

## Internal Revenue Service

## Department of the Treasury

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**March 24, 2000**

RE:

Distributing =

Controlled =

Shareholder A =

Shareholder B =

Shareholder C =

Shareholder D =

Shareholder E =

Shareholder F =

Shareholder G =

Shareholder H =

Shareholder I =

Shareholder J =

Shareholder K =

Shareholder L =

Shareholder M =

Shareholder N =

Business A =

Business B =

Business C =

Business D =

a =

b =

c =

State A =

Dear :

This letter is in reply to your letter dated September 15, 1999, requesting rulings as to the federal income tax consequences of a proposed transaction. Additional information was submitted in letters dated December 6, 1999, January 31, February 7, March 9, March 14, and March 22, 2000. The information submitted for consideration is summarized below.

Distributing is an accrual basis State A corporation. Distributing is directly engaged in Business A , Business B, and Business C through salaried and hourly wage employees and indirectly engaged in Business D through various subsidiaries. Distributing has a shares of common stock held in treasury and b shares of common stock outstanding as follows: Shareholder A (1.64%); Shareholder B (0.86%); Shareholder C (0.86%); Shareholder D (0.68%); Shareholder E (52.81%); Shareholder F (0.14%); Shareholder G (1.03%); Shareholder H (1.64%);

Shareholder I (11.03%); Shareholder J (1.64%); Shareholder K (1.64%); Shareholder L (1.64%); Shareholder M (1.37%); and Shareholder N (23.01%).

Controlled will be formed as a cash basis corporation to effectuate the proposed transaction. Controlled will have c shares of common stock outstanding, which will initially be owned by Distributing. Controlled will be directly engaged in Business B and Business C.

Financial information has been received which indicates that Distributing's Business A, Business B and Business C operations have had gross receipts and operating expenses representative of the active conduct of a trade or business for each of the past five years.

Serious disputes have arisen between the other shareholders and Shareholder N regarding the management, operations, and direction of Distributing's business. To enable Shareholder N to go separate ways to pursue his desires, the following transaction has been proposed:

- (i) Distributing will transfer a portion of its assets used in Business B consisting of unimproved and improved real estate to Controlled in exchange for Controlled stock. No investment credits will be claimed with respect to the property transferred.
- (ii) Immediately thereafter, Distributing will distribute all of the Controlled stock to Shareholder N in exchange for all of his stock in Distributing.

Following the transaction, Shareholder N will continue to engage in the same Business B operations that Distributing engaged in prior to the distribution, except that Shareholder N, as a salaried employee of Controlled, will manage the Business B operations and will hire at least one other full-time salaried employee. The newly hired salaried employee will assist in equipment maintenance and will maintain the Business B property. Additional salaried employees will be hired as needed by the Business B operations, and those employees will have such duties as are delegated by Shareholder N. No employees will be shared between Distributing and Controlled.

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

- (a) The fair market value of the Controlled stock to be received by Shareholder N will be approximately equal to the fair market value of the Distributing stock surrendered by the shareholder 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) Following the proposed distribution, Distributing and Controlled will each continue, independently and with their own separate employees, the active conduct of its business.
- (d) No intercorporate debt will exist between Distributing and Controlled at the time of or subsequent to the proposed distribution.
- (e) No two parties to the transaction are investment companies as defined in section 368(2)(F)(iii) and (iv) of the Internal Revenue Code.

- (f) The five years of financial information submitted on behalf of Distributing is representative of its present operations, and there have been no substantial operational changes since the date of the last financial statement submitted.
- (g) Distributing neither accumulated its receivables, nor made extraordinary payments of its payables in anticipation of the transaction.
- (h) There is no plan or intention to liquidate either Distributing or Controlled, to merge either corporation with any other corporation, or to sell or otherwise dispose of the assets of either corporation, except in the ordinary course of business.
- (i) There is no plan or intention by the shareholders of Distributing to sell, exchange, transfer by gift, or otherwise dispose of any of their stock in either Distributing or Controlled after the transaction.
- (j) There is no plan or intention by either Distributing or Controlled, directly or through any subsidiary corporation, to purchase any of its outstanding stock after the transaction, other than through purchases meeting the requirements of section 4.05(1)(b) of Rev. Proc. 96-30.
- (k) No property is being transferred between Distributing and Controlled in which an investment tax credit determined under section 46 of the Code has been (or will be) claimed with respect to any of such property.
- (l) No income items, such as accounts receivable, or any items resulting from a sale, exchange or disposition that would have resulted in income to Distributing, or any items of expense, will be transferred to Controlled.
- (m) Controlled will not assume liabilities or receive assets subject to liabilities in the proposed transaction.
- (n) There are no continuing, planned or intended transactions between Distributing and Controlled following the distribution, either directly or indirectly.
- (o) 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.
- (p) No Distributing shareholder or shareholders will hold immediately after the Distribution disqualified stock with the meaning of section 355(d)(3) which constitutes a 50% or greater interest in Distributing or Controlled.

- (q) The distribution is not part of a plan or series of related transactions (within the meaning of section 355(e)) pursuant to which one or more persons will acquire directly or indirectly stock possessing 50% or more of the total combined voting power of all classes of stock of either Distributing or Controlled, or stock possessing 50% or more of the total value of all classes of stock of either Distributing or Controlled.

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

- (1) The transfer by Distributing to Controlled of assets in exchange for Controlled stock, as described above, followed by the distribution of Controlled stock to Shareholder N, in exchange for all of his stock in Distributing, will constitute a reorganization within the meaning of section 368(a)(1)(D). Distributing and Controlled are each a "party to a reorganization" within the meaning of section 368(b).
- (2) No gain or loss will be recognized to Distributing upon the transfer of assets to Controlled in exchange for Controlled stock (section 361(a)).
- (3) No gain or loss will be recognized by Controlled on the receipt of the assets from Distributing in constructive exchange for shares of Controlled stock (section 1032(a)).
- (4) The basis of the assets received by Controlled will be the same as the basis of such assets in the hands of Distributing immediately prior to the transaction (section 362(b)).
- (5) The holding period of each Distributing asset received by Controlled will include the period during which that asset was held by Distributing (section 1223(2)).
- (6) No gain or loss will be recognized by Distributing upon the distribution of all of the Controlled stock to Shareholder N, in exchange for all of his stock in Distributing as described above (section 361(c)(1)).
- (7) No gain or loss will be recognized by (and no amount will be included in the income of) Shareholder N upon receipt of the Controlled stock (section 355(a)(1)).
- (8) The basis of the Controlled stock in the hands of Shareholder N will be the same as the basis of the Distributing stock exchange therefor (section 358(a)(1)).

- (9) The holding period of the Controlled stock received by Shareholder N will include the holding period of the Distributing stock exchanged therefor, provided that the Distributing stock is held as a capital asset on the date of the distribution (section 1223(1)).
- (10) As provided in 312(h), proper allocation of earnings and profits between Distributing and Controlled will be made under section 1.312-10(a) of the Income Tax Regulations.

No opinion is expressed about the tax treatment of the proposed transaction under other provisions of the Code and regulations or about the tax treatment of any conditions existing at the time of, or effects resulting from, the proposed transaction that are not directly covered by the above rulings.

This ruling letter is directed only to the taxpayer who requested 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 ruling letter is consummated.

The rulings contained in this letter are predicated upon the 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 material submitted in support of the request for a ruling. Verification of the factual information, representations, and other data may be required as part of the audit process.

Pursuant to the power of attorney on file in this office, a copy of this letter has been sent to your authorized representative.

Sincerely yours,  
Assistant Chief Counsel (Corporate)  
By: Christopher W. Schoen  
CC:DOM:CORP:1