

**THE IRS RECENTLY ANNOUNCED THAT IT WOULD NO LONGER
RULE ON CERTAIN ISSUES IN SPIN-OFF TRANSACTIONS**

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Corporations are able to spin-off the stock of a controlled subsidiary to their shareholders without a corporate or shareholder level tax provided the distribution satisfies certain requirements. Among other things, the distribution must be motivated by one or more corporate business purposes and must not be used as a device to distribute profits on a tax-free basis to shareholders. In Revenue Procedure 2003-48, the IRS stated that it would no longer issue private rulings as to whether a spin-off meets either of these requirements. This no-rule policy is effective for all private ruling requests postmarked after August 8, 2003.

In addition, the IRS announced that it would no longer rule on whether acquisitions prior to or subsequent to a spin-off are part of a plan for purposes of determining whether a spin-off is subject to corporate tax under Section 355(e) of the Internal Revenue Code of 1986, as amended (the "Code"). For more information on Code Section 355(e) generally, see our memorandum "IRS Liberalizes Regulations Defining the Scope of a Plan under Section 355(e)" dated May 6, 2002.

In issuing rulings on spin-offs, the IRS will rely on taxpayer representations that the transaction has a valid business purpose, is not being used principally as a device and, together with an acquisition, is not part of a plan under Code Section 355(e). Those issues will, however, be subject to review on audit. The IRS also announced that it would not issue subsequent rulings unless the request presents a significant issue, which generally would not include a change in circumstances arising after the original transaction.

The IRS has stated its intention to issue more formal, published guidance to assist taxpayers on these issues. To that end, the IRS also issued two revenue rulings addressing the business purpose requirement in spin-off transactions. In Revenue Ruling 2003-74, the IRS concluded that the distribution of stock of a subsidiary to enable the management of the two entities to concentrate on their own businesses satisfied the business purpose requirements even though there would be some overlap in directors (constituting a minority on each board) following the spin-off. In addition, the IRS issued Revenue Ruling 2003-75, holding that the

distribution of the stock of a subsidiary to resolve capital allocation problems between the two businesses satisfied the business purpose requirement. Again, the ruling noted a continuing relationship between the entities – a two-year transitional services agreement and working capital loan. The IRS held that because the continuing relationship was limited, transitional and designed to facilitate rather than impede the separation of the businesses, it was not incompatible with the stated business purpose.

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Taxpayers wishing to effect spin-off transactions in the near future may consider expediting their requests in order to beat the August 8, 2003 deadline. If you would like to discuss these recent IRS pronouncements, please call Steven C. Todrys (212-455-3750; stodrys@stblaw.com), Charles O. Rappaport (212-455-2548; corappaport@stblaw.com), Robert Holo (212-455-2514; rholo@stblaw.com), Gary B. Mandel (212-455-7963; gmandel@stblaw.com), Marcy G. Geller (212-455-3543; mgeller@stblaw.com) or any other member of our tax department.

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