

Internal Revenue Service

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Third Party Communication: None
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Person To Contact: , ID No.

Telephone Number:

Refer Reply To:
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Date:
May 15, 2012

LEGEND:

Distributing =

Business A =

Shareholder 1 =

Shareholder 2 =

Shareholder 3 =

Shareholder 4 =

Shareholder 5 =

Shareholder 6 =

Dear :

This letter responds to your letter dated October 15, 2011, requesting rulings under §§ 355 and 368 of the Internal Revenue Code and related provisions with respect to a

proposed transaction described below (the “Proposed Transaction”). The information submitted in that request and subsequent submissions is summarized below.

The rulings contained in this letter are based on facts and representations submitted by the taxpayer and accompanied by penalty of perjury statements executed by an appropriate party. 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 on audit. Moreover, no information provided by the taxpayer has been reviewed and no determination has been made regarding whether the Distributions (defined below): (i) satisfy the business purpose requirement of § 1.355-2(b) of the Income Tax Regulations; (ii) are used principally as devices for the distribution of the earnings and profits of the distributing corporation or of either of the controlled corporations or of more than one of the three corporations (see § 355(a)(1)(B) and § 1.355-2(d)); and (iii) are part of a plan (or series of related transactions) pursuant to which one or more persons will acquire directly or indirectly stock representing a 50-percent or greater interest in the distributing corporation or either of the controlled corporations (see § 355(e) and § 1.355-7).

FACTS

Distributing is a privately-held S corporation. It is directly engaged in Business A. It has only a single class of stock outstanding, which is common stock. It has six shareholders: Shareholder 1, Shareholder 2, Shareholder 3, Shareholder 4, Shareholder 5, and Shareholder 6.

Distributing has submitted financial information indicating that the Business A operations conducted by Distributing have had gross receipts and operating expenses representative of the active conduct of a trade or business for each of the past five years.

Distributing has determined that splitting off part of Business A is necessary because of disagreement among its shareholders as to how its business should be conducted, and, accordingly, the following transaction is proposed.

PROPOSED TRANSACTION

(i) In preparation for steps (ii) and (iii) of the Proposed Transaction, (a) Distributing and a second corporation that is owned by some of the same shareholders that own Distributing will exchange with each other some parcels of real estate of the type used in Business A and (b) Shareholder 3 and Shareholder 4 will purchase some shares in Distributing from the other four shareholders of Distributing.

(ii) Distributing will create two new corporations, Controlled 1 and Controlled 2. Distributing will contribute to each of Controlled 1 (in Contribution 1) and Controlled 2 (in

Contribution 2) a portion of its assets used in conducting Business A in exchange for all of the common stock in each of Controlled 1 and Controlled 2 (each of which will have outstanding only common stock). Distributing will retain other assets used in conducting Business A.

(iii) Distributing will distribute (Distribution 1) all of the stock in Controlled 1 to Shareholder 3 and Shareholder 4 in return for all of their stock in Distributing; and Distributing will distribute (Distribution 2) all of the stock in Controlled 2 to Shareholder 5 and Shareholder 6 in return for all of their stock in Distributing.

Neither Controlled 1 nor Controlled 2 is assuming liabilities or receiving assets subject to liabilities.

No investment credit determined under § 46 has been (or will be) claimed with respect to any of the property Distributing transfers to Controlled 1 and Controlled 2.

Distributing uses and will continue to use the cash method of accounting, and Controlled 1 and Controlled 2 will also use the cash method of accounting. The transaction does not involve and will not result in a situation where one party recognizes income but another party recognizes the deductions associated with such income or one party owns property but another party recognizes the income associated with the property. No actions have been taken or will be taken that are not in the ordinary course of business and that might affect the timing or the amount of any income or deduction to be recognized by a party to the transaction. No income items, such as amount realized, 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 1 or Controlled 2.

There will be no continuing, planned, or intended transactions between Distributing, Controlled 1, and Controlled 2, either directly or indirectly, following Distribution 1 or Distribution 2.

Distributing will have no current earnings and profits as of the date of the Distributions. The earnings and profits of Distributing in the year of distribution prior to the Distributions will be determined and the original shareholders will report their pro rata share of the earnings and profits, up to the date of the Distributions. All earnings and profits will be distributed to the original shareholders prior to execution of steps (ii) and (iii) above. Real estate owned by Distributing will be the only asset on its balance sheet at the time of execution of steps (ii) and (iii) above. No distribution of property by Distributing immediately before the transaction would require recognition of gain resulting in current earnings and profits for the taxable year of the Distributions; and Distributing is not aware of, nor is Distributing planning or intending, any event that will result in Distributing's, Controlled 1's, or Controlled 2's having positive current or accumulated earnings and profits after the Distributions.

Controlled 1 and Controlled 2 will each elect to be S corporations.

Distributing will employ someone, other than Shareholder 3 or Shareholder 5, to perform the operational and managerial activities of Distributing.

REPRESENTATIONS

- a) 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 shareholder of Distributing.
- b) The five years of financial information submitted on behalf of Distributing is representative of the present operations of Business A and, with regard to such business, there have been no substantial operational changes since the date of the last financial statements submitted.
- c) There is no plan or intention to liquidate Distributing, Controlled 1, or Controlled 2, to merge Distributing, Controlled 1, or Controlled 2 with any other corporation, or to sell or otherwise dispose of the assets of Distributing, Controlled 1, or Controlled 2 subsequent to the Distribution, except in the ordinary course of business.
- d) There is no plan or intention by the shareholders or any security holders of Distributing to sell, exchange, transfer by gift, or otherwise dispose of any stock in Distributing, Controlled 1, or Controlled 2 after the Distributions.
- e) There is no plan or intention by Distributing, Controlled 1, or Controlled 2, directly or through any subsidiary corporation, to purchase any of its outstanding stock after the Distribution.
- f) The total adjusted bases and the fair market value of the assets transferred to Controlled 1 and Controlled 2, respectively, by Distributing each equals or exceeds the sum of any liabilities assumed by Controlled 1 and Controlled 2, respectively, plus any liabilities to which the transferred assets are subject.
- g) Any liabilities assumed in the transaction and the liabilities to which the transferred assets are subject were incurred in the ordinary course of business and are associated with the assets being transferred.
- h) The income tax liability for the taxable year in which any investment credit property (including any building to which § 47(d) applies) is transferred will be adjusted pursuant to § 50(a)(1) or (a)(2) (or § 47, as in effect before amendment by Public Law 101-508, Title 11, 104 Stat. 1388, 536 (1990), if applicable) to reflect an early disposition of the property.

- i) Distributing will neither have accumulated its receivables nor made extraordinary payment of its payables in anticipation of the transaction.
- j) No intercorporate debt will exist between Distributing, Controlled 1, or Controlled 2 at the time of, or subsequent to, the distribution of Controlled 1 or Controlled 2 stock.
- k) Payments made in connection with all continuing transactions, if any, between Distributing, Controlled 1, and Controlled 2 will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.
- l) No two parties to the transaction are investment companies as defined in § 368(a)(2)(F)(iii) and § 368(a)(2)(F)(iv) of the Code.

RULINGS REGARDING DISTRIBUTION 1

- (1) Contribution 1 followed by Distribution 1 will be a reorganization within the meaning of § 368(a)(1)(D). Distributing and Controlled 1 will each be a "party to a reorganization" within the meaning of § 368(b).
- (2) Controlled 1 will recognize no gain or loss on Contribution 1 (§ 1032(a)).
- (3) Controlled 1's basis in each asset received in Contribution 1 will be the same as the basis of the asset in the hands of Distributing immediately before Contribution 1 (§ 362(b)).
- (4) Controlled 1's holding period for each asset received in Contribution 1 will include the period during which Distributing held such asset (§ 1223(2)).
- (5) Distributing will recognize no gain or loss on Distribution 1 (§ 361(c)(1)).
- (6) Shareholder 3 and Shareholder 4 will recognize no gain or loss (and no amount will be includible in such shareholders' income) on the receipt of Controlled 1 common stock in Distribution 1 (§ 355(a)(1)).
- (7) The basis of the Controlled 1 common stock received in Distribution 1 by Shareholder 3 and Shareholder 4 will be the same as the basis of the Distributing common stock exchanged therefor (§ 1.358(a)(1)).
- (8) The holding period of the Controlled 1 common stock received by Shareholder 3 and Shareholder 4 will include the holding period of the Distributing common stock surrendered in exchange therefor, provided that the Distributing common stock was held as a capital asset on the date of Distribution 1 (§ 1223(1)).
- (9) Earnings and profits of Distributing (if any) will be allocated between Distributing and Controlled 1 in accordance with § 312(h) and § 1.312-10(a).

RULINGS REGARDING DISTRIBUTION 2

- (1) Contribution 2 followed by Distribution 2 will be a reorganization within the meaning of § 368(a)(1)(D). Distributing and Controlled 2 will each be a “party to a reorganization” within the meaning of § 368(b).
- (2) Controlled 2 will recognize no gain or loss on Contribution 2 (§ 1032(a)).
- (3) Controlled 2’s basis in each asset received in Contribution 2 will be the same as the basis of the asset in the hands of Distributing immediately before Contribution 2 (§ 362(b)).
- (4) Controlled 2’s holding period for each asset received in Contribution 2 will include the period during which Distributing held such asset (§ 1223(2)).
- (5) Distributing will recognize no gain or loss on Distribution 2 (§ 361(c)(1)).
- (6) Shareholder 5 and Shareholder 6 will recognize no gain or loss (and no amount will be includible in such shareholders’ income) on the receipt of Controlled 2 common stock in Distribution 2 (§ 355(a)(1)).
- (7) The basis of the Controlled 2 common stock received in Distribution 2 by Shareholder 5 and Shareholder 6 will be the same as the basis of the Distributing common stock exchanged therefor (§ 1.358(a)(1)).
- (8) The holding period of the Controlled 2 common stock received by Shareholder 5 and Shareholder 6 will include the holding period of the Distributing common stock surrendered in exchange therefor, provided that the Distributing common stock was held as a capital asset on the date of Distribution 2 (§ 1223(1)).
- (9) Earnings and profits of Distributing (if any) will be allocated between Distributing and Controlled 2 in accordance with § 312(h) and § 1.312-10(a).

CAVEATS

No opinion was requested and no opinion is expressed as to qualification of the real estate exchanges in step (i), above, as exchanges under § 1031 or as to 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.

This ruling is directed only to the taxpayer requesting 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 ruling letter.

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

Sincerely,

Isaac W. Zimbalist
Senior Technician Reviewer
(Corporate)

cc: