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The End of an Era: IRS Expands “No-Rule” Policy for Spin-Offs and Other Common Corporate Transactions

On June 25, the IRS expanded its “no-rule” policy with respect to spin-offs and other tax-free corporate separations, liquidations, contributions, and reorganizations. Effective for letter ruling requests received by the IRS after August 23, 2013, Rev. Proc. 2013-32, 2013-28 I.R.B. 1, provides that the IRS will no longer rule on an entire transaction under § 332, § 351, § 355, § 368, or § 1036. Instead, the IRS will rule only on one or more “significant issues” arising in the context of such a transaction. Accordingly, taxpayers have a short window of time to send spin-off letter ruling requests to the IRS Office of Associate Chief Counsel (Corporate) if they would like to receive a letter ruling providing that no gain or loss will be recognized by the parties to such a transaction.

In brief, Rev. Proc. 2013-32 also:

- Potentially broadens the range of issues that may qualify as “significant” for letter ruling purposes.
- Discontinues the IRS’s single-issue letter ruling pilot program under § 355 (Rev. Proc. 2009-25, 2009-24 I.R.B. 1088), thereby eliminating the expedited treatment offered by the pilot program.
- Continues in effect all pertinent no-rule policies described in Rev. Proc. 2013-3, 2013-1 I.R.B. 113, governing the IRS’s letter ruling practice.

These and other notable aspects of Rev. Proc. 2013-32 are discussed in greater detail below.

Sutherland Observation: The IRS’s decision to expand its no-rule policy likely will have the most significant impact on public spin-offs. Historically, many such transactions have been contingent upon the receipt of a letter ruling from the IRS addressing the transaction’s qualification under § 355 and the ancillary tax consequences following from that determination. Upon the effectiveness of Rev. Proc. 2013-32, these types of transactions will have to proceed on the basis of an opinion of counsel. The ramifications of this new paradigm should be considered and closely followed.

Current IRS Letter Ruling Procedures

Ordinarily, the IRS will not issue a letter ruling on only part of an integrated transaction. If, however, part of an integrated transaction falls under an area of the Internal Revenue Code (Code), including those under the jurisdiction of the IRS Office of Associate Chief Counsel (Corporate) (ACC Corporate), on which the IRS will not issue letter rulings (a so-called “no-rule issue” or “no-rule area”), the IRS nonetheless may issue a letter ruling on other parts of the transaction. In addition, the IRS ordinarily will not issue letter rulings with respect to an issue that is clearly and adequately addressed by a statute, regulations, a decision of a court, or authority published in the Internal Revenue Bulletin (i.e., comfort rulings). However, in its discretion, the IRS may decide to issue a ruling on such an issue if the IRS otherwise is issuing a letter ruling to the taxpayer on another issue arising in the same transaction.

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Prior to the effective date of Rev. Proc. 2013-32, the IRS generally will not issue letter rulings addressing:

- Whether a transaction qualifies for nonrecognition treatment under § 332, § 351 (except for certain transfers undertaken before § 355 transactions), or § 1036;
- Whether a transaction constitutes a reorganization within the meaning of § 368(a)(1)(A) (including a transaction that qualifies under § 368(a)(1)(A) by reason of § 368(a)(2)(D) or § 368(a)(2)(E)), § 368(a)(1)(B), § 368(a)(1)(C), § 368(a)(1)(E), or § 368(a)(1)(F); or
- The tax consequences (such as nonrecognition and basis) that result from the application of the foregoing Code sections, unless the IRS determines that there is a “significant issue” within the meaning of Rev. Proc. 2013-3 (discussed below). If the IRS determines that there is a significant issue, and to the extent that the transaction is not described in another no-rule area, the IRS will rule on the entire transaction and not just the significant issue.

In Rev. Proc. 2009-25, the IRS announced a pilot program for letter rulings on issues arising in the context of § 355 transactions. Under this program, a taxpayer could request a letter ruling on part of a larger transaction or on a particular issue that a transaction presented. The IRS, in turn, would issue a letter ruling on the particular issue raised in the letter ruling request and not on any other issue (including, in some cases, qualification of the transaction under § 355) or on any other aspect of the transaction.

Updated IRS Letter Ruling Procedures Under Rev. Proc. 2013-32

In what is described as an effort to conserve IRS resources, Rev. Proc. 2013-32 restricts the scope of letter rulings that address issues with respect to transactions under § 332, § 351, § 355, and § 1036, and reorganizations within the meaning of § 368. Specifically, the IRS will no longer rule on whether a transaction qualifies for nonrecognition treatment under § 332, § 351, § 355, or § 1036, or on whether a transaction constitutes a reorganization within the meaning of § 368 (collectively, the Applicable Provisions), regardless of whether the transaction presents a significant issue and regardless of whether the transaction is an integral part of a larger transaction that involves other issues upon which the IRS will rule. The IRS will rule, however, on one or more issues under the Applicable Provisions to the extent that such issue or issues are “significant.”

For purposes of Rev. Proc. 2013-32, a “significant issue” is an issue of law that meets two requirements: (i) the resolution of the issue is not essentially free from doubt, and (ii) the issue is germane to determining the tax consequences of the transaction.

Sutherland Observation: Rev. Proc. 2013-3, which is applicable prior to the effective date of Rev. Proc. 2013-32, defines a “significant issue” as an issue of law that meets three requirements: (i) the issue is not clearly and adequately addressed by a statute, regulation, decision of a court, tax treaty, revenue ruling, revenue procedure, notice, or other authority published in the Internal Revenue Bulletin; (ii) the resolution of the issue is not essentially free from doubt; and (iii) the issue is legally significant and germane to determining the major tax consequences of the transaction. Thus, with regard to the definition of the term “significant issue,” Rev. Proc. 2013-32 eliminates the requirement that the issue not be clearly and adequately addressed by a statute, regulation, or other substantial authority and modifies the “germaneness” requirement. In making these changes, the IRS potentially broadened the range of issues that may qualify as “significant” for letter ruling purposes.

The IRS will rule on the tax consequences (such as nonrecognition and basis) that result from, or on another issue concerning, the application of the Applicable Provisions to the extent that a significant issue is presented. For example:

- A § 351 exchange that does not present any significant issues under § 351 may present a significant issue regarding the application of § 358 to the transferor in the exchange. In such a case, the IRS will rule only on the significant issue under § 358.
- The IRS will issue rulings addressing significant issues presented by the application of Treas. Reg. § 1.368-1(d) (concerning continuity of business enterprise in reorganizations) or Treas. Reg. § 1.368-2(k) (concerning certain transfers of assets or stock in reorganizations).

Sutherland Observation: Rev. Proc. 2013-32 does not limit the number of significant issues that may be the subject of a single letter ruling request. Also, the IRS has reserved the right to rule on any other issue in, or that is a part of, a transaction described in a letter ruling request (including ruling adversely) if the IRS believes that so doing is in “the best interests of tax administration.”

In brief, Rev. Proc. 2013-32 also notes the following points concerning the updated letter ruling process:

- All pertinent no-rule policies described in Rev. Proc. 2013-3 governing the IRS’s letter ruling practice will govern letter ruling requests made pursuant to Rev. Proc. 2013-32. For example, § 3.01(43) of Rev. Proc. 2013-3, which contains the no-rule policy regarding business purpose and “device” issues under § 355 and “plan” issues under § 355(e), continues in effect.
- In preparing a letter ruling request under Rev. Proc. 2013-32, taxpayers should continue to consult other applicable revenue procedures (e.g., Rev. Proc. 81-60, 1981-2 C.B. 680 (§ 368(a)(1)(E)); Rev. Proc. 83-59, 1983-2 C.B. 575 (§ 351); Rev. Proc. 86-42, 1986-2 C.B. 722 (§ 368(a)(1)(A), (B), (C), (D), and (F) (acquisitive reorganizations)); Rev. Proc. 90-52, 1990-2 C.B. 626 (§ 332); and Rev. Proc. 96-30, 1996-1 C.B. 696 (§ 355)) and include in the letter ruling request the information and representations described in such revenue procedures, but only to the extent that such information and/or representations relate to the significant issue(s) described in the letter ruling request.
- Before submitting a letter ruling request under Rev. Proc. 2013-32, a taxpayer should call ACC Corporate to discuss whether the IRS will entertain the letter ruling request.
- Rev. Proc. 2013-32 applies to all letter ruling requests postmarked or, if not mailed, received by the IRS after August 23, 2013.

Sutherland Observation: Given the effective date of Rev. Proc. 2013-32, taxpayers have eight weeks to send spin-off letter ruling requests to ACC Corporate if they would like to receive a letter ruling providing that no gain or loss will be recognized by the parties to such a transaction.

Effect of Rev. Proc. 2013-32 on Supplemental Letter Rulings

As provided in Rev. Proc. 2013-32, ACC Corporate will apply the same no-rule policy described above to supplemental letter ruling requests. Furthermore, with respect to supplemental letter rulings:

- A change of circumstances arising after a transaction has been completed ordinarily will not present a significant issue with respect to the transaction;
- An issue of fact (as opposed to an issue of law) does not present a significant issue; and
- All pertinent no-rule policies governing the IRS's letter ruling practice will govern supplemental letter ruling requests.

Effect of Rev. Proc. 2013-32 on Other Revenue Procedures

In order to effect the updated letter ruling process, Rev. Proc. 2013-32 modifies (or eliminates) the other revenue procedures that are referenced above and Rev. Proc. 2013-1, 2013-1 I.R.B. 1.

Sutherland Observation: Rev. Proc. 2013-32 does not impact the provisions of Rev. Proc. 2013-3 pursuant to which the IRS announced that it would no longer issue rulings concerning so-called "North-South" transactions, recapitalizations into control, and stock-for-debt swaps (see § 5.01(9), § 5.01(10), and § 5.02(2), respectively, of Rev. Proc. 2013-3) because those areas are "under study."



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