

**Internal Revenue Service**

Department of the Treasury

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Person to Contact:

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Refer Reply To:

**CC:CORP:1-PLR-103647-00**

Date:

**August 11, 2000**

Distributing =

Controlled =

Corporation X =

Corporation Y =

Corporation Z =

State A =

Date A =

Business A =

Business B =

Shareholder 1 =

Shareholder 2 =

Shareholder 3 =

aaa =

bbb =

ccc =

This is a reply to your letter dated February 10, 2000 requesting rulings under § 355 and § 332 of the Internal Revenue Code (the "Code") and other Code sections, as to the federal income tax consequences of a proposed transaction. Additional information was submitted in letters dated March 28, 2000; May 30, 2000; June 16, 2000 and August 3, 2000. The information submitted for consideration is substantially as set forth below.

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Distributing, a publicly traded State A corporation, is the common parent of an affiliated group that files a consolidated federal income tax return. Distributing is a holding company that, through its various tiers of subsidiaries, engages in Business A and Business B. As of Date A, Distributing had three institutional shareholders holding 5 percent or more of Distributing's only class of common stock. Shareholder 1 holds aaa%; Shareholder 2 holds bbb%; and Shareholder 3 holds ccc% of Distributing's shares outstanding.

Corporation X is one of several first-tier subsidiaries wholly owned by Distributing. Corporation X directly engages in Business A. Corporation Z is also a first-tier subsidiary wholly owned by Distributing that directly engages in Business B. Corporation Y is also a first-tier subsidiary wholly owned by Distributing. Corporation holds the trade names associated with Businesses A and B.

Over the past several years, Corporation X has been experiencing tremendous growth. As such, Distributing has focused its energy and resources on growing Business A. Thus, Distributing has enabled Corporation X to make numerous acquisitions funded, at least in part, by the revenue generated by Corporation Z and the other subsidiaries engaged in Business B. Moreover, Corporation Z has been unable to grow either via acquisition or organic expansion because of the redirection by Distributing of the resources of Business B to grow Business A. Corporation Z would like to utilize the strength of its business to grow its own business, as opposed to funding the growth of Corporation X.

Distributing proposes the following steps to effect the transaction:

1. Distributing will cause Corporation Y to merge upstream into Distributing in a merger intended to qualify under § 332.
2. Distributing will contribute all its operations engaged in Business B to Corporation Z and will retain the trade names associated with Business B.
3. Distributing will contribute all its Business A operations, including Corporation X, to Controlled and will contribute the trade names associated with Business A to Controlled.
4. Distributing will distribute, pro rata, the stock of Controlled to its shareholders.

Financial information has been received indicating that Business A and Business B conducted by Corporations X and Z, have each had gross receipts and operating expenses representative of the active conduct of a trade or business for each of the past five years.

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The following representations have been made by the taxpayer in connection with Step 1:

- (a) Distributing, on the date of adoption of the plan of complete liquidation, and at all times until the final liquidating distribution is completed, will be the owner of at least 80 percent of the single outstanding class of stock of Corporation Y.
- (b) No shares of Corporation Y stock will have been redeemed during the three years preceding the adoption of the plan of complete liquidation of Corporation Y.
- (c) Distributions from Corporation Y to Distributing pursuant to the plan of complete liquidation will be made within a single taxable year of Corporation Y.
- (d) As soon as the first liquidating distribution has been made, Corporation Y will cease to be a going concern and its activities will be limited to winding up its affairs, paying its debts, and distributing its remaining assets to its shareholders.
- (e) Corporation Y will retain no assets following the final liquidating distribution.
- (f) The liquidation of Corporation Y will not be preceded or followed by the reincorporation in, or transfer or sale to, a recipient corporation of any of the businesses or assets of Corporation Y, if persons holding, directly or indirectly, more than 20 percent in value of the Corporation Y stock also hold, directly or indirectly, more than 20 percent in value of the stock in the recipient corporation. For purposes of this representation, ownership will be determined immediately after the Spin-Off and by application of the constructive ownership rules of section 318(a) of the Code as modified by section 304(c)(3).
- (g) Prior to the adoption of the liquidation plan, no assets of Corporation Y will have been distributed in kind, transferred, or sold to Distributing, except for transactions occurring in the ordinary course of business and transactions occurring more than three years prior to adoption of the liquidation plan.
- (h) Corporation Y will report all earned income represented by assets that will be distributed to its shareholders such as receivables being reported on a cash basis, unfinished construction contracts, commissions due, etc.
- (i) The fair market value of the assets of Corporation Y will exceed its liabilities both at the date of the adoption of the plan of complete liquidation and immediately prior to the time the first liquidating distribution is made.
- (j) Distributing is not an organization that is exempt from federal income tax under

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section 501 or any other provision of the Code.

The following representations have been made by the taxpayer in connection with Steps 2, 3 and 4:

- (a) Any indebtedness owed by Controlled to Distributing will not constitute stock or securities.
- (b) No part of the consideration distributed by Distributing will be received by a shareholder of Distributing as a creditor, employee or in any capacity other than that of a shareholder in Distributing.
- (c) The five years of financial information submitted on behalf of Corporation Z is representative of the corporation's present operations and with regard to such corporation, there have been no substantial operational changes since the date of the last financial statement submitted.
- (d) Immediately after the Distribution, at least 90% of the fair market value of the gross assets of Distributing will consist solely of the stock and securities of Corporation Z, a controlled corporation engaged in the active conduct of a trade or business as defined in Section 355(b)(2).
- (e) Immediately after the Distribution, at least 90% of the fair market value of the gross assets of Controlled will consist solely of the stock and securities of Corporation X, a controlled corporation that is engaged in the active conduct of a trade or business as defined in Section 355(b)(2).
- (f) There is no plan or intention by Distributing or Controlled, directly or through any subsidiary corporation, to purchase any of its outstanding stock after the transaction, other than through stock purchases meeting the requirements of Section 4.05(1)(b) of Revenue Procedure 96-30.
- (g) The Distribution is being undertaken to permit the management of Business A and Business B each to focus more completely on developing and expanding its own business. The Distribution is motivated, in whole or in part, by this corporate business purpose.
- (h) There is no plan or intention to liquidate either Distributing or Controlled, to merge either Distributing or Controlled with any other corporation, or to sell or otherwise dispose of the assets of either corporation after the transaction, except for transactions in the ordinary course of business.
- (i) Immediately before the Distribution, items of income, gain, loss, deduction and

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credit will be taken into account as required by the intercompany transaction regulations (See §1.1502-13 and § 1.1502-14 as in effect before the publication of T.D. 8597, 1995-32 I.R.B. 6, and as currently in effect; § 1.1502-13 as published by T.D. 8597). Further, Distributing's excess loss account with respect to Controlled's common stock, if any, will be included in income immediately before the Distribution (See § 1.1502-19).

- (j) There is no plan or intention by any shareholder who owns five percent or more of the stock of Distributing, and the management of Distributing, to the best of its knowledge, is not aware of any plan or intention on the part of any remaining shareholder of Distributing, to sell, exchange, transfer by gift, or otherwise dispose of any stock in, or securities of, either Distributing or Controlled after the transaction.
- (k) Payments made in connection with all continuing transactions between Distributing (and its subsidiaries) and Controlled (and its subsidiaries) will be for fair market value, based on terms and conditions arrived at by the parties bargaining at arm's length.
- (l) Neither Distributing nor Controlled is, or will be, an investment company as defined in §§ 368(a)(2)(F)(iii) and (iv).
- (m) To the best knowledge of the management of Distributing and Controlled, the proposed distribution of Controlled is not part of a plan or a series of related transactions pursuant to which one or more persons would acquire, directly or indirectly, stock representing a 50% or greater interest in Distributing or Controlled. To the best knowledge of the management of Distributing and Controlled, there is no plan or intention on the part of one or more persons to enter into a plan or a series of related transactions pursuant to which such person or persons would acquire, directly or indirectly, a 50 percent or greater interest in Controlled.

Based solely on the information submitted and on the representations set forth above, it is held as follows in connection with Step 1:

- (a) The Liquidation will qualify as a complete liquidation of Corporation Y within the meaning of section 332.
- (b) No gain or loss will be recognized by Distributing on receiving the assets and liabilities of Corporation Y in the Liquidation. Section 332 (a).
- (c) No gain or loss will be recognized by Corporation Y on the distribution of its assets to, or the assumption of its liabilities by, Distributing. Sections 336(d)(3),

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337(a), and 337(b)).

- (d) Distributing's basis in each asset received from Corporation Y as a result of the Liquidation will equal the basis of that asset in the hands of Corporation Y immediately before the Liquidation. Section 334(b)(1).
- (e) Distributing's holding period in each asset received from Corporation Y as a result of the Liquidation will include the period during which that asset was held by Corporation Y. Section 1223(2).
- (f) Distributing will succeed to and take into account the items of Corporation Y described in section 381(c), subject to the conditions and limitations specified in sections 381, 382, 383, and 384 and the regulations thereunder. Sections 381(a) and 1.381(a)-1.
- (g) Except to the extent Corporation Y's earnings and profits are reflected in Distributing's earnings and profits, Distributing will succeed to and take into account the earnings and profits, or deficit in earnings and profits, of Corporation Y as of the date of the Liquidation. Sections 381(c)(2)(A), 1.381(c)(2)(1), and 1.1502-33(a)(2). Any deficit in the earnings and profits of Corporation Y or Distributing will be used only to offset earnings and profits accumulated after the date of the Liquidation. Section 381(c)(2)(B).

Based solely on the information submitted and on the representations set forth above, it is held as follows in connection with Steps 2, 3 and 4:

- (h) The Contribution of the Business A assets to Controlled, followed by the distribution, will be a reorganization under § 368(a)(1)(D). Distributing and Controlled will each be a "party to the reorganization" within the meaning of Section 368(b).
- (i) No gain or loss will be recognized by Distributing on the transfer of the stock of Corporation X in exchange for Controlled stock. Section 361(a) and 357(a).
- (j) No gain or loss will be recognized by Controlled on the receipt of the stock of Corporation X in exchange for Controlled stock. Section 1032(a).
- (k) Controlled's basis in the assets received from Distributing will equal the basis of that asset in the hands of Distributing immediately before the contribution of such assets to Controlled. Section 362(b).
- (l) The holding period of each asset contributed to Controlled by Distributing will

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include the period during which Distributing held that asset before the Contribution. Section 1223(2).

- (m) No gain or loss will be recognized by Distributing on the Distribution. Section 361(c)(1).
- (n) No gain or loss will be recognized by (and no amount will otherwise be included in the income of) the holders of Distributing common stock on receipt of Controlled common stock pursuant to the Distribution. Section 355(a)(1).
- (o) The holding period of Controlled common stock received by holders of Distributing common stock will include the holding period of the Distributing common stock on which the Distribution is made, provided the Distributing common stock is held as a capital asset on the date of the Distribution. Section 1223(1)(B).
- (p) The earnings and profits of the Distributing and Controlled will be allocated as provided in §§ 312(h), 1.312-10(a) and 1.1502-33(f)(2).
- (q) The aggregate basis of the Distributing common stock and the Controlled common stock in the hands of a holder of Distributing stock will equal the aggregate basis of the Distributing common stock held immediately before the Distribution by that shareholder, allocated between the Distributing common stock and the Controlled common stock in proportion to the relative fair market value of each on the date of the Distribution. Section 358(a)(1) and (b) and Treas. Reg. § 1.358-2(a)(2).
- (r) Immediately before the Distribution, all intercompany obligations existing between Distributing or any of its subsidiaries, and Controlled or any of its subsidiaries (as broadly defined in §1.1502-13(g)(2)) will be treated as satisfied for cash in an amount equal to its fair market value. See §1.1502-13(g)(3)(ii)(A). Such intercompany obligation will then be treated as new debt issued for an amount of cash equal to its fair market value immediately after the Distribution. See §1.1502-13(g)(3)(iii).

No opinion is expressed about the tax treatment of the proposed transaction under other provisions of the Code and regulations or about the tax treatment of conditions existing at the time of, or effects resulting from, the proposed transactions that are not specifically covered by the above rulings.

This ruling is directed only to the taxpayer(s) requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

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A copy of this letter should be attached to the federal income tax returns of the taxpayers involved for the taxable year in which the transactions covered by this ruling are consummated.

Sincerely,  
Associate Chief Counsel (Corporate)  
By: Mark Jennings  
Acting Chief, Branch 1