

**Internal Revenue Service**

Department of the Treasury

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Person to Contact:

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Date:

June 6, 2001

Distributing	=
Controlled	=
Bank	=
Subsidiary 1	=
Subsidiary 2	=
Subsidiary 3	=
Subsidiary 4	=
State A	=
Business X	=
Business Y	=
N	=
P	=

This letter responds to your letter dated January 26, 2001, in which you requested a ruling as to the federal income tax consequences of a proposed transaction. Additional information was provided in letters dated March 20, 2001, April 7, 2001, and April 5, 2001. The information you submitted is summarized below.

Distributing is a privately held corporation organized under the laws of State A. Distributing is a fiscal year, accrual method taxpayer that has been indirectly engaged, as the common parent of an affiliated group of corporations that file a consolidated tax return, in Business X. Specifically, Distributing has been engaged in Business X through Subsidiary 1, Subsidiary 2, Subsidiary 3, and Subsidiary 4, all of which are directly engaged in Business X. Currently, Distributing has N shares of voting and non-voting common stock outstanding.

Controlled is a wholly owned subsidiary of Distributing that was organized under the laws of State A. Controlled is directly engaged in Business Y. Controlled has a single class of P shares of common stock outstanding.

Currently, Controlled is facing severe competition from competitors engaged in Business Y. To offer its customers products and services commensurate with those offered by its competitors, and to attain funds at a lower cost, Controlled seeks to merge with Bank, an unrelated State A corporation. However, a merger of Controlled into Bank is prohibited by applicable banking laws because of the non-bank related assets held by Distributing. Therefore, the following transactions have been proposed:

- 1) Distributing will distribute pro rata all of the stock of Controlled to its shareholders (the "Distribution").
- 2) The shareholders of Distributing will immediately contribute the Controlled shares they received in the Distribution to a newly formed holding company solely in exchange for the holding company's stock (the "Contribution"). The Contribution is intended to qualify as tax free under § 351.
- 3) Within twelve months from the date of the Distribution, Controlled will be merged into Bank, with Bank surviving (the "Merger"). The Merger is intended to qualify as a tax-free reorganization under § 368(a)(2)(D). The Contribution and Merger (the "Subsequent Transactions") will not, either individually or collectively, constitute an acquisition of a "50-percent or greater interest" (within the meaning of § 355(e)(2)(A)(ii)) in Controlled.

The following representations have been made in connection with the proposed transactions:

- (a) 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.
- (b) The five years of financial information submitted on behalf of Distributing, Subsidiary 1, Subsidiary 2, Subsidiary 3, and Subsidiary 4 is representative of the corporations' present operations, and with regard to such corporations, there have been no substantial operational changes since the date of the last financial statements submitted.
- (c) The five years of financial information submitted on behalf of Controlled is representative of the corporation's present operations, and with regard to such corporation, there has been no substantial operational changes since the date of the last financial statements submitted.

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

(e) Following the transaction, Distributing, Subsidiary 1, Subsidiary 2, Subsidiary 3, Subsidiary 4, and Controlled will each continue the active conduct of its business, independently and with its separate employees.

(f) The Distribution is carried out for the following corporate business purpose: to facilitate an acquisition of Controlled by Bank. The Distribution of Controlled is motivated, in whole or substantial part, by this corporate business purpose.

(g) Except for the Subsequent Transactions, there is no plan or intention by the shareholders of Distributing to sell, exchange, transfer by gift, or otherwise dispose of any of their stock in Distributing or Controlled after the transaction.

(h) 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, other than through stock purchases meeting the requirement of section 4.05(1)(b) of Rev. Proc. 96-30.

(i) Except for the Subsequent Transactions, 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 transaction, except in the ordinary course of business.

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

(k) Immediately before the Distribution, items of income, gain, loss, deduction, and credit will be taken into account as required by the applicable intercompany transaction regulations. Furthermore, Distributing's excess loss account with respect to the Controlled stock, if any, will be included in income immediately before the distribution (see § 1.1502-19).

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

(m) 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 either

Distributing or Controlled.

(n) The Contribution will satisfy the statutory and judicial requirements of § 351.

(o) The Merger will satisfy the statutory and judicial requirements of § 368(a)(2)(D).

Based solely on the facts submitted and the representations made above, it is held as follows:

- (1) No gain or loss will be recognized by Distributing on the distribution of all the stock of Controlled to its shareholders (§ 355(c)).
- (2) No gain or loss will be recognized by (and no amount will otherwise be included in the income of) Distributing's shareholders on their receipt of the Controlled common stock in the Distribution (§ 355(a)(1)).
- (3) The basis of the Distributing and Controlled stock in the hands of Distributing's shareholders will be the same as the basis of Distributing's stock held immediately before the Distribution, allocated in proportion to the fair market value of each in accordance with section § 1.358-2(a)(2) (§ 358(a)(1) and (b)).
- (4) The holding period of the Controlled common stock received by each Distributing shareholder in the Distribution will include the holding period of the Distributing stock held by such shareholder immediately before the Distribution, provided that such shareholder held the Distributing stock as a capital asset on the date of the Distribution (§ 1223(1)).
- (5) As provided in § 312(h), proper allocation of earnings and profits between Distributing and Controlled will be made under §§ 1.312-10(b) and 1.1502-33(e).

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 any conditions existing at the time of, or effects resulting from, the proposed transaction that are not directly covered by the above rulings. We specifically express no opinion on the qualification of the Contribution as a § 351 transaction or the qualification of the Merger as a § 368(a)(2)(D) reorganization.

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.

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.

Sincerely,  
Associate Chief Counsel (Corporate)  
By: Michael J. Wilder  
Senior Technician Reviewer