

Internal Revenue Service

Department of the Treasury

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Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:

CC:CORP:1-PLR-111151-00

Date:

September 28, 2000

Re:

Distributing =

Controlled =

State A =

Date A =

Business A =

Business B =

Business C =

Shareholder 1 =

aaa =

This is a reply to your letter dated May 23, 2000 requesting rulings under § 355 of the Internal Revenue Code (the "Code") and other Code sections, as to the federal income tax consequences of a proposed transaction. The information submitted for consideration is substantially as set forth below.

Distributing is a State A corporation which, prior to Date A engaged in Businesses A, B and C. On Date A, in an unrelated transaction, Distributing contributed the assets and liabilities of Business C to Controlled, a newly formed, wholly owned subsidiary. The Contribution was effected to facilitate the sale of Business B. Since Date A, Controlled has joined Distributing in the filing of consolidated returns.

As of late, the principal shareholders and the officers of Distributing have become disenchanted with the prospects of Business C as an ongoing concern. Some of the shareholders have suggested discontinuing Business C altogether. Shareholder 1,

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however, believes that the prospects of Business C are brighter. Shareholder 1 is presently an officer of Distributing and owns aaa% of the outstanding shares of Distributing. Shareholder 1 was, prior to Date A, the active manager of the Business B and Business C divisions of Distributing. To resolve the shareholder conflicts regarding Business C, Distributing proposes to split off Controlled to Shareholder 1 in a non-pro rata distribution (the "Distribution") in exchange for Shareholder 1's shares of Distributing stock.

Financial information has been received indicating that Businesses A, B and C have each had gross receipts and operating expenses representative of the active conduct of a trade or business for each of the past five years.

The following representations have been made by the taxpayer in connection with the distribution:

- (a) Any indebtedness owed by Controlled to Distributing will not constitute stock or securities.
- (b) The fair market value of Controlled stock and other consideration to be received by Shareholder 1 will be approximately equal to the fair market value of the Distributing stock surrendered by Shareholder 1 in the exchange.
- (c) No part of the consideration distributed by Distributing will be received by a shareholder of Distributing as a creditor, employee or in any capacity other than that of a shareholder in Distributing.
- (d) The five years of financial information submitted on behalf of Distributing is representative of the corporation's present operations and with regard to such corporation, there have been no substantial operational changes since the date of the last financial statement submitted.
- (e) Following the proposed transaction, Distributing and Controlled will each continue the active conduct of its business, independently and with its separate employees.
- (f) The Distribution is being undertaken to resolve the shareholder conflict as to the continuation of Business C. The Distribution is motivated, in whole or in part, by this corporate business purpose.
- (g) There is no plan or intention by the shareholders of Distributing to sell, exchange, transfer by gift, or otherwise dispose of any stock in either Distributing or Controlled after the transaction.

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- (h) There is no plan or intention by Distributing or Controlled, 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 Section 4.05(1)(b) of Revenue Procedure 96-30.
- (i) There is no plan or intention to liquidate either Distributing or Controlled, to merge either Distributing or Controlled with any other corporation, or to sell or otherwise dispose of the assets of either corporation after the transaction, except for transactions in the ordinary course of business.
- (j) The total adjusted bases and the fair market value of the assets transferred to Controlled by Distributing each equal or exceed the sum of the liabilities assumed by Controlled plus any liabilities to which the transferred assets are subject; and the 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.
- (k) Payments made in connection with all continuing transactions 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) Immediately before the Distribution, items of income, gain, loss, deduction and credit will be taken into account as required by the intercompany transaction regulations (see § 1.1502-13 and § 1.1502-14 of the Income Tax Regulations as in effect before the publication of T.D. 8597, 1995-32 I.R.B. 6, and as currently in effect; § 1.1502-13 as published by T.D. 8597). Further, Distributing's excess loss account with respect to Controlled's common stock, if any, will be included in income immediately before the Distribution (see § 1.1502-19).
- (m) Neither Distributing nor Controlled is, or will be, an investment company as defined in §§ 368(a)(2)(F)(iii) and (iv).

Based solely on the information submitted and on the representations set forth above, it is held as follows:

- (a) No gain or loss will be recognized by Distributing upon the distribution of all of the Controlled stock to Shareholder 1. Section 355(c).
- (b) No gain or loss will be recognized by (and no amount will otherwise be included in the income of) Shareholder 1 upon the receipt of Controlled stock. Section 355(a)(1).

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- (c) The basis of the Controlled stock in the hands of Shareholder 1 will be the same as Shareholder 1's basis in his Distributing stock held immediately before the transaction. Section 358(a)(1).
- (d) The holding period of Controlled stock received by Shareholder 1 will include the holding period of the Distributing common stock surrendered by Shareholder 1 in the transaction, provided the Distributing common stock is held as a capital asset on the date of the Distribution. Section 1223(1)(B).
- (e) The earnings and profits of the Distributing and Controlled will be allocated as provided in §§ 312(h)(1), 1.312-10(b) and 1.1502-33(f)(2).
- (f) Immediately before the Distribution, all intercompany obligations existing between Distributing or any of its subsidiaries, and Controlled or any of its subsidiaries (as broadly defined in § 1.1502-13(g)(2)) will be treated as satisfied for cash in an amount equal to its fair market value. See § 1.1502-13(g)(3)(ii)(A). Such intercompany obligation will then be treated as new debt issued for an amount of cash equal to its fair market value immediately after the Distribution. See § 1.1502-13(g)(3)(iii).

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 conditions existing at the time of, or effects resulting from, the proposed transactions that are not specifically covered by the above rulings.

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 transactions covered by this ruling are consummated.

In accordance with the power of attorney on file in this office, a copy of this letter is being sent to the taxpayer and the second named representative.

Sincerely,
Associate Chief Counsel (Corporate)
By: Mark Jennings, Acting Chief
Branch 1