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Acquiring =

Acquiring Sub =

Target =

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This is in response to your letter of February 8, 1999, requesting rulings under sections 280G and 4999 of the Internal Revenue Code. Specifically you requested a ruling whether, under the facts outlined below, there will be a change in the ownership or effective control of Acquiring, or in the change in the ownership of a substantial portion of the assets of Acquiring within the meaning of section 280G(b)(2) of the Code. The facts as submitted are set forth below.

Acquiring and Target are both widely-held, publicly traded corporations. Acquiring, Acquiring Sub (a wholly-owned subsidiary of Acquiring), and Target entered into a Merger Agreement dated Date W. Pursuant to the Merger Agreement, Acquiring Sub will merge with and into Target. The separate corporate existence of Acquiring Sub shall cease and Target will become a wholly-owned subsidiary of Acquiring. The Merger Agreement has been approved by the Board of Directors of both Acquiring and Target.

Acquiring has outstanding b shares of common stock and options to acquire c shares of Acquiring stock. Target has outstanding d shares of common stock and options to acquire e shares of Target stock. Pursuant to the Merger Agreement, at the effective date of the Merger, each outstanding share of Target common stock will be converted into f shares of Acquiring common stock. Following the Merger, the pre-Merger Acquiring shareholders will own approximately g percent of Acquiring. The pre-Merger Target shareholders will own approximately h percent of Acquiring, subject to any stock option exercises by Acquiring and Target employees up until the consummation of the Merger. All outstanding options have been treated as stock for purposes of section 280G of the Code.

The Board of Directors will be increased from i to j members. The pre-Merger members of the Board of Directors of Acquiring will comprise k percent of the post-Merger Board of Directors of Acquiring (k being greater than 50 percent). The remaining post-Merger Board of Directors of Acquiring will be pre-Merger members of the Board of Directors of Target who will be endorsed by a majority of the pre-Merger Board of Directors of Acquiring.

Certain employees of Acquiring entered into management agreements prior to the Merger. Such employees may receive payments under the management agreements as a result of the Merger.

Acquiring represents that, to the best of its knowledge, no current shareholder of Target will hold more than five percent of the voting power of Acquiring immediately after the Merger. Acquiring also represents that, to the best of its knowledge, no shareholder of Target has any agreement, written or unwritten, express or implied, to act in concert to control Acquiring following the Merger.

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Section 280G of the Internal Revenue Code provides that no deduction will be allowed for any excess parachute payment. Section 280G(b)(1) of the Code defines the term "excess parachute payment" as an amount equal to the excess of any parachute payment over the portion of the base amount allocated to such payment.

Section 280G(b)(2)(A) of the Code defines the term "parachute payment" as any payment in the nature of compensation to (or for the benefit of) a disqualified individual if (i) such payment is contingent on a change (I) in the ownership or effective control of the corporation, or (II) in the ownership of a substantial portion of the assets of the corporation; and (ii) the aggregate present value of the payments in the nature of compensation to (or for the benefit of) such individual which are contingent on such change equals or exceeds an amount equal to three times the base amount.

Section 4999(a) of the Code imposes on any person who receives an excess parachute payment a tax equal to 20 percent of the amount of the payment.

Section 1.280G-1 of the Proposed Income Tax Regulations, Q&As 27, 28 and 29, published in the Federal Register on May 5, 1989, (54 Fed. Reg. 19,390), provides guidance concerning when a corporation will be considered to have undergone a change in ownership or effective control, or a change in the ownership of a substantial portion of its assets.

Q&A 27(a) provides that a change in the ownership or control of a corporation occurs on the date that any one person, or more than one person acting as a group, acquires ownership of stock of the corporation that, together with stock held by such person or group, possesses more than 50 percent of the total fair market value or total voting power of the stock of such corporation. Q&A 27(b) provides that persons will not be considered to be "acting as a group" merely because they happen to purchase or own stock of the same corporation at the same time, or as a result of the same public offering. However, persons will be considered to be "acting as a group" if they are owners of an entity that enters into a merger, consolidation, purchase or acquisition of stock, or similar business transaction with the corporation. Q&A 27(c) provides that section 318(a) shall apply in determining stock ownership.

Example (3) of Q&A 27 deals with a corporate merger. There, Corporation P merged into Corporation O and the shareholders of P received O stock in exchange for their P stock. The example concludes that because the P shareholders received a greater than 50 percent interest in O, O experienced a change in ownership. By implication, the example concludes that P did not experience such a change.

Q&A 28(a) provides, in part, that a change of effective control of a corporation is presumed to occur on the date that either (1) any one person, or more than one person acting as a group, acquires (or has acquired during the 12-month period ending on the date of the most recent acquisition by such person or persons) ownership of stock of

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the corporation possessing 20 percent or more of the total voting power of the stock of such corporation; or (2) a majority of the members of the corporation's board of directors is replaced during any 12-month period by directors whose appointment or election is not endorsed by a majority of the members of the corporation's board of directors prior to the date of the appointment or election.

The presumption of Q&A 28(a)(1) and (2) may be rebutted by establishing that the acquisition or acquisitions of the corporation's stock, or the replacement of the majority of the members of the corporation's board of directors, does not transfer the power to control (directly or indirectly) the management and policies of the corporation from any one person (or more than one person acting as a group) to another person (or group). Q&A 28(c) contains the same language as Q&A 27(b) concerning when persons will be considered to be "acting as a group." Q&A 28(d) contains the same language as Q&A 27(c) concerning the application of section 318(a).

It has been represented that, immediately following the Merger, the pre-Merger Acquiring shareholders will own more than 50 percent of the total fair market value and total voting power of the outstanding Acquiring stock. The pre-Merger Target shareholders will own more than 20 percent of the total voting power of the outstanding stock of Acquiring.

Viewing the merger from Acquiring's perspective, Acquiring will surrender potential ownership or control when it issues its stock to Target's shareholders in consideration for Target stock. Since Acquiring's shareholders will retain sufficient stock value and voting power due to this transaction, Acquiring will not experience a change of ownership under Q&A 27.

As part of the transaction, all of Target's stock will be transferred to Acquiring in consideration for the issuance of Acquiring stock to Target shareholders, which will result in Target's shareholders receiving a greater than 20 percent voting interest in Acquiring. Accordingly, under Q&A 28, it is presumed that Acquiring experienced a change in effective control.

However, the facts submitted indicate that the Target shareholders will not act in a concerted way to control the management and policies of Acquiring. The facts also indicate that a majority of Acquiring's board of directors is not being replaced. In addition, Acquiring's board of directors following the Merger will be endorsed by a majority of the pre-Merger Acquiring board of directors.

Accordingly, based strictly on the information submitted and Acquiring's representations set forth above, we rule as follows:

- 1) Provided that after the Merger the shareholders of Target do not act in a concerted way to control the management and policies of Acquiring, the

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Merger will not cause a change in the ownership or effective control of Acquiring, nor will it cause a change in the ownership of a substantial portion of Acquiring's assets within the meaning of section 280G of the Code.

2) The provisions of section 280G of the Code will not apply to any payments pursuant to management agreements that are made by Acquiring to employees or former employees of Acquiring that are contingent upon the Merger.

3) The provisions of section 4999 of the Code will not apply to any payments pursuant to management agreements that are made by Acquiring to employees or former employees of Acquiring and that are contingent upon the Merger.

Except as specifically ruled on above, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. Specifically, no opinion was requested and none is expressed regarding the federal income tax consequences of the Merger described above.

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. The Taxpayer should attach a copy of this ruling to any income tax return to which it is relevant.

Temporary or final regulations pertaining to one or more of the issues addressed in this ruling have not been adopted. Therefore, this ruling will be modified or revoked by the adoption of temporary or final regulations to the extent that the regulations are inconsistent with any conclusion in the ruling. However, when the criteria in section 12.05 of Rev. Proc. 99-1, 1999-1 I.R.B. 6, 47 are satisfied, a ruling is not revoked or modified retroactively, except in rare or unusual circumstances.

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In accordance with the Power of Attorney on file with this office, copies of this letter are being sent to Acquiring and to the other authorized representative.

Sincerely yours,

ROBERT B. MISNER
Assistant Chief, Branch 4
Office of the Associate
Chief Counsel
(Employee Benefits and
Exempt Organizations)

Enclosure:

Copy for 6110 purposes