

## Internal Revenue Service

Number: **200928005**

Release Date: 7/10/2009

Index Number: 302.02-00, 1001.00-00,  
1222.01-00

Department of the Treasury

Washington, DC 20224

Third Party Communication: None

Date of Communication: Not Applicable

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CC:CORP:04

PLR-141185-08

Date:

April 06, 2009

### Legend

Corporation =

Shareholder A =

Shareholder B =

Shareholder C =

Shareholder D =

Shareholder E =

Shareholder F =

Shareholder G =

Business A =

Date A =

Date B =

Date C =

Date D =

a =

Dear :

This letter responds to your August 29, 2008 request for rulings regarding certain federal income tax consequences of a completed transaction (described below).

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

### **Summary of Facts**

Corporation is a domestic corporation that was formed on Date A. The authorized and outstanding capital stock of Corporation consists of one class of common stock (the "Common Stock") that entitles shareholders a vote(s) per share. The Common Stock is publicly traded and widely held.

As part of its plan of formation, Corporation entered into certain arrangements that included the receipt of Common Stock, with Shareholder A, Shareholder B, Shareholder C, Shareholder D, Shareholder E, Shareholder F, Shareholder G (individually, the "Remaining Shareholder" and, collectively, the "Remaining Shareholders"), and five other shareholders (the "Previously Redeemed Shareholders" and, together with the "Remaining Shareholders", the "Initial Shareholders"). The Common Stock was issued to the Initial Shareholders on Date B, at which time the Corporation's stock was not yet publicly traded. On Date C, Corporation issued stock of the same class held by the Initial Shareholders to the public.

In connection with the issuance of Common Stock to the Initial Shareholders, each of the Initial Shareholders executed, pursuant to a Loan and Security Agreement (collectively, the "Loan Agreements"), a non recourse note payable to Corporation (singularly, a "Note" and, collectively, the "Notes"). The total amount of each Note was

equal to the total federal, state, and local withholding and payroll taxes attributable to the issuance of the Common Stock that Corporation paid to the Internal Revenue Service and to the state tax authorities on behalf of each of the Initial Shareholders. The Loan Agreements provided that Corporation could foreclose on the Common Stock in full satisfaction of the Notes owed to it by the Initial Shareholders. The Loan Agreements and the Notes were subsequently amended in part, but the amendments did not alter Corporation's right to foreclose on the Common Stock in satisfaction of the Notes owed by the Initial Shareholders.

In connection with the completed transaction, the redemptions of the Common Stock owned by the Previously Redeemed Shareholders were treated as a complete termination of interest under § 302(b)(3) of the Internal Revenue Code.

### **Completed Transaction**

After the close of trading on Date D, Corporation foreclosed on each Note in full exercise of its right under the Loan Agreements and accepted some of the Common Stock of each of the Remaining Shareholders in satisfaction of the Notes (the "Completed Transaction").

### **Representations**

The following representations are made with respect to the Completed Transaction:

- (a) No notes or other obligations of Corporation will be distributed to a redeemed shareholder.
- (b) The redemption from a redeemed shareholder is an isolated transaction and is not related to any other past or future transaction.
- (c) There have been no redemptions, issuances, or exchanges by Corporation of its stock in the past 5 years, except for transactions that occurred in the normal course of business.
- (d) Corporation has no plan or intention to issue, redeem, or exchange additional shares of its stock, except for transactions occurring in the normal course of business.
- (e) The redeemed shareholder is not related, within the meaning of § 318, to any remaining shareholders of Corporation.
- (f) None of the stock to be redeemed from a redeemed shareholder is "§ 306 stock" within the meaning of § 306(c).

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

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

(i) At the time of the exchange, the fair market value of the stock is substantially less than the nonrecourse notes secured by the stock to be redeemed.

(j) Immediately after the redemption, each redeemed shareholder will own less than 50 percent of the total combined voting power of all classes of outstanding stock entitled to vote.

(k) Each redeemed shareholder's percentage of the total outstanding voting stock immediately after the redemption will be less than 80 percent of its percentage ownership of such stock immediately before the redemption.

(l) Each redeemed shareholder's percentage of the total outstanding stock (voting or nonvoting) immediately after the redemption will be less than 80 percent of its percentage ownership of such stock immediately before the redemption.

### **Rulings**

Based solely on the information submitted and the representations made, we rule as follows on the Completed Transaction:

(1) The surrender by each Remaining Shareholder of Common Stock to Corporation in cancellation of the Note owed by such Remaining Shareholder to Corporation will be tested as a redemption under § 302.

(2) The surrender by each Remaining Shareholder of Common Stock to the Corporation in cancellation of the Note owed by each Remaining Shareholder to Corporation will be treated as a substantially disproportionate redemption under § 302(b)(2).

(3) The amounts distributed to each Remaining Shareholder will be treated as a distribution in part or full payment in exchange for the Common Stock surrendered as provided under § 302.

(4) Each Remaining Shareholder will recognize gain or loss on the surrender of the Common Stock in cancellation of the nonrecourse Note owed by each Remaining Shareholder to Corporation equal to the amount realized on the cancellation less each Remaining Shareholder's basis in the surrendered Common Stock. The amount

realized includes the amount of liabilities secured by the surrendered Common Stock. § 1.1001-2(a)(1) and (a)(4)(i).

(5) Each Remaining Shareholder will recognize long term capital gain or loss on the surrender of Common Stock provided the Common Stock was held for more than one year. §§ 1222(3) and 1222(4).

### **Caveats**

We express no opinion about the tax treatment of the Completed Transaction under other provisions of the Code and regulations or the tax treatment of any conditions existing at the time of, or effects resulting from, the Completed Transaction that is not specifically covered by the above rulings. In particular, we express no opinion regarding:

- (i) Whether the Note executed by each Remaining Shareholder will qualify as debt for federal income tax purposes;
- (ii) The federal income tax consequences to Corporation on the redemptions of the Common Stock from each Remaining Shareholder;
- (iii) Whether § 267 applies to the redemptions of the Common Stock from each Remaining Shareholder; and
- (iv) Whether any modification of the Note constitutes a disposition of the Note pursuant to § 1.1001-3.

### **Procedural Statements**

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) provides that it may not be used or cited as precedent. A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of this letter ruling.

In accordance with a power of attorney on file in this office, a copy of this ruling letter is being sent to your authorized representative.

Sincerely,

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Richard K. Passales  
Senior Counsel, Branch 4  
Office of Associate Chief Counsel  
(Corporate)