

## Internal Revenue Service

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December 23, 1998

### Legend

Taxpayer .

X Corp

Y Corp

Z Group

TY: 1998

Dear

This responds to a letter from your authorized representatives dated June 23, 1998. Taxpayer requests a ruling concerning two factors of the indirect ownership portion of the limited Derivative Benefits Test under paragraph 7 of the revised Memorandum of Understanding accompanying the Income Tax Convention between the United States and Switzerland (the "Swiss Treaty") and under Article 22, *Limitation on Benefits*, of the Swiss Treaty.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to

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verification on examination.

## STATEMENT OF FACTS

X Corp is incorporated under the laws of \_\_\_\_\_, which is a member state of the European Union. X Corp is the parent of the Z Group, which operates in numerous countries around the world. The Z Group held its treasury function in \_\_\_\_\_. At the time that the ruling request was submitted, X Corp planned to incorporate Y Corp as a 100 percent-owned Swiss finance subsidiary and to relocate the treasury function for its worldwide operations to Y Corp. This transaction has now been completed.

Taxpayer is a wholly-owned U.S. subsidiary of X Corp. Taxpayer will pay interest to Y Corp and must determine whether the interest paid to Y Corp will be exempt from U.S. withholding tax pursuant to the terms of the Swiss Treaty.

Taxpayer represents that X Corp meets the requirements of \_\_\_\_\_, of the comprehensive Income Tax Convention between the United States and \_\_\_\_\_, and that as a publicly-traded corporation, within the meaning of Article \_\_\_\_\_ Treaty, X Corp qualifies for all of the benefits of that treaty, without regard to the residence of its owners. Taxpayer further represents that all of the shares of X Corp are primarily and regularly traded on the \_\_\_\_\_, which is recognized by the European Union as a recognized stock exchange, and that X Corp is entitled to exemption from U.S. tax on payments of interest arising in the United States pursuant to the \_\_\_\_\_ Treaty.

In addition, Taxpayer represents that Y Corp will satisfy the base reduction test provided for in paragraph 7 of the revised Memorandum of Understanding regarding the Swiss Treaty.

## RULINGS REQUESTED

With respect to the Derivative Benefits Test in Article 22, paragraph 3(b) of the Swiss Treaty:

1. That X Corp will be considered to be the “ultimate beneficial owner” of Y Corp under the derivative benefits test without reference to the residence of X Corp’s shareholders.
2. That X Corp will satisfy the requirements of Article 22(3)(b) of the Swiss Treaty . In this regard, subparagraph 3(b)(ii) (regarding references to Switzerland) will apply in

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such a manner that, because X Corp is a resident of \_\_\_\_\_, the term “recognized stock exchange” includes a \_\_\_\_\_ stock exchange on which registered dealings in shares take place.

## STATEMENT OF LAW AND ANALYSIS

### RULING NO. 1

Section 881 (a) of the Internal Revenue Code (the "Code") generally imposes a 30% tax on the amount received by a foreign corporation as interest from sources within the United States to the extent that the interest is not effectively connected with the conduct of a trade or business in the United States. Section 1442 of the Code requires that a tax of 30% of any interest paid to a foreign corporation from sources within the United States be deducted and withheld at the source.

Section 894(a) of the Code maintains that the provisions of the Code shall be applied to any taxpayer with due regard to any treaty obligation of the United States which applies to such taxpayer. Moreover, §1.1441-6(a) of the Treasury Regulations provides that the 30% rate of withholding shall be reduced as may be provided by a treaty with any country.

Article 11, *Interest*, of the Swiss Treaty provides that interest derived and beneficially owned by a resident of Switzerland is taxable only in Switzerland. Thus, exemption from U.S. tax will be granted on interest derived and beneficially owned by a resident of Switzerland that meets the requirements of Article 22 of the Swiss Treaty. Generally, benefits of the Swiss Treaty will be extended to a resident of Switzerland only if the resident meets the specific criteria listed in paragraphs 1-3 of Article 22. Because Y Corp will be wholly-owned by a non-Swiss company, it will fail to meet the specific criteria of paragraphs 1-3 of Article 22.

Article 22(6) of the Swiss Treaty provides that a person not entitled to benefits of the Swiss Treaty under the Article 22, paragraphs 1-3 may, nevertheless, be granted benefits if the competent authority of the state in which the income arises so determines after consultation with the competent authority of the other Contracting State.

Paragraph 7 of the revised Memorandum of Understanding to the Swiss Treaty provides an additional method for qualifying for benefits pursuant to paragraph 6 of Article 22. In pertinent part, paragraph 7 provides that:

[I]t is understood that a company resident in one of the Contracting States will be granted the benefits of the Convention under paragraph 6 of Article

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22 with respect to the income it derives from the other Contracting State if the ultimate beneficial owners of 95 percent or more of the aggregate vote and value of all of its shares are seven or fewer persons that are residents of a member state of the European Union or the European Economic Area or a party to the North American Free Trade Agreement that meet the requirements of subparagraph 3(b) of Article 22....

Under Article 22(3)(b) of the Swiss Treaty, shares held by shareholder residents of member states of the European Union or the European Economic Area or a party to the North American Free Trade Agreement will not count toward disqualification only if the resident meets three tests. First, the person must be entitled to benefits of an income tax treaty between its state of residence and the Contracting State from which benefits are claimed. Second, the person must be described in the subparagraph 1 of Article 22, applied as if the person were a resident of the Contracting State in which the company claiming benefits is resident. Finally, the person must be entitled, under the income tax convention between its state of residence and the Contracting State from which the treaty benefits are claimed, to a rate of tax equal to or less than the rate provided under the Swiss Treaty with respect to income derived from that Contracting State.

Taxpayer represents that X Corp is a resident of \_\_\_\_\_ whose principal class of shares is primarily and regularly traded on the \_\_\_\_\_ in \_\_\_\_\_, and that X Corp is the direct owner of 100 percent of the shares of Y Corp. Taxpayer further represents that Y Corp's ownership requirements under paragraph 7 of the Memorandum of Understanding will be met if X Corp is considered the "ultimate beneficial owner" of Y Corp under the Derivative Benefits Test.

A publicly traded company, such as X Corp, is described in the Treasury Department's technical explanation of Article 22(3)(b) of the Swiss Treaty, which is incorporated in the Derivative Benefits Test, and which similarly refers to "ultimate beneficial" ownership by qualified residents of the European Union. For purposes of Article 22(3)(b) of the Swiss Treaty, the technical explanation provides "[T]he person (the "ultimate beneficial owner" of the Swiss company) must be described in one of the subparagraphs of paragraph 1, applied as if the person were a resident of the Contracting State in which the company claiming benefits is resident."

Under the Treaty's direct ownership test in Article 22(l)(e)(i), a Swiss resident is entitled to benefits under the Swiss Treaty if it is a company whose principal class of shares is primarily and regularly traded on a recognized stock exchange. A "look through" to the residence of the shareholders is not required. Likewise, under \_\_\_\_\_ Treaty, a resident of \_\_\_\_\_ will satisfy the limitation on benefits provision if it is a company whose principal class of shares is substantially and regularly traded on a recognized stock exchange.

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Holding No. 1

Based solely on the information submitted and representations set forth above, it is held that X Corp is considered the "ultimate beneficial owner" of Y Corp under the Derivative Benefits Test of the Swiss Treaty without reference to the residence of the shareholders of X Corp.

RULING NO. 2.

Under paragraph 7 of the revised Memorandum of Understanding to the Swiss Treaty it is understood that a company resident in one of the Contracting States will be granted the benefits of the Swiss Treaty under Article 22(6) with respect to the income it derives from the other Contracting State, if the ultimate beneficial owners of 95 percent or more of the aggregate vote and value of all of its shares are seven or fewer persons that are residents of a member state of the European Union or the European Economic Area or a party to the North American Free Trade Agreement that meet the requirements of Article 22(3)(b).

For a Swiss corporation 100 percent-owned by a shareholder resident in \_\_\_\_\_ to meet the requirements of subparagraph 3(b)(ii) of Article 22 of the Swiss Treaty, the \_\_\_\_\_ parent must be described in Article 22(1), applied as if the person were a resident of the Contracting State in which the company claiming benefits is resident.

Taxpayer represents that X Corp is a resident of \_\_\_\_\_, a member state of the European Union, and that all of the shares of stock of X Corp are primarily and regularly traded on the \_\_\_\_\_, which is recognized by the European Union as a recognized stock exchange. Taxpayer further represents that X Corp qualifies for benefits under the \_\_\_\_\_ Treaty, and would qualify for benefits under Article 22(l)(e)(i) of the Swiss Treaty if the term "recognized stock exchange," as defined in Article 22(7) of the Swiss Treaty, is read as if the reference to any "Swiss stock exchange on which registered dealings in shares take place" were a reference to any "\_\_\_\_\_ stock exchange on which registered dealings in shares takes place."

The term "recognized stock exchange," as defined in Treaty Article 22(7)(a) of the Swiss Treaty, includes any "Swiss stock exchange on which registered dealings in shares take place." In pertinent part, Article 22(3)(b)(ii) of the Swiss Treaty provides that for the purposes of Article 22(3)(a)(ii), shares whose ultimate beneficial owner is a person that is a resident of a member state of the European Union will be taken into account only if such person would qualify for benefits under Article 22(1) if that person were a resident of the first-mentioned Contracting State and if references in such paragraph to the first-mentioned Contracting State were references to that person's

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state of residence. In keeping with the instructions of Article 22(3)(b)(ii), the definition of "recognized stock exchange" should be read as if the reference to any "Swiss stock exchange on which registered dealings in shares takes place" were a reference to any "stock exchange on which registered dealings in shares takes place." Under , the is the only recognized stock exchange located in .

Holding No. 2

Article 22(3)(b)(ii) of the Swiss Treaty (regarding references to Switzerland) will apply in such a manner that, because X Corp is a resident of , the term "recognized stock exchange" includes the as if it were a Swiss stock exchange. Based solely on the information submitted and representations set forth above, it is held that Y Corp will satisfy the requirements of Article 22 (3)(b) of the Swiss Treaty.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

This ruling is directed only to the taxpayer(s) requesting it. Section 6110(j)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

A copy of this letter must be attached to any income tax return to which it is relevant.

Sincerely,

W. Edward Williams  
Senior Technical Reviewer, Branch 1  
Office of the Associate Chief Counsel  
(International)