ALSTON & BIRD LLP

WWW.ALSTON.COM

Federal Tax ADVISORY

JUNE 1, 2014

Last *Granite Trust* Ruling

LTR 201419011

We keep thinking we have seen the last letter ruling allowing a taxpayer to separate a subsidiary liquidation from a preliminary decontrolling stock sale but they keep coming—at least for now. The idea is for a corporate parent to recognize a loss on the majority of the stock of a wholly owned subsidiary by avoiding a Section 332 liquidation and having a Section 331 liquidation following its sale of some of the subsidiary's stock to an affiliate that is outside the corporation's consolidated group. A handy subsidiary to use in these cases is a REIT. A less-handy subsidiary is a foreign corporation. Alternately, the group owning the LossCo can just form a partnership and have it buy the LossCo stock.

Granite Trust

GraniteTrust Co. v. U.S., 238 F2d 670 (1st Cir. 1956) ruled that a parent's sale of more than 20 percent of the stock of a subsidiary to an unrelated person was a proper set up for a taxable liquidation of the subsidiary. As a result, the parent was able to recognize all of its loss on the subsidiary.

Granite Trust was not the first or only decision to rule as such, but it has come to be symbolic of the principle that a formal liquidation can be separated from a preliminary and intentional decontrolling sale of part of the subsidiary's stock. In other words, the step transaction doctrine was not applied as it otherwise might have been.

In 2014, the IRS announced that it no longer would rule on ***Granite Trust***-type liquidations, but with several rulings already in the pipeline, the decisions keep coming. The most recent is LTR 201419011.

Facts

The taxpayer owned LossCo and two REITs. It sold a portion of LossCo's stock to a REIT for nonqualified preferred stock. This type of stock is not property for Section 304 purposes, and so the sale could be treated as a Section 1001 loss recognition event. The next day, the parent and the REIT "will consider" adopting a plan of liquidation for LossCo.

Rulings

The decontrolling sale of stock will have to comply with the unified loss rule of Reg. Section 1.1502-36. The loss on that sale will be deferred under Section 267(f), but the loss on the liquidating distribution will not. LossCo will recognize losses on its distributions in liquidation, which will not be deferred.

The effect of the ruling is to allow, presumably, 79 percent of the loss on the LossCo stock to be currently recognized in the group, with the rest suspended until the seller or buyer leaves the Section 267 controlled group. That is an event that is not so hard to produce.

Representations

The taxpayer represented that "following the Share Sale: (i) REIT 1 will become the legal owner of the Transferred Shares; (ii) the Share Sale will be duly recorded on the records of LossCo; (iii) REIT 1 will have complete dominion and control over the Transferred Shares; (iv) REIT 1 will have the right to vote on all shareholder resolutions with respect to the Transferred Shares; (v) the Transferred Shares will provide REIT 1 the right to its proportionate share of current distributions; (vi) the Transferred Shares will provide REIT 1 the right to its proportionate share of the net assets of LossCo if LossCo were to liquidate; and (vii) REIT 1 will not hold itself out as owning the Transferred Shares as an agent, trustee, or nominee (or in any similar role) for another person."

In other words, the REIT has to really own the LossCo shares for the instant before the formal plan of liquidation is adopted.

Conclusion

If the IRS is down on ***Granite Trust*** deals, you would not know it from this ruling, which was issued five months after the request was submitted. Perhaps they really mean what they have said in explaining the no rule: they don't like the result and won't help taxpayers get it, but taxpayers are free to continue to rely on the authorities that have been out there for decades. Based on that, ***Granite Trust*** deals are likely to continue.

For more information, contact Jack Cummings at (919) 862-2302.

If you would like to receive future *Federal Tax Advisories* electronically, please forward your contact information to **taxgroup@alston.com.** Be sure to put "**subscribe**" in the subject line.

If you have any questions or would like additional information, please contact your Alston & Bird attorney or any of the following:

Federal Tax Group

Sam K. Kaywood, Jr.
Co-Chair
404.881.7481
sam.kaywood@alston.com

Edward Tanenbaum
Co-Chair
212.210.9425
edward.tanenbaum@alston.com

George Abney
404.881.7980
george.abney@alston.com

John F. Baron
704.444.1434
john.baron@alston.com

Henry J. Birnkrant
202.239.3319
henry.birnkrant@alston.com

James E. Croker, Jr.
202.239.3309
jim.croker@alston.com

Jasper L. Cummings, Jr.
919.862.2302
jack.cummings@alston.com

Brian D. Harvel
404.881.4491
brian.harvel@alston.com

L. Andrew Immerman
404.881.7532
andy.immerman@alston.com

Brian E. Lebowitz
202.239.3394
brian.lebowitz@alston.com

Clay A. Littlefield
704.444.1440
clay.littlefield@alston.com

Ashley B. Menser
919.862.2209
ashley.menser@alston.com

ALSTON & BIRD LLP

WWW.ALSTON.COM

ATLANTA: One Atlantic Center ▪ 1201 West Peachtree Street ▪ Atlanta, Georgia, USA, 30309-3424 ▪ 404.881.7000 ▪ Fax: 404.881.7777
BRUSSELS: Level 20 Bastion Tower ▪ Place du Champ de Mars ▪ B-1050 Brussels, BE ▪ +32 2 550 3700 ▪ Fax: +32 2 550 3719
CHARLOTTE: Bank of America Plaza ▪ 101 South Tryon Street ▪ Suite 4000 ▪ Charlotte, North Carolina, USA, 28280-4000 ▪ 704.444.1000 ▪ Fax: 704.444.1111
DALLAS: 2828 North Harwood Street ▪ 18th Floor ▪ Dallas, Texas, USA, 75201 ▪ 214.922.3400 ▪ Fax: 214.922.3899
LOS ANGELES: 333 South Hope Street ▪ 16th Floor ▪ Los Angeles, California, USA, 90071-3004 ▪ 213.576.1000 ▪ Fax: 213-576-1100
NEW YORK: 90 Park Avenue ▪ 12th Floor ▪ New York, New York, USA, 10016-1387 ▪ 212.210.9400 ▪ Fax: 212.210.9444
RESEARCH TRIANGLE: 4721 Emperor Blvd. ▪ Suite 400 ▪ Durham, North Carolina, USA, 27703-85802 ▪ 919.862.2200 ▪ Fax: 919.862.2260
SILICON VALLEY: 1950 University Avenue ▪ 5th Floor ▪ East Palo Alto, California, USA, 94303-2282 ▪ 650-838-2000 ▪ Fax: 650.838.2001
WASHINGTON, DC: The Atlantic Building ▪ 950 F Street, NW ▪ Washington, DC, USA, 20004-1404 ▪ 202.756.3300 ▪ Fax: 202.756.3333