

Internal Revenue Service (I.R.S.)

Revenue Procedure

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Conditions under which the Internal Revenue Service will issue rulings on waiver of dividends transactions where a family relationship exists between the waiving and remaining stockholders.

SECTION 1. PURPOSE.

The purpose of this Revenue Procedure is to specify the conditions which must be present before the Internal Revenue Service will consider issuing a ruling on a proposed waiver of dividends transaction.

SEC. 2. BACKGROUND.

The Service has published two Revenue Rulings involving a waiver by a majority stockholder of his right to future underdeclared dividends.

.01 Revenue Ruling 45, C.B. 1953--1, 178, described a fact situation under which no family or direct business relationship existed between the majority and minority stockholders, and the waiver was executed for a valid business purpose. The Revenue Ruling concluded that any dividend payments to the minority stockholders would not result in income to the waiving stockholder.

.02 On the other hand, Revenue Ruling 56--431, C.B. 1956--2, 171, involved a waiver by a majority stockholder whose relatives owned 25 percent of the stock of the corporation. Because of the existence of the significant family interest, the alleged business purpose was considered incidental and the waiver was considered as having been executed primarily for the benefit of the related stockholders. The Revenue Ruling concluded that the waiving stockholder would be taxed on the increased distribution to the related stockholders resulting from the waiver.

.03 Revenue Ruling 65--256, C.B. 1965--2, 85, although not involving an explicit waiver of dividends, did involve a merger under the terms of which the majority stockholder of one of the corporations agreed to accept a separate class of stock in the successor corporation subject to certain dividend limitations. In that ruling, members of the majority stockholder's family owned only 0.06 percent of the total capital stock of the surviving corporation and there were bona fide business reasons for the majority stockholder's acceptance of a class of stock with dividend restrictions. The ruling concluded that the majority stockholder would not be in constructive receipt of income when dividends are paid on a second class of stock.

SEC. 3. REQUESTS FOR RULINGS.

Based upon the Revenue Rulings described above, the Service will consider a request for a ruling on a proposed waiver of dividends transaction under the following conditions:

.01 A bonafide business reason must exist for the proposed waiver of dividends.

.02 The relatives of the stockholder proposing to waive his right to future dividends must not be in a position to receive more than 20 percent of the total dividends distributed to the nonwaiving shareholders. For this purpose the relatives of a waiving stockholder include his brother and sister (whether by the whole or half blood), spouse, ancestors, and lineal descendants, the spouses of his brothers and sisters (whether by the whole or half blood) and the spouses of his lineal descendants.

.03 A ruling issued on a proposed waiver of dividends transaction will clearly indicate that the ruling will no longer be applicable if any change in the stock ownership during the waiver period enables nonwaiving relatives to receive more than 20 percent of a dividend, unless the change occurs because of death.

.04 A ruling issued on a proposed waiver of dividends transaction will not be effective for a period longer than three years from the date of the ruling.

.05 A request for a ruling on a proposed waiver of dividends transaction must be submitted to the National Office in accordance with Revenue Procedure 67--1, page 544, this Bulletin.

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