DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

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OFFICE OF
CHIEF COUNSEL

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INTERNAL REVENUE SERVICE NATIONAL OFFICE FIELD SERVICE ADVICE

MEMORANDUM FOR

FROM: John Moriarty
Assistant to the Chief
CC:CORP:B05

SUBJECT: Request for Field Service Advice

This Chief Counsel Advice responds to your memorandum dated Date F. In accordance with Internal Revenue Code ("Code") § 6110(k)(3), this Chief Counsel Advice should not be cited as precedent.

LEGEND

Parent =

Sub 1 =

Sub 2 =

Sub 3 =

Company X =

Date A =

Date B =

Date C =

Year D =

Year E =

Date F =

R =

S =

T =

U =

V =

W =

X =

Y =

Z =

Q =

P =

N =

State X =

ISSUES

1. Whether the transfer of assets from Sub 1 to Sub 3 qualifies as a reorganization under § 368(a)(1)(F).

2. If the transaction qualifies as an F reorganization, whether Sub 3 must reduce the basis of the assets it received from Sub 1 pursuant to §§108 and 1017.

CONCLUSIONS

1. In a title 11 case, if a transaction qualifies as a reorganization under both § 368(a)(1)(F) (an "F" reorganization) and § 368(a)(1)(G) (a "G" reorganization), § 368(a)(3)(C) gives the type "G" reorganization exclusive jurisdiction over the transaction. Accordingly, the transaction in this case is subject to the "G" reorganization rules.

2. Pursuant to the “G” reorganization provisions, under §§ 108 and 1017, Sub 3 would not be required to reduce the basis of the assets it received from Sub 1.

FACTS

On Date A, Parent formed two wholly owned subsidiaries, Sub 1 and Sub 2. Parent contributed R real properties, with liabilities in excess of bases in an aggregate amount of approximately $S, to Sub 1. Parent contributed T real properties, with no excess liabilities, to Sub 2.

On Date B, Sub 1 filed a petition for relief under Chapter 11 of the U.S. Bankruptcy Code. Sub 1's plan of reorganization (the”Plan”) was confirmed on Date C. As a result of the bankruptcy proceeding, liabilities of Sub 1 in the amount of $U, owed primarily to its third party creditor, Company X, were discharged. Company X also received V of Sub 1's R real properties.

Under the Plan, a new corporation Sub 3, was formed in State Y and the remaining W real properties of Sub 1, with aggregate adjusted bases of $X, were transferred free of liabilities to Sub 3. Sub 3 was formed to accommodate Company X. Sub 1 had insufficient funds to pay its undischarged debts. Company X agreed to take a promissory note from a Parent affiliate (but not from Sub 1 because of Sub 1's poor financial standing). Consequently, Sub 3 was formed. Sub 3 executed a promissory note in favor of Company X in the amount of approximately $Y. In addition, Sub 3 drew approximately $Z against a line of credit from a foreign affiliate and paid this amount to Company X. Company X provided all the funds needed to pay Sub 1's undischarged debts, for a total amount of $Q.

The taxpayer’s Year D tax return shows a reduction of NOLs, attributable to Sub 1, in the amount of $P to offset the U cancellation of indebtedness (“COD”). However, the remaining $N COD did not reduce any other tax attributes.

LAW AND ANALYSIS

Under § 61(a)(12), gross income generally includes income from discharge of indebtedness. Section 108(a)(1)(A) excepts from this rule discharges of indebtedness in a title 11 case. Section 108(b), however, provides for a reduction of tax attributes, including NOLs (§ 108(b)(2)(A)) and basis of the property of the taxpayer (§108(b)(2)(E)), if COD income is excluded from gross income.

Sub 1's only tax attributes during Year D were an NOL of $P and its bases in real properties. Under §108(b)(2)(E)(ii), a reduction to the basis of the property of taxpayer is made pursuant to the rules of § 1017. Section 1017(a) provides that a reduction to basis of property is applied to the property at the beginning of the taxable year following the taxable year in which the discharge occurs. Sub 1 claims to have sold all of its assets, at a loss, to Sub 3 for $Q at the end of Year D,

and therefore not to have any assets, the basis of which could have been reduced, in Year E.

Your office suggests that the "sale" by Sub 1 of its assets to Sub 3 qualifies as a reorganization under § 368(a)(1)(F). Pursuant to § 1.381(b)-1 of the Income Tax Regulations, in an "F" reorganization the acquiring corporation is treated (for purposes of § 381) just as the transferor corporation would have been treated if there had been no reorganization. The taxable year of the transferor does not end on the date of the transfer of assets merely because of the transfer and the tax attributes of the transferor are taken into account by the acquiring corporation as if there had been no reorganization. Thus, if the transaction were subject to the "F" reorganization rules, Sub 3 would be required to reduce its basis of $X in the assets acquired in the "F" reorganization at the beginning of Year E by $N.

Section 368(a)(1)(F) defines an "F" reorganization as a mere change in identity, form, or place of organization of one corporation, however effected. Section 368(a)(1)(G) defines a "G" reorganization as a transfer by a corporation of all or part of its assets to another corporation in a title 11 or similar case; 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 which qualifies under § 354, 355, or 356. Each of the requirements set forth in § 368(a)(1)(G), excluding the title 11 aspect, is subsumed in the requirements of § 368(a)(1)(F).[1]

Section 368(a)(3)(C) provides that if a transaction would otherwise qualify both under § 368(a)(1)(F) and § 368(a)(1)(G), then such transaction shall be treated as qualifying only under § 368(a)(1)(G). Thus, in the instant case, even if the transaction otherwise qualifies as an "F" reorganization, its qualification as a "G" reorganization is controlling. As a "G" reorganization, the taxable year of the transferor corporation (Sub 1) ended on the date of the transfer. See § 1.381(b)-1. At the beginning of Year E, Sub 1 held no assets the basis of which could be reduced. The failure of the § 108 reduction of tax attributes in the context of a "G" reorganization has been noted. See Bittker & Eustice, Federal Income Taxation of Corporations and Shareholders, ¶12.30 [3] (Seventh Ed. 2000) ("...when the insolvent corporation does recognize COD income and such income is excluded by § 108(a), the concomitant attribute reduction occurs in the transferring corporation's subsequent year, when it generally no longer has any attributes to reduce.")

CASE DEVELOPMENT, HAZARDS AND OTHER CONSIDERATIONS

[1] For example, the "G" reorganization requirement (found in § 354(b)) that "substantially all" of the assets be received by the transferee corporation in the "G" reorganization is a less stringent requirement than that implied in the "mere change ... of one corporation" language of § 368(a)(1)(F).

This writing may contain privileged information. Any unauthorized disclosure of this writing may have an adverse effect on privileges, such as the attorney client privilege. If disclosure becomes necessary, please contact this office for our views.

Should you have any additional questions, please contact at

Associate Chief Counsel (Corporate)
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