Section 336(e) Elections in Taxable Dispositions

Tax Executives Institute
Orange County Chapter
April 2, 2014

David D. Sherwood
Ivins, Phillips & Barker
1700 Pennsylvania Ave., N.W.
Washington, DC 20006
(202) 393-7600
dsherwood@ipbtax.com

Adapted from ALI CLE Presentation by
Robert H. Wellen, Ivins, Phillips & Barker
Jasper L. Cummings, Alston & Bird LLP
Don A. Leatherman, Univ. of Tennessee
Kenneth Cohen, IRS Chief Counsel (Corporate)

Background –
Stock Sale With No §338 or §336(e) Election

- **Seller(s) of Target stock recognize gain or loss on stock sale.**
  - If Target is a consolidated return subsidiary, loss may be limited by Reg. §1.1502-36.
  - If Seller indemnifies Target or Purchaser for contingent liability, indemnity payment treated as capital contribution to Target, resulting in capital loss on stock sale under *Arrowsmith*.
- **No gain or loss recognized to Target.**
- **Target retains its asset basis and generally retains its other tax attributes (but *see* Reg. §1.1502-33(e) (if Target leaves a consolidated group, its E&P disappears to extent tiered up to its Parent)).**
- **Purchaser takes cost basis in Target stock.**

Background – Asset Sale

- **Asset Sale Mechanisms**
  - "Longhand" deeding of individual assets and assumption of liabilities.
  - Forward merger of Target into a corporate subsidiary of Purchaser for cash.
  - Conversion or merger of Target into LLC or other disregarded entity and sale of equity interest in Target.
- **Each of these mechanisms has disadvantages resulting from the need to dispense with the Target's corporate history, such as disruption of Target's contractual relationships and increased exposure to veil piercing. Longhand asset transfers can also involve substantial administrative cost.**
- **Tax Treatment**
  - Taxable gain or deductible loss on assets with no double tax.
  - For buyer, basis step-up under §1012 and a "fresh start," *i.e.*, no inheritance of Target's tax attributes, such as accounting elections and E&P.
  - Target's tax attributes generally are transferred to Target's parent under §331 or §332, as appropriate. In the case of S corporation Target, Target's attributes are eliminated.

Background – Stock Sale with §338 Election – QSPs

- **A Qualified Stock Purchase ("QSP") occurs if a purchasing corporation (or affiliated group) "purchases" Target stock meeting the requirements of §1504(a)(2) (generally, >80%) during a 12-month period.**
- **Broadly speaking every stock acquisition is a purchase except for stock acquired in a transferred-basis, exchanged-basis, or related party transaction.**
- **QSP Limitations**
  - Most important: QSP is limited to sale of Target stock to one corporate purchaser or affiliated group.
  - QSP is limited to *sale* of Target stock. Taxable stock distributions (other than certain stock redemptions) do not qualify.
  - Exclusion of sale to Related Persons.

Background – Stock Sale with §338(g) Election

- **Tax Consequences**
  - Target is deemed to sell its assets.
  - Target is then treated as a new corporation for federal income tax purposes.
  - Disregarding selling or buying costs, the Target assets are deemed sold and purchased for (i) the amount realized on the target stock sale plus (ii) the target liabilities.
  - The selling shareholder still recognizes gain or loss on the stock sale, as though no election had been made.
  - The purchasing corporation takes a cost basis in the Target stock.
- **This election generally makes sense only if:**
  - Target is not a U.S taxpayer;
  - The deemed asset sale is at a loss; or
  - Target has losses to shelter the gain on the deemed asset sale.

Background – Stock Sale with §338(h)(10) Election

- **Tax Consequences**
  - Target is deemed to sell its assets.
  - Target is then treated as a new corporation for federal income tax purposes.
  - Disregarding selling or buying costs, the Target assets are deemed sold and purchased for (i) the amount realized on the target stock sale (grossed up if less than all the stock is sold) plus (ii) the target liabilities.
  - Selling shareholders generally are treated as receiving sale proceeds in liquidation of Target, typically a §332 liquidation (or a §331 liquidation if Target is an S Corp Target).
  - The purchasing corporation takes a cost basis in recently purchased target stock under §1012, and is automatically deemed to have made a Gain Recognition Election for any non-recently purchased target stock.

Background – §338(g) vs. §338(h)(10) Elections

- **A § 338(g) election may be made for any QSP.**
- **A § 338(h)(10) election may be made only if as part of the QSP target stock meeting the requirements of §1504(a)(2) is acquired from –**
  - A selling consolidated group;
  - A selling affiliate; or
  - S corporation shareholders.
- **A §338(g) election is made by just the purchasing corporation.**
- **A §338(h)(10) election must be made jointly by the purchasing corporation and the Target shareholders, including non-selling S corporation shareholders (because the election affects these Target shareholders).**

§336(e) – History

- Section 336(e) was enacted in 1986 as part of General Utilities repeal and amended in 1988.
- Section 336(e) provides that, “under regulations,” an election may be made to treat a sale, exchange or distribution of >80% of the stock of a Target corporation as a sale of Target’s assets.
- The Government’s position is that §336(e) is not self-executing, and that the election is available only upon adoption of regulations.
- Regulations providing for §336(e) elections were proposed on August 25, 2008. 73 Fed. Reg. 49965.
- Final regulations were adopted on May 10, 2013 (TD 9619), effective for stock Dispositions with a Disposition Date on or after May 15, 2013 (which may include certain stock Dispositions before that date).

§336(e) – Overview

- **Deemed asset sale treatment for a taxable Disposition or series of Dispositions of >80% of the stock of a domestic Target corporation, within a 12-Month Disposition Period, to any person or persons other than Related Persons –**
  - By a domestic Parent corporation (or the members of a consolidated group) or
  - By the Shareholders of an S Corp Target.
- **Modeled on §338(h)(10), but –**
  - Applies to taxable distributions as well as sales of Target stock; and
  - Can apply where there as multiple and/or non-corporate Purchasers.
- **§338/§336(e) overlap**
  - A transaction satisfying the definition of both a QSP and a QSD is generally treated only as a QSP.
  - As an exception, if there is a deemed sale of stock of a Target Sub by reason of a QSD of Target stock with a §336(e) election, QSD trumps QSP.
  - As an exception to the exception, if there is a deemed sale of stock of a *foreign* Target Sub by reason of a QSD of Target stock with a §336(e) election, the deemed sale is a QSP, because it cannot be a QSD.

§336(e) – Overview

- **Tax Consequences**
  - Seller recognizes no gain or loss on a Disposition of the Target stock.
  - Target is deemed to dispose of all its assets to "New Target" in a taxable sale.
  - Any *net* loss on the deemed asset sale that is attributable to stock distributed by Seller during the 12-Month Disposition Period is disallowed.
  - Target is deemed to distribute the price received for the Target stock (and any "unwanted assets") to Seller in a liquidating distribution.
  - Target's tax attributes are generally transferred to Seller.
  - Special consequences if Disposition is a distribution (not sale) of Target stock that would be taxable to Parent due to application of §355(d) or §355(e).
  - Purchaser generally is not affected by Seller's § 336(e) election, but Target's deemed asset sale will affect its E&P, as well as the basis of its assets. Also, an 80 percent Purchaser (including Related Persons) with Nonrecently Disposed Stock can incur tax liability by reason of the Reg. § 1.336-4(c)(2) mandatory Gain Recognition Election.

Making the §336(e) Election

- **Reg. §1.336-2(h) provides the general rules, including specific requirements depending on whether Seller and Target are members of the same consolidated group, whether Target is an S Corp Target or a Target Sub.**
- **Election generally requires –**
  - Seller and Target entering into a binding written agreement on or before the due date of the earlier of Seller's or Target's return for the taxable year that includes the Disposition Date.
  - Attaching election statement to relevant returns of Seller and/or Target.
- **Target and New Target must report information concerning the deemed sale of Target's assets on Form 8883 "Asset Allocation Statement under Section 338" (making appropriate adjustments to report the results of the §336(e) election).**
- **Two Forms 8883 are filed by Target in the case of a Disposition subject to §355(d) or §355(e).**
- **The election is irrevocable.**

§336(e) – Overview – QSDs

- **Qualified Stock Dispositions (“QSDs”)**
  - Disposition or series of Dispositions totaling $\geq$80% of the Stock of Target, within the 12-Month Disposition Period, by Parent or by S Corp Shareholders (a “Seller”), to any person or persons other than Related Persons.
  - Disposition are sales, exchanges or distributions of Target stock.
  - The following stock transfers are not Dispositions:
    - Transfer at death (transferee’s basis determined under §1014(a)).
    - Transfer to which §351, §354, §355 or §356 applies.
    - Other transferred basis exchange (*e.g.*, gift or §721 transfer to partnership).
    - Transfer described in regulations in which not all gain or loss recognized.
    - Transfer to a Related Person, based on §338 principles.
  - Disposition includes a distribution by Parent to a Shareholder that is not a Related Person, if either
    - The distribution is taxable (*i.e.*, not subject to §355 or §361).
    - The distribution qualifies under §355, but there is gain recognized under §355(d) or §355(e).
  - Stock disposed of and reacquired by Parent or certain related persons during 12-Month Disposition Period is not considered disposed of.

§336(e) – Overview – Related Persons

- **A person is a Related Person to Seller if stock owned by the person would be attributed to Seller (or vice versa) under §318(a), except that—**
  - Section 318(a)(4) (option attribution) does not apply.
  - Sections 318(a)(2)(A) and 318(a)(3)(A) do not attribute stock ownership from a partnership to a partner or vice versa if the partner owns, directly or indirectly, a <5% interest in the partnership, by value.
- **Section 338 principles apply in determining whether a person is a Related Person.**
  - Relatedness generally is tested immediately after the Disposition.
  - Exception: If there is a series of Dispositions, relatedness is tested immediately after the last Disposition in the series.
- **Regulations do not specify whether, to be a Related Person, Purchaser must be related to its own Seller or could also be related to another Seller (as could occur with an S Corp Target).**

§336(e) – Overview – Restrictions Similar to §338(h)(10)

- **Reg. §1.336-1(a)(1) states:**
  - "Generally, except to the extent inconsistent with §336(e), the results of §336(e) should coincide with those of §338(h)(10). Accordingly, to the extent not inconsistent with §336(e) or these regulations, the principles of §338 and the regulations under §338 apply for purposes of these regulations."
- **Section 338(h)(10) restrictions that also apply to §336(e) elections:**
  - Disposition of Target stock must be fully taxable (but for the election)—no §351 transfers (including §304 sales), §721 transfers or reorganizations.
  - Neither Seller nor Target may be a foreign corporation (compare §338(g) election, available to foreign Seller and/or Target).
  - Disposition of Target stock to Related Persons does not qualify. Section 338 principles apply in determining whether a person is a Related Person.
- **Consistency rules apply, but only to Target assets owned by purchasers of >5% of the Target stock in the QSD. Reg. §1.336-1(a)(2).**

Deemed Asset Sale as Under §338(h)(10)

- **Deemed sale of Target assets is fully taxable (*e.g.*, no §1031 exchange even if consideration includes like-kind property).**
- **Installment method is available for deemed asset sale.**
- **Aggregate Deemed Asset Disposition Price ("ADADP") is similar to ADSP in §338(h)(10).**
  - Allocated among assets under residual method of Reg. §1.338-6.
- **Adjusted Grossed Up Basis ("AGUB") is similar to AGUB in §338(h)(10).**
  - Allocated among assets under residual method of Reg. §1.338-6.
- **Treatment of minority Target shareholders is similar to §338(h)(10) treatment.**
- **Treatment of Target stock retained by Seller is similar to §338(h)(10) treatment.**

Deemed Distribution as Under §338(h)(10)

- **Target is deemed to distribute –**
  - The consideration deemed received in the deemed asset sale to Seller.
  - Any Target assets not wanted by Purchaser(s) and distributed to Seller before sale of Target stock, as part of the "plan of liquidation."
- **Status of liquidation**
  - If Seller is a corporation, the distribution ordinarily is a tax-free liquidation under §§332 and 337.
  - If Sellers are S Corp Target Shareholders, the deemed distribution ordinarily is a taxable liquidation under §§331 and 336, with Seller(s)' stock basis adjusted to reflect the gains and losses recognized in the deemed asset sale.
- **As in a §338(h)(10) sale, deemed distribution could be an acquisitive §368(a)(1)(D) reorganization, if Seller transfers the stock sale proceeds and/or unwanted assets to another subsidiary.**
  - Could cause a triggered excess loss account in the "nominal share" of Target stock. Reg. §1.368-2(l)(2).

Deemed Distribution – Consolidated Group Issues

- **If Sellers are more than one member of a consolidated group –**
  - All group members "are treated as a single seller."
  - But §337(c) provides that a liquidating group member may distribute its assets tax-free only to one actual $\geq$80% Parent. Section 332 still applies to the distributee shareholder.
  - If Target is deemed to distribute only sale proceeds (cash or a note), there is no concern, because no gain is realized by Target.
  - If Target distributes assets unwanted by Purchasers, as part of its deemed "plan of liquidation," and the distributee is not an actual $\geq$80% Parent, §337(c) will trigger gain recognition to Target.
- **Intercompany Sale or Distribution of Target Stock**
  - Reg. §1.1502-13(f)(5)(ii)(C) relief is available for a taxable intercompany stock sale or distribution if followed by a sale or distribution of the stock outside the group, with a §336(e) election.

Open Issues – How far does the §338(h)(10) analogy go?

- **Anti-churning rule (§197(f)(9); Reg. §1.197-2(h)(8))**
  - "Special" rule for §338 deemed asset acquisition: New Target is not considered the person that held or used the assets.
  - Anti-churning rule "may nevertheless apply to a deemed asset purchase resulting from a §338 election if new target is related…to old target."
  - IRS officials have indicated that the intention is to apply these rules to §336(e) transactions.
- **Redemptions**
  - Does Reg. §1.338-3(b)(5) (testing 80% QSP after taking into account redemptions by target corporation) apply, or do redemptions of Target stock themselves constitute Dispositions (so long as the redemption is treated as a sale of the Target stock, and the redeemed Shareholder is not a Related Person to the Target)?
- **CERT (§172(h)(3)(B)(ii))**
  - "For CERT purposes, the term "major stock acquisition" does not include a QSP to which a §338 election applies. Does a similar rule apply to a stock Disposition subject to a §336(e) election?

ADADP and AGUB

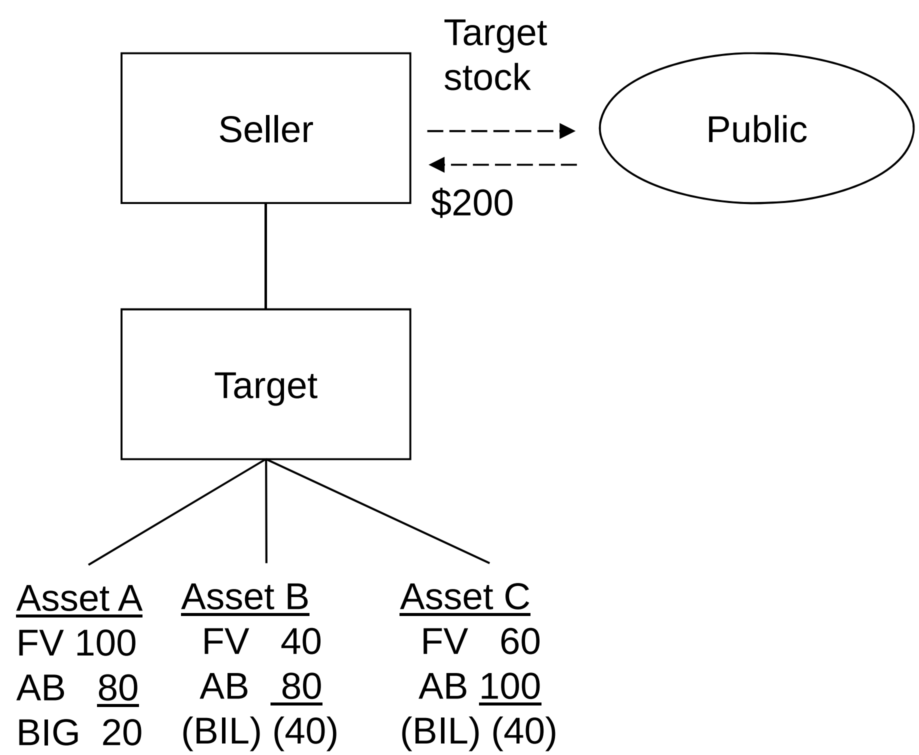
- **ADADP**
  - ADADP under §336(e) is essentially the same as ADSP under §338(h)(10). For "distributions" where there is no actual sale proceeds, fair market value of the stock on the date of the distribution is used to determine ADADP.
  - Formula does not necessarily reflect Target stock or asset value on the Disposition Date, if value changes during the 12-Month Disposition Period.
- **AGUB**
  - AGUB under §336(e) is essentially the same as AGUB under §338(h)(10). For "distributions" where there is no actual sale proceeds, fair market value of the stock on the date of the distribution is used to determine AGUB.
  - The complexities of AGUB are more likely to arise under §336(e), because of multiple Purchasers in §336(e) Dispositions.

Gain Recognition Elections

- **If a holder of Target stock makes (or is deemed to make) a Gain Recognition Election, Nonrecently Disposed Stock is treated as sold on the Disposition Date.**
  - The holder recognizes gain but not loss (even loss netted against gain) on a deemed sale of that stock.
  - The deemed sale price = "basis amount" = A*B/C:
    - A = Holder's basis in Recently Disposed Stock at the beginning of the day after the Disposition Date.
    - B = Percentage of Target stock that is that holder's Nonrecently Disposed Stock.
    - C = Percentage of Target stock that is that holder's Recently Disposed Stock.
  - Idea is to approximate the value of the Target stock per share, as determined by each holder's actual cost of its Recently Disposed Stock.
  - **Gain Recognition Election is mandatory for an 80 percent Purchaser (including Related Persons) with Nonrecently Disposed Stock.**

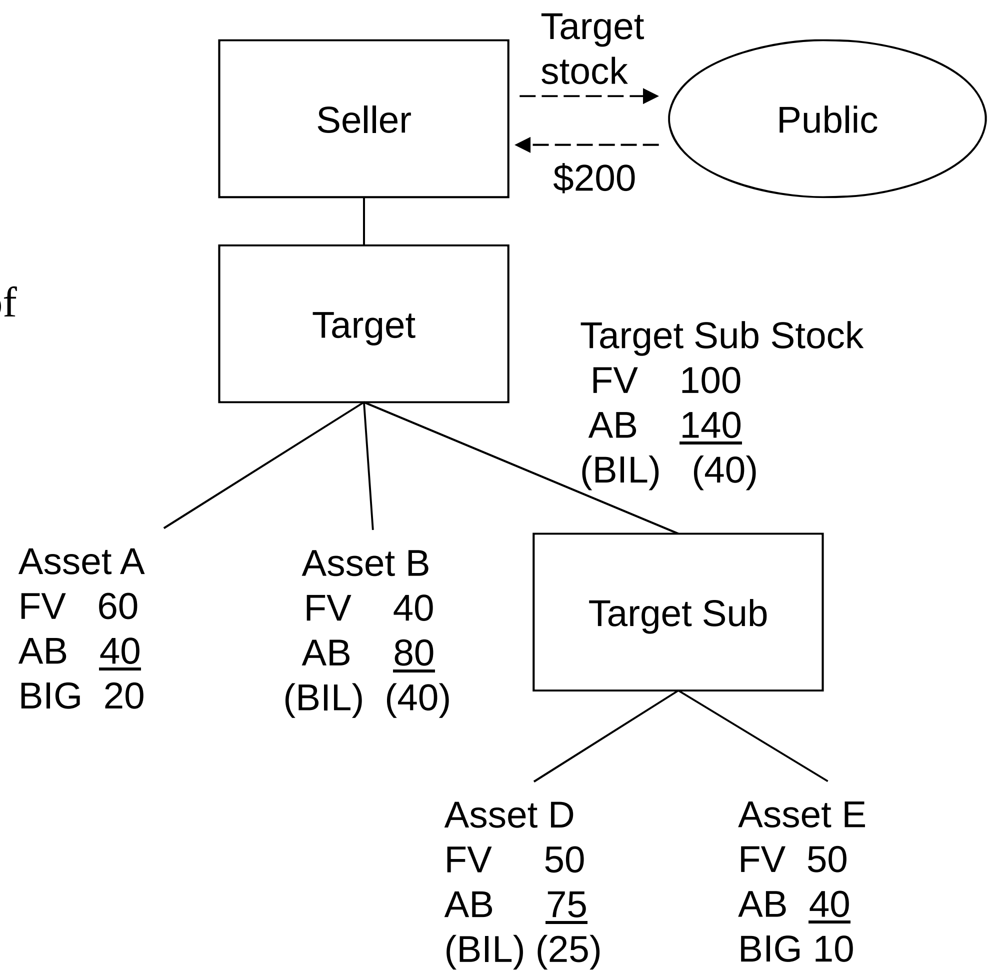
Example –
Sale of Target Stock to One or More Purchasers

- Seller sells the Target stock to the Public for $200. A §336(e) election is made.
- Target is deemed to sell all its assets to an unrelated person for ADADP ($200).
- Target realizes $20 gain on Asset A, $40 loss on Asset B, and $40 loss on Asset C—$60 net loss.
- Because all the Target stock is sold (not distributed), none of the net loss is disallowed.
- New Target is deemed to purchase the assets from an unrelated person for AGUB.
- Target is deemed to distribute the consideration deemed received for the assets to Seller (§332/337 liquidation).
- This transaction accomplishes the same result as a "busted" §351 exchange that can be a QSP.
  - Section 336(e) election eliminates need for a preliminary transfer of Target to a Newco.
  - On the other hand, a busted §351 transaction allows Seller to retain more than a 20% interest in Target.



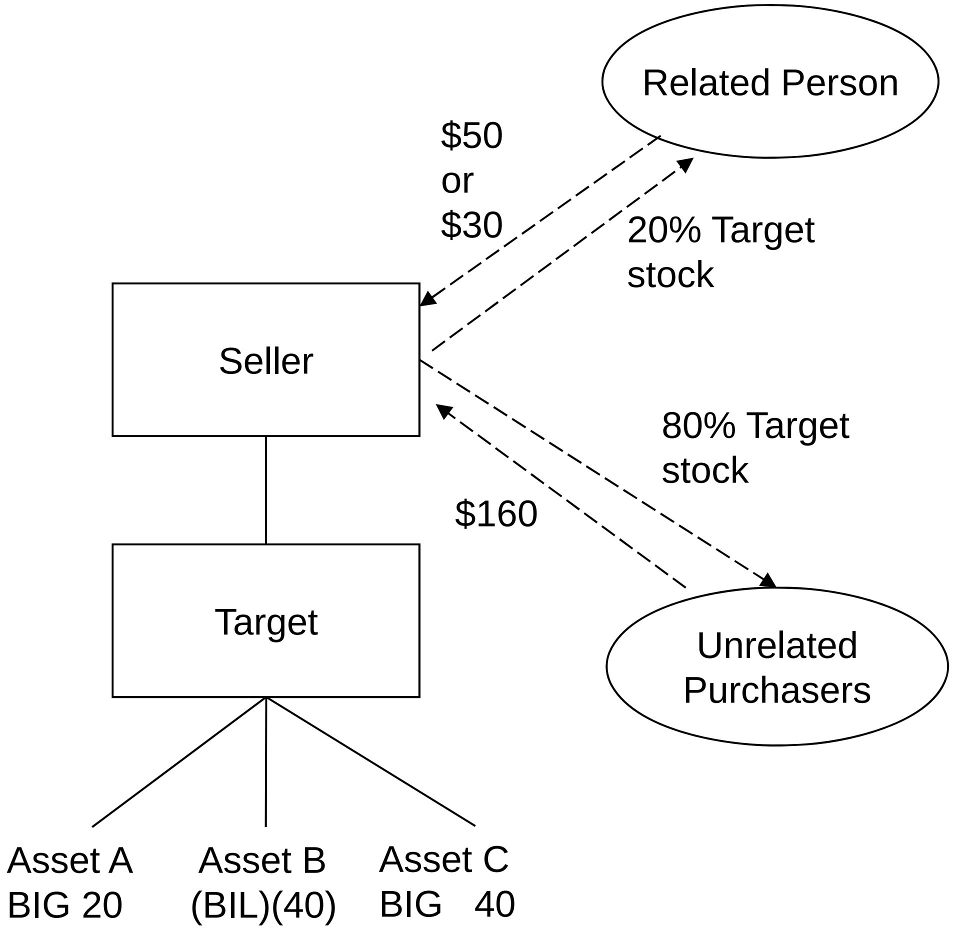
Example –
Sale of Target Stock to Public; Target Sub

- Seller sells all the Target stock to Public for $200. Section 336(e) elections are made for Target and Target Sub.
- Deemed asset sale by Target excludes stock of Target Sub.
- Deemed asset sale by Target is considered to precede deemed asset sale by Target Sub.
- Deemed asset sale by Target Sub and liquidation of Target Sub are treated as occurring before deemed liquidation of Target.

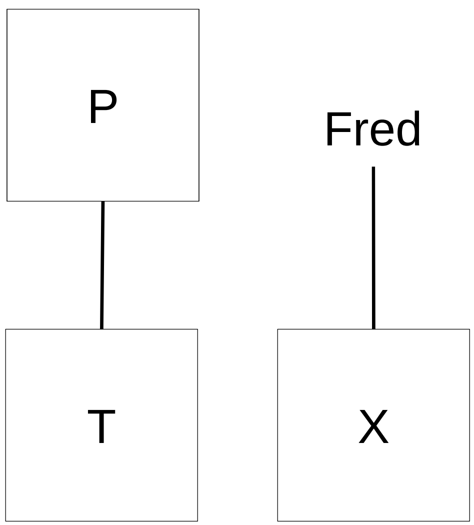


Example – Sale of 80% of Target Stock to Unrelated Purchasers and 20% to Related Person

- Seller sells 80% of Target stock to Unrelated Purchasers for a total of $160 (QSD) and 20% to Related Person for $50 (or $30). A §336(e) election is made.
- The stock sold to Related Person is not part of the QSD. Consideration paid for this stock is not taken into account in determining ADADP and AGUB.
- Target is deemed to sell all its assets to an unrelated person for ADADP ($200).
- New Target is deemed to purchase the assets from an unrelated person for AGUB ($200).
- Target is deemed to distribute the consideration deemed received for its assets to Seller (§§332/337 liquidation).



Example – Consistency Rules



- P owns all T stock and P and T join in filing consolidated returns.
- T sells an asset to Fred, recognizing a gain.
- Shortly thereafter P sells the T stock either to Fred or X, Fred's wholly owned corporation.
  - No Section 336(e) or Section 338 election is made for the stock sale.
  - *Does a consistency rule apply to T's asset sale?*

Consistency Rules – §338

- **The "principles" of the consistency rules that apply to QSPs also apply to QSDs.**
- **The preamble to the §336(e) regulations (TD 9619) describes the consistency rules that apply to QSPs –**
  - In general, section 1.338-8 provides that if
    - (1) a purchasing corporation (or an affiliate) acquires an asset meeting certain requirements from target (or a subsidiary of target) in a sale during the target consistency period,
    - (2) gain from the sale is reflected in the basis of target stock as of the target acquisition date, and
    - (3) the purchasing corporation acquires stock of target in a qualified stock purchase (but does not make a section 338 election),

    then the purchasing corporation is required to take a carryover basis in the acquired asset.
- **The §338 consistency rules are intended to apply only in potentially abusive situations.**

Consistency Rules – §336(e)

- **The §336(e) consistency rules apply—**
  - To all types of Purchasers in a QSD, not only to corporations.
  - Only if a Purchaser (or a Related Person) acquires both—
    - An asset with cost basis from Target or a Target Sub during the 12-Month Disposition Period, and
    - ≥5%, by value, of the Target stock in the QSD.
- **If no §336(e) election is made in the QSD, the affected Purchaser takes carryover basis in the acquired asset.**
- **Because of their application to any Purchaser that acquires >5% of the Target stock, and its Related Persons, the consistency rules are more likely to apply to a QSD than to a QSP.**

Stock Distributions Subject to §355(d) or §355(e) – Sale to Self Mechanics

- **Target is deemed to sell all its assets to an unrelated person for ADADP.**
  - Gains are recognized in full.
  - To implement the policy of §311(b), any net loss is disallowed in proportion to the amount of stock distributed compared with any amount of stock sold as part of the QSD.
- **Target is deemed to re-acquire its assets from an unrelated person for AGUB.**
- **Target is not deemed to liquidate.**
- **Seller distributes the Target stock.**
  - Seller recognizes no gain or loss on the distribution.
  - Target's tax attributes remain intact with Target.
  - Target's earnings and profits account is adjusted to reflect gain or loss on the deemed asset sale.
- **The distributee shareholders receive the Target stock tax-free under §355 and allocate their basis in their Seller stock between the Seller stock and Target stock, under §358.**

Stock Distributions Subject to §355(d) or §355(e) – Collateral Matters

- **Excess Loss Accounts**
  - IRS officials have indicated that any excess loss account ("ELA") in the stock of Target or Target Sub is triggered, whether or not the ELA was created in connection with the distribution.
  - Reg. §1.336-2(b)(2)(iii) ("No gain or loss is recognized by seller on the distribution."); Reg. §1.1502-19(b)(1)(i) ("if M is treated under this section as disposing of a share of S's stock, M takes into account its excess loss account in the share as income or gain from the disposition.").
- **Sections 197(f)(9) and 1091**
  - For purposes of §197(f)(9) (intangibles amortization anti-churning rule) and §1091 (wash sale), Target in its capacity as deemed seller "shall be treated as a separate and distinct taxpayer from, and unrelated to," Target in its capacity as deemed buyer in the deemed sale-to-self. Reg. §1.197-2(h)(8).
  - What if Seller spins Target pro rata, and one of Seller's shareholders owns 30% of Seller's stock (more than the 20% relatedness threshold under §197(f)(9))? IRS officials have stated that the intention was not to exempt sale-to-self transactions from anti-churning where anti-churning otherwise would apply.

Disallowed Loss - General

- **Some or all of the net loss realized in Target's deemed asset sale is disallowed**.
- **The proportion of net loss disallowed is determined by the "disallowed loss fraction":**
  - **Numerator**: Value on the Disposition Date of all Target stock distributed during the 12-Month Disposition Period (including stock distributed outside the QSD – *e.g.*, after the Distribution Date or to a Related Person).
  - **Denominator**: Sum of—
    - Value on Disposition Date of Target stock sold during 12-Month Disposition Period as part of QSD.
    - Numerator.
- **Proportion of net loss attributable to any Target stock sold during 12-Month Disposition Period as part of QSD is allowed.**
- **Disallowed losses are allocated among assets deemed sold at a loss in proportion to losses realized.**
- **Disallowed losses are permanently disallowed and do not result in any increase in basis of Target assets.**

Disallowed Loss – Target Subs

- **If Target has a Target Sub, and Target stock is distributed in a QSD, with §336(e) elections for both Target and Target Sub, the deemed disposition of the Target Sub stock is a deemed distribution of that stock.**
- **Loss disallowance, including netting losses against gains, is determined separately for Target (excluding stock of Target Subs for which §336(e) is elected) and for each Target Sub.**
- **Separate-entity netting reduces the benefit of loss netting.**
  - It may be difficult to determine the value of assets held by each Target Sub.
  - Computation of ADADP can complicate the process even further. *See* Reg. §1.336-2(b)(1)(i)(B)(*3*) Example (2).

Protective §336(e) Election

- **A protective §336(e) election should be considered in connection with any intended tax-free stock distribution (spin-off or split-off).**
  - Such an election mitigates the tax cost of the distribution becoming taxable under §355(d) or §355(e).
  - The tax sharing agreement could allocate the benefits of any basis step-up to the party that bears the tax cost of the taxable deemed asset sale.
  - The mitigation is less effective if Target or any Target Sub realizes net loss on a separate basis.
  - Steps to reduce or eliminate net losses in Target Subs should be considered.
  - If a net loss is large enough, a protective election could be counter-productive.
- **IRS officials have stated that IRS may be willing to issue an advance ruling that such a protective election is effective.**
  - Will the general no-rule for §355 distributions (Rev. Proc. 2013-32) affect IRS's willingness to rule on this issue?
  - Will a "significant" issue regarding the election be required?

Open Issues in Creeping Dispositions

- **Straddling Year End**. If the Pre-Deemed Sale Period straddles a taxable year end of Target or Seller, the tax consequences of the first part of a QSD in the first year are uncertain**.**
  - How does Seller report the sale or distribution of Target stock on its return for the first year?
  - If Target is an S Corp Target, how is Target's income or loss reported?
  - How can this reporting be changed once the 336(e) election is made with the Seller's return for the 2nd year?
  - How is Seller's E&P affected and adjusted to determine the shareholders' treatment of a distribution of Target stock during the first year?
- **Target a Consolidated Group Member.** If >20% of Target stock is sold to a non-group member during the Pre-Deemed Sale Period; the rest of the Target stock is sold on the Disposition Date; and a §336(e) election is made –
  - When does Target leave the group?
  - Does the group report the gain or loss on the deemed sale and any Target income or loss from the date of the >20% stock sale through the Disposition Date?

Drafting a Stock Purchase Agreement

- **Acquisition agreement needs to provide for reporting gain or loss, payment of tax on deemed asset sale and benefit of any loss carrybacks or carryovers.**
- **Seller and Target may agree to file election but then revoke the agreement, so long as they do it before the election is filed.**
  - The election itself is irrevocable.
  - Agreement should include procedures for revocation of agreement to elect section 336(e) if circumstances change.
- **Buyer of <80% of the Target stock from Seller, with Seller holding the remainder, could be buying liability for its share of the tax on the deemed asset sale, if a later stock sale is made with a §336(e) election.**
  - Buyer would benefit from its share of the basis step-up.
  - Nevertheless, agreement should provide procedures for deciding to make or not make the election.
- **Seller and Purchaser should consider whether to reach agreement on allocation of ADADP and AGUB for deemed asset sale. By not reaching such an agreement, they can avoid being bound vis-à-vis IRS.**

Section 338(h)(10)	Section 336(e)
Joint Seller and Purchaser election	Seller and Target election by agreement; Purchaser not involved (except by agreement with Seller)
Election filed on separate form filed within 8.5 months after closing	Election on tax return(s)
One domestic or foreign corporate Purchaser (or affiliated group)	Any number of corporate or non-corporate Purchasers
Seller must be a U.S. corporation (or consolidated group) with Target as ≥80% sub; or S Corp Target	Same
“12-month acquisition period”	“12-Month Disposition Period”
Sales of Target stock with ≥80% vote and value (excluding §1504(a)(4) stock) to one Purchaser—corporation or affiliated group	Sales and/or taxable distributions (including distributions subject to §355(d) or §355(e)) totaling ≥80% of the Stock
Related Person restriction—§318(a) attribution, excluding option attribution under §318(a)(4)	Same, except no attribution between partnership and <5% partner
Not available if Seller or Target is foreign	Same
Target’s amount realized on deemed asset sale is “aggregate deemed sale price” (ADSP)	Target’s amount realized on deemed asset sale is “aggregate deemed asset disposition price” (ADADP)
New Target’s basis in assets deemed purchased is “adjusted grossed up basis” (AGUB)	Same, except that stock held by <10% shareholder is not “nonrecently disposed stock”
Consistency rules	Same, but only for Target assets owned by Purchasers of ≥5% of the Target stock in QSD.

Glossary

- **12-Month Disposition Period.** 12-month period beginning on the date of the first Disposition of Target stock included in a QSD. Reg. §1.336-1(b)(7).
- **ADADP.** Grossed-up amount realized on Dispositions of Recently Disposed Stock, plus Target liabilities, less selling costs.
- **AGUB (under §336(e)).** Grossed-up basis in Recently Disposed Stock, plus basis in Nonrecently Disposed Stock, plus Target liabilities, plus acquisition costs.
- **Disposition Date.** The first day on which there is a QSD with respect to the Target stock. Reg. §1.336-1(b)(8).
- **New Target.** Hypothetical corporation deemed to purchase the assets of Target in a QSD with a §336(e) election, other than a distribution of stock subject to §355(d) or §355(e), which involves a "sale-to-self."
- **Nonrecently Disposed Stock.** Any Target stock that is not Recently Disposed Stock that is held on the Disposition Date by a Purchaser or a person related to such Purchaser, but only if such Purchaser or person actually and constructive owns $\geq$10% of the Target stock (by either vote or value).

Glossary

- **Parent.** Domestic corporation that sells or distributes Target stock in a QSD, a QSP or a similar transaction (i.e., Seller). References to Parent generally include any other members of its consolidated group that own Target stock.
- **Pre-Deemed Sale Period.** Portion of the 12-Month Disposition Period before the Disposition Date.
- **Purchaser(s).** Person or persons that purchase Target stock in a QSD, a QSP or a similar transaction.
- **QSD.** *See* Slide 12.
- **Recently Disposed Stock.** Any Target stock that is not held by Seller (or member of Seller's group or S Corp. shareholder) immediately after the close of the Disposition Date and was disposed of by Seller (or member of Seller's group or S Corp. shareholder), other than to a Related Person, during the 12-Month Disposition Period.
- **Related Person.** *See* Slide 13.

Glossary

- **S Corp Target.** Target that is an S corporation immediately before the Disposition Date.
- **S Corp Target Shareholder(s).** Shareholder(s) of an S Corp Target.
- **Seller.** Domestic C or S corporation that sells and/or distributes Target stock (i.e., Parent or members of its consolidated group) or S Corp Target Shareholder that sells stock, in either case in a QSD, a QSP or a similar transaction.
- **Shareholder.** Shareholder of Parent.
- **Target.** Domestic C or S corporation the stock of which is Disposed of in a QSD, a QSP or a similar transaction.
- **Target Sub.** Corporation of which Parent owns >80% of the stock (a domestic corporation, if the Target stock is disposed of in a QSD; a domestic or foreign corporation if the Target stock is sold in a QSP).
- **>80% of the Stock.** >80% of the stock of Target or Target Sub (as the case may be), by both vote and value, excluding plain vanilla nonvoting preferred stock.

Questions?

Section 230 Disclaimer

- This document was not intended or written to be used, and cannot be used, for the purpose of avoiding U.S. federal, state or local tax penalties.