

## Internal Revenue Service

## Department of the Treasury

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Distributing =

Controlled =

Sub 1 =

FSub 1 =

FSub 2 =

FSub 3 =

FSub 4 =

LLC 1 =

LLC 2 =

LLC 3 =

Company A =

Company B =

Country 1 =

Country 2 =

State X =

State Y =

Business A =

Business B =

Business C =

Activity 1A =

Activity 2A =

A =

Estate of A =

B =

C =

D =

E =

F =

G =

H =

I =

J =

K =

Plan A =

Plan B =

Plan C =

Plan D =

Year 1 =

Year 2 =

Year 3 =

Year 4 =

Year 5 =

Year 6 =

Year 7 =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Date 6 =

Date 7 =

Date 8 =

Date 9 =

Date 10 =

Date 11 =

Date 12 =

Date 13	=
Date 14	=
Date 15	=
Investment Banker	=
<u>a</u>	=
<u>b</u>	=
<u>c</u>	=
<u>d</u>	=
<u>e</u>	=
<u>f</u>	=
<u>g</u>	=
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This letter responds to Distributing's June 23, 2000 request for rulings on certain federal income tax consequences of a proposed and partially completed transaction. The information submitted in that letter and in later correspondence is summarized below.

The rulings in this letter are based on facts and representations submitted by the taxpayer 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 ruling request. Verification of the facts, representations, and other data in this ruling letter may be required as part of the audit process.

### **Summary of Facts**

Publicly traded Distributing is the common parent of a corporate group composed of various domestic and foreign corporations. Distributing joins with its includible affiliates in filing a consolidated federal income tax return. Distributing engages in Business A (which consists of Activity 1A and Activity 2A), Business B, and Business C directly and through selected subsidiaries and

other entities. Together, Activity 1A and Activity 2A allow Distributing to provide a to its customers.

Distributing has Class A voting common stock ("Distributing Class A Stock") and Class B voting common stock ("Distributing Class B Stock") outstanding. Holders of Distributing Class A Stock are entitled to elect b percent of Distributing's directors, and holders of Distributing Class B Stock are entitled to elect the rest. Pursuant to Distributing's certificate of incorporation adopted in Year 1 (almost 20 years ago), each share of Distributing Class B Stock is convertible by its holder into one share of Distributing Class A Stock. The decision to convert rests solely in each holder, and under no circumstances can Distributing require a holder to convert. Distributing has amended its certificate from time to time since its adoption, but only to increase the number of authorized shares of Distributing stock.

A was the chief executive officer and chairman of the board of directors of Distributing before his passing on Date 1. Immediately before his passing, A owned more than five percent of the Distributing Class B Stock and an insignificant amount of Distributing Class A Stock and stock of Controlled (a corporation described below). A's Distributing and Controlled stock passed to his estate ("Estate of A") upon his death. B, A's widow, is the executrix of the Estate of A.

Based on public securities filings (the "Filings"), Distributing believes that C and D are the only shareholders, other than the Estate of A, that currently own five percent or more of a class of Distributing stock (such a shareholder referred to as a "Distributing Five Percent Shareholder"). C and D are investment advisors that hold Distributing stock on behalf of their clients. The Filings also indicate that E and F, both of whom are investment advisors, formerly were Distributing Five Percent Shareholders. E was a Distributing Five Percent Shareholder during the two-year period preceding the expected date of the Distribution (defined below), and, depending on when the Distribution is completed, F may have been a Distributing Five Percent Shareholder during that two-year period. Although certain Filings indicate that G was a Distributing Five Percent Shareholder, Distributing believes, based upon recent Filings and other information exchanges, that G, also an investment advisor, never was a Distributing Five Percent Shareholder. Before its recent termination, H, an employee stock ownership plan, was a Distributing Five Percent Shareholder. The Estate of A is the only Distributing Five Percent Shareholder of Distributing Class B Stock.

On Date 2, Distributing adopted a stock award plan under which it has issued, and expects to continue issuing, shares of restricted Distributing Class A Stock to employees of Distributing and its affiliates ("Plan A"). As of Date 3, there were c shares of restricted Distributing Class A Stock outstanding under Plan A. On Date 4, Distributing adopted a stock award plan under which it has issued, and expects to continue issuing, nonqualified options to acquire Distributing Class A Stock as compensation to employees and directors of Distributing and its affiliates ("Plan B"). As of Date 3, there were d vested and e unvested options outstanding under Plan B. On Date 5, Distributing adopted a stock award plan under which it expects to issue additional nonqualified compensatory options to employees and directors of Distributing and its affiliates ("Plan C") (nonqualified compensatory options issued under Plan B or Plan C to employees and directors of Distributing and its affiliates together with any other compensatory options issued to employees or directors of Distributing and its affiliates under future plans that may be adopted by Distributing, the "Distributing Compensatory Options").

Before the Transaction (defined below), Distributing wholly owned Sub 1 and FSub 1. FSub 1 wholly owned FSub 2 and FSub 2 wholly owned FSub 3. Distributing also owned all of LLC 1 and f percent of LLC 2. An unrelated party owned the remaining g percent of LLC 2. LLC 2 wholly owned FSub 4.

All entities described above are domestic, except for FSub 1 (Country 1), FSub 2 (Country 1), FSub 3 (Country1) and FSub 4 (Country 2). LLC 1 has not elected, and will not elect, under § 301.7701-3 of the Procedure and Administrative Regulations to be treated as an entity that is not disregarded as separate from its owner. LLC 2 has not elected, and will not elect, under § 301.7701-3 to be treated as a corporation.

Before the Distribution and in a transaction separate from A's estate plan, the Estate of A may sell, for cash, Distributing Class A Stock and Controlled stock to unrelated parties (the "Estate Transfer"), and Distributing Class A Stock (with a value of h dollars) to an irrevocable life insurance trust established by A (the "Life Insurance Trust," and the sale to the Life Insurance Trust, the "Life Insurance Trust Transfer"). The Life Insurance Trust provides that B is entitled to receive discretionary distributions of income and principal from the trust during her lifetime. In addition, the Life Insurance Trust appoints B to a committee of special fiduciaries that will control matters relating to the voting and disposition of any Distributing stock (and any stock in Controlled distributed on Distributing stock as part of the Distribution) held in the trust. The Life Insurance Trust provides B with the power to appoint by will the Distributing stock and other

property held in the trust to any one or more of A's descendants, their spouses, or charitable organizations. After acquiring shares of Distributing Class A Stock from the Estate of A, but before the Distribution, the Life Insurance Trust may sell all or part of these shares to unrelated parties for cash (the "Life Insurance Trust Transaction").

The Estate of A will hold (i) the Distributing stock formerly held by A that is not part of the Life Insurance Trust Transfer or the Estate Transfer, (ii) the stock in Controlled formerly held by A that is not part of the Estate Transfer, and (iii) the stock in Controlled that is distributed on Distributing stock described in (i) ((i), (ii), and (iii), collectively, the "Remaining Stock"). Under A's estate plan, during the administration of the Estate of A, or at the time of its termination, the Estate of A will transfer the Remaining Stock to a trust established by A (the "A Trust"), which, in turn, will transfer such stock to two marital trusts created under the A Trust (the "Marital Trusts"). The A Trust and Marital Trusts provide that B is entitled to receive distributions of income and discretionary amounts of principal from such trusts during her lifetime. In addition, the A Trust and Marital Trusts provide that B is to serve as a co-trustee of such trusts and as a member of a committee of special fiduciaries that will control matters relating to the voting and disposition of Distributing stock (and any Controlled stock distributed on Distributing stock in the Distribution) held in the A Trust or the Marital Trusts or both. In addition, the Marital Trusts provide B with the power to appoint by will the Remaining Stock and other property held in the Marital Trusts to A's descendants or their spouses. The transfers of Remaining Stock described in this paragraph are collectively referred to as the "Estate Plan Transfers."

Before the Distribution, I, J, and K, each a child of A, each may sell shares of Distributing Class A Stock representing less than one-half of one percent of the voting power and value of Distributing (collectively, the "Inheritance Transfers").

Before the date on which Distributing announced its intention to effectuate the Transaction (the "Announcement Date"), C, E, F, and H engaged in transactions involving the acquisition or disposition of Distributing stock (the "C, E, F, and H Pre-Announcement Date Transactions"). In addition, E disposed of, and may have acquired, Distributing stock in transactions after the Announcement Date, but on or before Date 6 (the "E Transactions"), and D acquired and disposed of Distributing stock in transactions both before and after the Announcement Date, but in each case on or before Date 6 (the "D Transactions"). Date 6 is more than six months before the expected date of the Distribution. G may have acquired or disposed of Distributing stock in

transactions up to and including Date 7 (the "G Transactions"). Date 7 is less than six months before the expected date of the Distribution.

Pursuant to stock repurchase programs, Distributing repurchased a relatively small percentage of the Distributing Class A Stock in Year 2, Year 3, and Year 4 (each, a "Distributing Stock Repurchase," and, collectively, the "Distributing Stock Repurchases"). All of the Distributing Stock Repurchases occurred before both the date Distributing first announced its intention to pursue strategic alternatives for Business A and the Announcement Date.

Distributing acquired substantially all the assets of Company A and Company B in Year 5 (more than six years ago) in exchange for Distributing Class A Stock (collectively, the "Company A and Company B Acquisitions"). Pursuant to earnout arrangements, Distributing issued additional Distributing Class A Stock to the former shareholders of Company A and Company B in Year 2 and Year 6.

As of Date 3, holders of *j* shares of Distributing Class B Stock have converted the shares into Distributing Class A Stock (collectively with any other conversion of Distributing Class B Stock into Distributing Class A Stock by any person other than the Estate of A that may occur before or after the Distribution, the "Distributing Class B Stock Conversions"). Distributing is not aware of any current Distributing Five Percent Shareholder (including now deceased A) that participated in a Distributing Class B Stock Conversion. Furthermore, to the best of Distributing's knowledge, no person became a Distributing Five Percent Shareholder as a result of a Distributing Class B Stock Conversion.

Distributing issued a relatively small number of nonqualified options to acquire Distributing Class A Stock to two unrelated service providers (together, "Service Provider") in Year 4 and Year 7. The options were issued (i) in exchange for engineering services performed for Business A and Business B and (ii) on an arms-length basis. Some of the options issued to Service Provider may be canceled and converted into options to acquire Controlled stock in connection with the Distribution (the nonqualified options to acquire Distributing Class A Stock issued to Service Provider, together with any such options that are canceled and converted into options to acquire Controlled stock, the "Service Provider Options").

Financial information has been received indicating that Business A and Business B each has had gross receipts and operating expenses representing

the active conduct of a trade or business for each of the past five years.

Business A requires substantial capital to meet certain growth objectives. Management of Distributing is hesitant to provide Business A with this capital because that could deprive Business B and Business C of the capital they require. Investment Banker has advised Distributing that Business A could raise the required capital by means of a limited public offering of the stock of a newly formed corporation that would own and operate Business A. Investment Banker has further advised that a stock offering involving an announced intention to separate Business A from Business B and Business C would permit Business A to raise significantly more funds per share (net of transaction costs) than a stock offering not involving such an announcement.

### **Proposed Transaction**

To accomplish the above objectives, Distributing has proposed and partially completed the following transactions (collectively, the "Transaction"):

(i) On Date 8, Distributing formed Controlled as a State X corporation with a single class of voting common stock. Before the Distribution described in step (x) below, Controlled will adopt a shareholder rights plan under which preferred stock purchase rights will be issued with respect to outstanding Controlled stock (the "Controlled Rights").

(ii) On Date 9, for valid business reasons, H was terminated. As part of the termination, H distributed substantially all its assets at the option of each participant (a) directly to the participant, (b) to the participant's individual retirement account or another qualified retirement plan in a direct rollover pursuant to § 401(a)(31), or (c) to a defined contribution plan established by Distributing under § 401(k) in a direct plan-to-plan transfer that complied with the requirements of § 414(l) (H's termination and distribution of assets, the "H Termination"). At no time before the H Termination did H participate in the management of Distributing.

(iii) On Date 10, Controlled adopted a stock award plan to enable the issuance of nonqualified options to acquire Controlled stock as compensation to employees and directors of Controlled and its affiliates ("Plan D") (nonqualified compensatory options issued under Plan D to employees and directors of Controlled and its affiliates, together with any other compensatory options issued to employees or directors of Controlled and its affiliates under future plans that



may be adopted by Controlled, the "Controlled Compensatory Options"). Before the Distribution and subject to shareholder approval, Controlled will amend Plan D to increase the number of Controlled shares that may be issued pursuant to options.

(iv) As of Date 11, Distributing contributed substantially all of its directly owned Business A assets to newly formed LLC 3, a State X limited liability company, in exchange for all of the interests in LLC 3 and the assumption by LLC 3 of liabilities associated with the contributed assets (the "LLC 3 Contribution"). LLC 3 will be a disregarded entity for federal income tax purposes under § 301.7701-3.

(v) As of Date 12, Distributing contributed its interests in LLC 1, LLC 2, and LLC 3, its Sub 1 stock, and certain other Business A assets (collectively with the FSub 3 stock described in step (vii) below, the "Business A Assets") to Controlled in exchange for additional Controlled stock and the assumption by Controlled of liabilities associated with the contributed assets (the contribution described in this step together with the contribution of the FSub 3 stock described in step (vii) below, the "Controlled Contribution").

(vi) On Date 13, Distributing purchased the stock of FSub 3 from FSub 2 for j dollars.

(vii) On Date 13, Distributing contributed its FSub 3 stock to Controlled.

(viii) On Date 14 and Date 15, Controlled sold, in the aggregate, k percent of its voting common stock in an initial public offering (the "Stock Offering"). More specifically, (a) on Date 14, Controlled sold l percent of its stock to certain underwriters in a firm commitment underwriting who resold this stock to the public on the same date and (b) on Date 15, Controlled sold an additional m percent of its stock to certain underwriters pursuant to their exercise of over-allotment options, and the underwriters resold such additional Controlled stock to the public on the same date (Controlled's sale of Controlled stock to, and the purchase of Controlled stock by, the underwriters in (a) and (b), the "Underwriter Transactions"). Controlled has used, and expects to continue using, the proceeds of the Stock Offering to fund operations, capital expenditures, research and development, other business needs, and payments to Distributing for transition services. In addition, Controlled used part of the proceeds to fund the repayment of certain advances, the payment of additional purchase price in connection with a prior acquisition of certain Business A assets by Sub 1, and payments to satisfy a liability owing from FSub 3 to its former owner.

(ix) In connection with the Stock Offering, Controlled issued j Controlled Compensatory Options to certain employees and directors.

(x) Distributing will distribute its Controlled stock pro rata to its shareholders (the "Distribution"). Cash will be issued in lieu of fractional Controlled shares.

(xi) Adjustments will be made to the outstanding vested and unvested Distributing Compensatory Options (the "Vested Distributing Compensatory Options" and the "Unvested Distributing Compensatory Options," respectively) as follows: (a) Vested Distributing Compensatory Options and Unvested Distributing Compensatory Options held by holders who continue to be employed by Distributing or its subsidiaries will be adjusted in a manner that preserves the value of such options immediately before the Distribution, (b) Vested Distributing Compensatory Options held by holders who become employees of Controlled or its subsidiaries will be canceled unless exercised within 90 days after the Distribution and, if so exercised, such options will be adjusted in a manner that preserves the value of such options immediately before the Distribution, and (c) Unvested Distributing Compensatory Options held by holders who become employees of Controlled or its subsidiaries will be terminated, and Controlled will grant unvested options to acquire stock of Controlled to such holders, the terms of which will preserve the value the holder had in the Unvested Distributing Compensatory Options immediately before the Distribution (items (a), (b) and (c), collectively, the "Option Adjustments").

(xii) Adjustments will be made to the outstanding shares of restricted Distributing Class A Stock (the "Unvested Distributing Stock") as follows: (a) Unvested Distributing Stock held by holders who continue to be employed by Distributing or its subsidiaries will not be adjusted; rather shares of restricted Controlled stock (the "Unvested Controlled Stock") will be distributed with respect to such Unvested Distributing Stock in connection with the Distribution and the shares of Unvested Controlled Stock so distributed will be subject to the vesting and other restrictions applicable to the underlying Unvested Distributing Stock and (b) Unvested Distributing Stock held by holders who become employees of Controlled or its subsidiaries will be forfeited and such holders will receive Unvested Controlled Stock, the terms of which will be set so as to preserve the value the holder of the Unvested Controlled Stock had in the Unvested Distributing Stock immediately before the Distribution (items (a) and (b), collectively, the "Restricted Stock Adjustments").

In connection with the Transaction, Distributing and Controlled have

entered into a Master Separation Agreement, a General Assignment and Assumption Agreement, a Master Transitional Services Agreement, an Employee Matters Agreement, an Initial Public Offering and Distribution Agreement, a Registration Rights Agreement, and a Tax Sharing and Indemnification Agreement (collectively, the “Ancillary Agreements”).

## **Representations**

### The LLC 3 Contribution, the Controlled Contribution, and the Distribution

The taxpayer has made the following representations regarding the LLC 3 Contribution, the Controlled Contribution, and the Distribution:

(a) No election has been made or will be made under § 301.7701-3 that would cause LLC 3 to be classified as other than an entity disregarded as separate from its owner for federal tax purposes.

(b) The total adjusted basis and the fair market value of the assets transferred to Controlled by Distributing each equaled or exceeded the sum of the liabilities assumed (within the meaning of § 357(d)) by Controlled.

(c) The liabilities of Distributing assumed (within the meaning of § 357(d)) by Controlled were incurred in the ordinary course of business and were associated with the assets transferred.

(d) None of the Business A Assets transferred by Distributing to Controlled were subject to investment tax credit recapture.

(e) Except to the extent that the receipt of Unvested Controlled Stock by holders of Unvested Distributing Stock with respect to such Unvested Distributing Stock may constitute compensatory income for federal income tax purposes, 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. The sum of the total number of shares of Unvested Controlled Stock to be distributed in respect of Unvested Distributing Stock and the total number of shares of Controlled stock issued in the Stock Offering will constitute less than 20 percent of the Controlled stock outstanding immediately after the Distribution.

(f) The five years of financial information submitted on behalf of Business A and Business B represents, in each case, its present operations, and with regard to each business, there have been no substantial operational changes

since the date of the last submitted financial statements.

(g) Following the Distribution, Distributing and Controlled each will continue the active conduct of its business, independently and with its own employees, except for the sharing of certain employees for a limited time.

(h) The Distribution is being carried out to enable Controlled (Business A) to raise significantly more funds per share (net of transaction costs) in the Stock Offering than if Distributing did not effect the Distribution after the Stock Offering. The Distribution is motivated, in whole or substantial part, by this corporate business purpose and other business reasons.

(i) There is no plan or intention by any Distributing Five Percent Shareholder, and management of Distributing, to its best knowledge, is not aware of any plan or intention on the part of any remaining shareholder or security holder of Distributing, to sell, exchange, transfer by gift, or otherwise dispose of any stock in, or securities of, either Distributing or Controlled after the Transaction, except for the Estate Plan Transfers.

(j) 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, other than through stock purchases meeting the requirements of § 4.05(1) (b) of Rev. Proc. 96-30, 1996-1 C.B. 696, 705.

(k) 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 and except for the currently contemplated sale or other disposition of assets that will not be relied upon to satisfy the active trade or business requirement and which are expected to constitute less than one percent of the total assets of Distributing before the Distribution.

(l) No debt will exist between Distributing and Controlled at the time of, or after, the Distribution, other than debt arising in connection with: (i) indemnification obligations between Distributing and Controlled pursuant to the Master Separation Agreement, Registration Rights Agreement, and Initial Public Offering and Distribution Agreement, (ii) reimbursement obligations of Controlled to Distributing pursuant to the Employee Matters Agreement and General Assignment and Assumption Agreement, (iii) pay-ments between Distributing and Controlled for transitional services pursuant to the Master Transitional Services Agreement, (iv) indemnification obligations, reimburse-ment

obligations, and tax allocation payments between Distributing and Controlled pursuant to the Tax Sharing and Indemnification Agreement, (v) post-Controlled Contribution sales between Distributing and its subsidiaries and Controlled and its subsidiaries, and (vi) trade payables and receivables between Distributing and Controlled pursuant to ordinary course of business transactions.

(m) The indebtedness owed by Controlled to Distributing after the Transaction will not constitute stock or securities.

(n) Immediately before the Distribution, items of income, gain, loss, deduction, and credit will be taken into account as required by the applicable 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, 1995-2 C.B. 147, and as currently in effect; § 1.1502-13 as published by T.D. 8597). Further, any excess loss account Distributing may have in Controlled stock will be included in income immediately before the Distribution to the extent required by applicable regulations (see § 1.1502-19).

(o) 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, except that Distributing and its affiliates may provide certain corporate support and transitional services to Controlled on a fully allocated cost plus basis, which Distributing believes approximates fair market value.

(p) No two parties to the Transaction will be investment companies as defined in § 368(a)(2)(F)(iii) and (iv).

(q) The Distribution will occur within three months of the date of this letter.

(r) Distributing is not an S corporation (under § 1361(a)), and neither Distributing nor Controlled plans to make an S corporation election under § 1362(a) after the Transaction.

(s) The payment of cash in lieu of fractional shares of Controlled stock is solely for the purpose of avoiding the expense and inconvenience to Controlled of issuing fractional shares and does not represent separately bargained-for consideration. The total cash consideration that will be paid in the Transaction to the Distributing shareholders instead of issuing fractional shares will not exceed one percent of the total consideration issued in the Transaction. The fractional share interests of each Distributing shareholder will be aggregated, and no Distributing shareholder will receive cash in an amount equal to or

greater than the value of one full share of Controlled stock.

(t) For purposes of § 355(d), immediately after the Distribution, no person (determined after applying § 355(d)(7)) will hold stock possessing 50 percent or more of the total combined voting power of all classes of Distributing stock entitled to vote, or 50 percent or more of the total value of shares of all classes of Distributing stock, that was acquired by purchase (as defined in § 355(d)(5) and (8)) during the five-year period (determined after applying § 355(d)(6)) ending on the date of the Distribution, provided the Service rules as Distributing requests.

(u) For purposes of § 355(d), immediately after the Distribution, no person (determined after applying § 355(d)(7)) will hold stock possessing 50 percent or more of the total combined voting power of all classes of Controlled stock entitled to vote, or 50 percent or more of the total value of shares of all classes of Controlled stock, that was either (i) acquired by purchase (as defined in § 355(d)(5) and (8)) during the five-year period (determined after applying § 355(d)(6)) ending on the date of the Distribution or (ii) attributable to distributions on Distributing stock that was acquired by purchase (as defined in § 355(d)(5) and (8)) during the five-year period (determined after applying § 355(d)(6)) ending on the date of the Distribution, provided the Service rules as Distributing requests.

(v) 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 either Distributing or Controlled, provided the Service rules as Distributing requests.

(w) The Distributing Compensatory Options and the Controlled Compensatory Options contain, or will contain, customary terms and conditions, have been granted, or will be granted, in connection with the performance of services for Distributing or Controlled or a person related to the grantor under § 355(d)(7)(A), and are not, or will not be, excessive by reference to the services performed. Immediately after the Distribution and within six months thereafter (i) the Distributing Compensatory Options issued pursuant to Plan B will be nontransferable within the meaning of § 1.83-3(d) and (ii) the Distributing Compensatory Options and the Controlled Compensatory Options will not have a readily ascertainable fair market value as defined in § 1.83-7(b).

(x) Distributing's compensation committee will not permit holders of Distributing Compensatory Options issued pursuant to Plan C (or pursuant to any plan that Distributing may prospectively adopt) to transfer their options to persons other than related persons (within the meaning of § 267(b)) until at least six months after the Distribution.

(y) Controlled's compensation committee will not permit holders of Controlled Compensatory Options to transfer their options to persons other than related persons (within the meaning of § 267(b)) until at least six months after the Distribution.

(z) No holder of Distributing Class B Stock discussed the Distribution with Distributing before converting his or her Distributing Class B Stock into Distributing Class A Stock.

(aa) C, D, E, F, G, and H did not, and do not, participate in the management of either Distributing or Controlled, and there was no agreement, understanding, arrangement, or negotiations between Distributing and Controlled and any of C, D, E, F, G, and H concerning the Distribution on or before the dates on which C, D, E, F, G, and H acquired and/or sold any of their Distributing stock.

(bb) No Distributing Stock Repurchase occurred after Year 4. No Distributing Stock Repurchase consummated in Year 4 will have occurred within six months of the date of the Distribution.

(cc) The Controlled Rights cannot be separately traded and are not divisible from the Controlled stock before certain triggering events occur. Before the occurrence of these events, these rights may be redeemed by Controlled. At the time of the Distribution, the likelihood that the Controlled Rights will be exercised will be both remote and uncertain.

#### International

(dd) FSub 3 was a controlled foreign corporation within the meaning of § 957 at the time of FSub 2's sale of FSub 3 to Distributing, immediately before Distributing's transfer of the FSub 3 stock to Controlled, and immediately after Distributing's transfer of the FSub 3 stock to Controlled.

(ee) FSub 2 was a controlled foreign corporation within the meaning of § 957 at the time of FSub 2's sale of FSub 3 stock to Distributing.

(ff) FSub 4 was a controlled foreign corporation within the meaning of § 957 immediately before and immediately after Distributing's transfer of its interests in LLC 2 to Controlled.

(gg) The only foreign corporations being transferred (directly or indirectly) by Distributing to Controlled in the Transaction are FSub 3 and FSub 4.

(hh) Other than n dollars in cash and o dollars of capitalized organizational costs, the sole asset of LLC 2 is the stock of FSub 4.

### **Rulings**

#### The LLC 3 Contribution, the Controlled Contribution, and the Distribution

Based solely on the information submitted and the representations made, we rule as follows regarding the LLC 3 Contribution, the Controlled Contribution, and the Distribution:

(1) For federal tax purposes: (i) LLC 3 will be disregarded as an entity separate from its owner, (ii) Distributing will be treated as the direct owner of the assets of LLC 3 until Distributing's transfer of LLC 3 to Controlled, and (iii) thereafter, Controlled will be treated as the direct owner of the assets of LLC 3 (§§ 301.7701-2(a), -2(c)(2)(i), -3(b) (1)(ii)).

(2) The Controlled Contribution, followed by the Distribution, will be a reorganization under § 368(a)(1)(D). Distributing and Controlled will each be a "party to a reorganization" under § 368(b).

(3) No gain or loss will be recognized by Distributing on the Controlled Contribution (§§ 361(a) and 357(a)).

(4) No gain or loss will be recognized by Controlled on the Controlled Contribution (§ 1032(a)).

(5) The basis of each asset received by Controlled in the Controlled Contribution will equal the basis of that asset in the hands of Distributing immediately before its transfer (§ 362(b)).

(6) The holding period of each asset received by Controlled in the Controlled Contribution will include the period during which Distributing held the asset (§ 1223(2)).



(7) No gain or loss will be recognized by Distributing on the Distribution (§ 361(c)).

(8) No gain or loss will be recognized by (and no amount will otherwise be included in the income of) any shareholder of Distributing on receipt of Controlled stock (including any fractional share interests to which the shareholder may be entitled) in the Distribution (§ 355(a)(1)).

(9) The aggregate basis of the stock of Distributing and Controlled (including any fractional share of Controlled stock) in the hands of each Distributing shareholder immediately after the Distribution will equal the aggregate basis the shareholder has in Distributing stock held immediately before the Distribution. This aggregate basis will be allocated between the Distributing and Controlled stock in proportion to the fair market value of each in accordance with § 1.358-2(a)(2) (§ 358(b)(2) and (c)).

(10) The holding period of the Controlled stock (including any fractional share of Controlled stock) received by each Distributing shareholder in the Distribution will include the holding period of the Distributing stock on which the Distribution is made, provided the Distributing stock is held as a capital asset on the date of the Distribution (§ 1223(1)).

(11) Earnings and profits will be allocated between Distributing and Controlled in accordance with §§ 312(h), 1.312-10, and 1.1502-33(e)(3).

(12) To the extent a Distributing shareholder receives cash in exchange for a fractional share of Controlled stock, gain or loss will be recognized by the shareholder measured by the difference between the cash received and the basis of the fractional share of Controlled stock. If the fractional share qualifies as a capital asset in the hands of the shareholder, the gain or loss will be capital gain or loss, subject to the provisions of subchapter P of chapter 1 of the Internal Revenue Code (§§ 1221 and 1222).

(13) Provided that, at the time of the Distribution, the Controlled Rights remain contingent, non-exercisable, and subject to redemption, the receipt of the Controlled Rights by shareholders of Distributing in the Distribution will not be a distribution or receipt of property, an exchange of stock or property (either taxable or nontaxable), or any other event that gives rise to the realization of income by Distributing, Controlled, or the shareholders of Distributing (Rev. Rul. 90-11, 1990-1 C.B. 10).

(14) Section 304 will not apply to any transfer of stock by Distributing to Controlled in the Controlled Contribution (§§ 361 and 1.1502-80(b)).

(15) None of (i) the issuance or receipt of Distributing Compensatory Options or Controlled Compensatory Options to or by employees and directors, whether before or after the Distribution, (ii) adjustments to these options made in connection with the Distribution, or (iii) the acquisition of stock of Distributing or Controlled pursuant to the exercise of these options, as applicable, will constitute an acquisition that is part of a plan or series of related transactions (within the meaning of § 355(e)) that includes the Distribution.

(16) None of (i) the issuance or receipt of Service Provider Options to or by Service Provider, whether before or after the Distribution, (ii) adjustments to these options made in connection with the Distribution, or (iii) the acquisition of stock of Distributing or Controlled pursuant to the exercise of these options, as applicable, will constitute an acquisition that is part of a plan or series of related transactions (within the meaning of § 355(e)) that includes the Distribution.

(17) No Distributing Stock Repurchase is an acquisition that is part of a plan or series of related transactions (within the meaning of § 355(e)) that includes the Distribution.

(18) No acquisition of Distributing stock by the former shareholders of Company A and Company B in the Company A and Company B Acquisitions will constitute an acquisition that is part of a plan or series of related transactions (within the meaning of § 355(e)) that includes the Distribution.

(19) The Underwriter Transactions will not constitute an acquisition for purposes of § 355(e) (see § 1.351-1(a)(3)(i)).

(20) No Distributing Class B Stock Conversion will constitute an acquisition that is part of a plan or series of related transactions (within the meaning of § 355(e)) that includes the Distribution.

(21) No acquisition of Distributing stock by any person in the C, E, F, and H Pre-Announcement Date Transactions will constitute an acquisition that is part of a plan or series of related transactions (within the meaning of § 355(e)) that includes the Distribution.

(22) No acquisition of Distributing stock by any person in the E Transactions will constitute an acquisition that is part of a plan or series of related transactions (within the meaning of § 355(e)) that includes the

## Distribution.

(23) No acquisition of Distributing stock by any person in the D Transactions will constitute an acquisition that is part of a plan or series of related transactions (within the meaning of § 355(e)) that includes the Distribution.

(24) No acquisition of Distributing stock by any purchaser in the G Transactions will constitute an acquisition that is part of a plan or series of related transactions (within the meaning of § 355(e)) that includes the Distribution, regardless of whether G was a Distributing Five Percent Shareholder.

(25) None of (i) the receipt of the Distributing and Controlled stock held by A at the time of A's death by the Estate of A pursuant to A's estate plan, (ii) any transfer of the Distributing or Controlled stock held by A at the time of A's death or any Controlled stock distributed on such Distributing stock (collectively, the "A Stock") from the Estate of A to any trust pursuant to A's estate plan, (iii) any receipt of A Stock by, or transfer of A Stock from, any trust pursuant to A's estate plan, or (iv) any receipt of A Stock by any beneficiary pursuant to A's estate plan, will constitute an acquisition that is part of a plan or series of related transactions (within the meaning of § 355(e)) that includes the Distribution.

(26) None of (i) the receipt of the Distributing and Controlled stock held by A at the time of A's death by the Estate of A pursuant to A's estate plan, (ii) any transfer of A Stock from the Estate of A to any trust pursuant to A's estate plan, (iii) any receipt of A Stock by, or transfer of A Stock from, any trust pursuant to A's estate plan, or (iv) any receipt of A Stock by any beneficiary pursuant to A's estate plan, will constitute an acquisition of A Stock by purchase for purposes of § 355(d) (§ 355(d)(5)(A)).

## The Stock Offering

Based solely on the information submitted and the representations made, we rule as follows regarding the Stock Offering:

(27) No gain or loss will be recognized on the sale of Controlled stock in the Stock Offering (§ 1032(a)).

## **Caveats**

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

- (i) The transition payments referred to in representations (l) and (o);
- (ii) The tax treatment of the H Termination;
- (iii) The Subchapter K implications of Distributing's transfer of its interests in LLC 2 to Controlled, as described in step (v);
- (iv) The foreign tax implications of the purchase and contribution of the stock of FSub 3 described in steps (vi) and (vii), and the indirect transfer of the stock of FSub 4 to Controlled described in step (v);
- (v) The tax treatment of the Option Adjustments described in step (xi), apart from their effect on the Distribution in rulings (7), (8), (15), and (16);
- (vi) The tax effects of the Life Insurance Trust Transfer, the Life Insurance Trust Transaction, the Estate Transfer, and the Inheritance Transfers apart from their effect on the Distribution in rulings (7) and (8);
- (vii) The tax treatment of any conversion of Distributing Class B Stock to Distributing Class A Stock by the Estate of A;
- (viii) The tax treatment of the issuance, receipt, or vesting of Unvested Distributing Stock and Unvested Controlled Stock, and the Restricted Stock Adjustments described in step (xii); and
- (ix) The tax treatment of payments made or received under the Ancillary Agreements.

### **Procedural Statements**

This ruling letter 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 should be attached to the federal income tax return of each affected taxpayer for the tax year in which the Transaction covered by this letter is completed.

Under a power of attorney on file in this office, a copy of this letter is being sent to each of your authorized representatives.

Sincerely,  
Associate Chief Counsel (Corporate)  
By: Wayne T. Murray  
Senior Technician/Reviewer  
Branch 4