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From the Fiduciary Services Desk

In our last newsletter we wrote that the Pfizer-Allergan inversion merger would result in a taxable gain to U. S. holders of Pfizer, and we touched on charitable gift techniques that could be used to side-step the tax. As readers are probably aware, the Treasury imposed new rules effective April 11th that eliminate much of the tax savings that came from “inverting” to a foreign tax jurisdiction. Pfizer and Allergan promptly called off their merger because the deal was uneconomical without the tax savings. As of this writing Johnson Controls and Tyco are still moving forward with their proposed inversion merger, citing assumptions regarding non-tax savings.

In our prior discussion, we emphasized that steps to give Pfizer to a charity or a charitable trust “must be taken before the merger is approved.” The issue of *timing* implicit in that statement is important in any financial transaction where you are trying to shift tax results from yourself to charity.

Ripening: Timing Considerations for Charitable Gifts of Assets Involved in a Transaction

To avoid a capital gain triggered by a merger, cash buy-out or other transaction, you must give away an asset before the deal “ripens” [yes, “ripens,” a term taken from the decision in *Ferguson v. Commissioner*, 174 F. 3d 997 (9th Cir.1999)]. The IRS will treat a capital gain as having been realized by a taxpayer if the taxpayer gives away the asset after the deal is a sure thing. The argument is that once a deal gets too far down the road, the asset no longer represents traditional equity ownership (in the case of stock), in which the owner can exercise control over shareholder rights, but instead represents cash – that is, only the right to receive the proceeds of the deal.

The ripening point is a moving target, can often be determined only with 20/20 hindsight, and even then is subject to interpretation. For a public transaction (where the shareholder has little control), it is safest to give the stock when the deal is green – soon after announcement. The longer you wait (until after the shareholder votes, until after regulatory approvals, etc.), the more likely you are to be into or beyond the ripening period. Because stock needs to be donated while there is still risk of deal collapse, charitable intent and not avoidance of the potential gain should be of paramount importance. If a deal collapses, capital gains will not be triggered. If the stock has already been transferred to the charity, the donor who put charitable intent second may be disappointed. And as we saw with Pfizer, a deal can go from ripening to rotten overnight.

In 2016, an era of more regulatory oversight and international anti-trust hurdles, the timeline for ripening seems to have expanded. Close to home is the merger between CIGNA and Anthem. Because a portion of the transaction proceeds is in cash, the merger is being treated as a partial taxable sale of CIGNA and will result in capital gain. Some of the usual ripening benchmarks have gone by: the board vote, the shareholder votes, etc. However, on April 6th Connecticut’s comptroller, Kevin Lembo, called for hearings to discuss the merger’s implications for the State employee healthcare system and State premium rates

in light of healthcare industry consolidation. Query whether the protest of a single state comptroller represents enough of a hurdle on the path to deal completion to postpone ripening.

For the sale of closely held business assets, the point of ripening along the path to closing is a dynamic, facts-and-circumstances dependent, determination. Moreover, certain closely held assets and business structures are more difficult to give to charitable vehicles than others. We encourage closely held business clients who may be contemplating a charitable gift of stock or business assets to call their corporate or estate planning attorney to discuss strategy. We can often craft a solution that meets your needs, from a simple direct gift to a charity or community foundation, to a donor-advised fund, all the way to drafting a charitable trust or family foundation, together with walking it through the IRS approval process and handling the investment and administrative aspects.

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