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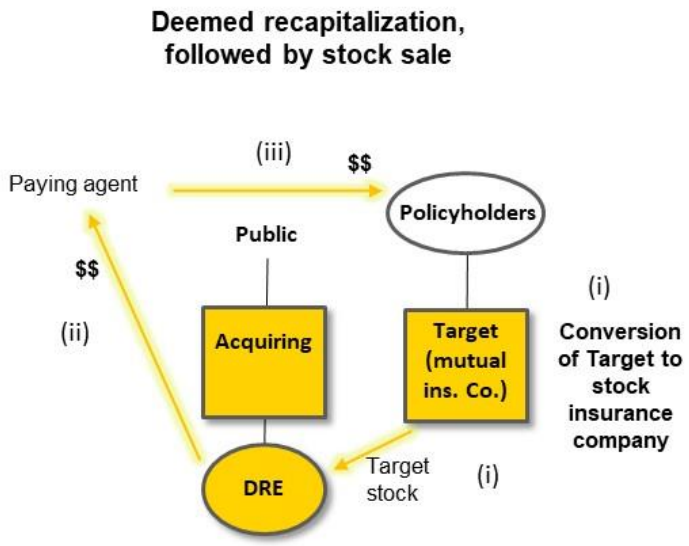
Technical Developments and Musings

Insurance company conversion and acquisition steps recast. PLR 202429001 addresses the conversion of a mutual insurance company to one that is stock-based, in connection with its acquisition by a publicly traded company ("Acquiring," or "Corp A" in the PLR). Ultimately, the policyholders of the mutual insurance company were cashed out, and the IRS effectively recast the steps for US federal tax purposes, treating the sale as following a recapitalization of the historic mutual insurance company. The relevant steps depicted here were described as occurring "contemporaneously": (i) the mutual insurance company ("Target" or "Corp B" in the PLR) undertakes a conversion to a stock insurance company and all of its newly issued shares are transferred to a disregarded entity of Acquiring (DRE); (ii) DRE makes a payment to a third-party "paying agent" and (iii) the agent pays over to each Target policyholder its share of the payment, representing an amount approved by the state insurance commissioner. The taxpayer represented that the conversion qualifies as a §368(a)(1)(E) and (F) reorganization "other than the issue of the stock of the newly converted" company being transferred to a disregarded entity of Acquiring. The IRS ruled that the conversion and cash payments received by the policyholders will be treated as if the Target stock was issued directly to the policyholders in exchange for their membership interests followed by a sale of such stock by the former policyholders to DRE in exchange for the payments received by policyholder. Under the §368(a)(1)(F) regulations, such ruling was likely critical to support an F reorganization conclusion for the conversion.



Installment sale treatment for shares sold to an ESOP. *Berman v Comm'r*, 163 TC No. 1, also addresses the sale of stock, in this case by individuals to an employee stock ownership plan (ESOP). While the individuals made valid elections under §1042 to defer gain on the stock sold to the ESOP, the full Tax Court concluded that their sale of qualified replacement property the following year triggered recapture of the gain. This in turn raised an issue of first impression—the interplay of the §1042 deferral and recapture provisions with the more generally applicable §453 installment sale rules —because at least one payment was to be received after the close of the tax year in which the sale occurred. The court concluded that the installment sale rules applied, because the taxpayers had not elected out of installment reporting.

Final Section 367(b) triangular reorganization regulations. Treasury and the IRS released final regulations under §367(b) on the treatment of property used to acquire parent stock or securities in connection with certain cross-border triangular reorganizations and inbound nonrecognition transactions. The final regulations, which are effective on July 17, 2024, adopt the proposed regulations without substantive change. For further info, see Tax Alert 2024-1416.

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