M&A Tax & Technology:

Recent Guidance and Strategies Related to Significant Technology M&A Transactions and Best M&A Tax Practices

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Bryan Keith
Andersen Tax
bryan.keith@andersen.com

Sarah-Jane Morin
Morgan Lewis
sarah-jane.morin@morganlewis.com

Tim Shapiro
Cooley
tshapiro@cooley.com

Myra Sutanto Shen
Wilson Sonsini
msutantoshen@wsgr.com

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Agenda

- QSBS Updates
- Reverse Acquihires
- Bespoke Financing Structures and How to Tax Them
- Tax Terms in M&A Deals
- Tax Diligence in M&A Deals
- Economic Substance in M&A Deals

QSBS Stacking Updates

QSBS History

- July 4, 2025: OBBBA signed into law
- 1202 guidance part of 2025-2026 and 2026-2027 Department of Treasury Priority Guidance plan
- Evan Adams of Treasury at May 9 ABA meeting
  - Confirmed regulations are in process
  - Not limited to OBBBA changes
  - Looking at trust stacking
- Statement from Kenneth Kies (former) Treasury assistant secretary for tax policy and acting IRS chief counsel
  - “We don’t like stacking, OK?”
  - Comments seemed to target more than one trust per family member planning

QSBS Stacking

- Multiply QSBS exclusion cap by (1) setting up multiple trusts to purchase stock or (2) gifting stock to multiple trusts
  - Trusts must be irrevocable nongrantor trusts
- Straightforward example
  - A has three children, J, M and E
    - 3 trusts = $45M in QSBS exclusion (plus A's $15 mil)
    - Questionable: JM trust, ME trust, JE trust etc.
- Possible challenges
  - Assignment of income
  - Economic substance
  - Multiple trust rule (Section 643(f))

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Reverse Acquihires

General Background

- **Traditional Acquihire:** Buyer acquires Target primarily to gain access to Target's workforce
  - This is a full M&A transaction: deal complexity, regulatory scrutiny, etc.
  - Buyer owns Target's business and is exposed to historic liabilities
  - Often, Target's founders are the key employees and the principal stockholders. Common questions regarding tax character of deal payments:
    - Consideration paid for founders' Target stock:
      - favorable tax treatment as long-term capital gains
      - QSBS gain exclusion
    - Compensation paid for founders' services:
      - taxed at ordinary income rates and subject to employment taxes
      - 280G

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General Background

- **"Reverse" Acquihire (a.k.a. "License and Release") Deal:** Buyer hires a portion of Target's workforce without acquiring the Target itself. Buyer typically pays Target for a non-exclusive technology license and release of employees from non-compete and similar obligations
  - Attractive from Buyer's perspective:
    - potential for faster execution
    - obtains access to the particular Target workforce of interest
    - no need to acquire unwanted Target business assets
    - no exposure to Target liabilities

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Reverse Acquihires – Tax Considerations for Target & Continuing Employees

- Buyer's license/waiver payments are generally taxable to Target
  - Availability of NOLs or other tax assets to offset corporate income?
  - State and local tax considerations: apportionment, state NOL suspensions
  - Potential for non-taxable treatment under Section 1032 if Buyer takes ongoing equity stake in Target, subject to commercial and regulatory constraints
- Continuing Employees typically surrender their Target stock for no consideration, and receive new compensation packages from Buyer
  - None of the payment is eligible for favorable LTCG or QSBS treatment
  - Go-forward incentives taxed as compensation

Reverse Acquihires – Target Post-Closing Structures

- **Alternative 1** - Target distributes proceeds and continues as ongoing business
  - Dividend treatment due to current E&P generated by Buyer's license/waiver payment
- **Alternative 2** - Target uses proceeds to redeem preferred stockholders, remaining employees/common stockholders pivot to different business application
  - Potential for "personal holding company" status under Section 542 if, at any time during last half of a taxable year, more than 50% of stock (by value) is owned, directly or indirectly, by or for 5 or fewer individuals
  - Undistributed PHC income (including certain royalties) is subject to a 20% federal penalty tax

Reverse Acquihires – Target Post-Closing Structures (ctd.)

- **Alternative 3** - Target negotiates an M&A exit sale to another buyer
  - Sale price accounts for Target's corporate income tax from the upfront license/wavier payment
  - What about future license/waiver payment entitlements?
    - For benefit of Target stockholders? Upward adjustment to sale price and/or earnout?
    - Reduced by associated taxes? Acquisition of Target may trigger 382 limitations on NOLs that might have otherwise offset taxable income on future license payments.

Bespoke Financing Structures and How to Tax Them

Structures and Themes

- Royalty financings/revenue-based financings
- Asset-backed securitizations
- Data financing structures
- Theme: nondilutive financing tied to specific assets or income streams

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Royalty Financings: Typical Structure

- Investor exchanges upfront cash for the right to a percentage of an existing royalty or license payments
- Nondilutive financing in royalty-based industries (life sciences, music, natural resources)
- Revenue-based financing/customer receipt royalty financing is a similar structure from a tax perspective
- Terms typically include:
  - Upfront payment
  - % of royalty/receipts
  - Repayment cap
  - Term

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Asset-backed Securitizations: Typical Structure

- Pool assets into a special purpose vehicle
- SPV issues bonds or notes
- Often issued in tranches, with different level of risk, credit rating and payout priority
- Purpose: isolate receivables, redistribute risk, finance assets separately
- Traditionally: mortgages, auto loans
- Now: clean energy customer leases and power purchase agreements, bitcoin and other crypto, digital receivables

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Data Center Financing: Typical Structure

- Data center project placed into (or developed by) a special purpose vehicle
- Lender takes collateral in equity ownership of SPV
- Debt (often at a holding company level) is funded through cash distributions from operating subsidiaries
- SPV issues bonds or notes
- Often issued in tranches, with different level of risk, credit rating and payout priority
- Purpose: isolate assets, cross-pledge of equity, easy access to collateral

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Tax treatment

- Possibilities:
  - Debt
  - Sale
  - Equity
- Issues
  - Income recognition for the borrower
  - Characterization of premium for the lender
  - Withholding

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Tax Terms in M&A Deals

What is the objective?

- Buyer
  - Asset basis step up – if available
  - Clean break from sellers/sellers' involvement post-closing
  - Integration with buyer structure
  - Indemnification from pre-ownership tax liabilities
- Seller
  - Most beneficial tax treatment/minimize taxes on transaction proceeds
  - Limit indemnification obligations
  - Get paid for tax attributes

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Key Purchase Agreement Tax Provisions

- Purchase price
- Tax representations of the target/sellers
- Tax indemnification obligations
- Tax covenants
- Tax return preparation
- Post-closing tax actions
- Tax refunds
- Tax contests
- Other

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Purchase Price

- Adjustments
  - Is it adjusted for working capital?
  - Is it adjusted for debt? What is included as debt?
  - Is there a separate adjustment for (known) pre-closing taxes?
- Withholding taxes
- What about transaction tax deductions/benefits?
- Is an allocation necessary? If so, who prepares?

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Tax Representations

- Scope varies (type of deal, public/private, target, RWI, commercial tenor)
- Is there recovery only for breach of reps or is there a separate tax indemnity?
- What happens if there are disclosures regarding a rep on the disclosure schedules?
- How long do the reps survive? Any other limitations?

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Tax Indemnification

- Is there a standalone tax indemnity?
- Are there limitations (deductible/basket, cap)?
- What about a “back door” tax indemnity in the reps or otherwise (e.g., all taxes required to have been paid as of Closing...”)?

Tax Covenants

- Are covenants relevant – simultaneous sign/close? Pre-signing and pre-closing?
- Are sellers required to do any pre-closing restructuring (e.g., F reorg)?

Tax Returns

- Which party prepares which returns?
- Does the counterparty get a say?
- What about elections made by one party that affect the other party (e.g., a Code section 338(g) election)?

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Post-Closing Tax Actions

- What can buyer do post-closing (file VDAs, amend prior year returns)?
- Any limitations? Do the limitations apply if, e.g., the action is required by law?

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Tax Refunds

- Are the parties aware of any specific refunds that may be coming?
- Which party gets the benefit of tax refunds received post-closing?
  - If sellers get the benefit, any limitations (net of taxes/expenses, time limit)?

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Tax Contests

- Who controls? Does the counterparty get to participate?
- Most commonly buyer will want a consent right over settlements, if not an option to fully control.
- Typically, a mutual cooperation provision also applies.

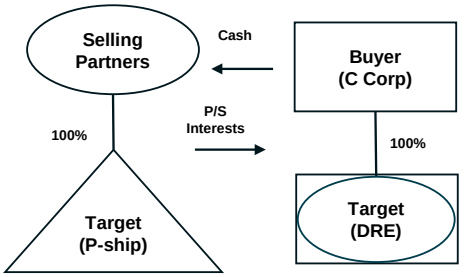
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Other

- Transfer taxes
- Non-US tax considerations (e.g., cross border withholding?)
- 1445/1446 withholding for partnerships
- 1445 withholding for corporations
- BBA issues for partnerships
- Many others!

Tax Diligence in M&A Deals

Diligence Issues – Example 1: Partnership Target & RWI/Tax Insurance

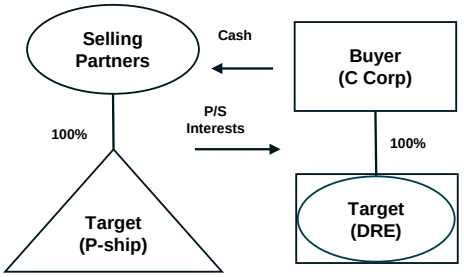


Example 1 Facts:

- Buyer (C Corp) acquires 100% of the outstanding interests of Target (Partnership) from multiple Selling Partners in transaction under Situation 2 of Rev. Rul. 99-6, and Target (Partnership) **ceases to be a tax partnership** in connection with the transaction
- **"Known" Tax Risks**:
  - Target takes positions on its final partnership return that are below "more likely than not level"
- **"Unknown" Tax Risks**:
  - Target has potential tax issues not identified in diligence process

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Diligence Issues – Example 1 (cont.): Partnership Target & RWI/Tax Insurance

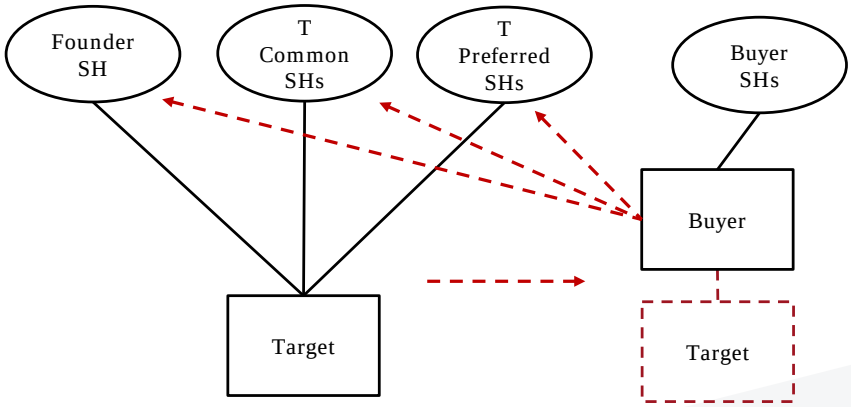


Example 1 Considerations:

- What items were identified in tax diligence? What was the scope of diligence?
- Scope of seller indemnities?
- Will parties to transaction take out RWI/tax insurance with respect to Target?
- Will Target and Selling Partners make a Section 6226 "push-out" election?
  - Do Selling Partners view this as a back door to indemnities that do not expressly exist?
- If no push-out election, what is Target (DRE) and Buyer (C Corp) successor liability related to an imputed underpayment at Target?
  - When is Target treated as if a push-out election had been made? (even though not express election)
- If a push-out election, did Target (Partnership) cease to exist?
  - Did Target cease to exist in hands of Buyer?
- What if transaction is not subject to Rev. Rul. 99-6 and the partnership continues in the hands of Buyer Group?

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Diligence Issues – Example 2: Compensation Considerations

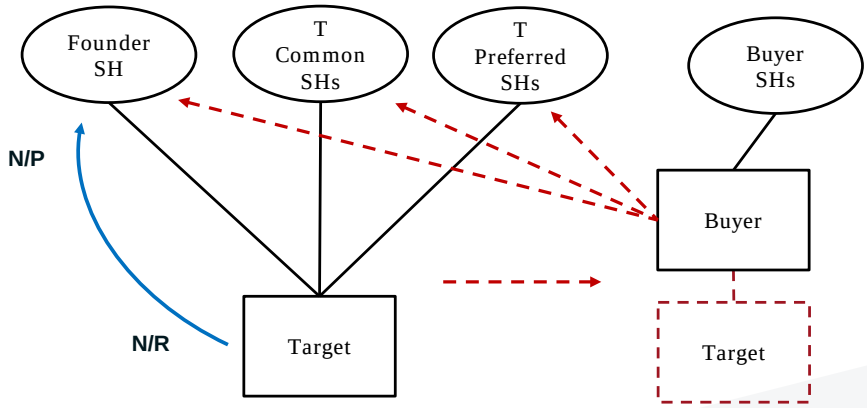


Example 2 Facts: Buyer acquires Target stock for cash

- What if the aggregate purchase price is less than the preference owed to the T Preferred SHs, but the negotiations result in some portion of the proceeds being allocated to the common holders?
- What if the Fonder SH gets more per share for his common than the other T Common SHs?
- What if some of the T common stock is restricted stock subject to vesting? Does the treatment differ depending on whether an "83b election" has been made by the selling shareholder with respect to the T stock being sold?

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Diligence Issues – Example 3: Founder Loan



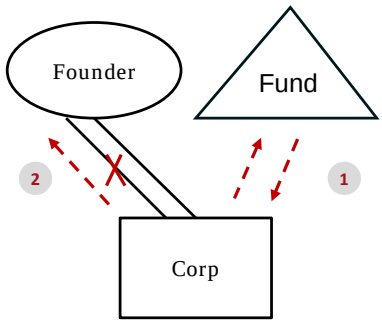
Example 3 Facts: Buyer acquires Target stock for cash, but **Founder SH has a loan payable to Target for more than his proceeds**. Shareholder plans to repay the loan to the extent of is sale proceeds, but Target intends to "waive" the remaining portion of the loan

- What is the treatment to Founder SH of the "waived" portion of the loan?
  - Distribution to Founder SH under REG 1.301-1(j) (formerly "l") (see also, Shepard 340 F2d 27 (1965))
  - Compensation to Founder SH? (see REG. 1.83-4(c) and Rev. Rul. 2004-37)
- What if Founder SH transfers some portion of his Target stock in redemption of such shares immediately before the sale transaction with Buyer?
- Does the amount of Target stock held Founder SH matter?

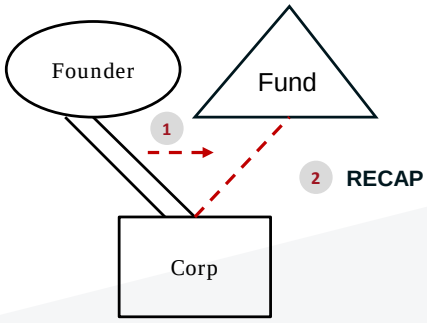
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Diligence Issues – Examples 4 and 5: Primary/Redemption vs Secondary/Recap

Example 4



Example 5



Example 4 Facts: Fund pays Corp $20 per share for Series A preferred stock. Corp redeems some but not all of Founder's common stock for $20 per share when 409A value is $16 per share

- Should the excess of $4 per share be W2 compensation to Founder?
- GAAP considerations?
- See Rev. Rul. 75-447 – Service did not recast Ex. 4 (when no recap); but see Rev. Rul. 2026-20, which distinguished 75-447

Example 5 Facts: Fund pays Founder $20 per share some of Founder's common stock when 409A value is $16 per share. Fund immediately recaps the common into Series A preferred stock

- Any difference? Should the excess of $4 per share be W2 compensation to Founder?

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Economic Substance Doctrine in M&A Deals

Economic Substance Doctrine

- In 2010, Congress added Code Section 7701(o)(1), codifying the judicial economic substance doctrine into a two-part inquiry
- Code Section 7701(o)(1): "In the case of any transaction **to which the economic substance doctrine is relevant**, such transaction shall be treated as having economic substance only if the transaction changes in a meaningful way (apart from Federal income tax effects) the taxpayer's economic position, and the taxpayer has a substantial purpose (apart from Federal income tax effects) for entering into such transaction"
- 2010 Joint Committee on Taxation:
  - Codified ESD is not intended to alter tax treatment of "basic business transactions," merely because the choice between meaningful economic alternatives is largely or entirely based on comparative tax advantages
  - E.g. debt/equity capitalization, use of domestic vs. foreign corporation, series of transactions that constitutes a reorganization

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Recent Caselaw

- *Liberty Global* – 10th Cir. – Apr. 21, 2026:
  - Involved a 4-step transaction designed to generate E&P that would give rise to a dividends-received deduction upon the sale of a foreign subsidiary out from under LG's U.S. tax group. Held that ESD was "relevant" and applied to deny taxpayer $2.4B deduction
  - Relevancy is not a separate threshold inquiry
  - Must analyze transaction holistically. A series of steps, each of which involve "basic business transactions" can still implicate ESD if the overall transaction is complex and designed to achieve a specific tax benefit not intended by Congress
  - For economically meaningless transactions (e.g. DISC tax benefits at issue in *Summa Holdings*), there must be Congressional intent to provide such tax benefit
- *Patel* – Tax Court (on appeal to 5th Cir):
  - Requires threshold relevancy determination before applying codified ESD
  - Is the transaction at issue one where courts have historically applied the common law economic substance doctrine to disallow tax benefits?

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Looking Ahead

- Potential broad and indefinite scope of ESD
  - Contemporaneous documentation of non-tax business reasons for the overall transaction
  - Heightened risk for tax planning that achieves an unusual result or heavily relies on literal operation of code provisions
  - When the transaction involves economically meaningless steps or relies upon a mechanical application of code provisions that lack a non-tax economic justification, query whether:
    - Congress intended those provisions to be applied mechanically *(Liberty Global*), or
    - the common law economic substance doctrine has historically been applied in similar circumstances *(Patel*)

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Thank you