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Report No. 1382
October 10, 2017

The Honorable David Kautter
Assistant Secretary (Tax Policy)
Department of the Treasury
1500 Pennsylvania Avenue, NW
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The Honorable John Koskinen
Commissioner
Internal Revenue Service
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The Honorable William M. Paul
Acting Chief Counsel
Internal Revenue Service
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Re: *Report No. 1382 on Final, Temporary and Proposed Regulations Under Section 337(d) Relating to Certain Transfers of Property to Regulated Investment Companies and Real Estate Investment Trusts*

Dear Messrs. Kautter, Koskinen and Paul:

I am pleased to submit the attached report of the Tax Section of the New York State Bar Association. The report provides comments on final and temporary regulations (the "**2016 Temporary Regulations**") and proposed regulations (the "**2016 Proposed Regulations**" and, together with the 2016 Temporary Regulations, the "**regulations**") issued under Sections 337(d) and 355(h) of the Internal Revenue Code of 1986, as amended, which require corporate-level gain recognition in certain transactions in which property of a C corporation becomes the property of a real estate investment trust (a "**REIT**").

Generally, the 2016 Temporary Regulations apply when a Section 355 distribution occurs within ten years before or after a "conversion transaction" (for this purpose, a transfer from a C corporation to a REIT or a C corporation's election of REIT status) involving the distributing or controlled corporation (or a predecessor, successor or member of the separate affiliated group ("**SAG**") of the distributing or controlled

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corporation). Where the Section 355 distribution precedes the “conversion transaction,” the 2016 Temporary Regulations generally treat the corporation transferring property to the REIT as making a “deemed sale election” and recognizing all built-in gain in the transferred assets. Where the conversion transaction precedes the Section 355 distribution, the 2016 Temporary Regulations generally require the REIT, in the year of the distribution, to recognize the remaining built-in gain in its assets attributable to the period when the assets were held by a C corporation (gain the recognition of which would otherwise be deferred, subject to the requirements of Section 1374).

In our view, the regulations in general appropriately focus on restricting transactions that achieve results similar to transactions barred by the Protecting Americans from Tax Hikes Act of 2015 (the “**PATH Act**”), chiefly the merger of a distributing or controlled corporation (or a SAG member of either) with and into a REIT acquiror, which has an effect similar to that of a REIT election by the corporation (which is barred in many circumstances by the PATH Act). However, as discussed in detail in the attached report, and as echoed in the Treasury Department’s October 2, 2017 report on identifying and reducing tax regulatory burdens, we believe that the 2016 Temporary Regulations require excessive corporate-level gain recognition in some situations. We recommend an alternative approach that we believe would address this concern and also suggest certain other minor amendments to the regulations.


Below is a brief summary of our principal comments:

- A. In the case of a conversion transaction involving a REIT occurring within ten years after a Section 355 distribution, the 2016 Temporary Regulations should be modified to require corporate-level gain recognition solely with respect to built-in gain existing at the time of the distribution and with respect to assets held at the time of the distribution (and possibly “successor assets”).
- B. The 2016 Temporary Regulations should not apply to certain wholly internal Section 355 distributions subsequent to which the ultimate parent of the distributing and controlled corporations elects REIT status.
- C. The definitions of “predecessors” and “successors” in Temporary Regulation Section 1.337(d)-7T(f)(2) should be clarified.
- D. The exception in Temporary Regulation Section 1.337(d)-7T(f)(3)(i) (for Section 355 distributions in which the distributing and controlled corporations are REITs immediately after the distribution and remain REITs for two years thereafter) should be amended to match the exception codified in Section 355(h)(2)(A) (which requires only that the distributing and controlled corporations are REITs immediately after the distribution), or the above temporary regulation should be amended to exempt inadvertent REIT terminations.

- E. The definition of “converted property” in the 2016 Proposed Regulations should be adopted, subject to minor clarifications.
- F. If the government believes that the regulations may properly permit REIT elections otherwise barred by Section 856(c)(8), at the cost of a toll charge on “converted property,” the regulations should clearly state as much.

We appreciate your consideration of our comments. Please let us know if you would like to discuss these matters further or if we can assist you in any other way.

Respectfully submitted,



Michael S. Farber
Chair

Attachment

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