

Internal Revenue Service

Department of the Treasury

Index Number: 0355.01-00

Washington, DC 20224

Number: **200023040**
Release Date: 6/9/2000

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Telephone Number:

Refer Reply To:
CC:DOM:CORP:2-PLR-113868-99
Date:
March 14, 2000

LEGEND:

Distributing 2 =

Forco =

Distributing 1 =

Subsidiary =

Controlled =

Country X =

Business A =

Business B =

Business C =

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Date 1 =

Date 2 =

Date 3 =

This letter responds to your letter dated August 10, 1999, requesting rulings as to certain federal income tax consequences of a proposed transaction. Additional information was submitted in letters dated December 6, 1999, January 24, February 4, March 10, and March 13, 2000. The information submitted for consideration is summarized below.

Distributing 2 (sometimes referred to hereinafter as "Taxpayer") is a domestic corporation and the common parent of a consolidated group (the "D group"), with a fiscal year ending on Date 1. Distributing 2 was formed on Date 2 in what is represented to have been a transaction qualifying under § 351 of the Internal Revenue Code. Distributing 2 has a single class of common stock outstanding, all shares of which are owned by Forco, a Country X corporation. Distributing 2 is a holding company that owns all of the stock of two domestic corporations, Distributing 1 and Subsidiary.

Distributing 1 is a domestic corporation in the D group engaged in Business A. Prior to the incorporation of Distributing 2, all of the outstanding stock of Distributing 1 was directly owned by Forco.

Subsidiary is a domestic corporation in the D group engaged directly, and indirectly through its wholly owned subsidiaries, in Business B. Subsidiary was formed on Date 3 in what is represented to have been a transaction qualifying under §351 of the Code.

Controlled is a domestic corporation in the D group engaged directly, and indirectly through its wholly owned subsidiaries, in Business C. All of Controlled's outstanding stock is owned by Distributing 1.

Financial information has been received indicating that Distributing 2 (through Distributing 1 and Subsidiary), Distributing 1, and Controlled each have had gross receipts and operating expenses representative of the active conduct of a trade or business for each of the past five years.

Taxpayer has provided sufficient documentation that management, systemic and

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other problems exist under the current corporate structure in which Controlled is controlled by Distributing 1. Specifically, the current structure of operating Business A and Business C with common ownership interferes with the ability of the management of Distributing 1 and Controlled to focus on their respective businesses. The separation will allow the management of each to make decisions based on factors relevant to each business' success.

Accordingly, to improve the fit and focus of the operations of Business A and Business C, the following transactions are proposed:

(i) Forco will incorporate Forco Sub under the laws of Country X through a contribution of a portion of its stock in Distributing 2, along with certain other stock and assets. The portion of the Distributing 2 stock to be contributed by Forco to Forco Sub will be equal to the net book value of Controlled.

(ii) Forco Sub will incorporate Newco, a domestic corporation, through a contribution of all of the stock in Distributing 2 received in Step (i) above.

(iii) To the extent necessary to eliminate any excess loss account (ELA) in its Controlled stock, Distributing 1 will make a cash contribution to Controlled.

(iv) Distributing 1 will distribute all of the Controlled stock to Distributing 2.

(v) Distributing 2 will distribute all of the Controlled stock to Newco in exchange for the Distributing 2 stock held by Newco.

The following representations have been made with respect to the proposed transactions:

(a) The indebtedness owed by Controlled to Distributing 1 after the distribution of the Controlled stock will not constitute stock or securities.

(b) No part of the consideration to be distributed by Distributing 1 will be received by a shareholder 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 and Controlled is representative of each corporation's present operation, and there have been no substantial operational changes since the date of the last financial statements submitted.

(d) Following the distribution of the Controlled stock to Distributing 2, Distributing 1 and Controlled will each continue the active conduct of its business, independently and with their own separate employees.

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(e) The distribution of the Controlled stock is carried out for the following corporate business purpose: to effect fit and focus. The distribution of the Controlled stock is motivated, in whole or substantial part, by this corporate business purpose.

(f) There is no plan or intention by Distributing 2 to sell, exchange, transfer by gift, or otherwise dispose of its stock in, or securities of, Distributing 1 after the transaction.

(g) 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 transaction.

(h) There is no plan or intention to liquidate either 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 transaction, except in the ordinary course of business.

(i) Distributing 1 neither accumulated its receivables nor made extraordinary payment of its payables in anticipation of the distribution.

(j) Other than trade account indebtedness created in the ordinary course of business through continuing transactions at terms comparable to those which could be obtained in an arm's-length transaction, no intercorporate debt will exist between Distributing 1 and Controlled at the time of, or subsequent to, the distributions. Except for amounts owed by Distributing 1 to Controlled resulting from intercompany loans, there is no intercorporate debt existing between Distributing 1 and Controlled, and none has been canceled, forgiven, or discounted.

(k) Immediately before the distributions, 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, any excess loss account Distributing 1 may have in the Controlled stock will be included in income immediately before the distribution (see § 1.1502-19).

(l) Payments made in connection with all continuing transactions, if any, between Distributing 1 and Controlled, will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.

(m) None of the parties to the transaction are investment companies as defined in § 368(a)(2)(F)(iii) and (iv).

(n) Less than 50 percent of the total combined voting power of all classes of

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Distributing 1 stock entitled to vote and less than 50 percent of the total value of shares of all classes of Distributing 1 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 of the Controlled stock to Distributing 2 (determined after applying § 355(d)(6)).

(o) 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 entitled to vote of either Distributing 1 or Controlled, or stock possessing 50 percent or more of the total value of all classes of stock of either Distributing 1 or Controlled.

(p) The indebtedness owed by Controlled to Distributing 2 after the distribution of the Controlled stock will not constitute stock or securities.

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

(r) The five years of financial information submitted on behalf of Distributing 2 and Controlled is representative of each corporation's present operation, and there have been no substantial operational changes since the date of the last financial statements submitted.

(s) The financial information submitted on behalf of Subsidiary for each year of its existence is representative of Subsidiary's present operation, and with regard to Subsidiary there have been no substantial operational changes since the date of the last financial statements submitted.

(t) Immediately after the transactions, at least 90 percent of the fair market value of the gross assets of Distributing 2 will 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).

(u) The assets representing Business B of Subsidiary represent at least five percent of the total gross assets of Subsidiary.

(v) Following the transactions, Distributing 2 and Controlled will each continue the active conduct of its business, independently and with its own separate employees.

(w) The distribution of the Controlled stock is carried out for the following corporate business purpose: to effect fit and focus. The distribution of the Controlled stock is motivated, in whole or substantial part, by this corporate business purpose.

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(x) There is no plan or intention by Forco to sell, exchange, transfer by gift, or otherwise dispose of its stock in, or securities of, Forco Sub, Distributing 2, or Controlled after the transaction.

(y) There is no plan or intention by Forco Sub to sell, exchange, transfer by gift, or otherwise dispose of its stock in, or securities of, Controlled or Newco after the transaction.

(z) There is no plan or intention by Newco to sell, exchange, transfer by gift, or otherwise dispose of its stock in, or securities of, Controlled after the transaction.

(aa) 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 transaction.

(bb) There is no plan or intention to liquidate either 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 transaction, except in the ordinary course of business.

(cc) Distributing 2 neither accumulated its receivables nor made extraordinary payment of its payables in anticipation of the distribution.

(dd) Other than trade account indebtedness created in the ordinary course of business through continuing transactions at terms comparable to those which could be obtained in an arm's-length transaction, no intercorporate debt will exist between Distributing 2 and Controlled at the time of, or subsequent to, the distributions. Except for amounts owed by Distributing 2 to Controlled resulting from intercompany loans, there is no intercorporate debt existing between Distributing 2 and Controlled, and none has been canceled, forgiven, or discounted.

(ee) Immediately before the distributions, 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, 1995-2 C.B. 147, and as currently in effect; § 1.1502-13 as published by T.D. 8597). Further, any excess loss account Distributing 2 may have in the Controlled stock will be included in income immediately before the distribution (see § 1.1502-19).

(ff) Payments made in connection with all continuing transactions, if any, between Distributing 2 and Controlled, will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.

(gg) None of the parties to the transaction are investment companies as defined

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in § 368(a)(2)(F)(iii) and (iv).

(hh) Less than 50 percent of the total combined voting power of all classes of Distributing 2 stock entitled to vote and less than 50 percent of the total value of shares of all classes of Distributing 2 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)).

(ii) 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 entitled to vote of either Distributing 2 or Controlled, or stock possessing 50 percent or more of the total value of all classes of stock of either Distributing 2 or Controlled.

(jj) Distributing 2, Distributing 1, Controlled, and Forco will each pay their own expenses, if any, incurred in connection with the transactions.

(kk) Forco and Forco Sub are corporations as defined in § 7701(a)(3), and are foreign corporations.

(ll) None of Distributing 1, Distributing 2, or Controlled are foreign corporations.

(mm) Neither Distributing 1 nor Distributing 2 is publicly traded.

(nn) Prior to the distributions, neither Distributing 1 nor Controlled has any direct foreign shareholders.

(oo) Distributing 1, Distributing 2, and Controlled have not been United States real property holding corporations, as defined in § 897(c)(2), at any time during the five year period ending on the date of the proposed distributions.

(pp) Distributing 1, Distributing 2, and Controlled will not be United States real property holding corporations immediately prior to the distributions.

(qq) Other than the stock of Distributing 2, Forco will not contribute any other U.S. asset or U.S. Branch to Forco Sub as part of its contribution.

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

(1) Solely for federal income tax purposes, the distribution of the Controlled stock by Distributing 2 to Newco will be characterized as the distribution of the Controlled stock by Distributing 2 to Forco, followed by a deemed contribution of the

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Controlled stock by Forco to Forco Sub, followed by a deemed contribution of the Controlled stock by Forco Sub to Newco.

(2) No gain or loss will be recognized by Distributing 1 upon the transfer of property to Controlled in constructive exchange for Controlled stock, as described above (§§ 351(a)).

(3) No gain or loss will be recognized by Controlled upon the receipt of property in constructive exchange for Controlled stock (§ 1032(a)).

(4) Controlled's basis in the property received will be the same as the basis of such property in the hands of Distributing 1 immediately prior to the transaction (§ 362(a)).

(5) The basis of the Controlled stock in the hands of Distributing 1 will be increased by an amount equal to the basis of the property transferred by Distributing 1 to Controlled (§ 358).

(6) The holding period of the Distributing 1 assets received by Controlled will include the period during which such assets were held by Distributing 1 (§ 1223(2)).

(7) No gain or loss will be recognized by Distributing 1 upon the distribution of the Controlled stock to Distributing 2, as described above (§ 355(c)).

(8) No gain or loss will be recognized by (and no amount will be included in the income of) Distributing 2 upon its receipt of the Controlled stock (§355(a)(1)).

(9) The aggregate basis of the Distributing 1 and Controlled stock in the hands of Distributing 2 after the First Distribution will be the same as the basis in the Distributing 1 stock held by Distributing 2 immediately before the First Distribution, allocated between the stock of Distributing 1 and Controlled in proportion to the fair market value of each in accordance with Treas. Reg. § 1.358-2(a)(2) (§§ 358(a)(1) and (b)(1)).

(10) The holding period of the Controlled stock received by Distributing 2 will include the holding period of its Distributing 1 stock, provided that such Distributing 1 stock is held as a capital asset on the date of the First Distribution (§ 1223(1)).

(11) As provided in § 312(h), proper allocation of earnings and profits between Distributing 1 and Controlled will be made under Treas. Reg. § 1.312-10(b) and § 1.1502-33(f)(2).

(12) No gain or loss will be recognized by Distributing 2 upon the distribution of

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the Controlled stock to Forco, as described in ruling (1) above (§ 355(c)).

(13) No gain or loss will be recognized by Distributing 2 under § 367(e)(1) upon the distribution of the Controlled stock to Forco, as described in ruling (1) above (§ 1.367(e)-1(c)).

(14) No gain or loss will be recognized by (and no amount will be included in the income of) Forco upon its receipt of the Controlled stock (§ 355(a)(1)).

(15) The aggregate basis of the Distributing 2 and Controlled stock in the hands of Forco after the distribution described in ruling (1) above will be the same as the basis in the Distributing 2 stock held by Forco immediately before such distribution, allocated between the stock of Distributing 2 and Controlled in proportion to the fair market value of each in accordance with Treas. Reg. § 1.358-2(a)(2) (§§ 358(a)(1) and (b)(1)).

(16) The holding period of the Controlled stock received by Forco will include the holding period of Forco's Distributing 2 stock, provided that such Distributing 2 stock is held as a capital asset on the date of the distribution of the Controlled stock to Forco (§1223(1)).

(17) As provided in § 312(h), proper allocation of earnings and profits between Distributing 2 and Controlled will be made under Treas. Reg. § 1.312-10(b) and § 1.1502-33(e).

(18) Application of § 1504(a)(3)(A) is hereby waived. Provided that after the transactions Newco and its subsidiaries constitute an affiliated group of corporations within the meaning of § 1504(a), Newco and its includible subsidiaries may join in the filing of a consolidated federal income tax return from the date they become members of a consolidated group of which Newco is the common parent and for subsequent taxable years.

No opinion is expressed about the tax treatment of the proposed transactions 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 proposed transactions that are not directly covered by the above rulings. In particular, no opinion is expressed on the qualification under § 351 of the deemed contribution of the Controlled stock by Forco to Forco Sub, or the deemed contribution of the Controlled stock by Forco Sub to Newco. In addition, no opinion is expressed on whether any or all of the above described foreign corporations are passive foreign investment companies ("PFICs") within the meaning of § 1297(a) and the related regulations to be promulgated. If it is determined that any of the above described foreign corporations are PFICs, no opinion is expressed related to the application of §§ 1291 through 1298 to the proposed transaction. In particular, in a transaction in which gain is not recognized, regulations under § 1291(f) may require gain recognition notwithstanding any other provisions of

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the Code.

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

This ruling letter is directed only to the taxpayer who requested it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

Each taxpayer involved in the proposed transactions should attach a copy of this letter to the taxpayer's federal income tax return for the taxable year in which the proposed transaction is completed.

In accordance with a power of attorney on file in this office, a copy of this letter is being sent to the taxpayer.

Sincerely,

Assistant Chief Counsel (Corporate)

By:

Lewis K Brickates
Assistant to Chief, Branch 2