International Multifoods Corp. v. Commissioner, 108 T. C. 579 (1997)

Losses from the sale of noninventory personal property are generally sourced at the residence of the seller, consistent with the sourcing of gains.

Summary

International Multifoods Corporation sold its stock in a Brazilian subsidiary, Paty S. A. , at a loss, which it claimed as a U. S. source loss for foreign tax credit purposes. The IRS argued the loss should be sourced abroad. The Tax Court, applying section 865 of the Internal Revenue Code, ruled that losses on noninventory personal property sales should generally be sourced at the seller's residence, mirroring the treatment of gains. This decision was influenced by the legislative intent to apply residence-based sourcing rules consistently, despite the absence of final regulations at the time of the case.

Facts

International Multifoods Corporation (IMC) and its subsidiary, Damca International Corp. , owned all the stock in Multifoods Alimentos, Ltda. (MAL), which in turn owned 85% of Paty S. A. -Produtos Alimenticios, Ltda. , a Brazilian pasta manufacturer. IMC acquired the remaining 15% of Paty's stock by February 1982. In 1984, MAL distributed its Paty stock to IMC and Damca upon liquidation. On March 30, 1987, IMC and Damca sold their Paty stock to Borden, Inc. , and its subsidiary for a loss of $3,922,310. IMC reported this loss as a U. S. source loss for foreign tax credit purposes under section 904(a) of the Internal Revenue Code.

Procedural History

The IRS issued a notice of deficiency to IMC for the taxable years ending February 28, 1987, and February 29, 1988. IMC paid the deficiencies and filed a petition with the U. S. Tax Court, claiming an overpayment. The court had previously disposed of several issues in the case, leaving the sourcing of the Paty stock loss as the sole remaining issue. This issue was severed pending proposed regulations on stock loss sourcing, but due to delays in finalizing these regulations, the court decided to rule on the issue.

Issue(s)

1. Whether the loss realized by IMC on the sale of its Paty stock should be sourced in the United States for purposes of computing IMC's foreign tax credit limitation under section 904(a) of the Internal Revenue Code.

Holding

1. Yes, because losses from the sale of noninventory personal property are generally sourced at the residence of the seller, consistent with the sourcing of gains under

© 2025 SCOTUSreports.com. All rights reserved. | 1

section 865(a) of the Internal Revenue Code.

Court's Reasoning

The court applied section 865 of the Internal Revenue Code, which generally sources income from the sale of noninventory personal property at the residence of the seller. The court interpreted section 865(j)(1), which directs the Secretary to promulgate regulations on loss sourcing, as indicating Congress's intent to apply residence-based sourcing to losses as well as gains. The court relied on the legislative history of section 865, which emphasized that the seller's residence is typically where the economic activity generating the income occurs. The absence of final regulations did not prevent the court from applying the statutory purpose of section 865, as the proposed regulations, if finalized, would have sourced IMC's loss in the U. S. The court rejected the IRS's argument that pre-1987 regulations under sections 861 and 862 should apply, noting these were superseded by the Tax Reform Act of 1986.

Practical Implications

This decision clarifies that losses from the sale of noninventory personal property should generally be sourced at the seller's residence, aligning loss sourcing with gain sourcing under section 865. Tax practitioners should consider this ruling when advising clients on the sourcing of losses for foreign tax credit purposes, especially in the absence of final regulations. The decision may influence how multinational corporations structure their investments and sales of foreign subsidiaries to optimize their tax positions. Subsequent cases and regulations should be monitored for any modifications to this general rule, as the court acknowledged that exceptions might be necessary to prevent abuse.

© 2025 SCOTUSreports.com. All rights reserved.