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Question 1.

This is a sale of Tipico's (T) assets at the corporate level followed by a distribution of the net proceeds to T's shareholders, Dawn (D), Eve (E), and Farid (F). The aggregate amount realized by T is 1500k (1200k + debt relief of 300k).

T tax effects:

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The seller T will be required to report gain or loss on each asset sold pursuant to §§61(a)(3) and 1001. Since there was no written agreement, the amount of the gain or loss per asset is determined under §1060. In the cascading allocation under 1060, the first allocation is to Class IV assets-Inventory [as there are no Class I, II, or III assets.] Then to Class V assets - Greenacre. Third, to Class VI assets-all intangibles except goodwill and going concern and finally to goodwill and going concern. As follows:

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	Adjusted Basis	FMV	<u>Net Gain/(Loss)</u>	Allocation
(from amount realized)				
Inventory	300	510	<u>210</u>	510

2 GreenAcre	900	800	<u>(100)</u>	800
2 Intangibles combined		190	<u>190</u>	190

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Therefore T recognizes an ordinary gain of 210 on the inventory and most likely, a LTCL of (100) on Greenacre and a LTCG of 190 on the Intangibles. T's substantial, but reasonable E & P disappears during the liquidation and has no impact on the gain recognized. T will incur a corporate tax liability on the ordinary income and the net LTCG. This liability should be paid prior to the distribution but the facts are not clear on that point.

#### Shareholders' tax effect:

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T will distribute 400k to each of the shareholders in complete liquidation of their stock. Under § 331, the shareholders amount realized is 400 each which, after basis recovery of 250, leaves a LTCG of 150 for each of the share holders. The Accumulated E&P of T has no effect on the transaction and disappears. If this were a "stock deal" instead, the accumulated E&P of T would not disappear. The individual shareholders have, in effect, paid to levels of tax on the deal. First at the corporate and then at the shareholder level.

#### P's Tax Effects:

2 P is entitled to a cost basis in the assets purchased of a total of 1500 (cash plus liabilities assumed) under §1012.

The allocation of the purchase price is to be the same under 1060 as the seller used since again there was no written agreement as part of the sales contract.

P's basis in assets:

Inventory 510

Greenacre 800

Intangibles 190

1 The inventory valuation is a good deal for P since any gain on sale will be reflected as income and this asset should be "flipped" the quickest. The step down in the basis of Greenacre is also good for P since it will pay any gain in the future at the capital asset rate. In general, a purchaser would favor a higher allocation to ordinary assets and a lower allocation to capital assets. I am assuming that Greenacre is an unimproved parcel and therefore is not subject to depreciation. The intangibles are another story. Under §197, goodwill and other intangibles connected in the conduct of a trade or business or investment activity are now amortized over 15 years.

If the shareholders had been "effective" tax planners they would have negotiated a reduced price to offset the double tax liability they incurred and to allocate the purchase price more

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aggressively to the intangibles and less to the ordinary assets.

Question 2:

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Hallie's Tax Consequences:

The March 1 transaction qualifies as a §351 exchange. One or more persons has transferred property to a corporation solely in exchange for stock in such corporation and, immediately after the transaction are in control as defined under §368. Hallie owns 100% of the stock. The basis in the stock received is

	AB	FMV	Debt
Blackacre:			
	650	1000	750

Hallie's Newco Stock:

Substituted basis of Blackacre	650
Less: Liability assumed	(750)
Plus: Gain recognized	100
Basis of newco stock	-0-

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