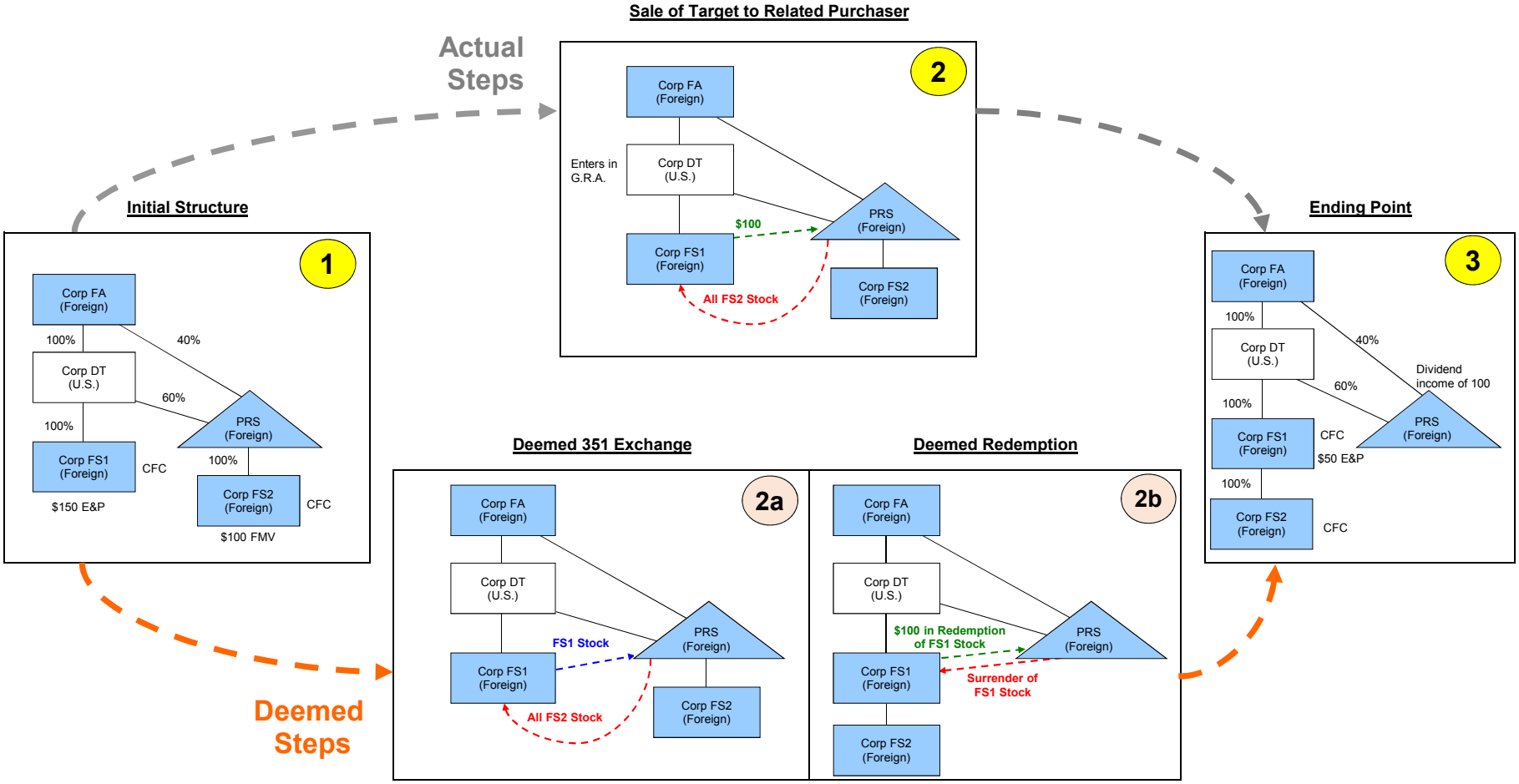
Notice 2014-52
Sec. 3.03 Example 2

Code §304(a)(1) & (b)(4)(B): 50% Rule Applies Only to Earnings of Foreign Acquiring (Limit Does Not Apply)



FA, a foreign corporation that is not a CFC, wholly owns DT, a domestic corporation. DT wholly owns FS1, a CFC. FA and DT own 40 percent and 60 percent, respectively, of the capital and profits interests of PRS, a foreign partnership. PRS wholly owns FS2, a CFC. The FS2 stock has a fair market value of $100x. FS1 has earnings and profits of $150x. PRS transfers all of its FS2 stock to FS1 in exchange for $100x of cash. DT enters into a gain recognition agreement that complies with the requirements set forth in section 4.01 of Notice 2012-15, 2012-9 IRB 424, with respect to the portion (60 percent) of the FS2 stock that DT is deemed to transfer to FS1 in an exchange described in Code §367(a)(1). See Treas. Reg. §1.367(a)-1T(c)(3)(i)(A).

Under Code §304(a)(1), PRS and FS1 are treated as if PRS transferred its FS2 stock to FS1 in an exchange described in Code §351(a) solely for FS1 stock, and, in turn, FS1 redeemed such FS1 stock in exchange for $100x of cash. The redemption of the FS1 stock is treated as a distribution to which section 301 applies pursuant to Code §302(d). Without regard to the application of Code §304(b)(5)(B), more than 50 percent of a dividend arising from the acquisition, taking into account only the earnings and profits of FS1 pursuant to section 3.03(b) of Notice 2014-52, would be subject to tax under Chapter 1 of the Code. In particular, 60 percent of a dividend from FS1 would be included in DT's distributive share of PRS's partnership income and therefore would be subject to tax. Accordingly, Code §304(b)(5)(B) does not apply and the entire distribution of $100x is treated under Code §301(c)(1) as a dividend (as defined in Code §316) out of the earnings and profits of FS1.