



DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[REG-134016-15]

RIN 1545-BN47

Guidance Under Section 355 Concerning Device and Active Trade or Business; Partial Withdrawal

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Partial withdrawal of notice of proposed rulemaking.

SUMMARY: This document partially withdraws a notice of proposed rulemaking containing proposed regulations regarding the application of the device prohibition and the active trade or business requirement for distributions of controlled corporation stock (or stock and securities) by a distributing corporation without income, gain, or loss. The proposed regulations would affect corporations and their shareholders and security holders.

DATES: The notice of proposed rulemaking published in the *Federal Register* on July 15, 2016 (81 FR 46004), is partially withdrawn as of [INSERT DATE OF PUBLICATION IN THE *FEDERAL REGISTER*].

ADDRESSES: Commenters may submit public comments electronically via the Federal eRulemaking Portal at <https://www.regulations.gov> by searching the Docket ID number (IRS-2016-0030) or may send paper submissions to CC:PA:01:PR (REG-134016-15), Room 5503, Internal Revenue Service, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044.

FOR FURTHER INFORMATION CONTACT: Aglaia Ovtchinnikova at (202) 317-6847 or Justin Du Mouchel at (202) 317-6975 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background

If a distribution of stock (or stock and securities) of a controlled corporation (within the meaning of section 355(a)(1)(A) of the Internal Revenue Code (Code)) satisfies the numerous requirements of section 355 and other relevant provisions of the Code and the Income Tax Regulations (26 CFR part 1),¹ the distribution may occur without recognition of any gain or loss to the distributing corporation (within the meaning of section 355(a)(1)(A)) and without recognition of any gain or loss to, or the inclusion of any amount in the income of, the shareholders or security holders of the distributing corporation.

Among the numerous requirements to qualify for the Federal income tax treatment available under section 355, section 355(a)(1)(B) and § 1.355-2(b)(4) and (d) provide that a transaction must not be used principally as a device for the distribution of the earnings and profits of the distributing corporation, the controlled corporation, or both (device prohibition). Additionally, section 355(a)(1)(C) and (b) and §§ 1.355-2(h) and 1.355-3 require each of the distributing corporation and the controlled corporation to be engaged, immediately after the distribution, in the active conduct of a trade or business (active trade or business requirement).

On July 15, 2016, the Department of the Treasury (Treasury Department) and the IRS published a notice of proposed rulemaking (REG-134016-15) in the *Federal Register* (81 FR 46004) that would modify the regulations under section 355 with respect to the device prohibition and the active trade or business requirement. Among other proposed changes, those modifications would have included a “per se” test in proposed § 1.355-2(d)(5) to determine whether a distribution violated the device prohibition and two sets of anti-abuse rules.

Under the proposed “per se” device rule, if the distributing corporation’s or the controlled corporation’s “Nonbusiness Asset Percentage” (as defined in proposed § 1.355-2(d)(2)(iv)(B)(5)) exceeded certain designated percentages (both individually and in comparison to the other corporation’s Nonbusiness Asset Percentage), the transaction would have been considered a

¹ Unless otherwise specified, all “section” or “§” references are to sections of the Code or the Income Tax Regulations (26 CFR part 1).

device notwithstanding the presence of any other nondevice factors (such as a corporate business purpose), with limited exceptions.

Under the first set of anti-abuse rules in proposed § 1.355-2(d)(2)(iv)(E) and (d)(5)(iv), a transaction or series of transactions (such as a change in the form of ownership of an asset; an issuance, assumption or repayment of indebtedness; or an issuance or redemption of stock) would not have been given effect if undertaken with a principal purpose of affecting the Nonbusiness Asset Percentage of any corporation to avoid a determination that a distribution was a device.

The second anti-abuse rule (minimum active trade or business anti-abuse rule) was set forth in proposed § 1.355-9(d) and related to the minimum active trade or business requirement in proposed § 1.355-9, under which the “Five-Year-Active-Business Asset Percentage” (as defined in proposed § 1.355-9(a)(6)) of each of the distributing corporation and the controlled corporation would be required to be at least five percent. Under the minimum active trade or business anti-abuse rule, a transaction or series of transactions would not have been given effect if undertaken with a principal purpose of affecting the Five-Year-Active-Business Asset Percentage of any corporation to avoid a determination that a distribution does not meet the minimum active trade or business requirement in proposed § 1.355-9.

The device anti-abuse rules and the minimum active trade or business anti-abuse rule generally would not have applied to (i) non-transitory acquisitions or dispositions of assets, or (ii) non-transitory transfers of assets between the distributing corporation and the controlled corporation.

The Treasury Department and the IRS received feedback from stakeholders that generally was critical of the proposed “per se” device rule and the two anti-abuse rules. In response to the feedback received, the Treasury Department and the IRS are withdrawing proposed §§ 1.355-2(d)(2)(iv)(E) and (d)(5) and 1.355-9(d). The withdrawal of these proposed rules does not affect the potential application of other rules or judicial doctrines, such as the substance-over-form or

step-transaction doctrines. The Treasury Department and the IRS continue to study the issues addressed in the 2016 proposed regulations.

Drafting Information

The principal author of this document is Aglaia Ovtchinnikova of the Office of Associate Chief Counsel (Corporate). However, other personnel from the Treasury Department and the IRS participated in its development.

List of Subjects in 26 CFR Part 1

Income Taxes, Reporting and recordkeeping requirements.

Partial Withdrawal of Proposed Amendments to the Regulations

Under the authority of 26 U.S.C. 7805, proposed §§ 1.355-2(d)(2)(iv)(E) and (d)(5) and 1.355-9(d), contained in the notice of proposed rulemaking (REG-134016-15) that was published in the *Federal Register* on July 15, 2016 (81 FR 46004), are withdrawn.

Frank J. Bisignano,

Chief Executive Officer.

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