

Internal Revenue Service

Department of the Treasury
Washington, DC 20224

Number: **200438010**

Release Date: 9/17/04

Index Number: 355.04-00

Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:CORP:B02 – PLR-112460-04

Date:

May 14, 2004

Distributing =

Controlled =

Partnership =

Corp A =

Corp B =

Corp C =

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LLC =

Business or
Business X =

Region C =

b =

c =

Z =

Dear :

This letter responds to your letter dated March 2, 2004, requesting a ruling supplementing the prior letter ruling dated September 30, 2003 (PLR 200405009, PLR-152829-02) (the "Prior Ruling"). The Prior Ruling addresses transactions treated for Federal income tax purposes as a transfer by Distributing of the Region C Assets to Controlled in exchange for Controlled's assumption of the Region C liabilities and all of Controlled's stock (other than a subscriber share), a distribution by Distributing of its Controlled Stock to the Region C Members in exchange for a portion of the Region C Members' equity in Distributing and a transfer by each Region C Member of its Controlled stock and its remaining equity in Distributing to Partnership in exchange for an Interest in Partnership.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. This office has not verified any of the materials submitted in support of the request for rulings. Verification of the information, representations, and other data may be required as part of the audit process.

Facts:

The facts as described in the Prior Ruling are unchanged, except as stated below.

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LLC, not Corp C, owns and operates c of the Zs. Accordingly, the fifth sentence in the second full paragraph on page 3 is restated as follows:

LLC is a limited liability company and a successor to Corp C (a subsidiary of Corp A). The members of LLC are Corp A, Corp B and Distributing. LLC owns and operates c of the Zs.

The agreements described in the Prior Ruling will be changed. Specifically, the Distributing/Partnership Group Member Agreement will be changed so that Partnership will be responsible for all the functions necessary to operate Business X in Region C (including functions that under the prior ruling were to be the responsibility of Controlled). Partnership and Controlled will enter into a new executory contract, the Partnership/Controlled Subcontractor Agreement, pursuant to which Controlled will perform virtually all of these functions as Partnership's subcontractor and agent. Neither the Distributing/Controlled Services Agreement nor the Partnership/Controlled Services Agreement, as described in the Prior Ruling, will be entered into. The membership agreements between the Region C Members and Partnership will be entered into as described in the prior ruling, but revised to reflect that the Region C Members will pay all their fees to Controlled as Partnership's collection agent.

The agreements are summarized as follows:

Distributing/Partnership Group Member Agreement: This agreement was revised to make clear that it is an executory contract. Under this revised agreement, Partnership will become the Regional Group Member for Region C. As the Regional Group Member for Region C, Partnership will have the right and obligation to perform all the functions required to operate Region C. In connection with this right, Distributing will grant to Partnership a non-exclusive, nontransferable, revocable license to use Distributing's name and trademarks subject to certain restrictions. The Taxpayer represents that Partnership's right to use the Distributing name and trademark is only for the purpose of carrying out its functions as a Regional Group Member in Region C. Partnership will also have the right to use Distributing's software and intellectual property (either directly or through Controlled or outside subcontractors) (i) to perform processing functions, and (ii) to participate in joint ventures in the transaction processing business outside Distributing system. Partnership is required to pay Regional Group Member fees allocable to Region C to Distributing. The Regional Group Member fees paid on behalf of Partnership will be taken into account in the formulas used to determine Partnership's Equity Interest in Distributing as provided in Distributing's bylaws. Distributing may terminate the Distributing/Partnership Group Member Agreement and consequently the license, if Partnership fails either to perform its required functions or to pay Regional Group Member fees.

Partnership/Controlled Subcontractor Agreement: Under this agreement, Controlled, as Partnership's subcontractor, will perform virtually all the functions for which Partnership is responsible and will receive compensation in return. Partnership, however, will make

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final decisions regarding setting rules and policies for Region C, including setting fees paid by the Region C Members. Controlled will collect all the fees owed to Partnership and will pay the Regional Group Member fees owed by Partnership to Distributing. Controlled will be granted a sublicense by Partnership such that Controlled will be able to use Distributing's name and trademarks in performing Controlled's functions as Partnership's subcontractor. Controlled will also have the right to use Distributing's software and intellectual property in performing processing functions for Partnership. Controlled's compensation for performing its subcontractor functions will be fees paid by the Region C Members to Partnership, less Partnership's Regional Group Member fee obligation to Distributing and any costs incurred by Partnership outside the Partnership/Controlled Subcontractor Agreement.

Membership Agreements between Partnership and Region C Members: These agreements will be revised to reflect that the Region C Members will pay all their fees to Controlled as Partnership's collection agent. As described in the prior ruling, Region C Members currently hold non-equity rights relating to the Region C Members' participation in Distributing's payment system. The Region C Members enjoy certain of these rights on an individual basis and others on a collective basis through representation on the Region C Regional Board. As a result of the proposed transactions, Partnership will become a Regional Group Member of Distributing for Region C and will have all the non-equity rights that the Region C Members currently enjoy. The Region C Members' memberships in Distributing will be cancelled, and they will become members of Partnership. Thereafter, the Region C Members will continue to participate in the payment system through their memberships in Partnership, under the rights granted by Partnership comparable to the rights they had before the proposed transactions. However, the Region C Members will retain their direct licenses from Distributing to use Distributing's name and trademarks in connection with their participation in the payment system.

Accordingly, the Prior Ruling is revised as follows:

- (1) Paragraphs 8. and 10. on pages 4-5 are deleted.
- (2) Paragraph 9. on page 5 is renumbered as paragraph 8. Furthermore, the last full sentence of former Paragraph 9 is deleted.
- (3) A paragraph is inserted after paragraph 8 (as so renumbered) as follows:
 9. Partnership and Controlled will enter into the Partnership/Controlled Subcontractor Agreement. Under this agreement, Partnership will obtain services from Controlled that relate to the portion of Distributing's Business X carried out in Region C. Controlled will be responsible to

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Partnership to perform all the functions for which Partnership is responsible except that Partnership will make final decisions regarding setting rules and policies for Region C, including setting fees paid by the Region C Members. Controlled will also collect fees from the Region C Members and Distributing on behalf of Partnership and pay on behalf of Partnership a certain portion of the fees to Distributing, as required by the Distributing/Partnership Group Member Agreement. In consideration for such services, Partnership will pay or procure the payment to Controlled of all fees paid by the Region C Members or Distributing, except the portion of such fees that Partnership is required to pay to Distributing as Regional Group Member fees and any costs incurred by Partnership outside the Partnership/Controlled Subcontractor Agreement in providing services to the Region C Members, Distributing or Distributing's members. Partnership will authorize Controlled to use the Distributing name, any other Distributing mark, and any other rights, which Partnership, as a Regional Group Member, is entitled to use during the term of the Partnership/Controlled Subcontractor Agreement, but only to the extent necessary for Controlled, as its subcontractor and agent, to provide the services under such agreement.

Representations:

The representations made in connection with the Prior Ruling remain valid, in full force and effect. In addition, the following representation is made:

- (y) Partnership's right to use the Distributing name and trademark (other than as part of the company and corporate names of itself and Controlled) is only for the purpose of carrying out its functions as a Regional Group Member in Region C pursuant to the By-Laws and other rules applicable to a Regional Group Member.

Section 61(a)(3) provides that gross income includes gains derived from dealings in property.

Section 1001 provides that the gain from the sale or other disposition of property shall be the excess of the amount realized over the adjusted basis provided in § 1001. Section 1.1001-1(a) of the Income Tax Regulations provides that gain or loss is realized

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on an exchange of property “differing materially either in kind or in extent.” See *Cottage Savings Association v. Commissioner*, 499 U.S. 554 (1991).

Rulings:

The rulings set forth in the Prior Ruling remain valid, in full force and effect, except as follows:

- (1) The introductory language in paragraph (2) is revised to read as follows:

Subject to paragraph (22), the proposed transactions will be treated as though:

- (2) Paragraph (22) is renumbered as paragraph (23).

- (3) The following rulings are added:

- (22) Other than with respect to Equity Interests in Distributing and Partnership, the admission of Partnership as a Regional Group Member of Distributing pursuant to the Distributing/Partnership Group Member Agreement (together with the termination of the Region C Members’ memberships in Distributing and their admission as members of Partnership) will be viewed for Federal income tax purposes as consisting of the following transactions:
 - (a) Termination of certain contractual relationships between the Region C Members and Distributing.
 - (b) Entry into new executory contractual relationships between the Region C Members and Partnership.
 - (c) Entry into a new executory contractual relationship between Distributing and Partnership.
- (24) The Distributing/Partnership Group Member Agreement is an executory contract and thus, the execution of such agreement and the admission of Partnership as a Regional Group Member is not a realization event under § 61. Therefore, no gain or loss will be realized by (and no amount will be included in the income of) Distributing, Partnership, or the Region C Members, and no property will be deemed distributed by Distributing to Partnership or to the Region C Members on execution of the Distributing/Partnership Group Member Agreement and the admission of Partnership as a Regional Group Member pursuant thereto. I.R.C. §§ 311(b) and 301.

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- (25) The transactions described in Ruling 22 are not an exchange of property differing materially in kind or in extent. After the transactions, the Region C Members will hold essentially the same bundle of rights as they held as members in Distributing. Accordingly, based on the information and representations made, the transactions described in Ruling 22 will not constitute an exchange between Distributing and Partnership or between Distributing and the Region C Members.

The additional information submitted will have no adverse effect on the rulings set forth in the Prior Ruling.

No opinion is expressed as to the tax treatment of the transactions under other provisions of the Code or regulations or about the tax treatment of any conditions existing at the time of, or effects resulting from, the transactions that are not specifically covered by the above ruling. Specifically, no opinion is expressed regarding the application of I.R.C. § 482 to the ongoing operations, including the application of I.R.C. § 482 to the Distributing/Partnership Group Member Agreement and the Partnership/Controlled Subcontractor Agreement.

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 must be attached to any income tax return to which it is relevant.

In accordance with the Power of Attorney on file with this office, copies of this letter are being sent to the taxpayer and its representatives.

Sincerely,

Marlene P. Oppenheim
Senior Counsel
Office of Associate Chief Counsel
(Corporate)