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Person To Contact:
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Telephone Number:

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Date:
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TY:

Legend

Taxpayer =
Parent =
State A =
Station =
City =
$x =
$y =
$z =
Date A =
Date B =
Date C =
Date D =
Target =

X percent =

Dear :

This responds to your request for a private letter ruling dated September 20, 2017, regarding the application of § 1033 of the Internal Revenue Code to your transaction. You have requested two rulings. First, that the sale of spectrum-based content distribution rights associated with Station pursuant to the actions of the Federal Communications Commission (FCC) constitutes a sale under a threat of an involuntary conversion of its FCC licenses and related property for purposes of § 1033. Second, that Taxpayer's acquisition of percent of the stock of Target on Date D constituted a purchase of "stock in the acquisition of control of a corporation" owning other property

similar or related in service or use to the spectrum-based content distribution rights associated with Station, within the meaning of § 1033(a)(2)(A).

FACTS

Taxpayer, a State A corporation, is a wholly-owned subsidiary of Parent, also a State A corporation. Parent is a television broadcasting company that, directly and through subsidiaries, owns and operates, or provides, certain programming, operating or sales services to television stations in numerous markets. Parent is the common parent of an affiliated group of corporations, including Taxpayer, and files a consolidated federal income tax return. Parent and Taxpayer use the accrual method of accounting, and file on a December 31 taxable year-end.

Substantially all of Parent's broadcast operations are carried on by, and substantially all of the assets associated therewith are owned and operated, by Taxpayer and subsidiaries of Taxpayer. Taxpayer owns and operates Station, a full-power UHF television station in City that operates in the "upper 600 MHz band". Station operates pursuant to licenses and permits issued by the FCC, which authorize Station to deliver video, audio, data, and other content over specific broadcast frequencies.

Pursuant to applicable provisions of the Middle Class Tax Relief and Job Creation Act of 2012 (Spectrum Act),[1] the FCC is implementing a mandate by Congress to repurpose spectrum in the 600 MHz band currently used by television broadcasters to help meet the nation's accelerating needs for mobile broadband and other new bandwidth-intensive technologies. The Spectrum Act calls for the FCC to undertake two related, but independent, processes to reclaim spectrum currently used for television broadcasting: (i) an "Incentive Auction" and (ii) a "Repacking".

The Incentive Auction is intended to motivate existing television broadcasters to relinquish some or all of their spectrum usage rights to accommodate the requirements of the wireless carriers within the repurposed spectrum. Repacking is an involuntary reassignment of remaining broadcast television stations to a narrower segment of spectrum lower in the band. This Repacking will allow the FCC to assemble a near nation-wide contiguous band of spectrum in the upper 600 MHZ band for reallocation to mobile broadband.

The Spectrum Act provides broadcasters with three relinquishment options for participating in the Incentive Auction. First, broadcasters can relinquish their spectrum-based content distribution rights in their entirety and cease broadcasting (Go Off-Air). Second, broadcasters currently operating on frequencies in the UHF band can

[1] Middle Class Tax Relief and Job Creation Act of 2012, Pub. L. No.112-96 §6403.

voluntarily agree to relocate to frequencies in the VHF band[2] (Move to VHF). Third, broadcasters can relinquish their rights to deliver content over a television broadcast channel and, instead, agree to share a single channel with another broadcaster (Sharing Arrangement).

Alternatively, broadcasters can also forgo participation in the Incentive Auction altogether and remain on the air. However, that would mean accepting, as part of the Repacking process, the potential to be reassigned to a different, possibly inferior, less valuable, UHF channel without compensation (other than reimbursement from a limited fund for the cost of moving to the new channel).

On May 15, 2014, the FCC released a *Report and Order*[3] adopting rules to implement the Spectrum Act, including the broadcast television spectrum Incentive Auction and Repacking. Under the rules, the Incentive Auction will consist of a "reverse" auction and a "forward" auction. The reverse auction will determine the price at which a broadcast station would be willing to relinquish some or all of its spectrum-based content distribution rights. The forward auction will set the price that the wireless carriers will pay for the new licenses for repurposed spectrum. After the auction is completed, broadcasters whose bids were accepted in the auction will receive their payments from the forward auction proceeds. The FCC will also use proceeds from the forward auction to reimburse certain spectrum relocation costs of broadcasters who do not elect to sell. Any remaining proceeds will be deposited with the federal treasury.

Broadcasters who choose to forego the Incentive Auction and instead remain on the air are subject to mandatory relocation to different operating frequencies at the direction of the FCC. Non-participating stations that currently operate in that portion of the upper 600 MHz band that will be repurposed for mobile broadband licenses will almost certainly be forced to change to a new channel in a lower portion of the existing UHF band. Non-participating stations that do not currently operate in the re-purposed band may still be required to operate on new channels, as necessary, to accommodate other stations being moved to other frequencies.

If Taxpayer does not participate in the Incentive Auction, it is highly likely that Taxpayer would be Repacked into a different channel. Taxpayer is one of only a limited number of broadcast television stations that the FCC is highly likely to force to relocate to another channel. Taxpayer's Station is located in one of the nation's 40 largest television markets. These circumstances make Taxpayer's Station strategically important to the FCC's spectrum reclamation project – making it highly likely that the FCC would compel Taxpayer to relocate to a new channel in the Repacking process if Taxpayer fails to participate in the Incentive Auction.

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[2] It is widely accepted within the industry that VHF spectrum is grossly inferior to UHF spectrum for distribution of video, audio, data and other content in digital form.

[3] *Expanding the Economic and Innovation Opportunities of Spectrum Through Incentive Auctions*, Report and Order, 29 FCC Rcd.

The FCC is obligated to use "all reasonable efforts" in the Repacking process to replicate a station's coverage area and population served. However, there is no guarantee that a broadcast station's coverage area and population served would, in fact, be preserved following the Repacking. Broadcasters forced to change to a new channel through Repacking will incur significant out-of-pocket costs to obtain new broadcasting facilities and equipment. Taxpayer represents that it believes that approximately $x of its total anticipated out-of-pocket Repacking costs to obtain new broadcasting facilities may not be reimbursed by the FCC.

Given Station's particular circumstances, Taxpayer believes that it would be highly likely that Station would be Repacked if Taxpayer did not sell Station's spectrum-based content distribution rights in the Incentive Auction. Taxpayer agreed in the Incentive Auction bidding process to sell all of Station's spectrum-based content distribution rights to the FCC for $y. The FCC distributed these auction proceeds to Taxpayer on Date A. Taxpayer expects to relinquish its spectrum-based content distribution rights to the FCC on Date B.

On Date C, Taxpayer entered into an agreement to acquire X percent of the stock in Target. The closing of the Target acquisition was conditioned on receipt of FCC approval as well as other customary closing conditions, including receipt of third party consents. On Date D, Taxpayer acquired X percent of the stock of Target for $z.

Taxpayer intends for the stock of Target to be used as replacement property for, among other things, Station's spectrum-based content distribution rights sold by Taxpayer in the Incentive Auction. Taxpayer represents that Target owns and operates, through its direct and indirect subsidiaries, broadcast stations containing property that are similar or related in service or use to the Station's spectrum-based content distribution rights. According to Taxpayer, neither Target nor its subsidiaries holds any assets that are not related to Target's broadcast stations' business. Target is not related to Taxpayer.

Taxpayer further represented that prior to the closing of Taxpayer's acquisition of Target, each Target subsidiary that was treated as a corporation for United States federal income tax purposes was restructured in a transaction treated as a complete liquidation under § 332 of the Code. As a result of these restructuring transactions, each Target subsidiary is disregarded as an entity separate from Target within the meaning of Treas. Reg. § 301.7701-3(b).[4]

REQUESTED RULINGS

[4] Target is not a party to this ruling request. Taxpayer has submitted a list of the former corporate subsidiaries of Target, the date on which each restructuring transaction occurred, a description of each restructuring transaction, and organizational structure charts for Target and its subsidiaries before and after the restructuring transactions. These materials are part of the file, but not part of this ruling letter.

You have requested two rulings. First, that the sale of spectrum-based content distribution rights associated with Station pursuant to the actions of the FCC constitutes a sale under a threat of an involuntary conversion of its FCC licenses and related property for purposes of § 1033.

Second, that Taxpayer's acquisition of X percent of the stock of Target on Date D constituted a purchase of "stock in the acquisition of control of a corporation" owning other property similar or related in service or use to the spectrum-based content distribution rights associated with Station, within the meaning of § 1033(a)(2)(A).

LAW AND ANALYSIS

Section 1033 (a)(2)(A) of the Code generally provides that if property (as a result of its destruction in whole or in part, theft, seizure, or requisition or condemnation or threat or imminence thereof) is compulsorily or involuntarily converted into money and the taxpayer, within the period provided in § 1033(a)(2)(B) and for the purpose of replacing such property, purchases other property similar or related in service or use to the property so converted, or purchases stock in the acquisition of control of a corporation owning such other property, at the election of the taxpayer the gain shall be recognized only to the extent that the amount realized upon such conversion (regardless of whether such amount is received in one or more taxable years) exceeds the cost of such other property or such stock. For purposes of § 1033(a)(2)(A), --

(i) no property or stock acquired before the disposition of the converted property shall be considered to have been acquired for the purpose of replacing such converted property unless held by the taxpayer on the date of such disposition; and

(ii) the taxpayer shall be considered to have purchased property or stock only if, but for the provisions of § 1033(b), the unadjusted basis of such property or stock would be its cost within the meaning of § 1012.

Section 1033(a)(2)(E)(i) provides that for purposes of § 1033(a)(2), the term "control" means the ownership of stock possessing at least 80 percent of the total combined voting power of all classes of stock entitled to vote and at least 80 percent of the total number of shares of all other classes of stock of the corporation.

Ruling 1. Sale Under Threat of Repacking under Section 1033

One of the circumstances in which a § 1033 requisition or condemnation occurs is where a taxpayer's property is subjected to a compensable governmental taking for public use under the Fifth Amendment of the U.S. Constitution. *American Natural Gas Co. v. United States*, 279 F.2d 220 (Ct. Cl. 1960); *Behr-Manning Corp. v. United States*, 196 F. Supp. 129 (D.C. Mass. 1961); Rev. Rul. 69-254, 1969-2 C.B. 162; Rev. Rul. 58-11, 1958-1 C.B. 273. The Fifth Amendment provides, in part, that no "private property be taken for public use without just compensation." However, the meaning of

condemnation or requisition for purposes of § 1033 of the Code is not strictly limited to takings within the meaning of the Fifth Amendment.

In Rev. Rul. 82-147, 1982-1 C.B. 190, a federal law prohibited the use of motor boats with motors of greater than 25 horsepower on designated lakes in wilderness areas. It also provided that, if the horsepower restriction made the operation of a resort uneconomical, the owner of the resort could require the government to purchase its resort at its fair market value (determined without regard to the horsepower restrictions). The horsepower restriction made the operation of the taxpayer's resort uneconomical and the taxpayer sold its fishing lodge to the federal government. In holding that the government's purchase of the resort constituted a condemnation within the meaning of § 1033, the Service did not refer to a Fifth Amendment taking, but instead emphasized that the horsepower restriction "in addition to the provision authorizing purchase of a resort at its fair market value without regard to the restriction, effectively constitutes a taking of property upon payment of fair compensation."

In the present case, the FCC's Repacking process is functionally equivalent to a direct physical taking of private property for a public use without the consent of the property owner because it effectively deprives the Taxpayer of its assets. Taxpayer's choice to participate in the Incentive Auction was not a meaningful choice. Choosing to forego the Incentive Auction would have subjected Taxpayer to the Repacking process. Due to Taxpayer's unique circumstances, if Taxpayer did not participate in the Incentive Auction with respect to Station, it was highly likely that Taxpayer would have been Repacked into a different channel without compensation other than reimbursement from a limited fund for the cost of moving to the new channel.

In Rev. Rul. 63-221, 1963-2 C.B. 332, the Service stated that for purposes of § 1033, threat or imminence of condemnation is generally considered to exist where a property owner is informed, either orally or in writing, by a representative of a governmental body that the government entity has decided to acquire his property and the property owner has reasonable grounds to believe, from the information conveyed to him by such representative, that the necessary steps to condemn the property will be instituted if a voluntary sale is not arranged.

In Rev. Rul. 81-180, 1981-2 C.B. 161, the Service considered a situation where a taxpayer learned through newspaper reports that a city intended to acquire its property by condemnation for public use if a sale could not be negotiated. City officials confirmed the accuracy of the reports. The taxpayer sold its property to a third party thereafter, but before the city actually condemned the property. The Service concluded that the sale was made under the "threat or imminence of condemnation" because the property was sold after the taxpayer was given reasonable grounds to believe that its property would be taken.

These authorities indicate that a voluntary sale qualifies as an involuntary conversion under § 1033 if the threat or imminence of condemnation is present at the time of sale. However, the threat need not be a certainty. A threat exists if the taxpayer may reasonably believe from representations of the government and surrounding circumstances that a forced sale is likely to take place.

In this case, the FCC's decision to impose on Taxpayer mandatory modification of its broadcast facilities if it decides not to participate in the Incentive Auction (including forced relocation to a different operating frequency, and the potential to incur service losses, unreimbursed out-of-pocket costs, and reduced value for its remaining assets), creates the reasonable grounds to believe that condemnation is forthcoming. The involuntary conversion is the FCC's threat of Repacking Taxpayer's Station to an inferior frequency and the consequent loss of economic utility of its related property.

The FCC has provided Taxpayer with notice, through the Spectrum Act and the *Report and Order*, of its intent to acquire the type of spectrum-based content distribution rights that Taxpayer possesses in Station. Under its unique circumstances, Taxpayer reasonably believed that if it did not participate in the Incentive Auction, it was highly likely that the FCC would take Taxpayer's spectrum, and then force Taxpayer to relocate Station to a different frequency.

Accordingly, under the FCC's relinquishment option to Go Off-Air, Taxpayer's sale of spectrum-based content distribution rights and related assets associated with Station to the FCC constitutes a disposition under the threat or imminence of condemnation for purpose of § 1033 of the Code.

Ruling No. 2: Whether Target stock, qualifies as replacement property for Taxpayer's Station for purposes of § 1033(a)(2).

On Date D, Taxpayer acquired X percent of Target's stock, which meets both the "purchase" and "stock in acquisition of control" requirements for § 1033(a)(2). In Rev. Rul. 64-237, 1964-2 C.B. 319, the Service indicated that "attention will be directed primarily to the similarity in the relationship of the services or uses which the original and replacement properties have" to the taxpayer. Rev. Rul. 82-70, 1882-1 C.B. 114, held that stock in a corporation primarily (but not solely) engaged in the operation of a radio broadcasting station qualified as replacement property for purposes of § 1033 with respect to the taxpayer's sale of a radio station pursuant to FCC policy.

In Rev. Rul. 66-33, 1966-1 C.B. 183, the taxpayer elected to treat the sale of a radio station as an involuntary conversion under § 1033 and former § 1071 (pertaining to exchanges to effectuate policies of the Federal Communications Commission, until its repeal as of January 17, 1995). As replacement property, the taxpayer acquired stock of a corporation that did not own property that was similar or related in service or use to

the converted property, but instead owned 100 percent of the stock in an entity that owned such property. Rev. Rul. 66-33 holds that the purchase by the taxpayer of stock of a corporation that does not own similar or related in service or use property, but owns all the stock of a subsidiary corporation which owns and operates such property, is not a valid replacement for purposes of § 1071. Consequently, the transaction failed to qualify for deferral of gain under §§ 1033 and 1071.

In the present case, Target, directly and through its wholly-owned subsidiaries, operated television broadcasting stations. Prior to the closing of Taxpayer's acquisition of Target's stock, each Target subsidiary that was treated as a corporation for U.S. federal income tax purposes engaged in a restructuring that constituted a § 332 complete liquidation. As a result, each subsidiary is disregarded as an entity separate from Target within the meaning of Treas. Reg. § 301.7701-3(b).

Accordingly, at the time Taxpayer acquired Target's stock, Taxpayer was not acquiring control of a corporation that only indirectly holds similar or related in service or use property through a subsidiary. Rather, prior to the time Taxpayer gained control of Target, each of Target's subsidiaries no longer existed for federal income tax purposes. Assuming that all of the restructurings of Target's subsidiaries are properly treated as complete liquidations for purposes § 332, and that such subsidiaries are indeed disregarded as entities separate from Target under Treas. Reg. § 301.7701-3(b), at the time Taxpayer gained control of Target, Target directly owned property that is similar or related in service or use to Taxpayer's Station, the converted property. Consequently, the purchase of Target stock by Taxpayer during the replacement period will qualify as "stock in the acquisition of control of a corporation owning property similar or related in service or use" to the spectrum-based content distribution rights associated with Station, within the meaning of § 1033(a)(2)(A) of the Code.

CONCLUSIONS

The sale of the spectrum-based content distribution rights and related assets currently associated with Taxpayer's Station to the FCC constitutes a sale under a threat of an involuntary conversion for purposes of § 1033. In addition, the purchase of Target stock by Taxpayer during the replacement period will qualify as "stock in the acquisition of control of a corporation owning property similar or related in service or use" to the spectrum-based content distribution rights associated with Station, within the meaning of § 1033(a)(2)(A) of the Code.

CAVEATS

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. Accordingly, our office makes no determination nor expresses any opinion about the tax consequences of the restructuring of any or all of Target's subsidiaries as

complete liquidations for purposes § 332, or whether such subsidiaries are indeed treated as disregarded entities under Treas. Reg. § 301.7701-3(b) at the time Target's stock was purchased by Taxpayer. This ruling is based on the facts as represented by the Taxpayer concerning the liquidations of Target's subsidiaries.

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

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter ruling.

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. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Sincerely,

William A. Jackson
Branch Chief, Branch 5
Office of Chief Counsel
(Income Tax & Accounting)

Enclosure (1)