Internal Revenue Service

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Department of the Treasury
Washington, DC 20224

Third Party Communication: None
Date of Communication: Not Applicable

Person To Contact:
, ID No.
Telephone Number:

Refer Reply To:
CC:INTL:B01
PLR-117376-06

Date:
November 30, 2006

In Re:

Legend

Taxpayer =
Company A =
Company B =

Dear :

This responds to your letter dated March 7, 2006, requesting a ruling concerning Article 10(3) (Dividends) of the United States-United Kingdom income tax treaty (the "Treaty"), as supplemented by a letter dated November 3, 2006.

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

FACTS

The Taxpayer is a U.K. corporation whose principal class of shares is traded on the London Stock Exchange. The Taxpayer holds 100 percent of the issued and outstanding capital stock of Company A, a domestic corporation, and has directly held

such stock for a period of more than 12 months. The Taxpayer will hold 100 percent of the issued and outstanding capital stock of Company B, a U.K. corporation, as a result of a proposed transaction. The Taxpayer plans to transfer Company A's stock to Company B in exchange for shares of Company B. Company B will make an election under Treas. Reg. section 301.7701-3(c) to be disregarded as an entity separate from its owner (i.e., the Taxpayer) for U.S. federal income tax purposes. Following the transfer, Company B will hold 100 percent of the issued and outstanding capital stock of Company A. It is anticipated that Company A will declare a dividend on a date less than 12 months after the date of the transfer.

RULING REQUESTED

For purposes of the 12-month stock ownership requirement in Article 10(3)(a) of the Treaty, the Taxpayer is the direct owner of shares in Company A that are owned by Company B, a wholly owned, disregarded entity of the Taxpayer.

LAW

Article 10(1) of the Treaty provides that dividends paid by a company that is a resident of a Contracting State to a resident of the other Contracting State may be taxed in that other State.

Article 10(2) provides that the dividends may also be taxed in the Contracting State of which the company paying the dividends is a resident, but if the dividends are beneficially owned by a resident of the other Contracting State, the tax so charged may not exceed certain limits.

Notwithstanding paragraph 2, paragraph 3 of Article 10 provides that dividends shall not be taxed in the Contracting State of which the company paying the dividends is a resident if the beneficial owner of the dividends is a resident of the other Contracting State and certain other requirements are satisfied.

Article 10(3)(a) provides that dividends are not taxable in the source State if the beneficial owner is a company resident in the other Contracting State that has owned shares representing 80 percent or more of the voting power of the company paying the dividends for a 12-month period ending on the date the dividend is declared and certain other requirements are satisfied.

ANALYSIS

Under Article 10(3)(a), the Taxpayer is required to have directly owned shares representing 80 percent or more of the voting power of Company A for a 12-month period ending on the date the dividend is declared. While the Technical Explanation to Article 10(3)(a) clarifies that the term "owned" includes only direct ownership, it does not define what types of ownership will be considered direct ownership. Under paragraph 2

of Article 3 (General Definitions), unless the context otherwise requires or the competent authorities agree on a common meaning, an undefined term will have the meaning that it would have under the law of the State applying the Treaty, with any meaning under the applicable tax laws of that State prevailing over a meaning given to the term under other laws. Thus, the term "directly owned" will have the meaning that it has under U.S. law, unless the context otherwise requires.

Domestic law clearly contemplates that the sole owner of a disregarded entity is considered to own the assets of the disregarded entity for federal tax purposes. Under Treas. Reg. section 1.367(e)-1(b)(2), "stock or securities owned by or for an entity that is disregarded as an entity separate from its owner (disregarded entity) under section 301.7701-3 of this chapter are owned directly by the owner of such disregarded entity." Accordingly, for purposes of the 12-month stock ownership requirement in Article 10(3)(a) of the Treaty, the Taxpayer will be considered to own directly the shares of Company A that are owned by Company B, a wholly owned, disregarded entity of the Taxpayer, unless the context otherwise requires.

As noted above, Article 3(2) provides that an undefined term will have the meaning that it would have under the law of the State applying the Treaty, unless the context otherwise requires. The Technical Explanation to Article 3 explains as follows:

> The reference in both paragraphs 1 and 2 to the "context otherwise requir[ing]" a definition different from the treaty definition, in paragraph 1, or from the internal law definition of the Contracting State whose tax is being imposed, under paragraph 2, refers to a circumstance where the result intended by the Contracting States is different from the result that would obtain under either the paragraph 1 definition or the statutory definition. Thus, flexibility in defining terms is necessary and permitted.

Therefore, to determine whether the "context" requires a definition of direct ownership that is different from that which is found in domestic law, it is necessary to determine whether the result that the Contracting States intended would be obtained under the provisions of Article 10(3).

The Joint Committee on Taxation Explanation of the Treaty discusses the rationale for the zero rate of withholding with respect to dividends, stating:

> If the dividend-paying corporation is at least 80-percent owned by the dividend-receiving corporation, it is arguably appropriate to regard the dividend-receiving corporation as a direct investor (and taxpayer) in the source country in this respect, rather than regarding the dividend-receiving corporation as having a more remote investor-type interest warranting the imposition of a second-level source-country tax.

Thus, the purpose of Article 10(3)(a) was to eliminate the withholding tax on certain direct investment. As noted above, the threshold for being considered a direct investor under Article 10(3)(a) is direct ownership of at least 80 percent of the payor's voting shares for the 12-month period ending on the date the dividend is declared.

In the case at hand, defining the term "direct ownership" to include stock directly owned by the Taxpayer's disregarded entity is not contrary to the purpose of Article 10(3)(a)--the elimination of the withholding tax on direct investment--and does not cause a result that was not intended by the Contracting States. Accordingly, on the facts presented, the context does not require "direct ownership" to be defined in a manner that differs from domestic law.

Based solely on the information submitted and the representations made by the Taxpayer, we conclude that, for purposes of the 12-month stock ownership requirement in Article 10(3)(a) of the Treaty, the Taxpayer is the direct owner of shares in Company A that are owned by Company B, a wholly owned, disregarded entity of the Taxpayer.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. In particular, no opinion is expressed as to whether either the Taxpayer or Company B meets other conditions required to claim benefits under Article 10(3) of the Treaty.

This ruling is directed only to the taxpayer requesting 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 your authorized representative.

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

Sincerely,

Elizabeth U. Karzon
Chief, Branch 1
Office of Associate Chief Counsel
(International)