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Person To Contact:

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**LEGEND:**

Taxpayer =

Corp X =

Corp LLC =

State A =

Individual A =

Individual B =

K =

News 1 =

News 2 =

News 3 =

W =

X =

Dear :

This letter responds to your ruling request dated August 15, 2003, submitted on behalf of Taxpayer, concerning the proper treatment of prepaid subscription income under section 455 of the Internal Revenue Code. Specifically, you request the following ruling:

That no portion of the amount of prepaid subscription income that Taxpayer has deferred but has not recognized pursuant to an election under section 455 will be immediately included in its gross income when Taxpayer's assets and liabilities

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are transferred to Corp LLC and no income, gain, or loss will be realized by Taxpayer, Corp X, and Corp LLC as a result of the transfer of property from Taxpayer to Corp LLC.

## FACTS

Taxpayer is a corporation formed under State A law and a wholly-owned subsidiary of Corp X. Taxpayer computes its income under the accrual method of accounting and is engaged in the publication of numerous K newsletters. These newsletters are offered to the public as well as K professionals on a subscription basis and subscribers prepay subscriptions for a fixed period of time.

Taxpayer currently has an election in effect to defer the inclusion of prepaid subscription income in gross income pursuant to section 455 of the Code. As a result, Taxpayer's prepaid subscription income is included in gross income ratably over the period of the subscription.

The editorial content of certain of Taxpayer's newsletters is the responsibility of Individual A, whereas the editorial content of other newsletters is the responsibility of Individual B. In order to maximize the marketing effectiveness of these two authors and to more clearly identify each author with an entity, Taxpayer desires to separate the marketing of Individual A's newsletters from the newsletters identified with Individual B. In order to accomplish this objective, Taxpayer has formed a new entity, Corp LLC, in accordance with State A law. Corp LLC, which is a single member limited liability company with Taxpayer as the sole member, will be a disregarded entity for Federal income tax purposes.

Taxpayer proposes to transfer its newsletters entitled News 1, News 2, and News 3, and potentially certain other newsletters, along with certain hard assets to Corp LLC. Moreover, Taxpayer also proposes to transfer the deferred subscription liabilities associated with the transferred newsletters to Corp LLC.

Taxpayer's deferred subscription liability income resulting from its section 455 election is \$w. The portion of this deferred subscription liability income that is applicable to the newsletters which taxpayer proposes to transfer to Corp LLC is \$x.

## LAW AND ANALYSIS

Section 455 of the Code provides that a taxpayer may elect to include "prepaid subscription income," as defined in section 455(d), in gross income for the taxable years during which a liability to furnish or deliver a periodical exists, rather than for the year in which the income was received.

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Section 455(d)(2) provides that the term “liability” means a liability “to furnish or deliver a newspaper, magazine, or other periodical.”

Section 455(b) describes two situations that require deferred subscription income to be immediately included in gross income. Section 455(b)(1) provides that if the liability described in section 455(d)(2) ends, then so much of the prepaid subscription income as was not includible in gross income for preceding taxable years must be included in gross income for the tax year in which the liability ends. Section 455(b)(2) provides a similar result “[i]f the taxpayer dies or ceases to exist.”

Section 455 represents an exception to the normal treatment of prepaid income for tax accounting purposes. Under the “all events” test of section 451 and pursuant to section 446, it is within the Commissioner’s discretion to require that, for a taxpayer on the accrual basis, all the events that fix the right to receive income occur when (1) the required performance takes place, (2) payment is due, or (3) payment is made, whichever happens first. See Schlude v. Commissioner, 372 U.S. 128 (1963); Rev. Rul. 79-195, 1979-1 C.B. 177.

Taxpayer does not die or cease to exist with the transfer of assets and liabilities to Corp LLC. Thus, the only reason for ending the deferral of the prepaid subscription income that will exist at the time of transfer is if Taxpayer’s liability ends with the transfers to Corp LLC.

Section 301.7701-3(b)(1)(ii) provides that a domestic eligible entity (a business entity that is not classified as a corporation under section 301.7701-2(b)(1), (3), (4), (5), (6), (7), or (8)) with a single owner is disregarded as an entity separate from its owner for federal tax purposes unless the entity elects to be treated as a corporation. If an entity is disregarded, and its owner is a corporation, its activities are treated in the same manner as those of a division of its owner. Section 301.7701-2(a). At the time of transfer of assets and liabilities from Taxpayer to Corp LLC, Corp LLC will be a disregarded entity with Taxpayer as its sole owner. Thus, in effect, Taxpayer will be treated for federal tax purposes as owning all of the assets and having all the liabilities of Corp LLC.

## CONCLUSION

Based solely on the information provided and the representations made, we conclude that no income, gain, or loss will be realized by Taxpayer, Corp X, and Corp LLC upon the transfer of property from Taxpayer to Corp LLC because Corp LLC will be disregarded as an entity separate from Taxpayer. Further, we conclude that Taxpayer’s liability under section 455 will not end when it transfers assets and liabilities to Corp LLC

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because Corp LLC will be disregarded as an entity separate from Taxpayer and its liabilities will not cease with the transfers to Corp LLC. Therefore, Taxpayer must continue to use the income deferral method of section 455 and the closing balances of Taxpayer's prepaid subscription income account are not accelerated into gross income when the assets and liabilities are transferred to Corp LLC.

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. Further, no opinion is expressed as to the tax treatment of the transaction under the provisions of any other section of the Code and regulations which may be applicable thereto, or the tax treatment of any conditions existing at the time of, or effects resulting from, the transaction which are not specifically set forth by the above ruling.

A copy of this letter must be attached to any income tax return to which it is relevant. We enclose a copy of the letter for this purpose. Also enclosed is a copy of the letter ruling showing the deletions proposed to be made in the letter when it is disclosed under section 6110.

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

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 the appropriate party. 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.

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

Sincerely,

ROBERT M. BROWN  
Associate Chief Counsel  
(Income Tax and Accounting)

By: \_\_\_\_\_  
THOMAS A. LUXNER  
Chief, Branch 6  
Office of Associate Chief Counsel  
(Income Tax and Accounting)

Enclosures:

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Copy of letter

Copy for section 6110 purposes

Cc: