

Internal Revenue Service

Department of the Treasury

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Person to Contact:

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Telephone Number:

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CC:DOM:CORP:5 PLR-119206-99

Date:

April 19, 2000

Re:

Parent =

PSub1 =

Subsidiary 1 =

PSub2 =

PSub2-LLC =

PSub2-LLC-A =

Subsidiary 2 =

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LLC-A2 =

LLC-A2's Subsidiary =

LLC-A1 =

PSub2-LLC-B =

LLC-B1 =

LLC-B2 =

LLC-C1 =

LLC-C2 =

PSub3 =

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PSub4 =

Subsidiary 4 =

PSub5 =

PSub6 =

PSub7 =

Subsidiary 7A =

Subsidiary 7B =

Subsidiary 7C =

PSub8 =

Distributing =

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DSub1 =

DSub1's Subsidiaries =

DSub2 =

DSub3 =

Corporation =

D-LLC1 =

D-LLC-A1 =

D-LLC-A2 =

D-LLC 2 =

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Controlled =

CSub 1 =

CSub 2 =

CSub3 =

CSub4 =

CSub4's LLC =

C-LLC1 =

C-LLC2 =

C-LLC4 =

C-LLC3 =

C-LLC5 =

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ServiceCo =

New LLC =

State X =

State Y =

Business A =

Activity A1 =

Activity A2 =

Activity A3 =

Asset Group 1 =

Asset Group 2 =

Asset Group 3 =

Asset Group 4 =

Asset Group 5 =

Asset Group 6 =

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Asset Group 7 =

Asset Group 8 =

Asset Group 9 =

Agreements =

State Commission =

Federal Commission =

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We reply to your letter dated December 7, 1999, in which you request rulings as to the federal tax consequences of a proposed transaction. Additional information was received in subsequent submissions. The information provided is summarized below.

Parent, an accrual basis taxpayer, is a holding company and the common parent of an affiliated group of corporations filing consolidated federal income tax returns. Parent's common stock is publicly traded on national exchanges. Parent has no preferred stock outstanding. Parent conducts its various businesses through directly and indirectly owned subsidiaries and limited liability companies.

Parent owns 100 percent of the stock of PSub1, PSub2, PSub3, PSub4, PSub5, PSub6, PSub7, and PSub8. PSub1 wholly owns the stock of Subsidiary 1. PSub2 owns various subsidiaries and PSub2-LLC, which owns the limited liability companies

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and subsidiaries that comprise Group 1 and Group 2. Specifically, Group 1 includes wholly-owned PSub2-LLC-A, which holds all of the stock of Subsidiary 2. Subsidiary 2 holds an f percent interest in LLC-A2, which in turn wholly owns the stock of LLC-A2's Subsidiary. PSub2-LLC-A also wholly owns LLC-A1. Group 2 includes PSub2-LLC-B, which wholly owns LLC-B1 and LLC-B2. LLC-B2 in turn wholly owns LLC-C1 and LLC-C2. PSub4 owns d percent of the stock of Subsidiary 4. PSub7 owns all of the stock of Subsidiary 7A, Subsidiary 7B, and Subsidiary 7C.

Parent also owns all of the outstanding common stock of Distributing, a State X corporation. The outstanding preferred stock of Distributing is publicly traded, and its market value represents approximately e percent of the total value of all outstanding capital stock of Distributing.

Distributing is engaged in all aspects of Business A, including Activity A1, Activity A2, and Activity A3. Distributing operates Business A directly and through a wholly-owned limited liability company, D-LLC1, for which Distributing has elected treatment as a disregarded entity. Activity A1 is accomplished through the operation of certain facilities in State X (Asset Group 1, Asset Group 2, Asset Group 3, Asset Group 4, and Asset Group 5). Activity A2 involves the provision of services to approximately i customers in State X, utilizing Asset Group 9. Distributing conducts the retail aspects of Activity A3 through D-LLC1 and Asset Group 8 and the wholesale aspects through a division of Distributing (Division) and Asset Group 7.

Distributing also owns all of the stock of DSub1, DSub2, DSub3, D-LLC2, and j percent of the stock of Corporation. DSub1 owns all of the stock of each of DSub1's Subsidiaries.

Controlled, a wholly-owned subsidiary of Distributing, is a State X corporation. Controlled currently owns all of the outstanding stock of CSub1 (a group finance subsidiary), CSub2 (which owns Asset Group 6), CSub3 (which is currently dormant), and CSub4 (which provides cash management services and intragroup loans to members of the Distributing group).

Distributing is subject to regulation by State Commission and certain of its activities are subject to regulation by Federal Commission. Parent's objective in this proposed transaction is to restructure its operations and assets related to Business A through a series of steps to place all of its unregulated activities (Activity A1 and Activity A3) in Controlled. Distributing will continue to own and operate the regulated Activity A2. Controlled will become, and Distributing will remain, a first-tier subsidiary of Parent.

Thus, Parent has proposed the following steps:

- (i) Controlled has formed a number of limited liability companies in State Y of which it will be the sole owner and member. Each limited liability

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company will be a disregarded entity treated as a division of Controlled for federal income tax purposes.

- (ii) Distributing will transfer assets associated with Activity A1 and the liabilities associated with those assets to each of Controlled's new limited liability companies formed in step (i) in constructive exchange for Controlled stock. Specifically, Distributing will transfer Asset Group 1 to C-LLC1, Asset Group 2 to C-LLC2, Asset Group 3 to C-LLC3, Asset Group 4 to C-LLC4, and Asset Group 5 (which includes Distributing's j percent stock ownership in Corporation) to C-LLC5.
- (iii) Controlled has formed New LLC in State Y of which it will be the sole owner and member and which will be a disregarded entity treated as a division of Controlled for federal income tax purposes. Controlled will transfer C-LLC1, C-LLC2, C-LLC3, C-LLC4, and C-LLC5 to New LLC.
- (iv) Distributing will transfer Division, which currently holds all of Distributing's assets associated with the wholesale aspect of unregulated Activity A3 and its related liabilities to D-LLC1. Distributing then will transfer D-LLC1 and all of its stock interests in DSub1, DSub2, and DSub3 to Controlled in constructive exchange for Controlled stock. Controlled then will transfer DSub1, DSub2, and DSub3 to New LLC.
- (v) In connection with these transfers, Controlled will assume Distributing's obligation under two debt instruments (the Debt Assumption): (1) Note 1

with a remaining principal balance of approximately \$g and (2) Note 2 payable to PSub3 in the amount of approximately \$h, which evidences a loan to be made by PSub3 to Distributing in connection with the proposed transaction. PSub3 will fund the loan with cash borrowed from unrelated third parties, and Distributing will use the cash to retire existing debt.

- (vi) Distributing will distribute the stock of Controlled to Parent.

In order to fully accomplish its internal restructuring, Parent proposes the following additional steps:

- (vii) Prior to Distributing's distribution of the Controlled stock, subject to State Commission approval, Controlled will distribute the stock of CSub3 to Distributing. CSub3 will be converted into a limited liability company.
- (viii) Controlled will transfer the stock of CSub2 to New LLC, which in turn will transfer that stock to C-LLC2, C-LLC3, and C-LLC4. CSub2 owns Asset

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Group 6, which is associated with the assets held by C-LLC2, C-LLC3, and C-LLC4.

- (ix) PSub2 will be converted into a limited liability company by merger into a limited liability company newly formed by Parent.
- (x) PSub2-LLC, a wholly-owned limited liability company of PSub2, will distribute all of its ownership interests in Group 1 and Group 2 to PSub2.
- (xi) PSub2 will distribute all of its ownership interests in Group 1 and Group 2 to Parent.
- (xii) Parent will transfer its interests in Group 1 and Group 2 to Controlled, which will transfer those interests to New LLC.
- (xiii) Parent will transfer all of its ownership interest in PSub2 and all of the outstanding stock of PSub1, PSub4, PSub6, PSub8, and PSub5 to Controlled.
- (xiv) Controlled will transfer all of the stock of PSub1, PSub4, PSub5, PSub6, and PSub8 to D-LLC1.
- (xv) PSub1 will distribute the stock of its wholly-owned Subsidiary 1 to D-LLC1.
- (xvi) Parent will transfer certain contracts and other assets related to Activity A3 to Controlled. Controlled then will transfer those items to D-LLC1.
- (xvii) Parent will form a new subsidiary ServiceCo, which will perform certain administrative services for all members of the Distributing group.

We have received financial information indicating that Business A has had gross receipts and operating expenses representing the active conduct of a trade or business for each of the past five years.

The taxpayer has not made any representations nor requested any rulings with respect to, and we express no opinion about, steps (vii) through (xvii). Taxpayer has made the following representations with respect to steps (i) through (vi):

- (a) Other than amounts owing from time to time under the Agreements, no intercorporate debt will exist between Distributing and Controlled (or Controlled subsidiaries) at the time of, or subsequent to, the transaction. None of such obligations are or will be stock or securities.
- (b) No part of the consideration distributed by Distributing will be received by

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Parent as a creditor, employee, or in any capacity other than as a shareholder of Distributing.

- (c) The five years of financial information submitted on behalf of Distributing represents the corporation's present operations, and, with regard to such corporation, there have been no substantial operational changes since the date of the last financial statement submitted.
- (d) Following the transaction, Distributing and Controlled each will continue the active conduct of its business, independently and with its separate employees.
- (e) The distribution of the stock of Controlled is motivated, in whole or substantial part, by the corporate business purpose of fit and focus. No securities (other than stock) of Controlled will be distributed.
- (f) There is no plan or intention by Parent to sell, exchange, transfer by gift, or otherwise dispose of any Distributing or Controlled stock after the transaction.
- (g) Except for periodic sinking fund redemptions of Distributing's publicly traded preferred stock, 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 § 4.05(1)(b) of Rev. Proc. 96-30, 1996-1 C.B. 696, 705.
- (h) 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 transaction, except in the ordinary course of business.
- (i) The total adjusted basis and the fair market value of the assets transferred to Controlled by Distributing will equal or exceed the amount of the liabilities assumed (as determined under § 357(d) of the Internal Revenue Code) by Controlled.
- (j) The liabilities assumed (as determined under § 357(d)), in the transaction, except for Note 1 and Note 2, were incurred in the ordinary course of business and are associated with the assets being transferred.
- (k) 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 (see § 1.1502-13 and

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§ 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). Distributing will not have an excess loss account with respect to the Controlled stock immediately before the distribution.

- (l) None of the assets transferred from Distributing to Controlled will be subject to investment tax credit recapture.
- (m) No two parties to the transaction are investment companies as defined in § 368(a)(2)(F)(iii) and (iv).
- (n) The distribution is not part of a plan (or series of related transactions) pursuant to which one or more persons will acquire, directly or indirectly, stock possessing 50 percent or more of the combined voting power of all classes of stock of Distributing or Controlled entitled to vote, or 50 percent or more of the total value of shares of all classes of Distributing or Controlled stock, within the meaning of § 355(e).
- (o) Payments made in connection with all continuing transactions between Distributing and Controlled will be at arm's length prices determined with reference to market conditions, subject to, where applicable, terms and conditions approved by the State Commission and/or Federal Commission.

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

- (1) The transfer of assets described in steps (ii) and (iv) by Distributing in constructive exchange for the stock of Controlled and Controlled's assumptions of Note 1 and Note 2 will qualify as a reorganization within the meaning of § 368(a)(1)(D). Distributing and Controlled each will be a "party to a reorganization" within the meaning of § 368(b).
- (2) No gain will be recognized by Distributing upon the transfers of assets to Controlled in constructive exchange for stock of Controlled and Controlled's assumptions of Note 1 and Note 2 (§§ 361(a) and 357(c)).
- (3) No gain or loss will be recognized by Controlled on the receipt of the assets from Distributing in constructive exchange for Controlled stock (§ 1032(a)).
- (4) The basis of the assets to be received by Controlled in the transaction will be the same as the basis of such assets in the hands of Distributing immediately prior to the transfer of such assets to Controlled (§ 362(b)).

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- (5) The holding period of each asset to be received by Controlled will include the period during which such assets were held by Distributing (§ 1223(2)).
- (6) No gain or loss will be recognized to Distributing on the distribution of all of the Controlled stock to Parent (§ 361(c)(1)).
- (7) No gain or loss will be recognized by (and no amount will be included in the income of) Parent on its receipt of Controlled stock in the distribution (§ 355(a)(1)).
- (8) The basis of the stock of Distributing and Controlled in the hands of Parent will be the same as the basis of the Distributing stock held by Parent immediately before the distribution, allocated between the Distributing stock and the Controlled stock in proportion to the fair market value of each in accordance with §1.358-2(a)(2) of the Income Tax Regulations (§ 358(a) and (b)(2)).
- (9) The holding period of the Controlled stock to be received by Parent will include the holding period of its Distributing stock on which the distribution is made, provided the stock is held as a capital asset on the date of the distribution (§ 1223(1)).
- (10) Proper allocation of earnings and profits between Distributing and Controlled will be made in accordance with §§ 312(h)(1), 1.312-10(a) and 1.1502-33(f)(2).

We express no opinion on the federal income tax treatment of the proposed transaction under other provisions of the Code or regulations (including the consolidated return regulations) or the tax treatment of any conditions existing at the time of, or effects resulting from, the proposed transaction that are not specifically covered by the above rulings. Specifically, the taxpayer understands that the National Office of the Internal Revenue Service, as requested by the taxpayer, has considered and ruled on only steps (i) through (vi). The taxpayer acknowledges that all other steps including, but not limited to, steps (vii) through (xvii) have not been reviewed or ruled upon by the National Office. The taxpayer further acknowledges that the federal income tax consequences of these other related steps may be examined and determined by the appropriate District Director's office on audit of the federal tax returns filed by Parent and its affiliates in which these steps are reported.

Temporary or final regulations relating to one or more of the issues addressed in this ruling (including regulations under § 358(g)) have yet to be adopted. Therefore, this ruling letter may be modified or revoked if adopted temporary or final regulations are inconsistent with any provision conclusions reached herein. See section 12.04 of Rev. Proc. 2000-1, 2000-1 I.R.B. 4, 46, which addresses, in greater detail, when a

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ruling will be revoked or modified. However, when the criteria in section 12.05 of Rev. Proc. 2000-1 are satisfied, a ruling is seldom revoked or modified retroactively, except in rare or unusual circumstances.

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

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

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

Sincerely,

Assistant Chief Counsel (Corporate)

By: *Filiz A. Serbes*

Filiz A. Serbes

Assistant to the Chief, Branch 5