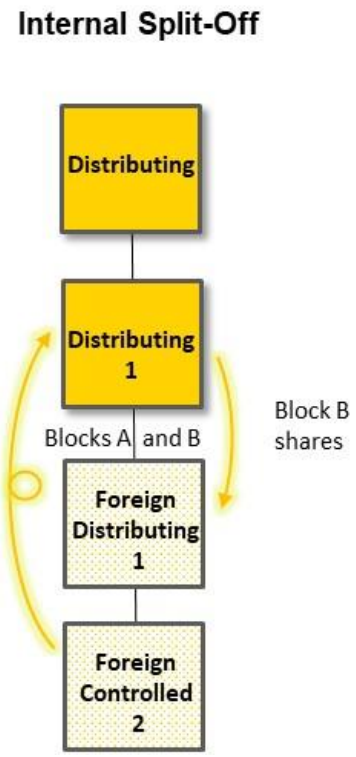
Tax M&A Update

National Tax M&A
International Tax and Transaction Services

Vol. XI, Issue 9 **May 2022**

Technical Developments and Musings

Stock basis considerations with internal split-offs. Doctrinal crosscurrents lurking beneath much of corporate tax practice often involve the question of whether the form of a particular step will be given independent, technical significance or instead possibly recharacterized under the "softer" judicial doctrines of step transaction or substance-over-form. Presumably this uncertainty was a consideration of the publicly traded corporation that sought an IRS ruling for an internal divisive transaction in PLR 202218002. As with many spin-offs involving affiliated groups, the ultimate spin-off was preceded by a series of internal affiliated group transactions, whereby groups of assets are collected in successive nonrecognition transactions that consolidate the active trades or businesses in the controlled corporation distributed to public shareholders. One such "packaging" transaction, depicted here, was an internal split-off of Foreign Controlled 2 by Foreign Distributing 1 to its sole shareholder Distributing 1. Although Distributing 1 owned all the shares of Foreign Distributing 1, it held two distinct blocks of such shares, perhaps with varying bases. And in this case, Foreign Controlled 2 was distributed to Distributing 1 *in exchange* for "Block B" shares of Foreign Distributing 1, as opposed to a *pro rata* distribution of Foreign Controlled 2. Here, IRS followed form, ruling that the basis in the Foreign Controlled 2 Common Stock received by Distributing 1 in the Internal Split-Off equaled the basis of the Block B Shares surrendered therefor, under Reg. §1.358-2(a)(2)(i), thus preserving Distributing 1's basis in its other block of shares held in Foreign Distributing 1.



Drop, spin, liquidate. IRS also favorably ruled that the form of a transaction would govern in another divisive transaction, PLR 202218001, which involved a "drop, spin, liquidate" fact pattern. The "drop" of business assets was by a distributing company into an existing controlled subsidiary (Controlled), followed by the "spin" of Controlled stock to a parent corporation in a § 355 distribution. As part of the same overall plan, the business assets then came to be directly held by the parent corporation when Controlled completely liquidated under § 332 into its new parent.

Legislative reenactment doctrine does not permit 10-year NOL carryback. In an internal legal memorandum, CCA 202219015, IRS chief counsel concluded that a taxpayer could not invoke the legislative reenactment doctrine to claim a 10-year carryback for that portion of a net operating loss comprised of a specified liability loss (SLL), since the taxpayer had already made a general NOL carryback waiver. Where applicable, the doctrine effectively "grandfathers" a prior judicial or regulatory interpretation of a provision when Congress substantially reenacts statutory text; i.e., the prior interpretation is presumed to be adopted by Congress. However, here IRS concluded that the SLL structure—added to the Code in 1990 but repealed in 2017—was a new statutory provision; thus, a 1986 regulation providing for carryback of a similar but different category of loss was not applicable where a general NOL waiver was in effect.