

## Internal Revenue Service

## Department of the Treasury

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Date:

March 28, 2002

Distributing =

Controlled =

Newco =

Corp Y =

State X =

Profession A =

B =

C =

Date a =

Exchanging  
Shareholders =

This letter responds to your November 5, 2001 letter requesting rulings on certain federal income tax consequences of a proposed transaction. The information submitted in such request and subsequent correspondence is summarized below.

The rulings contained in this letter are based upon the facts and representations submitted by the taxpayer and accompanied by a penalties of perjury statement executed by an appropriate party. This office has not verified any of the materials submitted in support of the request for a ruling. Verification of the information, representations, and other data may be required as part of the audit process.

### **Summary of Facts**

Distributing is a State X professional corporation that conducts Profession A. Distributing's only outstanding stock is voting common. On Date a, Distributing acquired Corp Y in a transaction the taxpayer represented to qualify as a reorganization described in § 368(a)(1)(A) of the Internal Revenue Code (the "Code"). The Corp Y shareholders became Distributing shareholders and continued to primarily specialize in B. Distributing's other shareholders specialize primarily in C.

Distributing shareholders have decided that the benefits from combining Distributing and Corp Y did not develop as expected, and the shareholders who specialize in B on the one hand, and the shareholders who specialize in C on the other hand now desire to be independent and go their separate ways. Accordingly, Distributing proposes the following transaction:

(i) Distributing will transfer the assets and liabilities associated with B to newly formed Controlled in exchange for all of Controlled's stock and the assumption by Controlled of related liabilities (the "Contribution").

(ii) Distributing will distribute the Controlled stock to the Exchanging Shareholders in exchange for all of their Distributing stock (the "Distribution").

(iii) Following the Distribution, Controlled will merge into newly formed Newco, and Controlled will cease to exist. This transaction is intended to qualify under § 368(a)(1)(F) of the Code.

### **Representations**

The taxpayer has made the following representations concerning the proposed transaction:

(a) The fair market value of the Controlled stock received by each Exchanging

Shareholder will approximately equal the fair market value of the Distributing stock surrendered in the exchange.

(b) No part of the consideration distributed by Distributing will be received by an Exchanging Shareholder as a creditor, employee, or in any capacity other than as Distributing shareholder.

(c) The five years of financial information submitted on behalf of Distributing represents its present operations and there have been no substantial operational changes since the date of the last financial statement submitted.

(d) Following the transaction, Distributing and Newco will each continue the active conduct of its business, independently and with its separate employees.

(e) The Distribution will be carried out to resolve management, systemic, and other problems that arise (or are exacerbated) by Distributing's operation of the B and C specialties within a single corporation. The Distribution is motivated, in whole or substantial part, by this corporate business purpose.

(f) Except for the proposed merger of Controlled into Newco after the Distribution, there is no plan or intention by the shareholders of Distributing to sell, exchange, transfer by gift, or otherwise dispose of the stock in either Distributing, Controlled, or Newco after the transaction.

(g) There is no plan or intention by either Distributing, Controlled, or Newco, directly or through any subsidiary corporation, to purchase any of its outstanding stock after the transaction, other than through stock purchases meeting the requirements of § 4.05(1)(b) of Rev. Proc. 96-30, 1996-1 C.B. 696, 705.

(h) Except for the proposed merger of Controlled into Newco after the Distribution, there is no plan or intention to liquidate Distributing, Controlled, or Newco, to merge any one corporation with any other corporation, or to sell or otherwise dispose of the assets of any one corporation after the transaction, except in the ordinary course of business.

(i) The total adjusted basis and the fair market value of the assets to be transferred to Controlled by Distributing in the Contribution will equal or exceed the amount of the liabilities assumed (as determined under § 357(d) of the Code) by Controlled.

(j) The liabilities to be assumed (as determined under § 357(d)) in the Contribution were incurred in the ordinary course of business and are associated with the assets being transferred.

(k) Payments made in connection with any continuing transactions between Distributing and Controlled, or Distributing and Newco, will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.

(l) No property is being transferred between Distributing and Controlled for which an investment tax credit has (or will be) claimed.

(m) No intercorporate debt will exist between Distributing and Controlled, or Distributing and Newco, at the time of, or after, the Distribution.

(n) No two parties to the transaction are investment companies as defined in § 368(a)(2)(F)(iii) and (iv).

(o) Immediately after the transaction, no person will hold "disqualified stock" in Distributing, Controlled, or Newco that constitutes a 50 percent or greater interest in such corporation within the meaning of § 355(d).

(p) Distributing neither accumulated its receivables nor made extraordinary payment of its payables in anticipation of the transaction.

(q) The Distribution is not part of a plan or series of related transactions (within the meaning of § 355(e)) pursuant to which one or more persons will acquire, directly or indirectly, stock possessing 50 percent or more of the total combined voting power of all classes of Distributing, Controlled, or Newco stock entitled to vote, or stock possessing 50 percent or more of the total value of all classes of Distributing, Controlled, or Newco stock.

(r) Distributing is not an S corporation (within the meaning of § 1361(a)) and there is no plan or intention by Distributing, Controlled or Newco to make an S corporation election pursuant to § 1362(a).

### **Rulings**

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

(1) The Contribution, followed by the Distribution, will be a reorganization under § 368(a)(1)(D). Distributing and Controlled each will be a "party to a reorganization" under § 368(b).

(2) No gain or loss will be recognized by Distributing on the Contribution (§§ 361(a) and 357(a)).

(3) No gain or loss will be recognized by Controlled on the Contribution

(§ 1032(a)).

(4) The basis of each asset received by Controlled in the Contribution will equal the basis of that asset in the hands of Distributing immediately before the Contribution (§ 362(b)).

(5) The holding period of each asset received by Controlled will include the period during which Distributing held that asset (§ 1223(2)).

(6) No gain or loss will be recognized by Distributing on the Distribution (§ 361(c)(1)).

(7) No gain or loss will be recognized by (and no amount will otherwise be included in the income of) the Exchanging Shareholders on the Distribution (§ 355(a)(1)).

(8) The basis of Controlled stock in the hands of each Exchanging Shareholder will equal the basis of the Distributing stock surrendered by such shareholder in exchange therefor (§ 358(a)(1)).

(9) The holding period of Controlled stock received by each Exchanging Shareholder will include the holding period of the Distributing stock exchanged therefor, provided the Distributing stock is held as a capital asset on the date of the Distribution (§ 1223(1)).

(10) As provided in § 312(h), proper allocation of earnings and profits between Distributing and Controlled will be made under § 1.312-10(a) of the Income Tax Regulations.

### **Caveats**

No opinion is expressed about the tax treatment of the proposed transaction under other provisions of the Code or regulations, or the tax treatment of any conditions existing at the time of, or effects resulting from, the proposed transaction that are not specifically covered by the above rulings. In particular, we express no opinion on the tax treatment of the proposed merger of Controlled into Newco described in step (iii) above or the tax treatment of the Date a merger of Corp Y with and into Distributing.

### **Procedural Statements**

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

Each taxpayer involved in this transaction should attach a copy of this ruling

letter to the taxpayer's federal income tax return for the taxable year in which the transaction covered by this letter is completed.

Under the power of attorney on file in this office, copies of this letter are being sent to your authorized representatives.

Sincerely,  
Lewis K Brickates  
Acting Chief, Branch 4  
Office of Associate Chief Counsel  
(Corporate