



Federal Tax ADVISORY ■

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Uncertain Tax Disclosures

There has been an increase in the use of tax disclosures in SEC filings on corporate transactions that either fail to conclude on the expected tax treatment or state how the company will report but that the shareholders may report differently. Such filings should be troubling to the IRS because they signal the potential for a whipsaw against the government. Shareholders might view them as helpful in providing flexibility, but more often shareholders want certainty.

At one time the SEC would not approve a discussion of material federal income tax consequences that did not conclude to a high degree of certainty on the tax treatment of the transaction involving shareholders. Then the “should” opinion crept into the lexicon of legal opinions about 20 years ago. That set the stage for even greater erosion of certainty in tax disclosures. Now the SEC can be satisfied if the company just tells the truth about the level of uncertainty.

Whipsaws can arise most easily in corporate reorganizations, including spinoffs. The problem is not new. The corporation in *King Enterprises Inc. v. United States*, 418 F2d 511 (Ct. Cl. 1969) had received a ruling that it was making a taxable purchase of stock. However, some shareholders claimed the acquisition was a reorganization and they prevailed.

Similar transactions occur today and are planned into. The corporation may expect the transaction to be taxable to it, and may arrange to use NOLs or cash dividended from a spun off corporation to pay the tax. But the corporation may tell the shareholders to consult their tax advisors.

In many cases, tax advisors do not have access to the facts needed to evaluate the tax treatment of a corporate transaction. It may depend on valuations, for example, not publicly revealed. Or the facts may be clear but the corporation may suggest that the shareholders can take an aggressive reporting position on the law.

This is new territory to the extent the whipsaw potential is promoted by the corporation. Stay tuned for some interesting litigation.

For more information, please contact [Jack Cummings](#) at 919.862.2302.

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