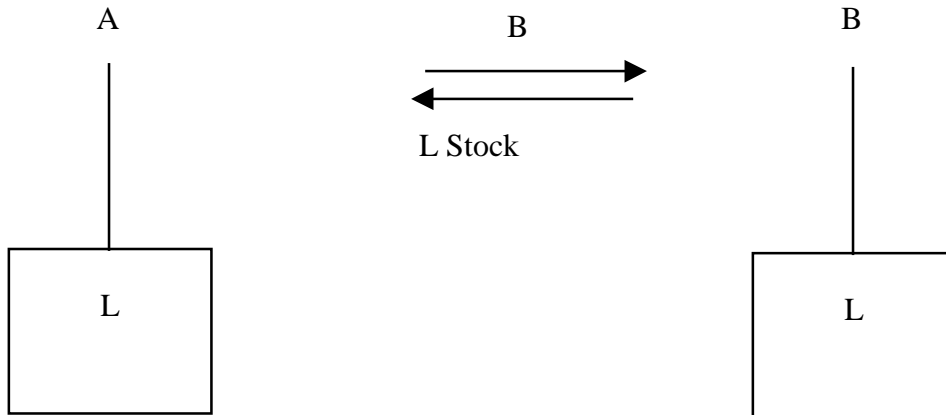


Overview of Section 382 - Ownership Change (p. 35)



1. On January 1, 1996, L corporation is owned by individual A.
2. A has owned all of L's only class of outstanding stock since L's inception in 1992. L has a \$200 NOL carryover from previous year.
3. On December 31, 1996, A sells all of the L stock to B for \$500. At that time, the applicable rate for section 382 is 5%. (Assume that L had no taxable income or loss for 1996.)
4. During 1997, L generates \$200 in taxable income.
5. The sale of L stock to B is an ownership change.
6. With respect to 1997, L's NOL carryover may be used to offset only \$25 of taxable income.
7. If L sold all of its assets in 1997, L's NOL carryover would be eliminated.

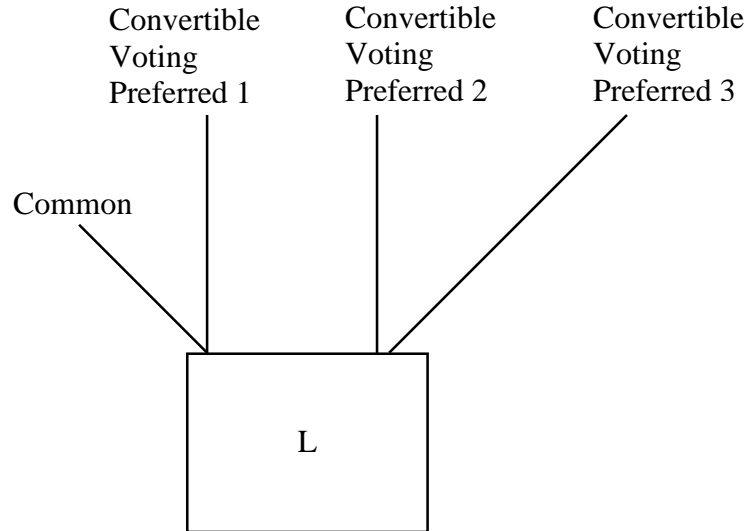
Stock (p. 56)

L, a solvent corporation organized in 1990, has the following classes of stock outstanding (each class of preferred stock would be described in section 1504(a)(4) but for the characteristics listed below):

<u>Common 1</u>	<u>Common 2</u>	<u>Preferred 1</u>	<u>Preferred 2</u>	<u>Preferred 3</u>	<u>Preferred 4</u>
Voting	Nonvoting	Voting	Voting Participating	Convertible	Voting Convertible

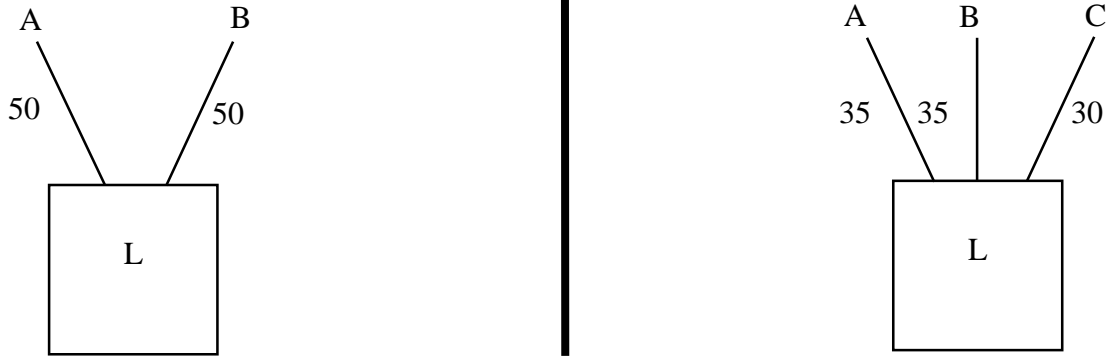
1. Common 1 and common 2 are both considered stock. However, there may be differences in the valuation of each due to the differences in voting privileges.
2. Preferred 1 comes under the statutory stock definition. However, it will probably be disregarded because it does not participate in the growth of the corporation.
3. Preferred 2 is stock.
4. Preferred 3 will not be considered stock, but an interest similar to an option. Notice 88-67. Under the option attribution rules, the option may be deemed exercised if it would cause an ownership change.
5. Preferred 4 would apparently be considered stock and not an option. Notice 88-67.
6. The value of all of the above classes of stock would be included in determining the section 382 limitation, notwithstanding the exclusion of section 1504(a)(4) stock in determining whether an ownership change has occurred.
7. For problems involving insolvent corporations, see the diagram on the following page.

Stock - Insolvent Corporation (p. 56)



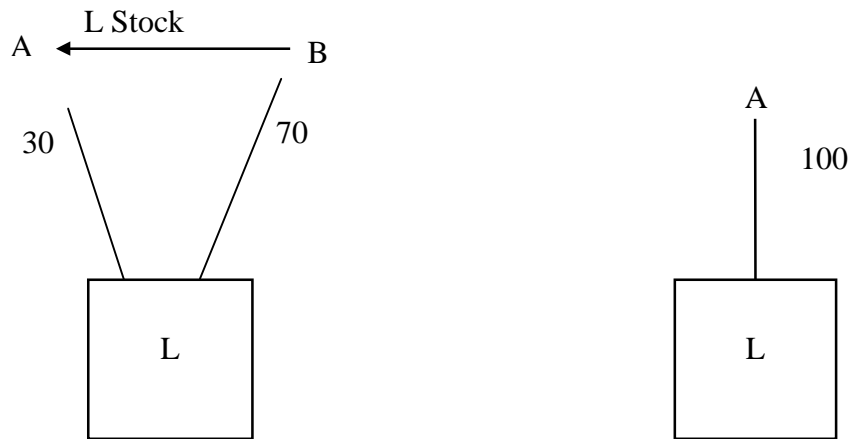
1. L has assets of \$10 million and liabilities of \$20 million. Preferred 3 has priority in liquidation over Preferred 2, which has priority over Preferred 1, which has priority over common.
2. The common and each class of preferred constitute stock under the statutory definition.
3. However, the creditors may be considered to own the company, to the extent they exercise control over corporate policy, under an expansive reading of the Alabama Asphaltic case.
4. Alternatively, Preferred 3 may be considered the only class of stock having value, since it has the best (albeit still remote) chance of participating in corporate growth, to the exclusion of the other classes, because of its priority in liquidation.
5. Fluctuation in value between classes of stock must also be considered. However, the treatment of such fluctuations in value is not clear.

Stock-Voting Trust (p. 56)



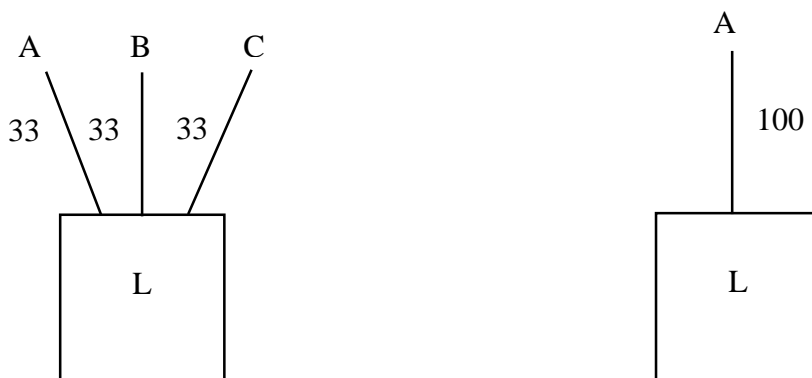
1. A and B have owned stock in L corporation equally for more than three years.
2. L issues 30 percent of its stock to C in exchange for a capital contribution. In addition, C requires that A and B place their shares in a voting trust with C as trustee.
3. No ownership change should result as C has only increased his percentage ownership by 30 points.
4. The voting trust should not be considered a separate class of stock owned by C since it does not participate in corporate growth.
5. A closer question is whether the value of the voting trust rights should be considered part of the value of C's stock. Absent unusual circumstances (voting trust perpetual or conveys with C's stock) the rights under the voting trust should be considered separate from the rights inherent in C's stock.

Ownership Change -- Taxable Purchase of Stock (p. 97)



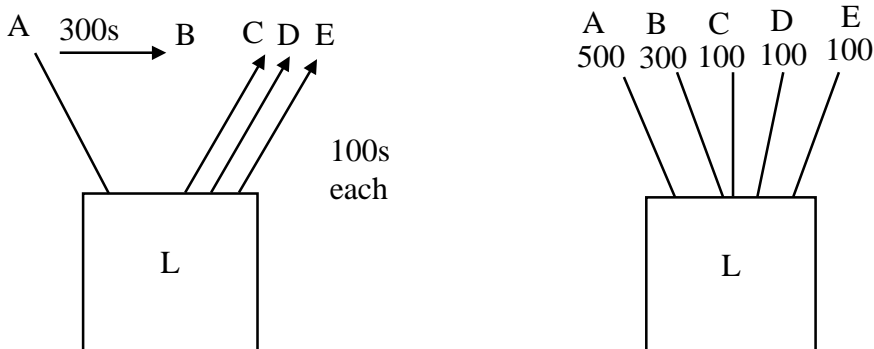
1. On January 1, 1996, L is owned 30 by A and 70 percent by B.
2. On July 1, 1996, A purchases all of B's stock for cash.
3. The testing period runs from May 6, 1995 to July 1, 1995.
4. A's acquisition is an owner shift involving a 5-percent shareholder.
5. An ownership change has occurred since A increased his holdings by more than 50 percentage points over his lowest percentage interest during the testing period.

Ownership Change -- Redemptions (p. 98)



1. L is equally owned by individuals A, B and C.
2. On July 1, 1996, L redeems B and C's stock for cash and notes.
3. The testing period runs from July 2, 1993 to July 1, 1996.
4. The redemption constitutes an owner shift involving a 5-percent shareholder.
5. The redemption results in an ownership change.

Ownership Change -- Multiple Owner Shifts (p. 99)



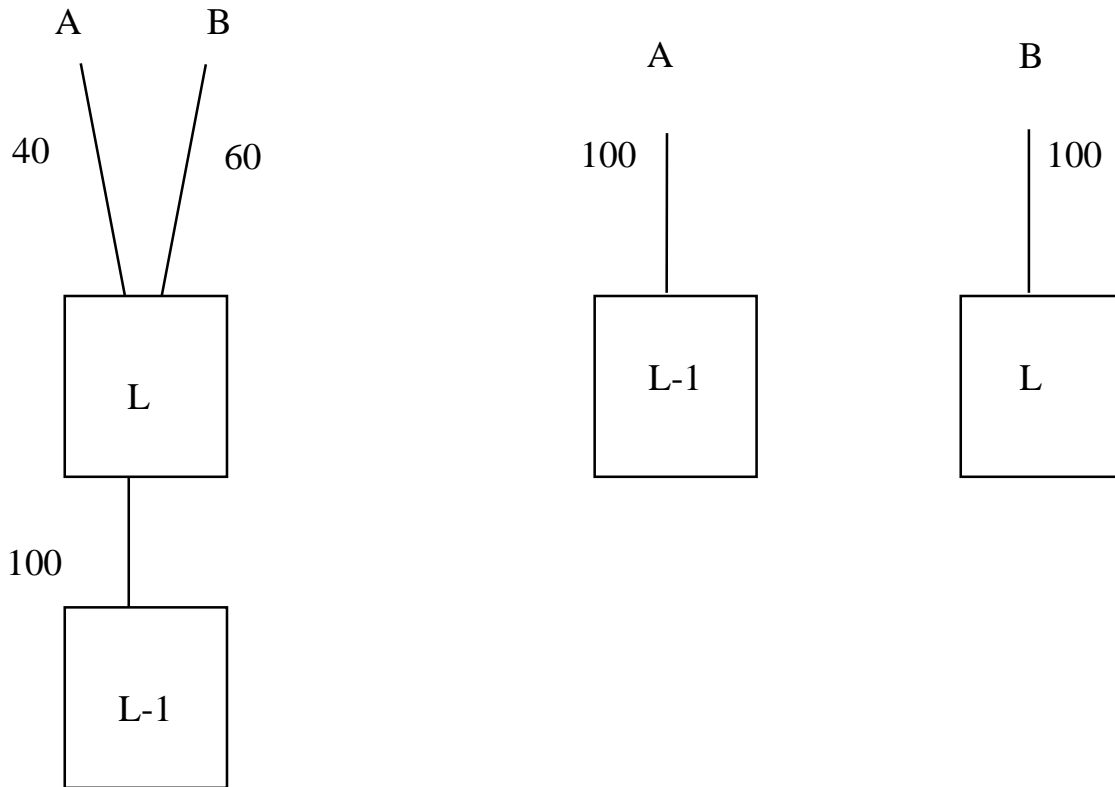
1. On January 1, 1995, A owns all 1000 shares of outstanding L stock.
2. On June 15, 1995, A sells 300 shares to B. This is an owner shift but not an ownership change.
3. On June 15, 1996, L issues 100 shares to each of C, D and E. This is also an owner shift but not an ownership change (see below).

	<u>Percentage After</u>	<u>Lowest Percentage Before</u>	<u>Increase</u>
A	54.0	70	0.0
B	23.0	0	23.0
C	7.7	0	7.7
D	7.7	0	7.7
E	7.7	0	<u>7.7</u>
			46.1

4. On December 15, 1996, L redeems 200 shares of stock held by A. This is both an owner shift and an ownership change (see below).

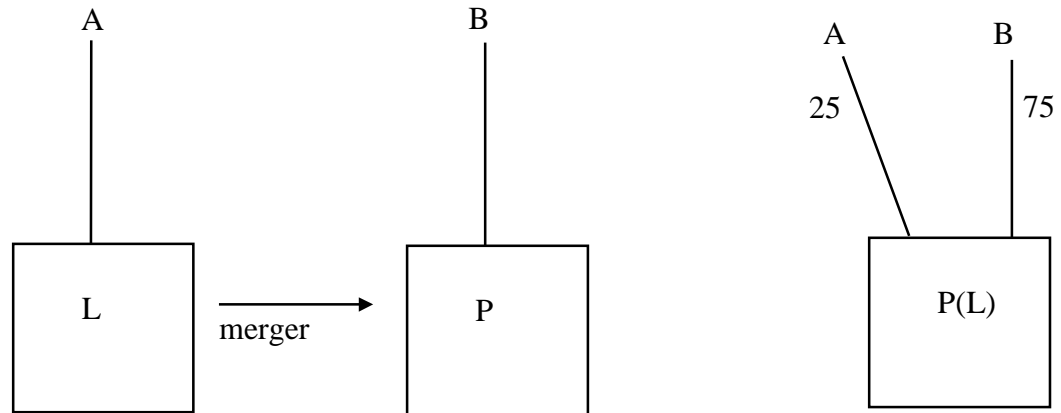
	<u>Percentage After</u>	<u>Lowest Percentage Before</u>	<u>Increase</u>
A	45	54	0
B	27	0	27
C	9	0	9
D	9	0	9
E	9	0	<u>9</u>
			54

Ownership Change -- Split-Off Transaction (p. 101)



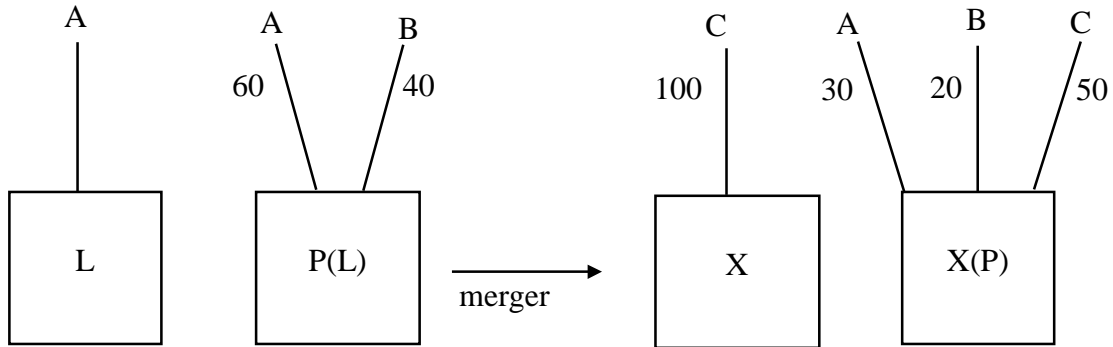
1. A and B own 40% and 60% of L, respectively.
2. L distributes all of the L-1 stock to A in exchange for all of A's L stock.
3. With respect to L-1, an ownership change occurred. Before the distribution, A owned 40% of L-1 through attribution, and after the distribution A actually owns 100 percent of L-1.
4. With respect to L, an ownership change does not occur. B owned 60 percent of L before the transaction, and 100 percent of L after the transaction.

Ownership Change -- Straight "A" Reorganization (p. 103)



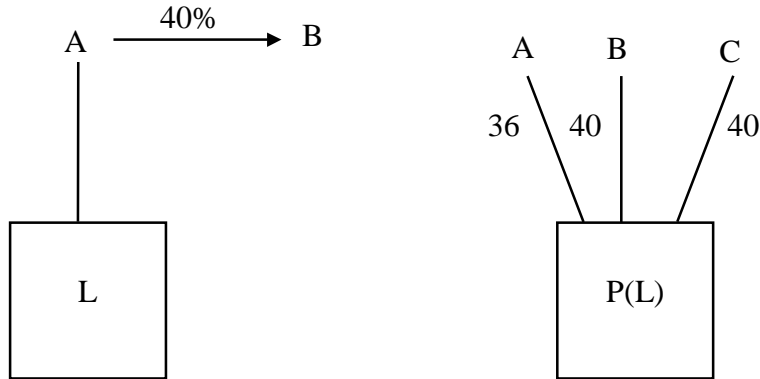
1. A owns all of the outstanding stock of L. B owns all of the outstanding stock of P.
2. L is merged into P, with P surviving. In the merger, A receives 25 percent of the stock of P.
3. The merger is an equity structure shift.
4. The merger results in an ownership change.

Ownership Change - Successive Equity Structure Shifts (p. 103)



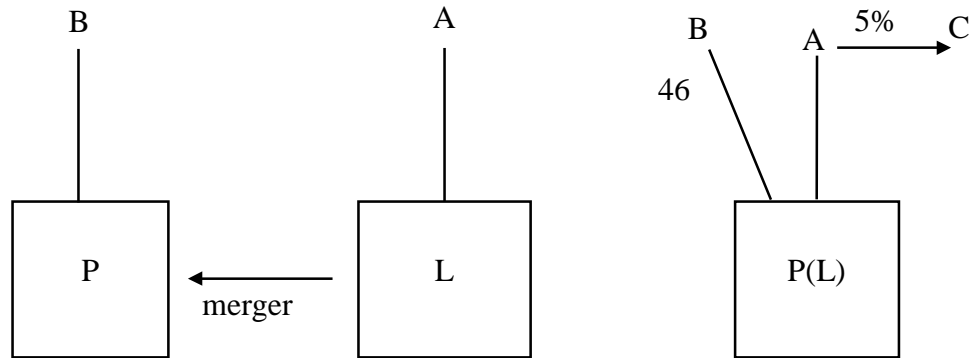
1. As of January 1, 1994, L is wholly-owned by A. P is wholly-owned by B.
2. On June 30, 1995, L is merged into P, with P surviving. A receives 60 percent of the P stock outstanding after the merger.
3. On June 30, 1996, P is merged into X. X is owned by C. The former P shareholders (A and B) receive 50 percent of the X stock outstanding after the merger.
4. The 1995 merger is an equity structure shift. However, no ownership change has occurred at this point. L is treated as continuing in existence.
5. The 1996 merger is also an equity structure shift. In addition, it constitutes an ownership change.
6. B and C's aggregate percentage interest in the new loss corporation X (70 percent) is more than 50 percentage points over their interest in the old loss corporation (L).

Ownership Change - Owner Shift Followed by a Merger (p. 105)



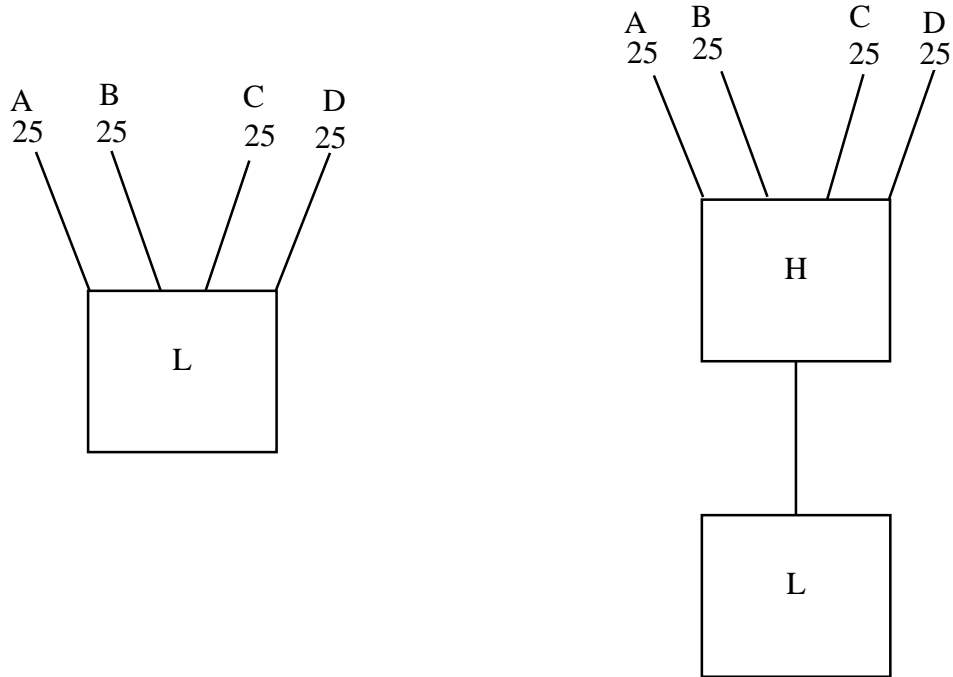
1. A owns all of the L stock.
2. On January 1, 1995, B purchases 40 percent of the L stock from A.
3. On July 1, 1995, L is merged into P with P surviving. In the merger, A and B receive 60% of the P stock.
4. Prior to the merger, C held 100% of P. C owns 40% of P after the merger.
5. B's purchase on January 1, 1995 is an owner shift but not an ownership change.
6. The merger is an equity structure shift, which, together with B's purchase, causes an ownership change. B and C's interest increased in the aggregate by 64 percentage points.

Ownership Change - Merger Followed by Owner Shift (p. 106)



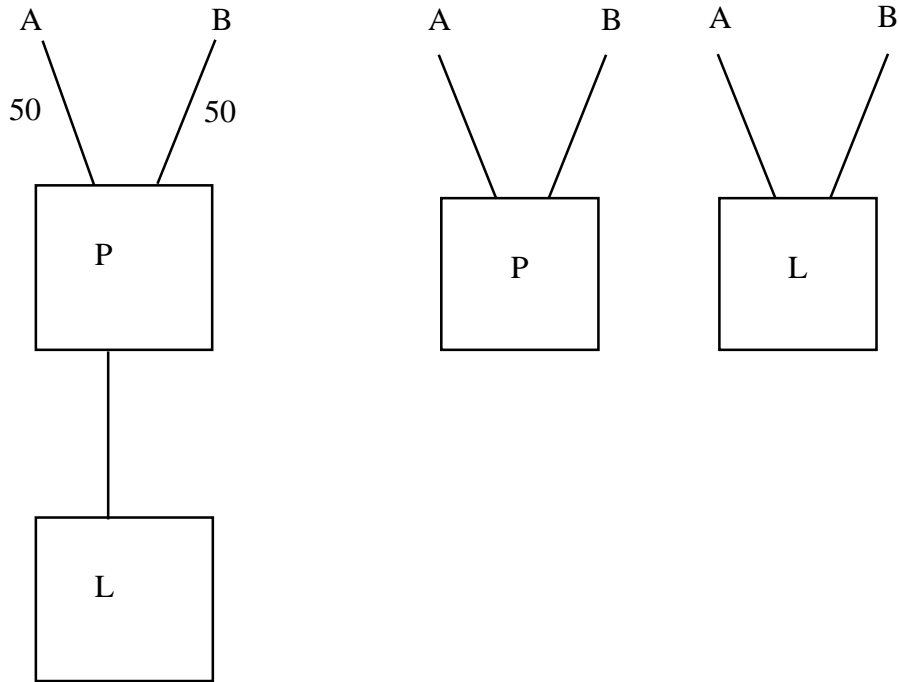
1. A owns all of the stock of L. B owns all of the stock of P.
2. On January 1, 1995, L is merged into P with P surviving. A receives 54% of the P stock outstanding after the merger.
3. On January 1, 1996, C purchases 5% of the P stock from A.
4. The merger is an equity structure shift but not an ownership change.
5. C's purchase is an owner shift, which results in an ownership change.
6. As a result of C's purchase, B and C have increased their holdings by more than 50 percent over their previous holdings in L.

Formation of Holding Company



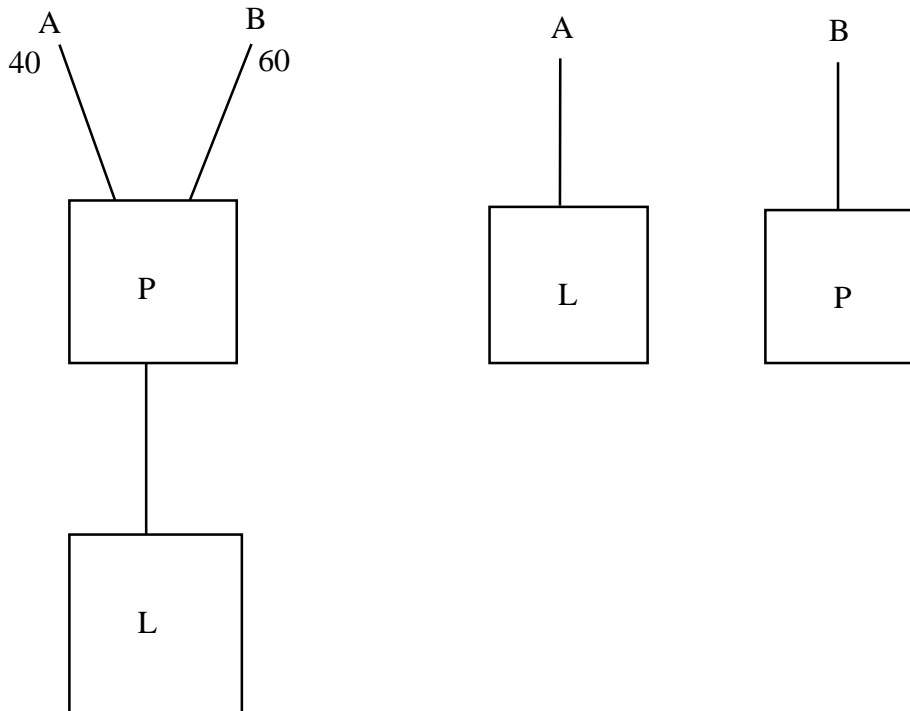
1. A, B, C, and D own all of the stock of L in equal proportions.
2. A, B, C, and D transfer their L stock to H in exchange for all of the H stock (25% each).
3. The L stock owned by H is considered to be owned by A, B, C, and D in proportion (by value) of their holdings in H. H's actual ownership of L stock is disregarded.
4. Viewed as a section 351 exchange, the formation of H is not an owner shift. A, B, C, and D's interest in L was not affected by the transaction.
5. Viewed as a "B" reorganization, the transaction constitutes an equity structure shift, but not an ownership change.

Constructive Ownership - Spin-Off Transaction



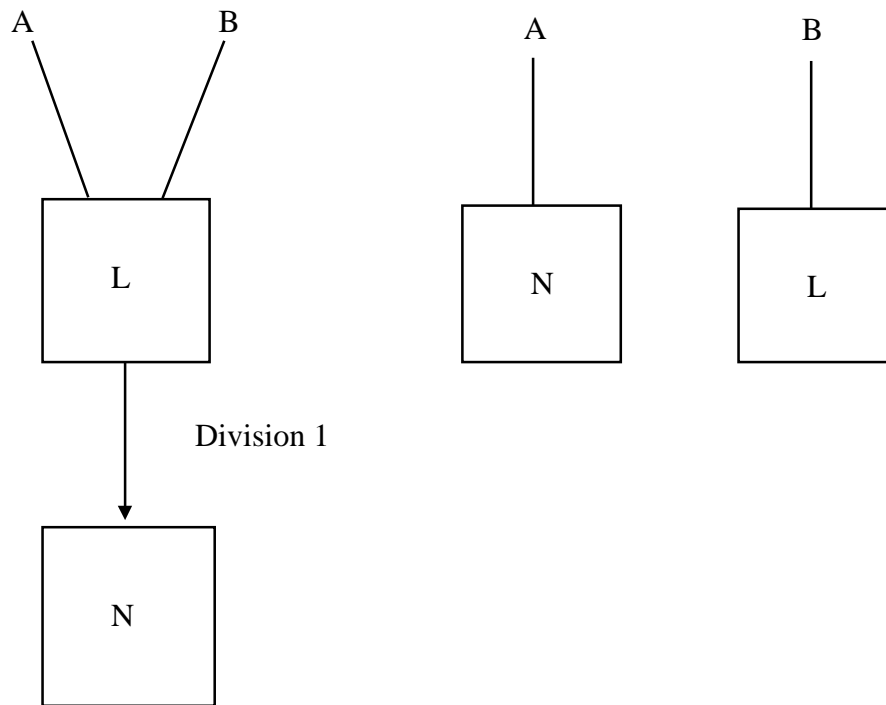
1. P is owned equally by individuals A and B. P owns all of the stock of L.
2. P distributes the L stock to A and B pro rate (i.e., a spin-off).
3. Prior to the transaction, A and B each held 50% of the L stock, constructively. P is not considered to own any L stock.
4. After the transaction, A and B each hold 50% of the L stock, actually.
5. For section 382 purposes, the transaction does not constitute an owner shift.

Constructive Ownership - Split-Off Transaction



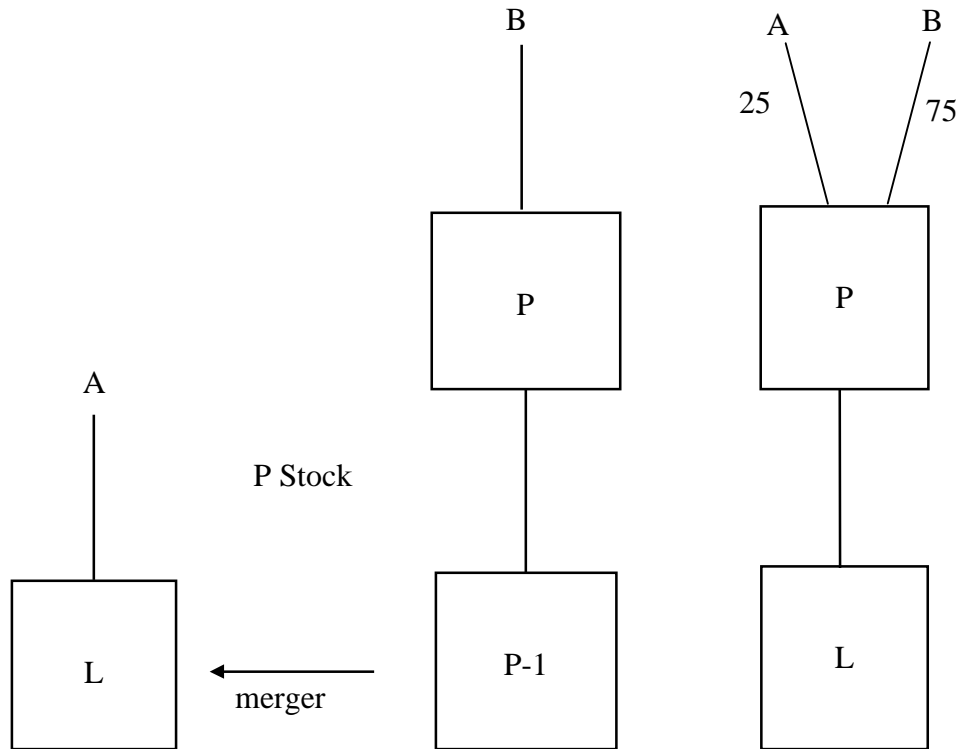
1. Individual A owns 40% of P; individual B owns 60% of P. P owns all of the stock of L.
2. P distributes all of the L stock solely to A in exchange for A's P stock (i.e., a split-off transaction).
3. Before the transaction, A held 40% and B held 60% of L, constructively. P is not considered as owning any L stock.
4. After the transaction, A owns 100% of L, actually.
5. As to L, the transaction results in an ownership change.
6. P is not a loss corporation; therefore, section 382 is irrelevant. Had P been a loss corporation, only a 40% owner shift would occur (B increased his interest from 60 percentage points to 100 points).

Constructive Ownership - D Reorganization



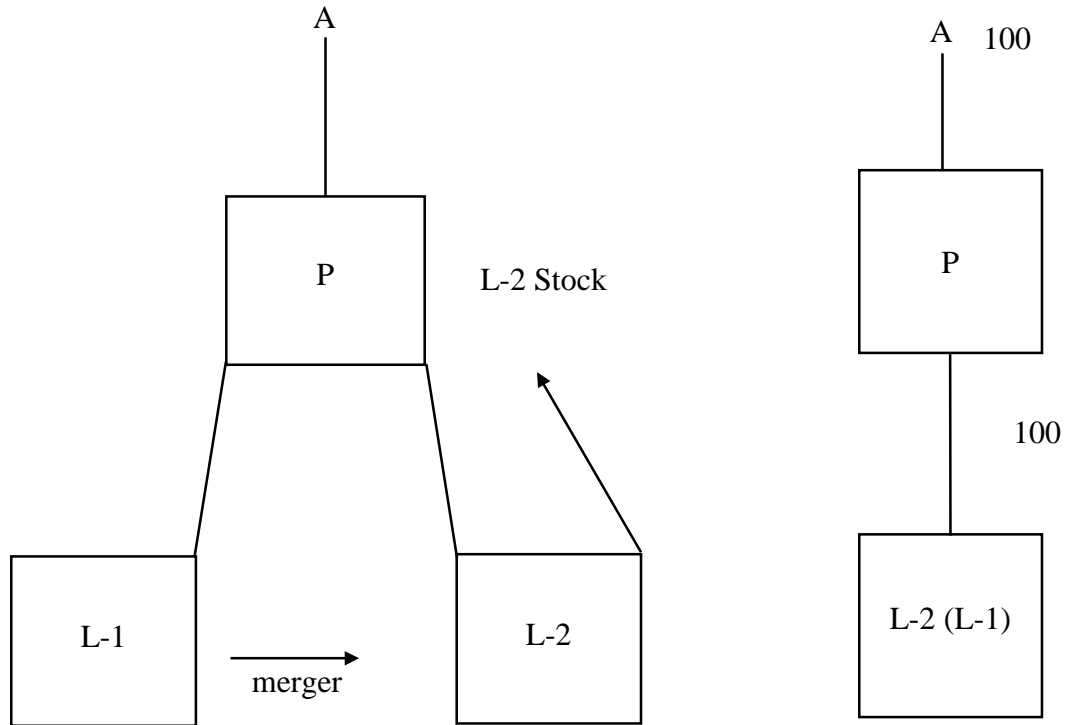
1. Individual A owns 40% of L. Individual B owns 60% of P. L operates two divisions.
2. L forms N and transfers one division to N in exchange for all of the N stock. L then distributes such N stock to A in exchange for all of A's L stock (i.e., a "D" reorganization).
3. The Service's position is that no loss carryovers are allocated to N. Thus, N is not a loss corporation, and section 382 is irrelevant.
4. As to L, B increased his interest from 60% to 100% as a result of the transaction. This increase of 40 points is not enough to trigger section 382.

Triangular "A" Reorganization



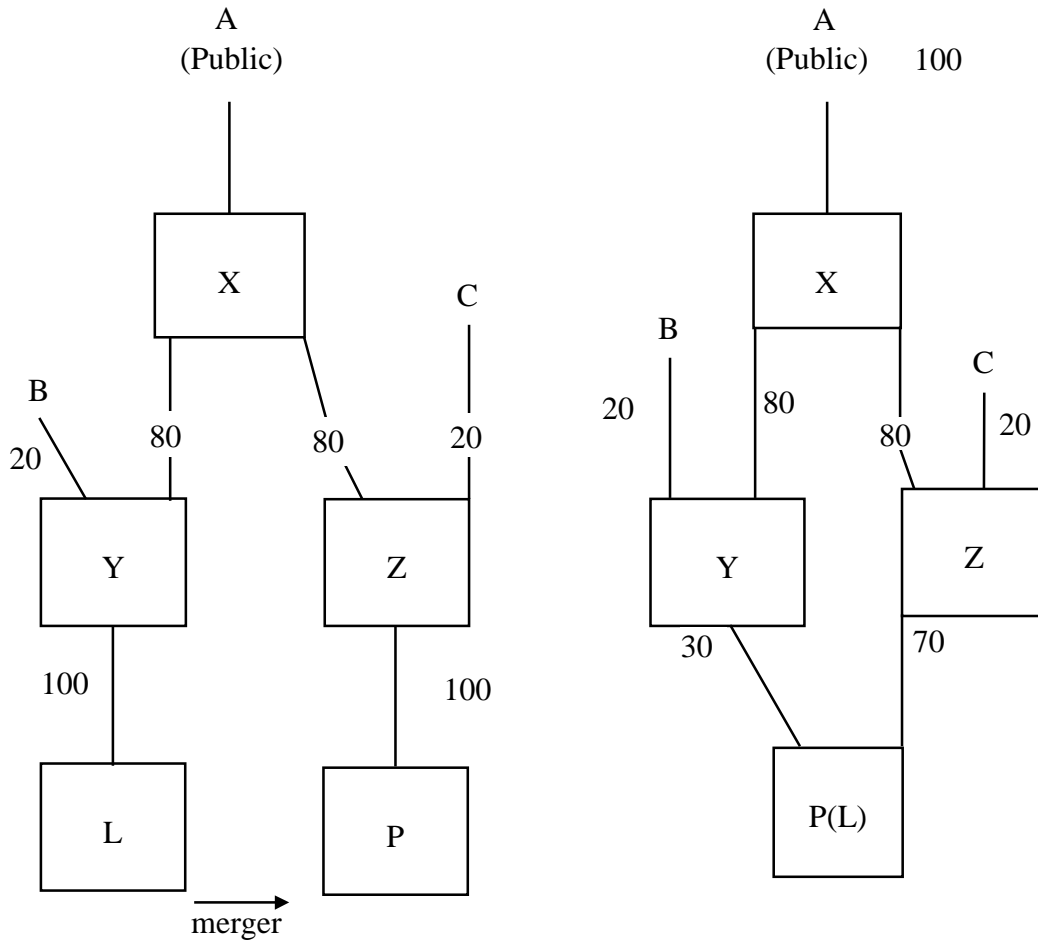
1. L is owned by A, and P is owned by B.
2. On January 1, 1995, P forms P-1. P-1 is merged into L, with L surviving. A receives P stock representing 25 percent of the P stock outstanding after the merger.
3. The merger of P-1 into L constitutes an equity structure shift.
4. Through attribution, A owns 25% of L, and B owns 75% of L. P's ownership of L stock is disregarded.
5. Thus, an ownership change has occurred.

Commonly Controlled Corporations (p. 121)



1. A owns all of the stock of P. P owns all of the stock of L-2 and L-2.
2. L-1 is merged into L-2, with L-2 surviving. P receives an additional 30% of the L-2 stock outstanding after the merger.
3. The merger of L-1 into L-2 is an equity structure shift.
4. Under the attribution rules, A owns 100% of the new loss corporation (L-2) and owned 100% of the old loss corporation (L-1).
5. No ownership change occurs.

Commonly Controlled Corporations (p. 122)



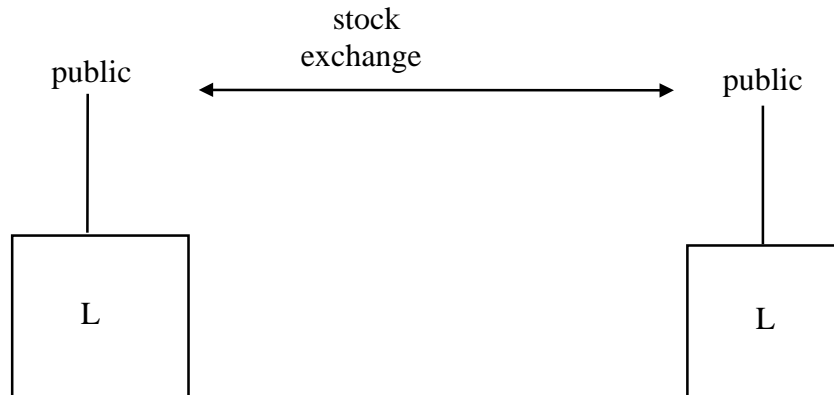
1. X is wholly-owned by A, a group of non-5-percent shareholders.
2. X owns 80% of the stock of Y and Z. The remaining 20 percent of Y and Z is held by B and C, respectively.
3. Y and Z own 100% of the stock of L and P, respectively.
4. On January 1, 1988, L is merged into P, with P surviving. Y receives 30% of the stock outstanding after the merger.
5. The merger of L into P is an equity structure shift, but not an ownership change.
6. Under the attribution rules, C is the only 5-percent shareholder to have increased its interest in the new loss

corporation (P) over its interest in the old loss
corporation (L) (14% increase).

Option Attribution (p. 124)

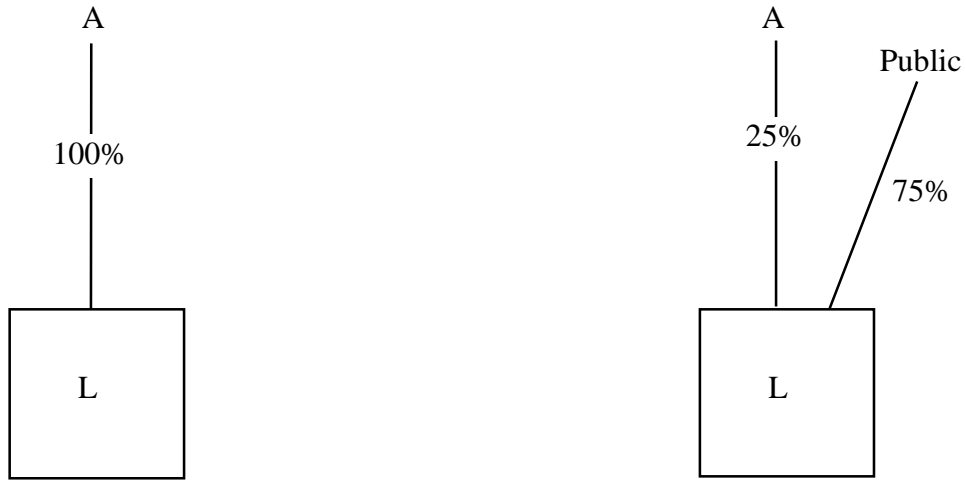
1. An option or interest similar to an option will be considered exercised if to do so would cause an ownership change. Treas. Reg. § 1.382-2T(h)(4).
2. In determining whether an option may be exercised, contingencies are disregarded. Treas. Reg. § 1.382-2T(h)(4)(iii).
3. If the option lapses or is forfeited, it is treated as if it had never been issued. Treas. Reg. § 1.382-2T(h)(4)(viii).
4. The following are considered options or interests similar to options:
 - a) warrants
 - b) convertible debt
 - c) convertible preferred stock (without other common equity rights, i.e., voting, participation - Notice 88-67)
 - (d) Put or call (including redemption privilege)
 - (e) Contract to acquire or sell stock
 - (f) Tender or exchange offers (at the time the offer cannot be withdrawn as a legal or practical matter)
 - (g) Right of first refusal
 - (h) Bankruptcy plans (on the Confirmation date). But see Treas. Reg. § 1.382-2T(h)(4)(x)(J)
 - (i) Buy-sell agreements
 - (j) Pledge
5. A non-binding letter of intent is not an option. Approval of a definitive written agreement by both corporations' Board of Directors creates an interest similar to an option.
6. The regulations provide a number of limited exceptions to the option attribution rules. See Treas. Reg. § 1.382-2T(h)(4)(x).

Ownership Change - Public Trading of L Stock



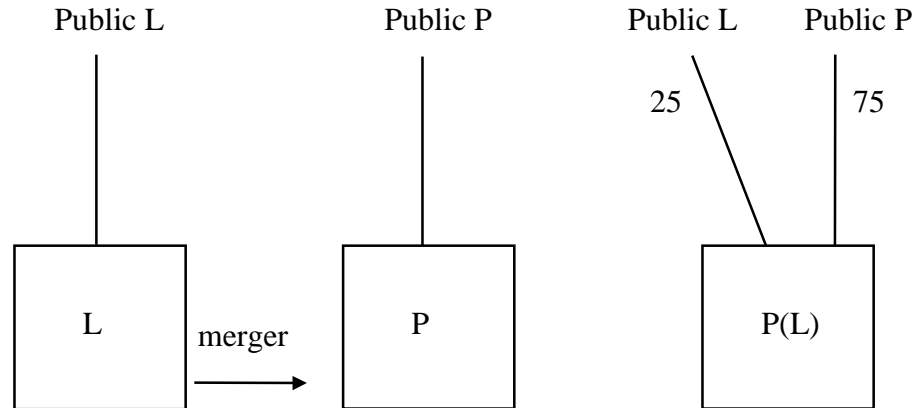
1. As of January 1, 1994, L is publicly held.
2. During the 3-year period ending on December 31, 1996, L's stock ownership undergoes a complete turnover through public trading.
3. No shareholder became a 5-percent shareholder during the testing period.
4. No owner shift has occurred. The 5-percent shareholder (non-5-percent shareholders aggregated) held 100% of the P stock throughout the testing period.

Aggregation Rules - Initial Public Offering



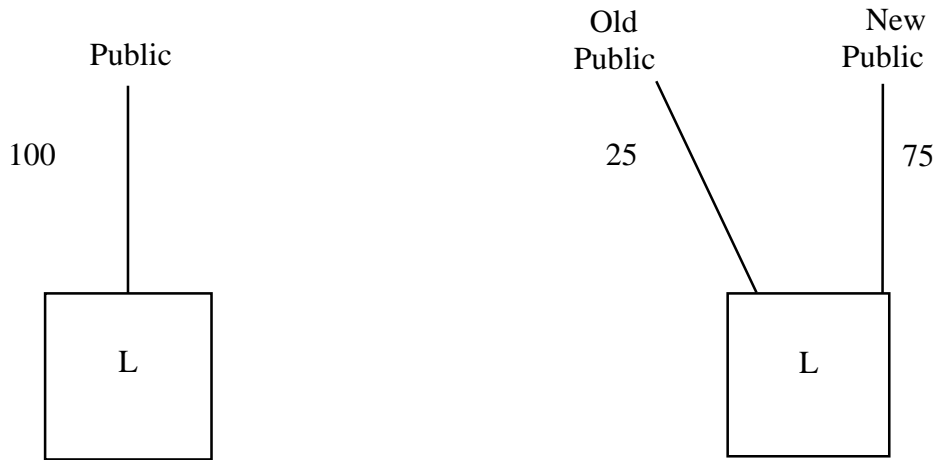
1. As of January 1, 1995, L is wholly-owned by individual A.
2. A has held the L stock throughout the previous three years.
3. L issues new stock to the public constituting 75% of L's outstanding stock.
4. The public shareholders are aggregated and treated as one shareholder.
5. The public offering results in an ownership change.

Ownership Change - Merger of Publicly-Held Corporations



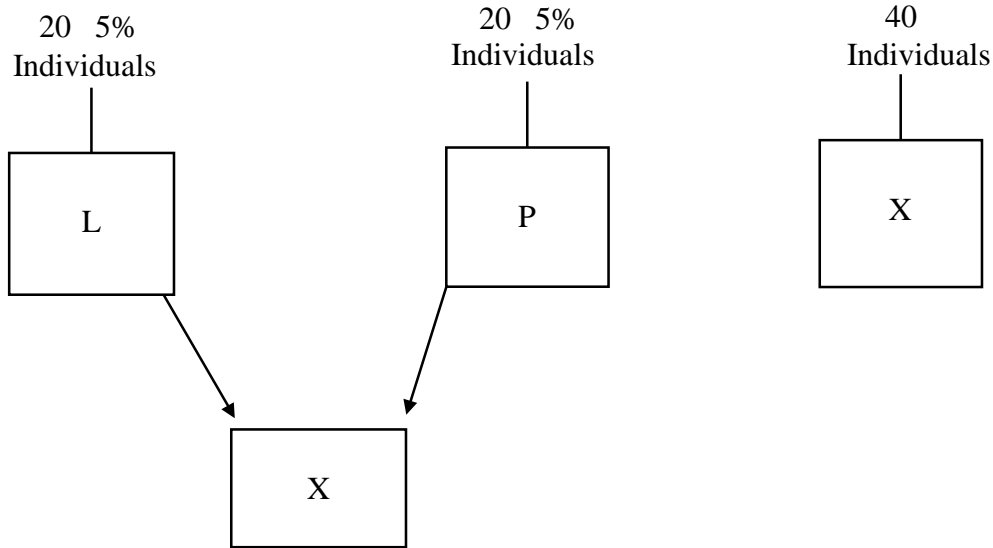
1. All of the L stock is owned by Public L (a group of non-5-percent shareholders). All of the P stock is owned by Public P (a group of non-5-percent shareholders.).
2. L is merged into P, with P surviving.
3. In the merger, Public L receives solely voting stock of P representing 25% of the P stock outstanding after the merger. No shareholder becomes a 5-percent shareholder.
4. The merger of L into P constitutes an equity structure shift.
5. In addition, the merger constitutes an ownership change.

Ownership Change - Additional Issuance of Stock
to the Public



1. On January 1, 1995, L is a publicly-held corporation. No shareholder of L is a 5-percent shareholder.
2. On June 30, 1995, L issues new stock to the public constituting 75% of L's outstanding stock. None of the new shareholders is a 5-percent shareholder.
3. If all of the non-5-percent shareholders are aggregated as one shareholder, no ownership change will occur. The aggregated shareholders would own 100% of L before and after the offering.
4. However, if the non-5-percent shareholders are segregated into two groups (Old Public and New Public), an ownership change would occur.

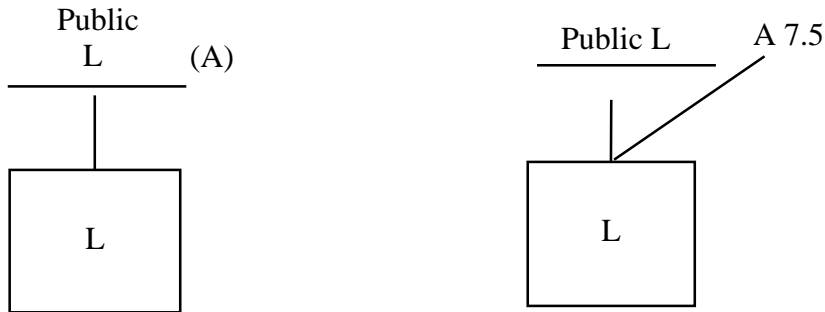
Operation of the 5-Percent Shareholder Rules –
Predecessor Corporations



1. L and P are owned by 20 individual shareholders (no overlapping), each owning 5% of the stock of the respective corporation.
2. L and P have equal value. The two corporations are consolidated into X. As a result, each shareholder holds 2-1/2% of the corporation.
3. There is no 5-percent shareholder of X. Neither section 382(k)(7) nor (g)(1) permits 5-percent shareholder status to be determined by looking to ownership in X's predecessors, L and P.
 - a. Thus, all the shareholders of X are aggregated as one 5-percent shareholder.
 - b. Technically, an ownership change occurs because the aggregated shareholder did not own any stock in L.
4. However, TCB 88 would add section 382(1)(8) to treat predecessor and successor entities as one entity.
 - a. Thus, the successor corporation, X, would be treated as the same corporation as P, and the same corporation as L.

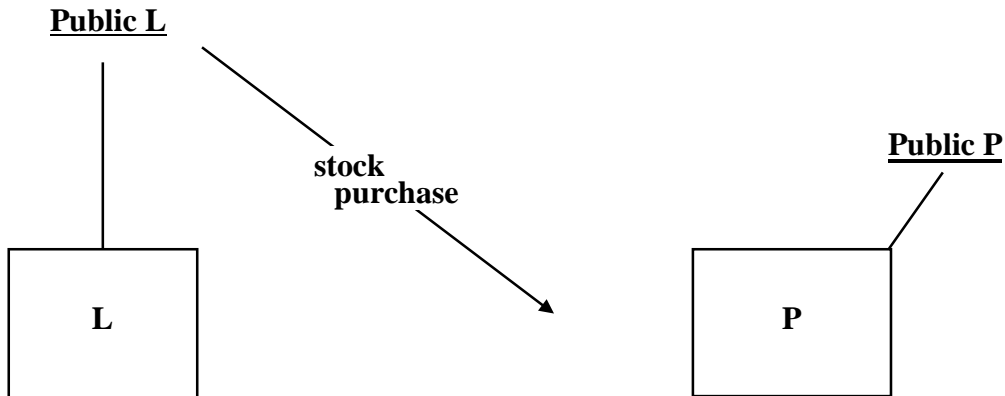
- b. Thus, the 20 shareholders of each corporation should remain as 5-percent shareholders because they held a 5% interest in either P or L, which is treated the same as X.
- c. Thus, the shareholders of X would not be aggregated.

5-Percent Shareholder Rules - Presumptions of Ownership (p. 193)



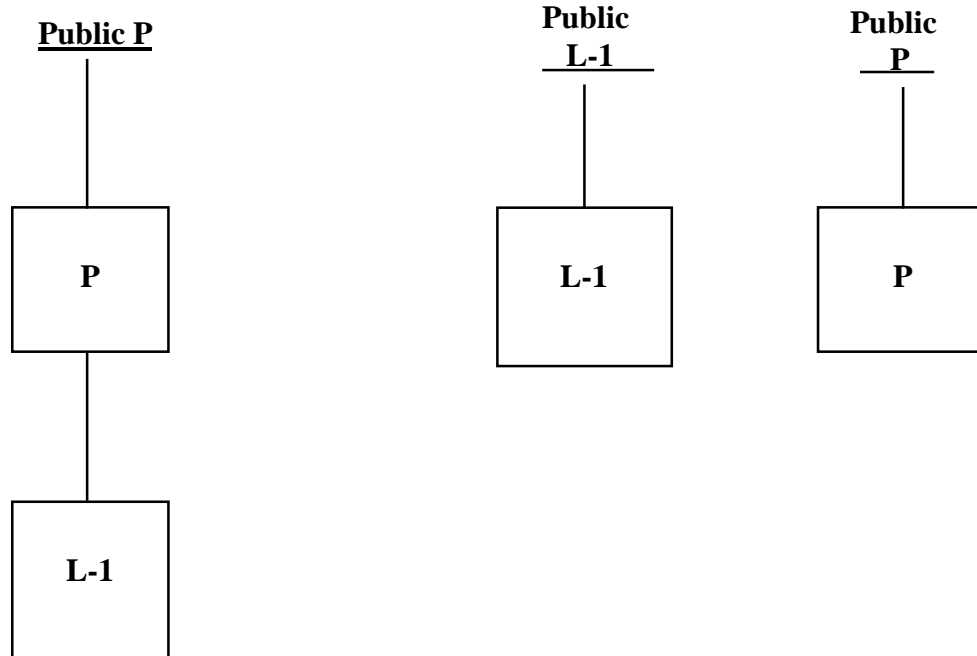
1. L is owned equally by 40 unrelated individuals, including A, who owns 2.5% of L.
2. On June 1, 1996, A acquires an additional 5%. As a result, A becomes a 5-percent shareholder of L.
3. A's actual increase in percentage ownership is 5% (7.5% from 2.5%).
4. However, L may presume that A's interest was 0 throughout the testing period, and that Public L owned 100% of L.
5. Under this presumption, A would be deemed to have increased his percentage interest by 7.5 points.

Takeover by Publicly-Held Corporation (p. 201)



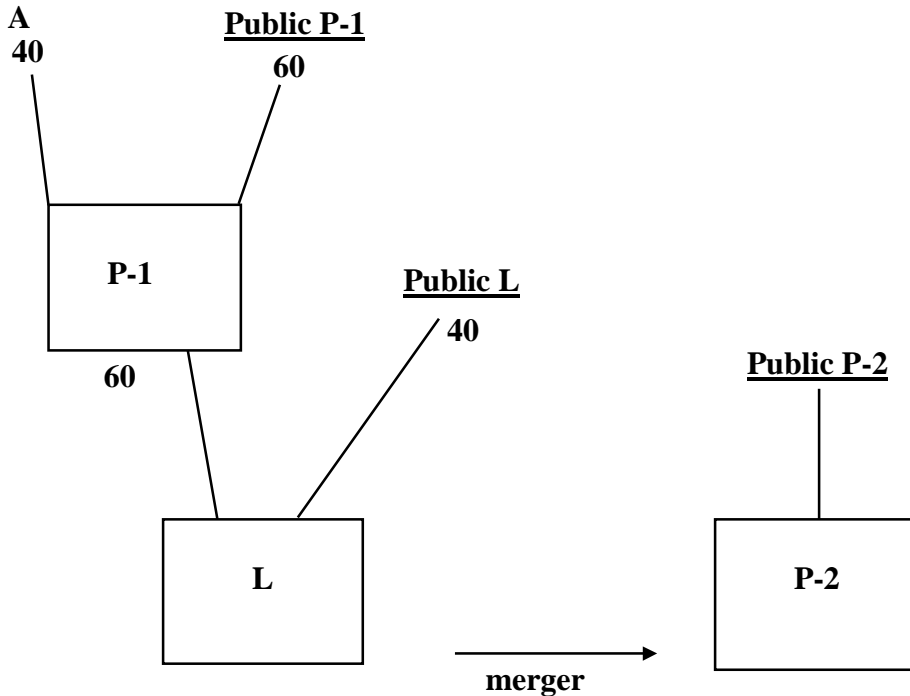
1. L is owned by Public L, a group of 1,000 non-5-percent shareholders.
2. P is owned by Public P, a group of 150,000 non-5-percent shareholders.
3. Between July 12 and August 13, 1988, P acquires all of the L stock. P first acquired 5% of L on July 15, 1988, and 51 percent of L on July 30, 1988.
4. Before July 15, 1988, P was a public shareholder of L -- P was aggregated with the other L shareholders as a member of Public L. No stock of L was attributed to Public P.
5. On July 15, 1988, P first acquired a 5% interest in L, and at that time, became a first tier entity.
 - a. Under the constructive ownership rules, L stock held by P is attributed to Public P.
 - b. Under the aggregation rules, Public P is treated as a public group which is a 5-percent shareholder of L.
 - c. Each acquisition of L stock by P on or after July 15, 1988, constitutes an owner shift.
6. On July 30, 1988, when P first acquired a more than 50% interest in L, an ownership change occurs.

Spin-off Transaction (p. 203)



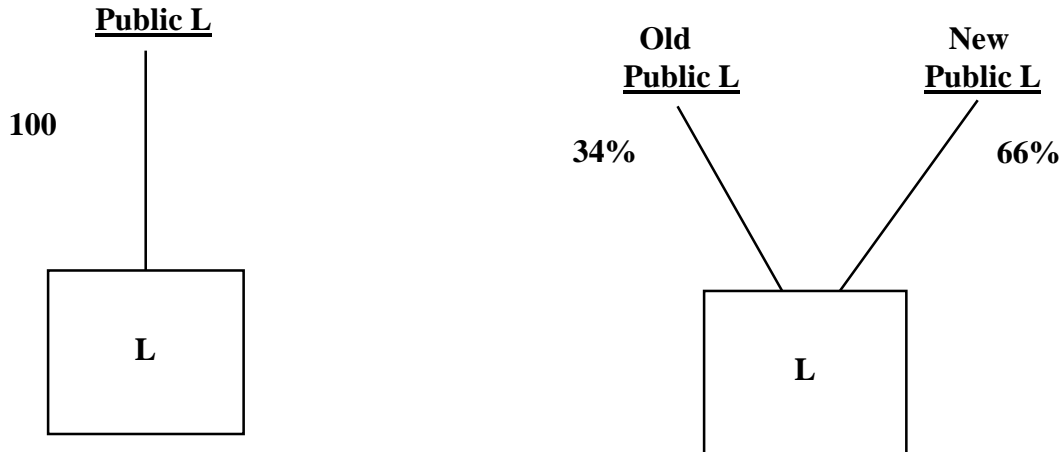
1. P is owned by 1,000 unrelated shareholders, none of whom are 5-percent shareholders. P owns all of the stock of L1.
2. On January 2, 1988, P distributes all of the L-1 stock to its shareholders on a pro rata basis.
3. Prior to the distribution, the shareholders of P are aggregated and treated as one 5-percent shareholder that owned, constructively, all of the L-1 stock (Public P).
4. Following the distribution, L-1 is actually owned by 1,000 shareholders, none of whom are 5-percent shareholders.
5. Public L-1 and Public P are treated as unrelated individual shareholders, Public P and Public L-1 are presumed not to have any common members. Under this presumption, an ownership change would occur.
6. However, this presumption does not apply because L-1 has actual knowledge that the shareholders were identical. Thus, the distribution does not constitute an owner shift.

Segregation Rules -- Section 381(a)(2) Equity
Structure Shift (p. 207)



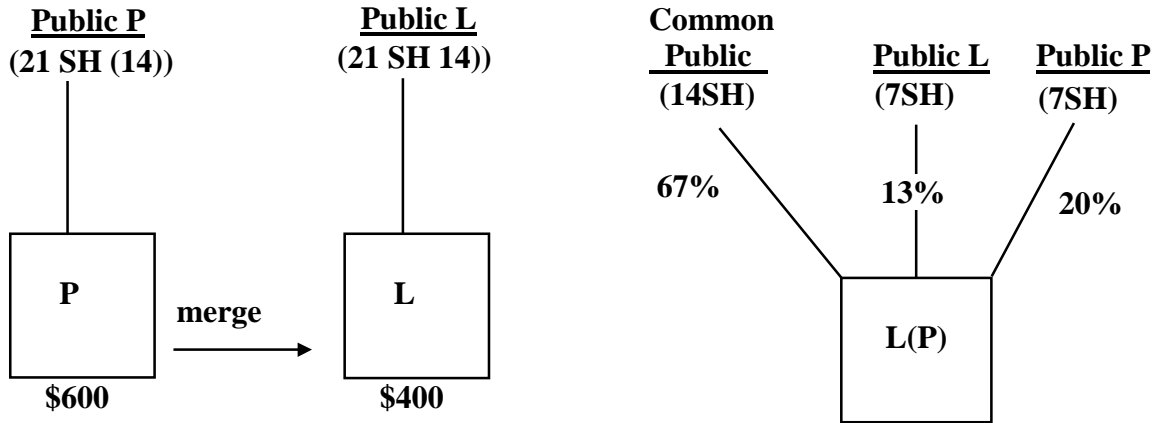
1. L is owned 60% by P-1 and 40% by Public L, a group of public shareholders. P-1 is owned 45% by individual A and 60% by Public P-1, a group of public owners.
2. P-2 is a publicly traded corporation, owned by Public P-2.
3. On May 22, 1988, L merges into P-2, with P-2 surviving. The L shareholders received 70% of the P-2 stock outstanding after the merger.
4. Before the merger, L's 5-percent shareholders were Public L (40%), Public P-1 (36%) and A (24%).
5. As a result of the merger, Public P-2 is deemed to acquire L stock.
6. The merger constitutes a segregation transaction -- Public L must be segregated from Public P-2. Public P-1 is aggregated separately from Public L and Public P-2.
7. Since Public P-2 increased its interest in the loss corporation by only 30 points, an ownership change does not occur.

Segregation Rules -- Additional Issuance Of Stock
to the Public (p. 209)



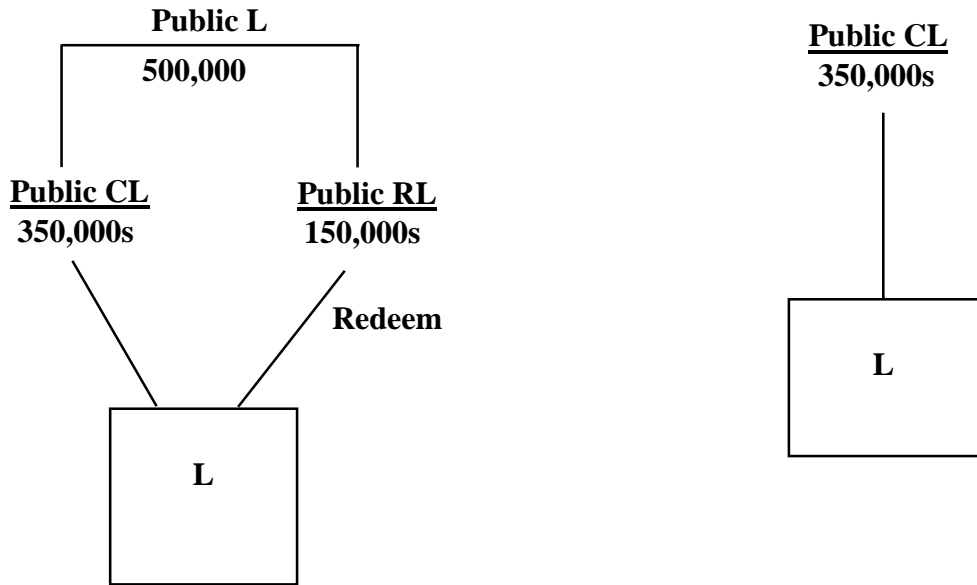
1. On January 1, 1988, L is owned by Public L. No shareholder of L is a 5-percent shareholder. L has 100,000 shares outstanding.
2. On January 22, 1988 L issues 200,000 shares of new stock to the public. None of the new shareholders is a 5-percent shareholder.
3. If all of the non-5-percent shareholders are aggregated as one shareholder, no ownership change will occur.
4. However, the transaction is a segregation transaction (a section 1032 transaction).
5. Public L, a direct public group, must be segregated from New Public L, the direct public group that acquired L stock.
6. New Public L has increased its interest by more than 50 points.
7. An ownership change thus occurs.

Segregation Rules -- Overlapping Ownership (p. 210)



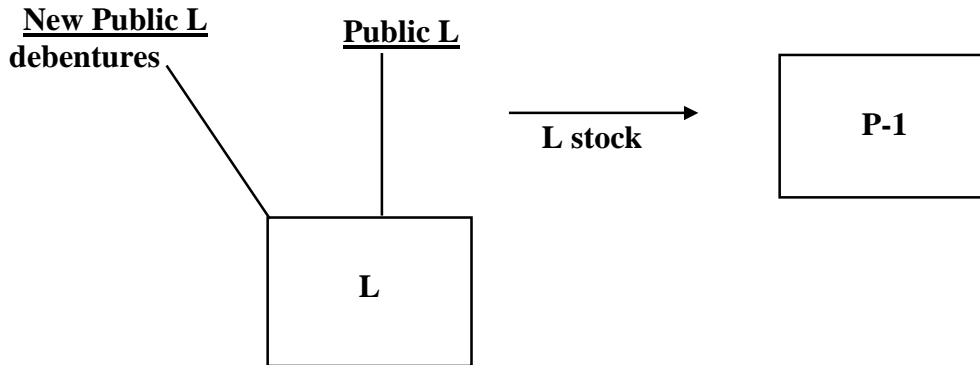
1. P and L corporations are each owned by 21 equal shareholders.
2. Of these shareholders, 14 are owners in both P and L. L has actual knowledge of this cross ownership.
3. P merges into L on June 10, 1988.
4. Under the usual segregation rules, Public P would be segregated from Public L. Thus, an ownership change would result (Public P would own 60% of L).
5. However, a third public group, Common Public (composed of the common owners), may be created to keep track of the interests of common owners in L.
6. In this case, an ownership change would not occur. The new 5-percent shareholders with respect to the loss corporation, (Public P (exclusive of the common owners)) has only increased its interest by 20 points.

Segregation Rules -- Redemption (p. 212)



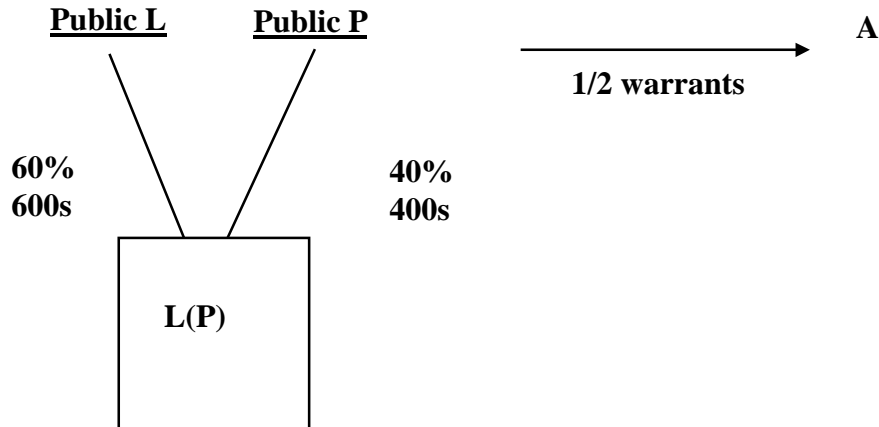
1. L has 500,000 shares of stock outstanding. L is considered to be owned by Public L, a public group composed of public shareholders.
2. On July 12, 1988, L acquires 150,000 shares of its stock for cash.
3. The redemption transaction is a segregation transaction. Public L must be segregated into two groups immediately before the merger -- Public CL and Public RL.
4. Immediately before the transaction, Public CL owned 70% and Public RL owned 30% of L.
5. Immediately after the close of the July 12, 1988 testing date, Public CL has increased its percentage interest by 30 points -- not enough for an ownership change.

Segregation Rules -- Stock Rights
Issued by the Loss Corporation (p. 215)



1. L has 700,000 shares outstanding, all of which are owned by Public L, a group of public shareholders.
2. On May 20, 1988, L issues a class of debentures to the public that may be converted into 300,000 additional shares of stock.
3. On September 7, 1988, P-1 acquires 210,000 shares of L stock over a public stock exchange. None of the L debentures have been converted,
4. As a result of L's issuance of convertible debentures, May 20, 1988 is a testing date. The deemed issuance of stock pursuant to the debentures is also a segregation transaction -- Public L must be segregated from New Public L.
 - a. The deemed exercise of debentures would result in total outstanding L stock of 1,000,000 shares, of which New Public L would own 300,000 shares.
 - b. This shift of 30% is not enough to trigger an ownership change, so the debentures are not deemed to be exercised.
5. Due to P-1's acquisition of common stock, September 7, 1988 is a testing date.
 - a. Public L is again segregated from New Public L.
 - b. P-1's acquisition results on a 21% owner shift, and combined with New Public L's increase of 30%, an ownership change occurs.

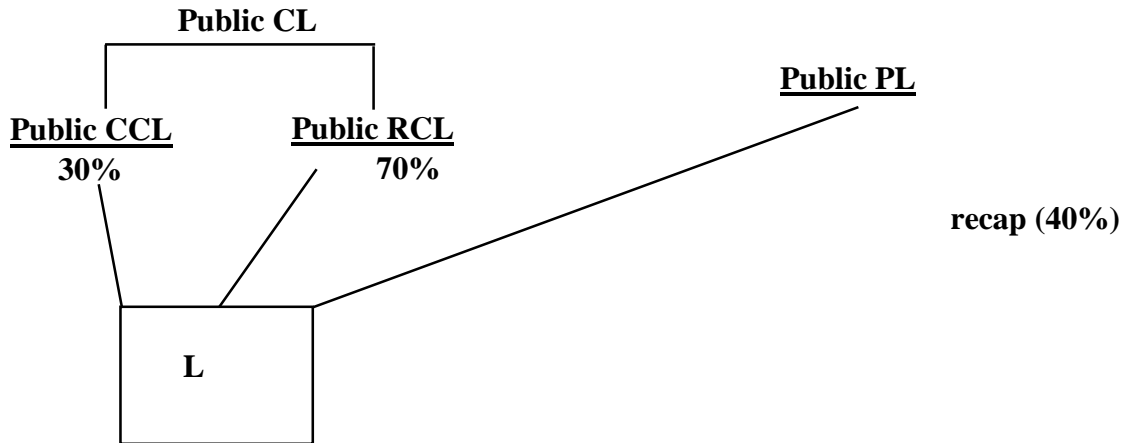
Segregation Rules -- Issuance Of Rights
to Multiple Public Groups



1. L is owned entirely by Public L. P is owned entirely by Public P. On November 30, 1995, P is merged into L, with Public P receiving 40% of the L stock outstanding after the merger. At that time, L has 1,000 shares outstanding.
2. Pursuant to the reorganization, L issues warrants to Public L and Public P, pro rata, that entitle the holders to an additional 200 shares in the aggregate.
3. On November 30, 1996, when only half of the outstanding warrants have been exercised, A acquires all of the unexercised warrants.
4. Without regard to the warrants, the November 30, 1995 merger results in a 40% owner shift (Public P's new interest in L).
 - a. The issuance of warrants does not require the creation of a third public group because L has actual knowledge that Public L and Public P acquired the warrants pro rata.
 - b. However, the largest increase occurs on November 30, 1995 if only Public P is treated as acquiring warrants.
 - c. In this case, Public P is deemed to own 44.4% of L ((400 shares acquired in the merger + 80 shares deemed exercised) / 1,080 deemed outstanding)).

5. The actual exercise of warrants is deemed to occur pro rata between Public L and Public P. Thus, Public P is deemed to own 40% of L $((400 + 40)/1100$ (actual shares outstanding)).
6. A's acquisition of the outstanding warrants on November 30, 1996 is a testing event. Since A would own 8-1/3%, A would be a 5-percent shareholder $((100$ shares deemed acquired) $/1200$ (actual and deemed shares outstanding)).
7. However, A is not treated as acquiring the stock because an ownership change would not occur, Public P's interest is only 36-2/3%. The increase for Public P and A is less than 50 points (i.e. , only 45 points).

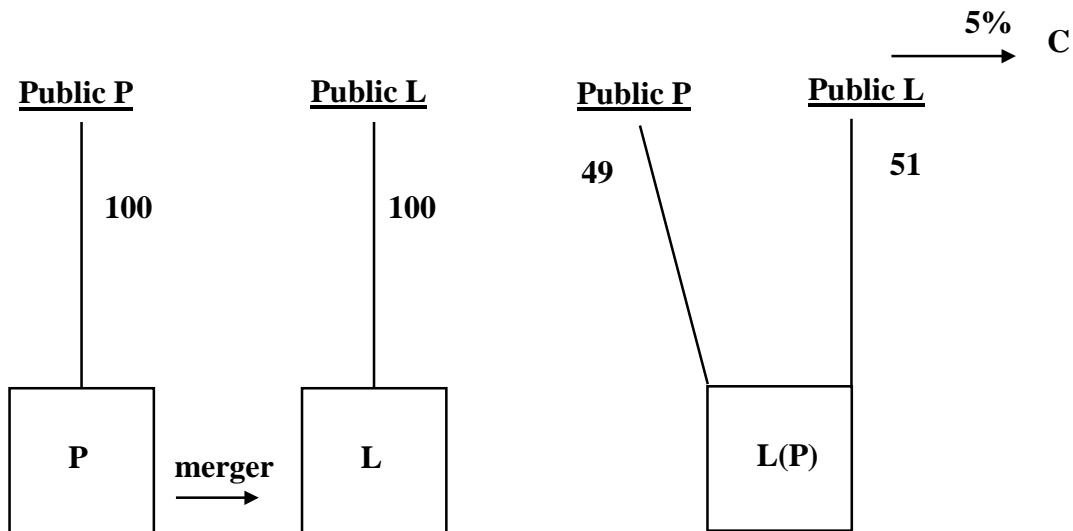
Segregation Rules -- Multiple Transactions (p. 221)



1. All of the common stock of L is owned by Public CL, a group of public shareholders,
2. All of the preferred stock is owned equally by 500 unrelated persons, Public PL. The preferred stock is section 1504(a)(4) stock.
3. On September 4, 1988, L redeems 70% of the common stock, L also exchanges nonvoting common stock for Public PL's preferred stock. The new class represents 40% of the value of L.
4. As to the redemption, Public CL is segregated into Public CCL and Public RCL immediately before the redemption.
 - a. All transactions on a single testing date are treated as occurring simultaneously, and each shareholder's interest is measured immediately after the close of the testing date.
 - b. Thus, Public CCL's percentage interest increases 30 points (from 30% to 60%, taking into account the recapitalization of preferred stock).
5. The recapitalization is a segregation transaction. Therefore, Public PL is segregated from the other direct public groups of L. As a group, Public PL increases its percentage interest by 40 points.

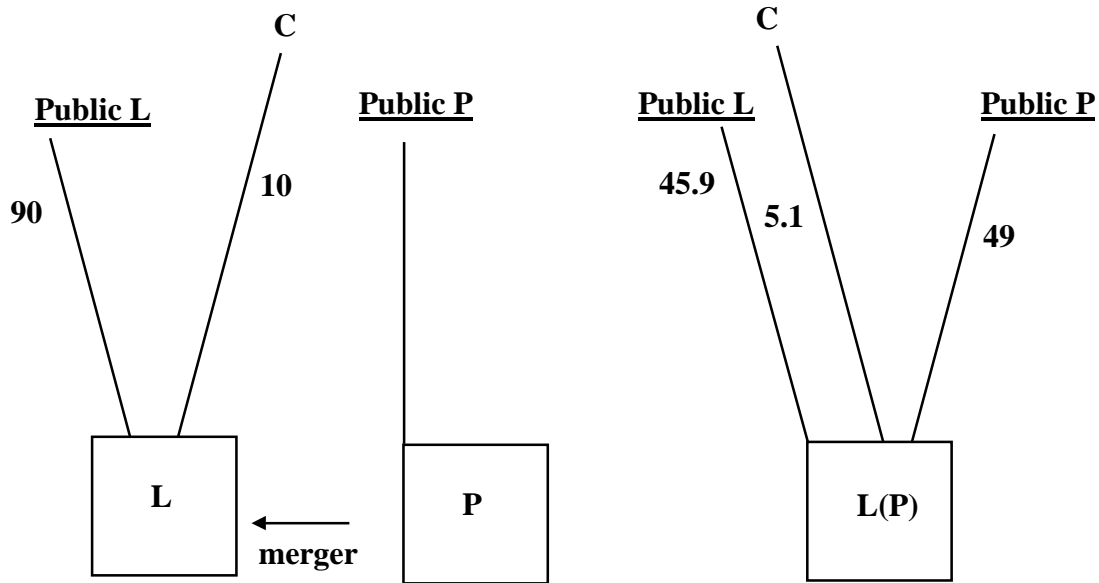
Thus, an ownership change occurs as a result of both transactions.

Ownership Change -- Equity Structure Shift
Followed by a Purchase



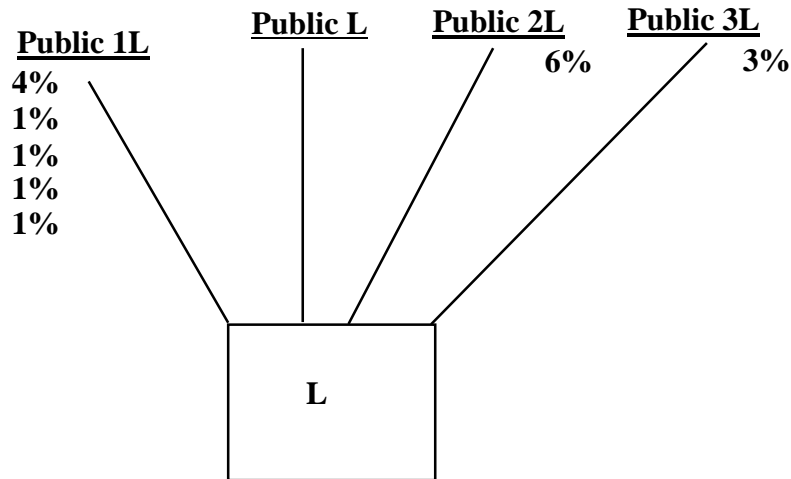
1. L is wholly-owned by Public L, a group of public shareholders. P is wholly-owned by Public P (a group of non-5-percent shareholders).
2. On January 1, 1996, P merges into L, with L surviving. In the merger, Public P receives 49% of the L stock outstanding after the merger.
3. On July 1, 1996, C acquires 5% of the L stock in the open market.
4. The merger of P into L is an equity structure shift, but not an ownership change. Public L and Public P are segregated and treated as separate 5-percent shareholders.
5. C's purchase is an owner shift. Unless C can show otherwise, C is deemed to have purchased stock ratably from Public L and Public P.
6. C's purchase results in an ownership change.

Ownership Change -- Purchase Followed by
Equity Structure Shift



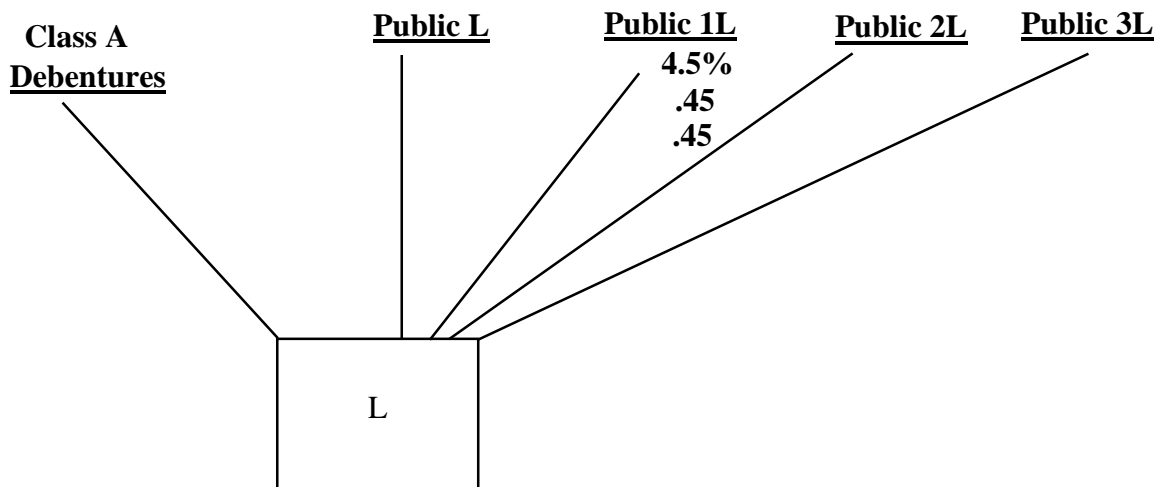
1. On January 1, 1996, C Purchases 10 percent of the L stock.
2. On July 1, 1996, P is merged into L, a corporation wholly-owned by Public P (a group of non-5-percent shareholders). In the merger, Public P receives 49 percent of the L stock outstanding after the merger.
3. C's purchase is an owner shift, but not an ownership change.
4. The merger constitutes an equity structure shift and an ownership change.
5. Public P and C's interest in the new loss corporation (L) has increased by more than 50 percentage points over their lowest percentage interest in the old loss corporation (L) (0% to 54.1%).

Segregation Rules -- Combination of De Minimis Groups (p. 225)



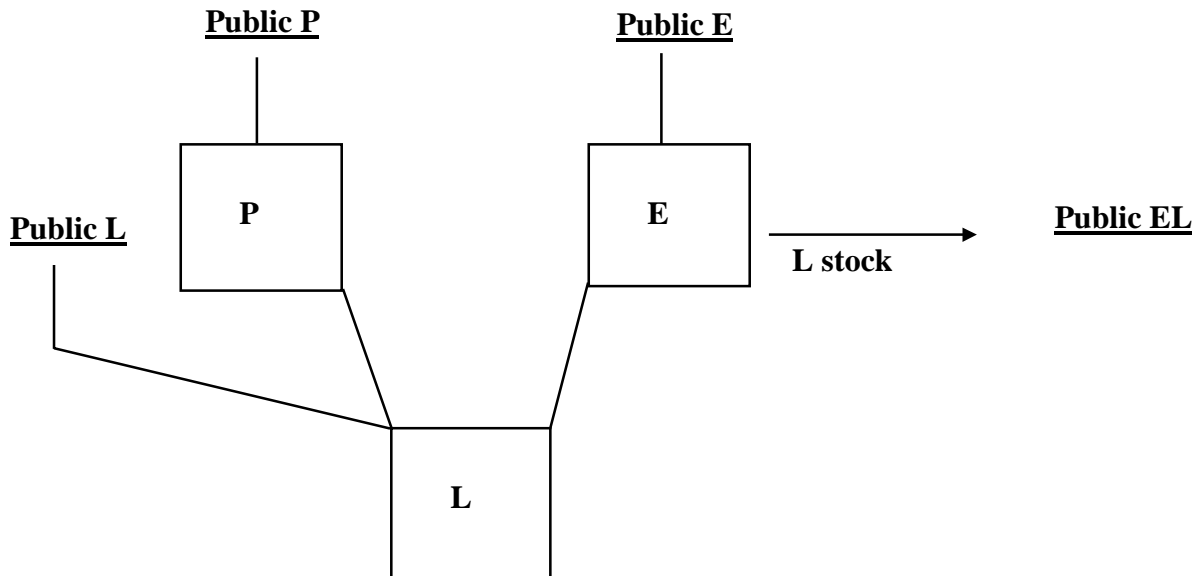
1. L is publicly owned, having no 5-percent shareholders. L is a calendar year taxpayer.
2. L has an employee stock option plan. On each of 4 quarterly dates during 1988, L issues 1 percent of its stock to different employees.
3. On May 1, 1988, L issues 4% of its stock to the public.
4. On October 31, 1988, L issues an additional 6 percent of its stock to the public.
5. During 1989, L acquires a target in exchange for 3% of its stock (i.e. a B reorganization).
6. Each of the stock issuances during 1988 normally would result in the creation of 6 separate public groups. However, L is permitted to combine the groups resulting from the employee stock issuances and the public stock offering of 4% into one group, Public 1L.
7. The second public offering for 6% cannot be combined because it exceeds 5%. Therefore, the separate group resulting from this transaction must remain separate (Public 2L).
8. The group resulting from the target acquisition (Public 3L) cannot be combined because it was identified in another year.

Segregation Rules -- Combination of De Minimis Groups (p. 226)



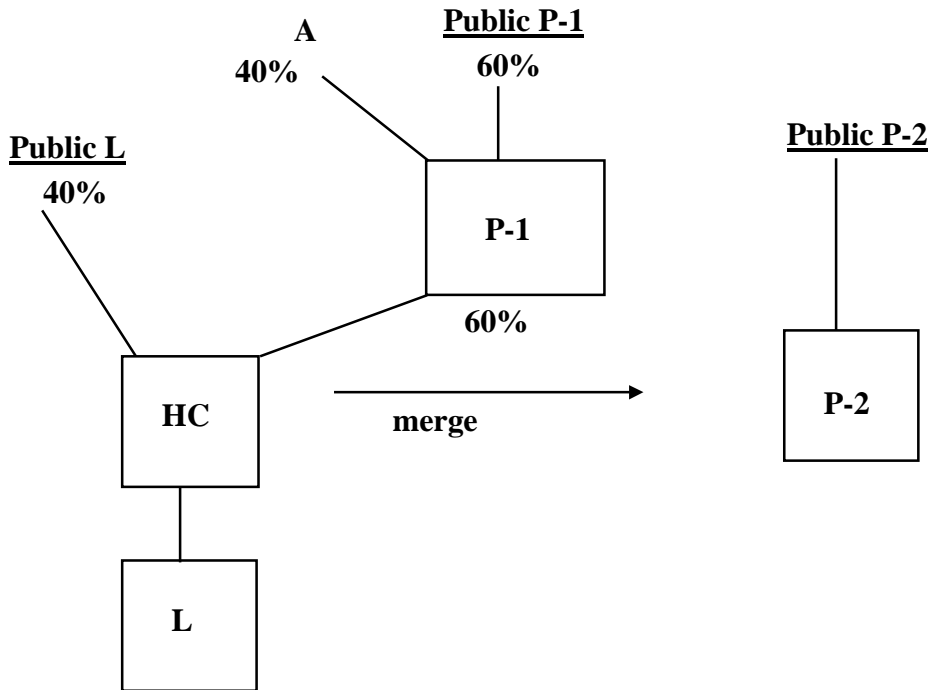
1. L is Publicly owned, having no 5-percent shareholders. L is a calendar year taxpayer.
2. On January 1, 1996, L issues Class A Debentures, which entitle the holder to receive L stock semi-annually in discharge of L's interest obligation.
3. During 1996, L issues additional stock to the public in two separate public offerings.
4. As of the close of 1996, L had issued .45% of its stock on each of two interest dates, 4.5% of its stock in the first public offering, and 6%, of its stock in the second public offering.
5. As of the close of 1997, L issued .41% of its stock on each of two interest dates.
6. L's obligation to issue stock in payment of interest is exempt from the option attribution rules.
7. Each of the stock issuances during 1996 normally would result in the creation of 4 separate public groups. However, L is permitted to combine the groups resulting from the two interest payments and the public stock offering of 4.5% into one group, Public 1L.

Segregation Transactions -- Disposition
by First Tier Entity (p. 227)



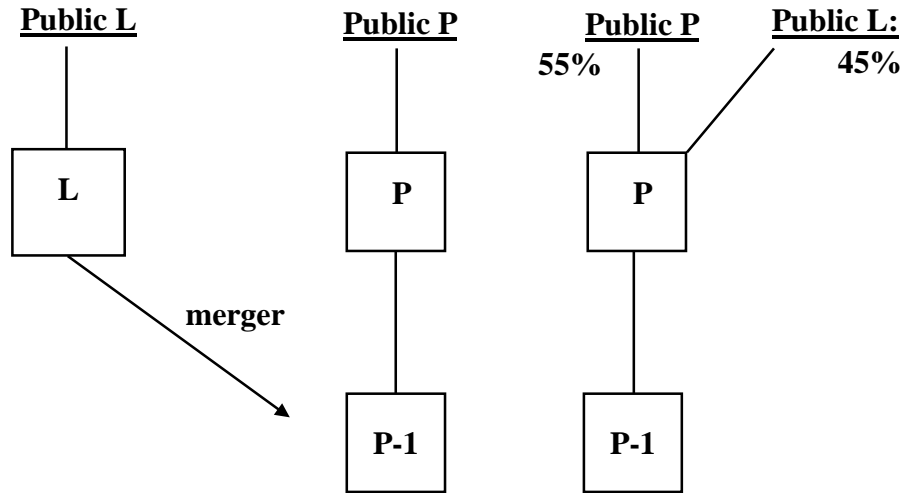
1. L is owned equally by Public L, P, and E. P is owned by Public P. E is a Partnership; none of its partners are 5-percent owners.
2. On October 22, 1988, E sells its interest in L over a public stock exchange. No individual acquires as much as 5% of L.
3. The disposition by E is a transaction that causes the acquiring group, Public EL, to be segregated from Public L, the direct Public group in existence immediately before the disposition.
4. As a result, L has three 5-percent shareholders -- Public L, Public P and Public EL. Public EL has increased its interest by 33-1/3 points,
5. For purposes of subsequent transactions, Public L and Public EL will be treated as separate groups until the October 22, 1988 date is no longer included within a testing period.
6. Note that this increase would result even if Public L were combined with the acquiring group.

Segregation Transactions -- Other Transactions (p. 217)



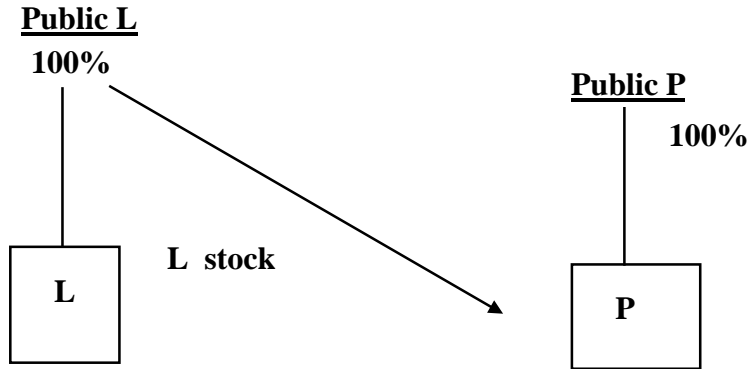
1. The ownership of L is depicted in the diagram above.
2. HC, a first tier entity, is merged into P-2, with the HC shareholders receiving 70% of the outstanding P-2 stock.
3. The merger is a segregation transaction occurring at the first tier entity
4. HC's direct public group, Public L, is segregated from Public P-2.
5. Public P-2 is deemed to acquire a 30% interest in L, not enough for an ownership change.

Segregation Transaction -- Forward Triangular Merger (p. 230)



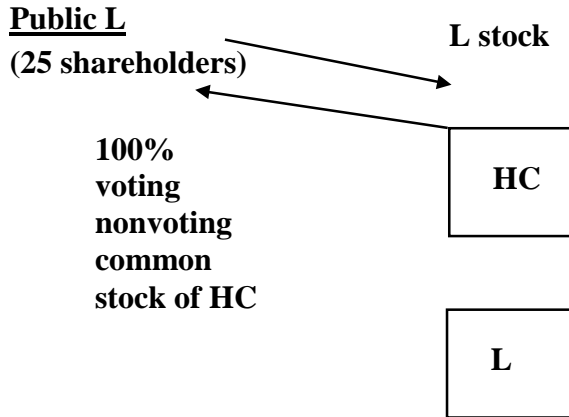
1. L is owned by Public L, P is owned by Public P.
2. On November 22, 1988, P forms P-1 and contributes P stock to P-1. P-1 then acquires all of L's properties in exchange for P stock (i.e., a forward triangular merger) The P stock transferred represents 45% of P.
3. Public P is treated as acquiring stock in the loss corporation (P-1) since P-1 succeeds to L's losses in a section 381(a) transaction.
4. Public P, the direct public group of P that exists immediately before the merger, must be segregated from Public L.
5. Thus, Public P's interest increases by 55 points, and an ownership change occurs.

Segregation Transactions -- B Reorganization (p. 231)



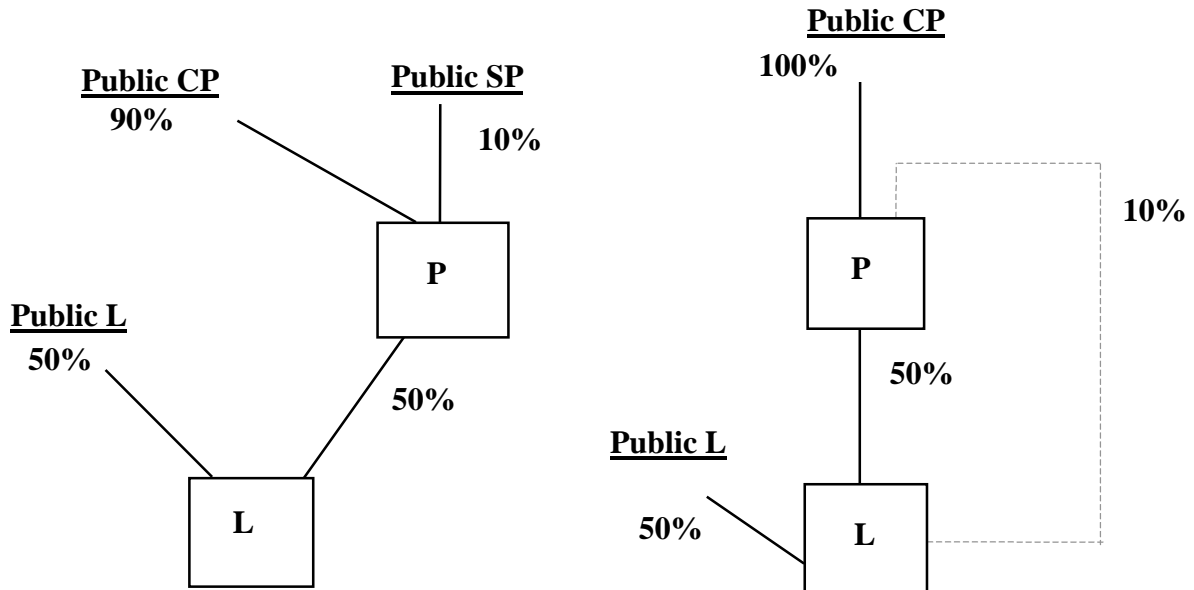
1. L is wholly owned by public shareholders (Public L). P is owned by unrelated individuals, none of whom own as much as 5 percent of P (Public P).
2. On October 31, 1988, P acquires all of the L stock from Public L in exchange for 20% of the P stock (i.e., a "B" reorganization).
3. The B reorganization is a segregation transaction at the first tier entity level (i.e., a section 1032 transaction). Thus, the direct public groups of P must be segregated -- Public L and Public P.
4. After the acquisition, L is owned by Public P -- 80% -- and Public L -- 20%.
5. The reorganization results in an ownership change because Public P increased its interest in L by 80 percentage points.

Segregation Transactions -- Holding
Company Formation (p. 232)



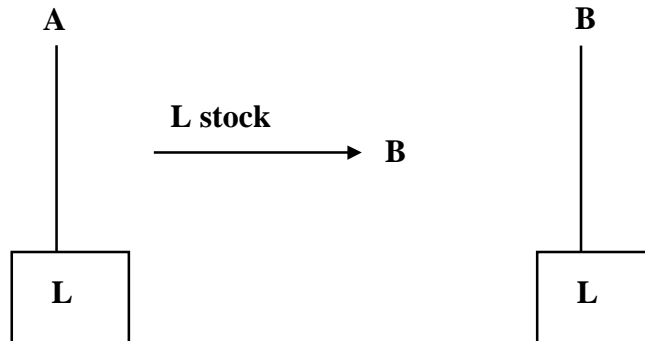
1. L is owned by 25 shareholders, each owning 4% of the L stock (Public L).
2. The L shareholders transfer their L stock to HC in exchange for 100% of each of its two classes of stock -- voting and nonvoting common stock.
3. The formation of HC is a section 1032 transaction and thus is a segregation transaction at the first tier entity level.
4. The shareholders of HC are presumed not to include any members of Public L.
5. However, the presumption does not apply since L has actual knowledge as to the identity of the HC and L shareholders, Both L and H are treated as if owned by the same public group.

Redemption Type Transaction (p. 234)



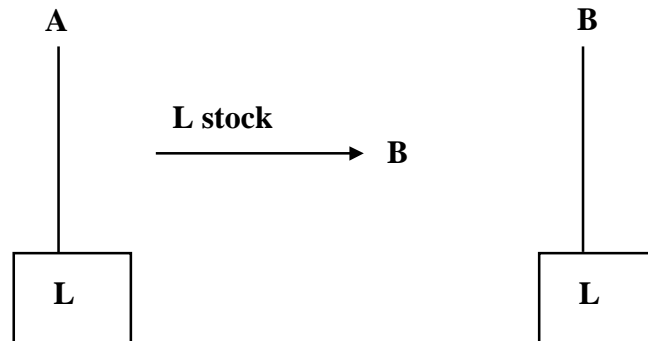
1. P owns 50 percent of L. The remaining 50 percent of L is held by public shareholders (Public L). P is wholly-owned by public owners.
2. L acquires 10 percent of the P stock in the open market,
3. Since the transaction is to be treated as a redemption-type transaction, Public P must be segregated into two groups -- Public CP owning 90 percent of P and Public SP owning 10 percent of P.
4. The transaction apparently is considered to reduce the outstanding P stock since it is treated as a redemption-type transaction.
5. Thus, Public CP increases its interest in L by 5 points -- from 45% constructively beforehand to 50% constructively afterwards.

Treas. Reg. § 1.382-6 and Notice 87-79



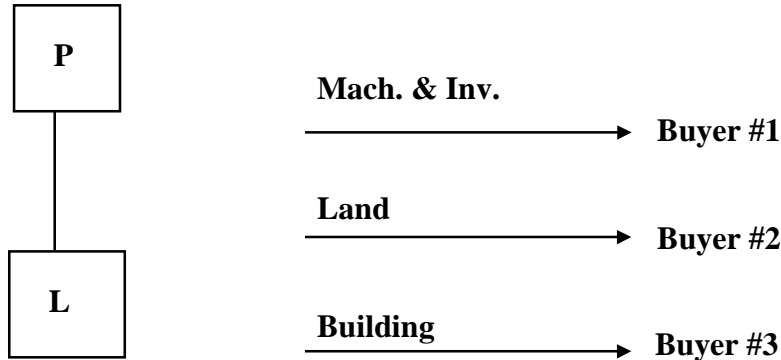
1. A owns all of the stock of L, L has an NOL carryover of \$1,000,000 from 1985.
2. On June 30, 1996, A sells his Stock to B for \$500,000 (an ownership change).
3. During 1996, L has income of \$300,000, \$200,000 of which accrued prior to the change date.
4. Treas. Reg. § 1.382-6 and Notice 87-79 permits L to obtain a ruling that will allow it to allocate income based on the closing of its books on the change date, rather than a pro rata allocation. Therefore, the \$200,000 pre-change date income may be offset by L's NOL without limitation.
5. The loss corporation must file the information statement evidencing the ownership change as per Treas. Reg. § 1.382-6(b)(2)(i), must not have accelerated income to the pre-change period or deferred loss to the post-change period, and must treat all corporations within the affiliated group consistently.
6. This election is especially helpful if the corporation has a large amount of cancellation of indebtedness income arising out of the ownership change transaction. The Service generally permits the COI income to be allocated to the period prior to the change date.

General Operation of Section 382 (p. 326)



1. A owns all of the stock of L. L has an NOL carryover of \$1,000,000 from 1985.
2. On June 30, 1988, A sells his stock to B for \$500,000 (an ownership change). The highest published tax rate for the 3-month period ending in June was 10 percent.
3. During 1988 L has income of \$100,000. For 1988, such taxable income must be allocated on a daily pro rate basis. Thus, \$50,000 is allocable to the period ending on June 30, 1988, and \$50,000 is allocated to the period beginning on July 1, 1988.
4. The section 382 limitation is \$50,000 (\$500,000 times 10%). For 1988, the limitation must be allocated on a daily pro rata basis. Thus, the limitation for the period beginning on July 1, 1988 is \$25,000.
5. Thus, for 1988, L may offset \$75,000 of its taxable income with its NOL carryover.

Built-in Gains (p. 328)



1. On December 31, 1987, P acquires all of the L stock in a transaction which constitutes an ownership change.
2. Immediately before the ownership change, L holds the following assets:

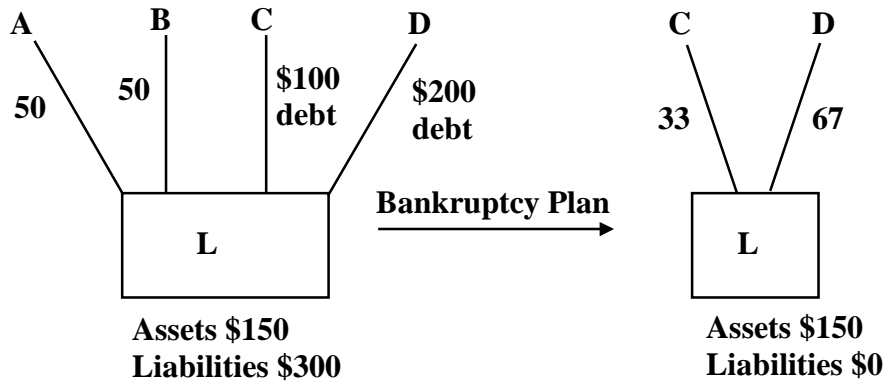
<u>Asset</u>	<u>Value</u>	<u>Basis</u>	<u>Built-in Gain (Loss)</u>
Cash	10	10	0
Land	200	100	100
Bldg.	500	250	250
Mach.	50	70	(20)
Inv.	0	80	<u>(80)</u>
Built-in gain (net)			250

3. L meets the threshold requirement for built-in gains. The net unrealized built-in gain (\$250) exceeds 15 percent of the total fair market value of L's assets less cash (\$750).
4. On July 1, 1988, L sells the machinery and inventory and recognizes a loss of \$100. This loss is not subject to limitation. It reduces the 1988 taxable income (which is subject to limitation).
5. On July 1, 1990, L sells the land and recognizes a total gain of \$200 (the land appreciated in value). L's recognized built-in gain is only \$100 -- the extent of built-in gain as of December 31, 1989.
6. On July 1, 1991, L sells the building and recognizes a gain of \$250. The full gain constitutes recognized built-in

gain. However, only \$150 may be used to increase the section 382 limitation.

7. Suppose that L sells the building in 1991 for an installment obligation, the first payment on which is not due until 1993. For purposes of both sections 382 and 384, the gain recognized on the installment payments will be considered recognized built-in gain, (increasing the section 382 limitation for those years) notwithstanding that such gain was recognized outside the normal 5-year recognition period. Notice 90-27.
8. In addition to lowering the percentage threshold from 25 to 15 percent, RRA89 added an absolute alternate threshold of \$10 million net unrealized built-in gain. This threshold will be much easier for a large corporation to meet.

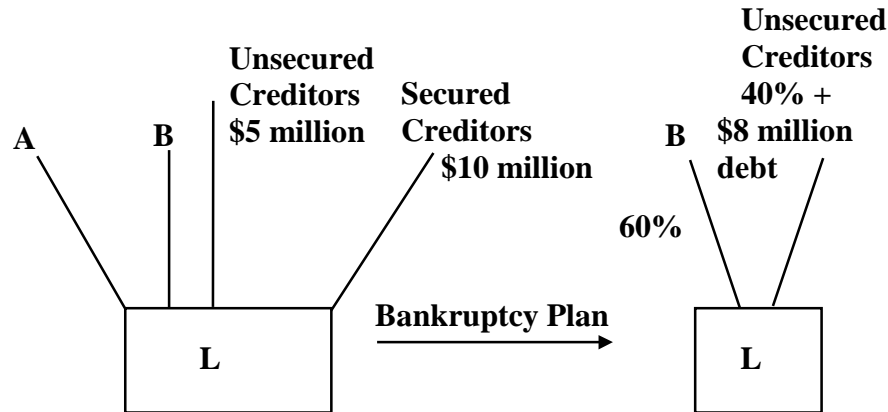
Bankruptcy Exception - Section 382(1)(5) (p. 332)



1. A and B own all the stock of L in equal shares. L has \$150 in assets and \$300 of liabilities. L has a \$500 NOL carryover from 1987. C and D have been creditors for more than 18 months. L has accrued and paid \$100 in interest on the debt to C and D within the past three years.
2. On June 1, 1990, L files a petition in bankruptcy. Under a plan of reorganization, confirmed by the bankruptcy court on June 1, 1991, the old common stock and the debt of L will be canceled. A and B will each receive nothing. C will receive 33 percent of L's newly issued common stock. D will receive 67 percent of the common stock. The effective date of the plan is January 1, 1992.
3. The bankruptcy plan will result in an ownership change on January 1, 1992, the effective date.
4. However, the section 382 limitation will not apply because shareholders and historic creditors own more than 50 percent of L's stock after the ownership change.
5. L's NOL carryover will be reduced by the interest paid on the debt that has been converted to stock (\$100).
6. In addition, L's NOL carryover will be further reduced by 50 percent of the COI income that would have been realized but for the section 108(e)(10)(B) bankruptcy exception. (\$300 Debt less \$150 common stock received in the exchange.)

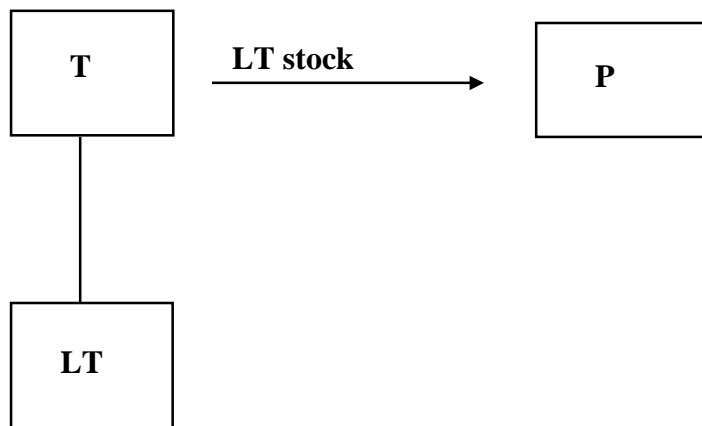
7. Therefore, on these facts, L's NOL would be reduced \$175 from \$500 to \$325. (\$100 interest reduction plus 50 percent of the \$150 COI income).
8. Apparently, the same result is reached if A guaranteed L's debt to D and was required to perform on the guarantee, and A received 67 percent of L's stock, so long as the purpose of guarantee was not to circumvent the qualified creditor limitation in section 382 (1)(5)(E) (claim must be held by creditor 18 months before bankruptcy filing or have arisen in the ordinary course of business).
9. A second ownership change within two years of a section 382(1)(5) transaction eliminates the loss corporation's NOL's.

Section 382(1)(5) - Capital Contributions



1. A and B own 75 percent and 25 percent, respectively, of L's stock. L has secured debt of \$ 10 million, all of which is owed to 382(1)(5) qualified creditors. L has unsecured debt of \$5 million. L has assets of \$10 million.
2. L files a petition in bankruptcy.
3. B contributes \$5 million to discharge the unsecured creditors and receives 60 percent of L's new common stock, A's stock is canceled. The secured creditors receive 40 percent of the new common stock and \$8 million in new debt.
4. The bankruptcy plan will result in an ownership change, because there is a 75 percentage point change in ownership.
5. In addition, section 382(1)(5) would probably not be available. B did not receive his stock as a result of being a shareholder immediately prior to the ownership change; rather, he received the stock as a result of the capital contribution.
6. Section 382(1)(5) would be available if the secured creditors received at least 50 percent of the stock in L.
7. Query what result if A contributed the \$5 million and received 60 percent of the stock instead of B.

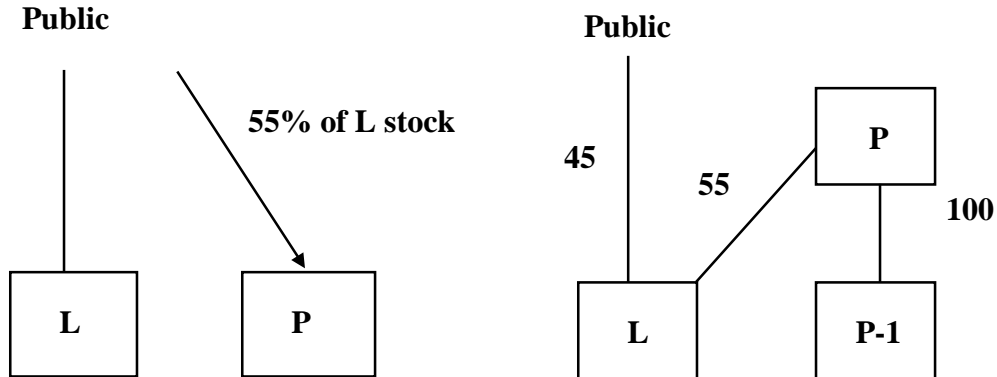
Sections 382 and 338 -- One-Step Acquisitions (p. 381)



1. T owns all of the stock of LT. T and LT file consolidated returns.
2. On December 31, 1987, P purchases all of the LT stock from T.
3. The transfer is both an ownership change and a qualified stock purchase. Thus, the change date and the acquisition date are the same date -- December 31, 1987.
4. If P makes a 338 election (and no section 338(h)(10) election is made), all of the section 338 gain will be reported on LT's one-day deemed sales return for December 31, 1987.
5. The one-day period is a separate taxable year ending on the change date. Therefore, such period is not a post-change year.
6. Section 382 does not apply.
7. Section 382 should not apply if T makes a section 338(h)(10) election. Under such an election, T is not considered to have sold LT's stock. LT is treated as selling its assets and then liquidating. T would inherit LT's NOL carryover in the deemed liquidation.
8. This analysis assumes that the change date does not precede the acquisition date due to the option attribution rules.

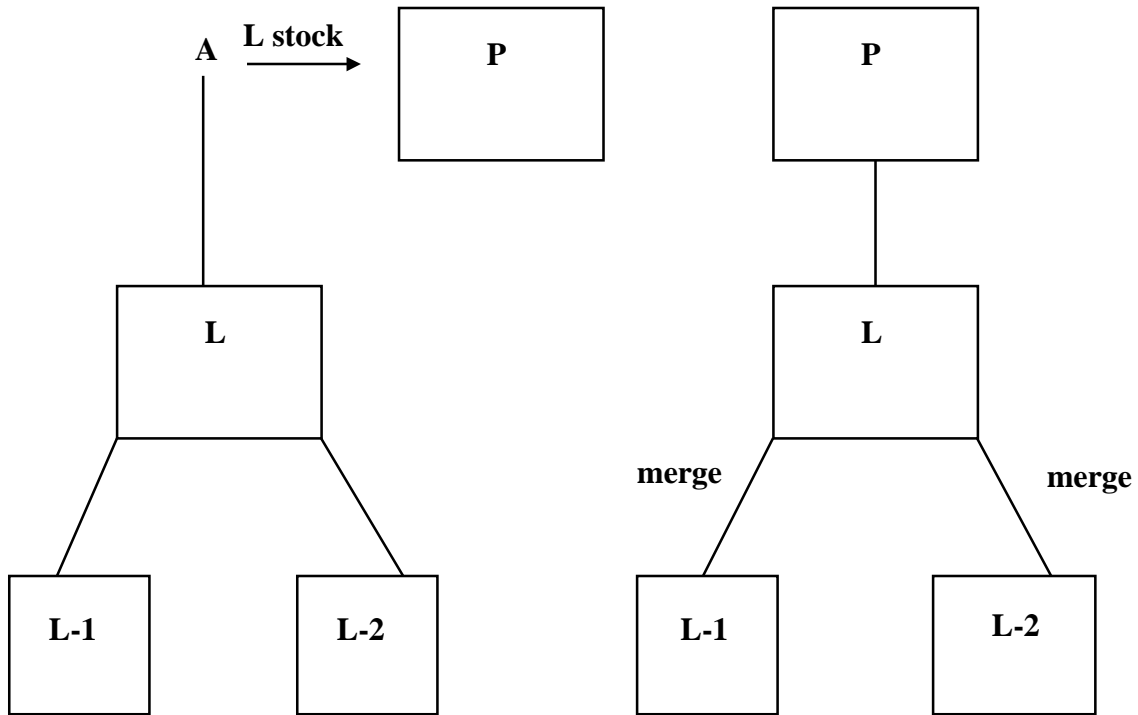
If the change date does precede the acquisition date, then the two-step analysis in the next diagram applies.

Section 382 and 338 -- Two-Step Acquisitions (p. 384)



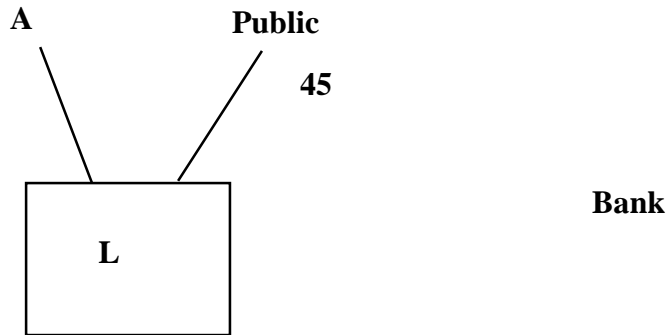
1. L is publicly-held.
2. On January 1, 1988, P buys 55% of the L stock in a cash tender offer.
3. On July 1, 1988, P acquires the remaining 45% of L stock in merger transaction.
4. The change date for section 382 purposes is January 1, 1987, the acquisition date for section 338 purposes is July 1, 1988.
5. The section 338 gain is reported on L's final return ending on July 1, 1988. Such year is a post-change year; therefore, section 382 applies.
6. Gain accrued as of January 1, 1988 is treated as recognized built-in gain and may be offset by L's NOL carryover to the extent permitted by section 382(h)(1)(A).
7. Special relief under amended section 382(h)(1)(C) is not available for gain accrued from January 2 through July 1, 1988.

Section 381 -- Impact of Subsequent Events (p. 388)



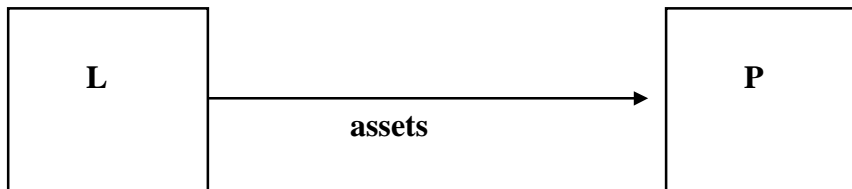
1. A owns all of the stock of L. L owns all of the stock of L-1 and L-2.
2. On January 1, 1988, P acquires all of the L stock in a transaction which constitutes an ownership change.
3. On January 1, 1989, P merges L-1 and L-2 into L.
4. NOL carryovers from the year 1987 and earlier are pre-change losses. The section 382(a) limitations apply during any post-change year, including 1989.
5. As a result of the ownership change, a separate section 382 limitation amount must be calculated for L-1 and L-2.
6. L-1's NOL carryovers may only offset L's income to the extent of L-1's section 382 limitation. L-2's NOL carryover may only offset L's income to the extent of L-2's section 382 limitation.

Planning -- Issuing Debt Instruments (p. 392)



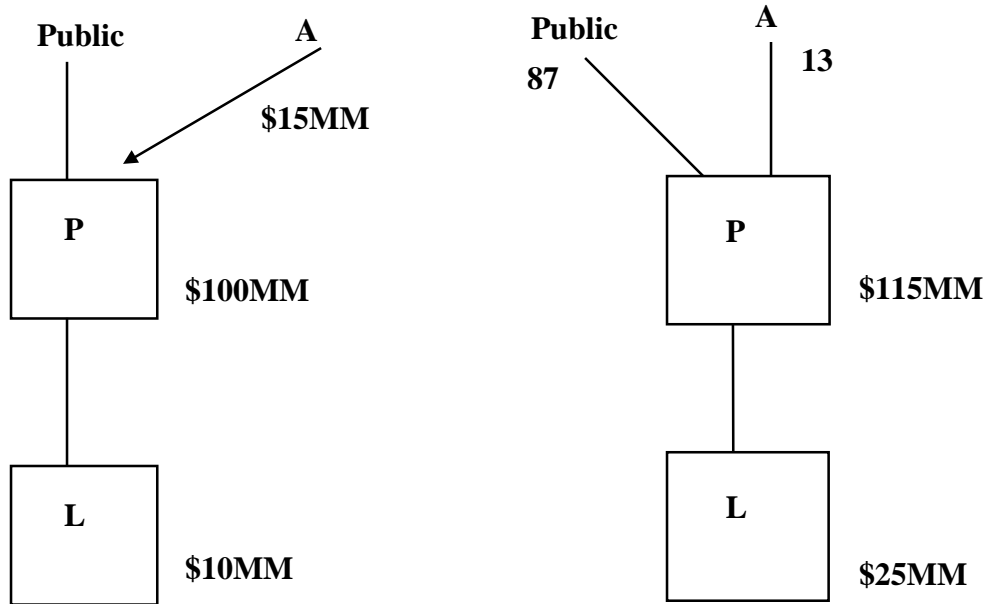
1. L is wholly-owned by A.
2. In 1987, L issues 45% of its stock to the public in an initial public offering.
3. In 1988, L must raise additional capital, but does not want to trigger an ownership change,
4. L may have to raise the funds either in the bond market or through bank lending.
5. If L stock is pledged on a loan, the pledge may be treated as an option which triggers an ownership change. The foreclosure could also trigger an ownership change (assuming the pledge itself did not).

Planning -- Sale or Lease of L's Assets (p. 393)



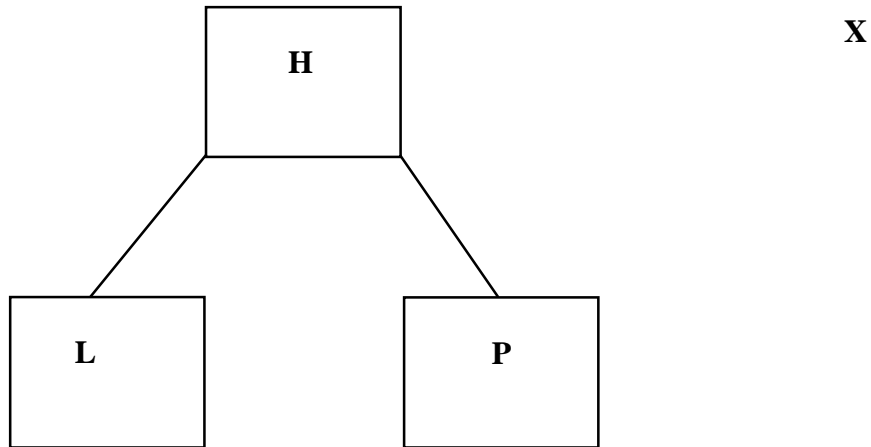
1. P is interested in acquiring the business of L.
2. If P acquires the stock of L, an ownership change will occur.
3. However, L may sell or lease its assets to P without impairing its NOL carryover.

Planning -- Subsidiary Tracking Stock (p. 393)



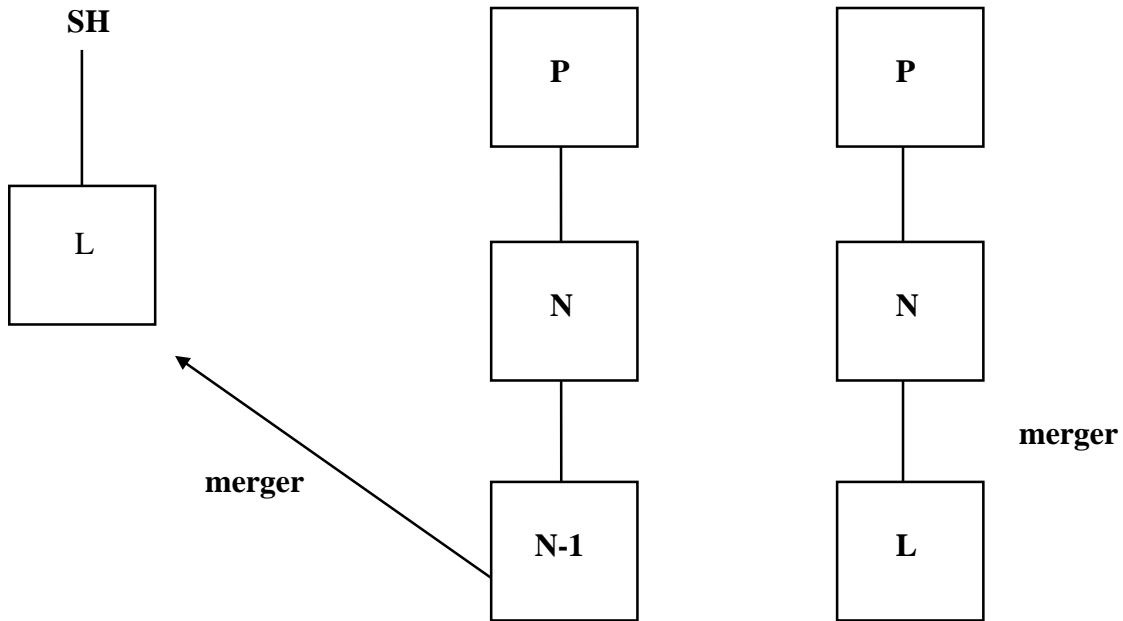
1. P owns all of the stock of L. L is worth \$10MM. P is worth \$100MM. P is publicly held.
2. A plans to invest \$15MM in L, without triggering an ownership change.
3. A may accomplish this by contributing \$15MM to P in exchange for all of a newly issued special class of P stock.
4. This class represents 13% of the value of P. Dividends on this class of stock depend on L's earnings.
5. P contributes the \$15MM to the capital of L.
6. No ownership change occurs because A has only increased his interest in L by 13%.

Planning -- Corporate Combinations Prior
to an Ownership Change (p. 394)



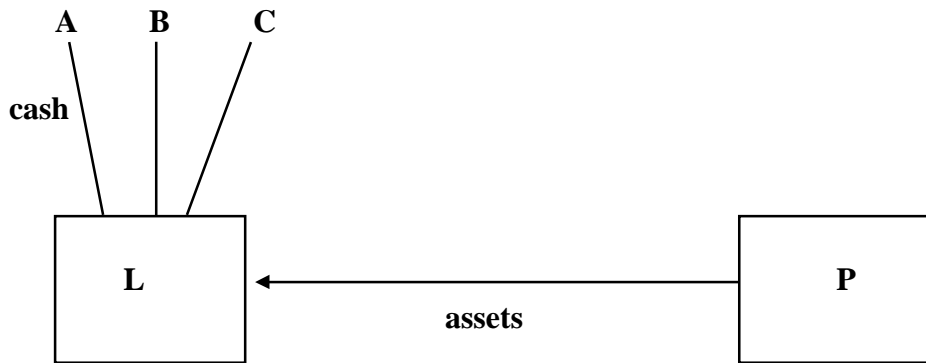
1. H has two wholly-owned subsidiaries -- L and P. X wishes to acquire H and its subsidiaries.
2. L has large NOL carryovers but little value, P has no NOL carryovers but high value,
3. If X acquires the stock of H, an ownership change will occur with respect to L,
4. The section 382 limitation calculation for L will reflect its low value.
5. If H merges L into P prior to X's acquisition, P will become a loss corporation. The section 382 limitation with respect to P will reflect both P and L's combined value unless the combination is viewed as a capital contribution.

Planning -- Leveraged Buy-Out Transaction (p. 394)



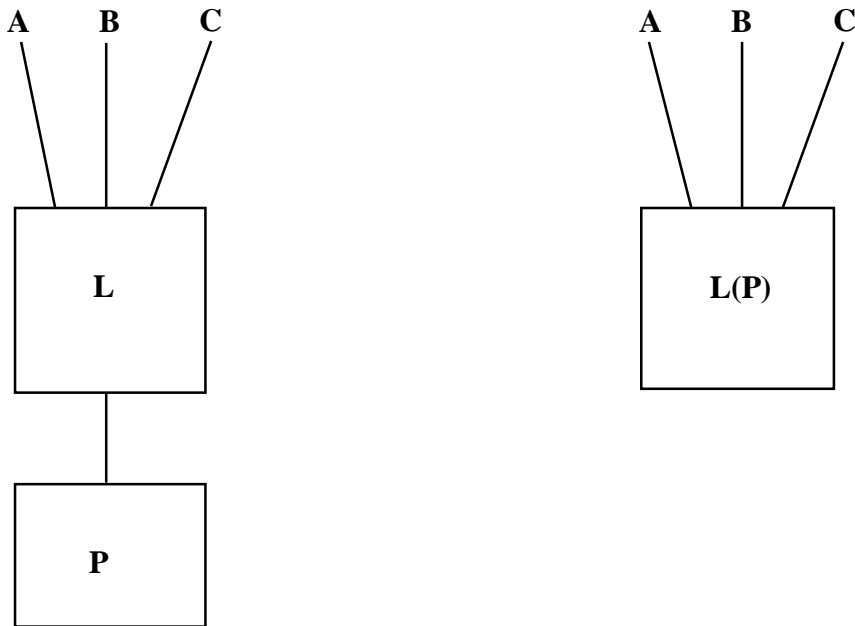
1. P wishes to acquire L using borrowed funds. L is worth \$100MM.
2. P forms N and contributes \$10MM.
3. N borrows \$90MM and contributes \$100MM (\$90MM + \$10MM) to N-1.
4. N-1 is merged into L, with L surviving. L's shareholders receive the \$100MM in exchange for the L stock,
5. The bank requires that L and N be combined.
6. If N is merged into L, the transaction should be viewed as a redemption by L of \$90MM of its stock. L's value for computing the section 382 limitation would be \$10MM.
7. However, if L is merged into N, the transaction should be viewed as a purchase of L stock. L's value for computing the section 382 limitation would be \$10MM.
8. Under TAMRA, the upstream merger may be treated as a redemption, even though the transaction is treated as a purchase for other tax purposes.

Planning -- L Purchases Assets of P (p. 396)



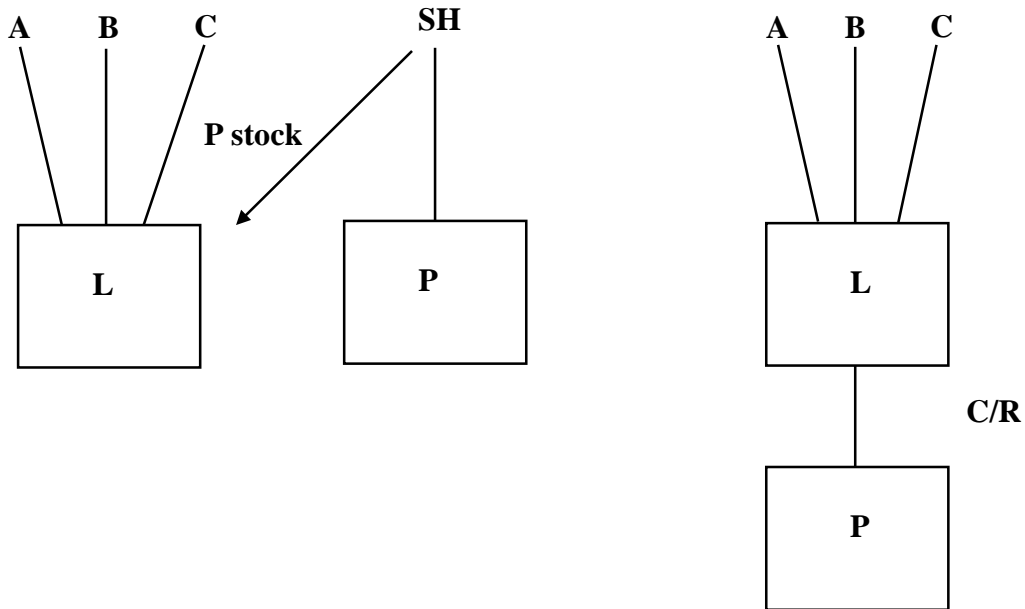
1. L is owned by A, B and C. L conducts business X.
2. P conducts business Y, and L would like to acquire that business.
3. A, B and C contribute cash to L, and L uses the money to acquire the assets of the Y business.
4. Shortly thereafter, L terminates its business X.
5. L's NOL carryovers should be able to offset income generated by its new business Y.
6. Sections 269(a) and 382 do not apply. Libson Shops should not apply.

Planning -- L Purchases Stock of P (p. 396)



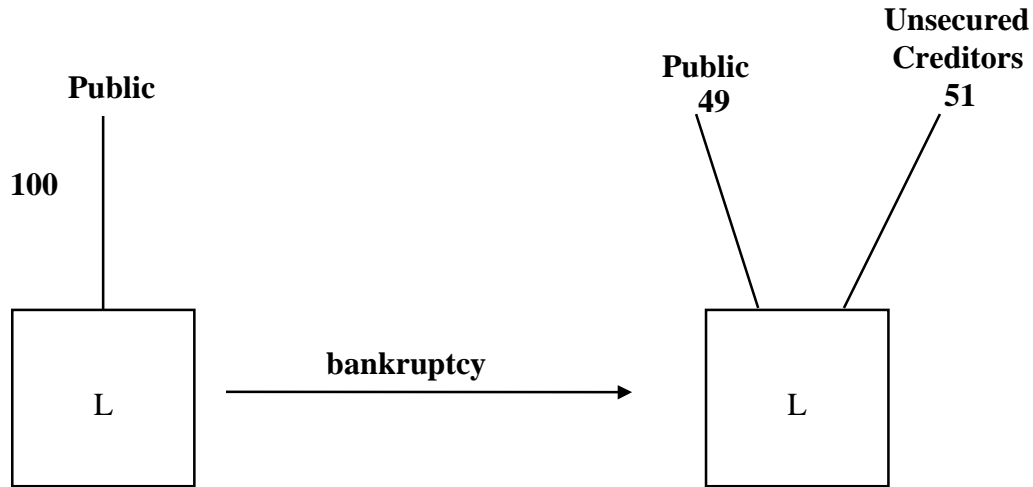
1. The facts are the same as in the previous diagram, except that L acquires all of the P stock, and elects section 338.
2. L then liquidates P under section 332.
3. L's NOL carryover should be able to offset the income generated by P's assets. It may not offset any section 338 gain.
4. Section 269(a) should not apply.
5. Sections 269(b) and 382 do not apply. Libson Shops also should not apply.

Planning -- L Acquires P Stock (p. 397)



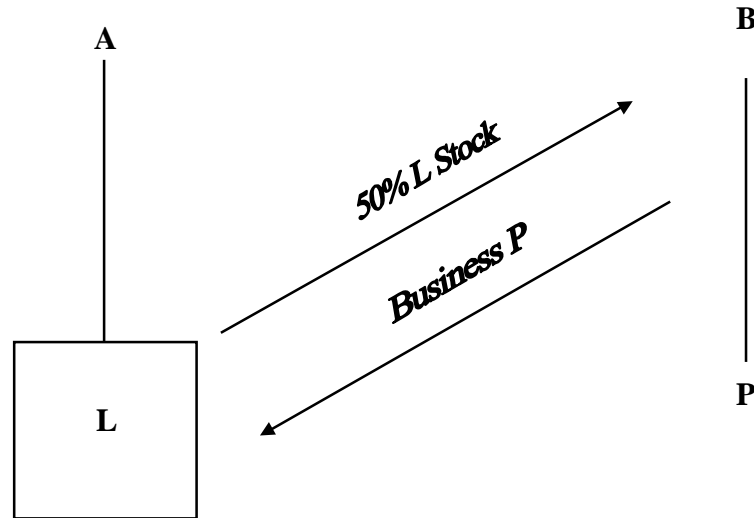
1. The facts are the same as in the second preceding diagram, except that L acquires P stock.
2. L and P then file consolidated returns.
3. Section 269(a)(1) should not apply here. This transaction is, in substance, equivalent to an asset purchase.
4. Section 382 does not apply. Libson Shops should not apply.
5. L's NOL carryovers are not subject to the SRLY restrictions.
6. Section 384 would prevent L from using its losses to offset P's built-in gains that are recognized in the recognition period.

Planning - Monitoring Stock Ownership (p. 398)



1. As a result of the above transaction, L underwent an ownership change.
2. However, section 382(1)(5) prevents the application of the section 382(a) limitations.
3. In order to avoid a second ownership change, which would eliminate any NOL carryover by making the 382 limitation zero, L may wish to monitor and control the trading in its stock.
4. A stock escrow arrangement may be feasible in situations involving a limited number of shareholders, all of which are agreeable to such an arrangement. A standstill agreement would have similar effect.
5. L may also adopt transfer restrictions, so long as such restrictions are enforceable under state law.
6. For example, a corporation amended its Articles of Incorporation to provide that any transfer to a person who would own 4.5 percent of the company's stock as a result of the transfer would be void. The acquirer is required to give up the shares on demand, and an agent of the corporation will sell such shares on the open market. The Service has ruled that the purported acquirer will be treated as not owning the transferred stock. LTR 8949040.

Planning - Insolvent Corporations



1. L has a \$10 million NOL carryover. L has \$3 million in assets and \$7 million in liabilities. L is wholly owned by A.
2. Investor B has a profitable business, P. He wishes to use L's NOL to shelter income from the business.
3. B cannot simply buy A's stock. This would result in an ownership change. Because L's value is zero, the NOL would be useless.
4. Consistent with section 382, B may receive up to 50 percent of the value of L in common stock, participating preferred stock or convertible preferred stock in exchange for a capital contribution of the profitable business.
5. The remainder of the value may be received in the form of debt or straight preferred stock,
6. As a practical matter, B will want to take the maximum out in the form of preferred stock or debt, since any value adhering to A's interest is a windfall.
7. However, to the extent L remains insolvent or is only marginally solvent, the Service may take the position that the creditors own "stock" in the company, or that the straight preferred stock is stock since it participates in corporate growth, therefore prompting an ownership change.

8. There can be no assurance that this type of restructuring will work in any given transaction. There are too many unresolved factual issues, including what constitutes stock, and the valuation of each such class. Further, while a transaction may work for 382 purposes, the Service may take the position that section 269 nonetheless applies.

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RESTRUCTURINGS 1998

APPENDIX TO OUTLINE ON
SECTION 382 OF THE
INTERNAL REVENUE CODE OF 1986

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