENDED ACTION:

A preliminary assessment, including a preliminary valuation, must be performed before an election can be recommended.

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*Material Discussed in this newsletter is meant to provide general information and should not be acted on without obtaining professional advice tailored to your firm's individual needs.*

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