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Accountants and Consultants

Subject:

IRS Issues Final and Temporary Regulations Addressing Gain Recognition Agreements Under Section 367

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International Tax Alert

Date/Timing

These regulations are effective February 5, 2007.

Affecting

U.S. taxpayers that transfer stock or securities to foreign corporations or that are involved in transactions that impact existing gain recognition agreements (“GRA”).

Background

Generally, section 367(a) provides that foreign corporations that receive property from a U.S. transferor are not considered corporations in connection with certain non-recognition transactions. An exception to this general rule applies for certain transfers by the U.S. transferor of stock to a foreign corporation when a GRA under Treas. Reg. §1.367(a)-8 is entered into. A GRA generally provides that the U.S. transferor agrees to include in income any gain realized, but not recognized, on the transfer of shares to the foreign corporation if certain “triggering events” occur.

On October 17, 2005, the IRS issued Notice 2005-74 announcing its intention to amend regulations under section 367(a) regarding the application and treatment of GRAs in certain asset reorganizations. Notice 2005-74 provided some safe harbors that prevented the triggering of GRAs for certain reorganizations where the ability of the service to collect tax was sufficiently preserved.

Summary of Guidance Provided

The new regulations (Treasury Decision 9311) incorporate many of the rules announced in Notice 2005-74 as well as address the impact to GRAs of transactions not addressed in the current regulations or Notice 2005-74. The new regulations ultimately increase the types of non-recognition transactions that do not trigger an existing GRA and provide guidance on how to report such transactions.

The new regulations focus much of their guidance on transactions that

include a disposition of the transferred corporation, a disposition of substantially all the assets of the transferee foreign corporation, or a disposition of the stock of the transferee foreign corporation. Also addressed by the new regulations are non-recognition transactions involving money or other property that is considered boot, the effect of consolidation or deconsolidation on GRAs, instances where the U.S. transferor goes out of existence in a transaction giving rise to a GRA, the “substantially all” requirement of transfers of the Transferred Corporation’s assets, certain transactions that terminate a GRA, and triangular reorganizations.

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