

**PRESENTED AT**

33rd ANNUAL LLCs, LPs and Partnerships

July 11-12, 2024

Austin, Texas

**SPIN OFFS & SPLIT UPS**

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## SPIN OFFS & SPLIT UPS

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### PART 1. SUBCHAPTER S CORPORATIONS

#### 1. Brief Introduction to Subchapter S Corporations

**1.1 Corporate Taxation.** Subchapter C of Chapter 1 of the Internal Revenue Code contains the C Corporation tax provisions. A corporation can be either a C Corporation or an S Corporation for federal income tax purposes.

- A. Basic premise of C Corporate tax: The corporation and its shareholders are two distinct taxpayers.
- B. Basic premise of S Corporate tax: The S corporation is a flow through entity in which its shareholders, rather than the corporation, are generally taxed on the corporation's earnings, regardless of whether the earnings are distributed. Subchapter C applies to an S corporation, except to the extent of any inconsistency involving an S corporation.

**1.2 Section 355.** Section 355 provides that when certain judicial and statutory requirements are satisfied, a corporation can be divided into two or more separate corporations on a tax-free basis. The rationale is that a corporate division is merely a change in the form of business which continues to be owned and operated by the same shareholders. The intended purpose of Section 355 separations is to facilitate the rearrangement of continuing business activities for business reasons in a form that does not resemble a cashing out of an equity investment.<sup>1</sup>

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<sup>1</sup> Bittker & Eustice, ¶11.06[1].

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First appeared as part of the conference materials for the  
33<sup>rd</sup> Annual LLCs, LPs and Partnerships session

"“Breaking Up is Hard to Do”: S Corp, LLC and Partnership Divisions"