

## Internal Revenue Service

## Department of the Treasury

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Person to Contact:

Telephone Number:

Refer Reply To:  
**CC:DOM:CORP:1-PLR-108378-00**  
Date:  
**June 26, 2000**

Re:

Distributing =

Controlled =

A =

B =

C =

D =

Estate =

Trust =

Business F =

G =

H =

J =

K =

L =

M =

N =

State X =

Dear :

This letter responds to your request dated April 6, 2000 (the "Supplemental Ruling Request"), for a letter ruling supplementing our letter ruling dated January 15, 1998 (PLR-115035-97, the "Prior Letter Ruling"). The Prior Letter Ruling concerned a proposed split-off transaction (the "Split-off Transaction"). The Split-off Transaction has not, as yet, been completed because an illness affecting one of Distributing's shareholders prevented the completion of negotiations with Distributing's lenders for debt restructuring related to the Split-off Transaction. The shareholder has recovered and the parties are prepared to complete the Split-off Transaction. This supplemental letter ruling revokes the Prior Letter Ruling and addresses the federal tax consequences of the currently proposed transaction. Additional information was submitted in letters dated May 9, 2000, and May 12, 2000. The facts submitted are summarized below.

Distributing is an accrual basis State X corporation. Prior to Date M, Distributing directly conducted Business F in location G and location H. After Date M, Distributing was directly engaged in Business F in location G and indirectly engaged in Business F in location H through its subsidiary, Controlled.

Distributing's business was founded by A. A's sons, C and D, operate Distributing. C manages Distributing's Business F in location G and D manages the H location.

Following A's death in 1985, and pursuant to a testamentary trust ("Trust") created by A's will, A's Distributing shares were transferred to Trust for the benefit of A's wife, B, during her lifetime. The trust corpus was to be divided equally among C and D after B's death.

B died in 1997. Subsequently, her shares in Distributing were held by her estate ("Estate"). In accordance with the trust agreement, Trust distributed the Distributing shares it held to C and D, pro rata, on Date K. Estate distributed the Distributing shares it held to C and D, pro rata, on Date L.

Distributing has issued and outstanding N shares of common stock, which are held in equal proportions by C and D. There are no Distributing or Controlled securities outstanding. Distributing and Controlled have not filed a consolidated federal income tax return.

Controlled was formed in State X on Date J to effectuate the proposed transaction. All of the outstanding Controlled stock is currently held by Distributing. Controlled is an accrual basis corporation engaged in Business F in location G.

Financial information has been submitted which indicates that Distributing's location G and location H divisions of Business F 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 taxpayer has provided evidence showing that serious business disputes have arisen between C and D regarding the operation and management of Business F. For example, C and D do not agree on how much additional capital Business F should raise and in what projects the capital should be invested. These disputes adversely affect the operation of the business. In addition, the distribution will allow C and D to concentrate on their separate businesses, enhancing their operations. Accordingly, the following partially completed transaction has been proposed and will be completed within one year of the date of this letter:

- (i) On Date M, Distributing transferred its location G Business F assets, subject to related liabilities, to Controlled in deemed exchange for additional Controlled stock.
- (ii) Distributing will distribute all of the Controlled common stock to C in exchange for all of C's Distributing stock. D will retain his stock in Distributing and will not receive stock in Controlled.

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

- (a) The fair market value of the controlled corporation stock and other consideration to be received by each shareholder of the distributing corporation will be approximately equal to the fair market value of the distributing corporation stock surrendered by the shareholder in the exchange.
- (b) No part of the consideration to be distributed by the distributing corporation 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 the distributing corporation is representative of the corporation's present operation, and with regard to such corporation, there have been no substantial operational changes since the date of the last financial statements submitted.
- (d) Following the transaction, the distributing and controlled corporations 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 the distributing corporation prior to consummation of the transaction.
- (e) The distribution of the stock, or stock and securities, of the controlled corporation is carried out for the following corporate business purposes: To eliminate shareholder disputes and to enhance the location G and H businesses by allowing C and D to concentrate on their independent businesses. The distribution of the stock, or stock and securities, of the controlled corporation is motivated, in whole or substantial part, by one or more of these corporate business purposes.
- (f) There is no plan or intention by the shareholders or security holders of the distributing corporation to sell, exchange, transfer by gift, or otherwise dispose of any of their stock in, or securities of, either the distributing or controlled corporation after the transaction.
- (g) There is no plan or intention by either the distributing corporation or the controlled corporation, 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 Rev. Proc. 96-30.
- (h) There is no plan or intention to liquidate either the distributing or controlled corporation, 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.
- (i) The total adjusted bases and the fair market value of the assets transferred to the controlled corporation by the distributing corporation each equals or exceeds the sum of the liabilities assumed by the controlled corporation plus any liabilities to which the transferred assets are subject.

- (j) 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) The income tax liability for the taxable year in which 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.
- (l) The distributing corporation neither accumulated its receivables nor made extraordinary payment of its payables in anticipation of the transaction.
- (m) No intercorporate debt will exist between the distributing corporation and the controlled corporation at the time of, or subsequent to, the distribution of the controlled corporation stock.
- (n) Payments made in connection with all continuing transactions, if any, between the distributing and controlled corporations 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 § 368(a)(2)(F)(iii) and (iv).
- (p) The distributing corporation is not an S corporation (within the meaning of § 1361(a)), and there is no plan or intention by the distributing or controlled corporation to make an S corporation election pursuant to § 1362(a).
- (q) 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 either Distributing or Controlled corporation, or stock possessing 50 percent or more of the total value of all classes of stock of either Distributing or Controlled.

Based solely on the information submitted and representations set forth above, and with respect to Distributing's transfer of assets to Controlled, provided that an examination of the taxable year that includes Date M has not been started by a district

director before the date of this supplemental letter ruling, we hold as follows:

- (1) The transfer by Distributing to Controlled of the location G Business F assets, solely in deemed exchange for additional stock of Controlled and the assumption of certain liabilities, followed by the distribution of the Controlled stock to C, as described above, will be a reorganization within the meaning of § 368(a)(1)(D) of the Code. Distributing and Controlled will each be "a party to a reorganization" within the meaning of § 368(b).
- (2) No gain or loss will be recognized to Distributing upon the transfer of assets, subject to liabilities, to Controlled in deemed exchange for additional Controlled stock, as described above (§§ 361(a) and 357(a)).
- (3) No gain or loss will be recognized to Controlled on the receipt of Business F assets in deemed exchange for additional Controlled stock (§ 1032(a)).
- (4) The basis of the assets received by Controlled will be the same as the basis of such assets in the hands of Distributing immediately prior to the transfer (§ 362(b)).
- (5) The holding period of each Business F asset received by Controlled from Distributing will include the period during which that asset was held by Distributing (§ 1223(2)).
- (6) No gain or loss will be recognized to C upon the exchange of Distributing stock for stock in Controlled (§ 355(a)(1)).
- (7) No gain or loss will be recognized to Distributing upon the distribution of all of the Controlled stock, as described above (§ 361(c)(1)).
- (8) The basis of the Controlled stock in the hands of C will, in each instance, be the same as the basis of the Distributing stock surrendered in exchange therefor (§ 358(a)(1)).
- (9) The holding period of the Controlled stock received by C will, in each instance, include the holding period of the Distributing stock surrendered in exchange therefor provided that such stock is held as a capital asset on the date of the exchange (§ 1223(1)).
- (10) As provided in § 312(h) of the Code, proper allocation of earnings and profits between Distributing and Controlled will be made in accordance with § 1.312-10(a) of the Regulations.

We express no opinion about the tax treatment of the proposed transactions

under any other provisions of the Code and regulations promulgated thereunder or the tax treatment of any conditions existing at the time of, or effects from, the proposed transactions that are not specifically covered by the above rulings.

This ruling letter has no effect on any earlier documents, except as described above, and is directed only to the taxpayer who requested 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 supplemental letter ruling is consummated.

We have sent copies of this letter to the representatives designated in the power of attorney on file in this office.

Sincerely yours,  
Assistant Chief Counsel (Corporate)

By: \_\_\_\_\_  
Christopher Schoen  
Assistant to the Chief, Branch 1