

Rev. Rul. 80-213

Section 301. -- Distributions of Property

26 CFR 1.301-1: Rules applicable with respect to distribution of money and other property .

July, 1980

[*1]

"Stapled," "paired," or "back-to-back" stock; valuation. Factors are set forth that should be considered, in addition to those in Rev. Rul. 59-60, in valuing the stock of a subsidiary corporation that is distributed to the shareholders of the former parent and that can be sold only with the stock of the distributing corporation; Rev. Rul. 59-60 amplified.

SECTION 1. PURPOSE

The purpose of this revenue ruling is to provide information and guidance to taxpayers, Internal Revenue Service personnel, and others concerned with the valuation for federal tax purposes, of stock of a subsidiary corporation that is distributed to the shareholders of the former parent and can be sold only with the stock of the distributing corporation. Such stock is referred to as "stapled," "paired" or "back-to-back" stock.

SEC. 2. BACKGROUND

There are variations in the methods by which stapling arrangements are created, but they generally have the following features in common: (a) An existing domestic corporation organizes a new foreign affiliate to conduct business in a foreign country. The affiliate is usually organized in a country with lower tax rates than the United States or that offers other [*2] tax advantages. (b) The affiliate issues the same number of shares as the parent company has outstanding. (c) The shares of the affiliate are distributed ratably to the shareholders of the domestic corporation. (d) The shares of the two companies are stapled or paired so that they can be transferred only as a unit. (e) There is generally a close association in the operations of the two companies.

The distribution by the parent of the subsidiary stock to the parent's shareholders under these circumstances is a distribution of property to the shareholders within the meaning of section 301(a) of the Internal Revenue Code and will be includable in the gross

incomes of the parent's shareholders as a dividend distribution to the extent provided in section 301(c) and section 316. Rev. Rul. 54-140, 1954-1 C.B. 116. Also, see *Wilkinson v. Commissioner*, 29 T.C. 421 (1957), nonacq., 1960-2 C.B. 8.

SEC. 3. NATURE OF THE PROBLEM

In many instances the stock of the distributing company is publicly traded on one of the organized exchanges or in the over-the-counter market. Therefore, market quotations are available for the stock of the distributing company prior to the distribution [*3] and for the stapled stock after the distribution. There are no market transactions solely in the stock of the distributed corporation. Consequently, some other measure of its value must be used.

Rev. Rul. 59-60, 1959-1 C.B. 237, outlines and reviews in general, the approach, methods and factors to be considered in valuing shares of capital stock of closely held corporations. The methods discussed therein also apply to the valuation of corporate stocks in which market quotations are either unavailable or are so infrequent that they do not reflect fair market value. Rev. Rul. 68-609, 1968-2 C.B. 327, points out that the general approach, methods, and factors outlined in Rev. Rul. 59-60, as modified, are equally applicable to valuations of corporate stocks for income and other tax purposes as well as for estate and gift tax purposes and apply in determining the fair market value of business interests.

Although Rev. Rul. 59-60 does not provide specific rules for stapled stock, it does provide general guidelines for valuing such stock of the distributed corporation. There are factors surrounding the formation of the distributed corporation, the distribution of its shares, its [*4] continued operation, and the sale of its stock that are not encountered in valuing the stock of a typical closely held corporation. A proper analysis of fair market value of stapled stock requires the consideration of all relevant facts and circumstances.

SEC. 4. VALUATION CONSIDERATIONS

The following factors, in addition to those mentioned in Rev. Rul. 59-60, should be considered in valuing stapled stock.

.01 Valuation of securities is, in essence, a prophecy as to the future and must be based on facts available and the prospective economic conditions as of the valuation date. Because the future of the distributed and distributing corporation will be closely associated by the stapling of the stock of the two corporations, the history and experience of the distributing corporation in conducting the same or similar business of the distributed corporation should be considered.

.02 In reviewing the prior earnings of the distributed company in operating the business either as a division or a subsidiary, adjustments must be made to the earnings to account for changes that will result because of the change in status. The distributed company may

not be subject to United States [*5] laws in general and may no longer be subject to federal income taxes.

.03 When the subsidiary is a foreign corporation, consideration should be given to the corporation laws of the host country, the political stability of the host country and the countries in which the company operates, the possibility of changes in the rate of exchange, and restrictions on the transfer of funds. Consideration should also be given to the fact that the management of the distributing company weighed these factors along with other advantages and disadvantages in arriving at the decision to conduct business under this form of organization.

.04 The quality, experience, and reputation of the company are important factors in the valuation of a business. Where the distributed company proposes to carry on a business on much the same basis as had existed prior to the distribution, consideration should be given to the good will and going concern value developed by the distributing company and also whether the management of the distributed company will be composed of largely the same persons as had existed prior to the realignment. Consideration should also be given to the possibility of the distributed [*6] company being able to call upon personnel of the distributing company for specialized areas of expertise.

.05 Any financial assistance in the form of direct loans, surety arrangements, or performance guarantees from the distributing company would tend to place the distributed company in a more favorable position than if it were to exist as an operationally independent entity.

.06 Whether the distributed company is to assume any existing contracts or is to be assigned contracts from any particular customers or in any particular geographical area should be noted.

.07 If the distributed company meets stock exchange listing requirements only by virtue of the stapling arrangement, this enhanced marketability is a valuation factor to be considered.

.08 In most instances, the best measure of the value of closely held stock is found in the prices at which the stock of companies engaged in the same or a similar line of business are selling in a free and open exchange. When stock is valued by this approach it is generally necessary to adjust the preliminary value in recognition that the shares of the comparative companies are publicly traded while the shares to be valued are not.

Where [*7] the stock of the distributing corporation is registered prior to the distribution, the stapled shares can be publicly traded after the distribution with the stock of the distributing corporation. Therefore, no discount for lack of marketability is appropriate in that instance.

SEC. 5. EFFECT ON OTHER DOCUMENTS

Rev. Rul. 59-60, as modified by Rev. Ruls. 65-193, 1965-2 C.B. 370, and 68-609, 1968-2 C.B. 327, and as amplified by Rev. Rul. 77-287, 1977-2 C.B. 319, is further amplified.