

The avoidance of tax is the only intellectual pursuit that carries any reward.

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Code and Regs:

- §§302(a), (b)(1)-(4), (b)(6), (c), (d); 312(n)(7); 317(b); 318 (skim references to trusts); 1059(e)(1)(A) and (e)(2)
 - §§1.302-2(a)-(c); 1.302-3; 1.302-4 (skim only)
1. C Corp is owned by the following individuals (and shares owned): A (100); B (200); C (300); Dad (D) (400), and E (300). A and B are C's children, Dad is C's wife, and E is C's father. How many shares does each own directly and constructively under §318?
 2. C Corp is owned 50%-50% by individuals A and B. C Corp owns 70% of D Corp. B owns 100% of E Corp. To better apply the constructive ownership rules, I suggest drawing an ownership diagram.
 - (a) How much does A own of D Corp and E Corp?
 - (b) How much of E Corp does D Corp own?
 - (c) How much of C Corp does E Corp own?
 - (d) How much of D Corp does E Corp own?
 3. C Corp has 1,000 common voting shares outstanding, and A owns 500 shares. C Corp redeems 200 of A's shares. Does the redemption qualify as substantially disproportionate under §302(b)(2)?
 4. Briefly explain the function of §302(b)(2)(D).
 5. V Corp is owned entirely by unrelated individuals J, K, and L, and has three classes of stock outstanding: voting common stock (CS), a class of voting preferred stock (VPS), and a class of nonvoting preferred stock (NVP). Each share of the VPS has the same voting rights as one share of the CS. J owns 200 shares each of the CS and the VPS. K owns 100 shares of each of the three classes of stock. L owns 100 shares of the NVP. Assume that V Corp has sufficient amount of E&Ps.
 - (a) V Corp redeems 100 shares each of J's CS and VPS. *See* Rev. Rul. 75-502.

- (b) V Corp redeems 20 shares of K's CS, 80 shares of VPS, and 50 shares of NVP.
 - (c) V Corp redeems 50 shares of K's CS, VPS, and NVP.
6. A owns 800 shares and B owns the remaining 200 shares of the common stock of C Corp. A is B's father. A's basis in his shares is \$80,000 (\$100/share), and the FMV of all of the C Corp stock is \$1MM. As part of succession planning, C Corp redeems all of A's shares for \$800,000.
- (a) Does this redemption qualify under §302(b)(3)? Why not? What happens to A's basis in the redeemed shares? See §1.302-2, Ex. 2.
 - (b) What can A do to bring the redemption under §302(b)(3). What are the consequences to A and B?
 - (c) Same as (a) but A receives a note in exchange for his shares with the interest rate pegged to the 10-year treasury rate plus 3%.
7. What would be the result if in Rev. Rul. 81-289, the corporation redeemed 1.5% of its shares (15,000x/1,000,000x)? Are there any enforcement problems with redemptions by public corporations?
8. When a shareholder invests in a mutual fund or requests redemption from the fund, the purchase or redemption price of each share is its net asset value (NAV), which is the net assets under management (AUM) divided by the numbers of shares outstanding. For example, if a fund has an AUM of \$1,000, and 100 shares outstanding, its NAV would be \$10/share (\$1,000 AUM / 100 shares).
- Assume that mutual fund (MF) has 10 unrelated shareholders (A through J) each owning 10 shares (a total of 100 shares outstanding), and each share is worth \$10. Assume that each shareholder has a basis of \$1 in each share. What are the tax consequences to A in the following alternatives?
- (a) MF redeems all of A's shares \$100.
 - (b) MF redeems one of A's shares for \$10.
 - (c) MF redeems one of A's shares for \$10, and simultaneously redeems all of B's and C's shares for \$100 each. Please answer the question before looking at §302(b)(5).
9. What are the tax goals of the seller and purchaser in *Zenz* and similar bootstrap acquisitions?
10. Describe the transaction undertaken in *H.J. Heinz Co. v. US*.

- (a) Read §1059(e)(1)(A)(ii) and Reg. §1.1059(e)-1(a). How would those provisions affect the transaction today?
- 11. Unrelated individuals A and B own 800 (80%) and 200 (20%) shares, respectively, of S Corp, which has been an S corp since its formation. A's basis in its S Corp stock is \$8,000 (\$10/share), and B's basis is \$2,000.
 - (a) S Corp distributes \$80 to A and \$20 to B. §§1367(a)(2); 1368(a) and (b).
 - (b) S Corp redeems 200 of A's shares for \$5,000. §302(b) and (d); 1368(a) and (b); and 1371(a). Would A prefer sale/exchange treatment or ordinary distribution treatment? What if all of A's shares were being redeemed?
 - (c) Does a redemption of an S Corp shareholder raise any "2nd class of stock" issues? *See* §1.1361-1(l)(2)(iii).
 - (d) Instead of redeeming A, S Corp redeems 100 of B's shares with appreciated stock of Exxon held for 5 years (FMV = \$1,000; AB = \$500).
- 12. Describe the Coca Cola buyback transaction posted on the class page.
- 13. Describe the Carrier transaction posted on the class page.
- 14. What are the proposals regarding the taxation of buybacks discussed in the Hemel article on the class web page?