Tax Basics for the Business Lawyer

May 25, 2017

Presented by the Taxation Committee

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Tax Aspects of Mergers and Acquisitions and the Purchase and Sale of a Business

May 25, 2017

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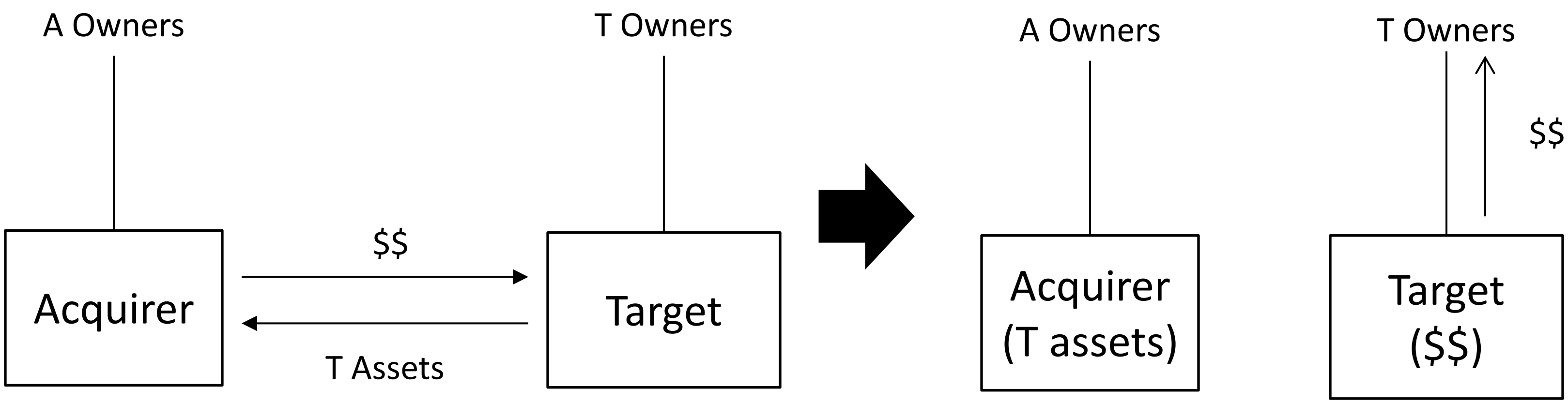
Sale of a Business

- Asset Sale vs. Ownership Interest Sale
- Buyer
  - Generally prefers asset sale
- Seller
  - Generally prefers ownership interest sale

Sale of a Business

Asset Sale



Step 1

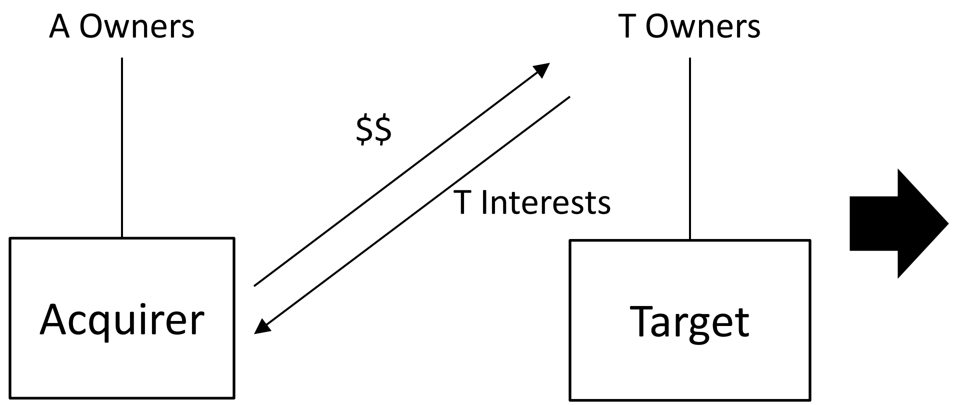
T realizes gain on assets
A obtains step-up basis
in the assets

Step 2

T owners realize gain
on distribution
A depreciates assets
using higher basis

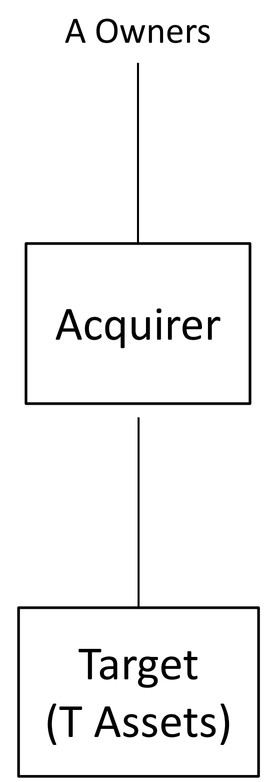
Sale of a Business

Ownership Interest Sale



Step 1

T Owners realize gain on sale of T interests
A obtains cost basis in T interests



T Owners
($$)

No Step 2!

T owners have no second level of tax

A depreciates assets using lower historical basis

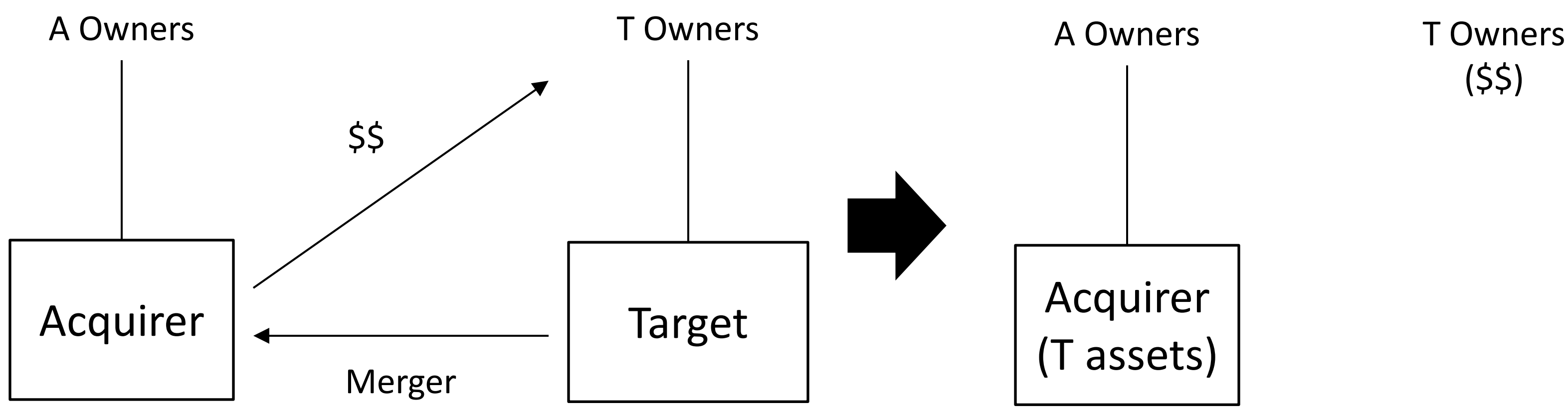
Sale of a Business

- C Corporation
  - 2 levels of tax vs. 1 level of tax
  - Higher marginal corporate tax rate vs. lower capital gains rate
- Passthrough (S Corp or Partnership)
  - Only 1 level of tax
    - UNLESS S Corp has C Corp built-in gain
  - Higher marginal ordinary income rate vs. lower capital gains rate

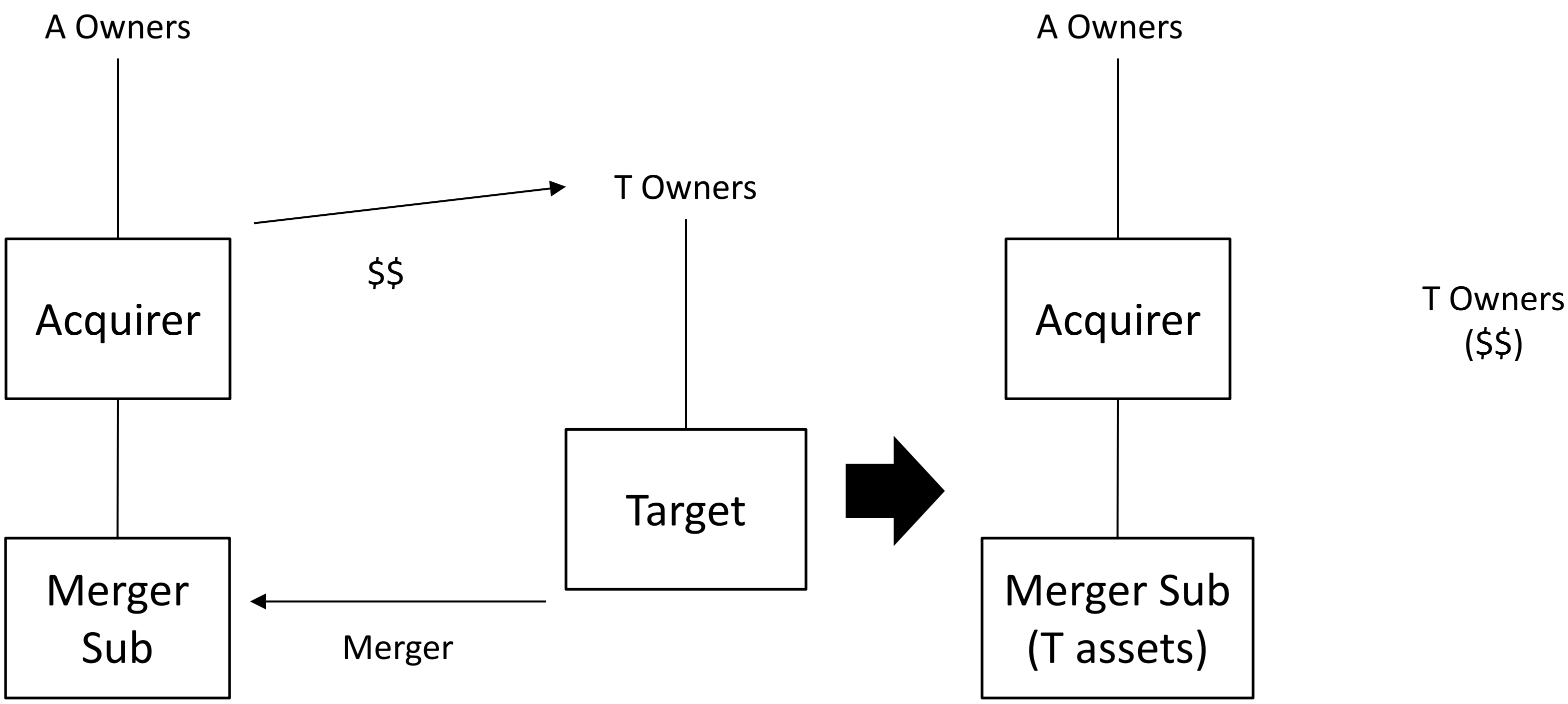
Mergers & Acquisitions

- Form Matters!
  - Statutory Merger
  - Forward Subsidiary Merger
  - Reverse Subsidiary Merger

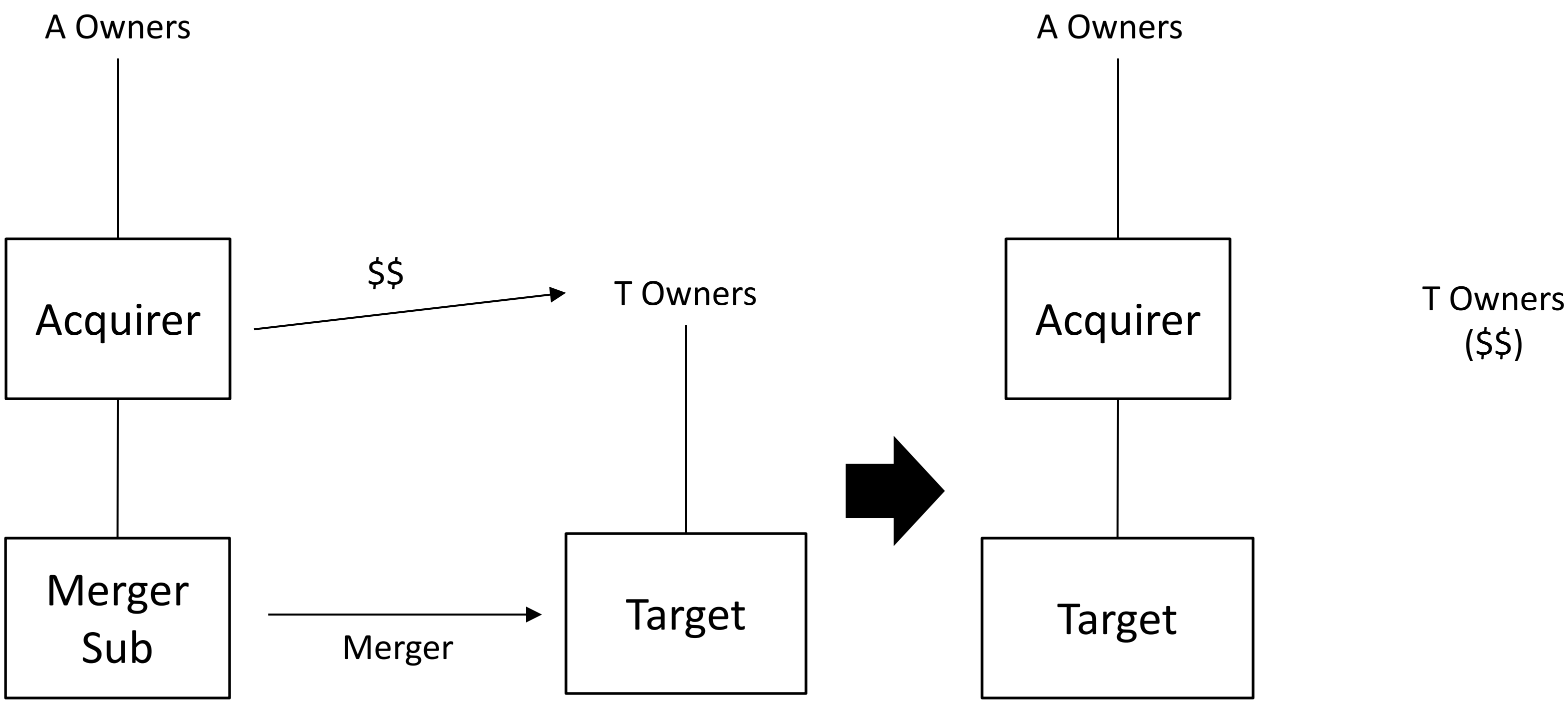
Statutory Merger



Forward Subsidiary Merger



Reverse Subsidiary Merger



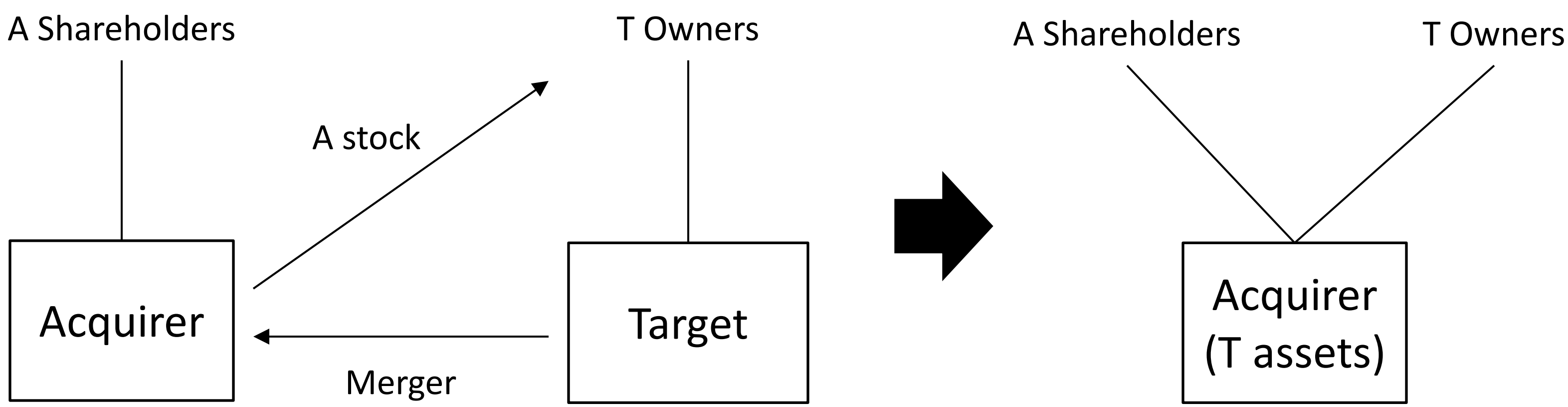
"Tax Free" Reorganizations

- Requires corporate parties to the reorg
- General requirements
  - Continuity of Interest (COI)
    - Generally at least 40% of the consideration must be stock in the acquirer
  - Continuity of Business Enterprise (COBE)
    - Use at least 1/3 of the historical assets
  - Business Purpose
    - Non-tax business reason

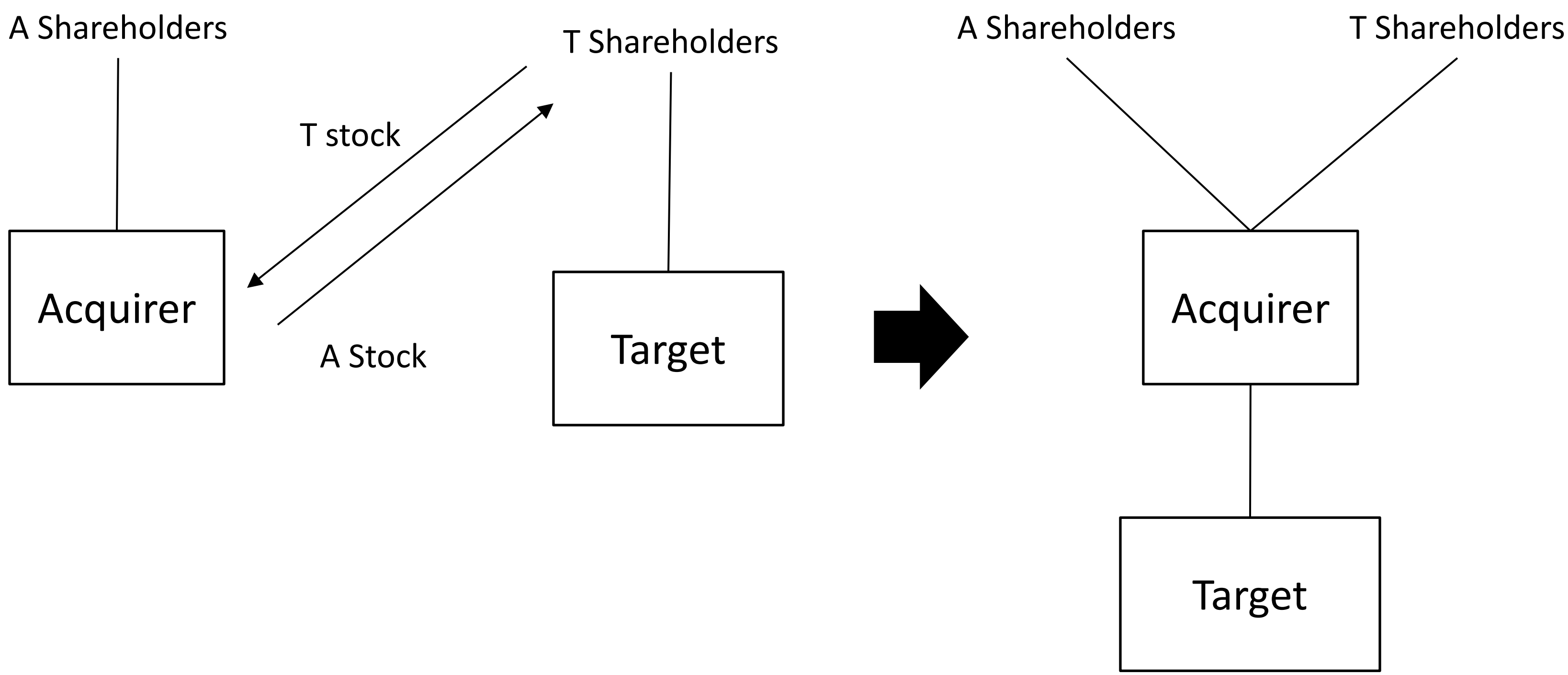
Reorganizations

- Type A (Statutory Merger)
- Type B (Stock Acquisition)
- Type C (Asset Acquisition)
- Type D (Divisive)
- Type F (Change in Form)

Type A (Statutory Merger)

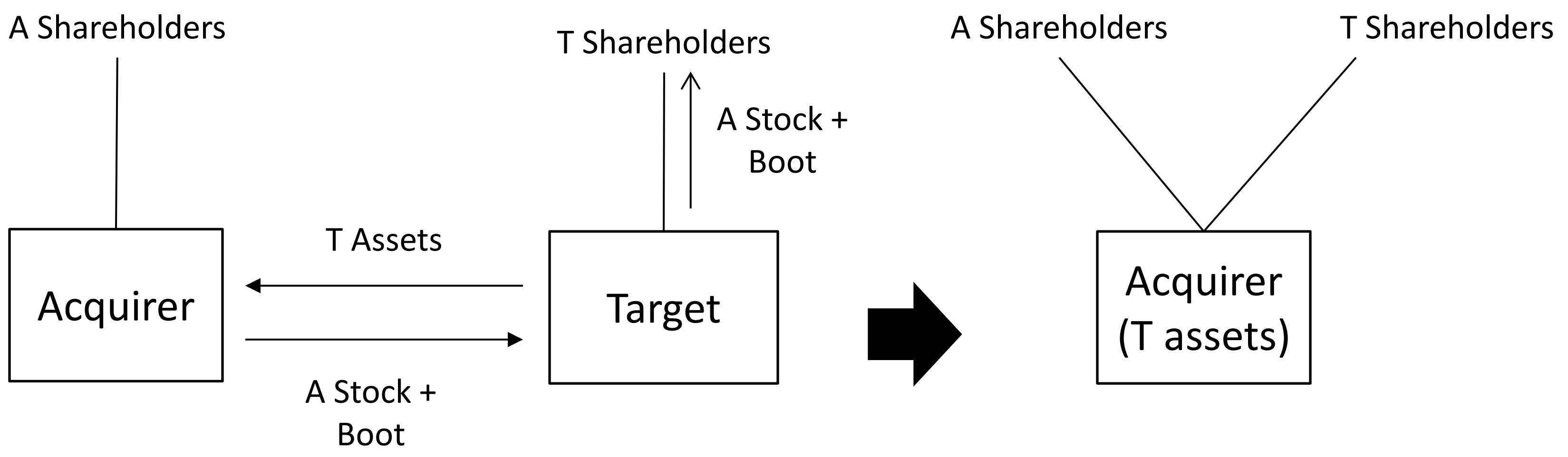


Type B (Stock Acquisition)



Target Shareholders must exchange T stock for A stock AND Acquirer must have control (80% of vote and value) immediately after the acquisition

Type C (Asset Acquisition)



Target must exchange substantially all of its assets (70% of gross, 90% of net) for A voting stock (at least 80% of fair market value of assets) AND Target distributes all its property to the T shareholders