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CLIENT ALERT

Treasury Substantially Pares Back Excise Tax on Stock Repurchases in Final Regulations

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I. Introduction

On November 24, 2025, Treasury published final regulations (the "**Final Regulations**") on Section 4501 of the Code, which imposes an excise tax on certain repurchases of corporate stock ("**Excise Tax**"). The Final Regulations adopt many recommendations provided by commentators and substantially limit the application of the Excise Tax as compared to the proposed regulations published on April 12, 2024 (the "**Proposed Regulations**").

Generally, Section 4501 of the Code imposes a nondeductible excise tax of 1% on repurchases of stock by a U.S. corporation whose stock is traded on an established securities market (a "**Covered Corporation**"), and acquisitions of a Covered Corporation's stock by a specified affiliate of a Covered Corporation.[1] A repurchase is defined as: (i) a redemption within the meaning of Section 317(b) of the Code and (ii) any transaction determined to be "economically similar" to a Section 317(b) redemption. Section 4501 includes a netting rule, which reduces the

[1] The Final Regulations define a "specified affiliate" as, with respect to a corporation, (i) any corporation more than 50% of the stock of which is owned (by vote or by value), directly or indirectly, by the corporation or (ii) any partnership more than 50% of the capital interests or profits interests of which is held, directly or indirectly, by the corporation.

Excise Tax base by the fair market value of stock "issued or provided" by the Covered Corporation during the same tax year, including to employees. In effect, only the net shrinkage of the corporation's equity is taxed. Section 4501 also includes a de minimis exception, under which the Excise Tax does not apply if the fair market value of the stock of a Covered Corporation that is repurchased during the relevant taxable period does not exceed $1,000,000.

The most significant changes in the Final Regulations are discussed below.

II. M&A and Corporate Transactions

(a) "Take Private" and Leveraged Buyout Transactions

Under the Proposed Regulations, unless an exception applies, the portion of the consideration funded by a target corporation in a leveraged buyout or other "take private" transaction would have been treated as a repurchase for purposes of computing the target corporation's Excise Tax base. However, in the Final Regulations, Treasury agreed with commentators that Congress generally did not intend for the Excise Tax to apply to leveraged buyouts and other "take private" transactions that fundamentally restructure corporate ownership or control through combinations of separate business entities. Accordingly, the Final Regulations provide that redemptions by a Covered Corporation that occur as part of a transaction in which the Covered Corporation ceases to be publicly traded are not treated as "repurchases," and therefore, are not subject to the Excise Tax.

(b) Acquisitive Reorganizations

Under the Proposed Regulations, the target corporation in "acquisitive reorganizations"[2] would have been subject to the Excise Tax to the extent of boot received by the target corporation shareholders. Commentators recommended that the Excise Tax should not apply to acquisitive reorganizations because these transactions do not bear the traditional hallmarks of stock repurchase transactions that were the intended focus of the Excise Tax.

Treasury agreed with the commentators that Congress generally did not intend for the Excise Tax to apply to transactions, such as acquisitive reorganizations, that fundamentally restructure corporate ownership or control through combinations of separate business entities. Accordingly, in the case of an acquisitive reorganization in which the target corporation is a publicly traded corporation prior to the transaction, the Final Regulations do not treat the exchange by the target corporation shareholders of their target corporation stock pursuant to the plan of reorganization as a repurchase by the target corporation, even if there is taxable boot exchanged.

In addition, unlike the Proposed Regulations, the Final Regulations allow for the stock of the acquiror issued as a part of the reorganization to be counted by the acquiror as "issued" for purposes of the netting rule, thereby generating a netting rule credit for the acquiror.

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[2] The Final Regulations define "acquisitive reorganizations" to include A, C, D, (a)(2)(D), (a)(2)(E), and G reorganizations.

(c) Single Entity Reorganizations

Under the Proposed Regulations, a recapitalizing corporation in an E reorganization or the transferor corporation in an F reorganization would have been treated as a repurchase to the extent of the FMV of the shares exchanged by its shareholders in the transaction. However, under the reorganizations' exception in the Proposed Regulations, the FMV of the repurchased shares exchanged for qualifying property (that is, non-boot property) would have reduced the corporation's gross repurchase amount. As a result, the corporation would have been subject to the Excise Tax only to the extent of the FMV of its shares repurchased with non-qualifying property (if any).

Treasury agreed with commentators that the issuance of qualifying property in exchange for stock in an E or F reorganization should not be treated as transactions subject to the Excise Tax. Accordingly, the Final Regulations apply the Excise Tax to E reorganizations only if and to the extent that (i) shareholders receive non-qualifying property (that is, boot) and (ii) the receipt of such property is not treated as a distribution under Section 301 of the Code. The result is that E reorganizations in which the recapitalizing corporation's shareholders receive only qualifying property (i) are not treated as repurchases for purposes of the de minimis exception and (ii) do not need to be reported on the Excise Tax return. Because, under traditional F reorganization authorities, any distribution of money or other property from either the transferor corporation or the resulting corporation in an F reorganization is treated as a separate transaction, the Final Regulations do not include an explicit rule treating F reorganizations in which the transferor corporation's shareholders receive non-qualifying property as economically similar transactions.

The Final Regulations also contain a rule providing that stock issued in an E or F reorganization is disregarded for purposes of the netting rule.

(d) Split-Offs

The Proposed Regulations provided that, in the case of a split-off qualifying under Section 355 (or so much of Section 356 of the Code as relates to Section 355) by a distributing corporation that is a Covered Corporation, the exchange by the distributing corporation shareholders of their distributing corporation stock is treated as a repurchase by the distributing corporation. Thus, under the Proposed Regulations, a split-off that involved the exchange of distributing corporation stock solely for qualifying property would be taken into account for purposes of the de minimis exception and would be required to be reported on the Excise Tax return. However, under the reorganizations' exception in the Proposed Regulations, the distributing corporation would be able to reduce its repurchase amount to zero. The Final Regulations generally retain this approach. In addition, the Final Regulations provide that stock issued by the controlled corporation in a split-off does not count for purposes of the netting rule.

(e) Constructive Specified Affiliate Acquisitions

The Proposed Regulations provided that stock of a Covered Corporation is treated as repurchased by the Covered Corporation if a corporation or partnership were to become a specified affiliate of the Covered Corporation, and

shares of the Covered Corporation that were acquired after December 31, 2022 represent more than 1% of the fair market value of such corporation or partnership at the time that such corporation or partnership were to become a specified affiliate of the Covered Corporation. Commentators criticized this rule as overly broad and potentially creating unexpected transaction costs to ordinary M&A transactions. Treasury agreed with commentators, and the Final Regulations do not adopt the constructive specified affiliate acquisition rule.

III. International – Funding Rule

Under Section 4501(d) of the Code, the acquisition of stock of a publicly traded foreign corporation by an "applicable specified affiliate"[3] of the corporation from a person that is not the applicable foreign corporation or a specified affiliate of the corporation will be treated as a repurchase by the specified affiliate that is subject to the Excise Tax (the "**Statutory Foreign Buyback Rule**").

The Proposed Regulations included a funding rule under which an applicable specified affiliate is treated as acquiring the stock of an applicable foreign corporation to the extent that it "funds by any means (including through distributions, debt, or capital contributions), directly or indirectly, a covered purchase with a principal purpose of avoiding the section 4501(d) excise tax" (the "**Proposed Funding Rule**"). The Proposed Funding Rule defined a "principal purpose of avoiding the section 4501(d) excise tax" broadly: "if a principal purpose of the covered funding is to fund, directly or indirectly, a covered purchase, then there is a principal purpose of avoiding the section 4501(d) excise tax." The determination of whether a principal purpose exists was based on all facts and circumstances. The Proposed Regulations also included a rebuttable presumption whereby a principal purpose was presumed to exist if the applicable specified affiliate funded by any means, directly or indirectly, a "downstream relevant entity" and the funding occurred within two years of a covered purchase by or on behalf of the downstream relevant entity. A taxpayer could rebut this presumption if the taxpayer demonstrated facts and circumstances clearly establishing that there was not "a principal purpose" of avoiding the Excise Tax.

The Proposed Funding Rule received severe criticism from commentators, who requested the rule be withdrawn. In light of the criticisms received, the Final Regulations do not adopt the Proposed Funding Rule.

IV. Capital Markets

(a) Straight Preferred Stock

The Proposed Regulations treated repurchases and issuances of preferred stock as subject to the Excise Tax. Commentators argued that preferred stock described in Section 1504(a)(4) of the Code ("**Straight Preferred Stock**") should be excluded from the Excise Tax because repurchases of such stock are more akin to repaying debt and do not implicate the policy concerns underlying the Excise Tax. Treasury agreed with this comment and the Final Regulations provide that Straight Preferred Stock is not treated as "stock" for purposes of the Excise Tax. As

[3] An "applicable specified affiliate" is a specified affiliate of an applicable foreign corporation, other than a foreign corporation or foreign partnership (unless the partnership has a domestic entity as a direct or indirect partner).

a result, repurchases of Straight Preferred Stock are not subject to the Excise Tax and issuances of Straight Preferred Stock do not generate an Excise Tax credit.

(b) Mandatorily Redeemable Stock

The Final Regulations provide transition relief for mandatorily redeemable stock and for stock subject by its terms to a unilateral put option of the holder, if such stock were outstanding prior to August 16, 2022.

V. Other Changes

The Final Regulations contain several other modifications, including:

- Expanding the exemption for repurchases by regulated investment companies to certain funds registered under the Investment Company Act of 1940 that do not qualify as regulated investment companies under the Code.
- Simplifying the procedures by which a Covered Corporation can rebut the presumption that a repurchase is subject to Section 302 or 356(a) of the Code and establishing that the repurchase is a dividend exempt from the Excise Tax.
- Allowing a netting rule credit for Covered Corporation stock provided by a specified affiliate to a non-employee as compensation for services rendered to the specified affiliate.

VI. Applicability Dates

Generally, the Final Regulations apply to repurchases of stock of a Covered Corporation occurring after December 31, 2022 and issuances and provisions of stock of a Covered Corporation occurring during taxable years ending after December 31, 2022. The Final Regulations also contain procedures to claim an Excise Tax refund if a taxpayer previously paid Excise Tax as a result of the application of the Proposed Regulations and prior guidance but would not be required to pay such tax under the Final Regulations.

If you have any questions regarding this client alert, please contact the following attorneys or the Willkie attorney with whom you regularly work.

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