

Internal Revenue Service

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Department of the Treasury

Washington, DC 20224

Third Party Communication: None

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Date:

June 22, 2007

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LEGEND:

Distributing =

Controlled =

Sub =

State X =

Shareholder A =

Shareholder B =

Shareholder C =

Business 1 =

Business 2 =

Irrevocable Trust =

Section Y =

Z =

Date =

Dear :

This letter responds to your letter dated September 16, 2006, requesting rulings as to the federal income tax consequences of a proposed transaction. Additional information was submitted on November 16, 2006 and January 17, 2007. The information submitted is summarized below.

The rulings contained in this letter are based on facts and representations submitted by the taxpayer and accompanied by a penalty 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 the controlled corporation or both (see § 355(a)(1)(B) of the Internal Revenue Code (the "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 fifty percent or greater interest in the distributing corporation or the controlled corporation (see §§ 355(e)(2)(A)(ii) and 1.355-7).

SUMMARY OF FACTS

Distributing is an accrual basis State X corporation and the common parent of an affiliated group of corporations that files a consolidated federal income tax return. Distributing has a single class of voting common stock outstanding, which is equally owned by three shareholders, Shareholder A, Shareholder B and Shareholder C (the "Shareholders").

Each of Sub and Controlled is a State X corporation and has a single class of voting common stock outstanding, all of which is owned by Distributing.

Sub conducts Business 1 and Controlled conducts Business 2. Shareholder A and Shareholder B are involved in Business 1 and Shareholder C is involved in Business 2. The Shareholders are related to one another.

Financial information has been received indicating that each of Business 1 and Business 2 has had gross receipts and operating expenses representative of an active trade or business for each of the past five years.

Sub and Controlled are distinct and separate businesses. The Shareholders disagree with respect to how to operate the businesses. It is the belief of management that the two businesses could be operated more efficiently if the ownership and management were separated. In order to provide key employees with an equity ownership of their respective business and allow each business to have a separate corporate focus, Distributing plans to exchange all of the issued and outstanding Controlled common stock owned by Distributing for all of the Distributing common stock owned by Shareholder C (the "Exchange").

Shareholder A was the grantor of the Irrevocable Trust which was partially funded with all of Shareholder A's Distributing common stock. Section Y provided that when Shareholder A attained the age of z, the trustees would distribute to Shareholder A outright and absolutely the balance of principal and accumulated income of the Irrevocable Trust and that it would then terminate. The Irrevocable Trust terminated and distributed its assets to Shareholder A on Date because the trustees felt that it was not practical to continue its administration.

REPRESENTATIONS

The following representations have been made with respect to the Exchange:

- (a) The fair market value of the Controlled common stock to be received by Shareholder C will be approximately equal to the fair market value of the Distributing common stock surrendered by Shareholder C 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) The five years of financial information provided on behalf of Business 1 conducted by Distributing's separate affiliated group, through Sub, is representative of the present business operations conducted Distributing's separate affiliated group, and, with regard to such business, there have been no substantial operational changes since the date of the last financial statements submitted.

- (d) The five years of financial information submitted on behalf of Business 2 is representative of Business 2's present operations, and with regard to Business 2 there have been no substantial operational changes since the date of the last financial statements submitted.
- (e) Following the transaction, Distributing (through Sub) and Controlled will each continue the active conduct of their respective businesses, independently and each with its separate employees.
- (f) The distribution of the stock of Controlled is carried out for the following corporate business purposes: to attain operating efficiencies for Business 1 and Business 2, to eliminate disagreement between the Shareholders with respect to how the two businesses should be operated and to allow the persons who are currently operating the respective businesses to have equity ownership of their respective businesses without having to share ownership with non-participating owners. The distribution of the stock of Controlled is motivated, in whole or substantial part, by one or more of these corporate business purposes.
- (g) The Exchange is not being used principally as a device for the distribution of earnings and profits of Distributing, Controlled, or both.
- (h) Distributing neither accumulated its receivables nor made extraordinary payment of its payables in anticipation of the transaction.
- (i) No intercorporate debt will exist between Distributing and Controlled at the time of, or subsequent to, the distribution of the stock of Controlled, other than payables and receivables that arise in the ordinary course of business.
- (j) Immediately before the Exchange, 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; § 1.1502-13, as published by T.D. 8597). Furthermore, Distributing's excess loss account, if any, with respect to Controlled common stock (or the excess loss account that Distributing may have in the stock of another member that is required to be taken into account by § 1.1502-19) will be included in income immediately before the Exchange (see § 1.1502-19).
- (k) 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.

- (l) Neither Distributing nor Controlled is an investment company as defined in § 368(a)(2)(F)(iii) and (iv).
- (m) The Exchange is not part of a plan or series of related transactions (within the meaning of § 1.355-7) pursuant to which one or more persons will acquire directly or indirectly stock representing a fifty percent or greater interest (within the meaning of § 355(d)(4)) in Distributing or Controlled (including any predecessor or successor of any such corporation).

Under § 673(a), a grantor will be treated as the owner of any portion of a trust in which he has a reversionary interest in either the corpus or the income therefrom, if, as of the inception of that portion of the trust, the value of such interest exceeds five percent of the value of such portion.

Rev. Rul. 85-13, 1985-1 C.B. 184, holds that if a grantor is treated as the owner of the entire trust, the grantor is treated as the owner of the trust's assets for federal income tax purposes.

RULINGS

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

- (1) Prior to Date, Shareholder A was treated as the owner of the corpus of the Irrevocable Trust because Shareholder A retained a reversionary interest described in section 673(a) over that portion of the Irrevocable Trust. In accordance with Rev. Rul. 85-13, Shareholder A was the owner of all of the Irrevocable Trust assets for federal income tax purposes.
- (2) No gain or loss will be recognized by Distributing upon the distribution of Controlled common stock to Shareholder C in the Exchange. Sections 355(c)(1).
- (3) No gain or loss will be recognized by Shareholder C (and no amount will be included in income) upon the receipt of Controlled common stock pursuant to the Exchange. Sections 355(a)(1) and (2).
- (4) Shareholder C's basis in the Controlled common stock will equal the basis in the shares of Distributing common stock surrendered in the Exchange. Section 358(a)(1).
- (5) The holding period of the Controlled common stock received by Shareholder C will include the holding period of the Distributing common stock surrendered in the Exchange, provided that the Distributing common

stock is held as a capital asset on the date of the Exchange. Section 1223(1).

- (6) Earnings and profits will be allocated between Distributing and Controlled in accordance with §§ 312(h), 1.312-10(b) and 1.1502-33(e)(3).

CAVEATS

No opinion is expressed about the tax treatment of the Exchange 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 Exchange that are not specifically covered by the above rulings. In particular, no opinion is expressed regarding whether the Exchange: (i) satisfies the business purpose requirement of § 1.355-2(b); (ii) is used principally as a device for the distribution of the earnings and profits of the distributing corporation or the controlled corporation or both (see §§ 355(a)(1)(B) 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 fifty percent or greater interest in the distributing corporation or the controlled corporation under § 355(e)(2)(A)(ii).

PROCEDURAL STATEMENTS

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

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

In accordance with the power of attorney on file in this office, a copy of this ruling letter will be forwarded to your authorized representative.

Sincerely,

Lisa A. Fuller
Senior Counsel, Branch 1
Office of Associate Chief Counsel (Corporate)