

Reporting Acquisitions of Control

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Information reporting is hardly a new phenomenon, but it is growing. Like a many-headed hydra it seems to get more and more pervasive, and occupy more and more of our time. One such reporting mechanism relates to changes of control implicating Internal Revenue Code Section (“Code Sec.”) 367. The IRS has issued final regulations requiring information reporting by a corporation if control of the corporation is acquired, or a shareholder has a substantial change in capital structure, and the corporation or any

shareholder must recognize gain under Code Sec. 367(a). [T.D. 9230, Dec. 2, 2005; Reg. §1.6045-3.] These regulations are effective for acquisitions of control and substantial changes in capital structure that occur after December 5, 2005.

Statutory Mechanism

Under Code Sec. 6043(c), if any person acquires control of a corporation, or if there is a recapitalization or other substantial change in a corporation’s capital structure, it must file a return. That return must reveal the identity of

the parties to the transaction, the fees involved, the changes in the capital structure involved and any other information the IRS requests.

Broker Reporting

There is broker reporting too. Under Code Sec. 6045, every broker must file a return (when required to do so by IRS) showing the name and address of each customer, with details on gross proceeds and any other information the IRS may request in forms or regulations.

The temporary regulations were issued on December 30, 2003, requiring a domestic corporation involved in an acquisition of control or substantial change in capital structure to file Form 8806, *Information Return for Acquisition of Control or Substantial Change in Capital Structure*, if it or any shareholder was required to recognize gain as a result of Code Sec. 367(a). Form 8806 was required to be filed within 45 days following the transaction. [Reg. §1.6043-4T(a)(3).] However, a reporting corporation wasn't required to file Forms 1099-CAP for its shareholders that were clearing organizations, or to furnish Forms 1099-CAP to them, if they made an election to allow IRS to publish information regarding the transaction. [Reg. §1.6043-4T(b)(1).]

Under these 2003 temporary regulations, brokers were exempt recipients. [Reg. §1.6043-4T(b)(5).] Brokers were required to file Form 1099-B, *Proceeds from Broker and Barter Exchange Transactions*, reporting the required information with respect to their customers who were not exempt recipients if they knew or had reason to know, based on readily available information, that an acquisitions of control or substantial changes in capital structure had occurred. [Reg. §1.6045-3T(c).]

Final Regulations

With minor exceptions, the final regulations generally adopt the 2003 temporary ones. Thus, information reporting is limited to transactions in which the reporting corporation or any shareholder is required to recognize

gain (if any) under Code Sec. 367(a). The final regulations do make some clarifying changes to the 2003 temporary regulations. Plus, in response to comments received, they add one modification.

The final regulations revise the definition of "acquisition of control of a corporation" in Reg. §1.6043-4T(c)(1)(i) to omit transactions where stock representing control of a corporation is distributed by a second corporation to shareholders of the second corporation, because these transactions will not result in a recognition of gain under Code Sec. 367(a) and its regulations. The final regulations also delete the following rules in the 2003 temporary rules as unnecessary, since they don't deal with transactions that may result in recognition of gain under Code Sec. 367(a):

- The rule regarding constructive ownership in Reg. §1.6043-4T(c)(3)
- The rule dealing with two or more corporations acting under a plan or arrangement in Reg. §1.6043-4T(c)(4)
- The rule on a Code Sec. 338 election in Reg. §1.6043-4T(c)(5)

Similarly, the definition of change in capital structure in Reg. §1.6043-4T(d)(2) is modified in the final regulations to remove the inclusion of recapitalizations and redemptions. Those transactions also will not result in a recognition of gain under Code Sec. 367(a).

Effective Date

The final regulations are effective for acquisitions of control and substantial changes in capital structure that occur after December 5, 2005. The Preamble notes that the 2003 proposed regulations remain outstanding for transactions not covered by the final regulations. The IRS will continue to consider the proper implementation of the additional information reporting provided in Code Sec. 6043A and the coordination of reporting requirements under Code Sec. 6043(c), Code Sec. 6043A and Code Sec. 6045 to transactions not covered by the final regulations.

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