§ 1.367(b)-5 Distributions of stock described in section 355.

(a) In general—(1) Scope. This section provides rules relating to a distribution described in section 355 (or so much of section 356 as relates to section 355) and to which section 367(b) applies. For purposes of this section, the terms distributing corporation, controlled corporation, and distributee have the same meaning as used in section 355 and the regulations thereunder.

(2) Treatment of distributees as exchanging shareholders. For purposes of the section 367(b) regulations, all distributees in a transaction described in paragraph (b), (c), or (d) of this section shall be treated as exchanging shareholders that realize income in a section 367(b) exchange.

(b) Distribution by a domestic corporation—(1) General rule. In a distribution described in section 355, if the distributing corporation is a domestic corporation and the controlled corporation is a foreign corporation, the following general rules shall apply—

(i) If the distributee is a corporation, then the controlled corporation shall be considered to be a corporation; and

(ii) If the distributee is an individual, then, solely for purposes of determining the gain recognized by the distributing corporation, the controlled corporation shall not be considered to be a corporation, and the distributing corporation shall recognize any gain (but not loss) realized on the distribution.

(2) Section 367(e) transactions. The rules of paragraph (b)(1) of this section shall not apply to a foreign distributee to the extent gain is recognized under section 367(e)(1) and the regulations thereunder.

(3) Determining whether distributees are individuals. All distributees in a distribution described in paragraph (b)(1) of this section are presumed to be individuals. However, the shareholder identification principles of §1.367(e)-1(d) (including the reporting procedures in §1.367(e)-1(d)(2) and (3)) shall apply for purposes of rebutting this presumption.

(4) Applicable cross-references. For rules with respect to a distributee that is a partnership, trust or estate, see §1.367(b)-2(k). For additional rules relating to a distribution of stock of a foreign corporation by a domestic corporation, see section 1248(f) and the regulations thereunder. For additional rules relating to a distribution described in section 355 by a domestic corporation to a foreign distributee, see section 367(e)(1) and the regulations thereunder.

(c) Pro rata distribution by a controlled foreign corporation—(1) Scope. This paragraph (c) applies to a distribution described in section 355 in which the distributing corporation is a controlled foreign corporation and in which the stock of the controlled corporation is distributed pro rata to each of the distributing corporation’s shareholders.

(2) Adjustment to basis in stock and income inclusion. If the distributee’s postdistribution amount (as defined in paragraph (e)(2) of this section) with respect to the distributing or controlled corporation is less than the distributee’s predistribution amount (as defined in paragraph (e)(1) of this section) with respect to such corporation, then the distributee’s basis in such stock immediately after the distribution (determined under the normal principles of section 358) shall be reduced by the amount of the difference. However, the distributee’s basis in such stock shall not be reduced below zero, and to the extent the foregoing reduction would have reduced basis below zero, the distributee shall instead include such amount in income as a deemed dividend from such corporation.

(3) Interaction with §1.367(b)-2(e)(3)(ii). The basis increase provided in §1.367(b)-2(e)(3)(ii) shall not apply to a deemed dividend that is included in income pursuant to paragraph (c)(2) of this section.

(4) Basis redistribution. If a distributee reduces the basis in the stock of the distributing or controlled corporation (or has an inclusion with respect to such stock) under paragraph (c)(2) of this section, the distributee shall increase its basis in the stock of the other corporation by the amount of the basis decrease (or deemed dividend inclusion) required by paragraph (c)(2) of this section. However, the distributee’s basis in such stock shall not be increased above the fair market value of such stock and shall not be increased...
to the extent the increase diminishes the distributee’s postdistribution amount with respect to such corporation.

(d) Non-pro rata distribution by a controlled foreign corporation—(1) Scope. This paragraph (d) applies to a distribution described in section 355 in which the distributing corporation is a controlled foreign corporation and in which the stock of the controlled corporation is not distributed pro rata to each of the distributing corporation’s shareholders.

(2) Treatment of certain shareholders as distributees. For purposes of the section 367(b) regulations, all persons owning stock of the distributing corporation immediately after a transaction described in paragraph (d)(1) of this section shall be treated as distributees of such stock. For other applicable rules, see paragraph (a)(2) of this section.

(3) Inclusion of excess section 1248 amount by exchanging shareholder. If the distributee’s postdistribution amount (as defined in paragraph (e)(2) of this section) with respect to the distributing or controlled corporation is less than the distributee’s predistribution amount (as defined in paragraph (e)(1) of this section) with respect to such corporation, then the distributee shall include in income as a deemed dividend the amount of the difference. For purposes of this paragraph (d)(3), if a distributee owns no stock in the distributing or controlled corporation immediately after the distribution, the distributee’s postdistribution amount with respect to such corporation shall be zero.

(4) Interaction with §1.367(b)—2(e)(3)(i) and (ii)—(i) Limited application. The basis increase provided in §1.367(b)—2(e)(3)(i) shall apply to a deemed dividend that is included in income pursuant to paragraph (d)(3) of this section only to the extent that such basis increase does not increase the distributee’s basis above the fair market value of such stock and does not diminish the distributee’s postdistribution amount with respect to such corporation.

(ii) Interaction with predistribution amount. For purposes of this paragraph (d), the distributee’s predistribution amount (as defined in paragraph (e)(1) of this section) shall be determined without regard to any basis increase permitted under paragraph (d)(4)(i) of this section.

(e) Definitions—(1) Predistribution amount. For purposes of this section, the predistribution amount with respect to a distributing or controlled corporation is the distributee’s section 1248 amount (as defined in §1.367(b)—2(c)(1)) computed immediately before the distribution (and after any section 368(a)(1)(D) transfer connected with the section 355 distribution), but only to the extent that such amount is attributable to the distributing corporation and any corporations controlled by it immediately before the distribution (the distributing group) or the controlled corporation and any corporations controlled by it immediately before the distribution (the controlled group), as the case may be, under the principles of §§1.1248–1(d)(3), 1.1248–2 and 1.1248–3. However, the predistribution amount with respect to the distributing group shall be computed without taking into account the distributee’s predistribution amount with respect to the controlled group.

(2) Postdistribution amount. For purposes of this section, the postdistribution amount with respect to a distributing or controlled corporation is the distributee’s section 1248 amount (as defined in §1.367(b)—2(c)(1)) with respect to such stock, computed immediately after the distribution (but without regard to paragraph (c) or (d) of this section (whichever is applicable)). The postdistribution amount under this paragraph (e)(2) shall be computed before taking into account the effect (if any) of any inclusion under section 356(a) or (b).

(f) Exclusion of deemed dividend from foreign personal holding company income. In the event an amount is included in income as a deemed dividend by a foreign corporation under paragraph (c) or (d) of this section (including amounts received as an intermediate owner under the rule of §1.367(b)—2(e)(2)), such deemed dividend shall not be included as foreign personal holding company income under section 954(c).

(g) Examples. The following examples illustrate the rules of this section:
Example 1. (i) Facts. USS, a domestic corporation, owns 40 percent of the outstanding stock of FD, a controlled foreign corporation (CFC). USS has owned the stock since FD was incorporated. FD always has been a CFC. USS has a basis of $80 in its FD stock, which has a fair market value of $200. FD owns 100 percent of the outstanding stock of FC. USS has owned the stock since FC was incorporated. FD has owned the stock since FD was incorporated. Neither FD nor FC own stock in any other corporation. FD has earnings and profits of $0 and a fair market value of $250. In a pro rata distribution described in section 355, FD distributes to USS stock in FC worth $100; thereafter, USS’s FD stock is worth $100 as well.

(ii) Result—(A) FD’s distribution is a transaction described in paragraph (c)(1) of this section. Under paragraph (c)(2) of this section, USS must compare its predistribution amounts with respect to FD and FC to its respective postdistribution amounts. Under paragraph (e)(1) of this section, USS’s predistribution amount with respect to FD or FC is its section 1248 amount computed immediately before the distribution, but only to the extent such amount is attributable to FD or FC. Under $1.367(b)-2(c)(1), USS’s section 1248 amount computed immediately before the distribution is $120, all of which is attributable to FC. Thus, USS’s predistribution amount with respect to FD is $0, and its predistribution amount with respect to FC is $120. These amounts are computed as follows: If USS had sold its FD stock immediately before the transaction, it would have recognized $120 of gain ($200 fair market value—$80 basis). All of the gain would have been treated as a dividend under section 1248, and all of the section 1248 amount would have been treated as a dividend under section 1248. If USS sold its FD stock immediately after the distribution, it would have a $60 gain ($100 fair market value—$40 basis), all of which would be treated as a dividend under section 1248.

(C) The basis adjustment and income inclusion rules of paragraph (c)(2) of this section apply to the extent of any difference between USS’s postdistribution and predistribution amounts. In the case of FD, there is no difference between the two amounts and, as a result, no adjustment or income inclusion is required. In the case of FC, USS’s postdistribution amount is $60 less than its predistribution amount. Accordingly, under paragraph (c)(2) of this section, USS is required to reduce its basis in its FC stock from $90 to $0 and include $20 in income as a deemed dividend. Under $1.367(b)-2(e)(2), the $20 deemed dividend is considered as having been paid by FC to FD, and by FD to USS, immediately prior to the distribution. Under paragraph (f) of this section, the deemed dividend is not included by FD as foreign personal holding company income under section 954(c).

Example 2. (i) Facts. USS1 and USS2, domestic corporations, each own 50 percent of the outstanding stock of FD, a controlled foreign corporation (CFC). USS1 and USS2 each own 50 percent of the outstanding stock of FC, a foreign corporation. FD has owned the stock since FD was incorporated. Neither FD nor FC own stock in any other corporation. FD has earnings and profits of $0 and a fair market value of $750. In a non-pro rata distribution described in section 355, FD distributes all of the stock of FC to USS2 in exchange for USS2’s FD stock.

(ii) Result—(A) FD’s distribution is a transaction described in paragraph (d)(1) of this section. Under paragraph (d)(2) of this section, USS1 is considered a distributee of its proportionate share of the FD stock. Under paragraph (d)(3) of this section, USS1 and USS2 must compare their predistribution amounts with respect to FD and FC stock to their respective postdistribution amounts. Under paragraph (e)(1) of this section, USS1’s predistribution amount with respect to FD or FC is USS1’s section 1248 amount computed immediately
before the distribution, but only to the extent such amount is attributable to FD or FC. USS2's predistribution amount is determined in the same manner. Under §1.367(b)-2(c)(4), USS1 has a section 1248 amount computed immediately before the distribution of $250, all of which is attributable to FC. Thus, USS1 and USS2 each have a predistribution amount with respect to FD of $0, and each have a predistribution amount with respect to FC of $250. These amounts are computed as follows: If either USS1 or USS2 had sold its FD stock immediately before the transaction, it would have recognized $250 of gain ($750 fair market value—$500 basis). All of the gain would have been treated as a dividend under section 1248, and all of the section 1248 amount would have been attributable to FC (based on USS1's and USS2's pro rata shares of FC's earnings and profits (50 percent × $500)).

(B) Under paragraph (d)(3) of this section, a distributee that owns no stock in the distributing or controlled corporation immediately after the distribution has a postdistribution amount with regard to that stock of zero. Accordingly, USS2 has a postdistribution amount of $0 with respect to FC and USS1 has a postdistribution amount of $250 with respect to FC. Under paragraph (e)(2) of this section, USS1's postdistribution amount with respect to FD is its section 1248 amount with respect to such corporation, computed immediately after the distribution (but without regard to paragraph (d) of this section). USS2's postdistribution amount with respect to FC is determined in the same manner. Under §1.367(b)-2(c)(1), USS1's section 1248 amount computed immediately after the distribution with respect to FD is $0 and USS2's section 1248 amount computed immediately after the distribution with respect to FC is $250 less than its section 1248 amount computed immediately after the distribution. If USS1 sold its FD stock immediately after the distribution, none of the resulting $250 gain ($750 fair market value—$500 basis) would be treated as a dividend under section 1248. If USS2 sold its FD stock immediately after the distribution, it would have a $250 gain ($750 fair market value—$500 basis), all of which would be treated as a dividend under section 1248.

(C) The income inclusion rule of paragraph (d)(3) of this section applies to the extent of any difference between USS1's and USS2's postdistribution and predistribution amounts. In the case of USS2, there is no difference between the two amounts with respect to either FD or FC and, as a result, no income inclusion is required. In the case of USS1, there is no difference between the two amounts with respect to its FD stock. However, USS1's postdistribution amount with respect to FC is $250 less than its predistribution amount. Accordingly, under paragraph (d)(3) of this section, USS1 is required to include $250 in income as a deemed dividend. Under §1.367(b)-2(e)(2), the $250 deemed dividend is considered as having been paid by FC to FD, and by FD to USS1, immediately prior to the distribution. This deemed dividend increases USS1's basis in FD ($500 + $250 = $750). Under paragraph (f) of this section, the deemed dividend is not included by FD as foreign personal holding company income under section 954(c).

§1.367(b)-6 Effective dates and coordination rules.

(a) Effective date.—(1) In general. Except as otherwise provided in this paragraph (a)(1), §§1.367(b)-1 through 1.367(b)-5, and this section, apply to section 367(b) exchanges that occur on or after January 23, 2006. The rules of §§1.367(b)-3 and 1.367(b)-4, as they apply to reorganizations described in section 368(a)(1)(A) (including reorganizations described in section 368(a)(2)(D) or (E)) involving a foreign acquiring or foreign acquired corporation, apply only to transfers occurring on or after January 23, 2006. Section 1.367(b)-4(b)(1)(ii) applies to all triangular reorganizations and reorganizations described in section 368(a)(1)(G) and (a)(2)(D) occurring on or after January 23, 2006, although taxpayers may apply §1.367(b)-4(b)(1)(ii) to triangular B reorganizations occurring on or after February 23, 2006, in a taxable year that is not closed by the period of limitations if done consistently with respect to all such triangular B reorganizations. The second sentence of paragraph (a) in §1.367(b)-4 shall apply to section 304(a)(1) transactions occurring on or after February 23, 2006; however, taxpayers may rely on this sentence for exchanges that occur before November 6, 2006, see 26 CFR part 1 revised as of April 1, 2006.

369