

Internal Revenue Service

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Department of the Treasury

Washington, DC 20224

Person To Contact:

Telephone Number:

Refer Reply To:

CC:CORP:B05 – PLR-140094-03

Date:

November 06, 2003

In re:

LEGEND

Distributing =

Controlled =

Sub1 =

Sub2 =

Sub3 =

Sub4 =

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Sub5 =

Sub6 =

Sub7 =

Sub8 =

Sub9 =

Sub10 =

Sub11 =

Sub12 =

Sub13 =

ShareholderA =

ShareholderB =

ShareholderC =

ShareholderD =

ShareholderE =

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ShareholderF =

ShareholderG =

ShareholderH =

ShareholderI =

ShareholderJ =

ShareholderK =

ShareholderL =

ShareholderM =

Bank1 =

Bank2 =

X =

Y =

Date1 =

Date2 =

Date3 =

a =b =

PLR-140094-03

c =

d =

e =

f =

g =

h =

i =

j =

k =

l =

m =

n =

Dear :

This letter responds to your June 30, 2003 request submitted on behalf of Distributing for rulings on certain federal income tax consequences of a proposed transaction. Additional information was received in subsequent letters submitted by mail and facsimile. The rulings in this letter are based on the facts and representations submitted under penalties of perjury in support of the request. Verification of that information may be required as part of the audit process. The material information is summarized below.

Distributing is a U.S. corporation that was incorporated on Date1 (more than 5 years ago). Distributing is the common parent of an affiliated group of corporations that files a consolidated federal income tax return.

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Distributing wholly owns Sub1 and Sub9. Each of Distributing, Sub1, and Sub9 is a financial services holding company. Sub1 owns all the stock of Sub2 and Sub8. Sub2 owns, directly or indirectly, all of the stock of Sub3, Sub4, Sub5, Sub6, and Sub7. Sub9 owns all of the stock of Sub10, which owns all of the stock of Sub11, Sub12, and Sub13.

Distributing is engaged in two primary businesses through its subsidiaries: the X business and the Y business. The X business is conducted by Sub1 through its direct and indirect subsidiaries. The Y business is conducted by Sub9 through its direct and indirect subsidiaries. Financial information has been submitted indicating that the X business and the Y business each have had gross receipts and operating expenses representing the active conduct of a trade or business for each of the past 5 years.

Distributing has only one class of voting common stock outstanding and only one class of preferred stock outstanding. All of the Distributing voting common stock is held by Shareholders A, B, C, D, E, F, G, H, I, J, K, and L in the respective amounts of a%, b%, c%, d%, e%, f%, g%, h%, i%, j%, k%, and l%. All of the Distributing preferred stock is held by Shareholder M, as nominee for Bank1. Bank1, in turn, is the custodian for Bank2, which is the trustee of a grantor trust established by Sub8 for the payment of amounts due in connection with the settlement of a class action lawsuit.

Controlled is a corporation incorporated on Date2. All of the stock of Controlled will be held by Distributing immediately prior to the distribution of the stock of Controlled.

Distributing has provided sufficient documentation indicating that ShareholderA is a valuable employee of Distributing. ShareholderA will cease to serve in such capacity unless (i) ShareholderA is permitted to focus exclusively on Distributing's X business, without having any relation to, or responsibility over, Distributing's Y business and (ii) ShareholderA receives an increased ownership interest in Distributing's X business, but not Distributing's Y business.

For the foregoing reasons, Distributing has proposed the following transaction:

- (i) Distributing will contribute to Controlled all of the stock of Sub9 in exchange for all of the Controlled stock and a note issued by Controlled in favor of ShareholderB (the "Controlled Note").
- (ii) Sub1 will contribute all of the stock of Sub8 to Sub2 in constructive exchange for additional shares of Sub2 stock.

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- (iii) Distributing will distribute all of the Controlled stock on a non pro-rata basis to Shareholders C-L in exchange for an amount of Distributing common stock approximately equal to the fair market value of the Controlled stock that Shareholders C-L each receive.
- (iv) Distributing will distribute the Controlled Note to ShareholderB in exchange for an approximately equal amount (by value) of ShareholderB's Distributing common stock.

As a result of the foregoing transaction, the percentage of outstanding Distributing common stock owned by ShareholderA shall increase from a% to m%.

Prior to the distribution of Controlled stock, Distributing and Controlled plan to enter into a Separation and Distribution Agreement, a Tax Sharing Agreement, an Employee Benefits Agreement, and a Transition Services Agreement, on terms similar to those that would be agreed to by parties bargaining at arm's-length. After the proposed transaction, Distributing and Controlled will continue certain transitional arrangements and practices for a limited time on terms similar to those that would be agreed to by parties bargaining at arm's-length.

In addition, Sub9 paid a cash dividend of \$n to Distributing on Date3, and Distributing anticipates that Sub9 will pay additional cash dividends to Distributing prior to the contribution of the stock of Sub9 to Controlled (collectively referred to herein as "the Sub9 Dividend Distributions").

In connection with the proposed transaction, it has been represented that:

- (a) The fair market value of the Controlled stock to be received by Shareholders C-L, and the Controlled Note to be received by ShareholderB, will be approximately equal to the fair market value of the Distributing stock surrendered by the shareholders in the exchange.
- (b) No part of the consideration to be distributed by Distributing will be received by a shareholder as a creditor, employee, or in any capacity other than that of a shareholder of the corporation.
- (c) Immediately after the distribution of Controlled stock, at least 90 percent of the fair market value of the gross assets of Distributing will consist of the stock of Sub1, a controlled corporation engaged in the active conduct of a trade or business as defined in § 355(b)(2).

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- (d) Immediately after the distribution of Controlled stock, at least 90 percent of the fair market value of the gross assets of Sub1 will consist of the stock of Sub2, a controlled corporation engaged in the active conduct of a trade or business as defined in § 355(b)(2).
- (e) The five years of financial information submitted on behalf of Distributing, Sub1, and Sub2 is representative of the present operations of Distributing, Sub1, and Sub2, and with regard to such corporations, there have been no substantial operational changes since the date of the last financial statements submitted.
- (f) Immediately after the distribution of Controlled stock, the fair market value of the gross assets of the X business directly conducted by Sub2 will equal at least five percent of the total fair market value of the gross assets of Sub2.
- (g) Immediately after the distribution of Controlled stock, at least 90 percent of the fair market value of the gross assets of Controlled will consist of the stock of Sub9, a controlled corporation engaged in the active conduct of a trade or business as defined in § 355(b)(2).
- (h) Immediately after the distribution of Controlled stock, at least 90 percent of the fair market value of the gross assets of Sub9 will consist of the stock of Sub10, a controlled corporation engaged in the active conduct of a trade or business as defined in § 355(b)(2).
- (i) The five years of financial information submitted on behalf of Sub9 and Sub10 is representative of the present operations of Sub9 and Sub10, and with regard to such corporations, there have been no substantial operational changes since the date of the last financial statements submitted.
- (j) Immediately after the distribution of Controlled stock, the fair market value of the gross assets of the Y business directly conducted by Sub10 will equal at least five percent of the total fair market value of the gross assets of Sub10.
- (k) Following the distribution of Controlled stock, Distributing and Controlled will each continue, independently and with its separate employees, the active conduct of the X business and the Y business, respectively.

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- (l) The distribution of Controlled stock will be carried out for the following business purpose: to retain a key employee. The distribution of Controlled stock is motivated, in whole or substantial part, by the corporate business purpose.
- (m) There is no plan or intention by the shareholders or security holders of Distributing to sell, exchange, transfer by gift, or otherwise dispose of any of their stock in, or securities of, either Distributing or Controlled after the transaction.
- (n) There is no plan or intention by either Distributing or Controlled, 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 Rev. Proc. 96-30, section 4.05(1)(b).
- (o) There is no plan or intention to liquidate either Distributing or Controlled, to merge either corporation with any other corporation, or to sell or otherwise dispose of the assets of either corporation after the transaction, except in the ordinary course of business.
- (p) Except in connection with continuing transactions under the intercompany agreements, no intercorporate debt will exist between Distributing and Controlled at the time of, or subsequent to, the distribution of Controlled stock.
- (q) Immediately before the distribution of Controlled stock, items of income, gain, loss, deduction, and credit will be taken into account as required by the applicable intercompany transaction regulations (See Treas. Reg. Sections 1.1502-13 and 1.1502-14 as in effect before the publication of T.D. 8597, 1995-32 I.R.B. 6, and as currently in effect; Treas. Reg. Section 1.1502-13 as published by T.D. 8597). Further, Distributing's excess loss account, if any, with respect to the Controlled stock, will be included in income immediately before the distribution of Controlled stock (see Treas. Reg. Section 1.1502-19).
- (r) Payments made in connection with all continuing transactions, if any, between Distributing and Controlled, will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.
- (s) No two parties to the transaction are investment companies as defined in § 368(a)(2)(F)(iii) and (iv).

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- (t) For purposes of § 355(d), immediately after the distribution of Controlled stock, no person (determined by applying § 355(d)(7)) will hold stock possessing 50 percent or more of the total combined voting power of all classes of Distributing stock entitled to vote, or 50 percent or more of the total value of shares of all classes of Distributing stock, that was acquired by purchase (as defined in §§ 355(d)(5) and (8)) during the five year period (determined after applying § 355(d)(6)) ending on the date of the distribution of Controlled stock.
- (u) For purposes of § 355(d), immediately after the distribution of Controlled stock, no person (determined after applying § 355(d)(7)) will hold stock possessing 50 percent or more of the total combined voting power of all classes of Controlled stock entitled to vote, or 50 percent or more of the total value of shares of all classes of Controlled stock, that was either (i) acquired by purchase (as defined in §§ 355(d)(5) and (6)) during the five year period (determined after applying § 355(d)(6)) ending on the date of the distribution of Controlled stock or (ii) attributable to distributions on Distributing stock that were acquired by purchase (as defined by §§ 355(d)(5) and (8)) during the five-year period (determined after applying § 355(d)(6)) ending on the date of the distribution of Controlled stock.
- (v) The distribution of Controlled stock is not part of a plan or series of related transactions (within the meaning of § 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 Controlled entitled to vote, or stock possessing 50 percent or more of the total value of all classes of stock of either Distributing or Controlled.

Based solely on the information submitted and the representations set forth above, we rule as follows regarding the transaction:

- (1) The Sub9 Dividend Distributions, as described above, shall be treated in the manner provided in § 301(c) (§ 301(a)).
- (2) The transfer by Distributing of assets in exchange for Controlled stock and the Controlled Note, followed by the distribution of Controlled stock and the Controlled Note, will be a reorganization within the meaning of § 368(a)(1)(D). Distributing and Controlled each will be "a party to a

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reorganization" within the meaning of § 368(b).

- (3) No gain or loss will be recognized by Distributing on the transfer of assets to Controlled in exchange for Controlled stock and the Controlled Note (§§ 357(a) and 361(a)).
- (4) No gain or loss will be recognized by Controlled on the receipt of assets from Distributing in exchange for Controlled stock and the Controlled Note (§ 1032(a)).
- (5) The basis of each asset received by Controlled from Distributing will equal the basis of such asset in the hands of Distributing immediately prior to the transaction (§ 362(b)).
- (6) The holding period of each asset received by Controlled from Distributing will include the period during which Distributing held such asset (§ 1223(2)).
- (7) No gain or loss will be recognized by Distributing upon the distribution to its shareholders of the stock of Controlled and the Controlled Note in exchange for Distributing stock held by such shareholders (§§ 361(c), 355(d), 355(e)).
- (8) No gain or loss will be recognized by (and no amount will be includible in the income of) the shareholders of Distributing on the receipt of stock of Controlled in exchange for Distributing stock (§ 355(a)(1)).
- (9) ShareholderB will recognize the entire amount of gain or loss, as determined under § 1001, on the exchange of Distributing stock for the Controlled Note (§ 1001(c)).
- (10) The aggregate basis of the Distributing stock and the Controlled stock held by each of Shareholders C-L immediately after the distribution of Controlled stock will equal the aggregate basis of each of such shareholder's Distributing stock held immediately before the distribution of Controlled stock, allocated in the manner described in Treas. Reg. § 1.358-2 (§ 358(a)(1); Treas. Reg. § 1.358-1(a)).
- (11) The holding period of the Controlled stock received by Shareholders C-L will include the holding period of the Distributing stock surrendered in exchange therefor, provided the Distributing stock is held as a capital

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asset by such shareholders on the date of the distribution (§ 1223(1)).

- (12) As provided in § 312(h), proper allocation of earnings and profits between Distributing and Controlled will be made under Treas. Reg. §§ 1.312-10(a) and 1.1502-33(e)(3).

Except as expressly provided herein, no opinion is expressed or implied concerning the tax treatment of the transaction under any other provision of the Code or with respect to consequences of any aspect of any transaction or item discussed or referenced in the rulings contained in this letter.

A copy of this letter must be attached to any income tax return to which it is relevant.

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.

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

Sincerely,

Thomas I. Russell
Assistant to the Branch Chief, Branch 5
Office of Associate Chief Counsel
(Corporate)