

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[REG-163892-01]

RIN 1545-AY42

Guidance under Section 355(e); Recognition of Gain on Certain Distributions of Stock or Securities in Connection with an Acquisition.

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Withdrawal of notice of proposed rulemaking; and notice of proposed rulemaking by cross-reference to temporary regulations.

SUMMARY: This document withdraws the notice of proposed rulemaking published in the **Federal Register** on January 2, 2001. In the Rules and Regulations section of this issue of the **Federal Register**, the IRS is issuing temporary regulations relating to recognition of gain on certain distributions of stock or securities of a controlled corporation in connection with an acquisition. The text of those regulations also serves as the text of these proposed regulations.

DATES: Written and electronic comments and requests for a public hearing must be received by July 25, 2002.

ADDRESSES: Send submissions to: CC:ITA:RU (REG-163892-01), room 5226, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand delivered Monday through Friday between the hours of 8 a.m. and 5 p.m. to:

CC:ITA:RU (REG-163892-01), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, DC. Alternatively, taxpayers may submit electronic comments directly

to the IRS Internet site at www.irs.gov/regs.

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, Amber R. Cook at (202) 622-7530; concerning submissions, Treena Garrett, (202) 622-7180 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background and Explanation of Provisions

On January 2, 2001, the IRS and Treasury published in the **Federal Register** (66 FR 66) a notice of proposed rulemaking (REG-107566-00) under section 355(e) of the Internal Revenue Code of 1986. Those proposed regulations are withdrawn.

Temporary regulations in the Rules and Regulations section of this issue of the **Federal Register** amend the Income Tax Regulations (26 CFR part 1) relating to section 355(e). The temporary regulations provide rules relating to recognition of gain on certain distributions of stock or securities of a controlled corporation in connection with an acquisition. The text of those regulations also serves as the text of these proposed regulations. The preamble to the temporary regulations explains the amendments.

Special Analysis

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory 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, and, because these regulations do not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant to section 7805(f) of the Internal Revenue Code, this notice

of proposed rulemaking will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact.

Comments and Requests for a Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written comments (a signed original and eight (8) copies) and electronic comments that are submitted timely to the IRS. The IRS and Treasury Department specifically request comments on the clarity of the proposed rules and how they may be made easier to understand. All comments will be available for public inspection and copying. A public hearing will be scheduled if requested in writing by any person that timely submits written comments. If a public hearing is scheduled, notice of the date, time, and place for the public hearing will be published in the **Federal Register**.

Drafting Information

The principal author of these regulations is Amber R. Cook, Office of Associate Chief Counsel (Corporate). Other personnel from the IRS and Treasury Department, however, participated in their development.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

Withdrawal of Proposed Amendments to the Regulations and Proposed Amendments to the Regulations

Accordingly, under the authority of 26 U.S.C. 7805 and 26 U.S.C. 355(e)(5), the notice of proposed rulemaking (REG-107566-00) that was published in the **Federal Register** on Tuesday, January 2, 2001, (66 FR 66) is withdrawn. In addition, 26 CFR part 1 is proposed to be

amended as follows:

PART 1--INCOME TAXES

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

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

Section 1.355-7 also issued under 26 U.S.C. 355(e)(5). * * *

Par. 2. Section 1.355-0 is amended by revising the introductory text and adding an entry for §1.355-7 to read as follows:

§1.355-0 Table of contents.

In order to facilitate the use of §§1.355-1 through 1.355-7, this section lists the major paragraphs in those sections as follows:

* * * * *

§1.355-7 Recognition of gain on certain distributions of stock or securities in connection with an acquisition.

- (a) In general.
- (b) Plan.
 - (1) In general.
 - (2) Certain post-distribution acquisitions.
 - (3) Plan factors.
 - (4) Non-plan factors.
- (c) Operating rules.
 - (1) Internal discussions and discussions with outside advisors evidence of business purpose.
 - (2) Takeover defense.
 - (3) Effect of distribution on trading in stock.
 - (4) Consequences of section 355(e) disregarded for certain purposes.
 - (5) Multiple acquisitions.
- (d) Safe harbors.
 - (1) Safe Harbor I.
 - (2) Safe Harbor II.
 - (3) Safe Harbor III.

- (4) Safe Harbor IV.
- (5) Safe Harbor V.
 - (i) In general.
 - (ii) Special rules.
- (6) Safe Harbor VI.
 - (i) In general.
 - (ii) Special rule.
- (7) Safe Harbor VII.
 - (i) In general.
 - (ii) Special rule.
- (e) Stock acquired by exercise of options, warrants, convertible obligations, and other similar interests.
 - (1) Treatment of options.
 - (i) General rule.
 - (ii) Agreement, understanding, or arrangement to write an option.
 - (iii) Substantial negotiations related to options.
 - (2) Instruments treated as options.
 - (3) Instruments generally not treated as options.
 - (i) Escrow, pledge, or other security agreements.
 - (ii) Compensatory options.
 - (iii) Options exercisable only upon death, disability, mental incompetency, or separation from service.
 - (iv) Rights of first refusal.
 - (v) Other enumerated instruments.
 - (f) Multiple controlled corporations.
 - (g) Valuation.
 - (h) Definitions.
 - (1) Agreement, understanding, arrangement, or substantial negotiations.
 - (2) Controlled corporation.
 - (3) Controlling shareholder.
 - (4) Coordinating group.
 - (5) Discussions.
 - (6) Established market.
 - (7) Five-percent shareholder.
 - (8) Similar acquisition.
 - (9) Ten-percent shareholder.
 - (i) [Reserved]
 - (j) Examples.
 - (k) Effective date.

Par. 3. Section 1.355-7 is added to read as follows:

§1.355-7 Recognition of gain on certain distributions of stock or securities in connection with an

acquisition.

[The text of proposed §1.355-7 is the same as the text of §1.355-7T published elsewhere in this issue of the **Federal Register**].

Robert E. Wenzel,
Deputy Commissioner of Internal Revenue.