Wednesday, October 3, 2012
11:00 AM - 12:30 PM

309 – Tax Considerations in M&A Transactions

Thomas Avent Jr
Partner
KPMG LLP

Priscilla Hughes
Senior Vice President & General Counsel, Americas
Thomson Reuters Markets

Eleanor Palmer
Managing Counsel
Nationwide Mutual Insurance Company

This material is protected by copyright. Copyright © 2012 various authors and the Association of Corporate Counsel (ACC).
Materials may not be reproduced without the consent of ACC.
Reprint permission requests should be directed to ACC's Legal Resources Department at ACC: +1 202.293.4103, x338; legalresources@acc.com

Faculty Biographies

Thomas Avent Jr
Partner
KPMG LLP

Priscilla Hughes

Priscilla Hughes is the senior vice president, general counsel, Americas and chief counsel for M&A at Thomson Reuters financial and risk. She has overall responsibility for the legal affairs of Thomson Reuters financial services businesses in the Americas and oversees M&A activities globally.

Prior to joining Thomson Reuters, Ms. Hughes worked with Thomson for over ten years as outside M&A counsel. She was a partner in the New York office of Morrison & Forester LLP and co-head of the firm's global M&A practice. Her practice focused on complex mergers and acquisitions, and federal securities regulation. She also has substantial experience in public offerings, debt and equity financings, restructurings, and regulatory compliance matters.

Ms. Hughes is a member of the board of directors of G-NY and has previously served on the Committee on Women in the Law of the NY State Bar Association, including as the first president of the Domestic Violence Subcommittee. She is an active volunteer in her community on Long Island, including with the Huntington Historical Society.

Ms. Hughes received a JD, cum laude, from Fordham University School of Law, where she was a member of the *Law Review*. She received her BA, cum laude, from New York University, where she was a member of Phi Beta Kappa.

Eleanor Palmer

Eleanor Palmer is managing counsel, tax in Nationwide's office of the chief legal and governance officer (OCLO). She is responsible for identifying and managing Nationwide's tax exposure and providing counsel on tax matters related to business initiatives. She advises on tax controversies and credit negotiations with the Internal Revenue Service and state and local taxing jurisdictions. She also assists with investment structuring, agent and executive compensation issues, vendor contract review and various projects presenting unintended tax consequences.

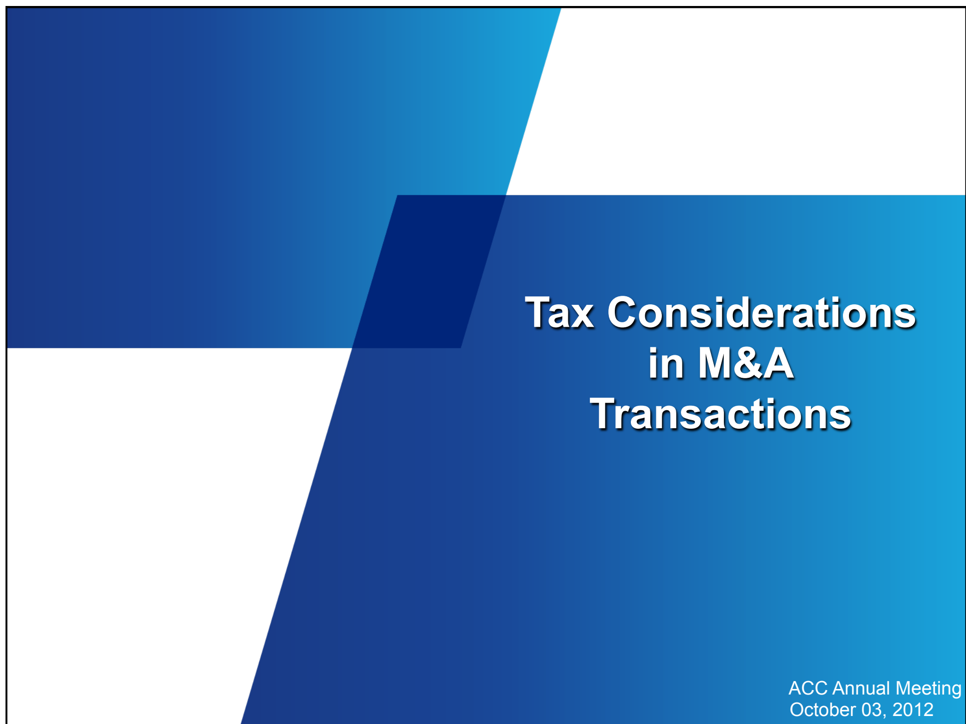
Ms. Palmer serves as a lead tax advisor in domestic mergers, acquisitions and dispositions, where she evaluates potential tax risks and provides legal structuring advice to mitigate negative tax consequences. Prior to joining Nationwide, she was a manager in Ernst & Young's state and local tax group. In that role, she was member of the state and

local tax due diligence team, where she provided advice specific to state and local tax liability and structuring for clients involved in mergers and acquisitions.

Ms. Palmer is a member of the Columbus Bar Association's Business Tax Committee. She has been a speaker on tax matters at the Ohio Tax Conference and a panelist for Women Lawyers of Franklin County, the John Mercer Langston Bar Association, and YWCA.

Ms. Palmer is a graduate of The Ohio State University, where she received a JD and MBA.

Copyright © 2012 Association of Corporate Counsel



ANY TAX ADVICE IN THIS COMMUNICATION IS NOT INTENDED OR WRITTEN BY KPMG TO BE USED, AND CANNOT BE USED, BY A CLIENT OR ANY OTHER PERSON OR ENTITY FOR THE PURPOSE OF (i) AVOIDING PENALTIES THAT MAY BE IMPOSED ON ANY TAXPAYER OR (ii) PROMOTING, MARKETING OR RECOMMENDING TO ANOTHER PARTY ANY MATTERS ADDRESSED HEREIN.

The information contained herein is general in nature and based on authorities that are subject to change. Applicability to specific situations is to be determined through consultation with your tax adviser.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Dated material

THE INFORMATION CONTAINED IN THESE COURSE MATERIALS IS CURRENT AS OF THE DATE PRODUCED. THE MATERIALS HAVE NOT BEEN AND WILL NOT BE UPDATED TO INCORPORATE ANY TECHNICAL CHANGES TO THE CONTENT SINCE THE PRODUCTION DATE, WHICH IS INDICATED AT THE BOTTOM OF EACH PAGE. YOU ARE RESPONSIBLE FOR VERIFYING WHETHER OR NOT THERE HAVE BEEN ANY TECHNICAL CHANGES SINCE THE PRODUCTION DATE.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

Agenda

- Taxable acquisitions
- Tax-free acquisitions
- Taxable versus Tax-Free considerations
- Acquisition Agreement
- Success Based Fees
- Rescinding transactions

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

Copyright © 2012 Association of Corporate Counsel

Types of acquisitions

	Taxable	Tax-free
Stock Acquisition	Stock Purchase	Reorganization (B)
	338	(a)(2)(E)
Asset Acquisition	Asset Purchase Subsidiary Stand-alone	Reorganization (A), (C), (D), (a)(2)(D)

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Taxable Acquisitions

Primary tax concerns

- Acquiring
  - Basis in Target's assets
  - Carryover of Target's attributes
- Target/Target Shareholders
  - Target level tax
  - Target shareholder level tax

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Stock purchase—business issues

- ALL T liabilities acquired/T liabilities isolated
- Must move (un)wanted assets (out of) into T
- Minimal asset transfer issues
- Tax rules generally don't limit type of consideration
  - (Except, all-voting-stock consideration may be a reorganization)
- Tax rules generally don't limit post-acquisition planning
  - BUT—post-purchase liquidation/merger can cause acquisition to be a reorganization; see Rev. Rul. 2001-46, 2001-42 IRB 321

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

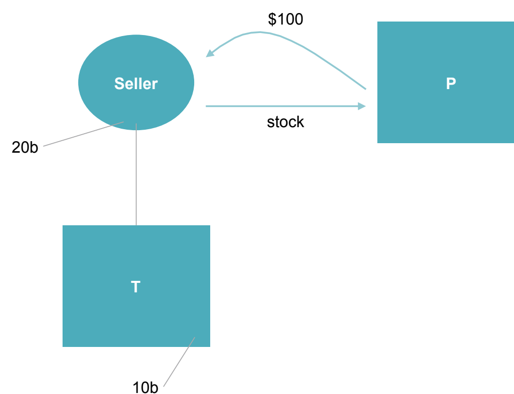
Stock sale

Generally favored by Seller

- Change cash management system and/or transfer accounts prior to closing
- Fewer assignment/consent Issues
  - Assignment by operation of law
  - Government licenses often cannot be transferred
- All of the employees are effectively "transferred" to buyer, so anyone seller wants to retain must be terminated and accept new employment with seller

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

Stock purchase



© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

Copyright © 2012 Association of Corporate Counsel

Stock purchase—alternate structure Reverse subsidiary cash merger

A
$
P
Merger
T
Newco
T shares convert to $

A
$
P
P owns all of T stock
T

See Rev. Rul. 90-95, 1990-2 C.B. 67

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

Stock purchase—tax effects

$100
$80 gain section 1001
S
P
Cost basis of $100 § 1012
T stock
20b
T
T
$10 basis and tax attributes
$10 basis and tax attributes subject to limitation

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

Types of acquisitions

	Taxable	Tax-free
Stock Acquisition	Stock Purchase	Reorganization (B)
	338	(a)(2)(E)
Asset Acquisition	Asset Purchase Subsidiary Stand-alone	Reorganization (A), (C), (D), (a)(2)(D)

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Asset purchase—business issues

- Significant legal transfer issues
- Need not assume liabilities (unless merger)
- Only need sell/buy wanted assets
- Tax rules don't limit type of consideration
  - BUT if more than 38% stock, may be a tax-free reorganization, if selling corporation is liquidated
- Tax rules don't generally limit post-acquisition planning

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Merger

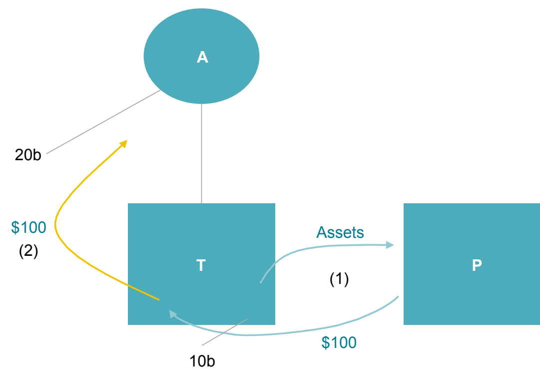
Generally favored by buyer

- Documents generally more complicated than stock sale
  - More extensive due diligence & detailed schedules
  - More closing documents (instruments of conveyance)
- Problems often arise with shared assets
  - Which party will have title?
  - What rights will the other party have?

Successor liability issues, particularly when acquiring assets from distressed seller

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Purchase of standalone corporation's assets



(1) Sale of assets
(2) Distribution of proceeds

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Alternative merger structure
Forward cash subsidiary merger

T stock converted to cash

A

P

T

State law merger

Acquiring

Treated as if T sold assets to Acquiring and T liquidated, *Cf.*, Rev. Rul. 69-6

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Asset sale (Noncorporate shareholder)

S

Stock basis of $20

$100

Corporate Level
$90 gain
§ 1001

T

$10 basis

P

Assets

Shareholder Level
$80 gain
§ 331

$100 proceeds over $20 basis

Asset basis of $100
§ 1012

T

$100 Cash

P

Liquidation

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Compare cash merger with asset sale

- Both alternatives result in:
  - Stepped-up basis in T assets
  - Two levels of tax
  - Any unused T NOLs disappear
- Merger
  - Requires both T Sh and Acq Sh approval
  - No re-titling of assets
  - Acq has unlimited liability exposure
- Direct Asset Sale
  - Only T shareholder approval
  - Acq assumes specific T liabilities

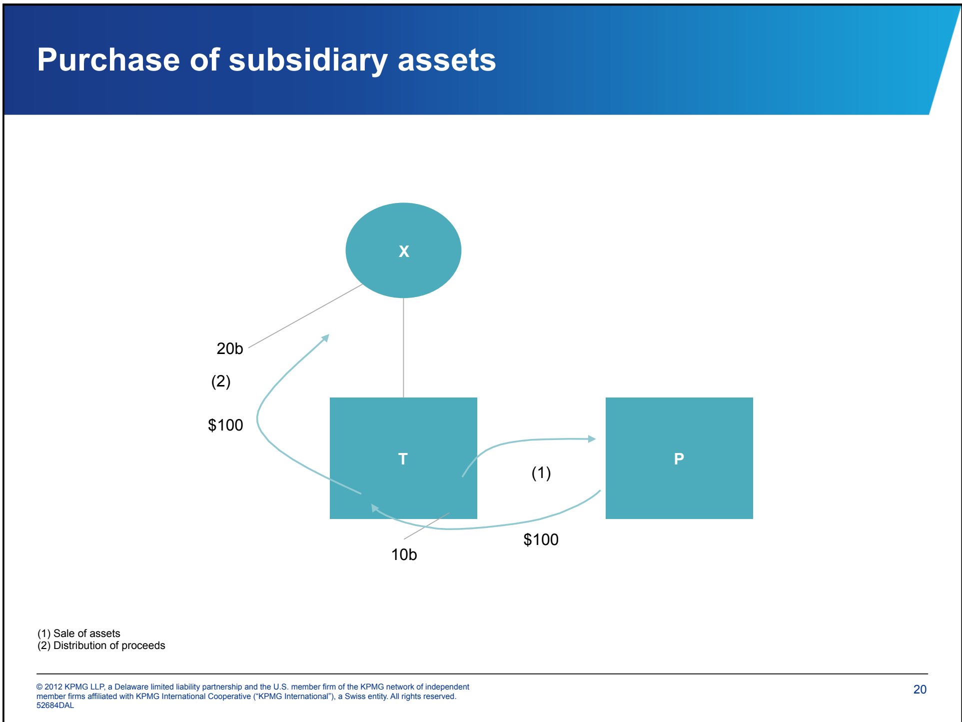
© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

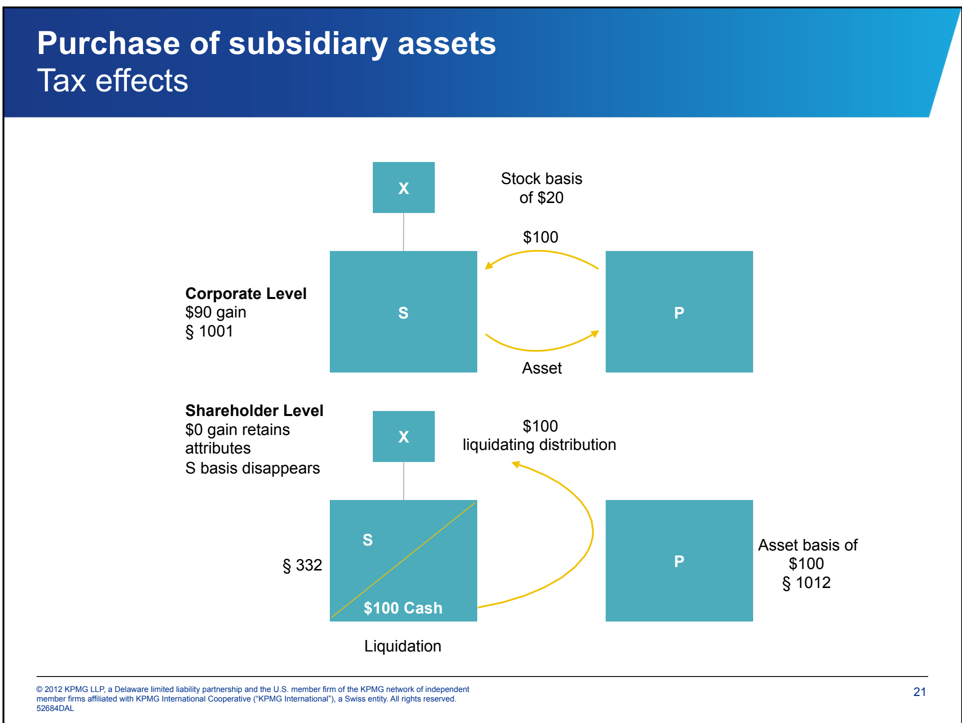
Asset sale

- All of assets and liabilities of target are vested in survivor
  - Use new subsidiary of buyer to merge with target to insulate liabilities below buyer company
- Generally target survives the merger if it is an operating company to minimize consent issues
- Private companies often use merger structure because target has too many stockholders to require all to sign a Stock Purchase Agreement and satisfy closing requirements
- Dissenters' Rights apply

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel


Purchase of subsidiary assets
X
20b
(2)
$100
T
(1)
P
$100
10b
(1) Sale of assets
(2) Distribution of proceeds
© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL
20


Purchase of subsidiary assets
Tax effects
X
Stock basis of $20
$100
Corporate Level
$90 gain
§ 1001
S
P
Asset
Shareholder Level
$0 gain retains attributes
S basis disappears
X
$100 liquidating distribution
S
§ 332
$100 Cash
P
Asset basis of $100
§ 1012
Liquidation
© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL
21

Why would we ever do an asset sale?

- Business Considerations
  - E.g., acquisition of discrete assets, need to pay cash, buyer does not want liabilities
- Tax
  - T has NOL that can be used to offset asset sale gain
  - T is foreign and sale is not subject to U.S. tax
  - High basis in T assets, so little or no gain on asset sale
  - T is subsidiary and inside basis in T assets greater than outside basis in T stock, and a § 332 liquidation of T is available, or T not distributing proceeds

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Types of acquisitions

	Taxable	Tax-free
Stock Acquisition	Stock Purchase	Reorganization (B)
	338	(a)(2)(E)
Asset Acquisition	Asset Purchase Subsidiary Stand-alone	Reorganization (A), (C), (D), (a)(2)(D)

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

§ 338

- Election to treat "qualified stock purchase" as an asset purchase
- Two types of elections:
  - 338(g)—Standalone T; two levels of tax
  - 338(h)(10)—Subsidiary T or S corp; one level of tax
- Legislative history says § 338 election is intended to replace all nonstatutory means of treating a stock purchase as an asset purchase (at least where doing so would result in a stepped-up basis in T's assets)

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

24

Business advantages/disadvantages

- Advantage—No asset transfer (e.g., retitling, loan covenants, local transfer taxes, leases, etc.)
- Disadvantage—Must move (un)wanted assets (out of) into T

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

25

§ 338—Qualified stock purchase

- Eligible purchaser acquires stock of another corp. (T) representing
- § 1504(a)(2) (80% vote and value) of the stock of T
- Within 12-months
- By "purchase"

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Eligible purchaser

- Corporation
  - Domestic or foreign
  - S corporations
  - LLCs treated as corporations
  - Disregarded entities
- Not partnerships or individuals
- Corporation must be the "purchaser" for federal tax purposes
- Individual wants to acquire T and make 338 election
- Individual forms Newco to acquire T
- Is Individual or Newco the "purchaser"?
- What if "Newco" is a pre-existing corporation?
- Look at facts and circumstances
  - Immediate downstream merger into T
  - Liquidation of Newco
  - Disposition of T stock by Newco
- FSA 200122007
  - PRS wants to acquire T1 (Holdco). T1's sole asset is stock in T2
  - PRS forms Newco to acquire T1. Newco purchases T1 stock and files 338 election for T1 and T2
  - Shortly thereafter and pursuant to the same plan, PRS buys T2 from T1 (no gain because of 338 step up)
  - Newco stays in existence (albeit with no assets other than the T1 stock which is virtually worthless)
- Who was the purchaser?

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

12-month acquisition period

- Target stock purchased in the 12-month acquisition period is referred to as "recently purchased stock"
- Target stock not purchased in the 12-month acquisition period is referred to as "nonrecently purchased stock"
- 12-month period can be extended if 1504(a)(2) purchased pursuant to an arrangement in a period > 12 months
- Because of the 12-month period, a purchasing corporation that has held > 20% of T stock for more than a year ordinarily can't make a QSP (unless extension applies)
- Can P "cure" this situation by selling T stock to a third party and repurchasing it?
  - See Rev. Rul. 72-354

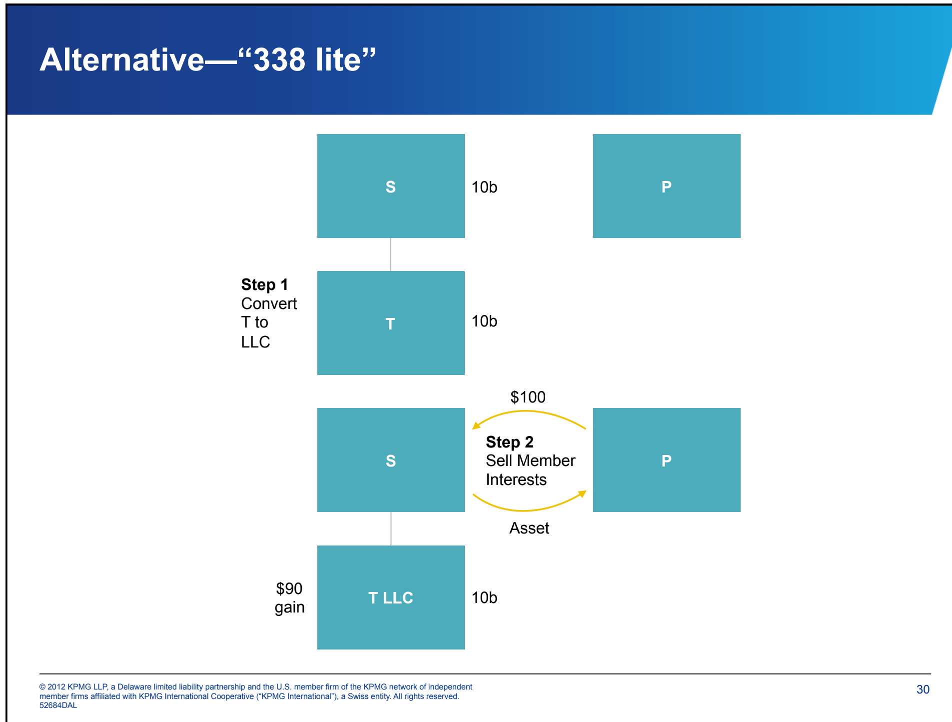
© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

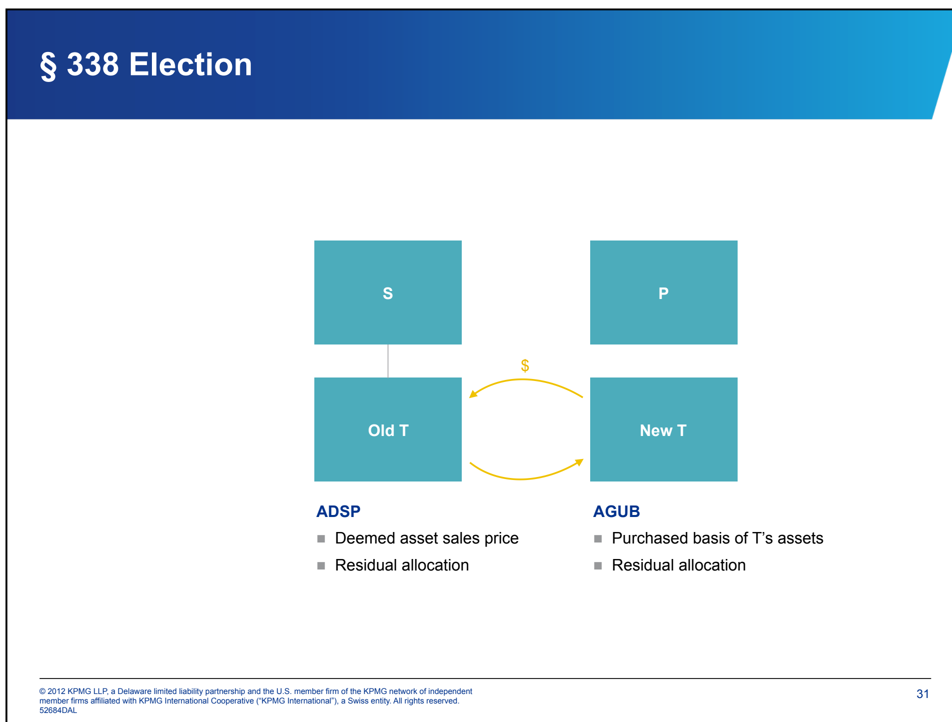
"Purchase"

- Generally, any acquisition of stock other than:
  - Carryover basis transactions
  - § 351, 354, 355, 356, or other tax-free transactions (probably even if transferor recognizes all of its gain because of boot)
  - Any acquisition from a related person
    - Person is related if their stock ownership would be attributed to purchaser under § 318
    - If series of transactions, test relationship after
- QSP can occur through combination of purchase by P and redemption of T stock from shareholders unrelated to P
- QSP can occur in an IPO
  - Ex. S owns all of T. S transfers T to Newco. At the time, S has firm commitment from Underwriter to acquire 60% of Newco and sell to the public
    - Transfer to Newco not a § 351 transaction
    - Test relationship between S and Newco after transactions occurring as part of a plan
    - So, Newco "purchased" T stock from S, an unrelated party
- Liquidating and non-liquidating distributions of T stock may be purchases
  - Always subject to related party rules
  - Won't apply to § 332 liquidations
- Deemed purchases of Target Subs—if § 338 election made for Target, deemed sale of Sub stock is a "purchase"

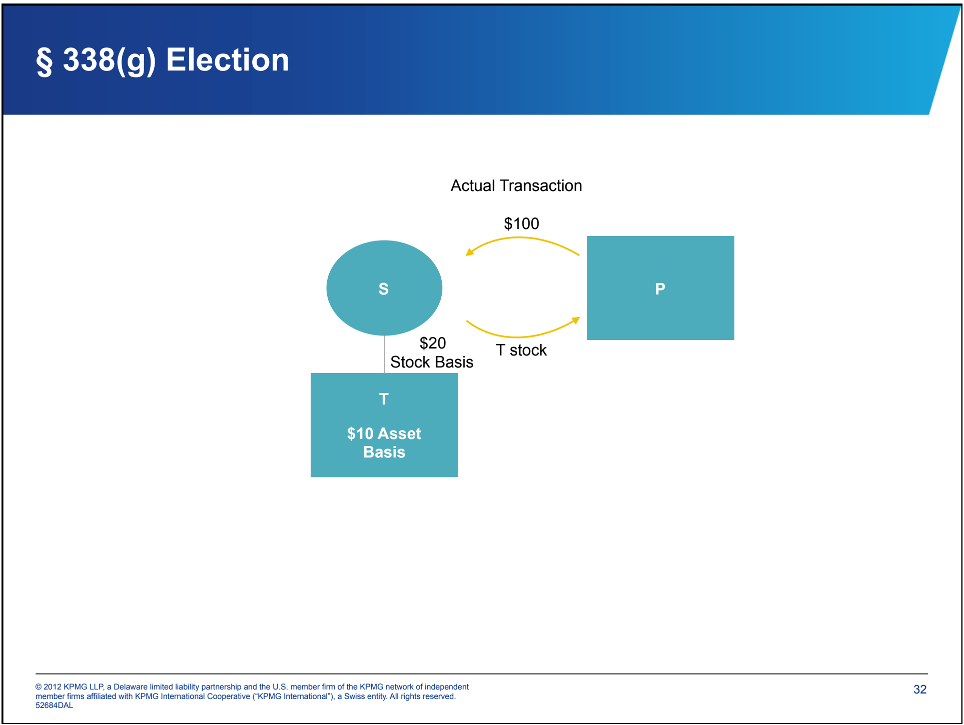
© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

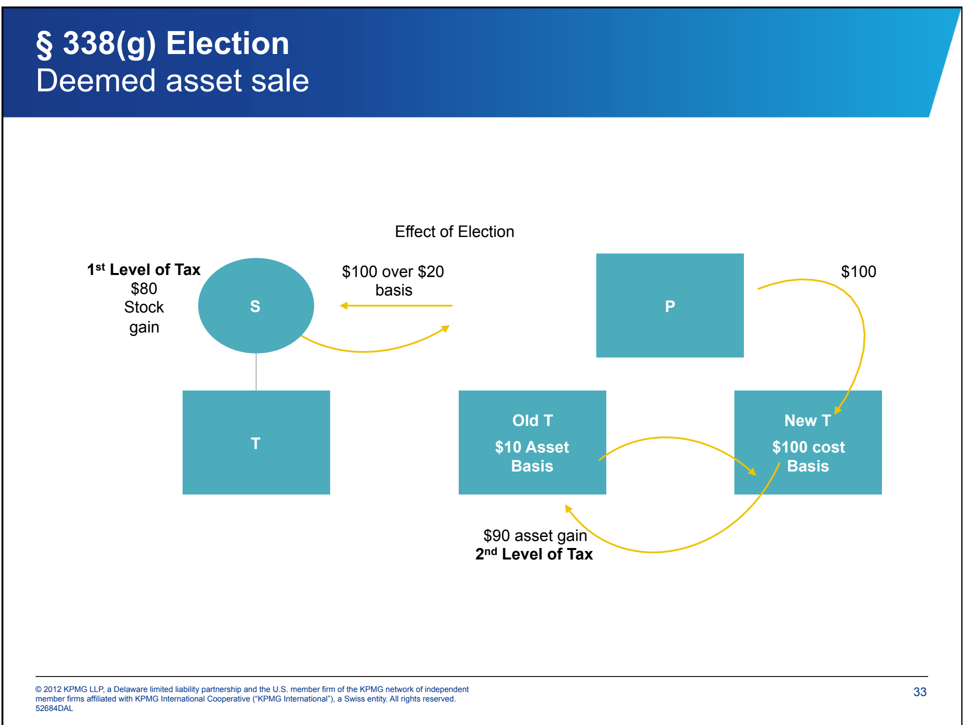
Copyright © 2012 Association of Corporate Counsel





Copyright © 2012 Association of Corporate Counsel


§ 338(g) Election
Actual Transaction
$100
S
P
$20
Stock Basis
T stock
T
$10 Asset
Basis
© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL
32


§ 338(g) Election
Deemed asset sale
Effect of Election
1st Level of Tax
$80
Stock
gain
S
$100 over $20
basis
P
$100
T
Old T
$10 Asset
Basis
New T
$100 cost
Basis
$90 asset gain
2nd Level of Tax
© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL
33

Impact of 338(g) election

- Old T treated as having sold all of its assets for FMV (ADSP)
- New T treated as having purchased those assets for price paid plus liabilities (AGUB)
- Old T's attributes disappear (used in old T asset sale)
- T Shs treated as selling T stock

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

§ 338(g)—Reporting deemed sale gain

- General rule—Reported in Old T's final return
- If Old T is part of consolidated group:
  - File a separate deemed sale return that includes only deemed sale
  - Combined return for all targets acquired on same date
- If Old T is an S corporation file a deemed sale return as a C corporation
- Old T's final return is due on the fifteenth day of the third month following the month in which the acquisition date falls
- Keep this in mind when we talk about when the § 338 election is due

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

Copyright © 2012 Association of Corporate Counsel

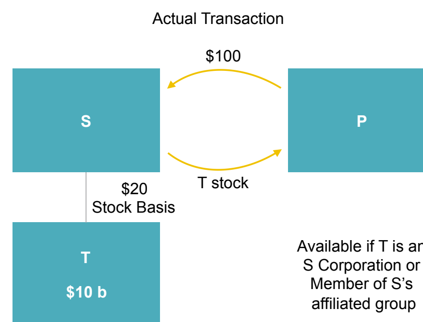
When to make a 338(g) election

- Make election if:
  - T has expiring NOL (or NOL may become limited)
  - T is foreign corporation where recognized gain is not subject to U.S. tax

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

§ 338(h)(10)

Actual Transaction



Available if T is an S Corporation or Member of S's affiliated group

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Requirements of § 338(g)/(h)(10)
Election

- Purchaser must be a corporation (in form and in substance)
- Purchaser makes a Qualified Stock Purchase (QSP)
  - "Purchase" from unrelated party (no CoB or transferred basis)
  - 80-80 test (Reg. § 1504(a)(2))
  - 12-month acquisition period
- Purchaser elects on or before fifteenth day of ninth month after QSP
  - Example: deal closes January 15, 2013, file election by October 15, 2013
  - Form 8023
  - Joint election if 338(h)(10) election
- In case of § 338(h)(10) election, T must be eligible target
- Key Difference
  - § 338(h)(10) election: joint election by purchaser and selling T Shs; S corp T Shs who do not sell T stock must also consent
  - § 338(g) election: unilateral election by purchaser

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Impact of a 338(h)(10) election

- T shareholder stock sale disregarded
- Old T treated as selling assets and distributing proceeds in complete liquidation
- New T deemed to purchase assets
- Old T's attributes carry over to selling T shareholder if § 332 liquidation

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

§ 338(h)(10)—Eligible targets

- Eligible Targets
  - Member of a selling consolidated group,
  - Member of a selling affiliated group, or an S corporation
- § 338(h)(10) essentially permits the T Shs to disregard the stock sale if the T assets could have been sold and T could have been liquidated with only one level of tax

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

§ 338(h)(10)—Deemed sale gain

- If old T was a member of a selling consolidated group or a selling affiliated group, asset sale is deemed to have occurred while old T was member of seller's group
- If old T is an S corporation, sale is deemed to have occurred while old T was still an S corporation
  - T Shs take prorata share of deemed sale gain into account under § 1366
  - Deemed sale increases basis in T stock under § 1367
  - § 1374 built-in gains tax remains two-level tax

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

§ 338(h)(10)—Deemed liquidation

- If Old T is a C corporation
  - Liquidation generally will be tax-free to Old T (§ 337) and Old T's parent (§ 332)
  - Old T's tax attributes c/o to Old T's parent (§ 381)
- Old T is an S Corporation
  - Liquidation taxable to Old T Shs (§ 331)
  - Note: T's Sh's basis was increased for pro rata share of deemed sale gain

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

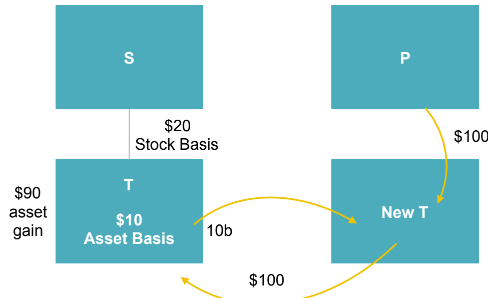
§ 338(h)(10)—Minority shareholders

- Target C Corporation
  - Nonselling minority shareholders—election has no effect on these holders
  - Selling minority shareholders—treat as stock sale
- Target S Corporation
  - All shareholders effected by election via flow through rules
  - All shareholders, including non selling shareholders, must sign election

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

Copyright © 2012 Association of Corporate Counsel

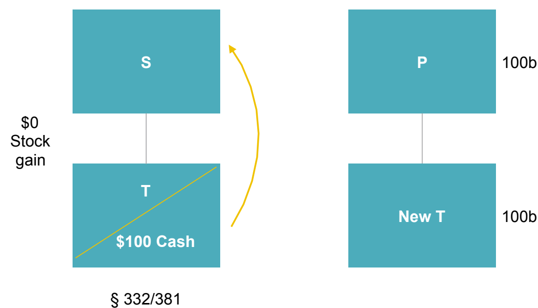
§ 338(h)(10)
Deemed asset sale



© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

44

§ 338(h)(10)
Deemed asset sale (continued)



© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

45

Factors in making a § 338(h)(10) election

- Want a stock transaction for legal purposes
  - Assets can be transferred only with third party consent
  - Non transferable licenses
  - Liability exposure
- Negotiate purchase price if election benefits one party and hurts the other party
- Factors for Purchaser
  - Amount of the basis step-up
  - Allocation of the step-up; i.e., whether it goes to "short-lived" assets or to LT depreciable assets
  - Ability to realize the benefit of the step-up
- Factors for Seller
  - Relationship between T's "net inside asset basis" and Seller's "outside stock basis"
  - If T is a consolidated subsidiary, consider whether:
    - Selling group has an ELA in the T stock (untaxed if election made)
    - The consolidated LDR would disallow a loss on sale of T stock (LDR does not apply to asset sales)
  - Seller may be able to use Target NOL faster than Purchaser due to § 382 limitation

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Uses of § 338(h)(10) pre-sale Distribution of unwanted assets

- Step 1: P enters into agreement with X to buy stock of T
- Step 2: T adopts plan of complete liquidation
- Step 3: T distributes unwanted assets to X as first liquidating distribution

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

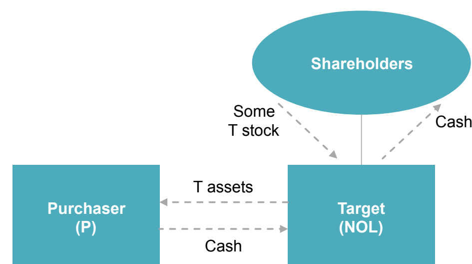
§ 338 Consistency rules

- No Stock Consistency Rules
  - Must make separate § 338 election for each target affiliate
- Asset Consistency Rules
  - Prevent avoidance of corporate level tax through
    - § 1502 investment adjustment rules
    - 100 % dividend received deduction
  - Penalty is carryover basis in tainted asset
- IRS can no longer impose involuntary § 338 election

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Bifurcated stock and asset acquisitions

Step 1:



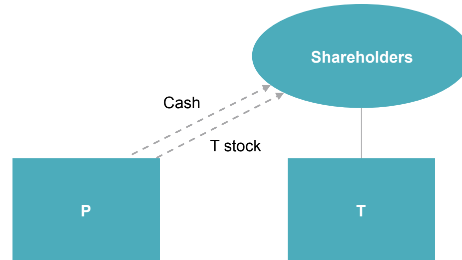
- T has an NOL
- P acquires certain appreciated assets from T for cash
- T distributes cash to its shareholders in part redemption

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Bifurcated stock and asset acquisitions (continued)

Step 2:

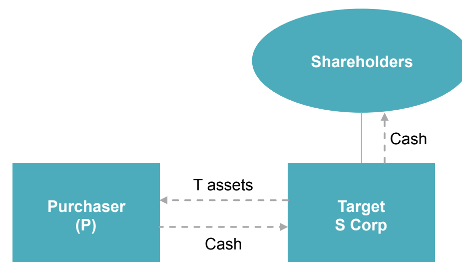


- P acquires T stock from shareholders for cash

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Bifurcated stock and asset acquisitions (continued)

Step 1:



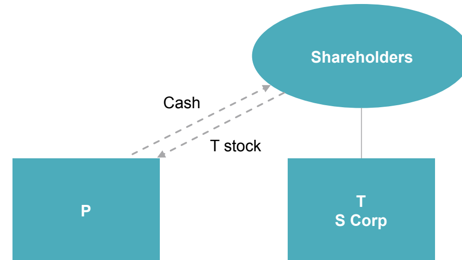
- T has assets with § 1374 built-in gain tax taint
- P acquires non-§ 1374 tainted assets for cash
- T distributes the cash to its shareholders

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Bifurcated stock and asset acquisitions (continued)

Step 2:



- P acquires T stock from shareholders for cash

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Tax-free Acquisitions

Copyright © 2012 Association of Corporate Counsel

Tax-free transactions
General

- A transaction is taxable unless it qualifies for tax-free treatment under a specific provision of the Internal Revenue Code (IRC)
  - IRC § 368 provides tax free treatment to acquisitions if certain criteria are met
- Tax Free transactions primarily distinguished by the consideration used by Buyer

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Reorganizations
General Principles

(1) Consideration – Acquiring stock

(2) Gain deferral (not elimination)

(3) Not elective, although structure chosen may be effective electivity

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

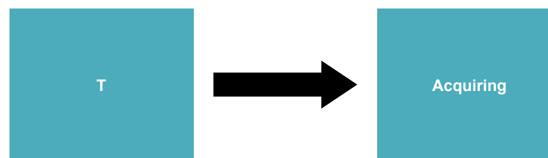
Copyright © 2012 Association of Corporate Counsel

Reorganization requirements

- Statutory requirements—§ 368(a)(1)
  - (A) State law merger
  - (B) Stock-for-stock
  - (C) Stock-for-assets
  - (D) Controlled corporations
  - (E) Recapitalization
  - (F) Mere change in form
  - (G) Bankruptcy
- Non-statutory requirements
  - Continuity of business enterprise
  - Business purpose
  - Continuity of proprietary interest

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

§ 368(a)(1)(A)



- "Statutory merger or consolidation"

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

§ 368(a)(1)(A)
Disregarded entities

Combining unit
(transferor unit)

Combining unit
(transferee unit)

P

Combining entity

T

Merger

LLC

LLC

(A) All assets of –or Unit become assets of –ee Unit
(B) Combining entity of –or Unit ceases its existence

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

368(a)(1)(A) with foreign corporations
Transactions on or after January 23, 2006

- Former regulation—merger under state or federal law
- New regulation—"statute or statutes necessary to effect the merger or consolidation"—includes foreign corporations!

FT

F Acquiring

(A) All assets of -or Unit become assets of -ee Unit
(B) Combining entity of -or Unit ceases its existence

NOTE—§ 367!

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

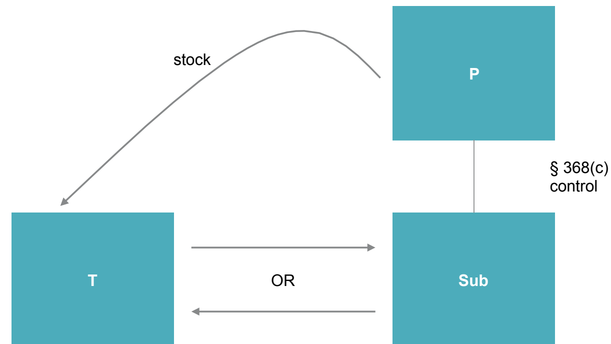
Copyright © 2012 Association of Corporate Counsel

Why do an (A)?

- Advantages
  - Easy tax qualification after merger—only nonstatutory requirements
  - Administratively easy all assets go by operation of state law
- Disadvantages
  - Automatic liability assumption in merger
  - Approval by T and Acq shareholders

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Triangular reorganizations



1. Isolates liabilities from P and other P subs
2. Simplifies shareholder approval procedures

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

§ 368(a)(2)(D)
Forward triangular

- Merger into P would have been an (A)
- Non-statutory requirements

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

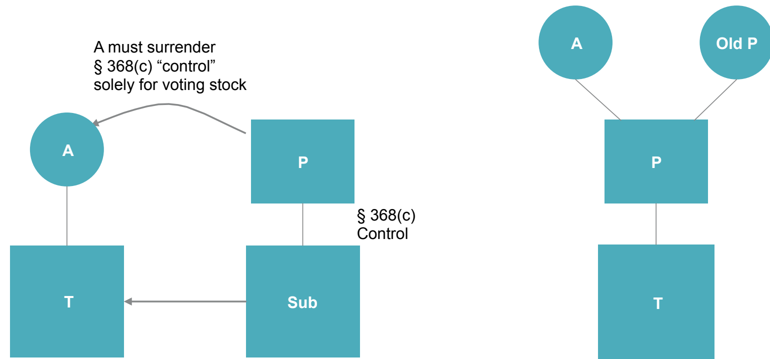
Why do an (a)(2)(D)?

- Advantages
  - Can isolate liabilities in S
  - Flexible consideration requirements—Continuity of Interest only constraint
  - Easier shareholder approval procedures
- Disadvantages
  - Limits on pre-merger asset dispositions "substantially all" requirement
  - Asset acquisition—corporate level tax if wrong
  - Rev. Rul. 2001-46

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

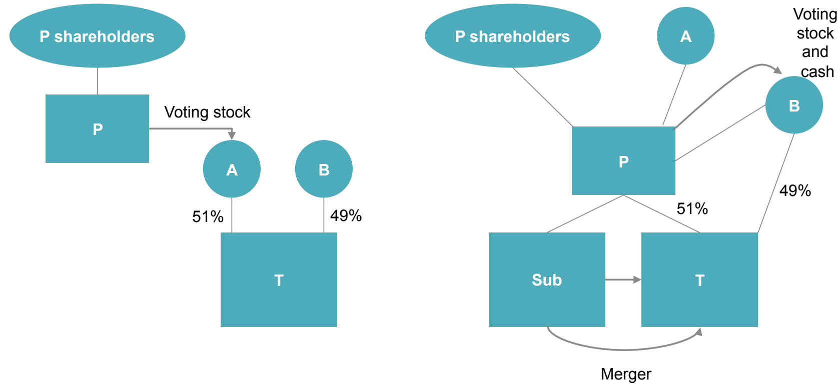
§ 368(a)(2)(E)
Reverse triangular



- State law merger
- T must hold "substantially all"
- Nonstatutory requirements

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

Rev. Rul 2001-26
Two-step stock acquisition



Step I

1) P acquires 51% of T stock in Tender offer solely for P voting stock

Step II

2) Sub merges into T and remaining T Shareholders receive P voting stock and cash

Ruling—Tender offer a part of statutory merger
§ 368(a)(2)(E) may apply

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

Copyright © 2012 Association of Corporate Counsel

Why do an (a)(2)(E)?

- Advantages
  - Effectively an acquisition of T stock
  - Easier corporate shareholder approval procedures
  - No transfer of T assets or liabilities
  - Some boot allowed
- Disadvantages
  - Limits on pre-merger (post-merger?) asset dispositions “substantially all” requirement
  - Creeping acquisitions problematic
  - Consideration limits—must use 80% voting stock only 20% can be boot

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative (“KPMG International”), a Swiss entity. All rights reserved. 52684DAL

§ 368(a)(1)(B)
Stock acquisition

- Stock for stock exchange
- Solely for voting stock
- Control immediately after

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative (“KPMG International”), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Stock acquisition
§ 368(a)(1)(B)

Solely Voting Stock

A stock

T stock

Acquiring

A

T

Old Acquiring

A

Acquiring

T

§ 368(c) Control

- No boot in a B

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Why do a (B)?

- Advantages
  - Easier approval procedures
  - No transfer of T assets or liabilities
  - Creeping acquisitions permitted
- Disadvantages
  - All consideration must be Acquiring voting stock
  - Beware of payment of shareholder expenses, etc. Rev. Rul. 73-54
  - Must monitor pre-reorganization acquisitions of T stock

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

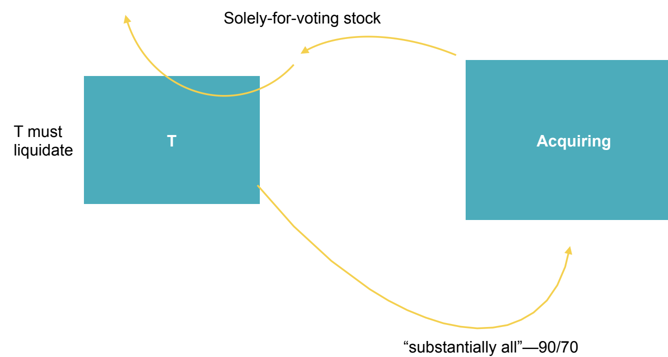
§ 368(a)(1)(C)

- Acquisition by one corporation (Acq)
- In exchange for *solely voting stock* of Acq (or voting stock of a corporation (P) in control of Acq)
  - (368(a)(2)(B)—boot relaxation rule)
- *Of substantially* all the properties of another corporation (T)
- Assumption of liabilities does not violate *solely voting stock*
- 368(a)(2)(G)—liquidation requirement

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

70

§ 368(a)(1)(C) (continued)



© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

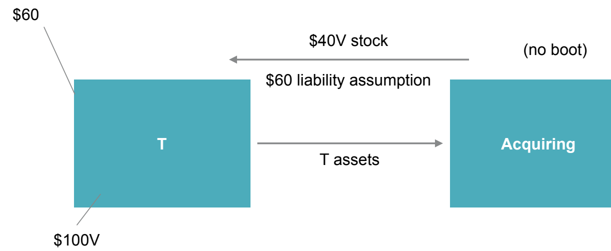
71

Solely-for-voting stock
368(a)(2)(B)—Boot relaxation rule

Liability assumption generally disregarded

Boot relaxation rule:

- 20% boot OK
- But—if ANY boot—liabilities count toward 20%



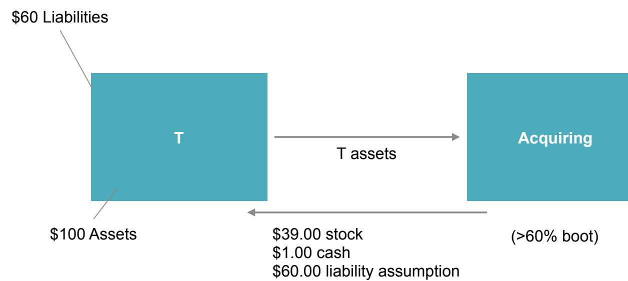
© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

72

Boot relaxation rule

Boot relaxation rule

- 20% boot OK
- But—if ANY boot—liabilities count toward 20%

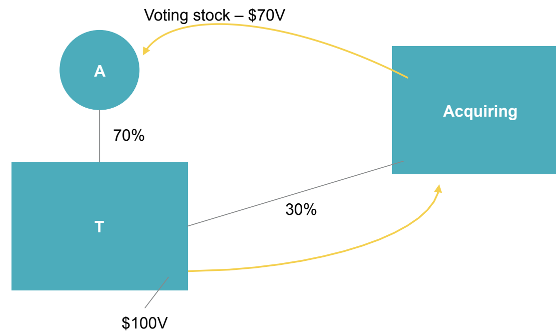


© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

73

§ 368(a)(1)(C)
Solely-for-Stock

Creeping Acquisitions



- *Bausch & Lomb*

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Substantially all

- Quantitative test: IRS ruling standard—90% FMV net assets and 70% FMV gross assets. Rev. Proc. 77-37
- Qualitative test: Courts consider nature of assets retained and reason for retention. Rev. Rul. 57-518
- Extraordinary distributions by T before transaction may impair substantially all
- Asset sales do not impair—substitution concept

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Why do a (C)?

- Advantages
  - Can isolate liabilities—leave behind in shell
  - Facilitates sale of charter
  - Can combine if no applicable merger law
- Disadvantages
  - Difficult to do with ongoing business with liabilities if boot is also issued
    If ANY boot—must count liabilities toward 20% boot allowance
  - Limits on pre-transaction asset dispositions “substantially all” requirement

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative (“KPMG International”), a Swiss entity. All rights reserved.
52684DAL

§368(a)(1)(D) D reorganizations

- The Code defines a D reorganization as a transfer by a corporation of all or a part of its assets to another corporation if, immediately after the transfer, the transferor or one or more of its shareholders (including persons who were shareholders immediately before the transfer), or any combination thereof, is in control of the corporation to which the assets are transferred; **but only if stock or securities of the controlled corporation are distributed in pursuance of a plan or reorganization in a transaction that qualifies under Code Secs. 354, 355, or 356.**

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative (“KPMG International”), a Swiss entity. All rights reserved.
52684DAL

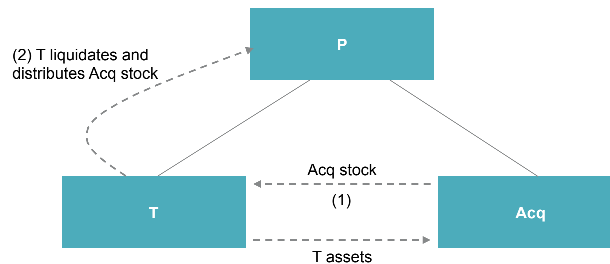
Copyright © 2012 Association of Corporate Counsel

Requirements for a D reorg

- The Control Requirement: A or TP must own at least 50% of the total combined voting power of all classes of stock entitled to vote or at least 50% of the total value of all classes of stock of B. Code Sec. 368(a)(2)(H).
- The Substantially all Requirement: B must acquire "substantially all" of A's assets. Code Sec. 354(b).
- The Distribution Requirement: A must distribute stock or securities of B to TP in a transaction qualifying under Code Secs. 354, 355 or 356.
- The COBE Requirement: B must continue A's historical business or use a significant portion of A's historical business assets in a business.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Basic transactions



Tax Consequences

- T—no gain, loss (§ 361)
- Acq—carryover basis in assets, succeeds to T tax attributes (§§ 362, 381)
- P—no gain, loss (§ 354); if "boot" received, gain recognized under boot-within-gain rule of § 356

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

All-cash D reorganizations – Meaningless gesture

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Meaningless gesture

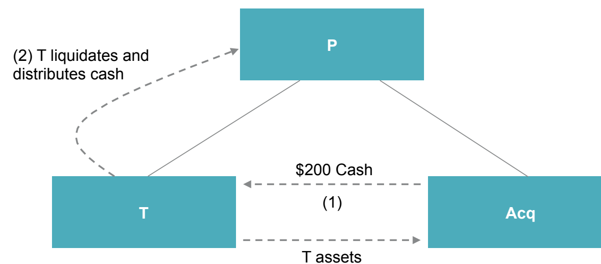
Meaningless Gesture

- Courts have held that an actual distribution of stock is not required where the shareholders of the transferor corporation already own, in the same proportions, stock in the acquiring or transferee corporation, because the issuance of further stock would be a meaningless gesture. *See, e.g.,* James Armour Inc. v. Commissioner, 43 T.C. 295 (1964).

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

All-cash D reorganizations – Meaningless gesture



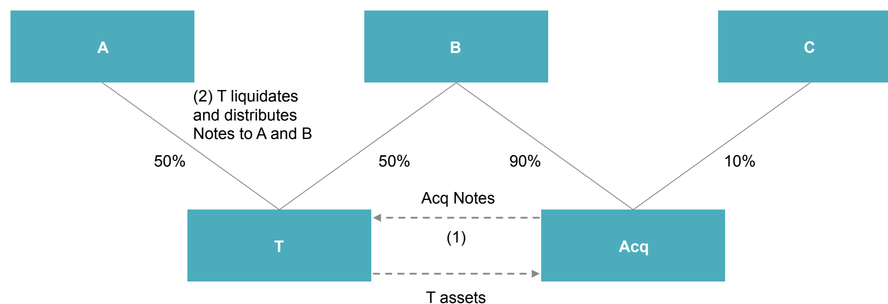
Tax Consequences

- Even though no "stock or securities of [Acq] are distributed in a transaction which qualifies under § 354 … or 356", the transaction qualifies as a D Reorganization.
- T is deemed to receive Acq stock from Acq (in addition to the cash it actually received) and distributing the stock and cash to P in exchange for the T stock held by T.
- Pursuant to § 356(a)(1), P will recognize gain to the extent of the cash received.
  - P's gain will be a dividend to the extent of the earnings of profits of T and Acq. § 356(a)(2).

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

All-cash D reorganizations – Meaningless gesture (continued)

Disproportionate Ownership



- This transaction does not qualify as an Acquisitive D Reorganization. See PLR 200551018. The meaningless gesture doctrine would not apply to deem an issuance of stock to A and B.
- What if a de minimis amount of Acq stock was issued to B?

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Temporary and final regulations – General

- In 2006, the IRS and Treasury published temporary regulations providing guidance regarding when the Distribution Requirement is satisfied nonwithstanding the fact that there is no actual distribution of stock and/or securities. T.D. 9303 (as amended by T.D. 9313).
- In 2009, the IRS and Treasury finalized these All-Boot D Reorganization regulations. T.D. 9475. The final regulations retain the rules of the prior temporary regulations, but include certain additions and modifications in response to comments received by the IRS and Treasury.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

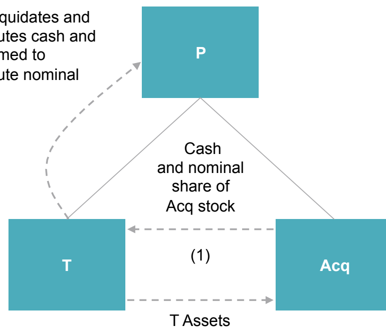
Temporary and final regulations – Basic rules

- The temporary and final All-Boot D Reorganization regulations provide that the Distribution Requirement will be satisfied even though no stock and/or securities are actually issued in the transaction if the same person or persons own, directly or indirectly, all of the stock of the transferor and transferee corporations in identical proportions.
- The transferee will be deemed to issue a nominal share of stock to the transferor in addition to the actual consideration exchanged for the transferor's assets.
  - The nominal share is then deemed distributed by the transferor to its shareholders and, when appropriate, further transferred through chains of ownership to the extent necessary to reflect the actual ownership of the transferor and transferee corporation.
  - The nominal shares are respected for all U.S. federal income tax purposes, including basis purposes.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Temporary and final regulations – Nominal share issuance



- If no consideration is received (or the consideration < FMV of Assets)
  - Transferee is treated as issuing stock with FMV equal to the excess of the FMV of Assets over FMV of Consideration.
- If FMV of Consideration = FMV of Assets
  - Transferee is deemed to issue a nominal share of stock.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

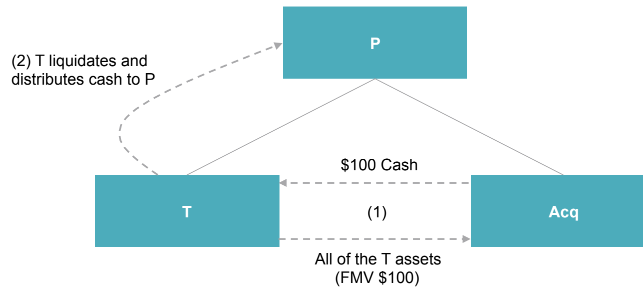
Temporary and final regulations – Other rules

- For purposes of determining the ownership of stock, the attribution rules of § 318(a) are applied with some modifications.
- De minimis variations in ownership and certain stock (e.g., § 1504(a)(4) stock) are not taken into account.
- The deemed issuance of stock does not apply if the transaction otherwise qualifies as a triangular reorganization

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

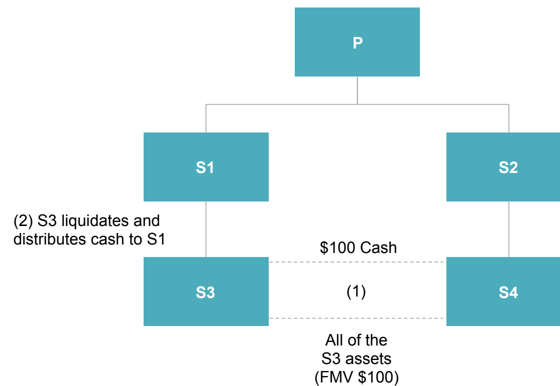
Temporary and final regulations – Basic example



- Because P owns all of the stock of both T and Acq, Acq is treated as issuing a nominal share of Acq stock to T, which T is treated as distributing to P.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Temporary and final regulations – Indirect ownership example



- Because P indirectly owns all of the stock of both S3 and S4, S4 is treated as issuing a nominal share of S4 stock to S3. S3 is treated as distributing the share to S1, who distributes it to P. P is then treated as contributing the share to S3.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Why do a (D)?

- Advantages
  - Can isolate liabilities—leave behind in shell
  - Merger law not necessary
  - Very flexible consideration requirements
- Disadvantages
  - Limits on pre-merger asset disposition “substantially all” requirement
- Scope of rules is uncertain
- Traps for the unwary—liquidation reincorporation

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative (“KPMG International”), a Swiss entity. All rights reserved. 52684DAL

90

D reorganizations – Overlap issues

- A merger by a corporation into another corporation controlled by the parent of the merging corporation or the parent corporation’s shareholders involves an overlap between an A reorganization and a D reorganization. In such overlap cases, the IRS has ruled that rules applicable to the D reorganization still apply.
- Similarly, a transfer of substantially all of a transferor corporation’s assets to an acquiring corporation solely for voting stock can qualify as both C reorganization and a D reorganization, if the acquiring corporation is controlled by the transferor’s shareholders and the transferor corporation liquidates following the transfer. In cases of overlaps between a C reorganization and a D reorganization, Code Sec. 368(a)(2)(A) provides that the D reorganization provisions will apply.
- By contrast, the IRS ruled in Rev. Rul. 57-276 that a transaction that qualifies as both a D reorganization and an F reorganization will be treated as a F reorganization for tax purposes.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative (“KPMG International”), a Swiss entity. All rights reserved. 52684DAL

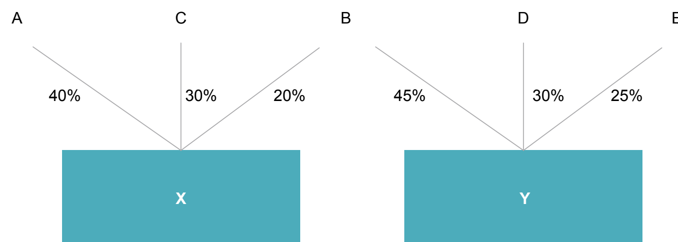
91

Overlap issues between code sec. 304 and the D reorganization

- Code Sec. 304 governs situations in which one or more persons are in control of each of two corporations and, in return for property, one of the corporations acquires stock in the other corporation from the person or persons in control. Rev. Rul. 75-161.
- When the target corporation is promptly liquidated, the transaction could also invoke the D reorganization provisions.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Rev. Rul. 77-427



A and B were father and son and C and D were father and son.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Rev. Rul. 77-427 (continued)

- A, B & C sold their X stock to Y for cash.
- Immediately thereafter X was liquidated into Y.
- A, B & C directly owned 100% of X prior to sale and by virtue of attribution under Code Sec. 318(a)(1)(A) owned 75% of Y.
- The IRS held that the transaction constituted a Code Sec. 304 stock acquisition followed by a Code Sec. 332 liquidation.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

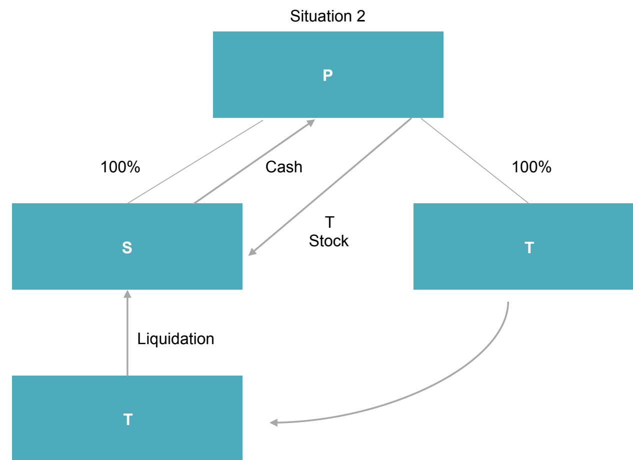
Significance of treating the transaction in Rev. Rul. 77-427 as a code sec. 304 transaction rather than a D reorganization.

- Entire amount of the cash received by A, B, and C for the sale of their X stock would be taxable as a dividend (under D Reorg Provisions, dividend income would be limited to gain realized. Code Sec. 356(a)).
- Dividends under Code Sec. 304 can draw from the E&P of both X and Y, while dividends under Code Sec. 356 are limited to the E&P of X.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Rev. Rul. 2004-83



© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Rev. Rul. 2004-83 (continued)

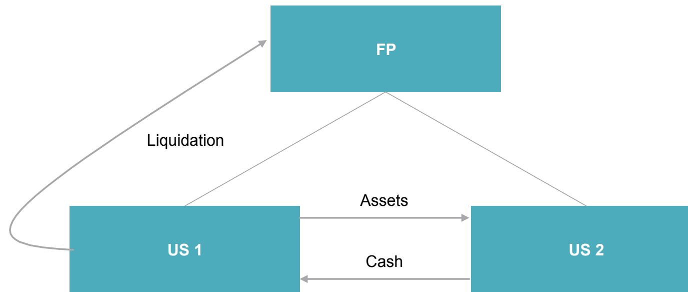
- As part of an integrated plan, S purchased all of the T stock from P for cash, following which T liquidated into S.
- P, S & T did not file consolidated returns.
- Declining to follow Rev. Rul. 77-427, the IRS held that the step transaction doctrine applied to treat the stock sale and liquidation as a D reorganization.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Pitfalls if a transaction qualifies as a D reorg

Transferor's basis in the transferred assets will carryover to the transferee corporation



US 1 has substantial NOLS subject to Code Sec. 382.
US 1 sells its assets at a gain to US 2 and liquidates

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

Pitfalls if a transaction qualifies as a D reorg (continued)

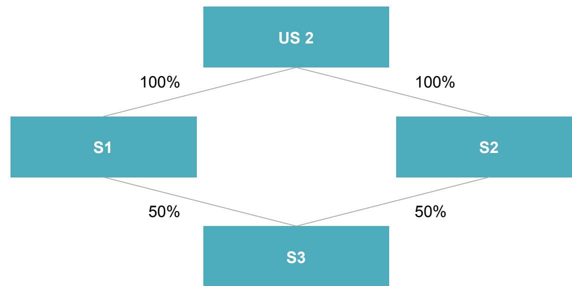
- If the sale is respected, the NOLs are refreshed (assuming the gains constitute RBIG) in the form of a basis step-up in the assets.
- If, however, the D reorg provisions apply, the basis of the transferred assets remains unchanged and US 1s NOLs carryover to US 2 subject to Code Sec. 382.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

Copyright © 2012 Association of Corporate Counsel

Options for breaking the D

- US 1 does not liquidate
- US 2 has 2 related corps acquire 1/3 each of US 1's assets so that no corporation acquires "substantially all"
- US 2 drops the acquired assets into a death diamond structure so that COBE is not satisfied.



© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

368(a)(1)(E) Recapitalization

- Some or all shareholder turn in stock or securities in a corporation and receive other stock or securities in the same corporation
- Frequent tool for transfer of closely held business from older generation to younger generation (but watch NQPS and § 306 w/pfd)
- No continuity requirements
- See also, § 1036

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

368(a)(1)(F)
Mere change in form

- Mere change in identify, form, or place of organization of one corporation
- Only one active corporation
- No continuity requirements
- Is an "F" an island? Rev. Rul. 96-29, proposed regulations

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

368(a)(1)(G)
Bankruptcy

- Transfer of assets from one corporation to another in a Title 11 or similar case

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

Copyright © 2012 Association of Corporate Counsel

Reorganization requirements

- Statutory requirements—§ 368(a)(1)
  A. State law merger
  B. Stock-for-stock
  C. Stock-for-assets
  D. Controlled corporations
  E. Recapitalization
  F. Mere change in form
  G. Bankruptcy
- Nonstatutory requirements
  – Business purpose
  – Continuity of proprietary interest
  – Continuity of business enterprise

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Continuity of Interest

- "Continuity of interest requires that in substance a substantial part of the value of the proprietary interests in the target corporation be preserved in the reorganization." Reg. 1.368-1(e)(1)(i)
- Type of interest
- Amount of interest

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

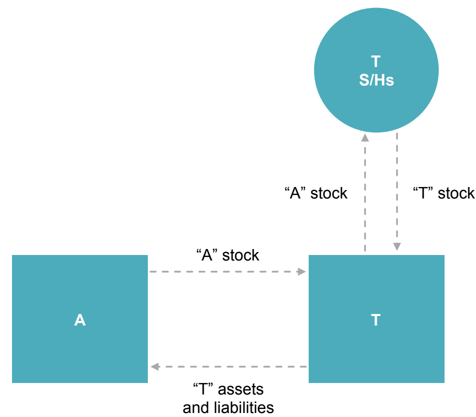
Copyright © 2012 Association of Corporate Counsel

COBE

- Old rules still applicable:
  - Acquiring must continue Target's historical business, or
  - Acquiring must use historical business assets in a business

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

Tax consequences of § 368 reorganizations



© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

Copyright © 2012 Association of Corporate Counsel

Tax consequences—Acquiring

- § 1032
  - No gain/loss on the use of A's (or generally stock of a corporation controlling A) stock to acquire property
  - Securities and cash are also okay
- Reg. § 1.1032-2
  - Gain/loss if use other property
- § 362(b): Transferred basis + gain recognized by T on such transfer [§ 357(b)]

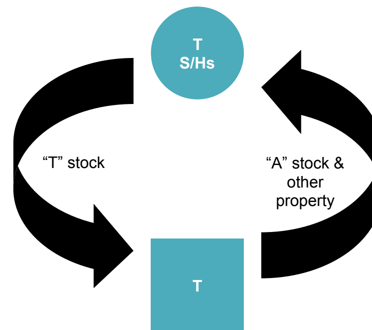
© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

Tax consequences—Target

- Receipt of boot—No gain [§361(a), (b)]
- § 357(a), (b)

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

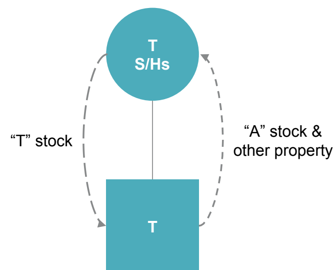
Tax consequences—Target (continued)



- §361(c)
- No G/L when consideration received from A is distributed
- However, if T retains appreciated property—gain on distribution

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Tax consequences—Target shareholders



- § 354(a)—No G/L—stock and securities for stock and securities
- § 356 (a)(1)—If boot received, gain recognized to extent of lesser of:
  1) Gain realized and
  2) Boot received
- §§ 356(a)(2)—Character of gain

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

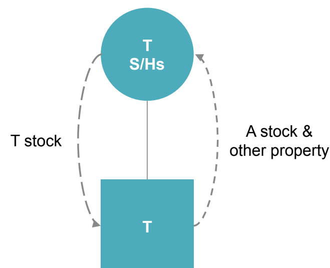
Copyright © 2012 Association of Corporate Counsel

Character of gain—§ 356(a)(2)

- If has the "effect of the distribution of a dividend," then dividend income to the extent of ratable share of E&P
- The remainder is gain from the exchange of property (capital gain)
- § 302(b) hypothetical redemption
- Clark, 109 S. Ct. 1455 (1989)
  - Uses post-reorganization redemption analysis

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Tax consequences—Target shareholder basis



- § 358(a)(1)
  - Basis of T stock minus boot received plus gain recognized equals basis of A stock
- § 358(a)(2)
  - Basis of other property = FMV

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Taxable versus Tax-Free Considerations

Taxable asset acquisition

- Buyer Consequences
  - Asset Basis = FMV
  - Asset Basis Allocation
  - Tax Attributes Stay with Seller
  - May Purchase select assets and liabilities
- Seller Consequences
  - Corporate level tax
  - Shareholder level tax upon distribution
    - CG vs. OI
  - Basis in consideration other than cash = FMV

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

Copyright © 2012 Association of Corporate Counsel

Tax-free acquisitions

- Buyer Consequences
  - Stock Basis = C/O
  - Asset Basis = C/O
  - Tax Attributes = C/O with limitations
  - Generally all assets and liabilities purchased
  - “Boot”
- Seller Consequences
  - No Shareholder level gain except “boot”
  - No Corporate level gain
  - Basis in stock of Buyer equals former basis in Target shares

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative (“KPMG International”), a Swiss entity. All rights reserved. 52684DAL

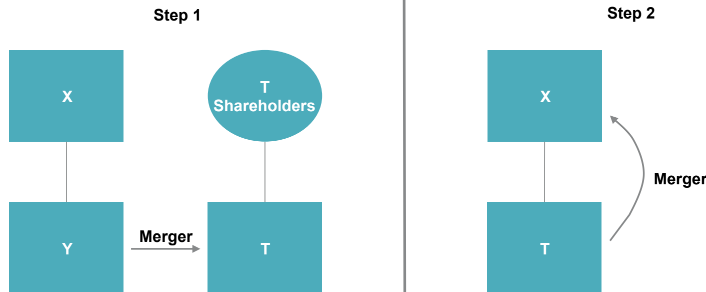
QSP as part of a larger transaction

- What if a QSP is part of a larger transaction that could be a tax-free reorg?

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative (“KPMG International”), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Revenue ruling 2001-46
Situation 1



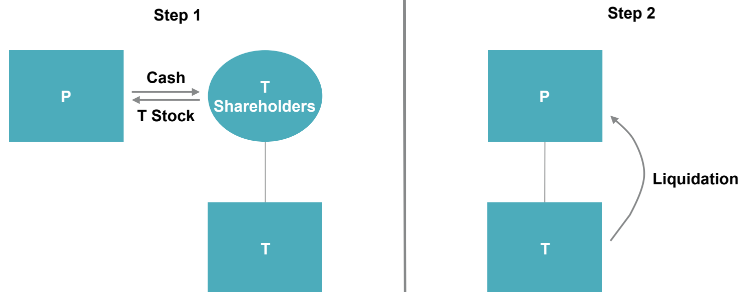
- Y merges into T
- T Shareholders receive 70% X voting stock and 30% cash

- As part of a plan, T merges into X

- Step 1 Merger would not qualify as an A reorganization
  Code § 368 (a)(2)(E) requires exchange 80% of T stock for X stock
- Rev. Rul. 67-274 v. 90-95

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL
118

Kimbell-Diamond
14 T.C. 74 (1950)



- P acquires T stock for cash

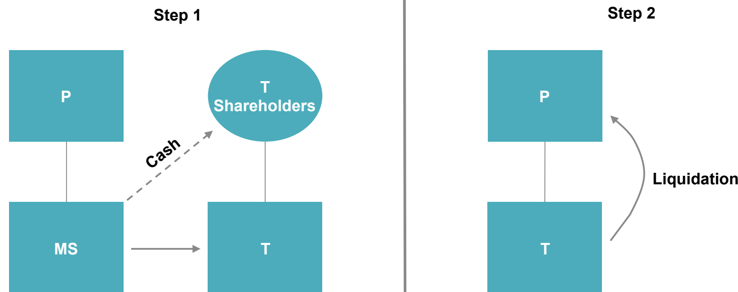
- T liquidates into P

- P's acquisition of T's stock for cash followed by the liquidation of T was recharacterized as a taxable acquisition of T's assets
  - P always planned on acquiring T's assets
- Congress repealed some or all of Kimbell-Diamond with Code § 338

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL
119

Revenue ruling 90-95 (situation 2)
See also treasury regulation § 1-338-3(d)

Step 1



- MS merges into T
- T shareholders receive cash in exchange for their T stock

Step 2

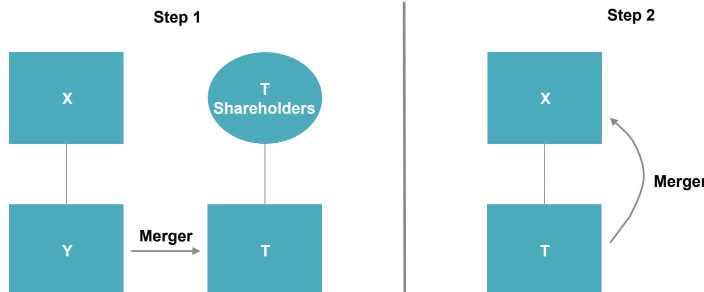
- As part of plan, T liquidates into P

- Step transaction doctrine applies to disregard MS and transaction is treated as a QSP under Code § 338
- Step transaction doctrine does not apply to treat stock acquisition and liquidation as an asset purchase

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Revenue ruling 2001-46
Situation 1

Step 1



- Y merges into T
- T shareholders receive 70% x voting stock and 30% cash

Step 2

- As part of a plan, T merges into X

- Steps are integrated and transaction is treated as a single statutory merger of T into X that qualifies as an A reorganization without regard to Code § 368(a)(2)(E)
- Treatment as a reorganization doesn't violate Code § 338 policy

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

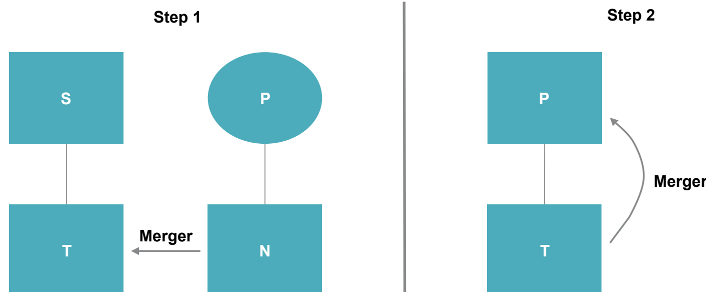
Copyright © 2012 Association of Corporate Counsel

Revenue ruling 2001-46

- Revenue Ruling 2001-46 applied the step transaction doctrine to create a reorganization, which did not violate the policy of Code § 338 because the target's inside asset basis is carried over
- The Problem: by applying the step transaction doctrine to create a reorganization, the government may upset the plans of the acquirer to make a Code § 338(h)(10) election and obtain an asset basis step-up
- Therefore, Treas. Reg. § 1.338(h)(10)-1(c)(2) allows a Code § 338(h)(10) election where the first step is a QSP, despite the fact that a related merger of target into acquirer or an affiliate would otherwise be viewed as a reorganization

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

Example 1



- P forms new corp. N
- N merges into T
- S receives 50% P stock and 50% cash

- As part of a plan, T merges into P

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

Copyright © 2012 Association of Corporate Counsel

Example 1 (QSP)

Step 1

- P forms new corp. N
- N merges into T
- S receives 50% P stock and 50% cash

Step 2

- As part of a plan, T merges into P

- Step one is a QSP
- Step Transaction Doctrine will treat Steps 1 and 2, combined together, as a statutory merger and an "A" reorganization
- Can make a Code § 338(h)(10) election to obtain step-up

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Example 2

Step 1

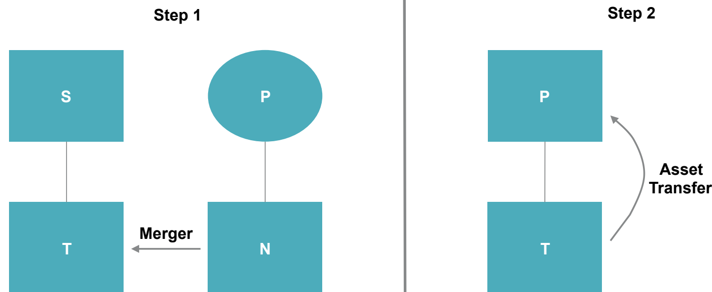
- P forms new corp. N
- N merges into T
- S receives 50% P stock and 50% cash

Step 2

- T assets assigned to P
- As part of a plan, T ceases its separate legal existence

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Example 2 (QSP)



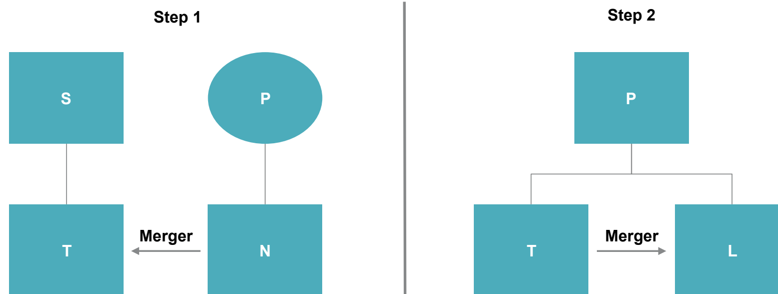
- P forms new corp. N
- N merges into T
- S receives 50% P stock and 50% cash

- T assets assigned to P
- As part of a plan, T ceases its separate legal existence

- Steps 1 and 2, combined together, do not constitute a reorganization
  - No statutory merger of T & P, so cannot be an "A" reorganization
  - Cannot be a "C" reorganization because consideration < 80% stock
- Step Transaction Doctrine cannot apply to create taxable asset deal
- Can get step-up only by Code § 338(h)(10) election

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Example 3



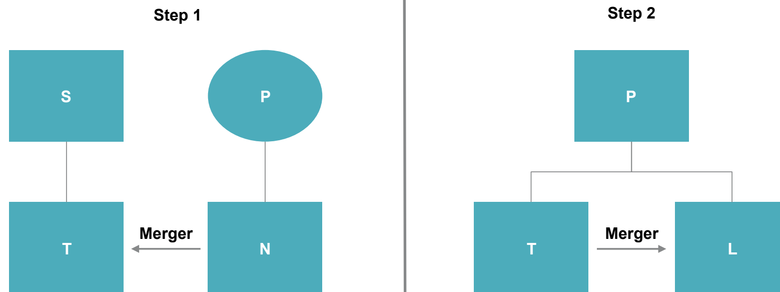
- P forms new corp N
- N merges into T
- S receives 50% P stock and 50% cash

- T merges into L in a sideways merger

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Example 3 (QSP)



- P forms new corp N
- N merges into T
- S receives 50% P stock and 50% cash

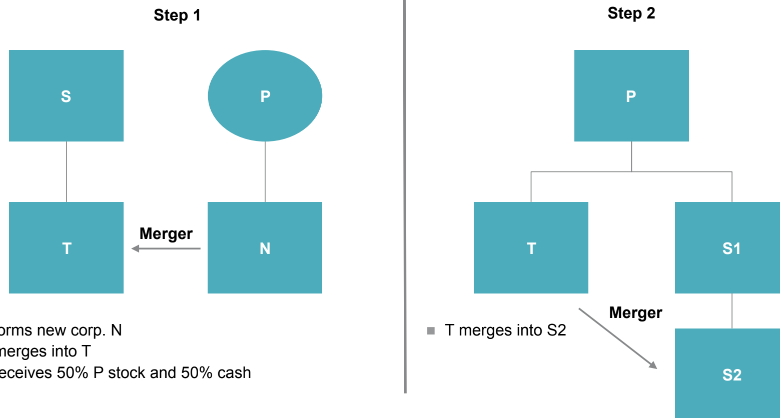
- T merges into L in a sideways merger

- Steps 1 and 2 combined together constitute a reorganization under Code § 368(a)(1)(A) via Code § 368(a)(2)(D)
- Step Transaction Doctrine applies to treat steps as an acquisition of T's assets by L through a single statutory merger
- Can also make a Code § 338(h)(10) election

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

128

Example 4



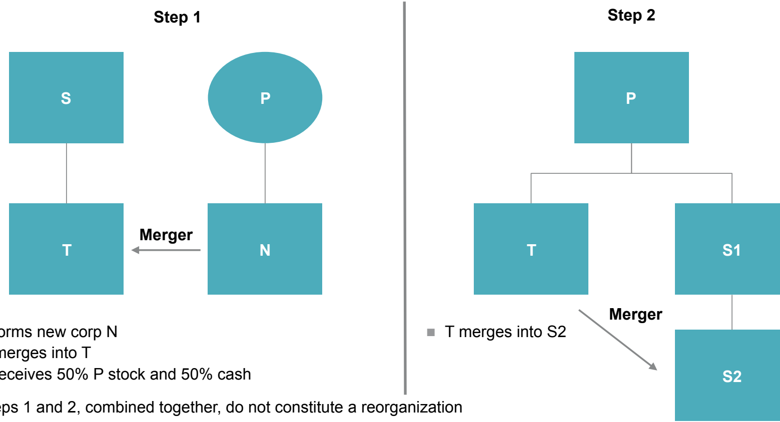
- P forms new corp. N
- N merges into T
- S receives 50% P stock and 50% cash

- T merges into S2

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

129

Example 4 (QSP)



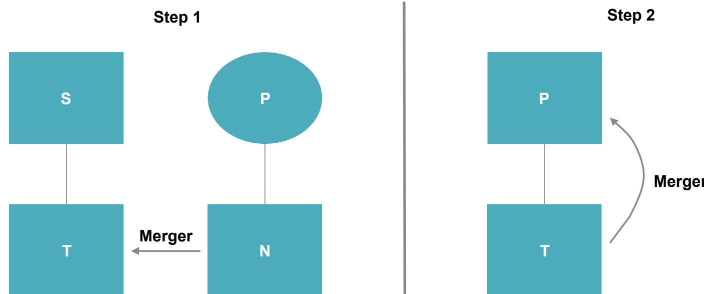
- P forms new corp N
- N merges into T
- S receives 50% P stock and 50% cash

- T merges into S2

- Steps 1 and 2, combined together, do not constitute a reorganization
  - Can only use parent stock in an (a)(2)(D)
  - No S1 stock used in merger (used P stock)
- Step Transaction Doctrine cannot apply
- P can only get a step up in T's assets by making a Code § 338(h)(10) election

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Example 5



- P forms new corp N
- N merges into T
- S receives P voting stock

- As part of a plan, T merges into P

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Example 5 (No QSP)

Step 1

S — P
T ← Merger — N

- P forms new corp N
- N merges into T
- S receives P voting stock

Step 2

P
T — Merger → P

- As part of a plan, T merges into P

- Steps 1 and 2, together, constitute an “A” reorganization
- No Code § 338(h)(10) election or asset step-up available

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Acquisition Agreements

Copyright © 2012 Association of Corporate Counsel

Four Basic Acquisition Structures

- Taxable stock acquisition
- Taxable asset acquisition
- Tax-free stock acquisition
- Tax-free asset acquisition

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Types of Acquisition Agreements

- Stock Purchase Agreement
- Asset Purchase Agreement
- 2 - Party Merger Agreement
- 3 - Party Merger Agreement
- Asset Contribution Agreement
- Stock Exchange Agreement

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Buyer's Primary Tax Issues

- Apportionment of Target's tax liability
- Basis in Target's assets
- Availability of Target's tax attributes (i.e., net operating loss carryovers)
- Control of Tax filings and audits

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Buyer's Secondary Tax Issues

- Basis in Target or Acquisition Vehicle
- Access to Information
- Deductibility of acquisition costs
- Target's E & P

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Seller's Tax Issues

- Recognition of Gain or Loss
- Appointment of Target's Tax Liabilities
- Control of Tax Filings and Audits
- Deductibility of Severance Costs

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Timing

- Most transactions involve a period of time in which Buyer familiarizes himself with Target's business
- Timing of due diligence period may vary depending upon the need for confidentiality, regulatory, political and market considerations
- Sometimes, Buyer will not commence any due diligence until after the parties have signed a definitive agreement
- At other extreme, parties may sign an option or non-binding letter of intent followed by a period of due diligence, but not sign a definitive agreement until closing
- Most common scenario is limited due diligence, followed by the signing of a definitive agreement with a period of more extensive due diligence prior to closing

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

First Principals

- Tax Professional as a team member
- Understand the Deal
- Start Fresh

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Private vs. Public Transactions

- **Private Transaction**
  - Should expect, as Buyer, to obtain representations and warranties on Target's tax history extending to the expiration of the Statute of Limitations.
  - Buyer should also expect Seller to indemnify for pre-closing taxes.
  - Indemnification can be separate or can be triggered by reps.
- **Public Transaction**
  - Normally, Buyer will receive extensive reps and warranties that expire upon closing.
  - Normally Sellers will not indemnify for pre-closing Taxes.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Function of Tax Provisions in Acquisition Agreements

- Supply the Buyer with a tax history of the Target business for pre-closing periods
- Designate the party responsible for filing any unfiled tax returns relating to the Business
- Designate the party responsible for any tax liabilities for pre-closing periods
- Apportion tax liabilities for the Business for taxable periods ending after but beginning before the Closing Date (the “Stub Period”)

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative (“KPMG International”), a Swiss entity. All rights reserved.
52684DAL

Function of Tax Provisions in Acquisition Agreements, continued

- Designate the party to control the settlement of any tax controversies relating to the Business
- Designate the party entitled to any tax benefits arising from the operation of the Business
- In a stock purchase agreement from an affiliated group, they provide a framework for settling existing tax sharing agreements between the Seller and the Target corporation
- Provide procedures for making relevant tax elections

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative (“KPMG International”), a Swiss entity. All rights reserved.
52684DAL

Copyright © 2012 Association of Corporate Counsel

Sections You Should Focus on as a Tax Professional

- Definitions Section
1. **"Taxes"**
2. **"Tax Returns"**
- Purchase Price – Is the purchase price a function of net assets or is there a purchase price adjustment provision
(Balance Sheet Deal)
- Allocation of Purchase Price

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

Tax Representations and Warranties

- **PURPOSE**
  - Due Diligence Function
  - Escape Function
  - Indemnification Function
  - Relationship to Disclosure Schedule

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

Copyright © 2012 Association of Corporate Counsel

Representations with respect to Pre-Closing Taxes

- Filing of Tax Returns
- Payment of Taxes
- Tax Reserves
- Tax Liens
- Withholding Taxes
- Extensions of Filing Dates
- Waivers of Statutes of Limitations
- Audit, Administrative and Court Proceedings
- Powers of Attorney
- Tax Rulings
- Availability of Tax Returns
- Tax Sharing Agreements

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

146

Representations with Respect to Tax Attributes

- Depreciation and Investment Tax Credits
- Changes in Accounting Methods
- Golden Parachute Payments
- Substantial Understatement Penalty
- Subchapter S Status
- Foreign Tax Returns
- Code §338 Elections
- Applicable High Yield Discount Obligations
- U.S. Real Property Holding Company status
- Deductibility of Contractual (Obligations (catch-all)
- Acquisition Indebtedness
- Contractual Liability for Taxes
- Intercompany Transactions
- Net Operating Loss Carryovers
- Tax Credit Carryovers

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

147

Qualifiers to Watch

- Materiality
- Material Adverse Effect
- Knowledge
- Taxes “Shown on Return”
- Disclosure Schedules

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative (“KPMG International”), a Swiss entity. All rights reserved. 52684DAL

Buyer’s Requested Representation

- All Tax Returns required to be filed by or on behalf of the Target/Seller have been duly filed on a timely basis and such Returns are true, complete and correct. Target/Seller has paid all pre-closing taxes due, whether or not shown on the tax returns.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative (“KPMG International”), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Seller's Revised Representation

- "To the knowledge of the Seller all material Tax Returns required to be filed by or on behalf of Target/Seller have been duly filed, and Target/Seller has paid all taxes shown due on such returns.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Survival of Representations and Warranties

- Generally do not survive Closing in a public transaction.
- Generally limited survival period in private transaction.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Tax Covenants or Tax Matters Article

- Code §338(h)(10) Elections
- Private Letter Rulings
- Loss Disallowance Rules
- Tax Sharing Agreements
- Unfiled Tax Returns
- Transfer Taxes
- Post-Closing and Stub Period Taxes
- Tax Cooperation
- Retention of Records
- Indemnification
- Tax Benefits Resulting from Audit Adjustments
- Post-Closing Adjustments to Deferred Tax Account
- Refunds
- Notification of Proceedings; Control
- Waiver of loss on sale of subsidiaries shares

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

152

Tax Indemnities – Private Targets

- Can be a part of the overall indemnification or can be separate
- Generally, if separate indemnities run both ways.
- Tax consequences of payment
- Creditworthiness issues

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

153

Limits on Indemnification

1. Baskets
2. Ceilings

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Asset vs. Stock Deal

- Current trend is towards extensive tax representations and warranties in both types of transactions
- However, the tax provisions are far more important when Buyer is purchasing stock
- When purchasing a subsidiary from a consolidated group, Buyer should always be cognizant of §1.1502-6 liability

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Buyer's Objectives

- Want Seller representations with respect to taxes that are extensive and unqualified
- Separate Tax Indemnification
- Section 338(h)(10) election
- Allocation of purchase price
- Tax benefits and refunds

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

Seller's Objectives

- Disclosure
- Limit liability to breaches of reps or warranties
- Control audits and settlements
- Audit adjustment provisions
- Purchaser to pay for any additional taxes from Code §338(h)(10)

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

Copyright © 2012 Association of Corporate Counsel

Basis Issues

- If no Code Sec. 338(h)(10) is available, Buyer will want to determine the tax basis in Target's assets.
- If Buyer intends to sell of some of Target's assets to finance the acquisition, it may be necessary to conduct a basis study to determine the feasibility of the acquisition.
- If basis is a critical issue to the Buyer, Buyer may ask Seller to represent Target's basis in its assets in the Acquisition Agreement.
- If Seller gives a representation with respect to basis, the parties must come up with a formula to calculate damages upon breech of the representation.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

E&P Issues

- If Buyer is a REIT or using a REIT to finance the acquisition, it may be necessary to conduct an E&P study to determine the feasibility of the acquisition.
- If E&P is a critical issue to Buyer, if basis is a critical issue to the Buyer, Buyer may ask Seller to represent Target's E&P in the Acquisition Agreement.
- If Seller gives a representation with respect to E&P, the parties must come up with a formula to calculate damages upon breech of the representation.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

NOLs

- If Buyer is pricing in the value of Target's NOLs, need to determine whether they are subject to any previous limitations under Code § 382.
- If NOLs are critical to Buyer, may ask the Seller to represent both the amount of Target's NOLs and the availability of such NOLs post-closing.
- If Seller gives a representation with respect to NOLs, the parties must come up with a formula to calculate damages upon breech of the representation.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Purchase Price Adjustments

- Price may or may not be a function of Target's net assets
- If there is a purchase price adjustment, Buyer needs to confirm the adequacy of Target's tax reserves
- Conversely, Seller should make sure that its tax indemnification obligations are net of tax reserves on closing balance sheet
- If Seller believes its tax reserves are overstated, it may want to require the Buyer to refund such excess, once proven
- If refunds are booked as an asset, make sure the agreement provides that refunds go to Buyer

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Tax Consequences of Indemnity Payments

- Effect on purchase price
- Effect on Code §(h)(10) election
- Sellers sometimes seek to reduce indemnity obligations for tax benefits realized by Target from the payment of the obligation for which they are indemnified.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Tax Sharing Agreements

- As Buyer, be sure to terminate tax sharing agreement as of closing date
- Acquisition Agreement should supercede all rights and obligations under the Tax Sharing Agreement

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Other Considerations

- **Auctions**
  - Sometimes need to temper position. Communication with financial executives is key
- **Private Placements**
  - Customary to receive tax representatives and Indemnification, but how do you measure "Damages"

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Final Word of Warning

- **Always Follow the Deal!**

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Success Based Fees

Rev. Proc. 2011-29
Safe Harbor allocation of success-based fees

- Treas. Reg. §1.263(a)-5(a) requires taxpayers to capitalize costs incurred to facilitate (i.e., to investigate or otherwise pursue) a capital transaction.
- Despite the general rule, taxpayers are not required to capitalize costs for certain transactions described in Treas. Reg. §1.263(a)-5(e) if:
  - The costs were incurred prior to the earlier of (i) the date a letter of intent, exclusivity agreement or other similar communication is executed or (ii) the date the material terms of the transaction are approved by the taxpayer's board of directors, and
  - The costs are not inherently facilitative, such as costs for
    - Securing an appraisal or fairness opinion
    - Structuring costs and obtaining tax advice
    - Preparing transaction documents

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Rev. Proc. 2011-29
Safe Harbor allocation of success-based fees

- Under Treas. Reg. §1.263(a)-5(f), success-based fees facilitate a transaction and must be capitalized if the transaction is consummated.
  - Success-based fees are contingent upon the successful closing of a transaction.
- Exception – A taxpayer may avoid capitalization by maintaining sufficient documentation to establish that a portion of the fees do not facilitate the transaction.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Rev. Proc. 2011-29
Safe Harbor allocation of success-based fees

- Regulations provide strict rules for maintaining documentation to avoid capitalization of success-based fees.
  - Documentation must be completed on or prior to the due date of the taxpayer's tax return (including extensions) for the year in which the transaction closes.
  - Mere allocation between facilitative and non-facilitative costs is not sufficient.
  - Must consist of supporting documentation (e.g., time records, itemized invoices, etc.) that identify:
    - The various activities performed by the service provider.
    - The amount of the fee (or percentage of time) allocable to each activity performed.
    - The date the activity was performed.
    - The name, address, and telephone number of the service provider.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Rev. Proc. 2011-29
Safe Harbor allocation of success-based fees

- Application of the Regulation created controversy between taxpayers and the IRS as to what counts as documentation (e.g., "other records") and what is sufficient.
- PLR 2008300009 (April 11, 2008)
  - The regulation does not require time records: other records may be used to establish an appropriate allocation.
  - A determination as to whether records establish the allocation is a question of fact to be determined upon examination.
- – TAM 201002036 (January 15, 2010)
  - Allocation spreadsheets developed by an accounting firm as a part of a transaction costs study qualify as a "record" for purposes of establishing the portion of an investment bank's success-based fee that did not facilitate the transaction.
  - The spreadsheets must be evaluated in determining whether the documentation maintained by the taxpayer is sufficient.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Rev. Proc. 2011-29
Safe Harbor allocation of success-based fees

- On April 8, 2011, IRS released Revenue Procedure 2011-29 (published in the May 2, 2011 IRB), providing a safe-harbor election for the allocation of success-based fees between facilitative and non-facilitative costs, in lieu of maintaining documentation.
- The IRS will not challenge a taxpayer's allocation of a success-based fee if the taxpayer
  - Treats 70% as an amount that does not facilitate the transaction (e.g., a deductible or amortizable cost),
  - Treats 30% as an amount that does facilitate the transaction (i.e., a capitalized cost), and
  - Attaches a statement to its return for the year the fee is paid or incurred in which it elects the safe harbor, identifies the transaction, and states that amount of the success-based fee amounts that are deducted and capitalized.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Rev. Proc. 2011-29
Safe Harbor allocation of success-based fees

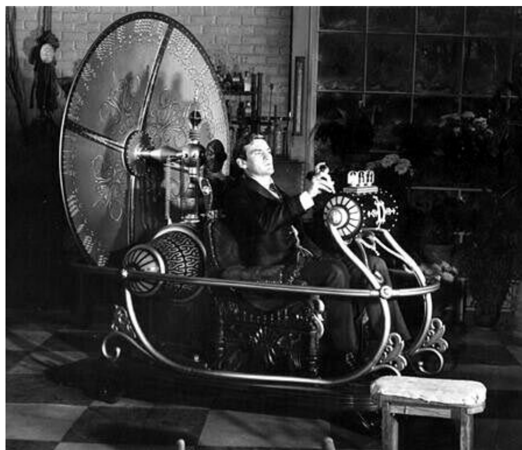
- The election:
  - Applies only to covered transactions
    - Taxable acquisition of assets that comprise a trade or business.
    - Taxable acquisition of an ownership interest in an entity if taxpayer and target are related parties immediately after the acquisition.
    - A reorganization under Section 368.
  - Must be made, if desired, for each transaction,
  - Cannot be protective, and
  - Is irrevocable, if made.
- Open items include:
  - Allocation of success-based fees for a covered transaction and a non-covered transaction (e.g., a borrowing).
    - Should the entire success-based fee be allocated on a 70%/30% basis?
    - If so, should the taxpayer determine the portion of the capital allocation attributable to borrowing costs and amortize a portion of the 30%?
  - Level of documentation required for taxpayers who do not make the election.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.
52684DAL

Rescinding transactions and other retroactive tax planning

Copyright © 2012 Association of Corporate Counsel

The Latest in tax technology solutions…



From the film "The Time Machine" (1960)

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Retroactive tax planning is Not Per Se wrong

- Some Examples of Government-Approved Time Travel:
  - Check-the-Box Election
  - § 9100 Relief
  - Carrybacks
  - Retirement Plan Contributions
  - Certain Charitable Donations (e.g., Haiti earthquake relief)
  - Any election that is not made contemporaneously with a completed transaction
  - Amendments to Partnership Agreements

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Rescinding transactions

- The IRS currently follows Revenue Ruling 80-58 in issuing private letter rulings on rescission.
  - Generally required elements of a rescission from the revenue ruling and relevant authorities:
    - Parties must be returned to status quo ante.
    - Rescission must occur in same tax year as original transaction.
    - Only a contract may be rescinded.
    - Rescission must be styled as such (i.e., cannot just do an opposite transaction and later claim that that constituted a rescission).
    - Parties must have no further obligations to each other with respect to the contract being rescinded.
  - However, more recent private letter rulings have interpreted these requirements quite liberally.

See also, Penn v. Robertson, 115 F.2d 167 (4th Cir. 1940); Rev. Rul. 78-119; Rev. Rul. 77-119; PLR 200701019; PLR 200613027; PLR 200533002; PLR 9312027; PLR 9104039.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Rescinding transactions: PLR 201113023

- A subsidiary ("Sub 1") of an affiliated group of corporations filing a consolidated federal income tax return sold certain assets to an unrelated third party (via sale of a disregarded entity).
- Following the sale, the affiliated group reviewed its operating structure and engaged in certain steps to restructure the group including the following:
  - Sub 1 transferred certain assets to new wholly-owned subsidiary ("NewCo");
  - Liquidated certain disregarded entities;
  - Sub 1 distributed an intercompany receivable to is parent;
  - Sub 1 merged into Parent and extinguished certain non-interest bearing payables and receivables.
- Parent became concerned about the tax consequences of certain steps of the transaction.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Rescinding transactions: PLR 201113023 (continued)

- Parent engaged in certain steps to unwind the undesirable steps of the restructuring
  - Parent formed a New Sub 1 with identical articles of incorporation and bylaws to former Sub 1 but noted that certain changes to voting rights may be made in the future.
  - Parent transferred all of the assets previously held be Sub 1 to New Sub 1.
    - Notably, certain assets of Sub 1 had been transferred to NewCo.
  - Parent transferred the stock of NewCo to New Sub 1.
  - All intercompany debt was reinstated.
  - "NewCo would have been formed without regard to the merger of Sub 1 into Parent."
- IRS ruled as follows:
  - Merger of Sub 1 into Parent will be treated as not having occurred. Sub 1 and Parent will be treated as two separate corporations at all times during the tax year.
  - Parent will be treated as shareholder of Sub 1 at all times during the tax year, and Sub 1 will be treated as a member of the affiliated group at all times during the tax year.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Rescinding transactions: PLR 201021002

- Pursuant to a restructuring plan, a parent company engaged in a series of steps in which it contributed various DEs to a regarded subsidiary for no consideration.
- The parent intended to contribute its interests in these DEs along with the outstanding debt between it and the DEs, which was disregarded for federal tax purposes.
- Parent inadvertently neglected to contribute the debt along with the DEs and, in the case of one subsidiary, also neglected to contribute all of the ownership interests.
- The debt of the DEs held by parent became regarded as debt owed by the new regarded owner of the DEs, presumably constituting boot in a § 351 transaction. Because of the incomplete transfer, one of the DEs became a regarded partnership with the parent and new regarded owner as its partners.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Rescinding transactions: PLR 201021002 (continued)

- Pursuant to a rescission agreement, parent undertook steps to undo the transaction.
  - The unintended steps of the transaction were unwound (i.e., all of the DEs to which the "springing debt" and unintended partnership issues applied were transferred back to their original owners).
- Parent sought rulings regarding the effectiveness of the rescission. Parent notified the IRS that it intended to re-do the transaction after the effective date of the rescission to achieve its initial objectives. Relevant rulings included:
  - The initial transactions were disregarded.
  - The DEs were treated as owned by parent at all times from the effective date of the initial transaction through the effective date of the rescission.
  - The DE debt was treated as disregarded at all times from the effective date of the initial transaction through the effective date of the rescission.
  - The unintended partnership was treated as a disregarded entity at all times from the effective date of the initial transaction through the effective date of the rescission.

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Rescinding transactions: Questions and considerations

- What does it mean to restore the parties to their original position?
- Is the time value of money relevant?
- Is a rescission treated as two offsetting transactions, or no transaction at all?
- What if the parties have different tax years?
- Does the taxpayer's purpose matter?
- Are the recent rulings too good to be true?

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel

Backdating documents

- Questions & Considerations:
  - What is the purpose of the backdated document?
  - Is there any contemporaneous evidence of the parties' intent or agreement?
  - When is the transaction treated as occurring under corporate law?
  - Does disclosure of backdating eliminate concerns? Is "as of" backdating adequate disclosure?
- *See, e.g.,:*

  Moore v. Comm'r, 93 TCM 1275 (2007).

  Medieval Attractions, 72 TCM 924 (1996).

  Baird v. Comm'r, 859 F.2d473 (7th Cir. 1988).

  Georgiou v. Comm'r, 70 TCM 1341 (1995).

© 2012 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. 52684DAL

Copyright © 2012 Association of Corporate Counsel