DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
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OFFICE OF
CHIEF COUNSEL

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INTERNAL REVENUE SERVICE NATIONAL OFFICE FIELD SERVICE ADVICE

MEMORANDUM FOR JODY TANCER
ASSOCIATE AREA COUNSEL (FINANCIAL SERVICES: MANHATTAN) CC:LM:FSH:LI

FROM: Ken Cohen
Senior Technician Reviewer, CC:CORP:B03

SUBJECT: Notice 2001-16 - POSTS-158256-01

This Field Service Advice responds to your memorandum dated October 30, 2001. Field Service Advice is not binding on Examination or Appeals and is not a final case determination. This document is not to be used or cited as precedent.

LEGEND

Target =

Purchaser =

Intermediary =

MergerSub =

State A =

Individual A =

Year 1 =

Year 2 =
Year 3 =

Date 1 =

Date 2 =

Date 3 =

$x =

$y =

ISSUES

1. Can this transaction be recast as a direct sale of Target stock from its shareholders to Purchaser, and if so, should a separate case be opened against Purchaser?

2. Should cases involving transactions in which intermediaries are used in accelerated lease strip and inflated basis cases, such as this one, be considered listed transactions under Notice 2001-16?

CONCLUSIONS

1. This transaction can be recast as a direct sale of Target stock from its shareholders to Purchaser, and a separate case should be opened against Purchaser.

2. Cases involving transactions in which intermediaries are used in accelerated lease strip and inflated basis cases, such as this one, should be considered listed transactions under Notice 2001-16.

FACTS

The facts of this case were fully set forth in our prior advice to you on June 1, 2001. See Chief Couns. Adv. 200136009, 2001 IRS CCA LEXIS 97. Only a short summary will be provided here.

During Year 1, Purchaser learned that Target was for sale. Negotiations between Purchaser and Target reached an impasse over price, and whether the acquisition was to be a stock or asset acquisition. The Target shareholders wanted to sell their stock and Purchaser wanted to acquire the Target assets.

Sometime during Year 2, Intermediary was engaged in discussions with Purchaser about an unrelated matter. At that time, Purchaser advised Intermediary of its problems with the Target acquisition. Intermediary agreed to facilitate the transaction by acquiring the stock from the Target shareholders and then selling to Purchaser the Target assets.

Intermediary entered into letters of intent on or about Date 1 with both the Target shareholders and Purchaser reflecting that Intermediary's purchase of the Target stock was conditioned on Purchaser's purchase of the Target assets and Purchaser's purchase of the Target assets was conditioned on Intermediary's purchase of the Target stock. In essence, the sale and asset acquisition were inter-linked so that one would not occur without the other. Intermediary assigned its rights in the letters of intent to MergerSub, a special purpose entity created by Intermediary solely for this transaction.

Individual A, the sole shareholder and director of Intermediary, and Intermediary were cognizant of the gain which would result from Target's sale of the assets to Purchaser, and, as part of the prearranged series of transactions, planned the transfer of various assets through Target from other Intermediary related entities ("Intermediary Group") in order to generate losses that would offset the gain from the asset sale. Additionally, it is uncontested that Individual A and Intermediary would not have engaged in the Target stock acquisition and immediate asset sale to Purchaser if the Intermediary Group did not have tax attributes that could be utilized by Target to offset the tax gain.

On Date 2, the Target shareholders sold their stock to MergerSub. On the same day, after MergerSub acquired the Target stock, members of the Intermediary Group assigned certain leases and subleases to Target in exchange for shares of Target stock.

On Date 3, Target sold its assets to Purchaser for $x plus the assumption of certain liabilities. Target then engaged in another series of transactions transferring the leases to a member of the Intermediary Group purportedly resulting in deductions and capital losses. These purported ordinary deductions and purported capital losses eliminated the entire gain from the Target asset sale, and, in addition, the losses generated by the transaction would be able to be carried back to prior years resulting in approximately $y in refunds. After the transactions described above, Target had minimal assets and its existence was terminated under State A law in Year 3.

Our prior advice to you focused on treating the transaction as an asset sale. We now address treatment as a sale of stock.

LAW AND ANALYSIS

Recast as Sale of Stock; Opening a Separate Case

Although our initial advice may not have discussed the possibility of recasting this transaction as a direct sale of Target stock by its shareholders to Purchaser, we do believe it would be a viable option to do so. If the transaction were recast as a direct sale of stock, a separate case should be opened against Purchaser.

As discussed below, the Service can challenge intermediary transactions such as these under Notice 2001-16, 2001-9 I.R.B. 730, and recast them as asset sales or direct sales of stock. Although our prior advice focused on treatment as an asset sale, the factual circumstances of this case would equally, if not more so, lend themselves to recast as a direct sale of the Target stock to Purchaser with Intermediary acting as Purchaser's agent (or equivalent), followed by the complete liquidation of Target and distribution of its assets to Purchaser.

Intermediary Transaction Tax Shelter, CCN 2001-023 (April 26, 2001), sets forth certain facts that may indicate recast of a transaction like the one at issue as a stock sale. Purchaser's relationship with Intermediary is one of the strongest factors supporting such recast of the transaction. Purchaser was aware that the Target shareholders only wanted to sell their stock to Purchaser and not the Target assets. In response to this problem, Purchaser brought Intermediary, a firm with which Purchaser had a previous relationship, into the negotiations for the purpose of facilitating the acquisition of the Target assets. Discussions concerning Intermediary's role in the transaction took place solely between Purchaser and Intermediary. This fact leads to the conclusion that Intermediary was the agent, or the functional equivalent of an agent, of Purchaser in the sale of the Target stock. Without the participation of Intermediary, Purchaser would not have received a stepped-up basis in the Target assets upon their purchase from Intermediary.

We recommend that you investigate the existence of any other factors set forth in CCN 2001-023 for recasting this transaction as a stock sale.

If the transaction is recast as a direct stock sale, the liquidation of Target into Purchaser would qualify as a complete liquidation under § 332 with no gain or loss to Purchaser on receipt of the Target assets. Target would recognize no gain or loss on the distribution and Purchaser would take a carryover basis in the Target assets. Sections 337(a) and 334(b)(1).

Listed Transactions Under Notice 2001-16

Since transactions involving intermediaries such as this one are practically identical to those transactions described in Notice 2001-16, they should be considered listed transactions under Notice 2001-16.

Notice 2001-16 describes, in general terms, transactions that involve four parties: a seller who wishes to sell the stock of a target corporation, the target corporation, an intermediary corporation, and a buyer who wishes to purchase the assets (but not the stock) of the target corporation. As part of a plan, seller sells the stock of the target corporation to the intermediary corporation. The target corporation then sells some or all of its assets to the buyer. The buyer claims a basis in the assets equal to the purchase price of those assets.

Whether the transaction before us should be a listed transaction under Notice 2001-16 depends on whether it is “the same as or substantially similar to” those transactions described in Notice 2001-16. We believe that it is.

The only facts in the instant case that are different from those in the Notice are that (a) in the instant case, the intermediary corporation formed a special purpose subsidiary to purchase the target corporation stock (such special purpose subsidiary then merged into the target corporation) rather than the intermediary corporation making the purchase itself and (b) the means by which the intermediary corporation in the instant case attempts to offset the purported income of the target corporation on the sale of the assets is by the use of artificially created losses, rather than losses incurred by other members of its consolidated group.

These facts in no way distinguish the transaction at issue (and similar transactions) from that described in Notice 2001-16. Accordingly, this transaction (and similar transactions) must be considered to be the same as or substantially similar to transactions described in Notice 2001-16 and are thus “listed transactions” for purposes of § 1.6011-4T(b)(2) of the Temporary Income Tax Regulations and § 301.6111-2T(b)(2) of the Temporary Procedure and Administration Regulations.

CASE DEVELOPMENT, HAZARDS AND OTHER CONSIDERATIONS

This writing may contain privileged information. Any unauthorized disclosure of this writing may have an adverse effect on privileges, such as the attorney client privilege. If disclosure becomes necessary, please contact this office for our views.

Please call (202) 622-7790 if you have any further questions.

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