NATIONAL ASSOCIATION OF
REAL ESTATE INVESTMENT TRUSTS®

March 5, 2002

VIA HAND DELIVERY AND E-MAIL

The Honorable Charles O. Rossotti
Commissioner of the Internal Revenue
CC:ITA:RU (REG-126485-01)
Courier's Desk
Internal Revenue Service
1111 Constitution Avenue, N.W.
Washington, D.C. 20044

RE: Certain Corporate Reorganizations Involving Disregarded Entities

Dear Commissioner Rossotti:

On behalf of the National Association of Real Estate Investment Trusts® ("NAREIT"), we wish to thank you for providing this opportunity to comment on Proposed Treasury Regulation section 1.368-2(b)(1), relating to certain corporate reorganizations involving disregarded entities, issued on November 15, 2001 (the "2001 Proposed Regulations").

The 2001 Proposed Regulations replaced proposed regulations issued on May 16, 2000 (the "2000 Proposed Regulations"). As you may recall, NAREIT and The Real Estate Roundtable ("RER") made written submissions and testified before the Internal Revenue Service (the "Service") and Treasury Department on the 2000 Proposed Regulations. This letter gratefully acknowledges the efforts of the Treasury and the Service in resolving most of the concerns that NAREIT and RER raised and offers two suggestions for amendments to the 2001 Regulations before they are finalized.

NAREIT is the national trade association for real estate investment trusts ("REITs") and publicly traded real estate companies. Members of NAREIT are REITs and publicly traded businesses that own, operate and finance income-producing real estate, as well as those firms and individuals who advise, study and service those businesses. REITs are companies the income and assets of which are mainly connected to income-producing real estate. NAREIT's membership includes over 200 REITs and publicly traded real estate companies that own over $250 billion of real estate assets, as well as over 2,000 industry professionals who provide a range of legal, investment, financial and accounting-related services to these companies.

I. EXECUTIVE SUMMARY

To begin with, NAREIT would like to thank the Treasury Department and the IRS for incorporating most of NAREIT and RER's comments in the 2001 Proposed Regulations. NAREIT respectfully asks the Service and Treasury to consider incorporating the following points in the final regulations. First, it would be helpful to mention a REIT in at least one of the examples (either in the regulations explicitly or in the preamble to the regulations) dealing with the forward merger of a target corporation into a disregarded entity. Second, NAREIT's respectfully requests the Service and Treasury Department to permit the reverse subsidiary merger of a qualified REIT subsidiary into a target corporation when the potential for a divisive transaction does not exist.

II. BACKGROUND - THE 2000 PROPOSED REGULATIONS

A. Merger of a Disregarded Entity into an Acquiring Corporation

In order for a merger to qualify as a reorganization under section 368(a)(1)(A) of the Code[1] (an "A Reorganization"), the 2000 Proposed Regulations provided that the merger must, by operation of the merger statute of the relevant jurisdiction, result in one corporation with a separate tax existence acquiring the assets of the merging corporation and the merging corporation ceasing to exist. Thus, under the 2000 Proposed Regulations, the merger of a Disregarded Entity (a "DRE") such as a qualified REIT subsidiary ("QRS"),[2] a qualified subchapter S subsidiary,[3] a single member limited liability company ("LLC") or any other entity that is disregarded as separate from its owner,[4] into an acquiring corporation could not qualify as an A Reorganization. The Preamble to the 2000 Proposed Regulations provided that such a transaction could qualify as a reorganization under section 368(a)(1)(C), (D), or (F) provided all the applicable requirements of the Code were met (including the liquidation of the DRE's corporate owner (the "Owner")), or as a transaction under section 351.

B. Merger of a Target Corporation into a Disregarded Entity

The 2000 Proposed Regulations further provided that the merger of a target corporation into a DRE that does not lose its status as a DRE as a result of the transaction would not qualify as an A Reorganization. The Preamble to the Proposed Regulations, however, provided that such a

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1 All references to the "Code" are to the Internal Revenue Code of 1986 (as amended) and, unless otherwise stated, all references to sections are references to sections of the Code.

2 Section 856(i)(2).

3 Section 1361(b)(3)(B).

4 Treas. Reg. § 301.7701-2(c)(2).

transaction could qualify as a reorganization, under section 368(a)(1)(C), (D), or (F), or as a transaction under section 351, if all the relevant requirements of the Code were met.

III. NAREIT/RER COMMENTS ON THE 2000 PROPOSED REGULATIONS

On August 4, 2000, NAREIT and RER submitted comments on the 2000 Proposed Regulations, and on August 8, 2000, Stefan F. Tucker testified on behalf of NAREIT and RER before the Treasury Department and the Service. In general, our comments agreed with the Service's treatment of a merger of a disregarded entity into an acquiring corporation when the potential for a divisive transaction existed. We disagreed, however, with the treatment of a merger of a target corporation into a disregarded entity under the 2000 Proposed Regulations.

We recommended that the 2000 Proposed Regulations be changed to reflect the view of the Service, as manifested through prior private letter rulings,[5] which treated a merger of a target corporation into a disregarded entity with a corporate owner as a merger into the owner. In our view, the 2000 Proposed Regulations took an unnecessarily formalistic approach and prevented taxpayers from engaging in legitimate business transactions that were motivated primarily or entirely by non-tax considerations.[6]

We agreed with the Service's proposed treatment of a merger of a DRE into an acquiring corporation when the potential for a divisive transaction existed. In our view, the merger of a DRE into an acquiring corporation should not qualify as an A Reorganization because the DRE's Owner does not merge into the acquiring corporation and the DRE's Owner does not cease to exist as a result of the merger. Nevertheless, we requested guidance on the federal income tax treatment of a reverse triangular merger when the potential for a divisive transaction does not exist.

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5 See PLR 8903074 (Oct. 26, 1988) holding that a merger of a target REIT into a wholly-owned acquisition subsidiary of an acquiring REIT was a valid reorganization under section 368(a)(1)(A) in which the target REIT and the acquiring REIT are each "a party to the reorganization"; PLR 9411035 (Dec. 20, 1993) holding that a merger of a subsidiary REIT into a qualified REIT subsidiary of the parent REIT would be treated as a merger and liquidation of the subsidiary REIT into the parent REIT; and PLR 9512020 (Dec. 29, 1994) holding that a merger of a target into a qualified REIT subsidiary will be treated as if the target merged into the parent REIT for federal income tax purposes.

6 Our recommendation was consistent with the recommendations of the American Bar Association Section of Taxation and the New York State Bar Association Tax Section. See American Bar Association, Section of Taxation, Comments on Guidance Needed Concerning the Treatment of Mergers Involving Single Member Entities Owned by Corporation submitted July 28, 1998, 98 TNT 151-11 (Aug. 6, 1998) and New York State Bar Association, Tax Section, Report on Reorganizations Involving Disregarded Entities, 98 TNT 171-12 (Aug. 27, 1998).

IV. 2001 PROPOSED REGULATIONS

NAREIT is grateful that the Service incorporated most of NAREIT's comments in the 2001 Proposed Regulations. The 2001 Proposed Regulations permit the merger of a corporation into a DRE to qualify as a good A Reorganization by including, within the definition of a statutory merger or consolidation under section 368(a)(1)(A), a transaction, effected pursuant to the laws of any State, in which all the assets and liabilities of a "combining unit" (comprised of a business entity which is taxed as a corporation (a "combining entity") and all DREs owned by that combining entity (together, the "transferor unit")) become the assets and liabilities of another combining unit and the combining entity of the transferor unit ceases its separate legal existence for all tax and non-tax purposes.

Example 2 of the 2001 Proposed Regulations provides guidance for taxpayers on how the mechanics of the Regulations are intended to apply to a "forward" merger of a target corporation into a DRE. Under the 2001 Proposed Regulations, the target corporation constitutes a combining entity (and, together with all the DREs owned by that target, a combining unit). When the Target merges with and into the DRE of an acquiring parent in a forward merger, all the assets and liabilities of the transferor unit (the target) become assets and liabilities of the transferee unit (comprised of the acquiring parent and all DREs owned by the acquiring parent), and the target (the combining entity of the transferor unit) ceases its separate legal existence for all tax and non-tax purposes.

It is our understanding that the 2001 Proposed Regulations permit a forward merger of a C corporation, or a target REIT, into a QRS of an acquiring REIT. Further, the merger of a target REIT into a QRS of an acquiring REIT may qualify as a good forward triangular merger under section 368(a)(2)(D) if the target shareholders receive stock of a corporation that "controls" the acquiring REIT. While the 2001 Proposed Regulations permit forward mergers into a DRE, Example 5 of the Regulations holds that the reverse merger of an acquiring parent's DRE into a target corporation cannot qualify as an A Reorganization.

We understand the 2001 Proposed Regulations were drafted to protect against the potential for a divisive A Reorganization. In the ordinary case when a target corporation merges with and into a DRE of an acquiring parent in a forward subsidiary merger, there is no divisive potential because the assets of the target corporation become assets of the acquiring parent. In the reverse case when the DRE merges with and into the target corporation, the assets and liabilities of the DRE (which are deemed to be held by the parent for tax purposes) become the assets and liabilities of the target corporation, which continues in existence after the merger. Such a merger is potentially divisive because the assets of the acquiring parent can be transferred to the target corporation, the stock of which may remain at least partially owned by the target shareholders.

The 2001 Proposed Regulations guard against the possibility of a divisive A Reorganization by providing that a merger will not qualify under section 368(a)(1)(A) unless all the assets and liabilities of the transferor unit become assets and liabilities of the transferee unit, and the target ceases its legal existence for all purposes. The Service's concern about divisive reorganizations can be traced to transactions such as those discussed in Revenue Ruling 2000-5,[7] in which the Service held that a state law merger did not qualify as an A Reorganization when the acquiring parent did not acquire all of the target's assets and the target continued in existence.

The Service's concern over the divisive potential in a reverse merger does not apply, however, to a reverse merger of a QRS with and into a target corporation when the target survives the merger and becomes a QRS of the REIT, because: (i) the target C corporation must be 100% held by a REIT after the reverse merger;[8] and (ii) by operation of law, the target C corporation will be disregarded for federal income tax purposes. As discussed below, the acquisition of a C corporation by a REIT is treated as a stock acquisition followed immediately by a section 332 liquidation; thus, the assets of the DRE merger subsidiary (which are deemed to be held by the acquiring parent for federal income tax purposes) remain assets and liabilities of the acquiring parent. The target, in form, continues its existence, but for all federal income tax purposes it is treated as having ceased to exist.

V. NAREIT COMMENTS ON THE 2001 PROPOSED REGULATIONS

In general, we are extremely pleased with the 2001 Proposed Regulations and thank the Treasury Department for responding favorably to most of the comments in NAREIT and the RER's August 4, 2000 submission. In particular, we believe that the 2001 Proposed Regulations' treatment of the merger of a target corporation into a disregarded entity as an A Reorganization is the correct result and will make it more efficient for the REIT industry to utilize tax-free reorganizations.

Nevertheless, please consider the following two comments in finalizing the 2001 Proposed Regulations. First, the 2001 Proposed Regulations could be clarified by mentioning a REIT in at least one of the examples dealing with the forward merger of a target corporation into a disregarded entity. We believe such an addition would provide additional certainty to the treatment of a target corporation into a DRE that is a QRS. If the examples cannot be revised, we would appreciate if, at the very least, you would reference this comment in the preamble to

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7 2000-5 I.R.B. 436.

8 Section 856(i). If less than 100% of the stock of the target is acquired by the REIT in a reverse merger, then the REIT's ownership of the target must meet the stringent asset tests of section 856(c)(4)(B): no more than 25% of a REIT's assets by value can be corporate stock or securities [section 856(c)(4)(B)(i)]; a REIT may not hold more than 10% of the vote or value of any one issuer and such holding cannot be more than 5% of the total value of the REIT's assets [section 856(c)(4)(B)(iii)], unless the issuer is a taxable REIT subsidiary ("TRS"); and no more than 20% of the value of a REIT's assets can be represented by stock or securities in TRSs [section 856(c)(4)(B)(ii)]. Furthermore, in cases when less than 100% of the target is acquired, the target does not become a section 856(i) QRS and thus is not deemed automatically liquidated pursuant to section 332; the analysis that generally applies to acquisitions by C corporations of other C corporations would apply in this instance.

the final regulations and indicate that the forward merger of a target corporation into a QRS of a REIT would qualify as an A Reorganization under circumstances similar to the LLC examples in the regulations.

Further, in NAREIT's opinion the Service and Treasury Department should reconsider the scope of Example 5 of the 2001 Proposed Regulations and its application to a reverse subsidiary merger of a QRS into a target corporation.

The practical effect of Example 5 of the 2001 Proposed Regulations is to prevent REITs from effecting tax-free reorganizations using reverse subsidiary mergers. Reverse subsidiary mergers are the preferred form of corporate reorganization because they allow the target to maintain continuity of corporate existence, and thus often minimize the need for the target to obtain consents from third parties to effect the merger. This is significant because, in addition to creditors, REITs often have contractual parties, landlords, licensors, licensees and other third parties whose consent to a forward (but not a reverse) merger needs to be obtained.

If, as the Service asserts, the merger of a QRS into a target C corporation or REIT is not eligible for qualification as an A Reorganization, the only tax-free alternatives available to a REIT that wishes to undertake an acquisitive reverse subsidiary merger are (1) a transaction that would qualify as a section 351 exchange, or (2) a reorganization under section 368(a)(1)(C). A reverse merger will not typically qualify as tax-free under section 351 as the target REIT will almost always be smaller, or the same size as, the acquiring REIT, and a reverse merger will often fail to qualify under section 368(a)(1)(C) due to the large amount of debt on the balance sheet of the target REIT which eliminates the ability of the acquiring REIT to use any "boot" in the reorganization. Thus, the consequence, albeit unintended, of Example 5 of the 2001 Proposed Regulations, is to place significant obstacles in the way of REITs that wish to engage in the preferred form of tax-free reorganization, the reverse subsidiary merger.

It should be noted that, due to the idiosyncrasies of REIT taxation, the direction of the merger between a target corporation and a QRS has no effect on the resulting tax structure of the merged entity. Whether or not the target survives the merger, the surviving entity will be a DRE of the REIT for tax purposes. Unlike situations outside the REIT context, a target corporation in a reverse subsidiary merger is treated as liquidating as of the time of the acquisition by the REIT and then is reconstituted as a QRS.[9] In the ordinary case, when a DRE reverse merges with and into a target corporation, the target corporation survives the merger so that the resulting structure comprises two corporations - the acquiring parent and the target corporation, each recognized as a separate corporation for tax purposes. When a QRS of a REIT merges with and into a target corporation, however, the surviving target corporation becomes, by operation of section 856(i), a

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See H.R. Rep. No. 220, 105th Cong., 1st Sess. 698 (1997). Unlike a reverse subsidiary merger in the non-REIT context, in order to maintain REIT status, the REIT must distribute the target corporation's "C corporation" earnings and profits by the end of the year of the merger. Accordingly, there is even less opportunity for abuse in the REIT context than in the non-REIT context.

new QRS treated as a DRE for tax purposes. Accordingly, from a tax standpoint, the end result of a merger of a QRS with a target corporation is identical regardless of the direction of the merger. As noted in NAREIT's and RER's submission, the ability to qualify as an A Reorganization should not hinge on the direction of the merger when the end result of a forward or reverse merger of a DRE is the same.

NAREIT submits that the above analysis is consistent, in principle, with the current structure of the 2001 Proposed Regulations. As noted above in our discussion of the 2001 Proposed Regulations, Proposed Regulation section 1.368-2(b) includes within the definition of a statutory merger or consolidation under section 368(a)(1)(A), a transaction, effected pursuant to the laws of any State, in which all the assets and liabilities of a combining unit (the transferor unit) become the assets and liabilities of another combining unit (the transferee unit), and the combining entity of the transferor unit ceases its separate legal existence for all purposes. As there is nothing in the 2001 Proposed Regulations that specifies the direction of the merger, a merger of a QRS with and into a target corporation could be brought within the language of the 2001 Proposed Regulations. When a QRS reverse merges into a target corporation, the assets of the target combining unit become the assets of the acquiring parent's combining unit and the target, which is deemed liquidated and reconstituted as a new QRS, does in fact cease its separate existence for tax purposes.

Nevertheless, Example 5 of the Regulations holds that the reverse merger of a DRE into a target corporation does not satisfy the technical requirements of the Proposed Regulations. Example 5 assumes that the acquiring parent and its DRE are the transferor unit. It then states that the merger fails to qualify because all the assets of the transferor unit do not become assets of the target. Nothing in Example 5 or the Regulations, however, requires the DRE's Owner and the DRE to be the "transferor unit." It is clear, from a tax standpoint, that following a merger with a QRS, the surviving target's assets and liabilities become the assets and liabilities of the acquiring parent's transferee unit, and therefore, in Example 5, the surviving corporation is more appropriately treated as the transferor unit. Example 5 further states that the merger fails to meet the requirements of the Regulations because the merger subsidiary that is a DRE does not constitute a combining entity. Again, this analysis is premised on the supposition that the acquiring parent and its DRE are the transferor unit. In the case of the reverse merger of a QRS with and into a target corporation, when the target corporation ceases its separate tax existence as a consequence of the merger, it is the target corporation that is more appropriately considered to be the transferor unit.[10]

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[10] We note that the current Prop. Treas. Reg. section 1.368-2(b)(1)(ii)(B) provides that the transferor combining entity must cease its legal existence for *all* purposes. However, in our opinion, the 2001 Proposed Regulations are over-broad in this respect. We suggest that they could be amended to read as follows: "The combining entity of each transferor unit either ceases its separate legal existence, or by operation of law or an election effective at the effective time becomes a disregarded entity of the transferee unit." A conforming amendment would need to be made to Treasury Regulation Section 1.368-

We further submit that allowing a reverse merger of a QRS into a target corporation to qualify as an A Reorganization is consistent with the Service's treatment of other stock and asset acquisitions.

The Service has indicated a willingness to rule in a number of private letter rulings that, on acquisition of a C corporation by a REIT, the C corporation and its pre-existing subsidiaries automatically become QRSs through a deemed tax-free section 332 liquidation and recontribution of assets to the new QRS. This transformation occurs without actual liquidation-reformation.[11] We agree with this analysis and, if the reverse merger of a QRS otherwise fails to meet the requirements of an A Reorganization, the same consequences should still obtain.[12] It is similarly well established that the reverse merger of a transitory corporate subsidiary of an acquiring parent will generally be treated as a stock purchase by the parent. In Revenue Ruling 67-448, [13] for example, a reverse merger of a transitory corporation into a target with the shareholders in the target receiving voting stock of the acquiring parent in exchange for at least 80% of the target's voting stock qualified as a good section 368(a)(1)(B) reorganization. The proper analysis of a merger of a transitory QRS with and into a target should therefore be that it is an acquisition of the target corporation stock followed immediately by a deemed liquidation of the target into the acquiring REIT.

While the acquisition of target stock followed by a prompt liquidation of the target into the acquiring parent pursuant to a single plan can qualify as a tax-free asset acquisition under section 368(a)(1)(C),[14] the Service also recently held, in Revenue Ruling 2001-46,[15] that if a newly formed wholly owned subsidiary of an acquiring corporation merges into a target corporation,

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2(b)(1)(iii) that the target which can now be a disregarded entity of the transferee unit, and all intervening disregarded entities between it and the transferee combining unit, be domestic. The above amendment could be illustrated by a new example in which an acquiror REIT uses a QRS to reverse merge into a target corporation wherein the target survives as a QRS of the REIT, and the whole transaction qualifies as an A Reorganization.

11 For an indication of the Service's ruling position, see PLR 9330022 (April 30, 1993); PLR 9421034 (Feb 28, 1994); PLR 9609024 (March 1, 1996); PLR 9612024 (March 22, 1996); PLR 9620031 (May 17, 1996); PLR 9625024 (June 21, 1996); and PLR 9717036 (April 25, 1997) (see above notes 8 and 9).

12 If the acquisition is taxable, then the ordinary analysis of the Service (set out in the PLRs cited in note 11 above) will apply. The transaction will be viewed as a taxable stock purchase followed by a section 332 liquidation. As a consequence, the acquiring REIT will take a carryover basis in the assets of the target and the acquisition of target stock will be taxable to target shareholders.

13 Revenue Ruling 67-448, 1967-2 CB 144.

14 See Revenue Ruling 67-274, 1967-2 C.B. 141.

15 Revenue Ruling 2001-46, 2001-42 IRB 321.

followed immediately by the upstream merger of the target corporation into the acquiring corporation, the transaction can be treated as a single statutory merger of the target corporation into the acquiring corporation that qualifies as a good A Reorganization. If the Service is prepared to consider that this series of separate steps, as part of an integrated plan, can be treated as an A Reorganization, the Service should also reach the same result when it is achieved by the simple expedient of merging a QRS into a target C corporation, a transaction correctly analyzed as an acquisition of target stock followed by a subsequent deemed liquidation of the target into the acquiring REIT parent and the reformation of the assets into a QRS. By operation of the Service's own rulings, the acquiring REIT parent has acquired, in a single transaction, the assets of the target corporation in a transaction appropriately analyzed as a stock acquisition followed by an upstream transfer. It seems sensible to conclude that the result under Revenue Ruling 2001-46 should not be any different simply because the acquiring parent is a REIT and no actual upstream merger takes place. The lack of an actual upstream merger does not preclude a forward merger into a DRE under the 2001 Proposed Regulations from qualifying as an A reorganization, and it should not do so in the case of a reverse merger of a QRS when the end result is identical.

A further practical effect of the 2001 Proposed Regulations is that ordinary C corporations can elect to structure a reverse subsidiary merger as an A Reorganization, whereas a REIT can only engage in a tax-free reverse subsidiary merger if the transaction will otherwise qualify under section 351 or section 368(a)(1)(C). An ordinary C corporation, acquiring a target in a reverse subsidiary merger can choose to use a disregarded entity or a C corporation as a merger subsidiary. If the C corporation uses a DRE or a transitory subsidiary, it can treat the reverse merger as a stock acquisition and, if it chooses to merge the target upstream into the acquiring parent as part of an integrated plan, it can treat the combined reverse and upstream mergers as qualifying as an A Reorganization. A REIT that wishes to engage in a reverse subsidiary merger must use a DRE (as all corporations wholly owned by REITs are DRE's)[16] and following the acquisition, a REIT is automatically and immediately deemed to receive the assets of the target in a section 332 liquidation. Thus, while an acquiring C corporation can elect to structure a reverse subsidiary merger as an A Reorganization, a REIT is prevented from doing so by the 2001 Proposed Regulations.

The ability to elect A Reorganization treatment is a factor to be taken into account in considering whether an ordinary C corporation should be entitled to qualify an acquisition under section 368(a)(1)(A) if, following a reverse subsidiary merger, the acquiring parent simply "checks the box" on the target corporation and elects to treat it as a DRE. As indicated, there are other mechanisms available to a C corporation to obtain A Reorganization treatment (including merging the target corporation into the acquiring parent under the terms of Revenue Ruling 2001-46 or qualifying the transaction under either section 368(a)(2)(E) or section 368(a)(1)(B) using the analysis of Revenue Ruling 67-448). Thus, the case for extending the rule to ordinary C corporations may not be as strong as it is for REITs that do not have these structuring alternatives.

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[16] Unless the REIT elects TRS status for the C corporation. However, there are severe restrictions on the ability of REITs to hold property through a TRS (see above note 8).

In order to qualify as a reorganization under section 368(a)(1)(A), a merger must be a statutory merger or consolidation. In light of the current ruling position of the Service, and the 2001 Proposed Regulations, a merger pursuant to state law includes a state law merger with a DRE of acquiring parent, provided all the assets and liabilities of the transferor unit become assets and liabilities of the transferee and provided that the transferor ceases its existence. The technical mechanics used to achieve this result should not affect whether there has been a state law merger for the purposes of section 368(a)(1)(A). As noted above, the merger of a newly formed subsidiary with and into a target corporation followed by a prompt upstream transfer of the target into the acquiring parent will, under Revenue Ruling 2001-46, be treated as a single statutory merger of the target into the acquiring parent under section 368(a)(1)(A). While Revenue Ruling 2001-46 involves an actual state law merger of target into the acquiring parent, the 2001 Proposed Regulations permit the "state law merger" requirement of an A Reorganization to be satisfied by a forward merger into a DRE. The 2001 Proposed Regulations do not require an actual state law merger with the acquiring parent. There should be no difference between a forward merger and the merger of a DRE with and into a target corporation which is automatically liquidated. A merger of a QRS into a target corporation should meet the state law merger requirement such that, when followed immediately by a deemed liquidation into the parent REIT under section 856(i), the entire transaction is treated as a good A Reorganization.

The refusal to allow reverse subsidiary mergers of QRSs into corporations would have unfortunate policy implications. An acquisition of target stock through a forward merger that qualifies as an A Reorganization leaves the acquiring parent with a carryover basis for the target's assets, in an acquisition that was generally tax-free to the target shareholders. If the transaction were accomplished as a reverse merger, the acquiring parent (absent a section 338(g) election) would still have a carryover basis in the target assets pursuant to the deemed section 332 liquidation, but the target shareholders would be fully taxable on the consideration received unless the transaction met the onerous requirements of section 368(a)(1)(C) or a section 351 exchange. Accordingly, under the 2001 Proposed Regulations, the direction of the merger of a DRE creates one, and only one, significant asymmetry – the taxability of the exchange to the target shareholders. Such a difference in result is not justifiable solely on the direction of the merger.

We would appreciate the opportunity to discuss this issue with you in more detail if you believe it would be helpful. Please contact me or Dara Bernstein, NAREIT's REIT Counsel, to discuss this issue in more detail. Thank you for your consideration, and again thank you for your revisions of the 2000 Proposed Regulations.

Respectfully submitted,

Tony M. Edwards

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