

Part III – Administrative, Procedural, and Miscellaneous

Announcement of amendment to effective date provision of Treas. Reg. §1.7874-2T

Notice 2006-70

This notice announces that the Treasury Department and the Internal Revenue Service (IRS) will, when finalizing Treas. Reg. §1.7874-2T, amend the effective date in Treas. Reg. §1.7874-2T(j), as it applies to certain acquisitions initiated prior to December 28, 2005.

BACKGROUND

On December 28, 2005, the Treasury Department and the IRS issued TD 9238, 2006-6 I.R.B. 408 (Feb. 6, 2006), Guidance Under Section 7874 for Determining Ownership by Former Shareholders or Partners of Domestic Entities, which promulgated Treas. Reg. §1.7874-1T. The preamble to TD 9238 states that the IRS and the Treasury Department are considering issuing regulations, which may be retroactive, to address certain structures which have the effect of inversion transactions and therefore should be subject to section 7874. Those structures include situations in which the shareholders (or partners) of a domestic corporation (or domestic partnership) arrange to transfer their shares (or partnership interests) to a newly formed foreign entity for which an entity classification election under Treas. Reg. §301.7701-3 is made to treat such

entity as a foreign partnership for Federal tax purposes. The preamble noted that other such structures involve the use of exchangeable shares to avoid the application of section 7874.

On June 6, 2006, the Treasury Department and the IRS issued TD 9265, Guidance Under Section 7874 Regarding Expatriated Entities and Their Foreign Parents, which promulgated Treas. Reg. §1.7874-2T. Treasury Reg. §1.7874-2T addresses the concerns raised in the preamble to Treas. Reg. §1.7874-1T involving acquisitions by foreign partnerships and exchangeable shares. Accordingly, Treas. Reg. §1.7874-2T(e) generally provides that any foreign partnership that would be treated as a corporation under section 7704 of the Code (but for the application of section 7704(c)) will be treated as a foreign corporation for purposes of determining whether the partnership is a surrogate foreign corporation, as the term is defined in section 7874. In addition, Treas. Reg. §1.7874-2T(f) generally provides that options and similar interests held by a former shareholder or former partner of the expatriated entity by reason of holding stock or a partnership interest in the expatriated entity will be treated, for purposes of the owner continuity test in section 7874, as exercised, to the extent that the effect is to treat the foreign corporation as a surrogate foreign corporation.

The effective date provision in Treas. Reg. §1.7874-2T(j) provides that Treas. Reg. §1.7874-2T applies to acquisitions completed on or after June 6, 2006. The effective date provision does not, however, address situations in which a binding commitment to make an acquisition described in section

7874(a)(2)(B)(i) had been entered into prior to June 6, 2006, but such acquisition had not been completed prior to June 6, 2006.

DISCUSSION

The Treasury Department and the IRS will, when finalizing Treas. Reg. §1.7874-2T, amend the effective date provision in Treas. Reg. §1.7874-2T(j) such that Treas. Reg. §1.7874-2 will not apply to an acquisition otherwise described in section 7874(a)(2)(B)(i) that was completed on or after June 6, 2006, provided such acquisition was entered into pursuant to a written agreement which was (subject to customary conditions) binding on December 28, 2005, and at all times thereafter (binding commitment). For purposes of the preceding sentence, a binding commitment shall include entering into options and similar interests in connection with one or more written agreements described in the preceding sentence. Accordingly, the provisions of Treas. Reg. §1.7874-2T, when finalized, will not apply to acquisitions that occur, in whole or in part, as a result of the exercise of such options or similar interests.

EFFECTIVE DATE

Taxpayers may rely on this notice until the issuance of regulations described herein.

COMMENTS

Written comments on the issues addressed in this notice may be submitted to the Office of Associate Chief Counsel International, Attention: Milton M. Cahn (Notice 2006-70), room 4555, CC:INTL:BR4, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, DC, 20224. Alternatively, taxpayers

may submit comments electronically to

Notice.Comments@m1.irs.counsel.treas.gov. Comments will be available for public inspection and copying. Treasury and the IRS request comments by November 30, 2006.

DRAFTING INFORMATION

The principal author of this notice is Milton M. Cahn of the Office of Associate Chief Counsel (International). For further information regarding this notice contact Mr. Cahn at (202) 622-3860 (not a toll-free call).