

Internal Revenue Service

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LEGEND

Taxpayer =

Products =

Non-LIFO Inventories =

Foreign Parent =

Report =

Pension Plan =

Pension Plan Assets =

Pension Plan Liabilities =

Section A =

Dear :

This is in response to your authorized representatives' letter and submissions of November 28, 2017 in which they requested, on your behalf, a ruling under section 472(e) of the Internal Revenue Code concerning whether operating assets used in

foreign operations constitute 30 percent or more of total operating assets of the consolidated group (the "30 percent test") under Rev. Rul. 78-246, 1978-1 C.B. 146. We are pleased to address your concerns.

FACTS

The information submitted indicates that Taxpayer is a wholesale distributor of Products. Taxpayer is a United States parent and as such files a consolidated U.S. Corporate Income Tax Return on behalf of itself and its U.S. subsidiaries. For U.S. tax purposes, Taxpayer and its U.S. subsidiaries use the Last-In First-Out (LIFO) inventory method for all inventories other than Non-LIFO Inventories.

Foreign Parent is an international business operating in multiple foreign regions and in the United States. Foreign Parent prepares its consolidated financial statements based on the International Financial Reporting Standards (IFRS). Foreign Parent operates the United States region through its subsidiary, Taxpayer.

The Report provides that Foreign Parent operates Pension Plan in a number of overseas locations. The Report further provides that the asset recognized on the balance sheet, as it relates to the Pension Plan, is the Pension Plan Assets less the Pension Plan Liabilities on the balance sheet date, which is a net value. However, the Pension Plan Assets and the Pension Plan Liabilities are separately stated at gross values in Section A of the notes to the consolidated financial statements of the Report. The notes to the consolidated financial statements, including Section A, are presented together and accompany the income statement in the Report.

Taxpayer operates Pension Plan in the United States. Taxpayer also operates a nonqualified deferred compensation plan (NQDC Plan). Unlike the Pension Plan Assets and Pension Plans Liabilities, which are presented in the Report as a net value on the balance sheet, the assets and the liabilities related to the NQDC Plan are presented in the Report at gross values on the balance sheet.

REQUEST

Taxpayer requests that, for purposes of the 30 percent test under Rev. Rul. 78-246, the asset valuation of Foreign Parent's operating assets may be determined using the gross fair values, rather than the net value, of the Pension Plan.

LAW

Section 472(c) provides that a taxpayer that elects to use the LIFO inventory method for federal income tax purposes must establish to the satisfaction of the Secretary that it has used no method other than LIFO in inventorying goods specified in its LIFO election to ascertain income, profit, or loss for the first taxable year for which

the method is to be used, for the purpose of a report or statement covering such taxable year to shareholders, partners, or other proprietors, or to beneficiaries, or for credit purposes.

Section 472(e)(2) imposes a requirement similar to that contained in section 472(c) for taxable years subsequent to the year of the LIFO election and provides that the taxpayer may be required to discontinue the use of the LIFO inventory method if this requirement is violated.

Section 472(g) provides that all members of the same group of financially related corporations are treated as a single taxpayer for purposes of the LIFO conformity requirement of sections 472(c) and (e)(2). The term “group of financially related corporations” means any affiliated group as defined in section 1504(a), determined by substituting “50 percent” for “80 percent” each place it appears and without regard to section 1504(b), and any other group of corporations that consolidate or combine for purposes of financial statements.

Section 1.472-2(e)(3) of the Income Tax Regulations provides specific rules related to the exception to the LIFO conformity requirement for supplemental or explanatory information.

Section 1.472-2(e)(3)(i) provides that information reported on the face of a taxpayer’s financial income statement for a taxable year is not considered a supplement to or explanation of the taxpayer’s primary presentation of the taxpayer’s income, profit, or loss for the taxable year in credit statement or financial reports. For purposes of paragraph (e)(3) of this section, the face of an income statement does not include notes to the income statement presented on the same page as the income statement, but only if all notes to the financial income statement are presented together.

Section 1.472-2(e)(3)(ii) provides, in part, that information reported in notes to a taxpayer’s financial income statement is considered a supplement to or explanation of the taxpayer’s primary presentation of income, profit, or loss for the period covered by the income statement, and therefore is considered in determining whether the LIFO conformity requirement is met, if all the notes to the financial income statement are presented together and if they accompany the income statement in a single report.

Rev. Rul. 78-246 holds that it is inappropriate to impose the LIFO method of inventory valuation upon a foreign parent corporation with respect to the inventory of any subsidiary that uses the LIFO method of inventory valuation for federal income tax purposes when the group is engaged in substantial foreign operations. Accordingly, the LIFO method of inventory valuation need not be used in the consolidated financial statements of the foreign parent corporation, provided that the foreign parent owns, either directly or through members of its consolidated group, operating assets of substantial value which are used in foreign operations. In making this determination,

operating assets regardless of their physical location will be treated as used in foreign operations if they are owned by, and used in the business of, corporations that: (1) are members (including the parent) of the consolidated group; (2) are foreign corporations; (3) do not use the LIFO method of accounting for Federal income tax purposes; and (4) engage in a business outside the United States. Operating assets for purposes of this test are all the assets necessary for the conduct of an active operating company. Operating assets will be considered to be of substantial value if they constitute 30 percent or more of the total operating assets of the consolidated group. This determination will be made annually and normally will be made on the basis of the asset valuation reflected in the consolidated financial statements of the group for the year.

Rev. Rul. 78-246 further holds that whether a foreign parent is engaged in substantial foreign operations will be decided on the basis of all the facts and circumstances presented if the consolidated group does not satisfy the foregoing 30 percent test.

ANALYSIS

Taxpayer is a domestic parent of domestic subsidiaries. Taxpayer files a consolidated U.S. federal income tax return for itself and its domestic subsidiaries. Taxpayer uses the LIFO inventory method. Taxpayer has a foreign parent who does not file its financial statements using a LIFO inventory method. In Foreign Parent's financial statements, the Pension Plan is reported as a net value on the face of the financial statements and at gross values in attached notes to the financial statements. Foreign Parent reports the NQDC Plan assets and liabilities separately at gross values on the face of its consolidated financial statement.

For purposes of establishing that the LIFO conformity requirements are met, information reported in notes to a taxpayer's financial income statement are considered a supplement to or explanation of the taxpayer's primary presentation for the period covered if all notes to the financial income statement are presented together and if they accompany the income statement in a single report.

Moreover, subject to conditions set forth therein, Rev. Rul. 78-246 provides relief from the use of LIFO method of inventory valuation in the consolidated financial statements of the foreign parent corporation engaged in "substantial foreign operations." Under Rev. Rul. 78-246, whether a foreign parent corporation is engaged in substantial foreign operations is made annually and normally will be made on the basis of the asset valuation reflected in the consolidated financial statement of the group for the year. Therefore, the asset valuation reflected in the consolidated financial statement of the group includes any supplemental and explanatory information as described in section 1.472-2(e)(3)(ii).

Accordingly, in the instant case, because the information reported in notes to the Report, including Section A, are presented together and accompany the income statement in a single report, the information contained in Section A concerning the gross values of the Pension Plan is considered a supplement to or explanation of the consolidated financial statement of the group for the period covered by the Report for purposes of section 1.472-2(e)(3).

CONCLUSION

Based on the information provided and the representations furnished, in determining whether foreign operating assets constitute 30 percent or more of the total operating assets of the consolidated group under Rev. Rul. 78-246, the gross asset valuation reflected in Section A constitutes supplemental and explanation information within the meaning of section 1.472-2(e)(3).

This letter ruling is based on the facts and representations provided by the Taxpayer and limited to the matters specifically addressed. No opinion is expressed as to whether Taxpayer meets the 30 percent test as stated in Rev. Rul. 78-246, or whether Taxpayer has otherwise complied with the conformity requirements of section 472(c) and (e)(2) of the Code in inventorying its goods to ascertain income, profit, or loss for the purposes of a report or statement (covering the taxable year for which the LIFO method is used) to shareholders, partners, other proprietors, or beneficiaries, or for credit purposes.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representatives.

Because it could help resolve federal tax issues, a copy of this letter should be maintained with Taxpayer's permanent records.

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Internal Revenue Code provides that it may not be used or cited as precedent.

Sincerely,

Christina Morrison
Senior Technician Reviewer Branch 6
Office of Associate Chief Counsel
(Income Tax & Accounting)