Internal Revenue Service

Department of the Treasury

Index Number: 355.03-00; 355.03-01

Washington, DC 20224

Number: **199949024**
Release Date: 12/10/1999

Person to Contact:

Telephone Number:

Refer Reply To:
CC:DOM:CORP:1-PLR-119319-98
Date:
August 30, 1999

Legend

Distributing	=
Controlled 1	=
Controlled 2	=
Controlled 3	=
Group A	=
Group B	=
Group C	=
Trust	=
Beneficiary	=
State A	=
Shareholder 1	=
Shareholder 2	=
Shareholder 3	=
Business A	=
Business B	=

Business C =

T =

R =

Dear :

We respond to your letter dated October 5, 1998, in which you requested rulings as to the federal income tax consequences of a proposed transaction. Additional information was submitted in letters dated November 17, 1998, January 19, 1999, January 25, 1999, February 3, 1999, March 2, 1999, March 4, 1999, April 8, 1999, May 4, 1999, June 8, 1999, and June 14, 1999. Specifically you requested rulings under section 355 of the Internal Revenue Code. The facts submitted are as follows.

Distributing is a closely held corporation organized under the laws of State A that is directly engaged in Business A, Business B and Business C. Distributing's capital structure consists of T shares of voting common stock all of which is owned by Trust and three groups of shareholders: Group A, Group B, and Group C. In addition to other assets, Distributing has inventory and cash.

Distributing's shareholders cannot agree on the business direction of Business A and the amount of resources that should be expended thereon. There are no disputes between the shareholders as to Business B and Business C except to the extent Business A may be affected through services or products provided by Business B and Business C. To resolve the disputes between the shareholders, Distributing will contribute portions of Business A to three newly formed corporations.

The steps that will be taken are as follows:

1) Distributing will form Controlled 1, Controlled 2, and Controlled 3 under the laws of State A. The capital structure of the three corporations will consist of voting common stock.

2) Distributing will divide Business A into three equal parts and contribute the parts to Controlled 1, Controlled 2, and Controlled 3.

3) Shareholder 2 and shareholder 3 will resign as co-trustees of Trust.

4) Distributing will distribute all the stock of Controlled 1 to Group A in exchange for all of Group's A stock in Distributing.

5) Distributing will distribute all the stock of Controlled 2 to Group B in exchange for all of Group's B stock in Distributing.

6) Distributing will distribute all the stock of Controlled 3 to Group C in exchange for all of Group's C stock in Distributing.

After the distribution, Distributing will retain Business B, Business C, the inventory, and the cash. Distributing will sell the inventory and use the proceeds and the cash to purchase assets for Business B. Shareholder 1, who will also receive Controlled 3 stock in the distribution, will remain as manager and employee of Distributing. In order to properly divide the value of the assets of Distributing, Controlled 3 will execute a note in the amount of R to Distributing. Shareholders of Controlled 3 will transfer cash after the distribution to Controlled 3 that will be used to pay off the note.

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

a) The indebtedness owed by Controlled 3 to Distributing after the distribution of the controlled corporations (including Controlled 3) will not constitute stock or securities.

b) No part of the consideration distributed by Distributing is being received by a stockholder of Distributing as a creditor, employee, or in any capacity other than that of a stockholder of Distributing.

c) The fair market value of the controlled corporations' stock and other consideration to be received by each shareholder of the distributing corporation will be approximately equal to the fair market value of the distributing stock surrendered by the shareholders in the exchange.

d) The 5 years of financial information submitted on behalf of the distributing corporation 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.

e) Following the transaction, the distributing and controlled corporations will each continue the active conduct of its business, independently and with its separate employees.

f) The distributions of the stock, or stock and securities, of the controlled corporations are carried out for the following corporate business purpose: to resolve shareholder disagreements concerning how Distributing's Business A should be managed. The distributions of the stock, or stock and securities, of the controlled corporations are motivated, in whole or substantial part, by this corporate business purpose.

g) There is no plan or intention by the shareholder or security holders of the distributing corporation to sell, exchange, transfer by gift, or otherwise dispose of any of their stock in, or securities of, either the distributing or the controlled corporations after the transaction.

h) There is no plan or intention by either the distributing corporation or the controlled corporations, directly or through any subsidiary corporation, to purchase any of its outstanding stock after the transaction, other than through stock purchases meeting the requirements of section 4.05(1)(b) of Rev. Proc. 96-30.

i) There is no plan or intent to liquidate either the distributing or Controlled corporations, to merge those corporations with any other corporation, or to sell or otherwise dispose of the assets of such corporations after the transaction, except in the ordinary course of business and except for Distributing's receipt of a note from Controlled 3 to compensate Distributing for a portion of an asset transferred to Controlled 3.

j) The total adjusted bases and the fair market value of the assets transferred to each controlled corporation by the distributing corporation each equals or exceeds the sum of liabilities assumed by each such controlled corporation plus any liabilities to which the transferred assets are subject; and the liabilities assumed in the transaction and the liabilities to which the transferred assets are subject were incurred in the ordinary course of business and are associated with the assets being transferred.

k) No intercorporate debt will exist between the distributing corporation and the controlled corporations at the time of, or subsequent to, the distribution of each controlled corporation's stock, except the note that will be issued from Controlled 3 to Distributing.

l) Payments made in connection with all continuing transaction, if any, between the distributing and controlled corporations, will be for fair market value based on terms and conditions arrived at by the parties' bargaining at arms length.

m) No two parties to the transaction are investment companies as defined in section 368(a)(2)(F)(iii) and (iv).

n) The distribution is not part of a plan or series of related transactions (within the meaning of section 355(e)) pursuant to which one or more persons will acquire directly or indirectly stock possessing 50 percent or more of the total combined voting power of all classes of stock of either distributing or the controlled corporations.

o) None of the distributions of the stock of Controlled 1, 2 and 3 will be a disqualified distribution within the meaning of section 355(d)(2).

p) The inventory amounts will be sold and the proceeds thereof as well as other cash held by Distributing will be used to purchase and maintain farm equipment, and to pay all accounts payables and accrued/deferred expenses listed on the pro forma balance sheet. All of such funds will be used in connection with businesses that are retained by Distributing.

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

1) The transfer of assets by Distributing to Controlled 1, followed by the distribution of Controlled 1 stock to Group A, will qualify as a reorganization within the meaning of section 368(a)(1)(D). Distributing and Controlled 1 will each be a “party to the reorganization” within the meaning of section 368(b).

2) The transfer of assets by Distributing to Controlled 2, followed by the distribution of Controlled 2 stock to Group B, will qualify as a reorganization within the meaning of section 368(a)(1)(D). Distributing and Controlled 2 will each be a “party to the reorganization” within the meaning of section 368(b).

3) The transfer of assets by Distributing to Controlled 3, followed by the distribution of Controlled 3 stock to Group C, will qualify as a reorganization within the meaning of section 368(a)(1)(D). Distributing and Controlled 3 will each be a “party to the reorganization” within the meaning of section 368(b).

4) No gain or loss will be recognized by Distributing upon the transfer of assets and liabilities to Controlled 1, Controlled 2, and Controlled 3 in actual or constructive exchange for Controlled 1, Controlled 2, and Controlled 3 stock as described above. Sections 361(a), and 357(a). However, Distributing will recognize some gain, if any, on property transferred to Controlled 3 due to the note Controlled 3 issued to Distributing. Section 361(b)(1).

5) No gain or loss will be recognized by Controlled 1, Controlled 2, and Controlled 3 upon receipt of assets and liabilities, in actual or constructive exchange for Controlled 1, Controlled 2, and Controlled 3 stock as described above. Section 1032(a).

6) The basis of the assets received by Controlled 1, Controlled 2, and Controlled 3 from Distributing will be the same as the basis of such assets in the hands of Distributing immediately prior to the proposed transaction except that the bases of assets received by Controlled 3 will be increased due to any gain recognized by Distributing on assets transferred to Controlled 3. Section 362(b).

7) The holding period of the assets received by Controlled 1, Controlled 2, and Controlled 3 from Distributing in the transaction will include the holding period of Distributing in those assets immediately before the transaction. Section 1223(2).

8) No gain or loss will be recognized by Distributing on the distribution of all of the stock of Controlled 1 to Group A. Section 361(c).

9) No gain or loss will be recognized by Distributing on the distribution of all of the stock of Controlled 2 to Group B. Section 361(c).

10) No gain or loss will be recognized by Distributing on the distribution of all of the stock of Controlled 3 to Group C. Section 361(c).

11) No gain or loss will be recognized and no amount will be included in the income of Group A, Group B, and Group C on the receipt of Controlled 1, Controlled 2, and Controlled 3 stock. Section 355(a).

12) The basis of Controlled 1 stock in the hand of Group A will be the same as Group A's basis in its Distributing stock held immediately before the transaction. Section 358(a)(1).

13) The basis of Controlled 2 stock in the hand of Group B will be the same as Group B's basis in its Distributing stock held immediately before the transaction. Section 358(a)(1).

14) The basis of Controlled 3 stock in the hand of Group C will be the same as Group C's basis in its Distributing stock held immediately before the transaction. Section 358(a)(1) of the Code.

15) The holding period of Controlled 1 stock received by Group A in the transaction will include the holding period of the Distributing stock surrendered by Group A in the exchange provided that such stock is held as a capital asset on the date of the exchange. Section 1223(1).

16) The holding period of Controlled 2 stock received by Group B in the transaction will include the holding period of the Distributing stock surrendered by Group B in the exchange provided that such stock is held as a capital asset on the date of the exchange. Section 1223(1).

17) The holding period of Controlled 3 stock received by Group C in the transaction will include the holding period of the Distributing stock surrendered by Group C in the exchange provided that such stock is held as a capital asset on the date of the exchange. Section 1223(1).

18) Proper allocation of earnings and profits among Distributing and Controlled 1, 2 and 3 will be made pursuant to Regulation Section 1.312-10(a). Section 312(h).

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.

This ruling letter is directed only to the taxpayer who requested 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,

Assistant Chief Counsel (Corporate)

By: ______________________________

Alfred Bishop
Chief, Branch 1