

Internal Revenue Service

Department of the Treasury

Index Number: 302.03-00, 302.03-02,
302.05-01, 302.05-03

Number: **200022020**

Release Date: 6/2/2000

Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:

CC:DOM:CORP:1-PLR-118169-99

Date:

March 1, 2000

LEGEND:

Company =

State A =

Business B =

Father =

Mother =

Daughter =

Son =

Year 1 =

Year 2 =

Value =

w =

Dear :

We respond to your letter dated November 5, 1999, requesting rulings concerning the federal income tax consequences of a proposed transaction. The information submitted for consideration is summarized below.

Company, an accrual method taxpayer with a July 31 year end, is incorporated in State A and is engaged in Business B. Company has outstanding a single class of stock (voting common stock), all of which is held by Father, Mother, Daughter, and Son. Mother holds w shares of the Company stock, some of which were acquired by Mother as a gift from Father within the ten year period prior to the proposed transaction.

All of the shares of Company stock acquired by Daughter and Son within the ten year period prior to the proposed transaction were given to them by Mother and Father. Mother's gifts to Daughter and Son occurred between Year 1 and Year 2. Mother and Father made these gifts to encourage Daughter and Son to increase their commitment to long-term involvement in Company, to equalize ownership between Daughter and Son, and for estate planning purposes.

Mother, Father, Daughter, and Son are all officers and directors of Company.

PLR-118169-99

Mother wishes to completely terminate her interest in Company. Accordingly, the following steps are proposed:

- (1) Mother will resign her position with the Company.
- (2) Company will redeem all the stock held by Mother, which will result in (i) Father, Daughter and Son holding all the Company stock directly; and (ii) Mother holding all the Company stock constructively through Father, Son, and Daughter under section 318(a)(1) of the Internal Revenue Code. In the redemption, Mother will receive a fractional interest in a parcel of real property owned by Company ("Property"). At the same time, Company will redeem a portion of Father's stock, for which Father will receive cash and the balance of Company's interest in Property.

The following representations have been made in connection with the proposed transaction:

(a) There are no outstanding options or warrants to purchase Company stock, nor are there any outstanding debentures or other obligations that are convertible into Company stock or would be considered Company stock.

(b) Company has no plan or intention to issue, redeem, or exchange any shares of its stock, except for the redemption of the stock held by Mother and Father, described above, and except for a possible stock redemption as described in the next sentence. It is possible that Company may redeem from Father additional shares of his stock in Company, not to exceed Value.

(c) No Company stock will be issued to Mother except for issuances occurring more than ten years after the redemption.

(d) Mother will execute and file the agreement required by section 302(c)(2)(A)(iii) of the Code with respect to the acquisition of any interest in Company within ten years from the date of the redemption.

(e) The gifts of Company stock from Father to Mother, as described above, were made for estate planning purposes. The gifts from Mother to Daughter and Son were made to increase their commitment to long-term involvement in Company, to equalize ownership between Daughter and Son, and for estate planning purposes. These gifts were not made in order to provide Mother with a post-redemption economic interest in, or influence over, Company.

(f) Throughout the ten year period following the redemption, Mother will have no interest in Company, including an interest as an officer, director, or employee (other than through constructive ownership under section 318(a)(1) of the Code).

PLR-118169-99

(g) No shareholder of Company has been or will be obligated to purchase any of the stock to be redeemed.

(h) The redemptions and other actions described in steps (1) and (2) above are an isolated event not related to any other past or future transactions.

(i) None of the stock to be redeemed is "section 306 stock" within the meaning of section 306(c) of the Code.

(j) There are no declared but unpaid dividends, or funds set apart for dividends, on any of the stock to be redeemed.

(k) At the time of the redemption, the fair market value of the consideration to be received by Mother and Father, respectively, will be approximately equal to the fair market value of the Company stock to be exchanged therefor. The redemption price was reached through arms-length bargaining between Company and the redeemed shareholders.

(l) The price to be paid for the Company stock to be redeemed will not result in a loss with respect to those shares of stock.

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

(1) The transfers of Company stock from Father to Mother, and by Mother to Daughter and Son, during the ten year period prior to the proposed transaction did not have as one their principal purposes the avoidance of federal income tax within the meaning of section 302(c)(2)(B). These transfers, therefore do not prevent Mother from using the section 302(c)(2)(A) waiver of attribution provision.

(2) Provided that (i) Mother files the agreement described in section 302(c)(2)(A)(iii) in accordance with section 1.302-4(a) of the regulations, and (ii) Mother satisfies the conditions stated in section 302(c)(2)(A)(i) and (ii), section 318(a)(1) will not apply and Company's redemption of all its stock owned by Mother will constitute a "complete termination" of Mother's interest in Company within the meaning of section 302(b)(3). The amount distributed in the redemption will be treated as a distribution in full payment in exchange for the stock redeemed, as provided in section 302(a).

(3) As provided in section 1001, Mother will realize and recognize gain on the redemption of Company stock, with the gain measured by the difference between the fair market value of the Property interest received by Mother and the adjusted basis of the shares of Company stock surrendered as determined

PLR-118169-99

under section 1011. Provided section 341 (relating to collapsible corporations) is not applicable and the stock is a capital asset in Mother's hands, the gain, if any, will constitute capital gain subject to the provisions and limitations of Subchapter P of Chapter 1. As provided by section 267(a), any loss to Mother on the redemption of a share of Company stock will be disallowed because Mother and Company are section 267(b)(2) related persons.

(4) Father, Daughter, and Son, the remaining shareholders of Company, will not be treated as having received a constructive dividend upon the redemption of Company stock held by Mother. (Rev. Rul. 58-614, 1958-2 C.B. 920).

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. 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.

We express no opinion concerning the federal income tax treatment of the transactions 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 transactions that are not specifically covered by the above rulings. In particular, we express no opinion about the tax treatment of any redemptions of Father's Company stock.

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 should be attached to the Federal Income Tax Returns of the taxpayers involved for the taxable year in which the transaction covered by this supplemental letter ruling was consummated.

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,
Assistant Chief Counsel (Corporate)
By: Mark S, Jennings
Acting Chief, Branch 1