

**Internal Revenue Service**

Department of the Treasury

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Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:  
**CC:DOM:CORP:2-PLR-100247-00**  
Date:  
**June 7, 2000**

Legend:

Distributing 2 =

Distributing 1 =

Controlled =

Sub A =

Sub B =

Sub C =

Date H =

Date I =

State X =

Business Y =

Business Z =

R =

S =

T =

U

=

Dear

This is in response to a letter dated December 30, 1999, requesting a ruling as to the federal income tax consequences of a transaction. Additional information was submitted in letters dated March 15, April 28, May 17, May 26 and May 30, 2000. The information submitted for consideration is substantially as set forth below:

Distributing 2, a State X corporation, is the common parent corporation of an affiliated group filing a consolidated return for federal income tax purposes that includes Distributing 2, Distributing 1, Controlled, and other affiliated corporations (the "Distributing Group"). Distributing 2 is a public company whose stock is widely held and traded on NASDAQ. Distributing 1, a State X corporation, is a wholly owned subsidiary of Distributing 2. Controlled was incorporated on Date A under the laws of State X to facilitate the transactions described herein. Prior to the Initial Public Offering (IPO) described herein, Controlled was wholly owned by Distributing 1. Subsequent to the IPO, Distributing retained ownership of at least 80% of Controlled's outstanding stock.

The Distributing Group is principally engaged in Business Y and Business Z. The expressed business purpose for the transactions is to facilitate Controlled's raising of equity capital on a substantially more cost effective basis than would be possible through i) an offering of additional stock by Distributing 2, or ii) an offering of stock by Controlled not made in connection with the separation of Controlled from Distributing 2. Controlled raised such capital with an IPO for less than 20% of its outstanding stock on Date B. Controlled needed to raise additional capital to pay off debt, fund capital expenditures, and for working capital needs.

### **Summary of Transaction**

Steps 1 through 4 have already been consummated. Steps 5 and 6 will be consummated within one year of Date H.

(1) On Date G, Distributing 1 formed a single member State X limited liability company (LLC), the only interest in which was issued to Distributing 1. Distributing transferred certain assets to the LLC.

(2) On Date H, Distributing 1 transferred to Controlled all the stock of Sub A, Sub B, Sub C, the LLC assets, and certain other assets in exchange for approximately R of cash, and the assumption of liabilities in the approximate amount of S (the "First Transfer"). Distributing 1 used the cash to satisfy third party creditors.

(3) Simultaneously with the First Transfer, Controlled consummated an IPO of the common stock of Controlled in an amount less than 20% of Controlled's total outstanding common stock.

(4) On Date H, Controlled contributed the LLC assets and other assets received from Distributing 1 in the First Transfer to Sub A in exchange for the assumption of liabilities in the approximate amount of S. The assets transferred to Sub A represent a *de minimis* amount of the assets Distributing 1 transferred to Controlled in the First Transfer.

(5) As set forth in the IPO prospectus pursuant to one overall plan of reorganization that includes the First Transfer, no later than one year following the IPO, Distributing 1 will distribute all of its stock of Controlled to Distributing 2 (the "First Distribution").

(6) Immediately after the First Distribution, Distributing 2 will distribute all of its Controlled stock pro rata to its shareholders (individually, the "Second Distribution"; together with the First Distribution, the "Distributions").

Financial information has been received that reflects that Distributing 1 and Distributing 2 have each had gross receipts and operating expenses representative of the active conduct of a trade or business for each of the past five years.

In Distribution 2, no fractional shares of Controlled will be distributed. In lieu of receiving fractional shares, each Distributing 2 shareholder's fractional shares will be aggregated and sold on the open market or to Distributing 2 by a distribution agent as soon as practicable after Distribution 2. The holders entitled to fractional share interests will receive their pro rata share of the cash proceeds from the sale.

In connection with the First Transfer and the Distributions, the following representations are made:

(a) 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.

(b) 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.

(c) The five years of financial information submitted on behalf of Distributing 1 is representative of the corporation's present operation, and with regard to such corporation, there has not been, and will not have been, any substantial operational changes since the date of the last financial statements submitted.

(d) Following the transaction, the Distributing 1, Distributing 2, 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) Immediately after the Distributions, at least five percent of Sub A, Sub B and Sub C's gross assets will be active trade or business assets as defined in § 355(b)(2).

(f) The five years of financial information submitted on behalf of Sub A, Sub B and Sub C is representative of what their operations will be at the time of the Distributions, and, with regard to each corporation, there has not been, and will not have been, any substantial operational changes since the date of the last financial statement submitted.

(g) Immediately after the Distributions, at least 90 percent of the fair market value of the gross assets of Distributing 2 will consist of the stock and securities of Distributing 1.

(h) Immediately after the Distributions, at least 90 percent of the fair market value of the gross assets of Controlled will consist of the stock or securities of Sub A, Sub B, and Sub C.

(i) Following the Distributions, Distributing 2, Distributing 1, and Controlled will continue the active conduct of its business, independently and with separate employees.

(j) The Distributions are being carried out, in whole or substantial part, for the following corporate business purpose: Controlled raised equity capital in the IPO on a basis that raised significantly more funds per share (net of transaction costs) than would have been possible in the stock offering without the planned Distributions.

(k) The payment of cash in lieu of fractional shares of Controlled is solely for the purpose of avoiding the expense and inconvenience of issuing fractional shares and does not represent separately bargained for consideration. The method used for handling fractional shares is designed to limit the amount of cash received by any one shareholder to less than the value of one full share of Controlled stock. The total amount of cash paid in lieu of fractional shares will not exceed one percent of the fair market value of Controlled stock distributed to Distributing 2's shareholders in the Second Distribution.

(l) Except for the receipt of cash in lieu of fractional shares, there is no plan or intention by any shareholder who owns five percent or more of the stock of Distributing 2, and the management of Distributing 2, to the best of its knowledge, is not aware of any plan or intention on the part of any particular remaining shareholder of Distributing 2, to sell, exchange, transfer by gift, or otherwise dispose of any of their stock in either Distributing 2, or Controlled after the Distributions.

(m) There is no plan or intention by either Distributing 1, Distributing 2, 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.

(n) There is no plan or intention to liquidate either Distributing 1, Distributing 2, or Controlled, to merge either corporation with any other corporation, or to sell or otherwise dispose of their assets after the Distributions, except in the ordinary course of business.

(o) The total adjusted bases and the fair market value of the assets transferred to Controlled by Distributing 1 equals or exceeds the sum of any liabilities assumed by Controlled.

(p) The liabilities assumed by Controlled in the First Transfer were incurred in the ordinary course of business and are associated with the assets being transferred.

(q) Distributing 1 and Distributing 2 neither accumulated their receivables nor made extraordinary payments of their payables in anticipation of the transaction.

(r) 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 Treas. Reg. §§ 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; Treas. Reg. § 1.1502-13 as published in T.D. 8597). Further, Distributing 2's excess loss account, if any, with respect to its Controlled stock or Controlled's excess loss account, if any, with respect to the stock of any consolidated subsidiary will be included in income, immediately before the Second Distribution (Treas. Reg. § 1.1502-19).

(s) Other than obligations incurred in the ordinary course of business, no intercorporate debt will exist between Distributing 1, Distributing 2, and Controlled at the time of, or subsequent to, the Distribution.

(t) Except as in connection with a Tax Allocation Agreement, payments made in connection with all continuing transactions between Distributing 1, 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. The parties have agreed that Distributing 1 will provide Controlled and its subs with various services until the completion of the Distributions. Controlled may, upon notice to Distributing 1, extend the agreement for up to one year following the IPO. Controlled is required to use all commercially reasonable efforts to obtain these services from a source other than Distributing 1 prior to the completion of the Distributions; however, if Controlled is unable to obtain these services from another source and such services are necessary for Controlled to operate its business, then Distributing 1 will continue to provide these services for an additional period not

to exceed 6 months.

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

(v) Each 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 1, 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 or Controlled.

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

(x) Neither Distributing 2 nor Controlled was a U.S. Real Property Holding Company within the meaning of § 897 at any time during the five-year period ending on the date of the Second Distribution.

(y) Neither Distributing 1 nor Controlled was a U.S. Real Property Holding Company within the meaning of § 897 at any time during the five-year period ending on the date of the First Distribution..

(z) Sub B was a controlled foreign corporation (CFC) within the meaning of § 957 immediately before Distributing 1's transfer of Sub B's stock to Controlled in the First Transfer and was a CFC immediately after the First Transfer.

(aa) Sub C was a CFC within the meaning of § 957 immediately before Distributing 1's transfer of Sub C stock to Controlled in the First Transfer and was a CFC immediately after the First Transfer.

In connection with the Second Transfer, the following representations are made:

(bb) No stock or securities will be issued for services rendered to or for the benefit of the transferee in connection with the Second Transfer. No stock or securities will be issued for indebtedness of the transferee that is not evidenced by a security or for an interest on indebtedness which accrued on or after the beginning of the holding period of the transferor for the debt.

(cc) The proceeds received in collection of the income items will be included in ordinary income in computing the income of the transferee.

(dd) The transfer is not the result of the solicitation by a promoter, broker or investment house.

(ee) The transferor will not retain any rights in the property transferred to the transferee.

(ff) There is no indebtedness between the transferor and the transferee and there will be no indebtedness created in favor of the transferor as a result of the Second Transfer.

(gg) The adjusted basis and the fair market value of the assets to be transferred by the transferor to the transferee, will, in each instance, equal or exceed the sum of the liabilities assumed by the transferee.

(hh) The liabilities of the transferor to be assumed by the transferee were incurred in the ordinary course of business and are associated with the assets to be transferred.

(ii) The transfers and exchanges occurred under a plan agreed upon before the transaction in which the rights of the parties are defined.

(jj) Taking into account any issuance of additional shares of the transferee stock, any issuances for services, the exercise of any transferee stock rights, warrants, or subscriptions, a public offering of transferee stock, and the sale, exchange, transfer by gift, or other disposition of any of the stock of the transferee to be received in the Second Transfer, the transferor will be in control of the transferee within the meaning of § 368(b).

(kk) The transferor received, in constructive exchange, stock, securities or other property approximately equal to the fair market value of the property transferred to the transferee or for services rendered or to be rendered for the benefit of the transferee.

(ll) All exchanges occurred on approximately the same date.

(mm) There is no plan or intention on the part of the transferee to redeem or otherwise reacquire any stock or indebtedness to be issued in the Second Transfer.

(nn) The transferee will remain in existence and retain and use the property transferred to it in a trade or business.

(oo) There is no plan or intention by the transferee to dispose of the transferred property other than in the normal course of operations.

(pp) Each of the parties to the Second Transfer paid its own expenses, if any, in

connection with the Second Transfer.

(qq) The transferee will not be an investment company within the meaning of § 1.351.1(c)(1)(ii) of the regulations.

(rr) The transferor is not under the jurisdiction of a court in a title 11 or similar case (within the meaning of § 368(a)(3)(A)) and the stock or securities received in the exchange will not be used to satisfy the indebtedness of such debtor.

(ss) The transferee will not be not a “personal service corporation” within the meaning of § 269A of the Code.

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

(1) Distributing 1's transfer of all the stock of Sub A, Sub B, Sub C, the LLC assets and certain other assets in constructive exchange for additional shares of the common stock of Controlled, cash in the approximate amount of R, and Controlled's assumption of liabilities, followed by Distributing 1's distribution of all of its Controlled stock to Distributing 2 constituted a reorganization within the meaning of § 368(a)(1)(D) of the Code. Distributing 1 and Controlled will each be “a party to a reorganization” within the meaning of § 368(b).

(2) No gain or loss is recognized by Distributing 1 upon its constructive receipt of Controlled stock, R cash, and Controlled's assumption of liabilities in exchange for the assets received in the First Transfer provided that the R cash is paid to Distributing 1's creditors, as described above. Sections 357(a), 361(a) and 361(b)(3).

(3) No gain or loss is recognized by Distributing 1 upon the distribution of Controlled stock pursuant to the First Distribution. Section 361(c).

(4) No gain or loss is recognized by Controlled upon the receipt of assets from Distributing 1 in constructive exchange for its issuance of shares of Controlled stock. Section 1032.

(5) The basis of each asset received by Controlled from Distributing 1 is equal to the basis of such assets in the hands of Distributing 1 immediately prior to the transfer. Section 362(b).

(6) The holding period of each asset received by Controlled from Distributing 1 includes the period during which Distributing 1 held such asset. Section 1223(2).

(7) As provided in § 312(h), proper allocation of earnings and profits between Distributing 1 and Controlled will be made in accordance with Treas. Reg. § 1.312-10(a) and 1.1502-33.

(8) No gain or loss will be recognized to (and no amount will be included in the income of) Distributing 2 upon the receipt of Controlled stock pursuant to the First Distribution, as described above. Section 355(a)(1).

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

(10) The holding period of the Controlled common stock received by Distributing 2 will include the holding period of the Distributing 1 common stock on which the distributions will be made, provided such stock is held as a capital asset on the date of the distribution. Section 1223(1).

(11) No gain or loss will be recognized to (and no amounts will be included in the income of) the shareholders of Distributing 2 upon their receipt of Controlled stock (including any fractional share interests to which they may be entitled) as described above. Section 355(a)(1); Treas. Reg. § 1.355-1(c).

(12) The basis of the stock (including any fractional share interest to which they may be entitled) of Distributing 2 and Controlled in the hands of the shareholders of Distributing 2 after the Second Distribution will, collectively, be the same as the aggregate basis of the Distributing 2 stock held immediately before the Second Distribution and such basis will be allocated between the Distributing 2 stock and Controlled stock in proportion to their relative fair market values at the time of the Second Distribution in accordance with Treas. Reg. 1.358-2(a). Sections 358(a)(1) and 358(b).

(13) The holding period of the Controlled stock received by the shareholders of Distributing 2 will, in each instance, include the holding period of the Distributing 2 stock with respect to which the Second Distribution will be made, provided that the Distributing 2 stock is held as a capital asset by the respective shareholders of Distributing 2 on the date of the Second Distribution. Section 1223(1).

(14) No gain or loss will be recognized by Distributing 2 upon the distribution of all of its Controlled stock to its shareholders. Section 355(c)(1).

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

(16) If cash is received by a Distributing 2 shareholder as a result of a sale of a fractional share of Controlled stock by the distribution agent, the shareholder will have gain or loss measured by the difference between the basis of the fractional share, as determined in ruling (12), above, and the amount of cash received. If

the Controlled stock is held by the shareholder as a capital asset at such time, the gain or loss will be capital gain or loss subject to the provisions and limitations of Subchapter P of Chapter 1 of the Code. Sections 1221 and 1222.

(17) 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. (Treas. Reg. § 1.1502-13 and Treas. Reg. § 1.1502-14 as in effect before the publication of T.D. 8597, 1995-32 I.R.B. 6, and as currently in effect; Treas. Reg. § 1.1502-13 as published by T.D. 8597). Further, Distributing 2's excess loss account, if any, with respect to the Controlled stock or any consolidated subsidiary of Controlled will be included in income immediately before the distribution. Treas. Reg. § 1.1502-19.

(18) No gain or loss is recognized by Controlled upon the transfer of the LLC assets and other assets received in the First Transfer along with T of IPO proceeds to Sub A in constructive exchange for additional Sub A stock and the assumption of liabilities, as described above. Sections 351(a) and 357(a).

(19) The basis of each asset received by Sub A in the Second Transfer will equal the basis of that asset in the hands of Controlled immediately before the Second Transfer. Section 362(a).

(20) The holding period of each asset received by Sub A in the Second Transfer included the holding period of that asset in the hands of Controlled. Section 1223(2).

(21) No gain or loss is recognized by Sub A upon the receipt of assets from Controlled in the Second Transfer in constructive exchange for its issuance of shares of Sub A stock. Section 1032(a).

(22) The earnings and profits of Sub B, to the extent attributable to such stock under Treas. Reg. § 1.1248-2 or Treas. Reg. § 1248-3 (whichever is applicable) which were accumulated in taxable years of such foreign corporation after December 31, 1962, during the period Distributing 1 held the Sub B stock (or was considered as holding it by reason of the application of § 1223) while Sub B was a controlled foreign corporation will be attributable to such stock held by Controlled. Treas. Reg. § 1.1248-1(a).

(23) The earnings and profits of Sub C, to the extent attributable to such stock under Treas. Reg. § 1.1248-2 or Treas. Reg. § 1248-3 (whichever is applicable) which were accumulated in taxable years of such foreign corporation after December 31, 1962, during the period Distributing 1 held the Sub C stock (or was considered as holding it by reason of the application of § 1223) while Sub C was a controlled foreign corporation will be attributable to such stock held by Controlled. Treas. Reg. § 1.1248-1(a).

No opinion is expressed whether any or all of the above-referenced foreign corporations are passive foreign investment companies (within the meaning of § 1297(a) of the Code and regulations to be promulgated thereunder). If it is determined that any or all of the above-described foreign corporations are passive foreign corporations, no opinion is expressed with respect to the application of §§ 1291 through 1298 to the proposed transactions. In particular, in a transaction in which gain is not otherwise recognized, regulations under § 1291(f) may require gain recognition notwithstanding other provisions of the Code.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

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.

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.

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

Sincerely,  
Assistant Chief Counsel (Corporate)

By: \_\_\_\_\_  
Lewis K Brickates  
Assistant to Chief, Branch 2