

**Internal Revenue Service**

Department of the Treasury

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Person to Contact:

Telephone Number:

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Date:

October 8, 1999

Parent =

Distributing 1 =

Distributing 2 =

Controlled =

Sub 1 =

Sub 2 =

Sub 3 =

Sub 4 =

Sub 5 =

Sub 6 =

Sub 7 =

Sub 8 =

Sub 9 =

Sub 10 =

Sub 11 =

Sub 12 =

Sub 13 =

Sub 14 =

Sub 15 =

Sub 16 =

Sub 17 =

Sub 18 =

Sub 19 =

Sub 20 =

Sub 21 =

Sub 22 =

Sub 23 =

Sub 24 =

Business A =

Business B =

Business C =

Business D =

Shareholder A =

Shareholder B =

Date 1 =

x =

Dear \_\_\_\_\_ :

This letter responds to your May 12, 1999 request for rulings on certain federal income tax consequences of a proposed transaction. The information submitted in that request and later correspondence is summarized below.

### **Summary of Facts**

Parent is the common parent of an affiliated group that conducts Business A, Business B, Business C, and Business D. Parent is publicly traded, and to the best of Parent's knowledge, Shareholder A and Shareholder B were as of date Date 1 its only shareholders that held five percent or more of its stock by vote or value.

Parent wholly owns Distributing 2, Sub 1, Sub 2, Sub 3, Sub 4, Sub 5, Sub 6, Sub 7, Sub 8, and Sub 9. Parent also owns 99 percent of Sub 10. Sub 7 owns the remaining one percent of Sub 10. Distributing 2 wholly owns Distributing 1. Sub 1 wholly owns Sub 11 and Sub 12. Sub 4 wholly owns Sub 13 and Sub 5 wholly owns Sub 14. Distributing 1 wholly owns Sub 15, Sub 16, Sub 17, Sub 18, and Sub 19. Sub 3 wholly owns Sub 20 and Sub 21. Sub 20 wholly owns Sub 22 and Sub 23. Sub 10 owns 99 percent of Sub 24 and Sub 7 owns the remaining one percent. Parent, Distributing 1, Distributing 2, Sub 1, Sub 2, Sub 4, Sub 5, Sub 6, Sub 7, Sub 8, Sub 11, Sub 14, and Sub 18 are domestic corporations and join in the filing of a consolidated federal income tax return. Sub 3, Sub 9, Sub 10, Sub 12, Sub 13, Sub 15, Sub 16, Sub 17, Sub 19, Sub 20, Sub 21, Sub 22, Sub 23, and Sub 24 are foreign corporations and do not join in the consolidated return.

Distributing 1 conducts Business A and Business B. Sub 1 conducts Business C. Sub 2 and Sub 13 conduct Business D. We have received financial information indicating that Business A, Business B, Business C, and Business D each has had gross receipts and operating expenses representing the active conduct of a trade or business for each of the past five years.

The management of Parent has determined that Business B and Business C cannot achieve their full potential as part of the Parent affiliated group due to systemic problems arising in the operation of Business A, Business B, Business C, and Business D in a single consolidated group. Specifically, Business B and Business C operate in high-growth industries in which products are developed and employed at a rapid rate, while Business A and Business D involve slower-growth industries employing well established technologies subject to more measured and incremental changes. Moreover, because Business A and Business D represent a larger share of the Parent group's overall sales and earnings, management has been heavily influenced by the business model appropriate to those businesses, which emphasizes the need to maintain steady and reliable earnings. As a result, the presence of Business A and

Business D impede both the rapid decision making and the investment in research and development and capital improvements necessary to succeed in Business B and Business C. In addition, the separation of Business B and Business C will enhance the ability of Business B and Business C to attract, retain, and provide appropriate incentives to highly qualified employees for key management and skilled positions.

Because the same business model is appropriate for both Business B and Business C, the management of an affiliated group containing only those businesses could act according to that model with no conflict potential. In addition, substantial synergies would be obtained by combining Business B and Business C in a single affiliated group. For example, it is anticipated that existing customers of Business C would become future customers of Business B as Business B expands its marketing of certain products into the Business C industry. The combination of Business B and Business C would also result in an entity large enough to function as a viable public entity.

### **Proposed Transaction**

To resolve these systemic problems, Parent proposes to separate Business B and Business C from Parent's affiliated group through the following transaction:

- (i) Parent has contributed, or before the distribution of Controlled described below will contribute, to Sub 2 all of its interests in Sub 3, Sub 5, Sub 6, Sub 7, Sub 8, and Sub 10; Sub 1 has transferred Sub 12 to Sub 2; and Sub 4 has transferred Sub 13 to Sub 2 (together, the "Preliminary Transactions"). Sub 1 will receive no stock in Sub 2.
- (ii) Distributing 1 will transfer all of the assets of Business B, subject to certain liabilities, to Controlled in exchange for 100 percent of the stock of Controlled (the "First Contribution").
- (iii) Distributing 1 will distribute all of the Controlled stock to Distributing 2 (the "First Distribution").
- (iv) Distributing 2 will distribute all of the Controlled stock to Parent (the "Second Distribution").
- (v) Sub 1 will declare and pay a dividend to Parent in the form of a negotiable promissory note with a one-year term bearing interest at the applicable federal rate (the "Sub 1 Note").
- (vi) Parent will transfer all of the stock of Sub 1 to Controlled (the "Second Contribution").

(vii) Controlled will issue an amount of common stock in a registered public offering that will be less than 20 percent of its common stock then outstanding, representing less than 20 percent of all equity interests in Controlled by vote and value (the "IPO").

(viii) Controlled will contribute to Sub 1 proceeds from the IPO sufficient to prepay the Sub 1 Note, and Sub 1 will prepay the Sub 1 Note, which will be canceled. Parent will segregate the proceeds of the Sub 1 Note for payment to its creditors or shareholders or both within one year after receipt of the proceeds.

(ix) Parent will distribute all of the stock of Controlled to Parent's shareholders pro rata (the "Third Distribution").

Distributing has, and Controlled will adopt, an award plan under which options and restricted stock are issued to directors, officers, employees, consultants, and advisors. Certain employees of Distributing or its subsidiaries will have performed services benefitting Sub 1 prior to the Third Distribution, and Controlled or Sub 1 may issue those employees options to acquire its stock. Controlled or Sub 1 may also issue options to Distributing directors prior to the Third Distribution. After the Third Distribution, neither Controlled nor Sub 1 will issue options or restricted stock to directors, officers, employees, consultants, or advisors of Distributing or its subsidiaries.

## **Representations**

### The First Contribution and First Distribution

The taxpayer has made the following representations regarding the First Contribution and the First Distribution:

- (a) Any indebtedness owed by Controlled to Distributing 1 after the First Distribution will not constitute stock or securities.
- (b) No part of the consideration distributed by Distributing 1 in the First Distribution will be received by Distributing 2 as a creditor, employee, or in any capacity other than that of a shareholder of Distributing 1.
- (c) The five years of financial information submitted on behalf of Distributing 1 represents the present operations of Distributing 1, and, with regard to Distributing 1, there have been no substantial operational changes since the date of the last financial statements submitted.
- (d) Immediately after the First Distribution, the gross assets of Business A

directly conducted by Distributing 1, and not by any of its subsidiaries, will have a fair market value of at least five percent of the total fair market value of Distributing 1's gross assets, including the stock of its subsidiaries, if any.

(e) Immediately after the First Distribution, the gross assets of Business B directly conducted by Controlled, and not by any of its subsidiaries, will have a fair market value of at least five percent of the total fair market value of Controlled's gross assets, including the stock of its subsidiaries, if any.

(f) Following the First Distribution, except for certain x services (the "Services") that Controlled will purchase from Distributing 1 at an arm's-length rate, Distributing 1 and Controlled each will continue the active conduct of its business independently and with its separate employees.

(g) The First Distribution will be carried out to enable Controlled and Sub 1 to (i) resolve systemic problems resulting from operating in the Parent affiliated group, and (ii) offer competitive equity incentives that will allow them to attract and retain the highest quality talent for key management and skilled positions. The First Distribution is motivated, in whole or substantial part, by these corporate business purposes.

(h) Except for the distribution of Controlled stock by Distributing 2 to Parent in the Second Distribution, there is no plan or intention by Distributing 2 to sell, exchange, transfer by gift, or otherwise dispose of any of its stock in, or securities of, either Distributing 1 or Controlled after the First Distribution.

(i) There is no plan or intention by either Distributing 1 or Controlled, directly or through any subsidiary corporation, to purchase any of its outstanding stock after the First Distribution, other than through stock purchases meeting the requirements of § 4.05(1)(b) of Rev. Proc 96-30, 1996-1 C.B. 696, 705.

(j) There is no plan or intention to liquidate Distributing 1 or Controlled, to merge either corporation with any other corporation, or to sell or otherwise dispose of the assets of either corporation after the First Distribution, except in the ordinary course of business.

(k) The total adjusted bases and the fair market value of the assets transferred by Distributing 1 to Controlled in the First Contribution each equals or exceeds the sum of the liabilities assumed (as determined under § 357(d) of the Internal Revenue Code) by Controlled.

(l) The liabilities assumed (as determined under § 357(d)) by Controlled in the First Contribution were incurred in the ordinary course of business and are associated with the assets being transferred.

(m) No investment credit has been (or will be) claimed for any of the property transferred in the First Contribution.

(n) Each of Distributing 1 and Controlled will utilize the accrual method of accounting.

(o) Other than intercompany payables and receivables between Distributing 1 and Controlled or their subsidiaries incurred for the Sublease (defined in representation (q) below) and for the Services, no intercorporate debt will exist between Distributing 1 (or any of its subsidiaries) and Controlled (or any of its subsidiaries) at the time of, or after, the First Distribution.

(p) Immediately before the First 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, Distributing 1's excess loss account, if any, with respect to the Controlled stock will be included in income immediately before the First Distribution (see § 1.1502-19).

(q) Controlled will sublease certain real property from Distributing 1 at an arm's length rental (the "Sublease"). Payments made in any continuing transactions between Distributing 1 and Controlled or the subsidiaries of either, including the Services and the Sublease, will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.

(r) No two parties to the First Contribution are investment companies under § 368(a)(2)(F)(iii) and (iv).

(s) The First 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 (other than the acquisitions of Controlled by Distributing 2, Parent, and Parent's shareholders in the First Distribution, Second Distribution, and Third Distribution) directly or indirectly stock possessing 50 percent or more of the total combined voting power of all classes of stock of either Distributing 1 or Controlled entitled to vote, or stock possessing 50 percent or more of the total value of all classes of stock of either Distributing 1 or Controlled.

### The Second Distribution

The taxpayer has made the following representations regarding the Second Distribution:

(t) Any indebtedness owed by Controlled to Distributing 2 after the Second

Distribution will not constitute stock or securities.

(u) No part of the consideration distributed by Distributing 2 in the Second Distribution will be received by Parent as a creditor, employee, or in any capacity other than that of a shareholder of Distributing 2.

(v) The five years of financial information submitted on behalf of Distributing 1 represents the present operations of Distributing 1, and, with regard to Distributing 1, there have been no substantial operational changes since the date of the last financial statements submitted.

(w) Immediately after the Second Distribution, at least 90 percent of the fair market value of the gross assets of Distributing 2 will consist of the stock of Distributing 1, which is engaged in the active conduct of a trade or business as defined in § 355(b)(2).

(x) Immediately after the Second Distribution, the gross assets of Business A directly conducted by Distributing 1, and not by any of its subsidiaries, will have a fair market value of at least five percent of the total fair market value of Distributing 1's gross assets, including the stock of its subsidiaries, if any.

(y) Immediately after the Second Distribution, the gross assets of Business B directly conducted by Controlled, and not by any of its subsidiaries, will have a fair market value of at least five percent of the total fair market value of Controlled's gross assets, including the stock of its subsidiaries, if any.

(z) Following the Second Distribution, except for the Services, Distributing 2 (through Distributing 1) and Controlled each will continue the active conduct of its business independently and with its separate employees.

(aa) The Second Distribution will be carried out to enable Controlled and Sub 1 to (i) resolve systemic problems resulting from operating in the Parent affiliated group, and (ii) offer competitive equity incentives that will allow them to attract and retain the highest quality talent for key management and skilled positions. The Second Distribution is motivated, in whole or substantial part, by these corporate business purposes.

(bb) Except for the distribution of Controlled stock by Parent to Parent's shareholders in the Third Distribution, there is no plan or intention by Parent to sell, exchange, transfer by gift, or otherwise dispose of any of its stock in, or securities of, either Distributing 2 or Controlled after the Second Distribution.

(cc) There is no plan or intention by either Distributing 2 or Controlled, directly or through any subsidiary corporation, to purchase any of its outstanding stock after the

Second Distribution, other than through stock purchases meeting the requirements of § 4.05(1)(b) of Rev. Proc 96-30.

(dd) There is no plan or intention to liquidate Distributing 2 or Controlled, to merge either corporation with any other corporation, or to sell or otherwise dispose of the assets of either corporation after the Second Distribution, except in the ordinary course of business.

(ee) Other than intercompany payables and receivables between Distributing 1 and Controlled or their subsidiaries incurred for the Sublease and the Services, no intercorporate debt will exist between Distributing 2 (or any of its subsidiaries) and Controlled (or any of its subsidiaries) at the time of, or after, the Second Distribution.

(ff) Immediately before the Second 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 as in effect before the publication of T.D. 8597 and as currently in effect; § 1.1502-13, as published by T.D. 8597). Further, Distributing 2's excess loss account, if any, with respect to the Controlled stock will be included in income immediately before the Second Distribution (see § 1.1502-19).

(gg) Payments made in any continuing transactions between Distributing 2 and Controlled or the subsidiaries of either, including the Services and the Sublease, will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.

(hh) The Second 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 (other than the acquisitions of Controlled by Parent and Parent's shareholders in the Second Distribution and Third Distribution) directly or indirectly stock possessing 50 percent or more of the total combined voting power of all classes of stock of either Distributing 2 or Controlled entitled to vote, or stock possessing 50 percent or more of the total value of all classes of stock of either Distributing 2 or Controlled.

#### The Second Contribution and Third Distribution

The taxpayer has made the following representations regarding the Second Contribution and the Third Distribution:

(ii) Any indebtedness owed by Controlled to Parent after the Third Distribution will not constitute stock or securities.

(jj) No part of the consideration distributed by Parent in the Third Distribution will

be received by any shareholder of Parent as a creditor, employee, or in any capacity other than that of a shareholder of Parent.

(kk) The five years of financial information submitted on behalf of Parent, Distributing 1, and Sub 2 represents the present operations of each corporation, and, with regard to each corporation, there have been no substantial operational changes since the date of the last financial statements submitted.

(ll) Immediately after Third Transaction, at least 90 percent of the fair market value of the gross assets of Distributing 2 will consist of the stock of Distributing 1, which is engaged in the active conduct of a trade or business as defined in § 355(b)(2).

(mm) Immediately after the Third Distribution, at least 90 percent of the fair market value of the gross assets of Parent will consist of the stock of Distributing 2 and Sub 2, each of which is engaged (directly or indirectly) in the active conduct of a trade or business as defined in § 355(b)(2).

(nn) Immediately after the Third Distribution, the gross assets of Business A directly conducted by Distributing 1, and not by any of its subsidiaries, will have a fair market value of at least five percent of the total fair market value of Distributing 1's gross assets, including the stock of its subsidiaries, if any.

(oo) Immediately after the Third Distribution, the gross assets of Business D directly conducted by Sub 2, and not by any of its subsidiaries, will have a fair market value of at least five percent of the total fair market value of Sub 2's gross assets, including the stock of its subsidiaries, if any.

(pp) Immediately after the Third Distribution, the gross assets of Business B directly conducted by Controlled, and not by any of its subsidiaries, will have a fair market value of at least five percent of the total fair market value of Controlled's gross assets, including the stock of its subsidiaries, if any.

(qq) Following the Second Distribution, except for the Services, Parent (through Distributing 2 and Sub 2) and Controlled each will continue the active conduct of its business independently and with its separate employees.

(rr) The Third Distribution will be carried out to enable Controlled and Sub 1 to (i) resolve systemic problems resulting from operating in the Parent affiliated group, and (ii) offer competitive equity incentives that will allow them to attract and retain the highest quality talent for key management and skilled positions. The Third Distribution is motivated, in whole or substantial part, by these corporate business purposes.

(ss) There is no plan or intention by Shareholder A or Shareholder B, and the management of Parent, to its best knowledge, is not aware of any plan or intention on

the part of any particular remaining shareholder or security holder of Parent to sell, exchange, transfer by gift, or otherwise dispose of any stock in, or securities of, either Parent or Controlled after the Third Distribution.

(tt) There is no plan or intention by either Parent or Controlled, directly or through any subsidiary corporation, to purchase any of its outstanding stock after the Third Distribution, other than through stock purchases meeting the requirements of § 4.05(1)(b) of Rev. Proc 96-30.

(uu) There is no plan or intention to liquidate Parent or Controlled, to merge either corporation with any other corporation, or to sell or otherwise dispose of the assets of either corporation after the Third Distribution, except in the ordinary course of business.

(vv) Controlled will assume (as determined under section 357(d)) no liabilities in the Second Contribution.

(ww) No investment credit has been (or will be) claimed for any of the property transferred in the Second Contribution.

(xx) Each of Parent and Controlled will utilize the accrual method of accounting.

(yy) Other than intercompany payables and receivables between Distributing 1 and Controlled or their subsidiaries incurred for the Sublease, the Services, and the Product Sales (defined in representation (aaa) below), no intercorporate debt will exist between Parent (or any of its subsidiaries) and Controlled (or any of its subsidiaries) at the time of, or after, the Third Distribution.

(zz) Immediately before the Third 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 as in effect before the publication of T.D. 8597 and as currently in effect; § 1.1502-13, as published by T.D. 8597). Further, Parent's excess loss account, if any, with respect to the Controlled stock will be included in income immediately before the Third Distribution (see § 1.1502-19).

(aaa) Sub 1 will purchase certain products from a subsidiary of Sub 8, and Controlled and Sub 1 may purchase certain products from Sub 14, for an arm's length price (the "Product Sales"). Payments made in any continuing transactions between Parent and Controlled or the subsidiaries of either, including the Services, the Sublease, and Product Sales, will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.

(bbb) No two parties to the Third Distribution are investment companies under

§§ 368(a)(2)(F)(iii) and (iv).

(ccc) The Third 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 (other than the acquisition of Controlled by Parent's shareholders in the Third Distribution) directly or indirectly stock possessing 50 percent or more of the total combined voting power of all classes of stock of either Parent or Controlled entitled to vote, or stock possessing 50 percent or more of the total value of all classes of stock of either Parent or Controlled.

(ddd) Parent will complete the Third Distribution within approximately 12 months after the receipt of a ruling letter from the Internal Revenue Service.

(eee) The payment of cash in lieu of fractional shares of Controlled stock is solely for the purpose of avoiding the expense and inconvenience to Parent 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 Parent shareholders instead of issuing fractional shares of Controlled stock will not exceed one percent of the total consideration that will be distributed in the transaction to the Parent shareholders. The fractional share interests of each record Parent shareholder will be aggregated, and no Parent shareholder will receive cash in an amount equal to or greater than the value of one full share of Controlled stock.

#### International Representations

(fff) Neither Parent nor Controlled was a United States real property holding corporation (as defined in § 897(c)(2)) ("USRPHC") at any time during the five-year period ending on the date of the Third Distribution, and neither Parent nor Controlled will be a USRPHC immediately after the Third Distribution.

(ggg) Neither Controlled nor any of its subsidiaries to be distributed in the Third Distribution to the shareholders of Parent are dual resident corporations, with dual consolidated losses, within the meaning of § 1.1503-2(c)(2) and (5).

(hhh) None of the assets associated with Business B that will be transferred to Controlled by Distributing 1 are located outside of the United States.

### **Rulings**

#### The First Contribution and First Distribution

Based solely on the information submitted and representations made, we rule as follows on the First Contribution and the First Distribution:

(1) The First Contribution followed by the First Distribution will be a reorganization under § 368(a)(1)(D) (see § 368(a)(2)(H)(ii); Rev. Rul. 98-44, 1998-37 I.R.B. 4). Distributing 1 and Controlled each will be “a party to a reorganization” under § 368(b).

(2) No gain or loss will be recognized by Distributing 1 on the First Contribution (§§ 361(a) and 357(a)).

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

(4) The basis of each asset received by Controlled in the First Contribution will equal the basis of that asset in the hands of Distributing 1 immediately before the First Contribution (§ 362(b)).

(5) The holding period of each asset received by Controlled in the First Contribution will include the period during which Distributing 1 held that asset before the First Contribution (§ 1223(2)).

(6) No gain or loss will be recognized by Distributing 1 on the First Distribution (§§ 361(c)(1); 355(e)(3)(A) and (4)(C)(ii)).

(7) No gain or loss will be recognized by (and no amount will otherwise be included in the income of) Distributing 2 on receipt of the Controlled stock in the First Distribution (§ 355(a)(1); see Rev. Rul. 62-138, 1962-2 C.B. 95; Rev. Rul. 98-27, 1998-22 I.R.B. 4; Rev. Rul. 98-44).

(8) The holding period of the Controlled stock received by Distributing 2 in the First Distribution will include the holding period during which Distributing 2 held the Distributing 1 stock on which the First Distribution will be made, provided the Distributing 1 stock is held as a capital asset on the date of the First Distribution (§ 1223(1)).

(9) The earnings and profits of Distributing 1 and Controlled will be allocated as provided in §§ 312(h), 1.312-10(a), and 1.1502-33(f)(2).

#### The Second Distribution

Based solely on the information submitted and representations made, we rule as follows on the Second Distribution:

(10) No gain or loss will be recognized by Distributing 2 on the Second Distribution (§§ 355(c)(1); 355(e)(3)(A) and (4)(C)(ii)).

(11) No gain or loss will be recognized by (and no amount will otherwise be included in the income of) Parent on the Second Distribution (§ 355(a)(1); see Rev. Rul. 62-138; Rev. Rul. 98-27).

(12) The holding period of the Controlled stock received by Parent in the Second Distribution will include the period during which Parent held the Distributing 2 stock on which the Second Distribution will be made, provided the Distributing 2 stock is held as a capital asset on the date of the Second Distribution (§ 1223(1)).

(13) The earnings and profits of Distributing 2 and Controlled will be allocated as provided in §§ 312(h), 1.312-10(b), and 1.1502-33(f)(2).

#### The Second Contribution and Third Distribution

Based solely on the information submitted and representations made, we rule as follows on the Second Contribution and the Third Distribution:

(14) The Second Contribution followed by the Third Distribution will be a reorganization under § 368(a)(1)(D). Parent and Controlled each will be “a party to a reorganization” under § 368(b).

(15) No gain or loss will be recognized by Parent on the Second Contribution and receipt of the proceeds of the Sub 1 Note, followed by the transfer of the proceeds of the Sub 1 Note to Distributing's creditors or shareholders or both (§§ 361(a), 361(b)(1)(A), and 361(b)(3)).

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

(17) The basis of the Sub 1 stock received by Controlled in the Second Contribution will equal the basis of the Sub 1 stock in the hands of Parent immediately before the Second Contribution (§ 362(b)).

(18) The holding period of the Sub 1 stock received by Controlled in the Second Contribution will include the period during which Parent held the Sub 1 stock before the Second Contribution (§ 1223(2)).

(19) No gain or loss will be recognized by Parent on the Second Distribution (§ 361(c)(1)).

(20) No gain or loss will be recognized by (and no amount will otherwise be included in the income of) Parent's shareholders on receipt of Controlled stock in the Second Distribution (§ 355(a)(1); see Rev. Rul. 62-138).

(21) The aggregate basis of the Parent stock and the Controlled stock (including any fractional shares deemed distributed under ruling (24) below) in the hands of a Parent shareholder immediately after the Third Distribution will equal the aggregate basis of the Parent stock held by that shareholder immediately before the Third Distribution, allocated between the Parent stock and the Controlled stock in proportion to the fair market value of each on the date of the Third Distribution in accordance with § 1.358-2(a)(2) (§ 358(a)(1), (b), and (c)).

(22) The holding period of the Controlled stock (including any fractional shares deemed distributed under ruling (24) below) received by each Parent shareholder will include the period during which that shareholder held the Parent stock on which the Second Distribution will be made, provided the Parent stock is held as a capital asset on the date of the Second Distribution (§ 1223(1)).

(23) The earnings and profits of Parent and Controlled will be allocated as provided in §§ 312(h), 1.312-10(a), and 1.1502-33(e)(3).

(24) Any payment of cash in lieu of a fractional share interest in Controlled will be treated for U.S. federal income tax purposes as if the fractional share interest had been issued in the Third Distribution and then had been redeemed by Controlled. The cash payment will be treated as having been received in exchange for the constructively redeemed fractional shares under § 302(a) (Rev. Rul. 66-365, 1966-2 C.B. 116; Rev. Proc. 77-41, 1977-2 C.B. 574).

#### International Ruling

(25) The earnings and profits of Sub 3, Sub 10, Sub 12, Sub 13, Sub 20, Sub 21, Sub 22, Sub 23, and Sub 24, to the extent attributable to such stock under § 1.1248-2 or 1.1248-3 (whichever is applicable) which were accumulated in taxable years of such foreign corporations beginning after December 31, 1962, during the period Parent, Sub 1, Sub 4, and Sub 7 held stock directly, indirectly, or constructively in Sub 3, Sub 10, Sub 12, Sub 13, Sub 20, Sub 21, Sub 22, Sub 23, and Sub 24 (or were considered as holding it by reason of the application of § 1223) while Sub 3, Sub 10, Sub 12, Sub 13, Sub 20, Sub 21, Sub 22, Sub 23, and Sub 24 were controlled foreign corporations, shall be attributable to such stock held by Sub 2 (§ 1.1248-1(a)(1)).

#### **Caveats**

We express no opinion about the tax treatment of the transaction under any other provision of the Code or regulations or the tax treatment of any conditions existing at the time of, or effects resulting from, the transaction not specifically covered by the above rulings. In particular, we express no opinion on the tax consequences of the

Preliminary Transactions (except for ruling (25) above), the IPO, the Sublease, the Services, the Product Sales, any restricted stock, or the exercise of any options (including the exercise of any Controlled or Sub 1 options issued to employees or directors of Distributing or its subsidiaries).

The rulings in this letter are based on the facts and representations submitted under penalties of perjury in support of the request. This office has not verified any of the material submitted in support of the request for a ruling. Verification of that information may be required as part of the audit process.

Temporary or final regulations pertaining to one or more of the issues addressed in this ruling letter (including regulations under § 358(g)) have not yet been adopted. Therefore, this ruling letter may be revoked or modified, in whole or in part, on the issuance of temporary or final regulations (or a notice with respect to their future issuance). See § 12.04 of Rev. Proc. 99-1, 1999-1 I.R.B. 6, 47, which discusses the revocation or modification of ruling letters. However, when the criteria in § 12.05 of Rev. Proc. 99-1 are satisfied, a ruling will not be revoked or modified retroactively except in rare or unusual circumstances.

### **Procedural Matters**

This ruling has no effect on any earlier document and 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 ruling letter should be attached to the federal income tax return of each affected taxpayer for the taxable year in which the transaction is completed.

Pursuant to a power of attorney on file in this office, we are forwarding a copy of this letter to your authorized representative.

Sincerely yours,

Assistant Chief Counsel (Corporate)

By \_\_\_\_\_  
Robert T. Hawkes  
Assistant to the Chief, Branch 4