

Internal Revenue Service

Department of the Treasury

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Date:
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Distributing =

Sub 1 =

Sub 2 =

Sub 3 =

Sub 4 =

Controlled =

Controlled Sub 1 =

Controlled Sub 2 =

Controlled Sub 3 =

Merger Sub =

Business A =

Business B =

Date 1 =

m =

n =

o =

p =

State R =

This letter responds to your November 22, 2000, in which rulings were requested

as to the federal income tax consequences of a proposed transaction. Additional information was submitted in letters dated March 19, March 23, April 24, May 11, May 18, May 21, and May 23, 2001. The information submitted for consideration is summarized below.

Distributing is an accrual basis State R corporation and the common parent of an affiliated group of corporations that files a consolidated federal income tax return. Distributing is indirectly engaged through its direct and indirect subsidiaries in Business A. Distributing wholly owns Sub 1, Sub 2, and Sub 3. Sub 3 wholly owns Sub 4. Sub 1, Sub 2, and Sub 4 are engaged directly in Business A. As of Date 1, Distributing had outstanding m shares of a single class of voting common stock (the "Distributing Common Stock"), which is widely held and publicly traded on a national exchange. Attached to each share of Distributing Common Stock are purchase rights entitling the holder thereof to a right to purchase Distributing stock at less than market value, under certain circumstances, as a means of responding to unsolicited offers to acquire Distributing (the "Distributing Rights").

Controlled is an accrual basis State R corporation. Controlled is indirectly engaged through its direct subsidiaries in Business B. Controlled wholly owns Controlled Sub 1, Controlled Sub 2, and Controlled Sub 3, each of which is directly engaged in Business B. As of Date 1, Controlled had outstanding n shares of a single class of voting common stock ("Controlled Common Stock"). Distributing owns o shares of Controlled Common Stock representing p% (an amount less than 80%) of the vote and value of Controlled (the "Historic Shares"); the remaining Controlled stock is publicly held. Attached to each share of Controlled Common Stock is a purchase right (the "Controlled Rights") similar to the Distributing Rights.

Financial information has been received which indicates that Distributing's Business A and Controlled's 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 and Business B are substantially different businesses and their present relationship creates managerial, systemic, and other problems that can be resolved only through a separation of those two businesses. Thus, the management of Distributing has decided to separate Business A and Business B.

To accomplish this separation, Distributing proposes the following series of transactions:

- (i) The Historic Shares will be converted into a new class of shares of Controlled Common Stock (the "Class B Controlled Common Stock") as follows: (a) Distributing will form a new State R corporation (the "Merger Sub"), (b) Distributing will transfer the Historic Shares to Merger Sub in exchange for all of the Merger Sub stock, and (c) Merger Sub will merge

with and into Controlled in exchange for the issuance of Class B Controlled Common Stock to Distributing on a share-for-share basis (altogether, the "Recapitalization"). The Controlled Common Stock (other than the Historic Shares) will remain issued and outstanding following the Recapitalization. The Class B Controlled Common Stock will have the right to elect at least 80% of Controlled's board of directors and will represent 0% of the fair market value of Controlled.

- (ii) Distributing will distribute the Class B Controlled Common Stock pro rata to the Distributing shareholders (the "Distribution"). In lieu of distributing fractional shares of Class B Controlled Common Stock, the distribution agent will aggregate all such share interests, sell the aggregated shares, and remit the proceeds to the Distributing shareholders entitled to fractional shares.

The taxpayer has made the following representations with respect to the transactions described in subparagraph (i) above:

- (a) The fair market value of the Controlled stock held by each Controlled shareholder immediately following the Recapitalization will approximately equal the fair market value of the Controlled stock held by such shareholder immediately before the Recapitalization.

- (b) Controlled is not under the jurisdiction of a court in a Title 11 or similar case within the meaning of § 368(a)(3)(A).

- (c) The management of Controlled has no plan or intention to, and for a period of five years beginning on the date of the Distribution will not, propose or support any plan or recapitalization or amendment to Controlled's organic documents or other action providing for (i) the conversion of shares of any class of Controlled stock into a different class of Controlled stock; (ii) any change in the absolute or relative voting rights of any class of Controlled stock from the rights existing at the time of the Distribution; (iii) any change in the manner of election or duties and responsibilities of the Controlled board of directors from those existing at the time of the Distribution; or (iv) any action having an effect similar to (i), (ii), or (iii).

- (d) The Recapitalization is a single, isolated transaction and is not part of a plan to periodically increase the proportionate interest of any shareholder in the assets or earnings and profits of Controlled.

The taxpayer has made the following representations with respect to the transactions described in subparagraph (ii) above:

- (f) No part of the consideration to be distributed by Distributing will be received by a Distributing shareholder as a creditor, employee, or in any capacity other

than that of a shareholder of Distributing.

(g) The indebtedness owed by Controlled to Distributing after the Distribution, if any, will not constitute stock or securities.

(h) The five years of financial information submitted on behalf of the active businesses of Distributing and Controlled represents the present operations of each business, and with regard thereto, there have been no substantial changes since the date of the last financial statements submitted.

(i) Immediately after the Distribution, the gross assets of Business A directly conducted by Sub 1, Sub 2, and Sub 4, and the gross assets of Business B directly conducted by Controlled Sub 1, Controlled Sub 2, and Controlled Sub 3 will each have a fair market value of at least 5% of the total fair market value of each corporation's respective gross assets.

(j) Immediately after the Distribution, at least 90% of the fair market value of the gross assets of Distributing, Sub 3, and Controlled will each consist of the stock and securities of controlled corporations that are engaged in the active conduct of a trade or business as defined in § 355(b)(2).

(k) Following the Distribution, Distributing and Controlled, through their wholly owned subsidiaries, will each continue the active conduct of its business, independently and with its separate employees.

(l) The Distribution is being carried out for the corporate business purpose of alleviating certain fit and focus problems that currently threaten the optimal development of Business A and Business B. The Distribution is motivated, in whole or substantial part, by this corporate business purpose.

(m) There is no plan or intention by any shareholder who owns 5% or more of the stock of Distributing, and the management of Distributing, to its best knowledge, is not aware of any plan or intention on the part of any particular 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 Distribution.

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

(o) 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 Distribution, except in the ordinary course of business.

(p) Distributing neither accumulated its receivables nor made extraordinary payment of its payables in anticipation of the Distribution.

(q) No intercorporate debt will exist between Distributing and Controlled at the time of, or subsequent to, the Distribution, except for any indebtedness incurred pursuant to any indemnification payments under a tax sharing agreement.

(r) 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.

(s) Payments made in connection with all continuing transactions between Distributing and Controlled, if any, will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.

(t) The Distributing Rights and the Controlled Rights are each of the type described in Rev. Rul. 90-11, 1990-1 C.B. 10.

(u) Cash distributed in lieu of fractional shares will be provided through a sale by a distribution agent of aggregated fractional shares of Class B Controlled Common Stock. The sale of fractional shares (i) is merely a method of rounding off fractional share interests, (ii) is undertaken solely for the purpose of avoiding the expense and inconvenience of issuing and transferring fractional shares, and (iii) does not represent separately bargained for consideration. The method used for handling fractional share interests is intended to limit the amount of cash received by any one shareholder to less than the value of one full share of Class B Controlled Common Stock.

(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% or more of the total combined voting power of all classes of stock of either Distributing or Controlled entitled to vote, or stock possessing 50% or more of the total value of all classes of stock of either Distributing or Controlled.

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

(1) The Recapitalization will be treated as an exchange by Distributing of its shares of Controlled Common Stock for shares of Class B Controlled Common Stock and will qualify as a reorganization defined in § 368(a)(1)(E). Controlled will be a "party to a reorganization" within the meaning of § 368(b).

(2) No gain or loss will be recognized by Controlled on the issuance of shares of Class B Controlled Common Stock in the Recapitalization (§ 1032(a)).

(3) No gain or loss will be recognized by Distributing upon the exchange of its shares of Controlled Common Stock for shares of Class B Controlled Common Stock (§ 354(a)(1)).

(4) The basis of the shares of Class B Controlled Common Stock received by Distributing will equal the basis of its shares of Controlled Common Stock surrendered in exchange therefor (§ 358(a)(1)).

(5) The holding period of the shares of Class B Controlled Common Stock received by Distributing will include the period during which Distributing held its shares of Controlled Common Stock surrendered in exchange therefor (§ 1223(1)).

(6) No gain or loss will be recognized by Distributing on the distribution of the Class B Controlled Common Stock to the Distributing shareholders (§ 355(c)).

(7) No gain or loss will be recognized by (and no amount will be included in the income of) the Distributing shareholders on their receipt of the Class B Controlled Common Stock (§ 355(a)(1)).

(8) The aggregate basis of the Distributing Common Stock and the Class B Controlled Common Stock held by each Distributing shareholder will equal the aggregate basis of such shareholder's Distributing Common Stock immediately before the Distribution, allocated between the Distributing Common Stock and the Class B Controlled Common Stock in proportion to the fair market values of each in accordance with Treas. Reg. § 1.358-2(a)(2) (§ 358(a)(1) and (b)).

(9) The holding period of the Class B Controlled Common Stock received by each Distributing shareholder will include the holding period of the Distributing Common Stock on which the Distribution is made, provided that such Distributing Common Stock is held as a capital asset on the date of the Distribution (§ 1223(1)).

(10) As provided in § 312(h), proper adjustment of the earnings and profits of Distributing and Controlled will be made in accordance with Treas. Reg. § 1.312-10(b).

(11) If a Distributing shareholder receives cash as the result of an independent distribution agent's sale of a fractional share of Class B Controlled Common Stock, gain or loss will be recognized by the shareholder measured by the difference between the basis of the fractional share interest and the amount of cash received. If the fractional share interest is a capital asset in the hands of the shareholder, the gain or loss will be capital gain or loss subject to the provisions and limitations of Subchapter P of Chapter 1 of the Code (§§ 1221 and 1222).

No opinion is expressed about the tax treatment of the transaction under other provisions of the Code and regulations or about the tax treatment of any conditions existing at the time of, or effects resulting from, the transaction that are not specifically

covered by the above rulings.

This ruling 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 ruling letter is consummated.

The rulings contained in this letter are predicated upon facts and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by the appropriate party. This office has not verified any of the material submitted in support of the request for a ruling. Verification of the factual information, representations, and other data may be required as part of the audit process.

Pursuant to the power of attorney on file in this office, a copy is being sent to the taxpayer.

Sincerely,
Associate Chief Counsel (Corporate)
By: Michael J. Wilder
Senior Technician Reviewer, Branch 1