TBL Licensing LLC f. k. a. The Timberland Company, and Subsidiaries (A Consolidated Group) v. Commissioner of Internal Revenue, 158 T. C. No. 1 (U. S. Tax Court 2022)

In a significant ruling, the U. S. Tax Court determined that a U. S. corporation must recognize immediate gain upon transferring intangible assets in an outbound F reorganization to a foreign subsidiary, even if the U. S. entity becomes disregarded for tax purposes. This decision underscores the complexities of tax treatment in corporate reorganizations involving intangible property transfers abroad, affirming the IRS's position on the application of Section 367(d).

Parties

TBL Licensing LLC f. k. a. The Timberland Company, and Subsidiaries (A Consolidated Group) (Petitioner) v. Commissioner of Internal Revenue (Respondent).

Facts

TBL Licensing LLC (TBL), a Delaware limited liability company treated as a corporation for U. S. federal income tax purposes, was involved in a post-acquisition restructuring following VF Corp. 's acquisition of Timberland. TBL came to own Timberland's intangible property, which it then constructively transferred to TBL Investment Holdings GmbH (TBL GmbH), a Swiss corporation, as part of an outbound F reorganization under Section 368(a)(1)(F). TBL subsequently elected to be disregarded as an entity separate from its owner, International Properties, which was owned by VF Enterprises S. à. r. l. , a foreign subsidiary of VF Corp. The parties agreed that this transaction constituted a reorganization described in Section 368(a)(1)(F) and that TBL's transfer of intangible property to TBL GmbH was subject to Section 367(d).

Procedural History

The Commissioner issued a notice of deficiency to TBL on May 11, 2015, asserting a deficiency of $504,691,690 in income tax for the taxable year ended September 23, 2011. TBL filed a petition in the U. S. Tax Court challenging the deficiency. Both parties moved for summary judgment. The Commissioner also filed a motion in limine to exclude certain stipulations and exhibits offered by TBL and a motion to strike material from TBL's memorandum in support of its motion for summary judgment.

Issue(s)

Whether TBL must recognize immediate gain under Section 367(d)(2)(A)(ii)(II) due to its constructive transfer of intangible property to TBL GmbH as part of an outbound F reorganization, given that TBL became a disregarded entity following the transaction?

Whether the fair market value of the transferred intangible property for gain recognition purposes under Section 367(d)(2)(A)(ii)(II) should be determined using the property's entire expected useful life, or limited to 20 years as per Temp. Treas. Reg. § 1. 367(d)-1T(c)(3)?

Rule(s) of Law

Section 367(d) of the Internal Revenue Code generally requires a U. S. transferor of intangible property to a foreign corporation to recognize gain in the form of ordinary income. The timing of income recognition varies depending on the circumstances, with Section 367(d)(2)(A)(ii)(II) mandating immediate gain recognition upon a "disposition" following the transfer, defined as including a distribution of the stock of the transferee foreign corporation.

Holding

The U. S. Tax Court held that TBL must recognize immediate gain under Section 367(d)(2)(A)(ii)(II) due to its constructive transfer of intangible property to TBL GmbH, as TBL's distribution of TBL GmbH stock to VF Enterprises constituted a "disposition" within the meaning of the statute. The Court further held that the fair market value of the transferred intangible property for gain recognition purposes should be determined based on the property's entire expected useful life, without applying the 20-year limitation imposed by Temp. Treas. Reg. § 1. 367(d)-1T(c)(3).

Reasoning

The Court reasoned that TBL's distribution of TBL GmbH stock to VF Enterprises was a "disposition" under Section 367(d)(2)(A)(ii)(II), as it was a constructive distribution of the stock received in exchange for the transferred intangible property. The Court rejected TBL's argument that the disposition did not occur within the transferred property's useful life, as the distribution necessarily followed the transfer of intangible property. The Court also found no provision in the regulations that allowed TBL to avoid immediate gain recognition by having another entity report deemed annual payments under Section 367(d)(2)(A)(ii)(I), especially since TBL ceased to exist as a separate entity for tax purposes after the reorganization. Regarding the fair market value of the transferred intangible property, the Court held that Temp. Treas. Reg. § 1. 367(d)-1T(c)(3)'s 20-year useful life limitation was not applicable for determining gain under Section 367(d)(2)(A)(ii)(II), as it was intended for the annual inclusion regime and not for immediate gain recognition. The Court emphasized that the fair market value should reflect the amount an unrelated purchaser would pay, considering the entire period during which the property would have value.

Disposition

The U. S. Tax Court granted the Commissioner's motion for summary judgment and denied TBL's motion for summary judgment. The Court also denied as moot the Commissioner's motion in limine and motion to strike.

Significance/Impact

This case clarifies the application of Section 367(d) in outbound F reorganizations involving intangible property transfers, emphasizing that immediate gain recognition is required upon a disposition, such as a distribution of stock of the transferee foreign corporation. The decision reinforces the IRS's position on the treatment of such transactions and highlights the importance of considering the entire useful life of transferred intangible property for gain recognition purposes. It may impact future corporate restructuring strategies involving foreign entities and intangible assets, prompting taxpayers to carefully consider the tax implications of electing disregarded entity status in such transactions.