In Part I of this series, we discussed A- and B-reorganizations. In this article, we will discuss C-, D-, E-, and F-reorganizations.

C-REORGANIZATIONS

A C-reorganization, otherwise known as a “practical merger,” is where a target corporation (“Target”) transfers “substantially all” of its properties to an acquiring corporation (“Acquiror”) solely in exchange for all or a part of Acquiror’s “voting stock,” and Target then liquidates, distributing all of its remaining assets including Acquiror’s voting stock, which it just received.

Substantially All

A C-reorganization requires that Target transfer substantially all of its properties to Acquiror. To satisfy this requirement, the transfer should generally represent at least 90% of the fair market value of Target’s net assets and at least 70% of the fair market value of Target’s gross assets held by Target immediately prior to the transfer.

Solely for Voting Stock

The phrase “solely for...voting stock” has the same meaning as in a B-reorganization. Generally, voting stock plus some other consideration does not meet the statutory requirement. As a general principle, the assumption of a liability in an acquisition is treated as additional consideration (i.e., as “boot”) to the transferor. Thus, if Acquiror assumes any of the liabilities of Target in the acquisition, it would be treated as if Target received boot. However, the statute specifically provides that for C-reorganization purposes, Acquiror’s assumption of Target’s liabilities is not considered boot.

Boot Relaxation Rule

For a C-reorganization, there is an exception to the solely for voting stock requirement.


2. In certain types of reorganizations that are often referred to as “triangular” reorganizations, the voting stock of the parent of Acquiror can be used in lieu of the voting stock of Acquiror. This article does not discuss triangular reorganizations.

3. Code §§368(a)(1)(C) and 368(a)(2)(G).


that is often referred to as the “boot relaxation rule.” Under this rule, an acquisition with partial non-voting stock consideration can still qualify as a C-reorganization as long as at least 80% of the fair market value of the total consideration received by Target is voting stock of Acquiror. In making this computation, however, liabilities of Target assumed by Acquiror are considered boot. Another way to think of the boot relaxation rule is that the Acquiror is permitted to transfer some non-voting stock consideration to Target as long as the fair market value of both that non-voting stock consideration and the assumption of Target’s liabilities does not exceed 20% of the total value going to Target.

As stated above, a C-reorganization takes place in two steps: First, Target transfers substantially all of its properties to Acquiror solely in exchange for all or a part of Acquiror’s voting stock, and second, Target liquidates. In the first step, Acquiror recognizes no gain or loss on the receipt of the property in exchange for its stock, and Target recognizes no gain or loss on the receipt of Acquiror’s stock. Acquiror takes the same bases in Target’s assets as when the property was in Target’s hands. In the second step, Target recognizes no gain or loss on the distribution. Target’s shareholders recognize gain equal to the lesser of gain realized or boot received. For Target’s shareholders, the bases in Acquiror stock received are generally the same as the bases in Target stock exchanged.

Diagram of a C-reorganization

If the reorganization meets the C-reorganization requirements above and at the same time qualifies as a D-reorganization under Code §368(a)(1)(D), then the reorganization must be treated as a D-reorganization.
D-REORGANIZATIONS

A D-reorganization is a transfer by a corporation of all or part of its assets to another corporation if, immediately after the transfer, the transferor or its shareholders are in control of the corporation to which the assets are transferred, but only if in pursuance of the plan, stock or securities of the corporation to which the assets are transferred are distributed in a transaction that qualifies under Code §§354, 355, or 356.15

D-reorganizations can be acquisitive or divisive in nature. A D-reorganization is acquisitive when one corporation (“Target”) transfers substantially all of its assets to another corporation (“Acquiror”) and pursuant to the plan Target liquidates, distributing all of its assets, including the stock or securities received from Acquiror, to its shareholders.16 Generally, a D-reorganization is divisive when a corporation (“Distributing”) transfers part of its assets to a controlled corporation (“Controlled”), and the transfer is followed by the distribution of the shares of Controlled to the shareholders of Distributing.17 This article does not address divisive reorganizations. For more on Divisive D-reorganizations and the requirements under Code §355, please see our article “Tax 101: How to Structure a Corporate Division.”18

Acquisitive D-reorganizations

As described above, there are two steps in an acquisitive D-reorganization. First, Target transfers substantially all of its properties to Acquiror, and second, Target liquidates. Note the similarity of acquisitive D-reorganizations to C-reorganizations described above. C- and acquisitive D-reorganizations are both “asset” reorganizations and are both acquisitive in nature. Thus, the tax analysis of both of these types of reorganizations is very similar. A difference, however, is that C-reorganizations have the solely for voting stock requirement and D-reorganizations do not.

In the first step of an acquisitive D-reorganization, Acquiror recognizes no gain or loss on the receipt of the property in exchange for its stock,19 and Target recognizes no gain or loss on the receipt of Acquiror’s stock.20 Acquiror takes the same bases in Target’s assets as when the property was in Target’s hands.21

In the second step, Target recognizes no gain or loss on the distribution.22 Target’s shareholders recognize gain equal to the lesser of gain realized or boot received.23 For Target’s shareholders, the bases in Acquiror stock received are generally the same as the bases in Target stock exchanged.24

15 Code §368(a)(1)(D).
16 Code §§368(a)(1)(D) and 354(b)(1).
17 Code §§368(a)(1)(D) and 355.
19 Code §1032.
20 Code §361(a) and (b).
21 Code §362(b).
22 Code §361(c).
23 Code §354.
24 Code §358.
Diagram of an Acquisitive D-reorganization

In a D-reorganization, the Acquiror shareholders are often the same persons as the Target shareholders.

Meaningless Gesture Doctrine

Notwithstanding the requirement in a D-reorganization that “stock or securities of the corporation to which the assets are transferred are distributed in a transaction which qualifies under section 354, 355, or 356,” the I.R.S. and the courts have not required the actual issuance and distribution of stock and/or securities of the transferee corporation in circumstances where the same person or persons own all the stock of Target and Acquiror. In these circumstances, the I.R.S. and the courts have viewed an issuance of stock by Acquiror to be a “meaningless gesture” not mandated by Code §§368(a)(1)(D) and 354(b). 25

In the international context, it is common to restructure foreign entities in a way that can qualify as a D-reorganization through the use of the ‘check-the-box’ rules.

For U.S. tax purposes, prior to the transactions there were two separate corporations. After the transactions, (because Foreign Target is now treated as a disregarded entity) in the eyes of U.S. tax law there is only one corporation – Foreign Acquiror. Foreign Acquiror has acquired all of the assets of Foreign Target, and Foreign Target is no longer taxed as a corporation for U.S. tax purposes. This type of planning, however, should not be undertaken without a thorough U.S. tax analysis to assure that the desired U.S. tax result will be achieved.

E-REORGANIZATIONS

An E-reorganization, also referred to as a “recapitalization,” involves a single corporation that is undertaking a readjustment, or reshuffling, of its capital structure. For example, an E-reorganization may include a corporation changing the mix of its debt/equity structure.

Typically, an E-reorganization involves exchange of bonds for stock, bonds for bonds, or stock for stock. Unlike most other reorganizations, an E-reorganization does not need to meet the “continuity of interest” or “continuity of business enterprise” requirements. However, to qualify as an E-reorganization, the transaction must have a valid non-tax business purpose.

The regulations provide five examples of transactions that qualify as recapitalizations (or E-reorganizations):

- A corporation with $200,000 par value of bonds outstanding, instead of paying them off in cash, discharges them by issuing preferred shares to the bondholders.
- There is surrendered to a corporation for cancellation 25% of its preferred stock in exchange for no par value common stock.
- A corporation issues preferred stock, previously authorized but unissued, for outstanding common stock.
- An exchange is made of a corporation’s outstanding preferred stock, having certain priorities with reference to the amount and time of payment of dividends and the distribution of the corporate assets upon liquidation, for a new issue of such corporation’s common stock having no such rights.
- An exchange is made of an amount of a corporation’s outstanding preferred stock with dividends in arrears for other stock of the corporation.

F-REORGANIZATIONS

An F-reorganization is a mere change of identity, form, or place of organization of
“one” corporation, however effected.\textsuperscript{33} Since 1982,\textsuperscript{34} the statute specifically provides that an F-reorganization must involve one corporation. One court has described the F-reorganization as follows:

[The F-reorganization] encompass[es] only the simplest and least significant of corporate changes. The (F)-type reorganization presumes that the surviving corporation is the same corporation as the predecessor in every respect, except for minor or technical differences. For instance, the (F) reorganization typically has been understood to comprehend only such insignificant modifications as the reincorporation of the same corporate business with the same assets and the same stockholders surviving under a new charter either in the same or in a different State, the renewal of a corporate charter having a limited life, or the conversion of a U.S.-chartered savings and loan association to a State-chartered institution.\textsuperscript{35}

Although a transaction will generally not qualify as an F-reorganization if there is any change to the existing shareholders or in the assets of the corporation, the I.R.S. has ruled that the failure of dissenting shareholders owning less than 1\% of the outstanding shares to participate in a merger did not disqualify the merger from being an F-reorganization.\textsuperscript{36} Among other things, an F-reorganization can be accomplished by (i) merging one corporation into a new corporation in a different jurisdiction or (ii) contributing corporate shares to a new corporation and liquidating the contributed corporation upstream into its then parent.\textsuperscript{37} In 2015, final regulations regarding F-reorganizations were promulgated,\textsuperscript{38} which provide six requirements that are necessary to be considered a “mere change” in order to qualify as an F-reorganization:

\begin{itemize}
  \item Immediately after the potential F-reorganization, all the stock of the resulting corporation, including any stock of the resulting corporation issued before the potential F-reorganization, must have been distributed (or deemed distributed) in exchange for stock of the transferor corporation in the potential F-reorganization.
  \item The same person or persons must own all of the stock of the transferor corporation, determined immediately before the potential F-reorganization, and of the resulting corporation, determined immediately after the potential F-reorganization, in identical proportions.
  \item The resulting corporation may not hold any property or have any tax attributes, including those specified in Code §381(c), immediately before the potential F-reorganization.
\end{itemize}

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\textsuperscript{33} Code §368(a)(1)(F).
\textsuperscript{35} Berghash v. Commr., 43 T.C. 743, 752 (1965) (citation and footnotes omitted), aff’d, 361 F.2d 257 (2d Cir. 1966).
\textsuperscript{37} Treas. Reg. §1.368-2(m)(4), Ex. 5.
\textsuperscript{38} T.D. 9739.
\end{flushleft}
The transferor corporation must completely liquidate, for Federal income tax purposes, in the potential F-reorganization.

Immediately after the potential F-reorganization, no corporation other than the resulting corporation may hold property that was held by the transferor corporation immediately before the potential F-reorganization, if such other corporation would, as a result, succeed to and take into account the items of the transferor corporation described in Code §381(c).

Immediately after the potential F-reorganization, the resulting corporation may not hold property acquired from a corporation other than the transferor corporation if the resulting corporation would, as a result, succeed to and take into account the items of such other corporation described in Code §381(c).\(^{39}\)

Similar to E-reorganizations, F-reorganizations do not need to meet the continuity of interest or continuity of business enterprise requirements.\(^{40}\)

F-reorganizations are often utilized in foreign reorganizations where a corporation desires to change its country of organization from one country to another. The I.R.S. has held that the objective of relocating from one foreign jurisdiction to another to reduce foreign income taxes qualified as a valid business purpose.\(^{41}\)

A change in the place of organization of a corporation is not necessarily treated as a transfer of assets from the “old” corporation to the “new” corporation. However, if a U.S. corporation changes its place of organization so as to become a non-U.S. corporation, the regulations deem that a transfer of assets occurs, from the old U.S. corporation to the new foreign corporation.\(^{42}\) Similarly, if a foreign corporation changes its place of organization so as to become a U.S. corporation, the regulations deem that a transfer of assets occurs, from the old foreign corporation to the new U.S. corporation.\(^{43}\) These deemed transfers can trigger gain or income inclusions under the special rules of Code §367.\(^{44}\)

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\(^{39}\) Treas. Reg. §1.368-2(m)(1).

\(^{40}\) Treas. Reg. §1.368-1(b).

\(^{41}\) P.L.R. 200626037.

\(^{42}\) Treas. Reg. §1.367(a)-1(f).

\(^{43}\) Treas. Reg. §1.1.367(b)-2(f).

\(^{44}\) Code §367 will be discussed further in upcoming articles.