

## Internal Revenue Service (I.R.S.)

## Revenue Ruling

## SPIN-OFF OF SUBSIDIARY, FOLLOWED BY ITS MERGER WITH UNRELATED CORPORATION

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Spin-off of subsidiary, followed by its merger with unrelated corporation. Based on the enactment of section 1012 of the Taxpayer Relief Act of 1997, the Service will not apply Court Holding (or any formulation of the step transaction doctrine) to determine whether the distributed corporation was a controlled corporation immediately before the distribution under section 355(a) solely because of any postdistribution acquisition or restructuring of the distributed corporation, whether prearranged or not. Rev. Ruls. 96-30, 1996-1 C.B. 36, and 75-406, 1975-2 C.B. 125, obsoleted. Rev. Rul. 70-225, 1970-1 C.B. 80, modified.

## PURPOSE

This revenue ruling obsoletes Rev. Ruls. 96-30, 1996-1 C.B. 36, and 75-406, 1975-2 C.B. 125, modified by Rev. Rul. 96-30. This revenue ruling also modifies Rev. Rul. 70-225, 1970-1 C.B. 80.

## BACKGROUND

Rev. Rul. 96-30 applies the principles of Commissioner v. Court Holding Co., 324 U.S. 331 (1945), to a distribution of controlled corporation stock by a publicly traded parent, followed by a merger of the controlled corporation into an unrelated acquiring corporation. The former shareholders of the controlled corporation receive a 25 percent interest in the acquiring corporation. Based on all the facts and circumstances, the ruling concludes that the transaction satisfies the requirements of § 355 of the Internal Revenue Code. Rev. Rul. 96-30 also modifies the factually similar Rev. Rul. 75-406 by eliminating the implication that an independent, post-distribution shareholder vote to approve the acquisition of a controlled corporation is, by itself, enough to prevent application of the step transaction doctrine.

Section 1012(c) of the Taxpayer Relief Act of 1997 (the "Act"), Pub.L. No. 105-34, 111 Stat. 788, 916-17, amended the control requirements of §§ 351 and 368(a)(1)(D) to provide that, generally for transactions seeking qualification after August 5, 1997 under either provision and § 355, the shareholders of the distributing corporation must own stock possessing more than 50 percent of the voting power and more than 50 percent of the total value of the controlled corporation's stock immediately after the distribution. Sections 351(c) and 368(a)(2)(H). In addition, § 1012(a) of the Act amended § 355 by adding subsection (c), which provides rules for the recognition of gain on certain distributions of stock or securities of a controlled corporation in connection with acquisitions of stock representing a 50 percent or greater interest in the distributing corporation or any controlled corporation. Section 1012(a) of the Act generally applies to distributions after April 16, 1997, pursuant to a plan (or series of related transactions) that involves

an acquisition described in § 355(e)(2)(A)(ii) occurring after such date.

The Conference Report accompanying the legislation states, in part, that:

The House bill does not change the present law requirement under section 355 that the distributing corporation must distribute 80 percent of the voting power and 80 percent of each other class of stock of the controlled corporation. It is expected that this requirement will be applied by the Internal Revenue Service taking account of the provisions of the proposal regarding plans that permit certain types of planned restructuring of the distributing corporation following the distribution, and to treat similar restructurings of the controlled corporation in a similar manner. Thus, the 80-percent control requirement is expected to be administered in a manner that would prevent the tax-free spin-off of a less-than-80-percent controlled subsidiary, but would not generally impose additional restrictions on post-distribution restructurings of the controlled corporation if such restrictions would not apply to the distributing corporation. H.R.Rep. No. 105-220, at 529-30 (1997).

#### ANALYSIS

The application of Court Holding principles to determine whether the distributed corporation was a controlled corporation immediately before the distribution under § 355(a) imposes a restriction on postdistribution acquisitions or restructurings of a controlled corporation that is inconsistent with § 1012 of the Act. See § 1012(c) of the Act and H.R.Rep. No. 105-220, at 529-30. Accordingly, the Service will not apply Court Holding (or any formulation of the step transaction doctrine) to determine whether the distributed corporation was a controlled corporation immediately before the distribution under § 355(a) solely because of any postdistribution acquisition or restructuring of the distributed corporation, whether prearranged or not. In otherwise applying the step transaction doctrine, the Service will continue to consider all facts and circumstances. See, e.g., Rev. Rul. 63-260, 1963-2 C.B. 147. An independent shareholder vote is only one relevant factor to be considered.

#### HOLDING

Based on the enactment of § 1012 of the Act, the Service will not apply Court Holding (or any formulation of the step transaction doctrine) to determine whether the distributed corporation was a controlled corporation immediately before the distribution under § 355(a) solely because of any postdistribution acquisition or restructuring of the distributed corporation, whether prearranged or not.

#### EFFECT ON OTHER REVENUE RULINGS

Rev. Ruls. 96-30 and 75-406 are obsoleted. Rev. Rul. 70-225 is modified to the extent inconsistent with this revenue ruling.

#### EFFECTIVE DATE

Pursuant to the authority of § 7805(b), this revenue ruling applies to distributions after April 16, 1997. However, this revenue ruling does not apply to a distribution pursuant to a plan (or series of related transactions) that involves an acquisition described in § 355(e)(2)(A)(ii) if the acquisition is pursuant to an agreement that was binding on April 16, 1997 and at all times thereafter, described in a ruling request submitted to the Service on or before that date, or described on or before that date in a public announcement or in a filing with the Securities and

Exchange Commission required solely by reason of the acquisition or restructuring. The previous sentence shall not apply to any agreement, ruling request, or public announcement or filing unless it identifies the acquirer of the distributed corporation.

Rev. Rul. 98-27, 1998-22 I.R.B. 4, 1998 WL 240430 (IRS RRU), 1998-1 C.B. 1159

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