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Person to Contact:

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Date:
October 4, 1999

Legend:

- Distributing =
- Controlled =
- Father =
- Brother A =
- Family Group A =
- Brother B =
- Family Group B =
- R =
- S =
- T =
- State X =

This is in response to a letter dated June 9, 1999, requesting a ruling as to the federal income tax consequences of a proposed transaction. Additional information was submitted in letters dated August 31, 1999, and October 1, 1999. The information submitted for consideration is substantially as set forth below:

Distributing is a State X corporation engaged in the business of Cattle Ranching. Distributing has outstanding common stock and non-voting preferred stock ("Preferred"). Family Groups A and B each own R percent of Distributing's Common

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Stock and S percent of its Preferred Stock. Father owns T percent of Distributing's Preferred Stock. Father owns no Common Stock. The division of Distributing into two separate ranching businesses is necessary because of the inability of Brother A and Brother B to agree upon fundamental management and operational issues. Father's attempt to retire and turn ownership and management of Distributing over to his two sons has been continuously frustrated by their inability to reconcile their differences. The Brothers have significant differences of opinion over fundamental business matters such as the nature, type and number of cattle which should be run on the ranch and whether the land should be kept in free range or developed into more crop land and hay production base. They also differ dramatically in their basic approach to agriculture with Brother B desiring to make wholesale changes resulting in a much more progressive approach to raising cattle and Brother A preferring to maintain a more traditional approach. The differing approaches of the Brothers are fundamentally at odds with each other and they cannot agree how to reconcile their differences in that regard.

The conflicting viewpoints between the Brothers is having an adverse effect on the day-to-day operations of the ranch. Consequently, the parties have proposed that Distributing transfer approximately one-half of its business assets to Controlled in exchange for all of the Common and Preferred stock of Controlled and the assumption of certain liabilities, followed by the distribution of Common Stock and Preferred Stock in Controlled to Family Group A in exchange for all of their Common Stock and Preferred Stock in Distributing and the distribution of Preferred Stock in Controlled to Father in exchange for an equivalent percentage but not all of his Preferred Stock in Distributing.

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

In connection with the proposed transaction, the following additional representations are made:

- (a) The fair market value of the Controlled stock and other consideration to be received by each shareholder of Distributing will be approximately equal to the fair market value of the Distributing stock surrendered by the shareholder in 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 operation, and with regard to such corporation, there have been no substantial operational changes since the date

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of the last financial statements submitted except for certain real property transactions.

(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 the consummation of the transaction.

(e) Following the transaction, Father will retire from the ranching business and will no longer be employed by either Distributing or Controlled.

(f) The Distribution is being carried out for the purposes set forth above. The Distribution is motivated, in whole or substantial part, by one or more of these corporate business purposes.

(g) Father has established a gifting program which he intends to continue after this reorganization transaction. If a favorable ruling is obtained, Father will gift shares of stock in Distributing to Family Group B and he will gift shares in Controlled to Family Group A. After the transaction, Father will not make gifts of any of his shares of Distributing to Family Group A or any of his shares of Controlled to Family Group B. It is possible that other members of the family will desire to commence stock gifting programs to facilitate their own business and estate planning objectives. Although there is no continuing resolution or exiting plan of redemption, it is possible that shares of Preferred Stock will periodically be redeemed from Father as has been done in the past. Except as otherwise provided in this representation, there is no plan or intention by the shareholders or security holders of Distributing to sell, exchange, transfer by gift, or otherwise dispose of any of their stock in, or securities of, either Distributing or Controlled.

(h) Except for the possible periodic redemption of Preferred Stock from Father, 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 section 4.05(1)(b) of Rev. Proc. 96-30.

(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 Distribution, 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 by Controlled plus any liabilities to which the transferred assets are subject; and the liabilities assumed in the transaction and the liabilities to which

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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 property.

(l) Distributing neither accumulated its receivables nor made extraordinary payments of its payables in anticipation of the Contribution and Distribution.

(m) No income items, including accounts receivable or any item resulting from a sale, exchange or disposition of property, that would have resulted in income to Distributing, and no items of expense will be transferred to Controlled if Distributing has earned the right to receive the income or could claim a deduction for the expense under the accrual or similar method of accounting.

(n) No intercorporate debt will exist between Distributing and Controlled at the time of, or subsequent to, the Distribution.

(o) 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.

(p) No two parties to the transaction are investment companies as defined in § 368(a)(2)(F)(iii) and (iv) of the Internal Revenue Code.

(q) The distribution is not part of a plan or series of related transactions (within the meaning of § 355(d)) 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 entitled to vote, or stock possessing 50 percent or more of the total value of all classes of stock of either Distributing or Controlled.

(r) Less than 50 percent of the total combined voting power of all classes of Distributing stock entitled to vote and less than 50 percent of the total value of shares of all classes of Distributing stock will have been acquired by purchase under § 355(d)(5) or (8) during the five-year period ending on the date of the Distribution (determined after applying § 355(d)(6)).

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

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(1) The transfer by Distributing to Controlled of approximately one-half of its business assets in exchange for all of the stock of Controlled, followed by the distribution of Common Stock and Preferred Stock in Controlled to Family Group A in exchange for all of their Common Stock and Preferred Stock in Distributing and the distribution of Preferred Stock in Controlled to Father in exchange for an equivalent percentage but not all of his Preferred Stock in Distributing will constitute a reorganization under § 368(a)(1)(D) of the Code. Distributing and Controlled will each be "a party to a reorganization" under § 368(b) of the Code.

(2) Distributing will recognize no gain or loss upon the transfer of certain assets to Controlled in exchange for all of Controlled's stock and the assumption of liabilities, as described above (Code §§ 361(a) and 357(a)).

(3) No gain or loss will be recognized by Controlled on receipt of the assets in exchange for all the shares of Controlled (§ 1032(a)).

(4) Controlled's basis in the Distributing assets received will be the same as the basis of such assets in the hands of Distributing immediately before the transfer (§ 362(b)).

(5) Controlled's holding period for the assets received will include the period during which Distributing held the assets (§1223(2)).

(6) Distributing will recognize no gain or loss upon the distribution of all of its Controlled stock to Distributing shareholders, as described above, pursuant to § 311(a).

(7) No gain or loss will be recognized to (and no amount will be included in the income of) each member of the Family Group A shareholders upon receipt of Controlled stock in exchange for all of their Distributing stock, as described above (§ 355(a)(1)).

(8) No gain or loss will be recognized to (and no amount will be included in the income of) Father upon receipt of Preferred Stock in Controlled in exchange for an equivalent percentage of Preferred Stock in Distributing, as described above (§ 355(a)(1)).

(9) The basis of the Controlled stock to be received by each member of Family Group A and Father will be the same as the basis of the Distributing stock that each shareholder surrendered in exchange therefor (§ 358(a)(1)).

(10) The holding period of the Controlled stock to be received by each member of Family Group A and Father, as described above, will include the period of the Distributing stock each shareholder surrendered in the exchange, provided that

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such stock is held as a capital asset by those respective shareholders on the day of the exchange (§ 1223(1)).

(11) As provided in § 312(h), proper allocation of earnings and profits between Distributing and Controlled will be made under § 1.312-10(a).

We express no opinion about the tax treatment of the transaction under any other section of the Code or regulations or the tax treatment of any conditions existing at the time of, or effects resulting from, the transaction that are not specifically covered in 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.

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.

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 your representative.

Sincerely,
Assistant Chief Counsel (Corporate)

By: Lewis K. Brickates

Lewis K. Brickates
Assistant to Chief, Branch 2
(Corporate)