

Internal Revenue Service

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Department of the Treasury
Washington, DC 20224

Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:CORP:B03 – PLR-134433-03

Date:

November 12, 2003

In Re:

Acquiring =

Parent =

Target =

Newco 2 =

Newco 3 =

Newco 4 =

Sub 1 =

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Sub 2 =

Sub 3 =

Sub 4 =

Sub 5 =

Sub 6 =

Sub 7 =

LLC 1 =

LLC 2 =

Partnership =

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Buyer =

State X =

Business A =

Business B =

Assets, Obligations =
and Officers

Certain Assets =

Date 1 =

Date 2 =

Dear :

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We respond to your letter dated May 30, 2003, for rulings concerning the Federal income tax consequences of a proposed transaction. Additional information was submitted in letters dated July 31, October 1, and October 29, 2003. The material information submitted for consideration is summarized below.

Parent is a publicly traded State X corporation and the common parent of a consolidated group (the Target Group). Parent's only authorized and outstanding class of stock is a single class of common stock. Parent is directly engaged in Business A and owns all of the stock of Subs 1 through 7. Parent also owns all of the interests of LLC 1 and LLC 2, which together own all of the partnership interests in Partnership. Subs 2 through 7 are engaged in Business B. Sub 1 holds intellectual property used by both Business A and Business B. Acquiring is a yet-to-be-formed State X corporation.

For what has been represented as a valid business purpose, the taxpayers have proposed and partially consummated the following transaction:

- (i) Parent forms Acquiring, Acquiring forms Newco 2 and Newco 4, and Newco 2 forms Newco 3. Each entity is a State X corporation.
- (ii) Newco 2 merges with and into Parent under State X law, with Parent surviving. As a result of this step (ii), and by operation of law, all of the Parent shareholders exchange their Parent stock for Acquiring stock, and all of the Newco 2 stock converts into Parent stock with Acquiring becoming the sole shareholder of Parent. The nominal Acquiring stock owned by Parent is cancelled. Pursuant to this step, Parent changes its name to Target. All references to Target refer to the entity surviving this step (ii).
- (iii) Newco 4 merges with and into Acquiring under State X law, with Acquiring surviving. Pursuant to this step, Acquiring changes its name to Parent's former name. All references to Acquiring refer hereinafter to the entity surviving this step (iii).
- (iv) Target distributes and/or assigns Assets, Obligations and Officers to Acquiring.
- (v) Sub 1 distributes certain intangibles associated with Business A, primarily intellectual property, to Target.

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- (vi) Target contributes the stock of Subs 1 through 7 and its interests in LLC 1 and LLC 2, who collectively own all of the interests in Partnership, to Newco 3, in actual or constructive exchange for the stock of Newco 3.
- (vii) Target distributes and/or assigns Certain Assets to Acquiring.
- (viii) Newco 3 merges with and into Acquiring under State X law, with Acquiring surviving. No consideration will be issued, and it will result in Acquiring's directly owning all of the stock of Subs 1 through 7 and all of the interests in LLC 1 and LLC 2, who collectively own all of the interests in Partnership.
- (ix) Acquiring will enter into an agreement to sell all of the stock of Target to an unrelated third party (Buyer), and Acquiring and Buyer will file a joint election under §338(h)(10) of the Internal Revenue Code with respect to the sale (the Sale). In connection with the Sale, Target will distribute any assets to Acquiring that were not previously distributed in steps (iv) and (vii).

Steps (i) through (iv) were completed on Date 1. Following the transaction, Acquiring indirectly will be engaged in Business B through its sole ownership of Subs 1 through 7 and LLC 1 and LLC 2, and Buyer will own the assets and liabilities of Business A. This proposed transaction will enable the Acquiring group to focus on the operation and growth of Business B.

The taxpayers have made the following representations in connection with the proposed and partially consummated transaction:

- (a) The fair market value of the Acquiring stock received by each Target shareholder in the proposed transaction will be approximately equal to the fair market value of the Target stock surrendered in the exchange.
- (b) At least 50 percent of the proprietary interest in Target will be exchanged for Acquiring stock and will be preserved (within the meaning of §1.368-1(e)(1)(i) of the Income Tax Regulations).
- (c) Acquiring will acquire approximately at least 90 percent of the fair market value of the net assets and at least 70 percent of the fair market value of the gross assets held by Target immediately prior to the proposed transaction. Acquiring will also acquire all of the proceeds of the Sale. For purposes of this representation, amounts used by Target to pay its

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reorganization expenses will be included as assets of Target held immediately before the proposed transaction. There will be no dissenters to the proposed transaction.

- (d) After the proposed transaction, the shareholders of Target will be in control of Acquiring within the meaning of § 368(a)(2)(H).
- (e) Acquiring has no plan or intention to reacquire, directly or through a related person, any of its stock issued in the proposed transaction.
- (f) Acquiring has no plan or intention to sell or otherwise dispose of any of the stock or assets of Target acquired in the proposed transaction, except for dispositions made in connection with the proposed transaction or dispositions made in the ordinary course of business.
- (g) The liabilities of Target assumed by Acquiring, if any, were incurred by Target in the ordinary course of its business and are associated with the assets transferred.
- (h) Following the proposed transaction, Acquiring will continue the historic business of Target or use a significant portion of Target's historic business assets in a business.
- (i) In connection with the proposed transaction, any warrants, options, convertible securities, or any other type of right pursuant to which any person could acquire stock in Target will be converted into an identical right to acquire Acquiring stock. Subsequent to the proposed transaction, there will be no outstanding warrants, options, convertible securities, or any other type of right pursuant to which any person could acquire stock in Acquiring that, if exercised or converted, would affect Target shareholders' acquisition or retention of control of Acquiring, as defined in §368(a)(2)(H).
- (j) Acquiring, Target, and the shareholders of Target will pay their respective expenses, if any, incurred in connection with the proposed transaction.
- (k) No debt exists or will exist between Acquiring and Target, and none has been cancelled, forgiven, or discounted, in connection with the proposed transaction.
- (l) No two parties to the proposed transaction are investment companies as defined in § 368(a)(2)(F)(iii) and (iv).

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- (m) Throughout the proposed transaction, the fair market value of the assets of Target transferred to Acquiring will equal or exceed the sum of the liabilities to be assumed by Acquiring within the meaning of § 357(d).
- (n) The total adjusted basis of the assets of Target transferred to Acquiring will equal or exceed the sum of the liabilities to be assumed by Acquiring within the meaning of § 357(c).
- (o) Target is not under the jurisdiction of a court in a Title 11 or similar case within the meaning of § 368(a)(3)(A).
- (p) Following the proposed transaction, Acquiring will own all of the issued and outstanding Target stock. Pursuant to the Sale by Acquiring of all of the outstanding Target stock to Buyer, Acquiring and Buyer will file a timely joint election under § 338(h)(10) after Buyer has made a “qualified stock purchase,” within the meaning of § 338(d)(3), of the stock of Target (Acquisition Date).
- (q) Target will be a member of the Target Group for the taxable period that includes the date of the Sale.

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

- (1) For Federal income tax purposes, the proposed transaction will be treated as if Buyer purchased all of the Target stock in a qualified stock purchase (QSP) within the meaning of § 338(d)(3), provided that (i) the QSP occurs by Date 2, which is not more than 12 months after the date of this letter, (ii) Buyer makes a timely election under § 338(g), and (iii) Buyer and Acquiring make a timely election under § 338(h)(10). Acquiring will be treated as if it did not sell the Target stock, but rather Target will be treated as if it (while owned by Acquiring) sold all of the assets and liabilities associated with Business A to Buyer in a single transaction (Deemed Sale) as of the Acquisition Date. Target will be treated as if (i) it transferred all of its assets (including the stock of Subs 1 through 7, the interests in LLC 1 and LLC 2, and the proceeds of the Deemed Sale) to Acquiring solely in exchange for voting shares of Acquiring stock (and assumption of liabilities), and (ii) Target distributed the Acquiring common stock to its shareholders, in exchange for their Target stock, pursuant to the complete liquidation of Target as of the close of the Acquisition Date

but after the Deemed Sale (§ 338(h)(10); §§ 1.338(h)(10)-1(a) and (d)). Accordingly, gain (including any items of recapture) and loss from the Deemed Sale will be included in the consolidated Federal income tax return of the Target Group for the taxable period that includes the Acquisition Date, and neither gain nor loss from the sale of Target stock will be included in the income of Acquiring (§ 338(h)(10); §§ 1.338(h)(10)-1(a) and (d)). Steps (vi) and (viii) of the proposed transaction and the transitory existence of Newco 3 will be disregarded (Rev. Rul. 78-397, 1978-2 C.B. 150). Target's transfer of substantially all of its assets to Acquiring solely in exchange for Acquiring stock, followed by the distribution of the Acquiring stock in complete liquidation of Target, will be treated as a reorganization described in § 368(a)(1)(D) (Rev. Rul. 67-274, 1967-2 C.B. 141; §§ 1.338(h)(10)-1(d) and 1.338(h)(10)-1(e), Example 3). For purposes of this ruling, "substantially all" means at least 90 percent of the fair market value of the corporation's net assets and at least 70 percent of the fair market value of the corporation's gross assets. Target and Acquiring each will be "a party to the reorganization" under § 368(b).

- (2) Target will recognize no gain or loss upon the transfer of all of its assets (including the stock of Subs 1 through 7) to Acquiring and the assumption by Acquiring of certain liabilities (if any), solely in exchange for Acquiring stock (§§ 361(a) and 357(a)).
- (3) Acquiring will recognize no gain or loss upon receipt of substantially all of the assets of Target, solely in exchange for Acquiring stock and the assumption of Target liabilities within the meaning of § 357(d) (§ 1032(a)).
- (4) Target will recognize no gain or loss on the distribution of Acquiring stock to Target shareholders pursuant to the proposed transaction (§ 361(c)(1)).
- (5) Target's shareholders will recognize no gain or loss (and no amount will be included in their income) upon the exchange of their shares of Target stock solely for shares of Acquiring common stock (§ 354(a)(1)).
- (6) Acquiring's basis in each Target asset received in the proposed transaction will be equal to the basis of such asset in the hands of Target immediately prior to the transfer (§ 362(b)).
- (7) Acquiring's holding period for each asset received from Target will include the period during which Target held such asset (§ 1223(2)).

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- (8) The basis of the Acquiring stock received by the Target shareholders in the proposed transaction will equal the basis of the Target stock surrendered in exchange therefor (§ 358(a)(1)).
- (9) The holding period of the Acquiring stock received by the Target shareholders will include the holding period of the Target stock surrendered in proposed transaction, provided that Target shareholders held such stock as a capital asset on the date of the exchange (§1223(1)).
- (10) Acquiring will succeed to and take into account the items of Target described in § 381(c) and the regulations thereunder, subject to the conditions and limitations specified in §§ 381, 382, 383, and 384 and the regulations thereunder (§§ 381(a); 1.381(a)-1; § 1.338(h)(10)-1(d)).
- (11) The distribution in step (v) will be treated as a distribution under § 311, resulting in deferred gain or loss under § 1.1502-13(c). Such gain or loss will be accelerated under § 1.1502-13(d) in the Sale.
- (12) Acquiring will succeed to, as of the close of the Acquisition Date, the entire remaining balance of any intercompany items recognized but not yet taken into account by Target (§§ 1.338(h)(10)-1(d), § 1.1502-13 and § 1.1502-14 as in effect before the publication of T.D. 8597, 1995-2 C.B. 147, and as currently in effect; § 1.1502-13 as published by T.D. 8597).
- (13) Members of the Acquiring group will take into account any items of intercompany gain or loss with respect to the assets that Target is deemed to transfer to Buyer pursuant to the Deemed Sale, as of the close of the Acquisition Date (§§ 1.338(h)(10)-1(d), 1.1502-13 and § 1.1502-14 as in effect before the publication of T.D. 8597, 1995-2 C.B. 147, and as currently in effect; § 1.1502-13 as published by T.D. 8597).
- (14) Acquiring will succeed to and take into account the earnings and profits, or deficit in earnings and profits, of Target immediately after the proposed transaction (§§ 381(c)(2)(A); 1.381(c)(2)-1). Any deficit in the earnings and profits of Target will be used only to offset earnings and profits accumulated after the proposed transaction (§§ 381(c)(2)(B) and 1.1502-33(a)).
- (15) The Target Group will remain in existence after consummation of the proposed transaction, with Acquiring as the new common parent (§1.1502-75(d)(2)(ii)).

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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 and are conditioned upon the completion of steps (v) through (ix) on or before Date 2. 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.

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.

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.

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

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

Sincerely,

Filiz A. Serbes

Filiz A. Serbes
Chief, Branch 3
Office of Associate Chief Counsel
(Corporate)

cc: