

Internal Revenue Service

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Department of the Treasury
Washington, DC 20224

Person To Contact:

, ID No.

Telephone Number:

In Re:

Refer Reply To:

CC:CORP:B01 – PLR-144766-03

Date:

October 31, 2003

Legend:

Distributing =

Controlled =

Business A =

Location X =

Location Y =

Z =

Shareholder 1 =

Shareholder 2 =

Shareholder 3 =

Dear

This letter responds to your letter dated July 17, 2003, which requests rulings on certain federal income tax consequences of a proposed transaction. Additional information was received in a subsequent letter dated September 4, 2003. The material information submitted for consideration is summarized below.

SUMMARY OF FACTS

Distributing is an accrual method taxpayer that is engaged in Business A in two separate geographic locations (Location X and Location Y). Distributing has outstanding z shares of a single class of voting common stock, which are owned equally by Shareholder 1, Shareholder 2, and Shareholder 3.

Financial information has been received indicating that Distributing has had gross receipts and operating expenses representative of the active conduct of a trade or business for each of the past 5 years.

In recent years, the focus of management in each of the two locations has become separate and distinct. The managers of Location X and Location Y have differing management philosophies and, as a result, shareholder disputes have arisen that are having an adverse effect on the daily operations of Business A. By separating Distributing's business along geographic lines, it is anticipated that the two management groups will be free to operate the business in accordance with their separate management philosophies. Accordingly, it is proposed that Distributing will transfer all of the assets and liabilities associated with Location Y to newly-formed Controlled in exchange for all of the stock of Controlled. Distributing will then distribute all of the Controlled stock to Shareholder 1 in exchange for all of Shareholder 1's Distributing stock.

REPRESENTATIONS

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

- (a) The fair market value of the stock of Controlled to be received by Shareholder 1 in the proposed transaction will be approximately equal to the fair market value of the stock of Distributing surrendered by Shareholder 1 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 the corporation.
- (c) The five years of financial information submitted on behalf of Distributing is representative of the corporation's present operations, and with regard to

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such corporation, there have been no substantial operational changes since the date of the last financial statements submitted.

- (d) Following the transaction, Distributing and Controlled will each continue, independently and with its separate employees, the active conduct of its share of all the integrated activities of the business conducted by Distributing prior to consummation of the transaction, except that the services of one employee will be shared.
- (e) The distribution of the stock of Controlled is carried out for the following corporate business purpose: to eliminate shareholder conflicts. The distribution of the stock of Controlled is motivated, in whole or substantial part, by this corporate business purpose.
- (f) Distributing is not an S corporation (within the meaning of section 1361(a)), and there is no plan or intention by Distributing or Controlled to make an S corporation election pursuant to section 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) The total adjusted bases and the fair market value of the assets transferred to Controlled by Distributing each equals or exceeds the sum of the liabilities assumed (within the meaning of section 357(d)) by Controlled plus any liabilities to which the transferred assets are subject.
- (k) The liabilities assumed (within the meaning of section 357(d)) 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.

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- (l) Distributing neither accumulated its receivables nor made extraordinary payment of its payables in anticipation of the transaction.
- (m) No intercorporate debt will exist between Distributing and Controlled at the time of, or subsequent to, the distribution of Controlled stock.
- (n) 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.
- (o) No two parties to the transaction are investment companies as defined in section 368(a)(2)(F)(iii) and (iv).
- (p) The distribution is not part of a plan or series of related transactions (within the meaning of section 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 Distributing or Controlled, or stock possessing 50 percent or more of the total value of all classes of stock of Distributing or Controlled.

RULINGS

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

- (1) The transfer by Distributing to Controlled of the Location Y assets solely in exchange for Controlled stock and the assumption by Controlled of related liabilities followed by the distribution of the Controlled stock to Shareholder 1, as described above, will be a reorganization within the meaning of section 368(a)(1)(D). Distributing and Controlled will each be a "party to a reorganization" within the meaning of section 368(b).
- (2) No gain or loss will be recognized by Distributing upon the transfer of the Location Y assets to Controlled solely in exchange for Controlled stock and the assumption of liabilities (sections 361(a) and 357(a)).
- (3) No gain or loss will be recognized by Controlled upon the receipt of the assets of Distributing in exchange for Controlled stock (section 1032(a)).
- (4) The basis of the Location Y assets to be received by Controlled will be the same as the basis of those assets in the hands of Distributing immediately prior to the transaction (section 362(b)).

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- (5) The holding period of the Distributing assets to be received by Controlled will include the period during which such assets were held by Distributing (section 1223(2)).
- (6) No gain or loss will be recognized by Distributing upon the distribution of all of its Controlled stock to Shareholder 1 (section 361(c)).
- (7) No gain or loss will be recognized by Shareholder 1 and no amount will be included in the income of Shareholder 1 upon the receipt of Controlled stock in exchange for stock in Distributing (section 355(a)).
- (8) The basis of the Controlled stock to be received by Shareholder 1 will be the same as the basis of his Distributing stock held immediately prior to the distribution (section 358(a)(1)).
- (9) The holding period of the Controlled stock to be received by Shareholder 1 will include the period during which Shareholder 1 held the Distributing stock, provided the Distributing stock is held as a capital asset on the date of the exchange (section 1223(1)).
- (10) As provided in Code Section 312(h), proper allocation of earnings and profits between Distributing and Controlled will be made in accordance with Treas. Reg. § 1.312-10(a).

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

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 must be attached to any income tax return to which it is relevant.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to the taxpayer.

Sincerely,

Michael J. Wilder

Michael J. Wilder
Senior Technician Reviewer, Branch 1
Office of Office of Associate Chief Counsel
(Corporate)