

## Internal Revenue Service

## Department of the Treasury

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Date:

June 19, 2001

### LEGEND:

Taxpayer	=
x	=
Corp A	=
Corp B	=
y	=
LLC1	=
LLC2	=
Entity A	=
Country A	=
Entity B	=
Country B	=
FSC1	=
Territory A	=

Dear Taxpayer:

This responds to your request dated August 22, 2000, for a private letter ruling concerning whether a corporate partner of a limited liability company classified as a partnership for federal income tax purposes is entitled to a 100% dividends-received deduction under section 245(c)(1)(A) of the Internal Revenue Code for the partner's distributive share of dividend income from earnings and profits of a foreign sales corporation (FSC) that are attributable to the FSC's foreign trade income.

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

FACTS:

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Taxpayer represents the following facts:

Taxpayer owns x% of the stock of Corp A. Corp A wholly owns Corp B. Taxpayer, Corp A and Corp B are U.S. corporations filing a consolidated federal income tax return.

Corp B owns y% of LLC1, a U.S. limited liability company classified as a partnership for federal income tax purposes. The remaining interests in LLC1 are owned by unrelated persons.

LLC1 wholly owns LLC2, a U.S. limited liability company, which wholly owns Entity A, an entity that is organized in Country A and wholly owns Entity B, an entity organized in Country B. LLC2, Entity A and Entity B are entities disregarded as separate from their owners pursuant to Treas. Reg. § 301.7701.

FSC1, a Territory A corporation, is a foreign sales corporation (FSC) governed by sections 921-27 of the Internal Revenue Code. FSC1 is wholly owned by LLC1 and acts as a commission agent for export sales of LLC2 and Entity B, which pay FSC1 a commission determined under the administrative pricing provisions of section 925 and related regulations. The products sold by LLC2 and Entity B for export are export property within the meaning of section 927(a), and the gross receipts derived from these export sales are foreign trading gross receipts within the meaning of section 924(a).

FSC1 pays dividends to LLC1. All of such dividends are from earnings and profits attributable to foreign trade income within the meaning of section 923(b).

You have requested a ruling that Taxpayer's consolidated group is entitled to a 100% dividends-received deduction under section 245(c)(1)(A) with respect to Corp B's distributive share of such dividends paid to LLC1.

#### LAW AND ANALYSIS:

Section 245(c)(1)(A) provides that in the case of a domestic corporation, there shall be allowed as a deduction an amount equal to 100 percent of any dividend received from another corporation which is distributed out of earnings and profits attributable to foreign trade income for a period during which such other corporation was a FSC.

Section 245(c)(4)(A) provides that the term "foreign trade income" has the meaning given such term under section 923. Section 923(b) defines foreign trade income to mean the gross income of a FSC attributable to foreign trading gross receipts as defined under section 924(a).

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Section 245(c)(2)(A) provides that the 100 percent dividends-received deduction shall not apply to any dividend distributed out of earnings and profits attributable to foreign trade income that is section 923(a)(2) nonexempt income as defined under section 927(d)(6). Section 927(d)(6) defines section 923(a)(2) nonexempt income to mean the nonexempt portion of foreign trade income with respect to which sections 925(a)(1) and 925(a)(2) (the administrative pricing rules) do not apply.

Treas. Reg. § 301.7701-2(a) provides that a business entity with two or more owners is classified for federal tax purposes as either a corporation or a partnership.

Section 701 provides that a partnership as such is not subject to income tax, and that persons carrying on business as partners shall be liable for income tax only in their separate or individual capacities.

Section 702(a) provides that, in determining a partner's income tax, each partner must take into account separately the partner's distributive share of items enumerated in section 702(a)(1) through (8).

Section 702(a)(5) provides that each partner must take into account separately the partner's distributive share of the partnership's dividends with respect to which there is a deduction under part VIII of subchapter B of chapter 1 of the Code.

Part VIII of subchapter B of chapter 1 of the Code includes section 245 (Dividends Received from Certain Foreign Corporations).

Treas. Reg. § 1.702-1(a)(5) provides, in pertinent part, that each partner shall take into account, as part of the dividends received by the partner from domestic corporations, the partner's distributive share of dividends received by the partnership, with respect to which the partner is entitled to a deduction under part VIII, subchapter B, chapter 1 of the Code.

Section 702(a)(7) provides that each partner must take into account separately any other items of income, gain, loss, deduction, or credit to the extent provided by regulations prescribed by the Secretary.

Treas. Reg. § 1.702-1(a)(8)(ii) provides that each partner must take into account separately the partner's distributive share of any partnership item which if separately taken into account by any partner would result in an income tax liability for that partner different from that which would result if that partner did not take the item into account separately.

Section 702(b) provides that the character of any item of income, gain, loss, deduction or credit included in a partner's distributive share under paragraphs (1) through (7) of section 702(a) is determined as if the item were realized directly from the

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source from which realized by the partnership, or incurred in the same manner as incurred by the partnership.

Section 703(a)(1) provides that the taxable income of a partnership shall be computed in the same manner as in the case of an individual, except that the items described in section 702(a) shall be separately stated.

A recipient of dividends distributed by a FSC out of earnings and profits attributable to foreign trade income is potentially entitled to a dividends-received deduction under section 245(c)(1)(A) with respect to the dividends distributed. Domestic corporations are entitled to this dividends-received deduction. Therefore, under section 702(a)(5) and Treas. Reg. § 1.702-1(a)(5), Corp B must take into account separately its distributive share of the dividends received by LLC1 from FSC1.

Such separate, partner-level accounting is additionally required under Treas. Reg. § 1.702-1(a)(8)(ii) because the income tax liability of Corp B as a domestic corporation is affected by the availability of the dividends-received deduction under section 245(c)(1)(A). Therefore, LLC1 must separately state Corp B's distributive share of dividends received from FSC1.

Under section 702(b), Corp B's distributive share of such dividends will retain the character of such dividends as distributions out of earnings and profits attributable to foreign trade income.

#### CONCLUSION:

Based on the information submitted and the representations made, we rule that Corp B is entitled to a 100% dividends-received deduction under section 245(c)(1)(A) with respect to Corp B's distributive share of dividends that are received by LLC1 from FSC1 and are distributed out of earnings and profits attributable to foreign trade income within the meaning of section 923(b) where the administrative pricing rules under section 925 are used in computing the foreign trade income.

This ruling is conditioned on use of the administrative pricing rules of section 925 in determining all foreign trade income, and on consistent treatment of Corp B for purposes of the FSC provisions as the deemed recipient of dividends paid by FSC1 to LLC1. Specifically, this ruling shall not apply if, in applying the administrative pricing rules, FSC1 treats more than 15/23 of the foreign trade income attributable to Corp B as exempt foreign trade income. See section 291(a)(4) and Temp. Treas. Reg. § 1.923-1T(b)(1)(i).

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any transaction or item, including but not limited to whether income is properly subject to any of the FSC provisions of sections 921-27 or is properly computed under such provisions; the effect of the rules governing "check-the-

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box” elections and disregarded entities under Treas. Reg. § 301.7701; and the effect of any special allocation of partnership income of LLC1.

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(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 two of your authorized representatives.

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

Sincerely,  
Elizabeth G. Beck  
Acting Chief, Branch 6  
Office of Associate Chief Counsel  
(International)