

Internal Revenue Service

Department of the Treasury

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Date:

March 03, 2000

LEGEND:

Distributing	=
Controlled	=
State X	=
Business Y	=
Business Z	=
Branch W	=
Type V assets	=
Shareholder A	=
Shareholder B	=

This is in response to your authorized representative's letter dated June 24, 1999, requesting rulings under § 355 of the Internal Revenue Code (the "Code") with respect to a proposed transaction. Additional information was received in letters dated November 12, 1999, December 30, 1999, January 25, 2000, and February 24, 2000. The material information submitted is summarized below.

Distributing is a State X corporation engaged in Business Y. Distributing has only one class of stock outstanding, 50% of which is owned by Shareholder A and Shareholder A's spouse and 50% of which is owned by Shareholder B and Shareholder B's spouse.

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Controlled, also a State X corporation, is a wholly owned subsidiary of Distributing engaged in Business Z. Controlled conducts Business Z in four locations in State X. Branch W of Business Z is in the same town as Distributing's Business Y headquarters. Financial information has been received indicating that Distributing and Controlled have each had gross receipts and operating expenses representing the active conduct of a trade or business for each of the last five years.

Shareholder A wishes to leave Business Y and to concentrate his attention and efforts on Business Z. Shareholder B is willing to remain in both Business Y and Business Z. In order to allow Shareholder A to focus on Business Z, the following series of transactions is proposed:

Controlled will distribute Branch W to Distributing. At the same time and in order to equalize values, Distributing will contribute to Controlled certain Type V assets (the "Contribution") in constructive exchange for Controlled stock and in exchange for the assumption of certain related liabilities. Immediately thereafter, Distributing will distribute all of its Controlled stock to Shareholder A and Shareholder A's spouse (the "Distribution") in exchange for their Distributing stock. After the distribution, Distributing will continue in the active conduct of Business Y and of Branch W of Business Z, and Controlled will continue in the active conduct of Business Z in its other locations.

The following representations have been made in connection with the Contribution:

(a)(i) No stock or securities will be issued for services rendered to or for the benefit of Controlled, and (ii) No stock or securities will be issued for indebtedness of Controlled that is not evidenced by a security or for interest on indebtedness of Controlled which accrued on or after the beginning of the holding period of Distributing for the debt.

(b) The transfer is not the result of the solicitation by a promoter, broker, or investment house.

(c) Distributing will not retain any rights in the property transferred to Controlled.

(d) The value of the stock received in exchange for accounts receivable will be equal to the net value of the accounts transferred, i.e. the face amount of the accounts receivable previously included in income less the amount of the reserve for bad debts.

(e) The adjusted basis and the fair market value of the assets to be transferred by Distributing will, in each instance, be equal to or exceed the sum of the liabilities to be assumed by Controlled.

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(f) The liabilities of Distributing to be assumed by Controlled were incurred in the ordinary course of business and are associated with the assets to be transferred.

(g) There is no indebtedness between Distributing and Controlled and there will be no indebtedness created in favor of Distributing as a result of the transaction.

(h) The transfers and exchanges will occur under a plan agreed upon before the transaction in which the rights of the parties are defined.

(i) All exchanges will occur on approximately the same date.

(j) There is no plan or intention on the part of Distributing to redeem or otherwise reacquire any stock or indebtedness to be issued in the proposed transaction.

(k) Taking into account any issuance of additional shares of Controlled stock; any issuance of stock for services; the exercise of any Controlled stock rights, warrants, or subscriptions; a public offering of Controlled stock; and the sale, exchange, transfer by gift, or other disposition of any of the stock of Controlled to be received in the exchange, Distributing will be in "control" of Controlled within the meaning of section 368(c) of the Code.

(l) Each transferor will receive stock, securities, or other property approximately equal to the fair market value of the property transferred to Controlled or for services rendered or to be rendered for the benefit of Controlled.

(m) There is no plan or intention by Controlled to dispose of the transferred property other than in the course of normal business operations.

(n) Each of the parties to the transaction will pay its own expenses, if any, incurred in connection with the proposed transaction.

(o) Controlled will not be an investment company within the meaning of § 351(e)(1) of the Code and § 1.351-1(c)(1)(ii) of the Income Tax Regulations.

(p) Distributing is not under the jurisdiction of a court in a Title 11 or similar case (within the meaning of § 368(a)(3)(A)) and the stock or securities received in the exchange will not be used to satisfy the indebtedness of a debtor.

(q) Controlled will not be a "personal service corporation" within the meaning of section 269A of the Code.

The following representations have been made in connection with the Distribution:

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(r) Any indebtedness owed by Controlled to Distributing will not constitute stock or securities.

(s) 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 Distributing.

(t) The five years of financial information submitted on behalf of Distributing and Controlled are representative of each corporation's present operation, and with regard to each such corporation, there have been no substantial operational changes since the date of the last financial statements submitted.

(u) Following the transaction, Distributing and Controlled will each continue the active conduct of its business, independently and with its separate employees.

(v) The Distribution is carried out for the following corporate business purpose: in order to separate interests so as to enhance shareholder/director/officer attention and expertise. The Distribution is motivated, in whole or substantial part, by that corporate business purpose.

(w) 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.

(x) 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 section 4.05(1)(b) of Rev. Proc. 96-30.

(y) 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.

(z) The income tax liability for the taxable year in which investment credit property (including any building to which section 47(d) applies), is transferred will be adjusted pursuant to section 50(a)(1) or (a)(2) (or section 47, as in effect before amendment by Public Law 101-508, Title 11, 104 Stat. 1388, 536 (1990), if applicable) to reflect an early disposition of the property.

(aa) Distributing neither accumulated its receivables nor made extraordinary payment of its payables in anticipation of the transaction.

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(bb) No intercorporate debt will exist between Distributing and Controlled at the time of, or subsequent to, the distribution of the Controlled stock.

(cc) Immediately before the Distribution, items of income, gain, loss, deduction, and credit will be taken into account as required by the applicable intercompany transaction regulations (see § 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; section 1.1502-13 as published by T.D. 8597). Further, Distributing's excess loss account with respect to the Controlled stock will be included in income immediately before the distribution (see § 1.1502-19).

(dd) 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.

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

Based solely on the information submitted and the representations made, we have concluded that:

(1) Pursuant to § 351(b)(1), gain, if any to Distributing shall be recognized on the Contribution as described above, but not in excess of the fair market value of Branch W (i.e., the property received from Controlled in the exchange other than the constructive receipt of Controlled stock). Loss will not be recognized. Section 351(b)(2). See Treas. Reg. § 1.1502-13(c)(7), Example 3(c). The gain will be taken into account immediately before the Distribution. Treas. Reg. 1.1502-13(c).

(2) No gain or loss will be recognized by Controlled on the constructive issuance of its stock in the Contribution. Section 1032.

(3) The basis of the assets received by Controlled in the Contribution will equal the basis of those assets in the hands of Distributing immediately prior to the Contribution, increased by the amount of gain, if any, recognized on the exchange. Section 362(a).

(4) The holding period of each asset received by Controlled in the Contribution will equal the holding period of the asset in the hands of Distributing immediately prior to the Contribution. Section 1223(2).

(5) Distributing will increase its basis in the stock of Controlled by the basis of the assets transferred to Controlled and by the fair market value of the property received from Controlled in the exchange, and reduce the basis by the sum of the liabilities assumed by Controlled. Section 358(a) and (d).

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(6) No gain or loss will be recognized by Distributing upon the distribution of the Controlled stock as described above. Section 355(c).

(7) No gain or loss will be recognized by (and no amount will be included in the income of) Shareholder A and Shareholder A's spouse upon the receipt of the stock of Controlled in exchange for their Distributing stock. Section 355(a)(1).

(8) The basis of the stock of Controlled to be received by Shareholder A and Shareholder A's spouse will equal the basis of the Distributing stock exchanged therefor. Section 358(a).

(9) The holding period of the Controlled stock to be received by Shareholder A and Shareholder A's spouse will include the period of the Distributing stock surrendered in the exchange, provided that such stock is held as a capital asset by those shareholders on the day of the exchange. Section 1223(1).

(10) As provided in section 312(h) of the Code, proper allocation of earnings and profits between Distributing and Controlled will be made under §§ 1.312-10(b) and 1.1502-33(e).

No opinion is expressed as to the tax treatment of the transaction 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 transaction that are not specifically covered by the above ruling.

In accordance with a power of attorney on file in this office, copies of this letter are being sent to your authorized representatives.

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

Sincerely yours,
Assistant Chief Counsel (Corporate)
By Lewis K Brickates
Assistant to the Chief, Branch 2