

Internal Revenue Service

Department of the Treasury

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Distributing =

Controlled =

S1 =

S2 =

Newco =

business m =

business n =

business o =

State Z =

Shareholder A =

Shareholder B =

Shareholder C =

aa =

bb =

cc =

Date a =

Date b =

Date c =

\$xxx =

This is in response to a letter dated July 26, 2000, for rulings concerning the federal income tax consequences of a proposed transaction. Additional information was submitted September 21, 2000, November 27 and November 28. The material information submitted for consideration is summarized below.

Distributing, a State Z corporation, is a holding company and the common parent of a consolidated group. Distributing wholly owns Controlled, a State Z corporation engaged in business m, S1 a State Z corporation engaged in business n, and S2, a State Z corporation engaged in business o. Distributing has three shareholders, Shareholder A, Shareholder B and Shareholder C (collectively "the Shareholders"), who own aa%, bb%, and cc% interests, respectively. Distributing acquired control of Controlled on Date a, from the Shareholders in a transaction qualifying under § 351 in which no party to the transaction recognized gain or loss. Distributing, Controlled, S1 and S2 each use the accrual method of accounting for their federal income tax returns, and have a taxable year ending on Date b.

We have received financial information indicating that business m, business n

and business o each had gross receipts and operating expenses representative of the active conduct of a trade or business for each of the past five years.

Significant disagreements between the Shareholders have taken place which have adversely effected the management and operations of Controlled, S1 and S2. Accordingly, the directors of Distributing propose the following transaction.

(1) Pursuant to an executed Agreement and Plan of Corporate Separation and Reorganization, signed on Date c, S1 and S2 declared and paid dividends totaling \$xxx to Distributing on Date c, who transferred the full amount of such dividends to Controlled on the following day.

(2) Distributing will distribute all of the Controlled stock to Shareholder A in exchange for all of Shareholder A's Distributing stock.

(3) Shareholder A will contribute all of Controlled stock to Newco in exchange for all of the Newco stock, pursuant to a § 351 transaction.

Following the transaction Controlled will be owned by Newco, which is wholly owned by Shareholder A, and Distributing will be owned by Shareholder B and Shareholder C.

The taxpayers have made the following representations in connection with the proposed transaction:

(a) The fair market value of the Controlled stock to be received by Shareholder A will be approximately equal to the fair market value of the Distributing stock surrendered in the exchange.

(b) No part of the consideration to be distributed by Distributing will be received by a shareholder as a creditor, employee, or in any capacity other than that of a shareholder of the corporation.

(c) The 5 years of financial information submitted on behalf of Controlled, S1 and S2, is representative of such corporation's present operations, and with regard to such corporations, there have been no substantial operational changes since the date of the last financial statements submitted.

(d) Following the transaction, at least 90% of the fair market value of the gross assets of Distributing will consist of stock and securities of S1 and S2, the controlled corporations, that are engaged in the active conduct of a trade or business as defined in § 355(b)(2) of the Code.

(e) Following the transaction, Controlled, S1 and S2 will each continue the active conduct of its trade or business, independently and with its separate employees.

(f) The proposed distribution of the stock of Controlled is carried out for the following corporate business purpose: to end shareholder disputes, resolve management deadlock and alleviate associated inefficiencies. The distribution of the stock of Controlled is motivated, in whole or substantial part, by the above corporate business purpose.

(g) Distributing is not a S corporation (within the meaning of § 1361(a)), and there is no plan or intention by Distributing or Controlled to make an S corporation election pursuant to § 1362(a), nor for anyone to make an election for Distributing or Controlled to be treated as a qualified subchapter S subsidiary within the meaning of §1361(b)(3)(B).

(h) There is no plan or intention by any shareholders of Distributing to sell, exchange, transfer by gift, or otherwise dispose of any of their stock in either Distributing, Controlled or Newco after the transaction (except for the planned transfer of stock of Controlled to Newco as described in step (3) of the proposed transaction).

(i) There is no plan or intention by either Distributing or Controlled, directly or through any subsidiary corporation, to purchase any of its outstanding stock after the transaction.

(j) There is no plan or intention to liquidate either Distributing or Controlled, to merge either corporation with any other corporation, or to sell or otherwise dispose of the assets of either corporation after the proposed transaction, except in the ordinary course of business.

(k) No intercorporate debt will exist between Distributing and Controlled at the time of, or subsequent to, the distribution of Controlled stock.

(l) Immediately before the proposed distribution, items of income, gain, loss, deduction, and credit will be taken into account as required by the applicable intercompany transaction regulations. Further, Distributing's excess loss account with respect to the Controlled stock (and Controlled's excess loss account, if any, with respect to any subsidiary stock) will be included in income immediately before the proposed distribution.

(m) Payments made in connection with all continuing transactions, if any, between Distributing (and its affiliates) and Controlled (and its affiliates), will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's

length.

(n) No two parties to the transaction are investment companies as defined in §§ 368(a)(2)(F)(iii) and (iv).

(o) The distribution is not part of a plan or series of related transactions (within the meaning of § 355(e)) pursuant to which one or more persons will acquire directly or indirectly stock possessing 50% or more of the total combined voting power of all classes of stock of either Distributing or Controlled, or stock possessing 50% or more of the total value of all classes of stock of Distributing or Controlled.

(p) The transfer of stock of Controlled by Shareholder A to Newco will qualify under § 351 of the Code.

Based solely on the information submitted and the representations as set forth above it is held as follows:

(1) Distributing will recognize no gain or loss on the distribution of the Controlled stock to Shareholder A.

(2) Shareholder A will recognize no gain or loss (and no amount will be included in Shareholder A's income) upon receipt of Controlled stock in exchange for Shareholder A's Distributing stock (§ 355(a)(1)).

(3) The basis of the Controlled stock received by Shareholder A in the transaction will equal the basis of the Distributing stock surrendered in exchange therefor (§ 358(a)(1)).

(4) The holding period of the Controlled stock received by Shareholder A in the transaction will include the holding period of the Distributing stock surrendered in exchange therefor, provided Shareholder A held the Distributing stock as a capital asset on the date of the distribution (§ 1223(1)).

(5) Proper allocation of earnings and profits between Distributing and Controlled will be made under §§ 1.312-10 and 1.1502-33 of the Income Tax Regulations.

Except as specifically set forth above, no opinion is expressed concerning the federal tax consequences of the proposed transaction under any other provision of the Code and regulations, or about the tax treatment of any conditions existing at the time of, or effects resulting from the proposed transaction.

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 transaction covered by this ruling letter is consummated.

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.

Pursuant to a power of attorney on file in this office, a copy of this letter has been sent to your authorized representative.

Sincerely yours,

Associate Chief Counsel (Corporate)

By: *Ken Cohen*

Ken Cohen
Senior Technical Reviewer, Branch 3