M&A Tax Talk
Distressed market series

The IRS and Treasury issue significant revisions to the applicability date provisions of the proposed section 382(h) regulations

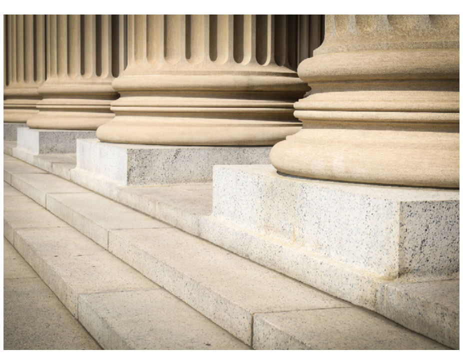
In September 2019, the Treasury and the IRS issued proposed regulations (the “Proposed Regulations”)[1] regarding a corporation’s ability to utilize net operating losses (NOLs) and other tax attributes following an ownership change within the meaning of section 382 (an “Ownership Change”). As we have previously discussed in the October edition of Deloitte’s M&A Tax Talk Series, the Proposed Regulations would significantly impact the value of tax attributes and built-in losses following an Ownership Change. For corporations with a net unrealized built-in gain (NUBIG), the most significant difference from existing guidance is that the Proposed Regulations would eliminate the benefit of “foregone amortization” under the so-called “section 338 approach.”

This change would, in many cases, materially reduce the ability of distressed and non-distressed corporations to utilize NOLs and other tax attributes following an Ownership Change.

Proposed regulations

As originally issued, the Proposed Regulations would apply only to Ownership Changes occurring after the date the Proposed Regulations are adopted as final. Until this date, the Proposed Regulations made clear that taxpayers were entitled to rely on the “section 338 approach” safe-harbor for determining built-in gains and losses.

This caused several taxpayers to raise concerns regarding the treatment of transactions that have signed or are otherwise being negotiated but have not yet closed (as well as transactions that are pending bankruptcy proceedings) at the time the Proposed Regulations are adopted as final.



2020 revisions

In January, the Treasury and the IRS issued significant revisions to the applicability date provisions of the Proposed Regulations (the “2020 Revisions”). The 2020 Revisions provide for a delayed applicability date, and certain transition relief exceptions described below.

Delayed Applicability Date: Other than in the case of a transitional relief exception described below, the applicability date of the final regulations is 30 days after the date the Proposed Regulations are adopted as final (the “Delayed Applicability Date”).

Transition Relief Exceptions: Under the transition relief provisions, the final regulations will not apply to certain Ownership Changes that occur after the Delayed Applicability Date if such Ownership Change occurs immediately after an owner shift or equity structure shift that occurs:

1. Pursuant to a binding agreement in effect on or before the Delayed Applicability Date and at all times thereafter;
2. Pursuant to a specific transaction described in a public announcement made on or before the Delayed Applicability Date;
3. Pursuant to a specific transaction described in a filing with the SEC submitted on or before the Delayed Applicability Date;
4. By order of a court (or pursuant to a plan confirmed, or a sale approved, by order of a court) in a Title 11 or similar case, provided that the taxpayer was a debtor in a case before such court on or before the Delayed Applicability Date; or
5. Pursuant to a transaction described in a private letter ruling request submitted to the IRS on or before the Delayed Applicability Date.

The preamble to the 2020 Revisions states that the “relevant owner shift or equity structure shift must be a specific, identifiable transaction” and, as an example, provides that a stock buyback pursuant to an announced, on-going program would not qualify.

Conclusion

Taxpayers may continue to rely on existing guidance with respect to any Ownership Change that either (i) occurs within 30 days of the date the Proposed Regulations are final or (ii) qualifies for a transition relief exception.

Notwithstanding the 2020 Revisions, however, the Proposed Regulations remain uniformly less favorable than existing guidance and would, in many cases, significantly impact the value of tax attributes and built-in losses following an Ownership Change. As a result, any corporation that has significant tax attributes, as well as potential buyers of such corporations, should consult a tax advisor to discuss the potential application and impact of the Proposed Regulations.

Want to learn more?
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Endnotes

1. REG-127510-18.