notice and public comment are unnecessary because this amendment to the regulations provides only technical changes to update the address for the submission of INDs regulated by CDER and to correct a typographical error in the Agency's bioequivalence regulations.

List of Subjects

21 CFR Part 312

Drugs, Exports, Imports, Investigations, Labeling, Medical research, Reporting and recordkeeping requirements, Safety.

21 CFR Part 320

Drugs, Reporting and recordkeeping requirements.

Therefore, under the Federal Food, Drug, and Cosmetic Act and under authority delegated to the Commissioner of Food and Drugs, 21 CFR parts 312 and 320 are amended as follows:

PART 312—INVESTIGATIONAL NEW DRUG APPLICATION

■ 1. The authority citation for 21 CFR part 312 continues to read as follows:

Authority: 21 U.S.C. 321, 331, 351, 352, 353, 355, 360bbb, 371; 42 U.S.C. 262.

§ 312.140 [Amended]

■ 2. Section 312.140 is amended in paragraph (a)(2) by removing ''CDER Therapeutic Biological Products'' and adding in its place ''Central'', and by removing ''12229 Wilkins Ave., Rockville, MD 20852'' and adding in its place ''5901–B Ammendale Rd., Beltsville, MD 20705–1266''.

PART 320—BIOAVAILABILITY AND BIOEQUIVALENCE REQUIREMENTS

■ 3. The authority citation for 21 CFR part 320 continues to read as follows:

Authority: 21 U.S.C. 321, 351, 352, 355, 371.

§ 320.33 [Amended]

■ 4. Section 320.33 is amended in paragraph (f)(3) by removing ''(first-class metabolism)'' and adding in its place ''(first-pass metabolism)''.

Dated: March 22, 2016.

Leslie Kux,

Associate Commissioner for Policy.

[FR Doc. 2016–06886 Filed 3–25–16; 8:45 am]

BILLING CODE 4164–01–P

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[TD 9759]

RINs 1545–BF43; 1545–BC88

Limitations on the Importation of Net Built-In Losses

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations under sections 334(b)(1)(B) and 362(e)(1) of the Internal Revenue Code of 1986 (Code). The regulations apply to certain nonrecognition transfers of loss property to corporations that are subject to certain taxes under the Code. The regulations affect the corporations receiving such loss property. This document also amends final regulations under sections 332 and 351 to reflect certain statutory changes. The regulations affect certain corporations that transfer assets to, or receive assets from, their shareholders in exchange for the corporation's stock.

DATES: *Effective Date:* These final regulations are effective on March 28, 2016.

FOR FURTHER INFORMATION CONTACT: John P. Stemwedel (202) 317–5363 or Theresa A. Abell (202) 317–7700 (not toll free numbers).

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

The collection of information contained in these final regulations revises a collection of information that has been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)) under control number 1545–2019. The revised collection of information in these final regulations is in §§ 1.332–6, 1.351–3, and 1.368–3. By requiring that taxpayers separately report the fair market value and basis of property (including stock) described in section 362(e)(1)(B) and in 362(e)(2)(A) that is transferred in a tax-free transaction, this revised collection of information aids in identifying transactions within the scope of sections 334(b)(1)(B), 362(e)(1), and 362(e)(2) and thereby facilitates the ability of the IRS to verify that taxpayers are complying with sections 334(b)(1)(B), 362(e)(1), and 362(e)(2). The respondents will be corporations and their shareholders.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid control number.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential, as required by section 6103.

Background

Sections 334(b)(1)(B) and 362(e)(1) (the anti-loss importation provisions) were added to the Code by the American Jobs Creation Act of 2004 (Pub. L. 108–357, 188 Stat. 1418) to prevent erosion of the corporate tax base when a person (Transferor) transfers property to a corporation (Acquiring) and the result would be an importation of loss into the federal tax system. Proposed regulations under sections 334(b)(1)(B) and 362(e)(1) were published in the **Federal Register** (78 FR 54971) on September 9, 2013 (the 2013 NPRM). Three written comments were submitted on the 2013 NPRM; no public hearing was requested or held. Additionally, on March 10, 2005, the Treasury Department and the IRS published in the **Federal Register** (70 FR 11903–01) a notice of proposed rulemaking (the 2005 NPRM) that, among other things, proposed amendments to the regulations under sections 332 and 351 to reflect statutory changes. No comments were received with respect to the amendments reflecting statutory changes to section 332 and 351, although several comments were received with respect to other aspects of the 2005 NPRM. The 2005 NPRM's proposed amendments that reflect statutory changes are included in this final rule.

The comments with respect to the 2013 NPRM, and the respective responses of the Treasury Department and the IRS, are described in the Summary of Comments and Explanation of Provisions that follows the Summary of the 2013 NPRM.

Summary of the 2013 NPRM

1. General Application of Sections and Interaction With Other Law

The 2013 NPRM provided specific rules to implement the statutory framework of the anti-loss importation provisions, such as rules for identifying ''importation property'' and for determining whether the transfer of that property occurs in a transaction subject to the anti-loss importation provisions (designated a ''loss importation

transaction'' under the 2013 NPRM and these final regulations).

a. Importation Property

The 2013 NPRM used a hypothetical sale analysis to identify importation property. Under this approach, the actual tax treatment of any gain or loss that would be recognized on a sale of an individual property, first by the Transferor immediately before the transfer and then by Acquiring immediately after the transfer, determined whether that individual property was importation property. If a Transferor's gain or loss on a sale of an individual property immediately before the transfer would not be subject to any tax imposed under subtitle A of the Code (federal income tax), the first condition for classification as importation property would be satisfied. If Acquiring's gain or loss on a sale of the transferred property immediately after the transfer would be subject to federal income tax, the second condition for classification as importation property would be satisfied. If both of these conditions would be satisfied, the property would be importation property.

In general, this determination was made by reference to the tax treatment of the Transferor(s) or Acquiring as hypothetical sellers of the transferred or acquired property, that is, whether the hypothetical seller would take the gain or loss into account in determining its federal income tax liability. This determination had to take into account all relevant facts and circumstances. The 2013 NPRM included a number of examples illustrating this approach. Thus, in one example, a tax-exempt entity transferred property to a taxable domestic corporation, and the determination took into account whether the transferor, though generally tax-exempt, would nevertheless be required to include the amount of the gain or loss in unrelated business taxable income (UBTI) under sections 511 through 514 of the Code. In other examples, a foreign corporation transferred property to a taxable domestic corporation and the determination took into account whether the foreign corporation would be required to include the amount of gain or loss under section 864 or 897 as income effectively connected with, or treated as effectively connected with, the conduct of a U.S. trade or business. Although the examples assumed that there was no applicable income tax treaty, in the case of an applicable income tax treaty, the determination of whether property is importation property would take into account whether the Transferor would be taxable under the business profits article or gains article of the income tax treaty.

i. Property Acquired From Grantor Trusts, Partnerships, and S Corporations

Although the general rule in the 2013 NPRM looked solely to the tax treatment of the Transferor(s) and Acquiring as hypothetical sellers, a look-through rule applied if a Transferor was a grantor trust, a partnership, or a small business corporation that elected under section 1362(a) to be an S corporation. In these cases, the determination of whether gain or loss from a hypothetical sale was subject to federal income tax was made by reference to the tax treatment of the gain or loss in the hands of the grantors, the partners, or the S corporation shareholders.

If an organizing instrument allocated gain or loss in different amounts, including by reason of a special allocation under a partnership agreement, the determination of whether gain or loss from a hypothetical sale by the entity was subject to federal income tax would be made by reference to the person to whom, under the terms of the instrument, the gain or loss on the entity's hypothetical sale would actually be allocated, taking into account the entity's net gain or loss actually recognized in the tax period in which the transaction occurred.

ii. Anti-Avoidance Rule for Certain Entities

In certain circumstances, the Code permits an entity that would otherwise be subject to federal income tax to shift the incidence of federal income taxation to the entity's owners. For example, under sections 651 and 652, and sections 661 and 662, distributions made by a trust are deducted from the trust's income for federal income tax purposes and included in the beneficiary's (or beneficiaries') gross income. Certain domestic corporations, including regulated investment companies (RICs, as defined in section 851(a)), real estate investment trusts (REITs, as defined in section 856(a)), and domestic corporations taxable as cooperatives (Cooperatives; see section 1381) are also able to shift the incidence of federal income taxation by distributing income or gain.

The Treasury Department and the IRS were concerned that disregarding the ability of these entities to shift the incidence of federal income taxation could undermine the anti-loss importation provisions. However, the Treasury Department and the IRS were also concerned that applying a look-through rule in all of these cases would impose a significant administrative burden.

Accordingly, the 2013 NPRM included an anti-avoidance rule that applied to domestic trusts, estates, RICs, REITs, and Cooperatives that directly or indirectly transferred property (including through other such entities) in a transaction described in section 362(a) or 362(b) (a Section 362 Transaction). The rule applied if the property had been directly or indirectly transferred to or acquired by the entity as part of a plan to avoid the application of the anti-loss importation provisions. When the look-through rule applied, the entity was presumed to distribute the proceeds of its hypothetical sale and the tax treatment of the gain or loss in the distributees' hands would determine whether the gain or loss was taken into account in determining a federal income tax liability. If the distributee were also such an entity, the principles of this rule applied to look to the ultimate owners of the interests in the entity.

iii. Gain or Loss Affecting Certain Income Inclusions

Prior to the publication of the 2013 NPRM, questions were raised regarding the treatment of property transferred by or to a controlled foreign corporation (CFC), as defined in section 957 (taking into account section 953(c)). The general rules of the 2013 NPRM would not treat gain or loss recognized on a hypothetical sale by a CFC as subject to federal income tax; however, because practitioners raised concerns prior to the publication of the 2013 NPRM, the 2013 NPRM expressly provided that gain or loss recognized on a hypothetical sale by a CFC is not considered subject to federal income tax solely by reason of an income inclusion under section 951(a). The 2013 NPRM similarly provided that gain or loss recognized by a passive foreign investment company, as defined in section 1297(a), was not subject to federal income tax solely by reason of an inclusion under section 1293(a).

iv. Gain or Loss Taxed to More Than One Person

If gain or loss realized on a hypothetical sale would be includible in income by more than one person, the 2013 NPRM treated such property, solely for purposes of the anti-loss importation provisions, as tentatively divided into separate portions in proportion to the allocation of gain or loss from a hypothetical sale to each person. Tentatively divided portions were treated and analyzed in the same manner as any other property for

purposes of applying the anti-loss importation provisions.

b. Loss Importation Transaction

Under the 2013 NPRM, once property had been identified as importation property, Acquiring would determine its basis in the importation property under generally applicable rules (disregarding sections 362(e)(1) and 362(e)(2)) and, if that aggregate basis exceeded the aggregate value of all importation property transferred in the Section 362 Transaction, the transaction was a loss importation transaction subject to the anti-loss importation provisions. If the aggregate basis of the importation property did not exceed such property's value, the anti-loss importation provisions had no further application.

i. Aggregate, Not Transferor-by-Transferor, Approach

By their terms, section 362(e)(1) and the provisions of the 2013 NPRM apply in the aggregate to all importation property acquired in a transaction, regardless of the number of transferors in the transaction. This rule differs from the transferor-by-transferor approach of section 362(e)(2), which is concerned with whether a transferor would otherwise duplicate loss by retaining loss in stock and transferring property with a net built-in loss.

ii. Valuing Partnership Interests

In response to concerns raised by practitioners prior to the publication of the 2013 NPRM, a special valuation rule for transfers of partnership interests was included in the 2013 NPRM. Under that rule, the value of a partnership interest would be determined in a manner that takes partnership liabilities into account. Specifically, the 2013 NPRM provided that the value of a partnership interest would be the sum of cash that Acquiring would receive for such interest, increased by any § 1.752–1 liabilities (as defined in § 1.752–1(a)(4)) of the partnership that were allocated to Acquiring with regard to such transferred interest under section 752. The 2013 NPRM included an example that illustrated the application and effect of this rule. The 2013 NPRM also clarified that any section 743(b) adjustment to be made as a result of the transaction was made after any section 362(e) basis adjustment.

c. Acquiring's Basis in Acquired Property

If a transaction was a loss importation transaction under the 2013 NPRM, Acquiring's basis in each importation property received (including the tentatively divided portions of property determined to be importation property) was an amount equal to the value of that property, notwithstanding the general rules in sections 334(b)(1)(B), 362(a), and 362(b). This rule applied to all importation property, regardless of whether the property's value was more or less than its basis prior to the loss importation transaction.

Immediately following the application of the anti-loss importation provisions (and prior to any application of section 362(e)(2)), any property that was treated as tentatively divided for purposes of applying the anti-loss importation provisions ceased to be treated as divided and was treated as one undivided property (re-constituted property) with a basis equal to the sum of the bases of the portions determined under the anti-loss importation provision, and the bases of all other portions determined under generally applicable provisions (other than section 362(e)(2)).

If the transaction was described in section 362(a), the transferred property was then aggregated on a transferor-by-transferor basis to determine whether further adjustment would be required to the bases of loss properties under section 362(e)(2). The 2013 NPRM included a cross-reference to section 362(e)(2) as well as examples illustrating the application of both section 362(e)(1) and (e)(2) to situations involving multiple transferors and multiple properties that were not all importation properties.

2. Filing Requirements

To facilitate the administration of both the anti-loss importation provisions and the anti-duplication provisions in section 362(e)(2), the 2013 NPRM modified the reporting requirements applicable in all affected transactions (section 332 liquidations and transactions described in section 362(a) or section 362(b)) to require taxpayers to identify the bases and values of properties subject to those sections.

3. Modifications to Liquidation Regulations

The 2013 NPRM also included several modifications to the regulations applicable to corporate liquidations. These modifications were not substantive changes to the law; they were solely to update the regulations to reflect certain statutory changes, including the repeal of the *General Utilities* doctrine (reflected in the modification of sections 334(a) and 337(a), and the repeal of sections 333 and 334(c)), the removal of former section 334(b)(2) (replaced by section 338), and the relocation of former section 332(c) (subsidiary indebtedness) to current section 337(b). In response to certain regulatory changes, the 2013 NPRM also added several cross-references to regulations under section 367 and 897 to highlight the treatment of certain transfers between foreign corporations.

Summary of Comments and Explanation of Provisions

In general, the commenters agreed with the general framework prescribed in the 2013 NPRM and the positions taken therein by the Treasury Department and the IRS. Accordingly, the final regulations generally adopt the provisions of the 2013 NPRM. However, the final regulations also adopt certain modifications and include certain clarifications in response to comments. These comments, and the respective responses of the Treasury Department and the IRS, are described in the following paragraphs.

1. Comments Related to Partnership Matters

The majority of comments received in response to the 2013 NPRM related to issues involving partnerships.

a. Items Taken Into Account To Determine Treatment of Hypothetical Sale

As described previously, under the 2013 NPRM, the determination of whether gain or loss on property transferred by a partnership is subject to federal income tax would be made by reference to the treatment of the partners, taking into account all partnership items for the year of the Section 362 Transaction. One commenter suggested a closing-of-the-books rule instead, asserting such an approach would be more administrable for transferor partnerships. The Treasury Department and the IRS are concerned that the allocation of partnership items as of the date of the transfer could differ from the allocation of such items at the end of the partnership tax year. In such a case, the partner to whom gain or loss on the hypothetical sale of the transferred property would be allocated as of the transfer date (using a hypothetical closing-of-the-books method) may not be the partner to whom the allocation would be made as of the end of the year, taking all items for the year into account. The Treasury Department and the IRS believe that the latter approach more accurately identifies the partner to whom the gain or loss on a sale of the property would be allocated, and thus more accurately determines whether

such amounts would be subject to federal income tax. Accordingly, these final regulations do not permit using a closing-of-the-books method.

In response to questions about how to determine to which partner an item would be allocated, and thus its federal income tax treatment, the final regulations clarify that the partnership agreement as well as any applicable rules of law are taken into account.

b. Widely-Held Partnerships and Publicly Traded Partnerships

Another commenter requested that widely held partnerships (WHPs) and publicly traded partnerships (PTPs) not be subject to the look-through rule applicable to all partnerships for determining whether gain or loss on a hypothetical sale is subject to federal income tax. Instead, the commenter requested these entities be afforded treatment similar to that of domestic estates, trusts, RICs, REITs, and Cooperatives (and therefore be subject to look-through treatment only in abusive situations). The commenter's reasons for this suggested modification included that look-through treatment would impose a substantial administrative burden on WHPs and PTPs and that these entities are not generally vehicles for abuse. However, the statute explicitly contemplates that partners, not partnerships, are the focus of the inquiry under section 362(e)(1). WHPs and PTPs are already required to apply a look-through approach to track and report information to their partners. For purposes of determining whether there is an importation of loss for PTPs, the Treasury Department and the IRS will respect determinations derived by applying generally accepted conventions in determining allocable income. *See,* for example, the conventions set forth in § 1.706–4(c)(3)(ii). Accordingly, the Treasury Department and the IRS do not believe it is necessary or appropriate to treat these partnerships as other than partnerships, and the final regulations retain the approach used in the 2013 NPRM.

c. Interactions of Sections 362(e) and 704(c)(1)(C)

Commenters also requested clarification of the interaction of the regulations proposed under section 362(e)(1), the regulations under section 362(e)(2), and regulations proposed under section 704(c)(1)(C) (79 FR 3041 (January 16, 2014)). The Treasury Department and the IRS agree that such clarification would be appropriate. However, the interaction of these provisions cannot be addressed independently of the promulgation of final regulations under section 704(c)(1)(C). Accordingly, these issues will be addressed as part of the finalization of regulations under that section.

d. Partnership Allocations in the Case of a Section 362(e)(2)(C) Election

The 2013 NPRM, like the final regulations under section 362(e)(2), included examples involving partnership transferors and allocation to partners of resulting adjustments under section 362(e)(1) and (2), including adjustments in the case of a section 362(e)(2)(C) election. The examples direct allocations to the partners that contributed the property transferred by the partnership in order to comply with the legislative purpose of section 362(e)(1) and (2) and to prevent distortions. Commenters agreed with the results provided in the examples but requested a clarification of the authority on which the analyses were based. The analysis reflected in the examples is based on general aggregate and entity principles of partnership tax law, taking into account the aggregate approach reflected in the statutory language of section 362(e)(1), and the purposes and principles of section 362(e)(1) and (2). The rule applying an aggregate approach to partnerships is set forth in § 1.362–3(d)(2) and is illustrated in Example 5 of § 1.362–3(f).

e. Rev. Rul. 84–111 and Rev. Rul. 99–6

One commenter requested that the final regulations clarify the effect of Rev. Rul. 84–111 (1984–30 IRB 6, 1984–2 CB 88) and Rev. Rul. 99–6 (1999–6 IRB 6, 1999–1 CB 432) on a transfer of all the interests in a partnership to a single transferee in a loss importation transaction. The Treasury Department and the IRS recognize that guidance would be helpful in this area but have concluded that resolution of the complex issues implicated by those rulings is beyond the scope of this project. Accordingly, these final regulations do not address this issue.

2. Comments Related to Other Special Entities

a. Anti-Avoidance Rule

As previously described, the 2013 NPRM would only subject domestic estates, trusts, RICs, REITs, and Cooperatives to look-through treatment in certain abusive situations. One comment suggested that the anti-avoidance rule would be strengthened if the final regulations provided certain operating presumptions or factors to be applied in determining whether the rule would apply. The Treasury Department and the IRS have considered this suggestion but determined that the approach of the 2013 NPRM, focusing on the existence of a plan to avoid the anti-loss importation provisions, is appropriate and administrable. Accordingly, the final regulations do not adopt this suggestion.

b. Foreign Non-Grantor Trusts

Another modification suggested by a commenter would allow a foreign non-grantor trust to prove that its beneficiaries were not foreign, in order to avoid treating gain or loss from its hypothetical sale as being treated as not subject to federal income tax. The Treasury Department and the IRS considered the suggestion and determined that such an approach is inconsistent with the anti-loss importation provisions and the general approach of the regulations because, subject to the anti-abuse rule, all non-grantor trusts, not their beneficiaries, are treated as transferors for purposes of the anti-loss importation provisions. In addition, adopting the commenter's suggestion would lead to inappropriate electivity with respect to the application of the anti-loss importation provisions because such an approach would depend on the identity of the foreign non-grantor trust's beneficiaries rather than a determination of whether the foreign non-grantor trust is subject to federal income tax. Accordingly, the final regulations do not adopt this suggestion.

c. Trusts With No Distributable Net Income

Another commenter suggested that a domestic trust should be excepted from look-through treatment under the anti-abuse rule if it has no distributable net income within the meaning of section 643(a) in the taxable year of the transaction. The Treasury Department and the IRS considered this suggestion and determined that it could lead to inappropriate electivity and abuse because the existence of distributable net income is not controlling in determining whether a transfer furthers a plan to avoid the anti-loss importation provisions. The existence of such a plan is controlling for determining that the transfer is subject to the anti-abuse rule. Accordingly, the final regulations do not adopt this suggestion.

d. Tax-Exempt Transferors of Debt-Financed Property

Under the 2013 NPRM, if a tax-exempt entity transferred debt-financed property (as defined in section 514), the

disposition of such property would be subject to federal income tax and thus the property could not be importation property. This rule applied even if there was only a de minimis amount of indebtedness and so only a small portion of any gain or loss would be subject to federal income tax. Commenters noted the cliff effect and resulting potential for avoidance of the anti-loss importation provisions. The Treasury Department and the IRS agree, and the final regulations adopt an approach that treats debt-financed property as subject to federal income tax in proportion to the amount of such gain or loss that would be includible in the transferor's UBTI on a sale under sections 511–514. The final regulations provide that portions of property determined under this rule are generally treated under the anti-loss importation provisions in the same manner as portions of property tentatively divided to reflect multiple owners of gain or loss on the property (for example, when a partnership transfers property to Acquiring).

3. Interaction With Regulations Under Section 367(b)

The proposed regulations requested comments on the appropriate treatment of transactions subject to section 367(b) and to either section 334(b)(1)(B) or 362(e)(1). Comments were also specifically requested on what effect a basis reduction required under section 334(b)(1)(B) or 362(e)(1) should have on earnings and profits and any inclusion required under § 1.367(b)–3. One comment suggested that if an inbound liquidation or inter-group asset reorganization gives rise to an inclusion of the all earnings and profits amount under § 1.367(b)–3, the basis reduction under section 334(b)(1)(B) or 362(e)(1), respectively, should be reduced to allow the transferee corporation to preserve an amount of built-in loss equal to the all earnings and profits amount. The comment suggested that this reduction is appropriate because the inclusion of the all earnings and profits amount is intended, in part, as a toll charge for importing basis into the U.S. tax system. However, the comment acknowledged that if such a rule was adopted, anti-abuse rules would be needed to address stuffing transactions and consideration should be given to adjusting the reduction for foreign tax credits associated with the inclusion of the all earnings and profits amount.

The Treasury Department and the IRS have determined that the basis reduction should not be affected by an inclusion of the all earnings and profits amount. First, there is no indication in section 334(b) or 362(e), or their legislative history, that the basis reduction should be reduced or otherwise affected by an inclusion of the all earnings and profits amount. Second, such a reduction may be contrary to the policies underlying these provisions. For example, the built-in loss may have arisen before a domestic corporation acquires all the stock of a foreign corporation such that the built-in loss bears no relation to the all earnings and profits amount. Finally, determining the extent to which the built-in loss relates to the all earnings and profits amount would involve undue complexity. Accordingly, the final regulations do not adopt this suggestion. Furthermore, the final regulations affirmatively state that the basis reduction does not affect the calculation of the all earnings and profits amount.

4. Transferred Basis Transaction

Commenters requested clarification of whether a transferee's basis in property continued to be considered determined by reference to its transferor's basis, notwithstanding the application of section 334(b)(1)(B) or section 362(e)(1). One comment specifically related to the application of regulations under section 755; other comments related to the treatment of the transaction more generally, including under sections 1223 (holding periods) and 7701(a)(4) (definition of transferred basis transaction). The Treasury Department and the IRS have concluded that the application of the anti-loss importation provisions to section 332 liquidations or Section 362 Transactions should not be viewed as altering the fundamental nature of the transactions to which section 334(b), or section 362(a) or (b), apply. Similarly, the Treasury Department and the IRS have concluded that the anti-duplication provisions in section 362(e)(2) and § 1.362–4 should not be viewed as altering the fundamental nature of the transactions to which they apply. Accordingly, the final regulations expressly provide that, notwithstanding the application of the anti-loss importation or anti-duplication provisions to a transaction, the transferee's basis is generally considered determined by reference to the transferor's basis for federal income tax purposes.

However, solely for purposes of determining the adjustment to the basis of partnership property under section 755 when a partnership interest is transferred in a loss importation transaction, the transferee's basis in the interest will be treated as not determined by reference to the transferor's basis. The reason for this exception under section 755 is that the treatment prescribed under § 1.755–1(b)(2) and (3) (generally applicable to non-substituted basis transactions and providing for basis increases to built-in gain property and basis decreases to built-in loss property) mirrors that prescribed under the anti-loss importation provisions. Accordingly, in order to align the adjustments to partnership property under § 1.755–1 with those made under the anti-loss importation provisions, the final regulations provide that, solely for purposes of applying section 755, a determination of basis under the anti-loss importation provisions is treated as not made by reference to the transferor's basis.

5. Applicability of Other Provisions for Determining Basis

A commenter noted that certain language in the 2013 NPRM could be read in a way that was not intended. The 2013 NPRM states the general rule that Acquiring's basis in importation property in a loss importation transaction is equal to the value of the property immediately after the transaction, ''[n]otwithstanding any other provision of law[.]'' The comment indicated that this language could be read to mean that, if the anti-loss importation provisions applied to a transaction, the transaction would not be subject to other provisions of law, such as section 482, that could further affect basis. Any such implication was wholly unintended and would be inappropriate. Accordingly, the final regulations clarify that other provisions of law do in fact continue to apply.

6. Miscellaneous

Immediately following the publication of the 2013 NPRM, a number of questions were raised regarding cross-references to the anti-loss importation and anti-duplication provisions that were proposed to be included in § 1.358–6 (basis in triangular reorganizations). Those cross-references were included solely to put taxpayers on notice that the anti-loss importation and anti-duplication provisions could modify the application of the triangular basis regulations to a transaction subject to those regulations. No substantive rule was intended or effected by the proposed cross-references. However, to clarify the purpose and scope of the cross-references, the final regulations do not include the individual cross-references included in the 2013 NPRM. Instead, the final regulations combine these multiple cross-references into one cross-

reference that is included in the general statement of scope in § 1.358–6(a).

Commenters also noted a number of nonsubstantive corrections and clarifications that have been adopted.

Finally, commenters suggested a number of issues that could be the subject of further study, such as the effect of tax treaties, nonfunctional currency, and the application of section 7701(g) (clarification of fair market value in the case of non-recourse indebtedness). These issues are beyond the scope of this project and are therefore not addressed in these final regulations. The Treasury Department and the IRS are considering whether further study of those issues should be undertaken.

In addition, nonsubstantive changes to conform nomenclature with that adopted in these final regulations, as well as to correct obvious errors and clarify cross-references, are made to final regulations under sections 362(e)(2), 705, and 1367 published under TD 9633.

Finally, these final regulations include modifications to §§ 1.332–2 and 1.351–1 that reflect certain statutory changes under sections 332 (relating to ownership of subsidiary stock) and 351 (relating to property permitted to be received by a transferor without recognition of gain or loss) proposed by the Treasury Department and the IRS in the 2005 NPRM (the statutory modifications). As no comments were received with respect to the statutory modifications, the statutory modifications are adopted as final regulations without change.

Effective/Applicability Date

The final regulations under sections 334(b)(1)(B) and 362(e)(1) generally adopt the proposed effective date and thus are applicable to transactions occurring on or after *March 28, 2016,* unless completed pursuant to a binding agreement that was in effect prior to *March 28, 2016,* and all times afterwards. The final regulations also apply to transactions occurring before *March 28, 2016* resulting from entity classification elections made under § 301.7701–3 that are filed on or after *March 28, 2016.* In addition, the final regulations provide that taxpayers may apply these rules to any transaction occurring after October 22, 2004.

Special Analyses

Certain IRS regulations, including this one, are exempt from the requirements of Executive Order 12866, as supplemented and reaffirmed by Executive Order 13563. Therefore, a regulatory impact assessment is not required. It has also been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations. Further, it is hereby certified that these final regulations will not have a significant economic impact on a substantial number of small entities. This certification is based on the fact that the collection of information requirement in these regulations modifies an existing collection of information by requiring that certain information be reported separately instead of in the aggregate. Although there should be an actual decrease in reporting burden, since taxpayers would no longer be required to aggregate the data they collect, any change is expected to be minimal. Accordingly, a Regulatory Flexibility Analysis under the Regulatory Flexibility Act (5 U.S.C. chapter 6) is not required. Pursuant to section 7805(f) of the Code, the proposed regulations preceding these final regulations were submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact on small business, and no comments were received.

Drafting Information

The principal author of these regulations is John P. Stemwedel of the Office of Associate Chief Counsel (Corporate), IRS. However, other personnel from the Treasury Department and the IRS participated in their development.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 1 is amended as follows:

PART 1—INCOME TAXES

■ **Paragraph 1.** The authority citation for part 1 is amended by adding entries in numerical order to read in part as follows:

Authority: 26 U.S.C. 7805 * * *

Section 1.334–1 also issued under 26 U.S.C. 367(b).

* * * * *

Section 1.362–3 also issued under 26 U.S.C. 367(b).

* * * * *

■ **Par. 2.** Section 1.332–2 is amended by revising the first sentence of paragraph (a) and adding paragraph (f) to read as follows:

§ 1.332–2 Requirements for nonrecognition of gain or loss.

(a) The nonrecognition of gain or loss under section 332 is limited to the receipt of property by a corporation that is the actual owner of stock (in the liquidating corporation) meeting the requirements of section 1504(a)(2). * * *

* * * * *

(f) *Applicability date.* The first sentence of paragraph (a) of this section applies to plans of complete liquidation adopted after March 28, 1985, except as specified in section 1804(e)(6)(B)(ii) and (iii) of Pubic Law 99–514.

■ **Par. 3.** Section 1.332–6 is amended by revising paragraph (a)(3) and adding a sentence at the end of paragraph (e) to read as follows:

§ 1.332–6 Records to be kept and information to be filed with return.

(a) * * *

(3) The fair market value and basis of assets of the liquidating corporation that have been or will be transferred to any recipient corporation, aggregated as follows:

(i) Importation property distributed in a loss importation transaction, as defined in § 1.362–3(c)(2) and (3) (except that ''section 332 liquidation'' is substituted for ''section 362 transaction''), respectively;

(ii) Property with respect to which gain or loss was recognized on the distribution;

(iii) Property not described in paragraph (a)(3)(i) or (ii) of this section;

* * * * *

(e) *Effective/applicability date.* * * * Paragraph (a)(3) of this section applies with respect to liquidations under section 332 occurring on or after March 28, 2016, and also with respect to liquidations under section 332 occurring before such date as a result of an entity classification election under § 301.7701–3 of this chapter filed on or after March 28, 2016, unless such liquidation is pursuant to a binding agreement that was in effect prior to March 28, 2016 and at all times thereafter.

■ **Par. 4.** Section 1.332–7 is amended by adding a sentence after the first sentence of the paragraph to read as follows:

§ 1.332–7 Indebtedness of subsidiary to parent.

* * * See section 337(b)(1). * * *

■ **Par. 5.** Section 1.334–1 is revised to read as follows:

§ 1.334–1 Basis of property received in liquidations.

(a) *In general.* Section 334 sets forth rules for determining a distributee's

basis in property received in a distribution in complete liquidation of a corporation. The general rule is set forth in section 334(a) and provides that, if property is received in a distribution in complete liquidation of a corporation and if gain or loss is recognized on the receipt of the property, then the distributee's basis in the property is the fair market value of the property at the time of the distribution. However, if property is received in a complete liquidation to which section 332 applies, including property received in satisfaction of an indebtedness described in section 337(b)(1), see section 334(b)(1) and paragraph (b) of this section.

(b) *Liquidations under section 332*—(1) *General rule.* Except as otherwise provided in paragraph (b)(2) or (3) of this section, if a corporation (P) meeting the ownership requirements of section 332(b)(1) receives property from a subsidiary (S) in a complete liquidation to which section 332 applies (section 332 liquidation), including property received in a transfer in satisfaction of indebtedness that satisfies the requirements of section 337(b)(1), P's basis in the property received is the same as S's basis in the property immediately before the property was distributed. However, see § 1.460–4(k)(3)(iv)(B)(*2*) for rules relating to adjustments to the basis of certain contracts accounted for using a long-term contract method of accounting that are acquired in a section 332 liquidation.

(2) *Basis in property with respect to which gain or loss was recognized.* Except as otherwise provided in Subtitle A of the Internal Revenue Code (Code) and this subchapter of the Income Tax Regulations, if S recognizes gain or loss on the distribution of property to P in a section 332 liquidation, P's basis in that property is the fair market value of the property at the time of the distribution. Section 334(b)(1)(A) (certain tax-exempt distributions under section 337(b)(2)); see also, for example, § 1.367(e)–2(b)(3)(i).

(3) *Basis in importation property received in loss importation transaction*—(i) *Purpose.* The purpose of section 334(b)(1)(B) and this paragraph (b)(3) is to modify the application of this section to prevent P from importing a net built-in loss in a transaction described in section 332. See paragraph (b)(3)(iii)(A) of this section for definitions of terms used in this paragraph (b)(3).

(ii) *Determination of basis.* Notwithstanding paragraph (b)(1) of this section, if a section 332 liquidation is a loss importation transaction, P's basis in each importation property received from S in the liquidation is an amount that is equal to the value of the property. The basis of property received in a section 332 liquidation that is not importation property received in a loss importation transaction is determined under generally applicable basis rules without regard to whether the liquidation also involves the receipt of importation property in a loss importation transaction.

(iii) *Operating rules*—(A) *In general.* For purposes of section 334(b)(1)(B) and this paragraph (b)(3), the provisions of § 1.362–3 (basis of importation property received in a loss importation transaction) apply, adjusted as appropriate to apply to section 332 liquidations. Thus, when used in this paragraph (b)(3), the terms ''importation property,'' ''loss importation transaction,'' and ''value'' have the same meaning as in § 1.362–3(c)(2), (3), and (4), respectively, except that ''the section 332(b)(1) distributee corporation'' is substituted for ''Acquiring'' and ''section 332 liquidation'' is substituted for ''section 362 transaction.'' Similarly, when gain or loss on property would be owned or treated as owned by multiple persons, the provisions of § 1.362–3(d)(2) apply to tentatively divide the property in applying this section, substituting ''section 332 liquidation'' for ''section 362 transaction'' and making such other adjustments as necessary.

(B) *Time for making determinations.* For purposes of section 334(b)(1)(B) and this paragraph (b)(3)—

(*1*) *P's basis in distributed property.* P's basis in each property S distributes to P in the section 332 liquidation is determined immediately after S distributes each such property;

(*2*) *Value of distributed property.* The value of each property S distributes to P in the section 332 liquidation is determined immediately after S distributes the property;

(*3*) *Importation property.* The determination of whether each property distributed by S is importation property is made as of the time S distributes each such property;

(*4*) *Loss importation transaction.* The determination of whether a section 332 liquidation is a loss importation transaction is made immediately after S makes the final liquidating distribution to P.

(C) *Effect of basis determination under this paragraph (b)(3)*—(*1*) *Determination by reference to transferor's basis.* A determination of basis under section 334(b)(1)(B) and this paragraph (b)(3) is a determination by reference to the transferor's basis, including for purposes of sections 1223(2) and 7701(a)(43). However, solely for purposes of applying section 755, a determination of basis under this paragraph (b)(3) is treated as a determination not by reference to the transferor's basis.

(*2*) *Not tax-exempt income or noncapital, nondeductible expense.* The application of this paragraph (b)(3) does not give rise to an item treated as tax-exempt income under § 1.1502–32(b)(2)(ii) or as a noncapital, nondeductible expense under § 1.1502–32(b)(2)(iii).

(*3*) *No effect on earnings and profits.* Any determination of basis under this paragraph (b)(3) does not reduce or otherwise affect the calculation of the all earnings and profits amount provided in § 1.367(b)–2(d).

(iv) *Examples.* The examples in this paragraph (b)(3)(iv) illustrate the application of section 334(b)(1)(B) and the provisions of this paragraph (b)(3). Unless the facts indicate otherwise, the examples use the following nomenclature and assumptions: USP is a domestic corporation that has not elected to be an S corporation within the meaning of section 1361(a)(1); FC, CFC1, and CFC2 are controlled foreign corporations within the meaning of section 957(a), which are not engaged in a U.S. trade or business, have no U.S. real property interests, and have no other relationships, activities, or interests that would cause their property to be subject to any tax imposed under subtitle A of the Code (federal income tax); there is no applicable income tax treaty; and all persons and transactions are unrelated. All other relevant facts are set forth in the examples:

Example 1. Basic application of this paragraph (b)(3). (i) *Distribution of importation property in a loss importation transaction.* (A) *Facts.* USP owns the sole outstanding share of FC stock. FC owns three assets, A1 (basis $40, value $50), A2 (basis $120, value $30), and A3 (basis $140, value $20). On Date 1, FC distributes A1, A2, and A3 to USP in a complete liquidation that qualifies under section 332.

(B) *Importation property.* Under § 1.362–3(d)(2), the fact that any gain or loss recognized by a CFC may affect an income inclusion under section 951(a) does not alone cause gain or loss recognized by the CFC to be treated as taken into account in determining a federal income tax liability for purposes of this section. Thus, if FC had sold either A1, A2, or A3 immediately before the transaction, no gain or loss recognized on the sale would have been taken into account in determining a federal income tax liability. Further, if USP had sold A1, A2, or A3 immediately after the transaction, USP would take into account any gain or loss recognized on the sale in determining its federal income tax liability. Therefore, A1, A2, and A3 are

all importation properties. See paragraph (b)(3)(iii)(A) of this section and § 1.362–3(c)(2).

(C) *Loss importation transaction.* Immediately after the distribution, USP's aggregate basis in the importation properties, A1, A2, and A3, would, but for section 334(b)(1)(B) and this section, be $300 ($40 + $120 + $140) and the properties' aggregate value would be $100 ($50 + $30 + $20). Therefore, the importation properties' aggregate basis would exceed their aggregate value and the distribution is a loss importation transaction. See paragraph (b)(3)(iii)(A) of this section and § 1.362–3(c)(3).

(D) *Basis of importation property distributed in loss importation transaction.* Because the importation properties, A1, A2, and A3, were transferred in a loss importation transaction, the basis in each of the importation properties received is equal to its value immediately after FC distributes the property. Accordingly, USP's basis in A1 is $50; USP's basis in A2 is $30; and USP's basis in A3 is $20.

(ii) *Distribution of both importation and non-importation property in a loss importation transaction.* (A) *Facts.* The facts are the same as in paragraph (i)(A) of this *Example 1* except that FC is engaged in a U.S. trade or business and A3 is used in that U.S. trade or business.

(B) *Importation property.* A1 and A2 are importation properties for the reasons set forth in paragraph (i)(B) of this *Example 1.* However, if FC had sold A3 immediately before the transaction, FC would take into account any gain or loss recognized on the sale in determining its federal income tax liability. Therefore, A3 is not importation property. See paragraph (b)(3)(iii)(A) of this section and § 1.362–3(c)(2).

(C) *Loss importation transaction.* Immediately after the distribution, USP's aggregate basis in the importation properties, A1 and A2, would, but for section 334(b)(1)(B) and this section, be $160 ($40 + $120). Further, the properties' aggregate value would be $80 ($50 + $30). Therefore, the importation properties' aggregate basis would exceed their aggregate value and the distribution is a loss importation transaction. See paragraph (b)(3)(iii)(A) of this section and § 1.362–3(c)(3).

(D) *Basis of importation property distributed in loss importation transaction.* Because the importation properties, A1 and A2, were transferred in a loss importation transaction, the basis in each of the importation properties received is equal to its value immediately after FC distributes the property. Accordingly, USP's basis in A1 is $50 and USP's basis in A2 is $30.

(E) *Basis of other property.* Because A3 is not importation property distributed in a loss importation transaction, USP's basis in A3 is determined under generally applicable basis rules. Accordingly, USP's basis in A3 is $140, the adjusted basis that FC had in the property immediately before the distribution. See section 334(b)(1).

(iii) *FC not wholly owned.* The facts are the same as in paragraph (i)(A) of this *Example 1* except that USP owns only 80% of the sole outstanding class of FC stock and the remaining 20% is owned by individual X. Further, on Date 1 and pursuant to the plan of liquidation, FC distributes A1 and A2 to USP and A3 to X. A1 and A2 are importation properties, the distribution to USP is a loss importation transaction, and USP's bases in A1 and A2 are equal to their value ($50 and $30, respectively) for the reasons set forth in paragraphs (ii)(C) and (D) of this *Example 1.* Under section 334(a), X's basis in A3 is $20.

(iv) *Importation property, no net built in loss.* (A) *Facts.* The facts are the same as in paragraph (i)(A) of this *Example 1* except that the value of A2 is $230.

(B) *Importation property.* A1, A2, and A3, are importation properties for the reasons set forth in paragraph (i)(B) of this *Example 1.*

(C) *Loss importation transaction.* Immediately after the distribution, USP's aggregate basis in the importation properties, A1, A2, and A3, would, but for section 334(b)(1)(B) and this section, be $300 ($40 + $120 + $140). However, the properties' aggregate value would also be $300 ($50 + $230 + $20). Therefore, the importation properties' aggregate basis would not exceed their aggregate value and the distribution is not a loss importation transaction. See paragraph (b)(3)(iii)(A) of this section and § 1.362–3(c)(3).

(D) *Basis of importation property not distributed in loss importation transaction.* Because the importation properties, A1, A2, and A3, were not distributed in a loss importation transaction, the basis of each of the importation properties is determined under the generally applicable basis rules. Accordingly, immediately after the distribution, USP's basis in A1 is $40, USP's basis in A2 is $120, and USP's basis in A3 is $140, the adjusted bases that FC had in the properties immediately before the distribution. See section 334(b)(1).

(v) *CFC stock as importation property distributed in loss importation transaction.* (A) *Facts.* USP owns the sole outstanding share of FC stock. FC owns the sole outstanding share of CFC1 stock (basis $80, value $100) and the sole outstanding share of CFC2 stock (basis $100, value $5). On Date 1, FC distributes its shares of CFC1 and CFC2 stock to USP in a complete liquidation that qualifies under section 332.

(B) *Importation property.* No special rule applies to the treatment of property that is the stock of a CFC. Thus, if FC had sold either the CFC1 share or the CFC2 share immediately before the transaction, no gain or loss recognized on the sale would have been taken into account in determining a federal income tax liability. Further, if USP had sold either the CFC1 share or the CFC2 share immediately after the transaction, USP would take into account any gain or loss recognized on the sale in determining its federal income tax liability. Thus, the CFC1 share and the CFC2 share are importation property. See paragraph (b)(3)(iii)(A) of this section and § 1.362–3(c)(2).

(C) *Loss importation transaction.* Immediately after the distribution, USP's aggregate basis in importation property (the CFC1 share and the CFC2 share) would, but for section 334(b)(1)(B) and this section, be $180 ($80 + $100) and the shares' aggregate value is $105 ($100 + $5). Therefore, the importation property's aggregate basis would exceed their aggregate value and the distribution is a loss importation transaction. See paragraph (b)(3)(iii)(A) of this section and § 1.362–3(c)(3).

(D) *Basis of importation property distributed in loss importation transaction.* Because the importation property (the CFC1 share and the CFC2 share) was transferred in a loss importation transaction, USP's basis in each of the shares received is equal to its value immediately after FC distributes the shares. Accordingly, USP's basis in the CFC1 share is $100 and USP's basis in the CFC2 share is $5.

Example 2. Multiple step liquidation. (i) *Facts.* USP owns the sole outstanding share of FC stock. On January 1 of year 1, FC adopts a plan of liquidation. FC makes the following distributions to USP in a transaction that qualifies as a complete liquidation under section 332. In year 1, FC distributes A1 and, immediately before the distribution, FC's basis in A1 is $100 and A1's value is $120. In Year 2, FC distributes A2, and, immediately before the distribution, FC's basis in A2 is $100 and A2's value is $120. In year 3, in its final liquidating distribution, FC distributes A3 and, immediately before the distribution, FC's basis in A3 is $100 and A3's value is $120. As of the time of the final distribution, USP had depreciated the bases of A1 and A2 to $90 and $95, respectively; the value of A1 had appreciated to $160; and, the value of A2 has declined to $0.

(ii) *Importation property.* If FC had sold either A1, A2, or A3 immediately before it was distributed, no gain or loss recognized on the sale would have been taken into account in determining a federal income tax liability. Further, if USP had sold either A1, A2, or A3 immediately after it was distributed, USP would take into account any gain or loss recognized on the sale in determining its federal income tax liability. Therefore, A1, A2, and A3 are all importation properties. See paragraph (b)(3)(iii)(A) of this section and § 1.362–3(c)(2).

(iii) *Loss importation transaction.* Immediately after it was distributed, USP's basis in each of the importation properties, A1, A2, and A3, would, but for section 334(b)(1)(B) and this section, have been $100. Further, immediately after each such property was distributed, its value was $120. Thus, the properties' aggregate basis, $300, would not have exceeded the properties' aggregate value, $360. Accordingly, the distribution is not a loss importation transaction irrespective of the fact that, when the liquidation was completed, the properties' aggregate basis was $285 and the properties' aggregate value was $280. See paragraph (b)(3)(iii)(B) of this section and § 1.362–3(c)(3).

(iv) *Basis of importation property not distributed in loss importation transaction.* Because the importation properties, A1, A2, and A3, were not distributed in a loss importation transaction, the basis of each of the importation properties is determined under the generally applicable basis rules. Accordingly, USP takes each of the properties with a basis of $100 and, immediately after the final distribution, has

an adjusted basis of $90 in A1 (USP's $100 basis less the $10 depreciation), $95 in A2 (USP's $100 basis less the $5 depreciation), and $100 in A3. See section 334(b).

(c) *Applicability date.* This section applies with respect to liquidations occurring on or after March 28, 2016, and also with respect to liquidations occurring before such date as a result of an entity classification election under § 301.7701–3 of this chapter filed on or after March 28, 2016, unless such liquidation is pursuant to a binding agreement that was in effect prior to March 28, 2016 and at all times thereafter. In addition, taxpayers may apply this section to any section 332 liquidation occurring after October 22, 2004.

■ **Par. 6.** Section 1.337–1 is added to read as follows:

§ 1.337–1 Nonrecognition for property distributed to parent in complete liquidation of subsidiary.

(a) *General rule.* If sections 332(a) and 337 are applicable with respect to the receipt of a subsidiary's property in complete liquidation, no gain or loss is recognized to the liquidating subsidiary with respect to such property (including property distributed with respect to indebtedness, see section 337(b)(1) and § 1.332–7), except as provided in section 337(b)(2) (distributions to certain tax-exempt distributees), section 367(e)(2) (distributions to foreign corporations), and section 897(d) (distributions of U.S. real property interests by foreign corporations).

(b) *Aplicability date.* This section applies to any taxable year beginning on or after March 28, 2016.

■ **Par. 7.** Section 1.351–1 is amended by:

■ 1. Adding headings for paragraphs (a) and (a)(1) and revising the first sentence of paragraph (a)(1) introductory text.

■ 2. Adding a sentence after the fifth sentence in paragraph (a)(1) introductory text and removing the phrase ''For purposes of this section'' at the end of paragraph (a)(1) introductory text and adding in its place the phrase ''In addition, for purposes of this section''.

■ 3. Revising paragraphs (a)(1)(i) and (ii).

■ 4. Removing the undesignated paragraph immediately following paragraph (a)(1)(ii).

■ 5. Adding a heading for paragraph (a)(2).

■ 6. Adding a heading for paragraph (b) and revising paragraph (b)(1).

■ 7. Adding a heading for paragraph (b)(2).

■ 8. Adding paragraph (d).

The additions and revisions read as follows:

§ 1.351–1 Transfer to corporation controlled by transferor.

(a) *In general*—(1) *Nonrecognition of gain or loss.* Section 351(a) provides, in general, for the nonrecognition of gain or loss upon the transfer by one or more persons of property to a corporation solely in exchange for stock of such corporation if, immediately after the exchange, such person or persons are in control of the corporation to which the property was transferred. * * * For purposes of this section, stock rights and stock warrants are not included in the term *stock.* * * *

(i) Stock will not be treated as issued for property if it is issued for services rendered or to be rendered to or for the benefit of the issuing corporation; and

(ii) Stock will not be treated as issued for property if it is issued for property which is of relatively small value in comparison to the value of the stock already owned (or to be received for services) by the person who transferred such property and the primary purpose of the transfer is to qualify under this section the exchanges of property by other persons transferring property.

(2) *Application.* * * *

* * * * *

(b) *Multiple transferors*—(1) *Disproportionate transfers.* When property is transferred to a corporation by two or more persons in exchange for stock, as described in paragraph (a) of this section, and the stock received is disproportionate to the transferor's prior interest in such property, the entire transaction will be given tax effect in accordance with its true nature, and the transaction may be treated as if the stock had first been received in proportion and then some of such stock had been used to make gifts (section 2501 and following), to pay compensation (sections 61(a)(1) and 83(a)), or to satisfy obligations of the transferor of any kind.

(2) *Application.* * * *

* * * * *

(d) *Applicability date.* Paragraphs (a)(1) and (b)(1) of this section apply to transfers after October 2, 1989, for tax years ending after such date, except as specified in section 7203(c)(2) and (3) of Public Law 101–239.

■ **Par. 8.** Section 1.351–3 is amended by revising paragraphs (a)(3) and (b)(3), and adding a sentence at the end of paragraph (f) to read as follows:

§ 1.351–3 Records to be kept and information to be filed.

(a) * * *

(3) The fair market value and basis of the property transferred by such transferor in the exchange, determined immediately before the transfer and aggregated as follows:

(i) Importation property transferred in a loss importation transaction, as defined in § 1.362–3(c)(2) and (3), respectively;

(ii) Loss duplication property as defined in § 1.362–4(g)(1);

(iii) Property with respect to which any gain or loss was recognized on the transfer (without regard to whether such property is also identified in paragraph (a)(3)(i) or (ii) of this section); and

(iv) Property not described in paragraph (a)(3)(i), (ii), or (iii) of this section.

* * * * *

(b) * * *

(3) The fair market value and basis of property received in the exchange, determined immediately before the transfer and aggregated as follows:

(i) Importation property transferred in a loss importation transaction, as defined in § 1.362–3(c)(2) and (3), respectively;

(ii) Loss duplication property as defined in § 1.362–4(g)(1);

(iii) Property with respect to which any gain or loss was recognized on the transfer (without regard to whether such property is also identified in paragraph (b)(3)(ii) of this section);

(iv) Property not described in paragraph (b)(3)(i), (ii), or (iii) of this section; and

* * * * *

(f) *Effective/applicability date.* * * * Paragraphs (a)(3) and (b)(3) of this section apply with respect to exchanges under section 351 occurring on or after March 28, 2016, and also with respect to exchanges under section 351 occurring before such date as a result of an entity classification election under § 301.7701–3 of this chapter filed on or after March 28, 2016, unless such exchange is pursuant to a binding agreement that was in effect prior to March 28, 2016 and at all times thereafter.

■ **Par. 9.** Section 1.358–6 is amended by adding a sentence at the end of paragraph (a), revising paragraphs (c)(4) introductory text, (e), and the first sentence of paragraph (f)(3), and adding paragraph (f)(4) to read as follows:

§ 1.358–6 Stock basis in certain triangular reorganizations.

(a) *Scope.* * * * See also sections 362(e)(1) and 362(e)(2) for further adjustments to basis that may be necessary under either or both of those sections.

* * * * *

(c) * * *

(4) *Examples.* The rules of this paragraph (c) are illustrated by the following examples. For purposes of these examples, P, S, and T are domestic corporations, the property transferred is not importation property within the meaning of § 1.362–3(c)(2) or loss duplication property within the meaning of § 1.362–4(g)(1), P and S do not file consolidated returns, P owns all of the shares of the only class of S stock, the P stock exchanged in the transaction satisfies the requirements of the applicable triangular reorganization provisions, and the facts set forth the only corporate activity.

* * * * *

(e) *Cross-references*—(1) *Triangular reorganizations involving members of a consolidated group.* For rules relating to stock basis adjustments made as a result of a triangular reorganization in which P and S, or P and T, as applicable, are, or become, members of a consolidated group, see § 1.1502–30. However, if a transaction is a group structure change, stock basis adjustments are determined under § 1.1502–31 and not under § 1.1502–30, even if the transaction also qualifies as a reorganization otherwise subject to § 1.1502–30.

(2) *Triangular reorganizations involving certain foreign corporations.* For rules relating to stock basis adjustments made as a result of triangular reorganizations involving certain foreign corporations, see §§ 1.367(b)–4(b), 1.367(b)–10, and 1.367(b)–13.

(f) * * *

(3) *Triangular G reorganization and special rule for triangular reorganizations involving members of a consolidated group.* Paragraph (e)(1) of this section shall apply to triangular reorganizations occurring on or after September 17, 2008. * * *

(4) *Triangular reorganizations involving importation property acquired in loss importation transaction or loss duplication transaction; triangular reorganizations involving certain foreign corporations.* Paragraphs (a) and (e)(2) of this section apply to triangular reorganizations occurring after October 22, 2004 unless effected to a binding agreement that was in effect prior to that date and at all times thereafter.

■ **Par. 10.** Section 1.362–3 is added to read as follows:

§ 1.362–3 Basis of importation property acquired in loss importation transaction.

(a) *Purpose.* The purpose of section 362(e)(1) and this section is to modify the application of section 362(a) (section 351 transfers, contributions to capital, or paid-in surplus) and section 362(b) (reorganizations) to prevent a corporation (Acquiring) from importing a net built-in loss in a transaction described in either section. See paragraph (c) of this section for definitions of terms used in this section.

(b) *Basis determinations under this section*—(1) *Basis of importation property received in loss importation transaction.* Notwithstanding the general rules of section 362(a) and (b), Acquiring's basis in importation property (as defined in paragraph (c)(2) of this section) acquired in a loss importation transaction (as defined in paragraph (c)(3) of this section) is equal to the value of the property immediately after the transaction.

(2) *Adjustment to basis of subsidiary stock in triangular reorganizations.* If a corporation (P) computes its basis in stock of a subsidiary (whether S or T) under § 1.358–6 (stock basis in certain triangular reorganizations), P's basis in property treated as acquired by P in § 1.358–6(c) is determined under section 362(e)(1) and this section to the extent such property, if actually acquired by P, would be importation property acquired in a loss importation transaction. See § 1.358–6(c)(1)(i)(A), (c)(2)(ii)(B), and (c)(3)(i). The subsidiary's basis in the property actually acquired in the transaction is determined under applicable law (including this section), without regard to the amount of any adjustment to P's basis in the subsidiary's stock. Thus, the basis of the property in S's or T's hands may differ from the amount of the adjustment to P's basis in its stock of S or T.

(3) *Acquiring's basis in other property transferred.* In general, Acquiring's basis in property received in a section 362 transaction (as defined in paragraph (c)(1) of this section) that is not determined under section 362(e)(1) and this section is determined under section 362(a) or section 362(b). However, if the transaction is described in section 362(a) (without regard to whether it is also described in any other section), further adjustment may be required under section 362(e)(2). See § 1.362–4.

(4) *Other effects of basis determination under this section*—(i) *Determination by reference to transferor's basis.* A determination of basis under this section is a determination by reference to the transferor's basis, including for purposes of sections 1223(2) and 7701(a)(43). However, solely for purposes of applying section 755, a determination of basis under this section is treated as a determination not by reference to the transferor's basis.

(ii) *Not tax-exempt income or noncapital, nondeductible expense.* The application of this section does not give rise to an item treated as tax-exempt income under § 1.1502–32(b)(2)(ii) or as a noncapital, nondeductible expense under § 1.1502–32(b)(2)(iii).

(iii) *No effect on earnings and profits.* Any determination of basis under this section does not reduce or otherwise affect the calculation of the all earnings and profits amount provided in § 1.367(b)–2(d).

(c) *Definitions.* For purposes of this section, the following definitions apply:

(1) *Section 362 transaction.* The term *section 362 transaction* means any transaction described in section 362(a) or in section 362(b).

(2) *Importation property*—(i) *General rule.* The term *importation property* means any property (including separate portions determined under paragraph (d)(4) of this section and separate portions of property tentatively divided under paragraph (e)(2) of this section) with respect to which—

(A) Any gain or loss that would be recognized on its sale by the transferor immediately before the transaction (the transferor's hypothetical sale) would not be subject to tax imposed under any provision of subtitle A of the Internal Revenue Code (federal income tax) (taking into account the provisions of paragraph (d) of this section); and

(B) Any gain or loss that would be recognized on its sale by Acquiring immediately after the transaction (Acquiring's hypothetical sale) would be subject to federal income tax (taking into account the provisions of paragraph (d) of this section).

(ii) *Special rules for applying this paragraph (c)(2).* See paragraph (d) of this section for rules for determining whether gain or loss on a hypothetical sale would be taken into account in determining a federal income tax liability and paragraph (e) of this section for rules applicable when more than one person would take such gain or loss into account.

(3) *Loss importation transaction.* The term *loss importation transaction* means any section 362 transaction in which Acquiring's aggregate basis in all importation property received from all transferors in the transaction would exceed the aggregate value of such property immediately after the transaction. For this purpose, Acquiring's basis in property received is determined without regard to this section or section 362(e)(2).

(4) *Value*—(i) *General rule.* The term *value* means fair market value.

(ii) *Special rule for transfers of partnership interests.* Notwithstanding the general rule in paragraph (c)(4)(i) of this section, when referring to a partnership interest, for purposes of this

section, the term *value* means the sum of the cash that Acquiring would receive for the interest, assuming an exchange between a willing buyer and a willing seller (neither being under any compulsion to buy or sell and both having reasonable knowledge of relevant facts), increased by any § 1.752–1 liabilities (as defined in § 1.752–1(a)(4)) of the partnership allocated to Acquiring with regard to such transferred interest under section 752 immediately after the transfer to Acquiring. If a partnership has elected under section 754, or if section 743(b) would require a downward basis adjustment to the partnership property, the partnership must apply the rules of § 1.743–1 to determine the amount of the basis adjustment to the partnership property.

(d) *Rules for determining whether gain or loss would be taken into account in determining a federal income tax liability*—(1) *General rule.* In general, any gain or loss that would be recognized on a hypothetical sale described in paragraph (c)(2) of this section is considered to be subject to federal income tax if, taking into account all relevant facts and circumstances, such gain or loss would affect or be taken into account in determining the federal income tax liability of the transferor or Acquiring, respectively. This determination is made without regard to whether such person has or would have any actual federal income tax liability for the taxable year of the transaction.

(2) *Look-through rule in the case of certain pass-through entities.* Notwithstanding the general rule in paragraph (d)(1) of this section, the determination of whether any gain or loss on a hypothetical sale would be treated as subject to federal income tax is made by reference to the person that would be required to include such gain or loss in its taxable income if the hypothetical seller is—

(i) A trust treated as owned by its grantors or others (see section 671);

(ii) A partnership (see section 701); or

(iii) An S corporation (see sections 1363 and 1366).

(3) *Controlled foreign corporation (CFC), passive foreign investment company (PFIC).* For purposes of this section, gain or loss that would be recognized by a CFC (as defined in section 957(a)) or a PFIC (as defined in section 1297(a)) is not deemed taken into account in determining a federal income tax liability solely because it could affect an inclusion under section 951(a) or section 1293(a).

(4) *Special rule for debt-financed property subject to section 512.* If property is debt-financed property (as defined in section 514(b)) owned by an organization subject to the unrelated business income tax described in section 511(a)(2) and, as a result, a portion of any gain or loss on a sale of the property would be included in unrelated taxable business income (UBTI) under section 512, such property is treated as divided into separate portions in proportion to the amount of such gain or loss that would be includible in UBTI. The rules of paragraph (e) of this section apply to determine the characterization of such portions (as includible in the determination of a federal income tax liability or not), and the tax treatment and consequences of the transaction in which such portions are transferred.

(5) *Look-through treatment in the case of certain avoidance transactions*—(i) *Application of this paragraph (d)(5).* This paragraph (d)(5) applies if—

(A) The transferor is a domestic entity that is a trust (other than a trust described in paragraph (d)(2)(i) of this section), estate, regulated investment company (as defined in section 851(a)), a real estate investment trust (as defined in section 856(a)), or a cooperative (as described in section 1381); and

(B) The transferor transfers, directly or indirectly, property that was transferred to or acquired by it as part of a plan (whether of transferor, Acquiring, or any other person) to avoid the application of section 362(e)(1) and this section to a section 362 transaction.

(ii) *Effect of application of this paragraph (d)(5).* Notwithstanding paragraph (d)(1) of this section, if a transferor is described in both paragraphs (d)(5)(i)(A) and (B) of this section—

(A) The transferor is treated as though it distributes the proceeds of the hypothetical sale (which, for this purpose, are presumed to be an amount greater than zero);

(B) To the fullest extent possible under the transferor's organizing instrument, the deemed distribution is treated as made to a distributee or distributees that would not take distributions from the transferor into account in determining a federal income tax liability; and

(C) The determination of whether the gain or loss on the hypothetical sale is treated as subject to federal income tax is made by reference to the deemed distributee or distributees.

(iii) *Tiered entities.* If a deemed distributee is an entity described in paragraph (d)(5)(i)(A) of this section, the determination of whether gain or loss on the hypothetical sale is taken into account in determining a federal income tax liability is made by treating the deemed distributee, and any successive such deemed distributees, as a transferor and applying the rules in paragraphs (d)(5)(i) and (ii) of this section to its deemed distribution (and to all successive deemed distributions), until no deemed distributee or successive deemed distributee is an entity described in paragraph (d)(5)(i)(A) of this section.

(e) *Special rules for gain or loss that would be taken into account by multiple persons*—(1) *In general.* If gain or loss from a disposition of property would be includible in income by more than one person, the property is treated as tentatively divided into separate portions in proportion to the amount of gain or loss recognized with respect to the property that would be allocated to each such person. If an entity's organizing instrument specially allocates gain and loss, the tentative division of property under this paragraph (e) must reflect the manner in which gain or loss on the disposition of such property would be allocated under the terms of the organizing instrument and any applicable rules of law, taking into account the net gain or loss actually recognized by the entity in that tax year.

(2) *Application of section.* The rules of this section apply independently to each tentatively divided portion to determine if the portion is importation property. Each tentatively divided portion that is determined to be importation property is included with all other importation property in the determination of whether the transaction is a loss importation transaction.

(3) *Acquiring's basis in property tentatively divided into separate portions.* Immediately after the application of section 362(e)(1) and this section and before the application of section 362(e)(2), each property treated as tentatively divided into separate portions for purposes of applying section 362(e)(1) and this section ceases to be treated as tentatively divided and Acquiring has a single, undivided basis in such property that is equal to the sum of—

(i) The value of each tentatively divided portion that is importation property, if the transaction is a loss importation transaction; and

(ii) Acquiring's basis in each tentatively divided portion that is not importation property received in a loss importation transaction, as determined under section 362(a) or section 362(b), as applicable, and without regard to any potential application of section 362(e)(2).

(f) *Examples.* The examples in this paragraph (f) illustrate the application of section 362(e)(1) and the provisions of this section. Unless otherwise indicated, the examples use the following nomenclature and assumptions: A and B are U.S. citizens. DC, DC1, and P are domestic corporations that have not elected to be S corporations within the meaning of section 1361(a)(1) and that are not members of a consolidated group. F is a foreign individual. FP is a foreign partnership. FC, FC1, and FC2 are foreign corporations. Unless the facts indicate otherwise, the foreign individuals, corporations, and partnerships are not engaged in a U.S. trade or business, have no U.S. real property interests, and have no other relationships, activities, or interests that would cause them, their shareholders, their partners, or their property to be subject to federal income tax. There is no applicable income tax treaty, all persons' tax years are calendar years, and all persons and transactions are unrelated unless the facts indicate otherwise.

Example 1. Basic application of section. (i) *Section 351 transfer of importation property in a loss importation transaction.* (A) *Facts.* FC owns three assets, A1 (basis $40, value $150), A2 (basis $120, value $30), and A3 (basis $140, value $20). On Date 1, FC transfers A1, A2, and A3 to DC in a transaction to which section 351 applies.

(B) *Importation property.* If FC had sold A1, A2, or A3 immediately before the transaction, no gain or loss recognized on the sale would have been taken into account in determining a federal income tax liability. Further, if DC had sold A1, A2, or A3 immediately after the transaction, DC would take into account any gain or loss recognized on the sale in determining its federal income tax liability. Therefore, A1, A2, and A3 are all importation properties. See paragraph (c)(2) of this section.

(C) *Loss importation transaction.* FC's transfer of A1, A2, and A3 is a section 362 transaction. Furthermore, but for section 362(e)(1) and this section and section 362(e)(2), DC's aggregate basis in the importation properties, A1, A2, and A3, would be $300 ($40 + $120 + $140) under section 362(a) and the properties' aggregate value would be $200 ($150 + $30 + $20). Therefore, the importation properties' aggregate basis would exceed their aggregate value and the transaction is a loss importation transaction. See paragraph (c)(3) of this section.

(D) *Application of section 362(e)(1) and this section to importation property received in loss importation transaction.* Because the importation properties, A1, A2, and A3, were transferred in a loss importation transaction, paragraph (b)(1) of this section applies and DC's basis in A1, A2, and A3 will each be equal to the property's value ($150, $30, and $20, respectively) immediately after the transfer.

(E) *Basis of property received in transaction.* Following the application of section 362(e)(1) and this section, the provisions of section 362(e)(2) must be taken into account because the transfer is a section 362(a) transaction. Taking into account the application of section 362(e)(1) and this section, DC's aggregate basis in the transferred properties would not exceed their aggregate value immediately after the transfer. Therefore, FC does not have a net built-in loss, FC's transfer is not a loss duplication transaction, and section 362(e)(2) does not apply to this transaction. DC's bases in A1, A2, and A3, as determined under paragraph (i)(D) of this *Example 1,* are $150, $30, and $20, respectively. Under section 358(a), FC receives the DC stock with a basis of $300 (the sum of FC's bases in A1, A2, and A3 immediately before the exchange).

(ii) *Reorganization.* The facts are the same as in paragraph (i)(A) of this *Example 1* except that, instead of transferring property to DC in a section 351 exchange, FC merges with and into DC in a transaction described in section 368(a)(1)(A). The analysis and results are the same as set forth in paragraphs (i)(B), (C), and (D) of this *Example 1.* However, the analysis in paragraph (i)(E) of this *Example 1* does not apply to these facts because the transaction is not subject to 362(e)(2) and § 1.362–4. Under section 358(a), FC's shareholders will take the DC stock with a basis determined by reference to their FC stock basis.

(iii) *FC's property used in U.S. trade or business.* (A) *Facts.* The facts are the same as in paragraph (i)(A) of this *Example 1,* except that FC is engaged in a U.S. trade or business and uses all the properties in that U.S. trade or business. In this case, none of the properties would be importation property because FC would take any gain or loss on the disposition of the properties into account in determining its federal income tax liability. Accordingly, this section does not apply to the transaction.

(B) *Basis of property received in transaction.* Following the application of section 362(e)(1) and this section, the provisions of section 362(e)(2) must be taken into account because the transfer is a section 362(a) transaction. Taking into account the application of section 362(e)(1) and this section but without taking into account the provisions of section 362(e)(2), DC's aggregate basis in the transferred properties would be $300 ($40 + $120 + $140) under section 362(a) and the properties' aggregate value immediately after the transfer would be $200 ($150 + $30 + $20). Therefore, FC has a net built-in loss and FC's transfer of A1, A2, and A3 is a loss duplication transaction. Accordingly, under the general rule of section 362(e)(2), FC's $100 net built-in loss ($300 aggregate basis over $200 aggregate value) would be allocated proportionately (by the amount of built-in loss in each property) to reduce DC's basis in the loss properties, A2 and A3. See § 1.362–4. As a result, DC's basis in A2 would be $77.14 ($120 basis under section 362(a) reduced by $42.86, A2's proportionate share of FC's net built-in loss, computed as $90/$210 × $100) and DC's basis in A3 would be $82.86 ($140 basis under section 362(a) reduced by $57.14, A3's proportionate share of FC's net built-in loss, computed as $120/$210 x $100). However, if FC and DC were to elect under section 362(e)(2)(C) to apply the $100 basis reduction to FC's basis in the DC stock received in the transaction, DC's bases in A2 and A3 would remain their section 362(a) bases of $120 and $140, respectively. Under section 362(a), DC's basis in A1 is $40 (irrespective of whether the section 362(e)(2)(C) election is made). If FC and DC do not make a section 362(e)(2)(C) election, FC's basis in the DC stock received in the exchange will be $300; if FC and DC do make the election, FC's basis in the DC stock will be $200 ($300 − $100 net built-in loss). See § 1.362–4(b).

Example 2. Multiple transferors. (i) *Facts.* The facts are the same as in paragraph (i)(A) of *Example 1* of this paragraph (f), except that FC only owns A1 (basis $40, value $150) and A2 (basis $120, value $30) and F owns A3 (basis $140, value $20). On Date 1, FC transfers A1 and A2, and F transfers A3, to DC in a single transaction described in section 351.

(ii) *Importation property.* A1 and A2 are importation properties for the reasons set forth in paragraph (i)(B) of *Example 1* of this paragraph (f). A3 is also an importation property because, if F had sold A3 immediately before the transaction, no gain or loss recognized on the sale would have been taken into account in determining a federal income tax liability, and, further, if DC had sold A3 immediately after the transaction, DC would take into account any gain or loss recognized on the sale in determining its federal income tax liability.

(iii) *Loss importation transaction.* The transfers by FC and F are a section 362 transaction. The transaction is a loss importation transaction for the reasons set forth in paragraph (i)(C) of *Example 1* of this paragraph (f) (notwithstanding that one of the transferors, FC, did not transfer a net built-in loss). See paragraph (c)(3) of this section.

(iv) *Application of section 362(e)(1) and this section to importation property received in loss importation transaction.* Because the importation properties, A1, A2, and A3, were transferred in a loss importation transaction, paragraph (b)(1) of this section applies and DC's basis in A1, A2, and A3 will each be equal to the property's value ($150, $30, and $20, respectively) immediately after the transfer.

(v) *Basis of property received in transaction.* Following the application of section 362(e)(1) and this section, the provisions of section 362(e)(2) must be taken into account because the transfer is a section 362(a) transaction. The application of section 362(e)(2) is determined separately for each transferor. See § 1.362–4(b). Taking into account the application of section 362(e)(1) and this section, neither DC's aggregate basis in FC's properties nor DC's basis in F's property would exceed the properties' respective values immediately after the transaction. Therefore neither FC nor F has a net built-in loss, neither transfer is a loss duplication transaction, and section 362(e)(2) does not apply to either transfer. DC's bases in A1, A2, and A3, as determined under paragraph (iv) of this *Example 2,* are $150, $30, and $20, respectively. Under section

358(a), FC's basis in the DC stock received is $160 ($40 + $120) and F's basis in the DC stock received in the exchange is $140.

Example 3. Transfer of importation and non-importation property. (i) *Facts.* As in paragraph (i) of *Example 2,* FC owns A1 (basis $40, value $150) and A2 (basis $120, value $30), and F owns A3 (basis $140, value $20). In addition, A2 is a U.S. real property interest as defined in section 897(c)(1). On Date 1, FC transfers A1 and A2, and F transfers A3, to DC in a single transaction described in section 351.

(ii) *Importation property.* A1 and A3 are importation properties for the reasons set forth in paragraph (i)(B) of *Example 1* and paragraph (ii) of *Example 2* of this paragraph (f), respectively. However, A2 is not importation property because, if FC had sold A2 immediately before the transaction, FC would take into account any gain or loss recognized on the sale in determining its federal income tax liability.

(iii) *Loss importation transaction.* FC's and F's transfer is a section 362 transaction. Furthermore, but for section 362(e)(1) and this section and section 362(e)(2), DC's aggregate basis in the importation properties, A1 and A3, would be $180 ($40 + $140) and the properties' aggregate value would be $170 ($150 + $20) immediately after the transaction. Therefore, the importation properties' aggregate basis would exceed their aggregate value immediately after the transaction, and the transfer is a loss importation transaction.

(iv) *Application of section 362(e)(1) and this section to importation property received in loss importation transaction.* Because the importation properties, A1 and A3, were transferred in a loss importation transaction, paragraph (b)(1) of this section applies and DC's basis in A1 and in A3 will each be equal to the property's value ($150 and $20, respectively) immediately after the transfer.

(v) *Basis of property received in transaction.* Following the application of section 362(e)(1) and this section, the provisions of section 362(e)(2) must be taken into account because the transfer is a section 362(a) transaction. The application of section 362(e)(2) is determined separately for each transferor. See § 1.362–4(b).

(A) *FC's transfer.* Taking into account the application of section 362(e)(1) and this section but without taking into account the provisions of section 362(e)(2), DC would have an aggregate basis of $270 in the transferred properties ($150 in A1, as determined under paragraph (iv) of this *Example 3,* plus $120 in A2, determined under section 362(a)), and the properties would have an aggregate value of $180 ($150 + $30) immediately after the transfer. Therefore, FC has a net built-in loss and FC's transfer of A1 and A2 is a loss duplication transaction. Accordingly, under the general rule of section 362(e)(2), FC's $90 net built-in loss ($270 aggregate basis to DC over $180 aggregate value) would be allocated proportionately to reduce DC's basis in the loss property transferred by FC. As a result, FC's entire net built-in loss would be allocated to A2, the only loss property transferred by FC, and DC's basis in A2 would be $30 ($120 basis under section 362(a) reduced by $90 net built-in loss). However, if FC and DC were to elect under section 362(e)(2)(C) to apply the $90 basis reduction to FC's basis in the DC stock received in the transaction, DC's basis in A2 would remain its section 362(a) basis of $120. DC's basis in A1 is $150 as determined under paragraph (iv) of this *Example 3* (irrespective of whether the section 362(e)(2)(C) election is made). If FC and DC do not make a section 362(e)(2)(C) election, FC's basis in the DC stock received in the exchange will be $160; if FC and DC do make the election, FC's basis in the DC stock will be $70 ($160 − $90 net built-in loss). See § 1.362–4.

(B) *F's transfer of A3.* Taking into account the application of section 362(e)(1) and this section, DC's basis in A3, the property transferred by F, would not exceed its value immediately after the transfer. Therefore, F does not have a built-in loss, F's transfer is not a loss duplication transaction, and section 362(e)(2) does not apply to F's transfer. DC's basis in A3, as determined under paragraph (iv) of this *Example 3,* is $20. Under section 358(a), F receives the DC stock with a basis of $140.

Example 4. Multiple transferors of non-importation properties. (i) *Facts.* DC1 owns A1 (basis $40, value $150). In addition, as in *Example 3* of this paragraph (f), FC owns A2 (basis $120, value $30), a U.S. real property interest as defined in section 897(c)(1), and F owns A3 (basis $140, value $20). On Date 1, DC1 transfers A1, FC transfers A2, and F transfers A3, to DC in a single transaction described in section 351.

(ii) *Importation property.* A2 is not importation property and A3 is importation property for the reasons set forth in paragraph (ii) of *Example 3* and paragraph (i)(B) of *Example 1* of this paragraph (f), respectively. A1 is not importation property because, if DC1 had sold A2 immediately before the transaction, DC1 would take into account any gain or loss recognized on the sale in determining its federal income tax liability.

(iii) *Loss importation transaction.* The transfer of A1, A2, and A3 is a section 362 transaction. Furthermore, but for section 362(e)(1) and this section and section 362(e)(2), DC's basis in importation property, A3, would be $140 and the value of the property would be $20 immediately after the transaction. Therefore, the importation property's basis would exceed value and the transfer is a loss importation transaction.

(iv) *Application of section 362(e)(1) and this section to importation property received in loss importation transaction.* Because the importation property, A3, was transferred in a loss importation transaction, section 362(e)(1) and paragraph (b)(1) of this section apply and DC's basis in A3 will be equal to A3's $20 value immediately after the transfer.

(v) *Basis of property received in transaction.* Following the application of section 362(e)(1) and this section, the provisions of section 362(e)(2) must be taken into account because the transfer is a section 362(a) transaction. The application of section 362(e)(2) is determined separately for each transferor. See § 1.362–4.

(A) *DC1's transfer.* Taking into account the application of section 362(e)(1) and this section, DC's basis in A1 ($40 under section 362(a)) would not exceed its value immediately after the transfer. Therefore, DC1 does not have a net built-in loss, DC1's transfer is not a loss duplication transaction, and section 362(e)(2) does not apply to DC1's transfer. DC's basis in A1, determined under section 362(a), is $40. Under section 358(a), DC1 receives the DC stock with a basis of $40.

(B) *FC's transfer.* Taking into account the application of section 362(e)(1) and this section, but without taking into account the provisions of section 362(e)(2), DC would have a section 362(a) basis of $120 in A2, which would exceed A2's $30 value immediately after the transfer. Therefore, FC has a net built-in loss and FC's transfer of A2 is a loss duplication transaction. Accordingly, under the general rule of section 362(e)(2), FC's $90 net built-in loss (DC's $120 basis in A2 over A2's $30 value) would be applied to reduce DC's basis in A2, the only loss property transferred by FC. As a result, DC's basis in A2 would be $30 ($120 basis under section 362(a), reduced by the $90 net built-in loss). However, if FC and DC were to elect under section 362(e)(2)(C) to apply the $90 basis reduction to FC's basis in the DC stock received in the transaction, DC's basis in A2 would be its $120 basis determined under section 362(a). If FC and DC do not make a section 362(e)(2)(C) election, FC's basis in the DC stock received in the exchange will be $120; if FC and DC do make the election, FC's basis in the DC stock will be $30 ($120 − $90). See § 1.362–4.

(C) *F's transfer.* F's transfer of A3 is a transaction described in section 362(a). However, taking into account the application of section 362(e)(1) and this section, DC's basis in A3 ($20) would not exceed its value immediately after the transfer. Therefore, F does not have a built-in loss, F's transfer is not a loss duplication transaction, and section 362(e)(2) does not apply to F's transfer. DC's basis in A3, as determined under paragraph (iv) of this *Example 4,* is $20. Under section 358(a), F receives the DC stock with a basis of $140.

Example 5. Partnership transactions. (i) *Transfer by foreign partnership, foreign and domestic partners.* (A) *Facts.* A and F are equal partners in FP. FP owns A1 (basis $100, value $70). Under the terms of the FP partnership agreement, FP's items of income, gain, deduction, and loss are allocated equally between A and F. Section 704(c) does not apply with respect to the partnership property. FP transfers A1 to DC in a transfer to which section 351 applies. No election is made under section 362(e)(2)(C).

(B) *Importation property.* If FP had sold A1 immediately before the transaction, any gain or loss recognized on the sale would be allocated to and includible by A and F equally under the partnership agreement. Thus, under paragraph (d)(2) of this section, A1 is treated as tentatively divided into two equal portions, one treated as owned by A and one treated as owned by F. If FP had sold A1 immediately before the transaction, any gain or loss recognized on the portion treated as owned by A would have been taken into account in determining a federal income tax

liability (A's); thus A's tentatively divided portion of A1 is not importation property. However, no gain or loss recognized on the tentatively divided portion treated as owned by F would have been taken into account in determining a federal income tax liability. Further, if DC had sold A1 immediately after the transaction, any gain or loss recognized on the sale would have been taken into account in determining a federal income tax liability (DC's); thus, F's tentatively divided portion of A1 is importation property.

(C) *Loss importation transaction.* FP's transfer of A1 is a section 362 transaction. Furthermore, but for section 362(e)(1) and this section and section 362(e)(2), DC's basis in the importation property, F's portion of A1, would be $50 under section 362(a) and the property's value would be $35 immediately after the transaction. Therefore, the importation property's basis would exceed its value and the transfer is a loss importation transaction.

(D) *Application of section 362(e)(1) and this section to importation property received in loss importation transaction.* Because the importation property, F's tentatively divided portion of A1, was transferred in a loss importation transaction, section 362(e)(1) and paragraph (b)(1) of this section apply and DC's basis in F's portion of A1 will be equal to its $35 value.

(E) *Basis of property received in transaction.* Following the application of section 362(e)(1) and this section, the provisions of section 362(e)(2) must be taken into account because the transfer is a section 362(a) transaction. Taking into account the application of section 362(e)(1) and this section but without taking into account the provisions of section 362(e)(2), DC's aggregate basis in A1 would be $85 (the sum of the $35 basis in F's tentatively divided portion of A1, as determined under paragraph (i)(D) of this *Example 5,* and the $50 basis in A's tentatively divided portion of A1, determined under section 362(a), see paragraphs (d)(2) and (e)(3) of this section) and A1's value immediately after the transfer would be $70. Therefore, FP has a net built-in loss and FP's transfer of A1 is a loss duplication transaction. Accordingly, under the general rule of section 362(e)(2), FP's $15 net built-in loss ($85 basis over $70 value) would be allocated to reduce DC's basis in the loss asset, A1, the only loss property transferred by FP. As a result, DC's basis in A1 would be $70 ($85 basis under section 362(a) and this section, reduced by the $15 net built-in loss). Under section 358, FP's basis in the DC stock received in the exchange will be $100. See § 1.362–4.

(ii) *Transfer with election to apply section 362(e)(2)(C).* The facts are the same as in paragraph (i)(A) of this *Example 5,* except that FP and DC elect to apply section 362(e)(2)(C) to reduce FP's basis in the DC stock received in the exchange. The analysis and results are the same as in paragraphs (i)(B), (C), (D), and (E) of this *Example 5,* except that the $15 reduction to DC's basis in A1 is not made and, as a result, DC's basis in A1 remains $85, and FP's basis in the DC stock received in the exchange is reduced from $100 to $85. The $15 reduction to FP's basis in DC stock reduces A's basis in its FP interest under section 705(a)(2)(B). See § 1.362–4(e)(1).

(iii) *Transfer by domestic partnership.* The facts are the same as in paragraph (i)(A) of this *Example 5* except that FP is a domestic partnership. The analysis and results are the same as in paragraphs (i)(B), (C), (D), and (E) of this *Example 5.*

(iv) *Transfer of interest in partnership with liability.* (A) *Facts.* F and two other individuals are equal partners in FP. F's basis in its partnership interest is $247. F's share of FP's § 1.752–1 liabilities (as defined in § 1.752–1(a)(4)) is $150. F transfers his partnership interest to DC in a transaction to which section 351 applies. If DC were to sell the FP interest immediately after the transfer, DC would receive $100 in cash or other property. In addition, taking into account the rules under § 1.752–4, DC's share of FP's § 1.752–1 liabilities (as defined in § 1.752–1(a)(4)) is $145 immediately after the transfer.

(B) *Importation property.* If F had sold his partnership interest immediately before the transaction, no gain or loss recognized on the sale would have been taken into account in determining a federal income tax liability. Further, if DC had sold the partnership interest immediately after the transaction, any gain or loss recognized on the sale would have been taken into account in determining a federal income tax liability. Therefore, F's partnership interest is importation property.

(C) *Loss importation transaction.* F's transfer is a section 362 transaction. However, but for section 362(e)(1) and this section and section 362(e)(2), DC's basis in the importation property, the partnership interest, determined under section 362(a) and taking into account the rules under section 752, would be $242 (F's $247 basis reduced by F's $150 share of FP liabilities and increased by DC's $145 share of FP liabilities) and, under paragraph (c)(4)(ii) of this section, the value of the FP interest would be $245 (the sum of $100, the cash DC would receive if DC immediately sold the partnership interest, and $145, DC's share of the § 1.752–1 liabilities (as defined in § 1.752–1(a)(4)) under section 752 immediately after the transfer to DC). Therefore, the importation property's basis ($242) would not exceed its value ($245), and the transfer is not a loss importation transaction.

(D) *Basis in property received in transaction.* Following the application of section 362(e)(1) and this section, the provisions of section 362(e)(2) must be taken into account because the transfer is a section 362(a) transaction. As described in paragraph (iv)(C) of this *Example 5,* taking into account the application of section 362(e)(1) and this section, DC's basis in the partnership interest would not exceed its value. Therefore, under § 1.362–4, F does not have a net built-in loss, the transfer is not a loss duplication transaction, and section 362(e)(2) does not apply to the transfer. DC's basis in F's partnership interest is $242, determined under sections 362(a) and 752. Under section 358, taking into account the rules under section 752, F's basis in the DC stock received in the exchange is $97 ($247 reduced by F's $150 share of FP liabilities). If FP had elected under section 754, or if section 743(b) required a downward basis adjustment to the partnership property, FP would apply the rules of § 1.743–1 to determine the amount of the basis adjustment to the partnership property.

Example 6. Transactions involving tax-exempt entities. (i) *Exempt transferor.* (A) *Facts.* InsCo is a benevolent life insurance association of a purely local character exempt from federal income tax under section 501(a) because it is described in section 501(c)(12). InsCo owns shares of stock of DC1 (basis $100, value $70) for investment purposes, which are not debt-financed property (as defined in section 514). On December 31, Year 1, InsCo transfers the DC1 stock to DC in exchange for DC stock in a transaction to which section 351 applies. No election is made under section 362(e)(2)(C).

(B) *Importation property.* If InsCo had sold the DC1 stock immediately before the transaction, any gain or loss realized would be excluded from UBTI under section 512(b)(5), and thus no gain or loss recognized on the sale would have been taken into account in determining federal income tax liability. Further, if DC had sold the DC1 stock immediately after the transaction, any gain or loss recognized on the sale would have been taken into account in determining federal income tax liability. Therefore, the DC1 stock is importation property.

(C) *Loss importation transaction.* InsCo's transfer is a section 362 transaction. Furthermore, but for section 362(e)(1) and this section and section 362(e)(2), DC's basis in importation property, the DC1 stock, would be $100, and the stock's value would be $70 immediately after the transaction. Therefore, the importation property's basis would exceed its value and the transfer is a loss importation transaction.

(D) *Application of section 362(e)(1) and this section to importation property received in loss importation transaction.* Because the importation property, the DC1 stock, was transferred in a loss importation transaction, paragraph (b)(1) of this section applies and DC's basis in the stock will be equal to its $70 value.

(E) *Basis of property received in transaction.* Following the application of section 362(e)(1) and this section, the provisions of section 362(e)(2) must be taken into account because the transfer is a section 362(a) transaction. Taking into account the application of section 362(e)(1) and this section, DC's basis in the DC1 stock does not exceed its value immediately after the transaction. Therefore, InsCo does not have a net built-in loss, InsCo's transfer is not a loss duplication transaction, and section 362(e)(2) has no application to the transaction. DC's basis in the DC1 stock, as determined under paragraph (i)(D) of this *Example 6,* is $70. Under section 358, InsCo's basis in the DC stock received in the exchange will be $100.

(ii) *Transferor loses tax-exempt status.* (A) *Facts.* The facts are the same as in paragraph (i)(A) of this *Example 6* except that InsCo fails to be described in section 501(c)(12) in Year 1.

(B) *Importation property.* If InsCo had sold the DC1 stock immediately before the transaction, any gain or loss recognized on the sale would have been taken into account in determining a federal income tax liability.

Therefore, the DC1 stock is not importation property and this section does not apply to the transaction.

(C) *Basis of property received in transaction.* Following the application of section 362(e)(1) and this section, the provisions of section 362(e)(2) must be taken into account because the transfer is a section 362(a) transaction. Taking into account the application of section 362(e)(1) and this section but without taking into account the provisions of section 362(e)(2), DC would have a section 362(a) basis of $100 in the stock, which would exceed its value of $70 immediately after the transfer. Therefore, InsCo has a net built-in loss and InsCo's transfer of the DC1 stock is a loss duplication transaction. Accordingly, under the general rule of section 362(e)(2), InsCo's $30 net built-in loss ($100 basis over $70 value) would be allocated to reduce DC's basis in the loss asset, the DC1 stock, the only loss property transferred by InsCo. As a result, DC's basis in the DC1 stock would be $70 ($100 basis under section 362(a), reduced by the $30 net built-in loss). Under section 358, InsCo's basis in the DC stock received in the exchange will be $100.

(iii) *Transfer of property that is subject to unrelated business tax.* (A) *Facts.* The facts are the same as in paragraph (i)(A) of this *Example 6* except that, on December 31, Year 1, instead of the DC1 stock, InsCo transfers A1 (basis $200, value $150) to DC. A1 is real property that InsCo owned from January 1 to December 31 of Year 1. During the entirety of this period, A1's basis was $200, and in the twelve months prior to December 31, Year 1, the highest amount of outstanding principal indebtedness on A1 was $40. For purposes of the UBTI rules under section 512, A1 is debt-financed property within the meaning of section 514(b).

(B) *Importation property.* If InsCo had sold A1 immediately before the transaction, 20 percent of any gain or loss recognized on that sale (that is, $40 of acquisition indebtedness on A1 divided by A1's $200 basis in Year 1) would, under sections 512 and 514, be includible in UBTI at the end of Year 1, and 80 percent would not. Thus, under paragraph (d)(4) of this section, A1 is treated as tentatively divided into two portions, one reflecting the gain or loss that would be taken into account in determining a federal income tax liability in InsCo's hands immediately before the transfer (the 20 percent portion) and one that would not (the 80 percent portion). Further, if DC sold A1 immediately after the transfer, any gain or loss on both portions would be taken into account in determining a federal income tax liability. Accordingly, the 20 percent portion is not importation property, but the 80 percent portion is.

(C) *Loss importation transaction.* InsCo's transfer of A1 is a section 362 transaction. Furthermore, but for section 362(e)(1) and this section and section 362(e)(2), DC's basis in the importation property, the 80 percent portion of A1, would be $160 (80 percent of InsCo's $200 basis) under section 362(a) and the property's value would be $120 (80% of A1's $120 value) immediately after the transaction. Therefore, the importation property's basis would exceed its value and the transfer is a loss importation transaction.

(D) *Application of section 362(e)(1) and this section to importation property received in loss importation transaction.* Because the importation property, the 80 percent portion of A1, was transferred in a loss importation transaction, section 362(e)(1) and paragraph (b)(1) of this section apply and DC's basis in that portion of A1 will be equal to its $120 value.

(E) *Basis of property received in transaction.* Following the application of section 362(e)(1) and this section, the provisions of section 362(e)(2) must be taken into account because the transfer is a section 362(a) transaction. Taking into account the application of section 362(e)(1) and this section but without taking into account the provisions of section 362(e)(2), DC's aggregate basis in A1 would be $160 (the sum of the $120 basis in the 80 percent importation portion of A1, as determined under paragraph (iii)(D) of this *Example 6,* and the $40 basis in the 20 percent portion of A1 that is not importation property, determined under section 362(a). See paragraph (e)(3) of this section). Further, A1's value immediately after the transfer would be $150. Therefore, InsCo has a net built-in loss in A1, and InsCo's transfer of A1 is a loss duplication transaction. Accordingly, under the general rule of section 362(e)(2), InsCo's $10 net built-in loss ($160 basis over $150 value) would be allocated to reduce DC's basis in the loss asset, A1, the only loss property transferred by InsCo. As a result, DC's basis in A1 would be $150 ($160 basis under section 362(a) and this section, reduced by the $10 net built-in loss). Under section 358, InsCo's basis in the DC stock received in the exchange will be $200. See § 1.362–4.

(iv) *Transfer with election to apply section 362(e)(2)(C).* The facts are the same as in paragraph (iii)(A) of this *Example 6,* except that InsCo and DC elect to apply section 362(e)(2)(C) to reduce InsCo's basis in the DC stock received in the exchange. The analysis and results are the same as in paragraphs (iii)(B), (C), (D), and (E) of this *Example 6,* except that the $10 reduction to DC's basis in A1 is not made and, as a result, DC's basis in A1 remains $160; however, InsCo's basis in the DC stock received in the exchange is reduced from $200 to $190.

Example 7. Transactions involving CFCs. (i) *Transfer by CFC.* (A) *Facts.* FC is a CFC with 100 shares of stock outstanding. A owns 60 of the shares and F owns the remaining 40 shares. FC owns two assets, A1 (basis $70, value $100), which is used in the conduct of a U.S. trade or business, and A2 (basis $100, value $75), which is not used in the conduct of a U.S. trade or business. FC transfers both assets to DC in a transaction to which section 351 applies.

(B) *Importation property.* If FC had sold A1 immediately before the transaction, any gain or loss recognized on the sale would have been taken into account in determining a federal income tax liability (FC's). See section 882(a). Therefore, A1 is not importation property. If FC had sold A2 immediately before the transaction, FC would not take the gain or loss recognized into account in determining its federal income tax liability, but the gain or loss could be taken into account in determining a section 951 inclusion to FC's U.S. shareholders. However, under paragraph (d)(3) of this section, gain or loss is not deemed taken into account in determining a federal income tax liability solely because it could affect an inclusion under section 951(a). Further, if DC had sold A2 immediately after the transaction, any gain or loss recognized on the sale would have been taken into account in determining a federal income tax liability. Therefore, A2 is importation property.

(C) *Loss importation transaction.* FC's transfer is a section 362 transaction. Furthermore, but for section 362(e)(1) and this section and section 362(e)(2), DC's basis in the importation property, A2, would be $100 and the property's value would be $75 immediately after the transaction. Therefore, the importation property's basis would exceed its value and the transfer is a loss importation transaction.

(D) *Application of section 362(e)(1) and this section to importation property received in loss importation transaction.* Because the importation property, A2, was transferred in a loss importation transaction, paragraph (b)(1) of this section applies and DC's basis in A2 will be equal to A2's $75 value immediately after the transfer.

(E) *Basis of property received in transaction.* Following the application of section 362(e)(1) and this section, the provisions of section 362(e)(2) must be taken into account because the transfer is a section 362(a) transaction. Taking into account the application of section 362(e)(1) and this section but without taking into account the provisions of section 362(e)(2), DC would have an aggregate basis of $145 in the transferred properties ($70 in A1, determined under section 362(a), plus $75 in A2, determined under this section) and the properties would have an aggregate value of $175 ($100 + $75) immediately after the transfer. Therefore, FC does not have a net built-in loss, FC's transfer is not a loss duplication transaction, and section 362(e)(2) does not apply to the transaction. DC's basis in A1 will be $70, determined under section 362(a), and DC's basis in A2 will be $75, as determined under paragraph (i)(D) of this *Example 7.* Under the general rule in section 358(a), FC receives the DC stock with a basis of $170 ($70 attributable to A1 plus $100 attributable to A2).

(ii) *Transfer of CFC stock.* (A) *Facts.* The facts are the same as in paragraph (i)(A) of this *Example 7,* except that A transfers its 60 shares of FC stock (basis $80, value $105) and F transfers its 40 shares of FC stock (basis $100, value $70) to DC in an exchange that qualifies under section 351.

(B) *Importation property.* If A had sold its FC shares immediately before the transaction, any gain or loss recognized on the sale would have been taken into account in determining a federal income tax liability (A's). Therefore, A's FC shares are not importation property. However, if F had sold its FC shares immediately before the transaction, no gain or loss recognized on the sale would have been taken into account in determining a federal income tax liability. Further, if DC had sold F's FC shares immediately after the

transaction, any gain or loss recognized on the sale would have been taken into account in determining a federal income tax liability. Therefore, F's FC shares are importation property.

(C) *Loss importation transaction.* The transfer of the FC shares is a section 362 transaction. Furthermore, but for section 362(e)(1) and this section and section 362(e)(2), DC's aggregate basis in the importation property, F's shares of FC stock, would be $100 under section 362(a) and the shares' aggregate value would be $70. Therefore, the importation property's aggregate basis would exceed its aggregate value, and the transfer is a loss importation transaction.

(D) *Application of section 362(e)(1) and this section to importation property received in loss importation transaction.* Because the importation property, F's shares of FC stock, was transferred in a loss importation transaction, paragraph (b)(1) of this section applies and DC's aggregate basis in the shares will be equal to their $70 aggregate value immediately after the transfer.

(E) *Basis of property received in transaction.* Following the application of section 362(e)(1) and this section, the provisions of section 362(e)(2) must be taken into account because the transfer is a section 362(a) transaction. The application of section 362(e)(2) is determined separately for each transferor. See § 1.362–4(b).

(*1*) *A's transfer.* Taking into account the application of section 362(e)(1) and this section, DC's aggregate basis in the shares ($80 under section 362(a)) would not exceed the shares' value ($105) immediately after the transaction. Therefore A does not have a built-in loss, A's transfer is not a loss duplication transaction, and section 362(e)(2) does not apply to A's transfer. DC's aggregate basis in A's shares, determined under section 362(a), is $80. Under section 358(a), A receives the DC stock with a basis of $80.

(*2*) *F's transfer.* Taking into account the application of section 362(e)(1) and this section, DC's aggregate basis in the shares would not exceed their value immediately after the transaction. Therefore, F does not have a built-in loss, F's transfer is not a loss duplication transaction, and section 362(e)(2) does not apply to F's transfer. DC's aggregate basis in F's shares, as determined under paragraph (ii)(D) of this *Example 7,* is $70. Under section 358(a), F receives the DC stock with a basis of $100.

Example 8. Property subject to withholding tax. (i) *Facts.* FC owns a share of DC1 stock (basis $100, value $70) as an investment. FC receives dividends on the share that are subject to federal withholding tax of 30 percent of the amount received under section 881(a); under section 1442(a), DC1 must withhold tax on the dividends paid. FC transfers the DC1 share to DC in a transaction to which section 351 applies.

(ii) *Importation property.* Although any dividends received with respect to the DC1 stock were subject to withholding tax, if FC had sold the share of stock of DC1, no gain or loss recognized on the sale would have been taken into account in determining a federal income tax liability. See section 865(a)(2). Further, if DC had sold the share of DC1 stock immediately after the transaction, any gain or loss recognized on the sale would be taken into account in determining federal income tax liability. Therefore, the share of DC1 stock is importation property.

(iii) *Loss importation transaction.* FC's transfer is a section 362 transaction. Furthermore, but for section 362(e)(1) and this section and section 362(e)(2), DC's basis in the importation property, the share of DC1 stock, would be $100 and the share's value would be $70 immediately after the transaction. Therefore, the share's basis would exceed its value and the transfer is a loss importation transaction.

(iv) *Application of section 362(e)(1) and this section to importation property received in loss importation transaction.* Because the importation property, the DC1 share, was transferred in a loss importation transaction, paragraph (b)(1) of this section applies and DC's basis in the share will be equal to the share's $70 value.

(v) *Basis of property received in transaction.* Following the application of section 362(e)(1) and this section, the provisions of section 362(e)(2) must be taken into account because the transfer is a section 362(a) transaction. Taking into account the application of section 362(e)(1) and this section, DC's basis in the DC1 share would not exceed the share's value immediately after the transaction. Therefore, FC does not have a net built-in loss, FC's transfer is not a loss duplication transaction, and section 362(e)(2) does not apply to the transaction. DC's basis in the DC1 share, as determined under paragraph (iv) of this *Example 8,* is $70. Under section 358, FC's basis in the DC stock received in the exchange will be $100.

Example 9. Property transferred in triangular reorganization. (i) *Foreign subsidiary.* (A) *Facts.* P owns the sole outstanding share of stock of FC (basis $1), FC1 owns the sole outstanding share of FC2 (basis $100), and FC2 owns one asset, A1 (basis $100, value $20). In a forward triangular merger described in § 1.358–6(b)(2)(i), FC2 merges with and into FC, and FC1 receives shares of P stock in exchange for its FC2 stock. The forward triangular merger is a transaction described in section 368(a)(2)(D) and, therefore, in section 362(b).

(B) *Determining P's basis in its FC share.* Pursuant to § 1.358–6, for purposes of determining the adjustment to P's basis in its FC shares, P is treated as though it first received A1 in a transaction in which its basis in A1 would be determined under section 362(b) and then it transferred A1 to FC in a transaction in which P's basis in its FC stock would be determined under section 358.

(*1*) *P's deemed acquisition and transfer of A1.* If FC2 had sold A1 for its value immediately before the deemed transaction, no gain or loss recognized on the sale would have been taken into account in determining a federal income tax liability. If P had sold A1 immediately after the deemed transaction, any gain or loss recognized on the sale would have been taken into account in determining a federal income tax liability (P's). Therefore, with respect to P's deemed acquisition, A1 is importation property. Furthermore, immediately after the deemed transaction, P's basis in A1, but for section 362(e)(1) and this section and section 362(e)(2), would be $100 and A1's value is $20. Therefore, the importation property's basis would exceed its value and the transfer is a loss importation transaction. Accordingly, P's deemed basis in A1 will be equal to A1's $20 value.

(*2*) *P's FC stock basis.* As a result of P's deemed transfer of A1 to FC (and applying the principles of § 1.367(b)–13), P's basis in its FC stock is increased by its $20 deemed basis in A1. Accordingly, following the transaction, P's basis in its share of FC stock will be $21 (the sum of its original $1 basis and the $20 adjustment for the deemed transfer of A1).

(C) *FC's basis in A1.* FC's basis in A1 is determined under the rules of this section without regard to the determination of P's adjustment to its basis in FC stock. If FC2 had sold A1 for its value immediately before the transaction, no gain or loss recognized on the sale would have been taken into account in determining a federal income tax liability. However, if FC had sold A1 immediately after the transaction, no gain or loss recognized on the sale would have been taken into account in determining a federal income tax liability, so A1 is not importation property. Accordingly, this section will not apply to the transaction. Although there is a net built-in loss in A1, the transaction is not described in section 362(a), and so section 362(e)(2) and § 1.362–4 will not apply to the transaction. Thus, under section 362(b), FC's basis in A1 will be $100.

(D) *FC1's basis in P stock.* Under section 358, FC1's basis in the P stock it receives in the exchange will be $100.

(ii) *Property transferred to U.S. subsidiary in triangular reorganization.* (A) *Facts.* The facts are the same as in paragraph (i)(A) of this *Example 9,* except that P also owns the sole outstanding share of DC (basis $1) and, instead of merging into FC, FC2 merged into DC.

(B) *Determining P's basis in its DC share.* As determined under paragraph (i)(B)(*2*) of this *Example 9,* P's basis in its DC share is $21, the sum of its original $1 basis plus the $20 adjustment for the deemed transfer of A1.

(C) *DC's basis in A1.* If FC2 had sold A1 for its value immediately before the transaction, no gain or loss recognized on the sale would have been taken into account in determining a federal income tax liability. However, if DC had sold A1 immediately after the transaction, any gain or loss recognized on the sale would have been taken into account in determining a federal income tax liability, so A1 is importation property with respect to DC. Furthermore, immediately after the transaction, DC's basis in A1, but for section 362(e)(1) and this section and section 362(e)(2), would be $100 and A1's value is $20. Therefore, the importation property's basis would exceed its value and the transfer is a loss importation transaction. Accordingly, DC's basis in A1 will be $20, A1's value immediately after the transaction.

(D) *FC1's basis in P stock.* Under section 358, FC1's basis in the P stock it receives in the exchange is $100.

(g) *Applicability date.* This section applies with respect to any transaction occurring on or after *March 28, 2016,* and also with respect to any transaction occurring before such date as a result of an entity classification election under § 301.7701–3 of this chapter filed on or after *March 28, 2016,* unless such transaction is pursuant to a binding agreement that was in effect prior to *March 28, 2016* and at all times thereafter. In addition, taxpayers may apply this section to any transaction occurring after October 22, 2004.

■ **Par. 11.** Section 1.362–4 is amended by:

■ 1. Revising the heading to paragraph (c) and adding paragraph (c)(3).

■ 2. Revising the introductory text in paragraph (h).

■ 3. Revising the third sentence of paragraph (h) *Example 4* paragraph (iv)(B).

■ 4. Revising paragraph (h) *Example 11.*

■ 5. Adding a sentence to the end of paragraph (j).

The revisions and additions read as follows:

§ 1.362–4 Basis of loss duplication property.

* * * * *

(c) *Exceptions and special rules.* * * *

* * * * *

(3) *Other effects of basis determination under this section*—(i) *Determination by reference to transferor's basis.* A determination of basis under this section is a determination by reference to the transferor's basis, including for purposes of sections 755, 1223(2), and 7701(a)(43).

(ii) *Treatment as tax-exempt income or noncapital, nondeductible expense.* A determination of basis under paragraph (b) of this section does not give rise to an item treated as a noncapital, nondeductible expense under § 1.1502–32(b)(2)(iii). However, a determination of basis under paragraph (d) of this section does give rise to an item treated as a noncapital, nondeductible expense under § 1.1502–32(b)(2)(iii).

* * * * *

(h) *Examples.* The examples in this paragraph (h) illustrate the application of section 362(e)(2) and the provisions of this section. Unless the facts otherwise indicate, the examples use the following nomenclature and assumptions: X, Y, P, S, S1, and S2 are domestic corporations; A and B are U.S. individuals; FC1 and FC2 are foreign corporations and are not engaged in a U.S. trade or business, have no U.S. real property interests, and have no other relationships, activities, or interests that would cause them, their shareholders, or their property to be subject to tax imposed under any provision of subtitle A of the Internal Revenue Code (federal income tax); there is no applicable income tax treaty; PRS is a domestic partnership; no election is made under section 362(e)(2)(C); and the transferred property is not importation property (as defined in § 1.362–3(c)(2)) and the transfers are not loss importation transactions (as defined in § 1.362–3(c)(3)), so that the basis of no property is determined under section 362(e)(1). All persons and transactions are unrelated unless the facts indicate otherwise, all taxpayers are on a calendar tax year, and all other relevant facts are set forth in the examples. See § 1.362–3(f) for additional examples illustrating the application of section 362(e)(2) and this section, including to transactions that are subject to section 362(e)(2), and section 362(e)(1).

* * * * *

Example 4. * * *

(iv) * * *

(B) *Analysis.* * * * For the reasons set forth in paragraph (iii)(B) of this *Example 4,* Y would have been required to reduce its basis in the transferred assets by $1.60. * * *

* * * * *

Example 11. Transfers of importation property with non-importation property. (*i*) *Single transferor, loss importation transaction.* (A) *Facts.* FC1 transfers Asset 1 (basis $80, value $50), Asset 2 (basis $120, value $110), and Asset 3 (basis $32, value $40) to DC in a transaction to which section 351 applies. Asset 1 is not importation property within the meaning of § 1.362–3(c)(2). Asset 2 and Asset 3 are importation property within the meaning of § 1.362–3(c)(2).

(B) *Application of section 362(e)(1).* Immediately after the transfer, and without regard to section 362(e)(1) or section 362(e)(2) and this section, DC's aggregate basis in importation property (Asset 2 and Asset 3) would be $152. The aggregate value of the importation property immediately after the transfer is $150. Accordingly, the transaction is a loss importation transaction within the meaning of § 1.362–3(c)(3) and, under section 362(e)(1), DC's bases in Asset 2 and Asset 3 would equal the value of each, $110 and $40, respectively.

(C) *Application of section 362(e)(2) and this section.* (*1*) *Analysis.* (*i*) *Loss duplication transaction.* FC1's transfer of Asset 1, Asset 2, and Asset 3 is a transaction described in section 362(a). But for section 362(e)(2) and this section, DC's aggregate basis in those assets would be $230 ($80 under section 362(a) + $110 + $40 under section 362(e)(1)), which would exceed the aggregate value of the assets $200 ($50 + $110 + 40) immediately after the transaction. Accordingly, the transfer is a loss duplication transaction and FC1 has a net built-in loss of $30 ($230 − $200).

(*ii*) *Identifying loss duplication property.* But for section 362(e)(2) and this section, DC's basis in Asset 1 would be $80, which would exceed Asset 1's $50 value immediately after the transaction. Accordingly, Asset 1 is loss duplication property. But for section 362(e)(2) and this section, DC's basis in Asset 2 would be $110, which would not exceed Asset 2's $110 value immediately after the transaction. Accordingly, Asset 2 is not loss duplication property. But for section 362(e)(2) and this section, DC's basis in Asset 3 would be $40, which would not exceed Asset 3's $40 value immediately after the transaction. Accordingly, Asset 3 is not loss duplication property.

(D) *Basis in loss duplication property.* DC's basis in Asset 1 is $50, computed as its $80 basis under section 362(a) reduced by FC1's $30 net built-in loss.

(E) *Basis in other property.* Under section 362(e)(1), DC's basis in Asset 2 is $110 and DC's basis in Asset 3 is $40. Under section 358(a), FC1 has an exchanged basis of $232 in the DC stock it receives in the transaction.

(ii) *Multiple transferors, no importation of loss.* (A) *Facts.* The facts are the same as paragraph (i)(A) of this *Example 11,* except that, in addition, FC2 transfers Asset 4 (basis $100, value $150) to DC as part of the same transaction. Asset 4 is importation property within the meaning of § 1.362–3(c)(2).

(B) *Application of section 362(e)(1).* Immediately after the transfer, and without regard to section 362(e)(1) or section 362(e)(2) and this section, DC's aggregate basis in importation property (Asset 2, Asset 3, and Asset 4) would be $252 ($120 + $32 + $100). The aggregate value of the importation property immediately after the transfer is $300 ($110 + $40 + $150). Accordingly, the transaction is not a loss importation transaction within the meaning of § 1.362–3(c)(3) and DC's bases in the importation property is not determined under section 362(e)(1).

(C) *Application of section 362(e)(2) and this section.* Notwithstanding that the transfers by FC1 and FC2 are pursuant to a single plan forming one transaction, section 362(e)(2) and this section apply to each transferor separately.

(*1*) *Application of section to FC1.* (*i*) *Loss duplication transaction.* FC1's transfer of Asset 1, Asset 2, and Asset 3 is a transaction described in section 362(a). But for section 362(e)(2) and this section, DC's aggregate basis in those assets would be $232 ($80 + $120 + $32), which would exceed the aggregate value of the assets $200 ($50 + $110 + $40) immediately after the transaction. Accordingly, the transfer is a loss duplication transaction and FC1 has a net built-in loss of $32 ($232 − $200).

(*ii*) *Identifying loss duplication property.* But for section 362(e)(2) and this section, DC's basis in Asset 1 would be $80, which would exceed Asset 1's $50 value immediately after the transaction. Accordingly, Asset 1 is loss duplication property. But for section 362(e)(2) and this section, DC's basis in Asset 2 would be $120, which would exceed Asset 2's $110 value

immediately after the transaction. Accordingly, Asset 2 is also loss duplication property. But for section 362(e)(2) and this section, DC's basis in Asset 3 would be $32, which would not exceed Asset 3's $40 value immediately after the transaction. Accordingly, Asset 3 is not loss duplication property.

(*iii*) *Basis in loss duplication property.* DC's basis in Asset 1 is $56, computed as its $80 basis under section 362(a) reduced by $24, its allocable portion of FC1's $32 net built-in loss ($30/40 × $32). DC's basis in Asset 2 is $112, computed as its $120 basis under section 362(a) reduced by $8, its allocable portion of FC1's $40 net built-in loss ($10/$40 × $32).

(*iv*) *Basis in other property.* Under section 358(a), FC1 has an exchanged basis of $232 in the DC stock it receives in the transaction.

(*2*) *Application of section to FC2.* FC2's transfer of Asset 3 is not a loss duplication transaction because Asset 3's value exceeds its basis immediately after the transaction. Accordingly, under section 362(a), DC's basis in Asset 3 is $100.

* * * * *

(j) *Effective/applicability date.* * * * The introductory text and *Example 11* of paragraph (h) of this section apply with respect to transactions occurring on or after *March 28, 2016,* and also with respect to transactions occurring before such date as a result of an entity classification election under § 301.7701–3 of this chapter filed on or after *March 28, 2016,* unless such transaction is pursuant to a binding agreement that was in effect prior to *March 28, 2016* and at all times thereafter. In addition, taxpayers may apply such provisions to any transaction occurring after October 22, 2004.

■ **Par. 12.** Section 1.368–3 is amended by revising paragraphs (a)(3) and (b)(3) and adding a sentence to the end of paragraph (e) to read as follows:

§ 1.368–3 Records to be kept and information to be filed with returns.

(a) * * *

(3) The value and basis of the assets, stock or securities of the target corporation transferred in the transaction, determined immediately before the transfer and aggregated as follows—

(i) Importation property transferred in a loss importation transaction, as defined in § 1.362–3(c)(2) and (3), respectively;

(ii) Loss duplication property as defined in § 1.362–4(g)(1);

(iii) Property with respect to which any gain or loss was recognized on the transfer (without regard to whether such property is also identified in paragraph (a)(3)(i) or (ii) of this section);

(iv) Property not described in paragraph (a)(3)(i), (ii), or (iii) of this section; and

* * * * *

(b) * * *

(3) The value and basis of all the stock or securities of the target corporation held by the significant holder that is transferred in the transaction and such holder's basis in that stock or securities, determined immediately before the transfer and aggregated as follows—

(i) Stock and securities with respect to which an election is made under section 362(e)(2)(C); and

(ii) Stock and securities not described in paragraph (b)(3)(i) of this section.

* * * * *

(e) *Effective/applicability date.* * * * Paragraphs (a)(3) and (b)(3) of this section apply with respect to reorganizations occurring on or after March 28, 2016, and also with respect to reorganizations occurring before such date as a result of an entity classification election under § 301.7701–3 of this chapter filed on or after March 28, 2016, unless such reorganization is pursuant to a binding agreement that was in effect prior to March 28, 2016 and at all times thereafter.

■ **Par. 13.** Section 1.705–1 is amended by revising paragraph (a)(9) to read as follows:

§ 1.705–1 Determination of basis of partner's interest.

(a) * * *

(9) For basis adjustments necessary to coordinate sections 705 and 362(e)(2), see § 1.362–4(e)(1).

* * * * *

■ **Par. 14.** Section 1.755–1 is amended by adding a sentence after the second sentence of paragraph (b)(1)(i) to read as follows:

§ 1.755–1 Rules for allocation of basis.

* * * * *

(b) * * *

(1) * * *

(i) *Application.* * * * For transfers subject to section 334(b)(1)(B), see § 1.334–1(b)(3)(iii)(C)(*1*) (treating a determination of basis under § 1.334–1(b)(3) as a determination not by reference to the transferor's basis solely for purposes of applying section 755); for transfers subject to section 362(e)(1), see § 1.362–3(b)(4)(i) (treating a determination of basis under § 1.362–3 as a determination not by reference to the transferor's basis solely for purposes of applying section 755); for transfers subject to section 362(e)(2), see § 1.362–4(c)(3)(i) (treating a determination of basis under § 1.362–4 as a determination by reference to the transferor's basis for all purposes). * * *

* * * * *

■ **Par. 15.** Section 1.1367–1 is amended by revising the last sentence of paragraph (c)(2) to read as follows:

§ 1.1367–1 Adjustments to basis of shareholder's stock in an S corporation.

* * * * *

(c) * * *

(2) *Noncapital, nondeductible expenses.* * * For basis adjustments necessary to coordinate sections 1367 and 362(e)(2), see § 1.362–4(e)(2).

* * * * *

John M Dalrymple,

Deputy Commissioner for Services and Enforcement.

Approved: February 16, 2016.

Mark J. Mazur,

Assistant Secretary of the Treasury (Tax Policy).

[FR Doc. 2016–06227 Filed 3–25–16; 8:45 am]

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DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

Tax Treatment of Cafeteria Plans

CFR Correction

In Title 26 of the Code of Federal Regulations, Part 1 (§§ 1.61 to 1.139), revised as of April 1, 2015, on page 545, § 1.125–4T is removed.

[FR Doc. 2016–07018 Filed 3–25–16; 8:45 am]

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DEPARTMENT OF HOMELAND SECURITY

Coast Guard

33 CFR Part 165

[Docket No. USCG–2015–0530]

Safety Zones; Annual Events Requiring Safety Zones in the Captain of the Port Lake Michigan Zone—Michigan City Summerfest Fireworks, Lake Michigan

AGENCY: Coast Guard, DHS.

ACTION: Notice of enforcement of regulation.

SUMMARY: The Coast Guard will enforce the Michigan City Summerfest Fireworks Safety Zone on a portion of Lake Michigan on July 4, 2016. This action is necessary and intended to ensure safety of life and property on navigable waters prior to, during, and immediately after the fireworks display. During the enforcement period listed below, the Coast Guard will enforce restrictions upon, and control movement of, vessels in the safety zone. No person or vessel may enter, transit,