

Internal Revenue Service
Notice 2015-59 (October 5, 2015)

Request for Comments; Areas Under Study Relating to
§§ 337(d) and 355 of the Internal Revenue Code

SECTION 1. PURPOSE

The Treasury Department and the Internal Revenue Service (Service) are studying issues under §§ 337(d) and 355 of the Internal Revenue Code (Code) relating to transactions having one or more of the following characteristics: (i) ownership by the distributing corporation or the controlled corporation of investment assets, within the meaning of § 355(g)(2)(B), with modifications (Investment Assets), having substantial value in relation to (a) the value of all of such corporation's assets and (b) the value of the assets of the active trade(s) or business(es) on which the distributing corporation or the controlled corporation relies to satisfy the requirements of § 355(b) (a Qualifying Business or Qualifying Business Assets); (ii) a significant difference between the distributing corporation's ratio of Investment Assets to assets other than Investment Assets and such ratio of the controlled corporation; (iii) ownership by the distributing corporation or the controlled corporation of a small amount of Qualifying Business Assets in relation to all of its assets; and (iv) an election by the distributing corporation or the controlled corporation (but not both) to be a regulated investment company (RIC), within the meaning of § 851, or a real estate investment trust (REIT), within the meaning of § 856.

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SECTION 2. DISCUSSION

Background

Section 355 of the Code generally provides that, if certain requirements are satisfied, a distributing corporation may distribute the stock (or stock and securities) of a controlled corporation to its shareholders and security holders without the distributing corporation, its shareholders, or its security holders recognizing income, gain, or loss on the distribution. However, § 355 does not apply to a distribution if the transaction is used principally as a device for the distribution of the earnings and profits of the distributing corporation or the controlled corporation or both (a device). Section 355(a)(1)(B). Numerous other requirements also must be satisfied for § 355 to apply to a distribution.

One such requirement is that the distributing corporation and the controlled corporation each be engaged in the active conduct of a trade or business immediately after the distribution (active trade or business requirement). Section 355(a)(1)(C) and (b)(1)(A). For this purpose, § 355(b)(3)(A) provides that all members of a corporation's separate affiliated group are treated as one corporation. Another such requirement is that the transaction must be carried out for one or more corporate business purposes (business purpose requirement). Section 1.355-2(b)(1).

The Treasury Department and the Service have become aware, in part through requests for letter rulings, that some taxpayers are taking the position that certain distributions that have one or more of the characteristics described in section 1 of this notice satisfy the requirements of § 355. The Treasury Department and the Service believe that these transactions may present evidence of device for the distribution of earnings and profits, may lack an adequate business purpose or a Qualifying Business, or may violate other § 355 requirements. In addition, these transactions may circumvent the purposes of Code provisions intended to repeal the Supreme Court's decision in *General Utilities & Operating Co. v. Helvering*, 296 U.S. 200 (1935) (General Utilities repeal). See, e.g., §§ 311(b), 337(d), 367(a)(5), and 367(e); H.R. Rep. No. 100-391, at 1080-1084 (1987).

Nature of Assets of Distributing Corporation and Controlled Corporation

The Treasury Department and the Service are most concerned about transactions that result in (i) the distributing corporation or the controlled corporation owning a substantial amount of cash, portfolio stock or securities, or other Investment Assets, in relation to the value of all of its assets and its Qualifying Business Assets, and (ii) one of the corporations having a significantly higher ratio of Investment Assets to Non-Investment Assets than the other corporation. While these matters are under study, the Service will not rule on any issue that relates to the qualification of a distribution under § 355 and related provisions and is presented in a distribution described in section 5.01(26) of Rev. Proc. 2015-3.

Small Amounts of Qualifying Business Assets

The Treasury Department and the Service are also concerned about transactions in which the distributing corporation or the controlled corporation owns a small amount of Qualifying Business Assets compared to its other assets (non-Qualifying Business Assets). Before enactment of § 355(b)(3), such transactions were common due to the restrictive nature of the "holding company" rule (§ 355(b)(2)(A) prior to its amendment by the Technical Corrections Act of 2007, Pub. L. No. 110-172, § 4(b)(1), 121 Stat. 2473, 2476 (2007)). The Treasury Department and the Service have concluded that, under current law, distributions involving small Qualifying Businesses may have become less justifiable. Accordingly, the Service ordinarily will not rule on any issue that relates to the qualification of a distribution under § 355 and related provisions and is presented in a distribution described in section 4.01(58) of Rev. Proc. 2015-3, but will consider ruling in unique and compelling circumstances.

In determining whether unique and compelling circumstances exist to justify the issuance of a ruling or determination letter, the Service will consider all facts and circumstances, including whether a substantial portion of the non-Qualifying Business Assets would be Qualifying Business Assets but for the five-year requirement of § 355(b)(2)(B) and whether there is a relationship between the business purpose for the distribution and the Qualifying Business of the distributing corporation or the controlled corporation.

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SECTION 3. REQUEST FOR COMMENTS

The Treasury Department and the Service request comments concerning the transactions described in this notice. In particular, comments are requested with respect to: (i) the facts and circumstances relevant to whether the transactions satisfy the requirements of § 355 and/or circumvent the purposes of General Utilities repeal; (ii) whether investment assets, within the meaning of § 355(g)(2)(B), as modified by section 5.01(26) of Rev. Proc. 2015-3, are the appropriate assets to consider in addressing the concerns raised by the transactions; (iii) whether the treatment of transactions solely within an affiliated group should differ from the treatment of transactions in which stock of one or more corporations will be distributed outside the affiliated group; (iv) whether the Service should rule on issues presented in distributions in which the distributing corporation or the controlled corporation owns a relatively small amount of Qualifying Business Assets, and if so in what circumstances; and (v) whether other classes of transactions subject to section 4.01(57), 4.01(58), or 5.01(26) of Rev. Proc. 2015-3 should be excepted therefrom.

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