

Internal Revenue Service

Department of the Treasury

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Date:

August 15, 2002

Distributing =

Controlled =

Trust 1 =

Trust 2 =

Sub 1 =

Shareholder 1 =

Trustee 1 =

Trustee 2 =

business m =

business n =

Date 1 =

Date 2 =

State X =

aa =

bb =

cc =

dd =

ee =

ff =

XXX =

Dear :

We respond to your representative's letter dated April 9, 2002, for rulings concerning the federal income tax consequences of a proposed transaction. Additional information was submitted in a letter dated June 10, 2002. The material information submitted for consideration is summarized below.

Distributing, a State X corporation, is currently engaged directly in business m and business n. The shares of Distributing are all held by Shareholder 1 or for the benefit of his descendants through Trust 1 and Trust 2. Distributing has aa shares of common stock outstanding, which are held in the following manner: bb shares by Trust 1, cc shares by Trust 2, and dd shares by Shareholder 1. Shareholder 1 is not in a position of control as to Trustee 1, trustee of Trust 1, and does not have the power to remove Trustee 2, trustee of Trust 2. Controlled is a newly created State X corporation, and is wholly owned by Distributing.

Distributing and Controlled use an accrual method of accounting for each of their federal income tax returns with a taxable year ending on Date 1. On Date 2,

Distributing sold its ownership interests in Sub 1 to a third party in a transaction unrelated to the proposed transaction discussed herein.

We have received financial information indicating that business m and business n each have had gross receipts and operating expenses representative of the active conduct of a trade or business for each of the past five years.

A difference of opinion has arisen between Shareholder 1, and Trustee 1 and Trustee 2, as trustees to Trust 1 and Trust 2, respectively, regarding the future operations of the businesses of Distributing. Business n tends to produce more stable and consistent annual returns, which better matches the investment goals of the two trusts. Business m tends to be more sporadic and long-term in nature, and possesses opportunities to expand into development activities in which additional capital contributions by the shareholders or debt could be required, which Shareholder 1 favors. Accordingly, to resolve the conflicting goals of the shareholders, the following transaction is proposed:

- (i) Distributing will contribute cash, having an approximate value of \$XXX and ee% of business n to Controlled (the "Contribution").
- (ii) Distributing will distribute bb shares of Controlled stock to Trust 1 in exchange for all of Trust 1's stock in Distributing. Distributing will distribute cc shares of Controlled stock to Trust 2 in exchange for all of Trust 2's stock in Distributing (together the "Distribution").

After the proposed transaction Controlled will be wholly owned by Trust 1 and Trust 2, and Distributing will be wholly owned by Shareholder 1. Distributing will remain engaged directly in business n and business m. Controlled will be directly engaged in business n, independent of Distributing.

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

- (a) The fair market value of the Controlled stock to be received by each shareholder of Distributing will be approximately equal to the fair market value of 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 Distributing.

- (c) The five years of financial information submitted on behalf of business m and business n is representative of each business' respective present operations, and with regard to each business, there has been no substantial operational changes since the date of the last financial statements submitted, except for the sale of Distributing's interest in Sub 1 in a transaction otherwise unrelated to the transaction proposed herein.
- (d) Following the Distribution, Distributing and Controlled each will continue the active conduct of its business, independently and with its separate employees, and Controlled may employ Distributing as a consultant for its business n assets for a period not greater than ff months.
- (e) The distribution of Controlled stock is carried out for the following corporate business purposes: fit and focus. The distribution of Controlled stock is motivated, in whole or substantial part, by this corporate business purpose.
- (f) Distributing is not an S corporation (within the meaning of § 1361(a)), and there is no plan or intention by Distributing or Controlled to make an S corporation election pursuant to § 1362(a).
- (g) 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.
- (h) 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.
- (i) 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 after the transaction, except in the ordinary course of business.
- (j) No intercorporate debt will exist between Distributing and Controlled at the time of, or subsequent to, the Distribution.
- (k) 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.
- (l) Neither Distributing nor Controlled is an investment company as defined in §§ 368(a)(2)(F)(iii) and (iv).

- (m) 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 stock of either Distributing or Controlled, or stock possessing 50 percent or more of the total value of all classes of stock of Distributing or Controlled.

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

- (1) The Contribution followed by the Distribution will constitute a reorganization within the meaning of § 368(a)(1)(D). Distributing and Controlled each will be a “party to a reorganization” within the meaning of § 368(b).
- (2) Distributing will recognize no gain or loss on the Contribution (§§ 361(a), 357(a) and 357(c)).
- (3) Controlled will recognize no gain or loss on the Contribution (§ 1032(a)).
- (4) Controlled’s basis in each asset received in the Contribution will equal the basis of that asset in the hands of Distributing immediately prior to the transfer (§ 362(b)).
- (5) Controlled’s holding period for each asset received from Distributing will include the period during which Distributing held such asset (§ 1223(2)).
- (6) Distributing will recognize no gain or loss on the Distribution (§ 361(c)(1)).
- (7) Trust 1 and Trust 2 will recognize no gain or loss (and no amount will be included in their income) upon receipt of Controlled stock in exchange for their Distributing stock (§ 355(a)(1)).
- (8) The basis of the Controlled stock received by Trust 1 and Trust 2, in the transaction will equal the basis of the Distributing stock surrendered by each of the shareholders, respectively, in exchange therefor (§ 358(a)(1)).
- (9) The holding period of the Controlled stock received by Trust 1 and Trust 2 in the transaction will include the holding period of the Distributing stock surrendered in exchange therefor, provided the respective shareholder held the Distributing stock 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).

Except as specifically set forth above, no opinion is expressed concerning the federal tax consequences of the proposed transaction under any other provision 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.

The rulings contained in this letter are predicated upon the facts and representations submitted by the taxpayers 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. See section 12.04 of Rev. Proc. 2002-1, 2002-1 I.R.B. 1, 50, which discusses in greater detail the revocation or modification of ruling letters. However, when the criteria in section 12.05 of Rev. Proc. 2002-1, 2002-1 I.R.B. at 50-51, are satisfied, a ruling is not revoked or modified retroactively except in rare or unusual circumstances.

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 ruling letter is consummated.

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

Sincerely yours,

Richard E. Coss

Richard E. Coss
Senior Counsel
Office of Associate Chief Counsel
(Corporate)

cc: