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memorandum

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to: Mary K. Black
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from: Peter H. Blessing
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subject: Application of Section 165(i) With Respect to Stock in a Controlled Foreign Corporation

This memorandum responds to your request for assistance regarding application of section 165(i) to losses sustained with respect to stock of three controlled foreign corporations ("CFCs"). This memorandum is limited in scope and does not address related issues such as whether the taxpayer is permitted to take a stock loss, whether a stock loss can be taken as a disaster loss eligible for the section 165(i) election, whether a stock loss can be attributable to a federally declared disaster, or whether the taxpayer's CFCs' entity classifications were appropriate under U.S. tax principles. This advice may not be used or cited as precedent.

ISSUE

Whether losses sustained by ("Subsidiary") in three controlled foreign corporations – ("Country 1 CFC"), ("Country 2 CFC"), and ("Country 3 CFC") (collectively, the "CFCs") – of which Subsidiary was the sole shareholder, "occur[red] in" a federally declared disaster area for purposes of meeting the requirements of section 165(i)(1) and Treas. Reg. §1.165-11(b)(3).[1]

[1] Unless otherwise indicated, all references to "section" are to the Internal Revenue Code of 1986, as amended (the "Code"), and all references to "Treas. Reg. §" are to the Treasury regulations promulgated thereunder.

CONCLUSION

The losses sustained by Subsidiary with respect to stock in the CFCs did not occur in a federally declared disaster area within the meaning of section 165(i)(1) and Treas. Reg. §1.165-11(b)(3), and, therefore, the losses do not qualify as disaster losses under section 165(i).[2]

FACTUAL BACKGROUND

On March 13, 2020, President Trump declared that the COVID-19 outbreak in the United States constituted a nationwide emergency pursuant to the Robert T. Stafford Disaster Relief and Emergency Assistance Act, 42 U.S.C. 5121-5207 (the "Stafford Act").[3] Specifically, the declaration letter provided:

> I have determined that the ongoing Coronavirus Disease 2019 (COVID-19) pandemic is of sufficient severity and magnitude to warrant an emergency determination under section 501(b) of the Robert T. Stafford Disaster Relief and Emergency Assistance Act, 42 U.S.C. 5121-5207 (the "Stafford Act").
>
> . . .
>
> Therefore, as an initial step, I hereby determine, under section 501(b) of the Stafford Act, that an emergency exists nationwide. In accordance with this determination, the Federal Emergency Management Agency may provide, as appropriate, assistance pursuant to section 502 and 503 of the Stafford Act for emergency protective measures not authorized under other Federal statutes.
>
> . . .
>
> In addition, after careful consideration, I believe that the disaster is of such severity and magnitude nationwide that requests for a declaration of a major disaster as set forth in section 401(a) of the Stafford Act may be appropriate.

For purposes of this memorandum, the declaration is referred to as the "COVID Declaration" and the emergency is referred to as the "COVID National Emergency."

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[2] This memorandum does not address whether the losses sustained by Subsidiary with respect to the CFCs were "attributable to" the federally declared disaster within the meaning of section 165(i)(1) and Treas. Reg. §1.165-11(b)(3), which is an additional requirement for the losses in this case to qualify under section 165(i), regardless of where they occurred.

[3] Letter from Donald J. Trump, President of the United States, to Acting Secretary Wolf, Secretary Mnuchin, Secretary Azar, and Administrator Gaynor (Mar. 13, 2020), https://trumpwhitehouse.archives.gov/briefings-statements/letter-president-donald-j-trump-emergency-determination-stafford-act/.

After the COVID Declaration, President Trump approved requests for major disaster declarations under the authority of the Stafford Act with respect to all fifty states, District of Columbia, U.S. Virgin Islands, Commonwealth of Puerto Rico, American Samoa, Northern Mariana Islands, Guam, and a number of tribes, beginning from January 20, 2020 (the "COVID Disaster Area").[4] The COVID National Emergency with respect to each COVID Disaster Area remains effective until terminated by notice of publication in the Federal Register.[5]

FACTS

, a corporation that is , is the common parent of an affiliated group of corporations filing a consolidated U.S. federal income tax return (the "Taxpayer"). The Taxpayer's taxable year is the calendar year. Taxpayer's taxable years are under examination. The Taxpayer is headquartered in .

The Taxpayer is in the , with in the United States, , and . In addition to , the Taxpayer also operates within its . Before the COVID pandemic, the Taxpayer operated in the United States and . The Taxpayer leased all of its . None of the CFCs' operations in derived material revenue from customers in the United States.

In , the Taxpayer undertook a restructuring plan "

" One of the Taxpayer's wholly owned subsidiaries, Subsidiary, was the sole shareholder of the

[4] Federal Emergency Management Agency, COVID-19 Disaster Declarations, https://www.fema.gov/coronavirus/disaster-declarations (last visited March 22, 2023). These FEMA notices are published in the Federal Register. See, e.g., New Jersey; Major Disaster and Related Determinations, 85 Fed. Reg. 20,700 (Apr. 14, 2020); New Mexico; Major Disaster and Related Determinations, 85 Fed. Reg. 26, 701 (May 5, 2020); and Ohio; Major Disaster and Related Determinations, 85 Fed. Reg. 26,702 (May 5, 2020).

[5] See 44 C.F.R. §206.32(f), which provides that federal assistance under the Stafford Act may be approved if the damage or hardship giving rise to a Presidential declaration of a major disaster or emergency took place during the "incident period or was in anticipation of that incident." "The incident period will be established by FEMA in the FEMA-State Agreement and published in the Federal Register." Id.

CFCs that were part of the Taxpayer's restructuring. In , Subsidiary was a domestic eligible entity treated as an association taxable as a corporation.

The Taxpayer's tax returns and related filings for the years under examination, plus information submitted in response to Exam's questions, indicate that the restructuring involved the following entities and transactions:

1. As of , Country 1 CFC was a limited liability company organized under the laws of the that was a disregarded entity for U.S. federal income tax purposes and was 100 percent owned by Subsidiary. On , , a corporation for U.S. federal income tax purposes, contributed assets to Country 1 CFC in exchange for membership interests therein. On , , a disregarded entity for U.S. federal income tax purposes whose sole owner was Subsidiary, contributed assets to Country 1 CFC in exchange for membership interests therein. As of , Country 1 CFC's default entity classification for U.S. federal income tax purposes was as a partnership. Country 1 CFC was a holding company for the Taxpayer's and operations.

   In , Country 1 CFC filed an IRS Form 8832 to change its entity classification from a foreign eligible entity that was classified as a partnership to a foreign eligible entity treated as an association taxable as a corporation, effective .[6] Pursuant to the restructuring plan,

   contributed its interest in Country 1 CFC to Subsidiary on , in an exchange governed by section 351. As a result, Subsidiary was the sole shareholder of Country 1 CFC as of . Country 1 CFC then reorganized as a limited liability company effective , with Subsidiary as its sole owner. Pursuant to Treas. Reg. §301.7701-3(b)(1)(ii), Country 1 CFC was treated as a domestic eligible entity that was disregarded as separate from its owner as of . This change in entity classification resulted in a deemed liquidation of Country 1 CFC under Treas. Reg. §301.7701-3(g)(1)(iii).

   Subsidiary claimed a worthless securities deduction under sections 165(a) and (g) in the amount of $ in respect of its shares of stock in Country 1

[6] This election was filed in and, therefore, was filed late to make the requested change effective as of . See Treas. Reg. §301.7701-3(c)(1)(iii). Late election relief was sought by the Taxpayer and granted under IRS Revenue Procedure 2009-41. Gain Recognition Agreements, pursuant to Treas. Reg. §1.367(a)-8, were filed with the Taxpayer's tax return, reflecting built-in gain of $. Exam may wish to consider whether there was a correct representation as to reasonable cause, and whether hindsight was used.

CFC immediately before its deemed liquidation.[7] Subsidiary elected to claim this deduction on the Taxpayer's consolidated U.S. federal income tax return pursuant to section 165(i)(1).[8]

2. Country 2 CFC was a corporation organized under the laws of the and was 100 percent owned by Subsidiary. Country 2 CFC was a holding company for the Taxpayer's operations in .

Country 2 CFC timely filed an IRS Form 8832 to change its entity classification from a foreign eligible entity treated as an association taxable as a corporation to a foreign eligible entity that is disregarded as separate from its owner, effective . This change in entity classification resulted in a deemed liquidation of Country 2 CFC pursuant to Treas. Reg. §301.7701-3(g)(1)(iii).

Subsidiary claimed a worthless securities deduction under sections 165(a) and (g) in the amount of $ in respect of its shares of stock in Country 2

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[7] The Taxpayer explained that it determined insolvency of each of the CFCs as of the date that all of the CFCs were deemed liquidated for U.S. federal income tax purposes and because the CFCs no longer existed after those dates, they were not expected to have any potential future value. Compare I.R.S. Rev. Rul. 2003-125, 2003-2 C.B. 1243 (2003).

[8] Exam should consider whether the steps involved here, including Country 1 CFC's election in to change its entity classification to a corporation (claimed to be retroactive to) followed a month later in by the corporation's liquidation in order to claim recognition of a loss in the deemed newly issued shares, appropriately results in a loss deduction. In addition to considering whether the Revenue Procedure predicates for the approximately retroactive entity classification election were correctly represented in the request for late election relief, various articulations of the substance over form doctrine appear relevant, including step transaction principles (collapsing steps), transitory corporation principles (permitting disregard of a transitory corporation), and circularity principles (permitting a contribution of property into a corporation and related distribution of the property by the corporation to be disregarded), as well as disregard of a corporation that, even if not transitory, serves no non-federal income tax function. See, e.g., Helvering v. Gregory, 69 F.2d 809, 810 (2d Cir. 1934), aff'd sub nom. Gregory v. Helvering, 293 U.S. 465 (1935); Hay v. Comm'r, 2 T.C. 460 (1943), aff'd, 145 F.2d 1001 (4th Cir. 1944), cert. den., 324 U.S. 863 (1945); Portland Manufacturing Co. v. Comm'r, 35 AFTR 2d 75-1439 (9th Cir. 1975); Asiatic Petroleum Co. Ltd. v. Comm'r, 79 F.2d 234 (2d Cir. 1935), cert. den., 296 U.S. 645 (1935); Haberman Farms, Inc. v. United States, 305 U.S. 787 (8th Cir. 1962); Packard v. Comm'r, 85 T.C. 397 (1985); West Coast Marketing v. Comm'r, 46 T.C. 32 (1966); Casco Products Corp. v. Comm'r, 49 T.C. 32 (1967); Custom Chrome Inc. v. Comm'r, T.C. Memo. 1998-317. (For purposes of applying these concepts, we believe the date the reclassification election was filed rather than the effective date of the change is relevant.) We note that there appears to have been no commercial purpose for the change in classification to a corporation (i.e., deemed formation of a corporation) beyond what was already met by the foreign partnership, and such formation appears to have been part of a plan intended solely to have a form of entity to subsequently (on conversion to an LLC, which had the effect of circumventing the Treas. Reg. §301.7701-3(c)(1)(iv) 60-month limitation on elective changes in entity classification) claim recognition of a loss without disposing of the loss property to an unrelated party, and a loss ordinary in character under section 165(g)(3), as well as the claimed benefit of section 165(i). (Any duplication of loss should be prevented under section 362(e)(2).) Under these circumstances, section 269 also should be considered (deductions may be disallowed if resulting from certain acquisitions or liquidations with a principal purpose of evading or avoiding tax).

CFC immediately before its deemed liquidation.[9] Subsidiary elected to claim this deduction on the Taxpayer's consolidated U.S. federal income tax return pursuant to section 165(i)(1).

3. Country 3 CFC was a organized under the laws of and was 100 percent owned by Subsidiary. Country 3 CFC operated throughout before the COVID pandemic.

   Country 3 CFC timely filed an IRS Form 8832 to change its entity classification from a foreign eligible entity treated as an association taxable as a corporation to a foreign eligible entity that is disregarded as separate from its owner, effective . This change in entity classification resulted in a deemed liquidation of Country 3 CFC pursuant to Treas. Reg. §301.7701-3(g)(1)(iii).

   Subsidiary claimed a worthless securities deduction under sections 165(a) and (g) in the amount of $ in respect of its shares of stock in Country 3 CFC immediately before its deemed liquidation.[10] Subsidiary elected to claim this deduction on the Taxpayer's consolidated U.S. federal income tax return pursuant to section 165(i)(1).

The total worthless securities deductions that Subsidiary claimed on the Taxpayer's consolidated U.S. federal income tax return in respect of the CFCs is $.[11] Claiming these loss deductions, pursuant to section 165(i)(1), in allowed the Taxpayer to carry back such losses to prior tax years and, as a result, trigger beneficial tax consequences.[12]

The COVID National Emergency was in effect when the Taxpayer implemented the transactions described above.

Before the COVID pandemic, the Taxpayer was "

" It closed

[9] Supra note 7.

[10] Supra note 7.

[11] The Taxpayer also claimed $ of operating losses with respect to other related entities on its consolidated U.S. federal income tax return pursuant to section 165(i)(1). The Taxpayer filed IRS Form 8886 (Reportable Transaction Disclosure Statement) with its consolidated U.S. federal income tax return disclosing the losses it carried back pursuant to section 165(i)(1).

[12] See sections 172(b)(1)(D) and 172(b)(2)(C) (allowing net operating losses arising in tax years beginning after December 31, 2017, and before January 1, 2021, to be carried back five years without limitation on the amount thereof to 80 percent of taxable income); section 11(b) (replacing the 35 percent rate on corporations with a 21 percent rate effective for taxable years beginning after December 31, 2017, thereby increasing the value of the Taxpayer's net operating losses for years before 2018).

its in the United States to comply with government mandates imposed in the respective jurisdictions on (in the case of its U.S.) and (in the case of its).

Because of decreased cash flow resulting from having to close its , the Taxpayer "

" Without the Taxpayer's financial support, the CFCs became insolvent, causing Subsidiary to conclude that its respective equity investment in such CFCs became worthless. Specifically, the CFCs "

"

The Taxpayer treated the worthless securities losses claimed with respect to the CFCs as disaster losses under section 165(i) because "

"

LAW

Section 165(a) provides generally for a deduction of any loss sustained during the taxable year and not compensated by insurance or otherwise. Treas. Reg. §1.165-1(a).

No deduction is allowed under section 165(a) solely on account of a decline in the value of stock owned by the taxpayer when the decline is due to a fluctuation in the market price of the stock or to another similar cause, except if the stock loss is recognized pursuant to Treas. Reg. §1.1002-1 upon the sale or exchange of stock or as provided for pursuant to Treas. Reg. §1.165-5 with respect to worthless stock. Treas. Reg. §1.165-4(a).

Section 165(g) provides that if any security, including a share of stock (or right to subscribe for, or to receive, a share of stock) in a corporation, which is a capital asset becomes worthless during the taxable year, the loss resulting therefrom is treated, for purposes of subtitle A, as a loss from the sale or exchange, on the last day of the taxable year, of a capital asset. Sec. 165(g)(1) and (2). Treas. Reg. §1.165-5 provides additional details regarding section 165(g), including treatment of ordinary and capital losses, treatment of worthless securities of an affiliated corporation, and abandonment of securities.

Section 165(i)(1) provides that, notwithstanding section 165(a), any loss occurring in a disaster area and attributable to a federally declared disaster may, at the election of the taxpayer, be taken into account for the taxable year immediately preceding the taxable year in which the disaster occurred. See also Treas. Reg. §1.165-11(a) (noting that the loss must be "sustained"). Section 165(i)(2) provides that, if an election is made under section 165(i), the casualty resulting in the loss shall be treated for purposes of Title 26 as having occurred in the taxable year for which the deduction is claimed. The loss

otherwise must be allowable as a deduction for the disaster year under section 165(a) and Treas. Reg. §§1.165-1 through 1.165-10. Treas. Reg. §1.165-11(b)(3).

Section 165(h), the predecessor to section 165(i), was enacted in 1962 in response to a massive severe storm that struck the Atlantic seaboard causing damage to life and property. 108 Cong. Rec. 4146 (Mar. 14, 1962). The Congressional record indicates that section 165(h) was enacted to provide relief from tax liability of those "adversely affected who have lost their entire life savings through the destruction of their homes, their places of business, or the livestock on their farms." Id. (statement of Senator John J. Williams). Section 165(h) was redesignated as section 165(i) in 1982. Tax Equity and Fiscal Responsibility Act of 1982, Pub. L. No. 97-248, §203(a).[13]

For purposes of section 165(i), the term "federally declared disaster" means any disaster subsequently determined by the President of the United States to warrant assistance by the federal government under the Stafford Act. Sec. 165(i)(5)(A); Treas. Reg. §1.165-11(b)(1). The COVID National Emergency constitutes a "federally declared disaster" within the meaning of section 165(i)(5)(A). The term "disaster area" means the area so determined to warrant assistance by the federal government. Sec. 165(i)(5)(B). The COVID Disaster Area constitutes a "disaster area" within the meaning of section 165(i)(5)(B).

Treas. Reg. §1.165-11(c) provides that an election made pursuant to section 165(i) for a disaster loss attributable to a particular disaster applies to the entire loss sustained by the taxpayer from that disaster during the disaster year.

ANALYSIS

To qualify as a disaster loss within the meaning of section 165(i), the loss must both occur in a disaster area and be attributable to a federally declared disaster. Regardless of whether the losses sustained by Subsidiary are attributable to a federally declared disaster, they did not occur in the COVID Disaster Area. Therefore, the losses sustained by Subsidiary with respect to its stock in the CFCs do not qualify as disaster losses within the meaning of section 165(i).

To qualify for the election under section 165(i)(1), the loss must occur "in" the COVID Disaster Area. No authority is directly on point clarifying where a loss sustained with respect to stock in a foreign corporation occurs under section 165(i). Previous disasters that could have given rise to an accelerated deduction under section 165(i) were triggered by an event, such as a hurricane, flood, or drought, that resulted in a discrete geographic disaster zone (including specific county level designations).[14] This is

[13] Congress amended section 165(i) multiple times after 1982 to conform defined terms to other changes in law.

[14] See, e.g., FM-5433-NM, available at, https://www.fema.gov/disaster/5433, designating Lincoln County as a disaster area in connection with the New Mexico Nogal Canyon Fire. See also, e.g., Stevens v.

consistent with Congress's intent that section 165(i) should provide relief by alleviating the financial impact of damages resulting from a physical disaster that is geographically confined. See 108 Cong. Rec. 4146 (Mar. 14, 1962).

The Taxpayer states that "

" The rules under Subchapter N, Part 1, for determining the source of stock losses, however, do not provide a framework for locating a loss sustained with respect to stock in a foreign corporation for purposes of section 165(i). The source rules are motivated by various concerns meaningfully different than the concern motivating the requirement of section 165(i) that the loss occur in a disaster area. For example, the section 865(a) and Treas. Reg. §1.865-2 source rules for gain or loss on the disposition of stock generally focus on facts relevant to the recognition event (the disposition itself). The requirement that the loss occur in a disaster area, on the other hand, appears motivated by a concern that the economic decrease in the value of property giving rise to the loss must have a nexus to the location of the disaster.

A more reasonable approach to locating where a loss with respect to stock in a foreign corporation economically arose would be to look to certain business metrics applicable to the foreign corporation.[15] This memorandum addresses this approach below, and contrasts it with an approach based on whether selling shareholders are "United States residents" or "nonresidents," as those terms are used in section 865(a), or an approach looking to the place of sale, or an approach based on the place where the foreign corporation is headquartered.

An approach looking to business metrics would reflect the location of the economic loss. Business metrics that might be applicable to a foreign corporation for purposes of analyzing the location of a loss with respect to stock in the foreign corporation include income producing assets, customers, employees, or revenue streams. An appropriate standard by analogy to physical assets would be to require that substantially all of the applicable metrics occur in the COVID Disaster Area for the loss sustained to be

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Comm'r, T.C. Memo. 1984-365 (1984) (drought); Radding v. Comm'r, T.C. Memo. 1988-250 (1988) (landslide); Novack v. Comm'r, T.C. Memo. 1989-538 (1989) (flood); Gordon v. U.S., 1995 WL 429248 (N.D. Calif. July 3, 1995) (earthquake); Tudyman v. Comm'r, T.C. Memo. 1996-215 (1996) (earthquake); and Rower v. Comm'r, T.C. Memo. 1998-117 (1998) (earthquake).

[15] An example of the section 865 sourcing rules relying on the location of economic activity can be found in section 865(f), which sources gain from a U.S. resident's sale of foreign affiliate stock based (in part) on whether the foreign affiliate is in the active conduct of a trade or business in a foreign country. This test generally is consistent with the "business metrics" approach discussed in this Memorandum. See also The Black & Decker Corp. v. Comm'r, T.C. Memo. 1991-557 (1991) (applying the "geographical situs test" to treat the taxpayer's worthless stock loss under section 165(g)(3) as foreign source income because the loss sustained grew out of an activity and use of property in the foreign country). See also Treas. Reg. §1.954-2(b)(4)(x) (for purposes of subpart F's "same country" rules, the location of stock of a controlled foreign corporation is determined by reference to underlying assets).

considered to occur in a disaster area.[16] The "substantially all" standard has been used in other instances when, for U.S. federal income tax purposes, a tax consequence is dependent on locating a business, property, or services within a specific zone. In one instance, the new markets tax credit under section 45D considers "substantially all" as satisfied if at least 85 percent of the taxpayer's investment is directly traceable to qualified low-income community investments.[17] However, that standard is not dispositive for purposes of section 165(i).

Applying the "substantially all" approach to the Taxpayer's circumstances, none of the CFCs derived substantially all of their revenues from U.S. customers. Other possible metrics, such as income producing assets, employees, and revenue streams, all were located or occurred outside the United States. As such, this approach would not result in the losses sustained by Subsidiary being treated as occurring in the COVID Disaster Area.

In contrast to looking at business metrics, section 865(a) and Treas. Reg. §1.865-2 are predicated on a single event of a disposition, rather than the location of the underlying cause of loss. For a variety of reasons, including ease of administration, these rules, as noted above, generally focus on the residence of the seller. Even so, exceptions apply, including that, in the case of a CFC, as here, a hybrid rule may apply to treat part of the gain characterized as a dividend under section 1248 and sourced accordingly.[18] This hybrid treatment, as well as other specific rules in section 865, illustrates the residual, default aspect of the section 865(a) and Treas. Reg. §1.865-2 rules, as opposed to being rules based on substantive principles.

It follows that determining whether a loss sustained with respect to stock in a foreign corporation occurred in the COVID Disaster Area based on the residence of the shareholder is inappropriate. The location of the occurrence of the loss is conceptually different than the location of the shareholder's residence, and the latter has no direct bearing on location of the foreign corporation's operations. For example, this approach would locate a loss sustained with respect to stock in a corporation within the United States if the shareholder were a U.S. resident, despite all other applicable business

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[16] This approach is consistent with past judicial application of section 165(i) requiring the affected property to be located in the disaster area. See, e.g., Kohn v. Comm'r, T.C. Memo. 2017-159, 39 (2017) ("The President determined that in 1993 St. Charles County, where petitioners' docks were located, suffered a natural disaster warranting assistance under the Disaster Relief and Emergency Assistance Act.") (emphasis added); Cziraki v. Comm'r, T.C. Memo. 1998-439, *1 (1998) ("The area in which properties A and B are situated was declared a Federal disaster area for the period January 5 through March 20, 1993.") (emphasis added).

[17] See Treas. Reg. §1.45D-1(c)(5). See also, e.g., Treas. Reg. §§1.108(i)-2(b)(6)(i)(B); 1.250(b)-5(c)(7); 1.1400L(b)-1(c)(3) (Liberty Zones, since repealed); Treas. Reg. §§1.1400Z2(d)-1(d)(2), 1.1400Z2(d)-2(d)(4)(ii); and Notice 2006-77, 2006-2 C.B. 590 (Sept. 1, 2006) (Gulf Opportunity Zone; since repealed). (These regulations illustrate a range of thresholds that have been used for purposes of determining "substantially all" in certain contexts).

[18] Further, a recapture rule in respect of prior dividends applies under Treas. Reg. §1.865-2.

metrics of the corporation being located outside the United States; and conversely, would locate a loss sustained with respect to stock of a corporation outside the United States (denying section 165(i) relief) if the shareholder were a U.S. citizen having a tax home abroad (or other nonresident as defined in section 865) despite all applicable business metrics of the corporation being in the United States.

Locating a loss sustained with respect to stock in a foreign corporation for purposes of section 165(i) based on the location of the place of sale or disposition is inappropriate for reasons similar to those discussed relating to the residence of the shareholder.[19] Moreover, in the case of the CFCs, the location of the sale of stock can be unclear, such as when, as here, the deemed liquidations occurred by reason of a tax election or, in the case of Country 1 CFC, a reorganization. Such a formalistic approach to locating a loss sustained for purposes of section 165(i) is inconsistent with the motivation behind section 165(i) that the disaster caused the economic decrease in value of property giving rise to the loss.

Locating a loss sustained with respect to stock in a foreign corporation for purposes of section 165(i) based on the place where the foreign corporation is headquartered also would not necessarily appropriately target the tax relief intended by Congress. Whereas Congress intended section 165(i) to provide relief to those directly impacted by a particular disaster, locating a loss on the basis of where a foreign corporation is headquartered would not necessarily relate to the geographic location of the foreign corporation's business operations. For example, it would not be appropriate to grant relief under section 165(i) to a shareholder who owns stock in a foreign corporation that only is headquartered within the United States, but whose operations and/or revenue streams are located outside the United States.

For these reasons, the losses sustained by Subsidiary with respect to stock of the CFCs did not occur in the COVID Disaster Area for purposes of section 165(i). As such, these losses do not qualify as disaster losses within the meaning of section 165(i).

SCOPE AND CASE DEVELOPMENT

This memorandum addresses only whether losses with respect to stock in a foreign corporation occurred in the COVID Disaster Area for purposes of meeting the requirements of section 165(i). Specifically, this memorandum does not consider the additional requirement of whether the losses sustained by Subsidiary with respect to stock of the CFCs were attributable to a federally declared disaster within the meaning of section 165(i)(1) and Treas. Reg. §1.165-11(b)(3). No opinion is expressed or implied concerning whether a loss with respect to stock (either domestic or foreign) may qualify as a disaster loss under section 165(i). This memorandum also does not address whether the stock of the CFCs was worthless for purposes of section 165(g). Finally, this memorandum does not conclude as to whether the steps involved to

[19] See Hay v. Comm'r, supra, 2 T.C. 460, 471 (gain on liquidation sourced by reference to where the corporation conducted "all its business" rather than where "a technical bill of sale" was executed).

change Country 1 CFC’s entity classification were appropriate under U.S. tax principles. Exam may wish to pursue one or more of these issues.

Please call (202) 317-6938 if you have any further questions.