

Internal Revenue Service

Department of the Treasury

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Distributing =

Controlled =

Sub =

Controlled Sub 1 =

Distributing
Savings Plan 1 =

Distributing
Savings Plan 2 =

Agreement =

Individual A =

Individual B =

Individual C =

Business A =

Business B =

a =

b =

C =

This letter responds to your September 10, 1999 request for rulings on certain federal income tax consequences of the proposed transactions described below.

The rulings given 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. Verification of the information, representations, and other data may be required as part of the audit process.

Summary of Facts

Publicly traded Distributing is the common parent of a consolidated group and has outstanding Class A Stock and Class B stock (together, the "Distributing Stock") and one series of preference stock. Individual A, Individual B, Individual C, and Distributing Savings Plan 1 each owns five percent or more of the vote or value of the Distributing Stock.

Distributing engages in Business A and Business B directly and through wholly owned subsidiaries. Distributing wholly owns Sub.

We have received financial information indicating that Business A, which will be conducted by Distributing, and Business B, which will be conducted by Controlled, each has had gross receipts and operating expenses representing the active conduct of a trade or business for each of the past five years.

Proposed Transactions

Business A and Business B each suffers significant competitive disadvantages by being affiliated with the other. Distributing therefore proposes to separate the two businesses in the following series of transactions:

(i) Distributing will contribute to newly formed, wholly owned Controlled Sub 1 certain intellectual property used principally in Business B. Controlled Sub 1 will grant to Sub a nonexclusive, royalty-free license to use this intellectual property in exchange for a non-exclusive, royalty-free license to use certain Business A intellectual property owned by Sub. The two licenses will be approximately equal in value.

(ii) Distributing will contribute its Business B assets, including the stock of

Controlled Sub 1 and other entities engaged in Business B, to newly formed Controlled in exchange for all of the Controlled stock, the assumption by Controlled of related liabilities, and the Cash Payment described below in step (iv) (the "Contribution").

(iii) It is expected that Controlled will effect a recapitalization (the "Recapitalization") before the IPO described below in step (iv) to increase or decrease the number of shares of Controlled stock outstanding.

(iv) Controlled will issue up to a percent of its stock (determined post-issuance) in an initial public offering (the "IPO"). Controlled will distribute b dollars of the IPO proceeds to Distributing (the "Cash Payment"). Distributing will segregate the Cash Payment and, within one year after the Distribution described below in step (vi), use it to pay creditors or distribute it to Distributing shareholders.

(v) Controlled will borrow from third parties an amount determined to be appropriate by Distributing and Controlled after consulting with their financial advisors, with the proceeds of this borrowing being used: (i) as working capital; (ii) to repay debts of Controlled that have arisen in the ordinary course of business; and (iii) to repay intercompany debts that subsidiaries of Controlled owe to Distributing and its subsidiaries that have arisen in the ordinary course of the borrowing corporation's and the lending corporation's business.

(vi) Distributing will distribute the Controlled stock pro rata to the holders of Distributing Stock (other than Distributing Savings Plan 1 and Distributing Savings Plan 2) (the "Shareholders" and the "Distribution"). Cash will be paid to each registered holder of Distributing Stock entitled to receive less than one share of Controlled stock in the Distribution in lieu of issuing fractional shares of Controlled stock.

(vii) Distributing will distribute to each of Distributing Savings Plan 1 and Distributing Savings Plan 2 (the "Plans") an amount of cash with respect to each share of Distributing Stock held by a Plan that approximately equals the fair market value of the Controlled stock distributed to each Shareholder in the Distribution on each share of Distributing Stock held by the Shareholder.

Representations

Distributing makes the following representations concerning the proposed transactions:

(a) 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 Distributing Shareholder.

(b) The five years of financial information submitted on behalf of Distributing's

Business A and Business B represents, in each case, its present operations, and there have been no substantial operational changes since the date of the last financial statements submitted.

(c) Following the transactions, Distributing and Controlled each will continue the active conduct of its business, independently and with its separate employees, except for (i) certain transitional services and (ii) employee arrangements resulting from the Agreement.

(d) The Distribution is being carried out to allow Business A and Business B each to pursue business opportunities that are unavailable while the two businesses remain affiliated. The Distribution is motivated, in whole or substantial part, by this and other corporate business purposes.

(e) Apart from possible charitable gifts of Controlled stock by Individual A, Individual B, and Individual C of less than percent of the Controlled stock each receives in the Distribution, there is no plan or intention by the Distributing Savings Plan 1, Individual A, Individual B, or Individual C, and the management of Distributing, to the best of its knowledge is not aware of any plan or intention by any remaining shareholder, to sell, exchange, transfer by gift, or otherwise dispose of any stock of Distributing or Controlled after the transactions.

(f) 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 § 4.05(1)(b) of Rev. Proc. 96-30, 1996-1 C.B. 696,705, and purchases of Distributing Stock made pursuant to Distributing's existing buyback program.

(g) 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.

(h) No intercorporate debt will exist between Distributing and Controlled at the time of, or after, the Distribution, other than trade payables having arm's length terms that are (i) incurred by Controlled in receiving transitional services from Distributing, (ii) incurred by Distributing in purchasing products manufactured by Controlled, or (iii) otherwise incurred in the ordinary course of Distributing's or Controlled's business.

(i) To the extent required by law, the income tax liability for the taxable year in which investment credit property (including any building to which § 47(d) of the Internal Revenue Code applies) is transferred will be adjusted pursuant to § 50(a)(1) or (a)(2) (or § 47, as in effect before amendment by P.L. 101-508, Title 11, 104 Stat. 1388, 536 (1990), if applicable) to reflect an early disposition of the property.

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

(k) The liabilities assumed (within the meaning of § 357(d)) in the Contribution were incurred in the ordinary course of business and are associated with the assets being transferred.

(l) Immediately before the Distribution, any 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). Any excess loss account Distributing may have in Controlled Stock will be included in income immediately before the Distribution as required by the applicable regulations (see § 1.1502-19).

(m) Payments made in any continuing transactions between Distributing and Controlled will be for fair market value based on terms and conditions arrived at by the parties bargaining at arms' length.

(n) No two parties to the transactions are investment companies as defined in § 368(a)(2)(F)(iii) and (iv).

(o) The payment of cash in lieu of fractional shares will be undertaken solely for the purpose of avoiding the expense and inconvenience of issuing and transferring fractional shares and does not represent separately bargained for consideration. The method used for handling fractional share interests is designed to limit the amount of cash received by any one shareholder to less than the value of one full Controlled share.

(p) For purposes of § 355(d), immediately after the Distribution, no person (as determined after the application of § 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 with respect to 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.

(q) For purposes of § 355(d), immediately after the Distribution, no person (as determined after the application of § 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.

(r) 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 entitled to vote or stock possessing 50 percent or more of the total value of all classes of stock of either Distributing or Controlled.

Rulings

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

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

(2) No gain or loss will be recognized by Distributing on the Contribution (§§ 357(a), 361(a), and 361(b)(1)(A) and (3)).

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

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

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

(6) No gain or loss will be recognized by Distributing on the Distribution (§ 361(c)(1)).

(7) No gain or loss will be recognized by (and no amount will otherwise be included in the income of) any Distributing Shareholder on receipt of Controlled stock in the Distribution (§ 355(a)(1)).

(8) The aggregate basis of the Distributing Stock and the Controlled stock in the hands of each Distributing Shareholder after the Distribution (including any fractional interests to which the Shareholder would be entitled) will equal the aggregate basis of

the Distributing Stock held by the Shareholder immediately before the Distribution, allocated between the Distributing Stock and Controlled stock in proportion to the fair market value of each in accordance with § 1.358-2(a)(2) (§ 358(a)(1), (b)(2), and (c)).

(9) The holding period of the Controlled stock received by each Distributing Shareholder will include the period during which the Distributing Shareholder has held the Distributing shares on which the Distribution is made, provided the Distributing Stock is held as a capital asset on the date of the Distribution (§ 1223(1) and (1)(B)).

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

(11) If a Distributing Shareholder receives cash as the result of an independent distribution agent's sale of a fractional share of Controlled stock, gain or loss will be recognized by the Shareholder measured by the difference between the basis of the fractional share interest, as determined in ruling (8), above, 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 a capital gain or loss subject to the provisions and limitations of Subchapter P of Chapter 1 of the Code (§§ 1221 and 1222).

Caveats

We express no opinion on the tax treatment of the transactions under other sections of the Code or regulations or the tax treatment of any conditions existing at the time of, or effects resulting from the transactions that are not specifically covered by the above rulings. In particular, we express no opinion about (i) the exchange of licenses described above in step (i), (ii) the Recapitalization described above in step (iii), (iii) the distribution of cash in lieu of Controlled stock described above in step (vii), (iv) the qualified status of the Plans under § 401(a) or the effects of the transactions described herein on such status, and (v) any issue arising under § 404(k).

Procedural Statements

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 transactions covered by this letter are completed.

Under a power of attorney on file in this office, a copy of this letter is being sent to the taxpayer and to the second authorized representative.

Sincerely,

Assistant Chief Counsel (Corporate)

By: Wayne T. Murray

Wayne T. Murray

Senior Technician/Reviewer

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