



Robert W. Wood

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Yahoo Alibaba Spinoff Raises IRS Ruling v. Legal Opinion Debate

In January 2015, Yahoo CEO Marissa Mayer announced [a tax savvy spinoff plan](#) for Yahoo's remaining 384 million shares in Alibaba, now worth [\\$23 billion](#). But now, the IRS revealed that it will not issue a [private letter ruling](#), and that smarts. A ruling is advance blessing from the IRS, a binding letter you attach to your tax return, worth its weight in gold.

It is not yet clear if the deal will go ahead as planned based on a law firm's tax opinion, if the deal will change, or perhaps even be scuttled. Plainly, the fact that the IRS will not rule does *not* mean it will be taxable even if it proceeds exactly as advertised. But the IRS certainly *knows* about it.



Yahoo President and CEO Marissa Mayer speaks during the International Consumer Electronics Show in Las Vegas. Yahoo Inc. on April 21, 2015 (AP Photo/Julie Jacobson, File)

Yahoo is big enough that it is under permanent IRS audit. Even so, there is a kind of *in terrorem* effect of asking for a ruling and not getting it. Just imagine Clint Eastwood as IRS Commissioner. Refusing to issue an IRS ruling, he would say, "Well, punk, do you feel lucky today?"

If the deal proceeds and is taxable—and if the tax lawyers don't fight about it, which they would—there's talk about what it could mean. Some say Yahoo would face a tax bill of \$7 billion on the distribution to its shareholders. Yahoo shareholders would be hurt too.

But whatever happens to Yahoo's mega-spin, it is causing renewed discussions of the old opinion vs. ruling fork in the road. "Do you want a [tax opinion](#) or a private letter ruling?" is rarely a simple question. Cost, speed, certainty, and risk must be considered, but you may not have a choice.

Binding vs. Not. Rulings are binding on the IRS, [tax opinions are not](#). That is one reason you must attach a copy of the ruling to your tax return when you file it. You never attach an opinion to a tax return.

No Rule Areas. A tax opinion can be written on just about anything. In contrast, the IRS has lists of subjects on which it will not rule. A first line of inquiry should be whether your subject is on a no-rule list.

Appropriate Questions. If the tax issue is plain vanilla in character, it may not be possible to get a ruling, even if it is not on a no-rule list. If the issue is plain vanilla, the IRS may call your request one for a "comfort ruling," something the IRS generally will not issue. Conversely, if the tax issue is unique or difficult, it may be outside the realm of rulings on the other extreme. Maybe that was Yahoo's Alibaba problem?

Many taxpayers feel the middle ground—where you *can* get an IRS ruling—is generally where you do not need one. If the law is unclear and you really need a ruling, you may not be able to get it. If the law is settled and you are perceived as too needy for comfort, you can't get that either. Fortunately, tax opinions fill the gaps.

Don't Ask. One generally should not *ask* for a ruling unless there is a high likelihood you can get it. A ruling is gold-plated certainty, but the IRS does not usually give it in close or tough cases. There are consequences for asking, too.

When you request a ruling, you generally must pay a fee. There is a range of fees, but a common fee is \$28,300. If the IRS answer is no, practitioners customarily withdraw their ruling request and may get their fee back. You don't want a "no" answer on the books.

If the IRS says it can't rule and you withdraw your request, the IRS sends an audit notice to the IRS field office in your area. The notice informs field IRS employees that you asked for a ruling, didn't get it, and withdrew your request. If you proceed with the transaction, your return could be flagged.

Rulings Take Time. A tax opinion can be knocked out in days or weeks. A ruling takes weeks or months. Most take six months or more.

Pre-Ruling Conference. Today, almost no IRS ruling is submitted without an informal trial run. You talk to the IRS and get their general view on your proposed ruling. Then, you submit a short (5 page or so) memo about the facts, the issue, and the ruling you want. The IRS meets informally in person or by phone, generally with 2 to 5 IRS attorneys covering different aspects of the topic.

The IRS reacts orally to the memo, and often can suggest a tentative result. If all is positive, you prepare and submit your ruling request. If not, you don't. Either way, the informal request is not official and triggers no fee. If it does not go well and you never make a formal ruling request, it triggers no audit notice—at least not that I know about!

Conclusion. IRS rulings and tax opinions each have their place. Rulings can seem counterintuitive. If your position is weak or uncertain, the IRS will not rule. If your position is plainly correct, the IRS may call it a comfort ruling. A ruling makes sense only in the sweet spot in between.

If the dollar consequences of being wrong are catastrophic, as in Yahoo's situation, a ruling is clearly best. But sometimes, you cannot get a ruling and should not ask. In contrast, opinions are a kind of everyman. They are flexible and probably deserve more credit. Plus, tax opinions are not just about protection from IRS penalties.

Some people want a tax opinion to give them protection from IRS penalties. Opinions do much more, and should help you prevail in the event of an audit. Besides, if all an opinion accomplishes is protection from IRS penalties—meaning you have to pay all the taxes and all the interest—isn't the opinion a big failure?

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