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October 24, 2014

The Honorable Mark Mazur
Assistant Secretary (Tax Policy)
Department of the Treasury
1500 Pennsylvania Avenue, NW
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The Honorable John Koskinen
Commissioner
Internal Revenue Service
1111 Constitution Avenue, NW
Washington, DC 20224

The Honorable William J. Wilkins
Chief Counsel
Internal Revenue Service
1111 Constitution Avenue, NW
Washington, DC 20224

Re: **Report on the Kimbell-Diamond Doctrine**

Dear Messrs. Mazur, Koskinen and Wilkins:

I am pleased to submit the attached report (the "Report") of the Tax Section of the New York State Bar Association. The Report comments on the continuing application (if any) of the Kimbell-Diamond doctrine (the "KD doctrine").

The KD doctrine refers to an application of the step transaction doctrine pursuant to which the acquisition of the stock of a target corporation by an acquirer followed by a liquidation or merger of the target corporation into the acquirer pursuant to an integrated transaction is treated as an acquisition of the target corporation's assets. If KD doctrine applies, the acquirer is treated as acquiring the target corporation's assets for the consideration that the acquirer, in form, paid to the target corporation's stockholders. In a taxable transaction, application of the KD doctrine results in the acquirer taking a tax basis in the target corporation's assets equal to the acquirer's purchase price for the stock rather than the target corporation's historic basis in its assets.

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The tax consequences of an application of the KD doctrine to the target corporation and its shareholders are less settled. Under one approach, the tax effect of the recast applies only to the acquirer, and the transaction is not recast with respect to the target corporation or its shareholders. Under this approach, in accordance with the form of the transaction, the target corporation's shareholders are treated as transferring their stock to the acquirer in exchange for consideration provided by the acquirer, and the target corporation is then treated as transferring its assets to the acquirer by liquidation or merger. Under a second approach, the tax effect of the recast applies not just to the acquirer, but also to the target corporation and its shareholders. Under this symmetric application of the KD doctrine, the acquirer is treated as acquiring the assets of the target corporation in exchange for the consideration that the acquirer, in form, provided to the target shareholders, and the target corporation is then treated as distributing the consideration to its shareholders pursuant to a liquidating distribution.

Since the enactment of Section 338, the Department of the Treasury ("Treasury") and the Internal Revenue Service (the "IRS") have issued regulations and other administrative guidance confirming that the KD doctrine was repealed in relation to a qualified stock purchase ("QSP") of a target corporation. However, it is not entirely clear whether the KD doctrine has continuing application to acquisitions that do not qualify as QSPs, and the recent issuance of regulations under Section 336(e) has reinvigorated the importance of addressing this gap.

We believe that the KD doctrine should not apply to recast, as a taxable acquisition of the target corporation's assets, the acquisition of the stock of a target corporation by an acquirer that is followed by a liquidation or merger of the target corporation into the acquirer pursuant to an integrated transaction. In these circumstances, the step transaction doctrine should not apply and the federal income tax consequences should follow the form of the transactions. As a result, the transaction generally should be treated as an acquisition of the stock of the target in exchange for the consideration provided by the acquirer, followed by a liquidation of the target into the acquirer. This result should apply even if the acquisition is neither a QSP nor a qualified stock disposition ("QSD") and even if the acquirer is not a corporation.

More specifically, to eliminate ambiguity regarding the possible application of the KD doctrine outside the context of transactions involving a first-step QSP, we recommend that Treasury and the IRS issue guidance confirming that, if the integrated transaction does not qualify as a reorganization under Section 368(a), the federal income tax consequences of the acquisition of the stock of a target corporation by an acquirer in a QSD or any other transaction that is not a QSP, followed by a liquidation or merger of the target corporation into the acquirer, should follow the form of the transactions, taking into account all other relevant transactions that occur in connection with the acquisition and the subsequent liquidation or merger.

We believe that our recommendations do not require any change to current law pursuant to which the acquisition of the stock of a target corporation by an acquirer, followed by a liquidation or merger of the target corporation into the acquirer, is treated as a reorganization under Section 368(a) if, under the step transaction doctrine, the integrated transaction satisfies the requirements of the reorganization provisions.

We appreciate your consideration of the Report. If you have any questions or comments, please feel free to contact us. We would be glad to discuss or assist in any way.

Respectfully submitted,

David H. Schnabel
Chair

Attachment

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