Internal Revenue Service

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Department of the Treasury

Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:
CC:ITA:2 – PLR-112101-02
Date:
January 31, 2003

In Re:

LEGEND:

A =

B =

C =

D =

E =

F =

G =

H =

Family =

Company 1 =

Company 2 =

Company 3 =

Company 4 =

Partnership =

Trust =

Year =

Dear :

This is in response to your private letter ruling request on behalf of A, B, C, D, E, F, G, and H (the Taxpayers) dated January 31, 2002. The Taxpayers request a ruling on whether the proposed contributions of shares of Company 1 ADSs (defined below) to one or more private foundations or charitable remainder trusts of which private foundations are or may be remaindermen constitute contributions of "qualified appreciated stock" within the meaning of § 170(e)(5) of the Internal Revenue Code.

RULING REQUESTED

The Taxpayers request the following ruling:

Do the Company 1 ADSs that the Taxpayers plan to contribute to the Donees constitute "qualified appreciated stock" within the meaning of § 170(e)(5)(B) of the Internal Revenue Code?

CONCLUSION

Yes. The Company 1 ADSs that the Taxpayers plan to contribute to the Donees constitute "qualified appreciated stock" within the meaning of § 170(e)(5)(B).

FACTS

Immediately prior to the merger transactions described below, Partnership, a general partnership, the sole partners of which are the Taxpayers and Trustees of trusts for the benefit of the Taxpayers under the Trust, owned common shares of Company 2 for a period exceeding one year.

In Year, Company 2, Company 3, and Company 4 completed a series of merger transactions, which resulted in the formation of Company 1 (the Merger).

Pursuant to the Merger, Partnership received Company 1 American Depository Shares (ADSs) in exchange for its Company 2 common shares. An ADS is issued by as U.S. depository bank and represents an interest in the underlying ordinary shares of a non-U.S. company. An ADS is evidenced by an American Depository Receipt (an ADR). An ADR is a negotiable receipt issued in certificate form representing an ADS. The

holder of an ADR is entitled to demand delivery of the underlying shares. Each Company 1 ADS represents one ordinary share of Company 1. The number of Company 1 ADSs received was determined pursuant to a specific exchange ratio for each Company 2 common share owned. The Company 1 ADSs are traded on the New York Stock Exchange. The Company 1 ADSs are the equivalent of an ADR pursuant to the Merger agreement, which states that direct holders of Company 1 ADSs whose ownership is registered on the books of the depository are Company 1 ADR holders.

Partnership is prepared to distribute a portion of its Company 1 ADSs to the Trustees of Trust, and the Trustees of Trust, in turn, are prepared to distribute those Company 1 ADSs to the Taxpayers. The Taxpayers presently intend to contribute some Company 1 ADSs to one or more private foundations or charitable remainder trusts of which private foundations may be the remaindermen (the Donees). At the time of the contributions, the foundations will be private foundations within the meaning of § 509(a), and not foundations described in § 170(b)(1)(E). Each charitable remainder trust will be for the benefit of a Taxpayer (or a Taxpayer and one or more family members of the Taxpayer, or just for one or more family members of a Taxpayer) for a specified period and, at the end of such period, will terminate and the assets will pass to one or more charitable organizations, which may be private foundations.

It is anticipated that the basis of the Company 1 ADS to be contributed by each Taxpayer will be less than the fair market value on the dates of the contributions.

The total value of the Company 1 ADS to be contributed to the Donees by all of the Taxpayers will be less than 10% (in value) of the outstanding Company 1 stock (including ADSs).

The Company 1 ADSs that the Taxpayers propose to contribute are subject to certain contractual and statutory limitations on their transferability.

In connection with the Merger, Partnership, certain Taxpayers and other members of the Family and other entities related to the Family (the Family Shareholders) entered into the Governance Agreement with Company 1. Under the Governance Agreement, the Family Shareholders may contribute Company 1 ADSs to the Donees without restriction. Such contributed Company 1 ADSs may be sold by the Donees without restriction.

The Company 1 ADSs acquired by Donees pursuant to the proposed transaction will be subject to Rule 145 of the General Rules and Regulations promulgated under the Securities Act of 1933, as amended (the Securities Act), because such securities were originally acquired in the Merger. The Merger constituted a Rule 145(a) transaction under that rule. Rule 145 of the Securities Act imposes certain limitations on the "offer" or "sale" of securities acquired in a Rule 145(a) transaction. In general, Rule 145 of the Securities Act, 17 C.F.R. § 230.145 (2001), provides that securities acquired in a “Rule

145(a) transaction" such as the Merger may be resold without the selling party being deemed an underwriter of registered securities under the Securities Act if certain provisions of Rule 144 are followed. In particular, the following conditions must be met:

1. adequate current information is available about the issuer of the securities prior to resale;
2. the amount of restricted securities sold in any three-month period is limited to the greater of (i) one percent of the shares outstanding as shown by the then most recent report or statement published by the issuer, and (ii) the average weekly reported trading volume of the shares during the four calendar weeks preceding the sale; and
3. the securities may only be sold in "brokers transactions" within the meaning of Section 4(4) of the Act.

The Taxpayers have taken steps to ensure that the Donees will be able to sell the contributed ADSs in compliance with Rule 145. The Taxpayers represent that the aggregate contributions to the Donees will be limited such that the total number of Company 1 ADSs contributed by the Taxpayers to the Donees (including any ADSs already held by Donees) will be substantially less than 1% of the shares outstanding of Company 1 as shown by the most recent report or statement published by Company 1. The Taxpayers also represent that contributions will be made by the Donees only at such times when, to the best of their knowledge, there will not be any proposed recapitalization, tender or exchange offer, stock repurchase program or similar plan that would have the effect of substantially reducing the number of outstanding shares of Company 1 within the 3-month period following the contribution.

The Taxpayers will, prior to the proposed contribution, provide a statement to the Donees that the requirements of Rule 145 are met for all transfers of the Company 1 ADSs by the Taxpayers and that the Taxpayers will not take any steps that will prevent the Donees from making transfers of Company 1 ADSs free of any Rule 145 resale restrictions.

The Taxpayers represent that, at the time of the contributions, the contributed Company 1 ADSs (i) in the hands of each of Partnership and the Taxpayers will be deemed, under § 1223(1) to have been held by each of Partnership and the Taxpayers for more than one year from the date such ADSs were acquired by each of them and (ii) will not come within any of the exceptions set forth in subsections (1) through (5) of § 1221. In addition, the Taxpayers anticipate that the fair market value of the Company 1 ADSs on the contribution date will be more than the adjusted basis of the ADSs.

LAW

Section 170(a) of the Code allows a deduction for any charitable contribution (as defined in § 170(c)) payment of which is made within the taxable year.

Section 1.170A-1(c)(1) of the Income Tax Regulations states that if a charitable contribution is made in property other than money, the amount of the contribution is the fair market value of the property at the time of the contribution reduced as provided in § 170(e)(1) and paragraph (a) of § 1.170A-4.

Section 170(e)(1)(B)(ii) of the Code provides that in the case of charitable contributions to or for the use of a private foundation (as defined in § 509(a)), other than a private foundation described in § 170(b)(1)(E), the amount of the charitable contribution of property otherwise taken into account under § 170 is reduced by the amount of gain that would have been long-term capital gain if the property contributed had been sold by the taxpayer at its fair market value (determined at the time of the contribution).

Section 170(e)(5)(A) of the Code states that § 170(e)(1)(B)(ii) does not apply to any contributions of "qualified appreciated stock."

Section 170(e)(5)(B) of the Code defines "qualified appreciated stock," except as provided in § 170(e)(5)(C), to mean any stock of a corporation (i) for which (as of the date of the contribution) market quotations are readily available on an established securities market, and (ii) which is capital gain property (as defined in § 170(b)(1)(C)(iv)).

Section 170(e)(5)(C)(i) of the Code provides that, in the case of any donor, the term "qualified appreciated stock" shall not include any stock of a corporation contributed by the donor in a contribution to which § 170(e)(1)(B)(ii) applies (determined without regard to § 170(e)(5)) to the extent that the amount of the stock so contributed (when increased by the aggregate amount of all prior such contributions by the donor of stock in such corporation) exceeds 10 percent (in value) of all of the outstanding stock of such corporation. For purposes of § 170(e)(5)(C)(i), an individual shall be treated as making all contributions made by any member of his family (as defined in § 267(c)(4)). Section 170(e)(5)(C)(ii).

Section 170(b)(1)(C)(iv) of the Code defines the term "capital gain property" to mean, with respect to any contribution, any capital asset the sale of which at its fair market value at the time of the contribution would have resulted in gain which would have been long-term capital gain.

Section 1222(3) of the Code defines "long-term capital gain" to mean gain from the sale or exchange of a capital asset held for more than one year, if and to the extent the gain is taken into account in computing gross income.

Section 1221 of the Code defines the term "capital asset" to mean property held by the taxpayer (whether or not connected with his trade or business) but does not include (1) stock in trade; (2) certain property used in a trade or business; (3) certain property that is the product of the taxpayer's personal efforts; (4) accounts or notes receivable; (5) certain publications of the United States government; (6) certain commodities derivative financial instruments; (7) certain hedging transactions; and (8) certain supplies.

ANALYSIS

For stock to be "qualified appreciated stock," it must meet the requirements of § 170(e)(5)(B) of the Code.

Section 170(e)(5)(B)(i) requires that market quotations for the stock be readily available on an established securities market as of the date of the contribution. The market quotations requirement has the same meaning for the purpose of defining qualified appreciated stock and in determining when securities are publicly traded (so as to exempt a donor from the substantiation requirements of § 1.170A-13(c)). Todd v. Commissioner, 118 T.C. 354 (April 19, 2002). The definition of an established securities market for purposes of determining when securities are publicly traded (so as to exempt a donor from the substantiation requirements) is in § 1.170A-13(c)(7)(xi) of the regulations. Section 1.170A-13(c)(7)(xi)(A)(1) provides that, for purposes of § 1.170A-13, market quotations are readily available on an established securities market with respect to a security if the "security is listed on the New York Stock Exchange, the American Stock Exchange, or any city or regional exchange in which quotations are published on a daily basis, including foreign securities listed on a recognized foreign, national, or regional exchange in which quotations are published on a daily basis." Company 1 ADSs are traded on the New York Stock Exchange. Accordingly, market quotations for Company 1 ADSs are readily available on an established securities market.

We further conclude that Company 1 ADSs are stock for purposes of § 170(e)(5). An ADS is issued by a U.S. depository bank and represents an interest in the underlying ordinary shares of a non-U.S. company. An ADS is evidenced by an American Depository Receipt (an ADR). An ADR is a negotiable receipt issued in certificate form representing an ADS. The holder of an ADR is entitled to demand delivery of the underlying shares. Each Company 1 ADS represents one ordinary share of Company 1. The Company 1 ADSs are the equivalent of an ADR pursuant to the Merger agreement, which states that direct holders of Company 1 ADSs whose ownership is registered on the books of the depository are Company 1 ADR holders. The Service has interpreted ADRs to be treated as shares of stock for various tax purposes, such as the foreign tax credit, Rev. Rul. 65-218, 1965-2 C.B. 566, and the interest equalization tax, Rev. Rul. 72-271, 1972-1 C.B. 369. Therefore, for purposes of

§ 170(e)(5), Company 1 ADSs are stock for which market quotations are readily available on an established securities market.

The Taxpayers represent that the Taxpayers have taken steps to ensure that the Donees will be able to sell the contributed ADSs in compliance with Rule 145. The Taxpayers also represent that the aggregate contributions of the Donees will be limited such that the total number of Company 1 ADSs contributed by the Taxpayers to the Donees (including any ADSs already held by the Donees) will be substantially less than 1% of the shares outstanding of Company 1 as shown by the most recent report or statement published by Company 1. The taxpayers also represent that contributions will be made to the Donees only at such times when, to the best of their knowledge, there will not be any proposed recapitalization, tender or exchange offer, stock repurchase program or similar plan that would have the effect of substantially reducing the number of outstanding shares of Company 1 within the 3-month period following the contribution. The Taxpayers represent that the Taxpayers will, prior to the proposed contribution, provide a statement to the Donees that the requirements of Rule 145 are met for all transfers of the Company 1 ADSs by the Taxpayers and that the Taxpayers will not take any steps that will prevent the Donees from making transfers of Company 1 ADSs free of any Rule 145 resale restrictions.

The Taxpayers also represent that, under the Governance Agreement, the Family Shareholders may contribute Company 1 ADSs to the Donees without restriction and that such contributed Company 1 ADSs may be sold by the Donees without restriction.

Based on the Taxpayers' representations, we conclude that the ADSs that the Taxpayers plan to contribute to the Donees constitute stock for which, for purposes of § 170(e)(5), market quotations are readily available on an established securities market.

To meet the requirements of § 170(e)(5)(B)(ii) of the Code, the shares must be capital gain property within the meaning of § 170(b)(1)(C)(iv), which means that the shares would have to result in long-term capital gain if sold at their fair market value. Under § 1222(3), long-term capital gain results from the sale of a capital asset held for more than one year. The Taxpayers represent that, at the time of the contribution, the contributed Company 1 ADSs (i) in the hands of each of Partnership and the Taxpayers will be deemed, under § 1223(1) to have been held by each of Partnership and the Taxpayers for more than one year from the date such ADSs were acquired by each of them and (ii) will not come within any of the exceptions set forth in subsections (1) through (5) of § 1221. In addition, the Taxpayers anticipate that the fair market value of the Company 1 ADSs on the contribution date will be more than the adjusted basis of the ADSs. Based upon the Taxpayers' representations, we conclude that the Company 1 ADSs that will be contributed to the Donees represent long-term capital gain property within the meaning of § 170(b)(1)(C)(iv), and Taxpayers' contribution of the shares will meet the requirements of § 170(e)(5)(B)(ii).

Since clauses (i) and (ii) of § 170(e)(5)(B) are met, and Taxpayers will not contribute more than 10 percent (within the meaning of § 170(e)(5)(C)) of all outstanding stock of Company 1 to the Donees, we conclude that the Company 1 ADSs that the Taxpayers plan to contribute to the Donees are qualified appreciated stock as defined in § 170(e)(5).

CAVEATS:

A copy of this letter must be attached to any income tax return to which it is relevant. We enclose an extra copy of the letter for this purpose. Also enclosed is another copy of the letter ruling showing the deletions proposed to be made in the letter when it is disclosed under § 6110 of the Internal Revenue Code.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any item discussed or referenced in this letter. This ruling is directed only to the taxpayers requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

Sincerely,

KARIN G. GROSS
Senior Technician Reviewer, Branch 1
Office of Associate Chief Counsel
(Income Tax & Accounting)

Enclosures(2)