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Third Party Communication: None

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Person To Contact:

, ID No.

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CC:CORP:3

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Date:

December 21, 2004

Distributing =

Controlled 1 =

Controlled 2 =

Controlled 3 =

State X =

A =

B =

C =

D =

E =

Business F =

h =

k =

l =

m =

n =

o =

p =

q =

r =

s =

Dear :

We respond to your request dated August 19, 2004, for rulings on the federal income tax consequences of a proposed transaction. Additional information was received in letters dated November 17, 2004, and December 14, 2004. The material information submitted for consideration is summarized below.

The rulings contained in this letter are based on facts and representations submitted by the taxpayer and accompanied by a penalties 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. Moreover, no information provided by the taxpayer has been reviewed and no determination has been made regarding whether the proposed transaction: (i) satisfies the business purpose requirement of §1.355-2(b) of the Income Tax Regulations, (ii) is used principally as a device for the distribution of the earnings and profits of the distributing corporation or any of the controlled corporations or both (see §355(a)(1)(B) of the Internal Revenue Code and §1.355-2(d)), or (iii) is part of a plan (or series of related transactions) pursuant to which one or more persons will acquire directly or indirectly stock representing a 50-percent or greater interest in the distributing corporation or any of the controlled corporations (see §355(e)(2)(A)(ii) and §1.355-7T).

Distributing is a State X corporation engaged directly in Business F. Distributing has outstanding h shares of \$100 par value voting common stock that are owned by five members of a single family, as follows: A (k shares), B (l shares), C (m shares), D (n shares), and E (o shares). A, B, C, D, and E are also the sole employees of Distributing. Financial information has been received that indicates that Business F has had gross receipts and operating expenses representative of the active conduct of a trade or business for each of the past five years.

Controlled 1, Controlled 2, and Controlled 3 each will be formed as a State X corporation and wholly owned subsidiary of Distributing in order to effectuate the proposed transactions. For what are represented to be valid business purposes, the following transactions are proposed:

- (i) Distributing will transfer p of its net worth represented by assets and liabilities of its Business F to Controlled 1 in exchange for k shares of Controlled 1 stock. Immediately thereafter, Distributing will transfer the k shares of Controlled 1 stock to A in exchange for all of A's k shares of Distributing stock.
- (ii) Distributing will transfer q of its net worth represented by assets and liabilities of its Business F to Controlled 2 in exchange for n shares of Controlled 2 stock. Immediately thereafter, Distributing will transfer the n shares of Controlled 2 stock to D in exchange for all of D's n shares of Distributing stock.
- (iii) Distributing will transfer r of its net worth represented by assets and liabilities of its Business F to Controlled 3 in exchange for o shares of Controlled 3 stock. Immediately thereafter, Distributing will transfer the o shares of Controlled 3 to E in exchange for all of E's o shares of Distributing stock.

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

- (a) The fair market value of the Controlled 1 stock, the Controlled 2 stock, and the Controlled 3 stock to be received by A, D, and E, respectively, will be approximately equal to the fair market value of the Distributing Corporation stock surrendered by each of the shareholders in the exchange.
- (b) No part of the consideration to be distributed by Distributing will be received by the Distributing shareholders as a creditor, employee, or in any capacity other than that of a shareholder of the corporation.
- (c) The five years of financial information submitted on behalf of Distributing 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 statements submitted.

- (d) Following the transaction, Distributing and Controlled 1, Controlled 2, and Controlled 3 will each continue, independently and with its separate employees, its share of all the integrated activities of the Business F conducted by Distributing prior to consummation of the proposed transactions.
- (e) The distribution of the stock of Controlled 1, Controlled 2, and Controlled 3 is carried out for the following corporate business purpose: to resolve shareholder disputes with regard to the management and operation of Business F, which are having an adverse effect on the day-to-day operations of Distributing. The distribution of the stock of each of Controlled 1, Controlled 2, and Controlled 3 is motivated, in whole or substantial part, by this corporate business purpose.
- (f) The transaction is not used principally as a device for the distribution of the earnings and profits of Distributing or Controlled 1, Controlled 2, or Controlled 3, or both.
- (g) The total adjusted bases and the fair market value of the assets to be transferred to Controlled 1, Controlled 2, and Controlled 3 by Distributing each equals or exceeds the sum of the liabilities to be assumed (as determined under §357(d)) by Controlled 1, Controlled 2, and Controlled 3.
- (h) The liabilities to be assumed (as determined under §357(d)) in the transactions were incurred in the ordinary course of business and are associated with the assets being transferred.
- (i) The income tax liability for the taxable year in which investment credit property (including any building to which §47(d) applies) is transferred will be adjusted pursuant to §50(a)(1) or (a)(2) (or §47, as in effect before amendment by Pub. L. No. 101-508, Title 11, 104 Stat. 1388, 536 (1990), if applicable) to reflect an early disposition of the property.
- (j) No intercorporate debt will exist between Distributing and any of the Controlled corporations at the time of, or subsequent to, the distribution of the Controlled 1, Controlled 2, or Controlled 3 stock.
- (k) There will not be any continuing transactions between Distributing and any of the Controlled corporations subsequent to the consummation of the three proposed transactions.

- (l) No two parties to the transaction are investment companies as defined in §368(a)(2)(F)(iii) and (iv).
- (m) There is no acquisition of stock of Distributing or Controlled 1, Controlled 2, or Controlled 3 (including any predecessor or successor of any such corporation) that is part of a plan or series of related transactions (within the meaning of §1.355-7T) that includes the distribution of the Controlled 1, Controlled 2, or Controlled 3 stock.
- (n) Distributing is not an “S” corporation within the meaning of §1362(a), but immediately before the distribution, Distributing will be eligible to make an “S” corporation election pursuant to §1362(a). Controlled 1, Controlled 2, and Controlled 3 may elect to be an “S” corporation pursuant to §1362(a) on the first available date after the distribution.

Based solely on the information submitted and the representations made, we hold as follows concerning the proposed transactions:

- (1) The transfer by Distributing of the Business F assets to each of Controlled 1, Controlled 2, and Controlled 3, as described above, in exchange for all of the issued and outstanding stock of each of Controlled 1, Controlled 2, and Controlled 3 and the assumption by Controlled 1, Controlled 2, and Controlled 3 of the liabilities associated with those assets, followed by the distribution of all of the stock of Controlled 1, Controlled 2, and Controlled 3 to A, D, and E, respectively, in exchange for all of A, D, and E’s stock in Distributing, as described above, will be a reorganization within the meaning of § 368(a)(1)(D). Distributing, Controlled 1, Controlled 2, and Controlled 3 each will be a “party to a reorganization” under section 368(b).
- (2) Distributing will recognize no gain or loss upon the transfer of the Business F assets to each of Controlled 1, Controlled 2, and Controlled 3 in exchange for Controlled 1, Controlled 2, and Controlled 3 stock and the assumption of liabilities by each of Controlled 1, Controlled 2, and Controlled 3, as described above (§§ 361(a) and 357(a)).
- (3) Controlled 1, Controlled 2, and Controlled 3 will recognize no gain or loss on the receipt of the Business F assets of Distributing in exchange for Controlled 1, Controlled 2, and Controlled 3 stock, respectively, as described above (§ 1032(a)).
- (4) Controlled 1’s, Controlled 2’s, and Controlled 3’s basis in each asset will be the same as the basis of such assets in the hands of Distributing immediately prior to the transfer (§ 362(b)).

- (5) Controlled 1's, Controlled 2's, and Controlled 3's holding period for each asset received from Distributing will, in each case, include the period during which such asset was held by Distributing (§ 1223(2)).
- (6) No gain or loss will be recognized by Distributing upon the distribution of all of its stock in Controlled 1, Controlled 2, and Controlled 3 to A, D, and E, respectively, in exchange for all of A, D, and E's stock in Distributing (§ 361(c)(1)).
- (7) No gain or loss will be recognized to (and no amount will be included in the income of) A, D, and E upon their receipt of all the stock of Controlled 1, Controlled 2, and Controlled 3, respectively, in exchange for all of their Distributing stock (§ 355(a)(1)).
- (8) The basis of the Controlled 1, Controlled 2, and Controlled 3 stock in the hands of A, D, and E, respectively, after the proposed transactions will, in each instance, be the same as the basis of the Distributing stock surrendered by each of A, D, and E in exchange therefor (§ 358(a)(1)).
- (9) The holding period of the Controlled 1, Controlled 2, and Controlled 3 stock in the hands of A, D, and E, respectively, after the proposed transactions will, in each instance, include the holding period of the Distributing stock surrendered by each of A, D, and E in exchange therefore, provided such stock is held by each of A, D, and E as a capital asset on the date of the transaction (§ 1223(1)).
- (10) As provided in section 312(h), proper allocation of earnings and profits between Distributing and each of Controlled 1, Controlled 2, and Controlled 3 will be made under § 1.312-10(a) of the Income Tax Regulations.

No opinion is expressed about the tax treatment of the proposed transaction under other provisions of the Code or regulations or the tax treatment of any conditions existing at the time of, or effects resulting from, the proposed transaction that are not specifically covered by the above rulings. In particular, no opinion is expressed regarding: (i) whether the proposed distribution satisfies the business purpose requirement of § 1.355-2(b); (ii) whether the proposed transaction is used principally as a device for the distribution of the earnings and profits of Distributing or any of the Controlled corporations or both (see § 355(a)(1)(B) and § 1.355-2(d)); and (iii) whether the distribution and an acquisition or acquisitions are part of a plan (or series of related transactions) under § 355(e)(2)(A)(ii).

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

It is important that a copy of this letter be attached to the federal income tax returns of the taxpayers involved for the taxable year in which the transaction covered by this letter is consummated.

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

Sincerely,

Richard Coss
Senior Counsel, Branch 3
Office of Associate Chief Counsel (Corporate)