

**Internal Revenue Service**

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CC:CORP:1-PLR-158635-01  
Date:  
April 11, 2002

Legend:

A =

B =

C =

D =

E =

Investment Banker =

Distributing 1 =

Distributing 2 =

Controlled 1 =

Controlled 2 =

MergedCo 1 =

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MergedCo 2 =

Country A Assets =

S1 =

S2 =

S3 =

S4 =

S5 =

S6 =

S7 =

S8 =

S9 =

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S10 =

S10A =

S11 =

S12 =

S13 =

S14 =

S15 =

S16 =

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S18 =

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S19 =

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S24 =

F1 =

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F5 =

F6 =

F7 =

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F8 =

F9 =

F10 =

F11 =

F12 =

LLC 1 =

Country A =

State A =

Business A =

Business B =

Business C =

Specialty =

a =

b =

c =

d =

e =

f =

g =

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h =

i =

j =

k =

Plan L =

Plan M =

Plan N =

Plan O =

Date 1 =

Dear

This letter responds to a letter dated June 26, 2001 (as resubmitted on November 13, 2001), submitted on your behalf by your authorized representative, in which rulings are requested as to the federal income tax consequences of a proposed transaction. The information submitted in that request and the additional information that was submitted in letters dated September 20, 2001, October 5, 2001, October 16, 2001, October 19, 2001, November 29, 2001, December 31, 2001, February 25, 2002, and April 3, 2002, is summarized below.

#### SUMMARY OF FACTS

Distributing 1, a publicly traded corporation and the common parent of an affiliated group, is organized under the laws of State A. Distributing 1 is a holding company whose operating subsidiaries carry on business in three distinct operating segments: Business A, Business B and Business C. Distributing 1 has common and preferred shares outstanding. More than 5% of Distributing 1's common shares are held by (i) A, the chairman of the board and CEO of Distributing 1, (ii) two wholly-owned subsidiaries of Distributing 1 (the "Specified Shareholders"), (iii) B and (iv) C. D and E own 100% of Distributing 1's preferred shares.

Distributing 1 owns all of the stock of S1, S2, S3, S4, S5, S6, S7, F1, F2 and F3, all of the preferred stock and a% of the common stock of Distributing 2, b% of LLC 1 and c% of the stock of F4, F5 and F6. Distributing 2 is a Country A corporation that owns all the stock of F7, F8, F9 and F10 and the Country A Assets. S2 owns all the stock of S8 and d% of S9. S3 owns all the stock of S10. S1 owns the remaining e% of F4, F5 and

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F6 and e% of F11. S4 owns all of S11, S12, S13, S14, f% of the common stock of Distributing 2 and the remaining g% of S9. S11 owns all of the stock of S15 and c% of F11. S12 owns all of S16. S13 owns all of the stock of S17, S18, S19, S20 and S21 and h% of S22. S14 owns i% of the common stock of Distributing 2. F10 owns all of F12. S8 owns all of S23 and S24. Unrelated third parties own j% of S22 and k% of LLC 1. F8, F10 and F12 have each made an election under Treasury Regulation §1.7701-3 to be treated as a disregarded entity for United States federal income tax purposes.

Distributing 1 seeks to separate Business C from Businesses A and B because of inherent conflicts of interest that exist between the businesses. These conflicts are preventing each business from realizing its full potential and are making it difficult for Business C to expand into Specialty.

Distributing 1 has also been advised by Investment Banker that the announcement of a spin-off of Business C would permit Distributing 1 to raise common equity capital during a period after the announcement and before the spin-off of Business C at a higher price per share (net of transaction costs) as compared to an offering absent a public commitment to the spin-off. Distributing 1 thus intends to issue common shares after the announcement and before the spin-off of Business C.

Accordingly, Distributing 1 intends to separate Business C from Businesses A and B in the following series of transactions (steps 1 through 25 referred to as the "Facilitating Transactions"):

- (1) S13 will convert to a State A limited liability company ("LLC 3") and will then distribute its stock in S17, S18, S19, S20, S21, and its h% interest in S22 to S4 in complete liquidation.
- (2) S11 will distribute its stock in S15 and its c% interest in F11 to S4.
- (3) S4 will distribute its stock in S15, S17, S18, S19, S20, S21, its c% interest in F11 and its h% interest in S22 to Distributing 1.
- (4) S12 will merge with and into a newly formed State A limited liability company ("LLC 2"), all of the membership interests of which will be owned by S4, with LLC 2 as the surviving entity. LLC 2 will distribute its stock in S16 to S4.
- (5) S4 will distribute its stock in S16 to Distributing 1.
- (6) S4 will purchase S2's d% interest in S9 either for cash or in exchange for property.

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- (7) S2 will distribute the stock of S8 to Distributing 1.
- (8) S8 will distribute the stock of S23 to Distributing 1.
- (9) S8 will merge with and into S24 with S24 as the surviving entity.
- (10) Distributing 2 will form a Country A corporation ("Holdco"). Distributing 2 will contribute the Country A Assets other than entities engaged in Business C to Holdco (such contributed Country A Assets, the "Contributed A Assets") in exchange for all the stock of Holdco and the assumption by Holdco of the debt of Distributing 2. Holdco will make an election under Treasury Regulation §1.7701-3 to be treated as a disregarded entity for United States federal income tax purposes.
- (11) Distributing 1, S4, and S14 will form a Country A corporation ("Controlled 2").
- (12) S4 will contribute a note ("Note 1") to Controlled 2 in an amount equal to f% of the fair market value of the common stock of Distributing 2.
- (13) S14 will contribute a note ("Note 2") to Controlled 2 in an amount equal to i% of the fair market value of the common stock of Distributing 2.
- (14) Distributing 1 will contribute a note ("Note 3") to Controlled 2 in an amount equal to the value of Holdco less the combined amounts of Note 1 and Note 2.
- (15) Controlled 2 will acquire the stock of Holdco from Distributing 2 for Note 1, Note 2 and Note 3.
- (16) Distributing 2 will distribute Note 1 to S4 in exchange for S4's f% interest in Distributing 2 common stock. Distributing 2 will distribute Note 2 to S14 in exchange for S14's i% interest in Distributing 2 common stock. Distributing 2 will distribute Note 3 to Distributing 1 without a corresponding exchange of Distributing 1's shares in Distributing 2 (steps 10 through 16 referred to as the "Internal Spin-Off").
- (17) Distributing 1 will contribute its stock in each first-tier entity (other than Distributing 2, S1, S2, S3, S5, S7, S15, S17, S18, S19, S20, S21, F1, F2, F3, the Specified Shareholders, its b% interest in LLC 1, its h% interest in S22 and its c% interests in F4, F5, F6 and F11) to S16.
- (18) Distributing 1 will form Controlled 1, a State A corporation.
- (19) Distributing 1 will contribute its interest in the following entities (the "Business C Entities") to Controlled 1 (the "Contribution"): Distributing 2, S1, S2, S3, S7, S19, S20, S21, its h% interest in S22, its b% interest in LLC 1 and its c% interest in

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F4, F5, F6 and F11.

- (20) Distributing 1 will transfer the following entities to S1 in partial satisfaction of the debt owed by Distributing 1 to S1: S5, S17, S18, F1, F2 and F3.
- (21) Distributing 1 will transfer S15 to S2 in partial satisfaction of debt owed by Distributing 1 to S2.
- (22) S3 will merge with and into S10, with S10 as the surviving entity.
- (23) S10 will change its name to "S10A."
- (24) Controlled 1 will contribute the stock of S19 and S7 to S10A.
- (25) Controlled 1 will contribute the stock of S20 and S21 to S1.
- (26) Distributing 1 will distribute all of the outstanding stock of Controlled 1 to Distributing 1's common shareholders other than the Specified Shareholders. The distribution will be pro rata, except the Specified Shareholders will receive additional common shares in Distributing 1 in lieu of Controlled 1 common shares (this step 26 referred to as the "External Spin-Off").

## STOCK OPTIONS AND OTHER STOCK-BASED EMPLOYEE BENEFITS

### Stock Options

Presently, Distributing 1 has in effect several stock option plans for its executives and key employees, including Plan L, Plan M, and Plan N (collectively, the "Option Plans"). Outstanding options granted under the Option Plans are collectively referred to as "Current Distributing Options."

Prior to the External Spin-Off, Controlled 1's Board of Directors will adopt a stock option plan that will be substantially similar to Plan L (the "Controlled 1 Option Plan"). It is expected that the Controlled 1 Option Plan will be approved by the shareholders of Controlled 1 after the External Spin-Off. Under the Controlled 1 Option Plan, (i) awards will be granted by a compensation committee comprised solely of two or more outside directors within the meaning of §162(m) and Treas. Reg. §1.162-27(e)(3), (ii) the plan document will state the maximum number of shares of Controlled 1 common stock with respect to which options may be granted during a specified period to any employee and (iii) except in the case of the substitute options described below, it is expected that the exercise price of each option will be equal to the fair market value of one share of Controlled 1 common stock as of the date of grant.

Each Current Distributing Option that was granted as an incentive stock option that is outstanding immediately prior to the External Spin-Off will be converted as of

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immediately prior to the External Spin-Off into (i) an adjusted incentive stock option to purchase Distributing 1 common shares (an "Adjusted Distributing ISO") and (ii) a substitute incentive stock option under the Controlled 1 Option Plan to purchase shares of Controlled 1 common stock (a "Controlled 1 ISO"). Each nonqualified Current Distributing Option that is outstanding immediately prior to the External Spin-Off will be converted as of immediately prior to the External Spin-Off into (i) an adjusted nonqualified option to purchase Distributing 1 common shares (collectively with an Adjusted Distributing ISO, an "Adjusted Distributing Option") and (ii) a substitute nonqualified option under the Controlled 1 Option Plan to purchase shares of Controlled 1 common stock (collectively with a Controlled 1 ISO, a "Controlled 1 Option").

The number of Distributing 1 common shares subject to each Adjusted Distributing Option will be the same as the number of shares subject to the Current Distributing Option. The exercise price of each Adjusted Distributing Option will equal the exercise price of the Current Distributing Option multiplied by a fraction, the numerator of which is the fair market value of one Distributing 1 common share immediately following the External Spin-Off and the denominator of which is the sum of (i) the fair market value of one Distributing common share immediately following the External Spin-Off and (ii) the fair market value of one share of Controlled 1 common stock immediately following the External Spin-Off multiplied by the number of shares of Controlled 1 common stock received in the External Spin-Off with respect to each Distributing common share (the "Spin-Off Ratio"). Distributing 1 interprets the Option Plans as providing that employment with Controlled 1 after the External Spin-Off will be treated as employment with Distributing 1 for purposes of determining the optionee's right to exercise the Adjusted Distributing Options and the termination of the exercise period thereunder. Each Adjusted Distributing Option will be identical, in all other respects, to the Current Distributing Option being adjusted, except that an Adjusted Distributing Option may be "stapled" with the Controlled 1 Option that relates to the same Current Distributing Option. If an Adjusted Distributing Option is "stapled" with a Controlled 1 Option, such options must be exercised together.

The number of shares of Controlled 1 common stock subject to each Controlled 1 Option granted in substitution of a Current Distributing Option will equal the number of shares of Controlled 1 common stock that would have been received in the External Spin-Off with respect to the number of Distributing 1 common shares subject to the Current Distributing Option. The exercise price of each Controlled 1 Option will equal the exercise price of the Current Distributing Option multiplied by a fraction, the numerator of which is the fair market value of one share of Controlled 1 common stock immediately following the External Spin-Off and the denominator of which is the sum of (i) the fair market value of one Distributing 1 common share immediately following the External Spin-Off and (ii) the fair market value of one share of Controlled 1 common stock immediately following the External Spin-Off multiplied by the Spin-Off Ratio. Each Controlled 1 Option will provide that employment with Distributing 1 after the External Spin-Off will be treated as employment with Controlled 1 in determining the

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optionee's right to exercise the Controlled 1 Option and the termination of the exercise period thereunder. Each Controlled 1 Option will, in all other respects, be subject to substantially the same terms as the Current Distributing Option being substituted, except that, as described above, a Controlled 1 Option may be "stapled" with the Adjusted Distributing Option that relates to the same Current Distributing Option. If a Controlled 1 Option is "stapled" with an Adjusted Distributing Option, such options must be exercised together.

### Restricted Stock

Pursuant to the terms of Plan L and Plan M, Distributing 1 has granted its executives and other key employees Distributing 1 common shares under outstanding restricted stock awards. Pursuant to the External Spin-Off, holders of restricted stock outstanding immediately prior to the External Spin-Off ("Outstanding Distributing Restricted Stock") will receive shares of Controlled 1 common stock in the same manner as any holder of Distributing 1 common shares. Such shares of Controlled 1 common stock ("Controlled 1 Restricted Stock") will be subject to the same terms and vesting schedule as the applicable Current Distributing Restricted Stock. Distributing interprets Plan L and Plan M as providing that employment with Controlled 1 after the External Spin-Off will be treated as employment with Distributing 1 for purposes of determining the vesting of Outstanding Distributing Restricted Stock and Controlled 1 Restricted Stock.

### Stock Acquired Under the Distributing 1 Employee Stock Purchase Plan

Pursuant to the terms of Plan O, Distributing 1 has granted eligible employees who have elected to participate in Plan O options to purchase Distributing 1 common shares at a discounted price. Participating employees deposit a portion of their eligible compensation into an account (a "Periodic Deposit Account") that is used to purchase Distributing 1 common shares underlying the options at the end of each option period (the "Option Period"). Distributing 1 intends that the Option Period in effect immediately prior to the External Spin-Off will automatically terminate immediately prior to the External Spin-Off and the Periodic Deposit Account of each participant will be used to purchase Distributing 1 common shares immediately prior to the External Spin-Off. All holders of Distributing 1 common shares acquired under Plan O will receive shares of Controlled 1 common stock in the same manner as any holder of Distributing 1 common shares, except that the shares of Controlled 1 common stock received pursuant to the External Spin-Off will be subject to the same holding period requirements under §423(a) as the applicable Distributing 1 common shares.

### Stock-Based Deferred Compensation

Distributing 1 maintains several plans (each a "Distributing Deferred Compensation Plan") that allow certain employees and directors to defer the receipt of compensation and to be paid such deferred compensation in Distributing 1 common shares. It is

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expected that prior to the External Spin-Off, the Board of Directors of Controlled 1 will adopt deferred compensation plans that will be substantially similar to the corresponding Distributing 1 Deferred Compensation Plans (each a "Controlled 1 Deferred Compensation Plan").

It is intended that each participant's right to receive deferred compensation in the form of Distributing 1 common shares outstanding under each of the Distributing Deferred Compensation Plans, to the extent accrued as of immediately prior to the External Spin-Off ("Existing Deferred Compensation Amounts"), will be converted as of immediately prior to the External Spin-Off into a right to receive deferred compensation in the form of an equal number of Distributing 1 common shares and the number of shares of Controlled 1 common stock that would have been received in the External Spin-Off with respect to such number of Distributing 1 common shares. Pursuant to the External Spin-Off, all Existing Deferred Compensation Amounts with respect to employees and directors of Controlled 1 will be assumed by Controlled 1 and each such employee or director will receive a substitute right under the applicable Controlled 1 Deferred Compensation Plan to receive the same number Distributing 1 common shares and Controlled 1 common shares as immediately prior to the External Spin-Off, with the same terms and conditions as the original right to receive deferred compensation under the applicable Distributing Deferred Compensation Plan.

Distributing 1 and Controlled 1 intend to enter into an agreement providing for the issuance to participants in the Distributing Deferred Compensation Plans of the shares of Controlled 1 common shares that become distributable with respect to Existing Deferred Compensation Amounts under the Distributing Deferred Compensation Plans and for the issuance to participants in the Controlled 1 Deferred Compensation Plans of the Distributing 1 common shares that become distributable with respect to Existing Deferred Compensation Amounts under the Controlled 1 Deferred Compensation Plans.

## REPRESENTATIONS

With respect to the External Spin-Off, the taxpayer has made the following representations:

- (1) The payment of cash in lieu of fractional shares of Controlled 1 will be solely for the purpose of avoiding the expense and inconvenience to Distributing 1 of distributing fractional shares and does not represent separately bargained-for consideration. The total cash consideration to be paid in lieu of fractional Controlled 1 common shares will not exceed one percent of the total consideration that will be issued in the transaction to Distributing 1 shareholders. The fractional share interests of each Distributing 1 shareholder will be aggregated and no Distributing 1 shareholder will receive cash in an amount equal to or greater than the value of one full Controlled 1 common share.

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- (2) No part of the consideration to be distributed by Distributing 1 in the External Spin-Off will be received by a shareholder as an employee or in any capacity other than that of a shareholder of Distributing 1.
- (3) Immediately after the External Spin-Off, at least 90 percent of the fair market value of the gross assets of Distributing 1 will consist of the stock of S16, a controlled corporation that is engaged in the active conduct of a trade or business as defined in §355(b)(2).
- (4) Immediately after the External Spin-Off, the gross assets of the active business of S16 will have a fair market value that is at least five percent of the total fair market value of the gross assets of S16.
- (5) The 5 years of financial information submitted on behalf of S16 is representative of the business's present operations, and with regard to such business, there have been no substantial operational changes since the date of the last financial statements submitted.
- (6) Immediately after the External Spin-Off, at least 90 percent of the fair market value of the gross assets of Controlled 1 will consist of the stock of S1, S2, S10A and Distributing 2, each of which is a controlled corporation engaged in the active conduct of a trade or business as defined in §355(b)(2).
- (7) Immediately after the External Spin-Off, the gross assets of the active business of S2 will have a fair market value that is at least five percent of the total fair market value of the gross assets of S2.
- (8) Immediately after the External Spin-Off, the gross assets of the active business of S1 will have a fair market value that is at least five percent of the total fair market value of the gross assets of S1.
- (9) Immediately after the External Spin-Off, the gross assets of the active business of S10A will have a fair market value that is at least five percent of the total fair market value of the gross assets of S10A.
- (10) The 5 years of financial information submitted on behalf of S1, S2 and S10A is representative of each corporation's present operation, and with regard to each such corporation, there have been no substantial operational changes since the date of the last financial statements submitted.
- (11) Following the External Spin-Off, Distributing 1 (through S16) and Controlled 1 (through S1, S2, S10A and Distributing 2) will each continue the active conduct of its business, independently and with its separate employees.
- (12) The distribution of stock of Controlled 1 is carried out for the following corporate

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business purposes: (i) to resolve the inherent conflicts associated with engaging in Businesses A, B, and C; and (ii) to facilitate a stock issuance by Distributing 1. The distribution of the stock of Controlled 1 is motivated, in whole or in substantial part, by these corporate business purposes.

- (13) There is no plan or intention by any individual shareholder of Distributing 1 (or the Specified Shareholders) who owns 5 percent or more of the stock of Distributing 1, and the management of Distributing 1, to its best knowledge, is not aware of any plan or intention on the part of any particular remaining shareholder or security holder of Distributing 1 to sell, exchange, transfer by gift, or otherwise dispose of any stock in, or securities of, either Distributing 1 or Controlled 1 after the External Spin-Off.
- (14) There is no plan or intention by either Distributing 1 or Controlled 1, directly or through any subsidiary corporation, to purchase any of its outstanding stock after the External Spin-Off, other than through stock purchases meeting the requirements of §4.05(1)(b) of Rev. Proc. 96-30.
- (15) There is no plan or intention to liquidate either Distributing 1 or Controlled 1, to merge either Distributing 1 or Controlled 1 with any other corporation, or to sell or otherwise dispose of the assets of either Distributing 1 or Controlled 1 after the External Spin-Off, except in the ordinary course of business.
- (16) The External Spin-Off 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 or Controlled 1, or stock possessing 50 percent or more of the total value of all classes of stock of either Distributing 1 or Controlled 1.
- (17) The total adjusted bases and the fair market value of the assets transferred to Controlled 1 by Distributing 1 each equals or exceeds the sum of the liabilities assumed by Controlled 1 plus any liabilities to which the transferred assets are subject.
- (18) The liabilities assumed in the External Spin-Off and the liabilities to which the transferred assets are subject were incurred in the ordinary course of business and are associated with the assets being transferred.
- (19) 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 (§1.1502-13 and §1.1502-14 as in effect before the publication of T.D. 8597, 1995-32 I.R.B. 6, and currently in effect; §1.1502-13 as published by T.D. 8597). Further, Distributing 1’s excess loss account, if any,

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with respect to the Controlled 1 stock and any excess loss account with respect to the stock of Controlled 1 subsidiaries will be included in income immediately before the distribution (§1.1502-19).

- (20) Payments made in connection with all continuing transactions between Distributing 1 and Controlled 1 will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.
- (21) No two parties to the External Spin-Off are investment companies as defined in §368(a)(2)(F)(iii) and (iv).
- (22) The exercise price of all Current Distributing Options is at least equal to the fair market value of a Distributing 1 common share on the date the options were granted.
- (23) None of the Current Distributing Options had a readily ascertainable fair market value, within the meaning of Treas. Reg. §1.83-7(b), at the time such options were granted. Each outstanding Current Distributing Option satisfies the requirements for "qualified performance-based compensation," as defined in Treas. Reg. §1.162-27(e).
- (24) Neither Distributing 1 nor Controlled 1 is a foreign corporation.
- (25) Neither Distributing 1 nor Controlled 1 will have been a United States real property holding corporation (USRPHC) as defined in §897(c)(2) at any time during the 5-year period ending on the date of the External Spin-off, and neither will be a USRPHC immediately after the External Spin-off.

With respect to the Internal Spin-Off, the taxpayer has made the following representations:

- (1) The fair market value of the Controlled 2 stock to be received by Distributing 1, S4 and S14 will be approximately equal to the fair market value of the Distributing 2 common shares surrendered by Distributing 1, S4 and S14 in the exchange.
- (2) No part of the consideration to be distributed by Distributing 2 in the Internal Spin-Off will be received by a shareholder as a creditor, employee, or in any capacity other than that of a shareholder of Distributing 2.
- (3) Immediately after the Internal Spin-Off, the gross assets of the active business of Controlled 2 will have a fair market value that is at least five percent of the total fair market value of the gross assets of Controlled 2.

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- (4) The 5 years of financial information submitted on behalf of Controlled 2 is representative of the corporation's present Business C operations, but does not include the expansion into Business B and Business A by F12 resulting from the Date 1 merger into F12 of MergedCo 1 and MergedCo 2.
- (5) Immediately after the Internal Spin-Off, at least 90 percent of the fair market value of the gross assets of Distributing 2 will consist of the stock of F7 and F9, controlled corporations that are engaged in the active conduct of a trade or business as defined in §355(b)(2).
- (6) Immediately after the Internal Spin-Off, the gross assets of the active business of F7 will have a fair market value that is at least five percent of the total fair market value of the gross assets of F7.
- (7) Immediately after the Internal Spin-Off, the gross assets of the active business of F9 will have a fair market value that is at least five percent of the total fair market value of the gross assets of F9.
- (8) The 5 years of financial information submitted on behalf of F7 and F9 is representative of their present operations, and there have been no substantial operational changes since the date of the last financial statements submitted.
- (9) Following the Internal Spin-Off, Distributing 2 (through F7 and F9) and Controlled 2 will each continue the active conduct of its business, independently and with its separate employees.
- (10) The business purpose for the Internal Spin-Off is to facilitate the External Spin-Off.
- (11) There is no plan or intention by Distributing 1, S4 or S14 to sell, transfer by gift, or otherwise dispose of any stock in, or securities of, either Distributing 2 or Controlled 2, except as described in the Facilitating Transactions.
- (12) There is no plan or intention by either Distributing 2 or Controlled 2, directly or through any subsidiary corporation, to purchase any of its outstanding stock after the Internal Spin-Off.
- (13) There is no plan or intention to liquidate either Distributing 2 or Controlled 2, to merge either Distributing 2 or Controlled 2 with any other corporation, or to sell or otherwise dispose of the assets of either Distributing 2 or Controlled 2 after the Internal Spin-Off, except in the ordinary course of business or as described in the Facilitating Transactions.
- (14) The total adjusted basis and the fair market value of the assets deemed transferred to Controlled 2 by Distributing 2 each equals or exceeds the sum of

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the liabilities deemed assumed by Controlled 2 plus any liabilities to which the transferred assets are subject.

- (15) The liabilities deemed assumed in the Internal Spin-Off and the liabilities to which the transferred assets are subject were incurred in the ordinary course of business and are associated with the assets being transferred.
- (16) Distributing 2 neither accumulated its receivables nor made extraordinary payments of its payables in anticipation of the transaction.
- (17) Payments made in connection with all continuing transactions, if any, between Distributing 2 and Controlled 2 will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.
- (18) No two parties to the Internal Spin-Off are investment companies as defined in §368(a)(2)(F)(iii) and (iv).
- (19) The Internal Spin-Off 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 2 or Controlled 2, or stock possessing 50 percent or more of the total value of all classes of stock of either Distributing 2 or Controlled 2.
- (20) Each of Distributing 2, Controlled 2, F1, F2, F3, F4, F5, F6, F7, F9, and F11 is a foreign corporation within the meaning of §7701(a) of the Code.
- (21) None of the foreign entities, Distributing 2, Controlled 2, F1, F2, F3, F4, F5, F6, F7, F9, or F11 was a PFIC, as defined in §1297(a), immediately before or after the External Spin-off.
- (22) Distributing 2, Controlled 2, F1, F2, F3, F4, F5, F6, F7, F9, and F11 were each a controlled foreign corporation, as defined in §957(a), before and immediately after the Internal Spin-off.
- (23) F8, F10, and F12 are each treated for United States federal income tax purposes as a disregarded entity pursuant to an election made under Treasury Regulation §301.7701-3(c).

## RULINGS

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

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Contribution

- (a) The Contribution followed by the External Spin-Off, will be a reorganization within the meaning of §368(a)(1)(D). Distributing 1 and Controlled 1 will each be a “party to the reorganization” within the meaning of §368(b).
- (b) No gain or loss will be recognized by Distributing 1 on the transfer of the stock of the Business C Entities to Controlled 1 or on the assumption by Controlled 1 of liabilities of Distributing 1. Sections 361(a) and 357(a).
- (c) No gain or loss will be recognized by Controlled 1 on the receipt of the stock of the Business C Entities from Distributing 1. Section 1032(a).
- (d) Controlled 1’s basis in the stock of each Business C Entity received from Distributing 1 will equal the basis of the stock of the respective Business C Entity in the hands of Distributing 1 immediately before the contribution of such stock to Controlled 1. Section 362(b).
- (e) The holding period of the stock of each respective Business C Entity transferred to Controlled 1 by Distributing 1 will include the period during which Distributing 1 held the respective stock. Section 1223(2).

External Spin-Off

- (f) No gain or loss will be recognized by Distributing 1 or Controlled 1 on the distribution of all the Controlled 1 common shares held by Distributing 1 immediately prior to the External Spin-Off to the holders of Distributing 1 common shares. Section 361(c).
- (g) No gain or loss will be recognized by and no amount will be included in the income of the holders of Distributing 1 common shares upon receipt of the Controlled 1 common shares. Section 355(a)(1).
- (h) The aggregate tax basis of the Distributing 1 common shares and Controlled 1 common shares in the hands of the holders of Distributing 1 common shares will be the same as the aggregate tax basis of the Distributing 1 common shares held by such holders immediately before the External Spin-Off allocated in proportion to the fair market value of each. Section 358(a)(1) and (b); Treas. Reg. §1.358-2(a).
- (i) Assuming that the Distributing 1 common shares held by the Distributing 1 common shareholders are capital assets in the hands of such shareholders, the holding period of the Controlled 1 common shares received by the Distributing 1 shareholders will include their holding period for the Distributing 1 common

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shares. Section 1223(1).

- (j) If cash is received by a Distributing 1 shareholder in lieu of a fractional share interest in Controlled 1, such cash will be treated as if the fractional share of Controlled 1 were received by such Distributing 1 common shareholder and then redeemed by Controlled 1. Such cash will be treated as having been received as a distribution in full payment for stock redeemed as provided in §302(a).
- (k) As provided in §312(h), proper allocations of earnings and profits will be made pursuant to Treas. Reg. §1.312-10(a) and Treas. Reg. §1.1502-33(c). Section 312(h).
- (l) No amount will be included in the gross income of the Specified Shareholders upon the receipt of additional Distributing 1 common shares. Section 305(a).
- (m) The basis of the Distributing 1 common shares held by each Specified Shareholder immediately after the External Spin-Off will equal the basis of the Distributing 1 common shares held before the External Spin-Off, allocated between the Distributing 1 common shares held before the External Spin-Off and the Distributing 1 common shares received in the External Spin-Off in proportion to the fair market value of each. Section 307(a); Treas. Reg. §1.307-1(a).
- (n) The holding period of the Distributing 1 common shares received by each Specified Shareholder in the External Spin-Off will include the period during which such Specified Shareholder held the Distributing 1 common shares on which the Distributing 1 common shares will be distributed. Section 1223(5).

#### Internal Spin-Off

- (o) For federal income tax purposes, the circular flow of notes from Distributing 1, S4, and S14 first to Controlled 2, then to Distributing 2, and finally back to Distributing 1, S4 and S14 will be ignored. The proposed transaction will be treated as if Distributing 2 had created Controlled 2 as a wholly-owned subsidiary, transferred the Contributed A Assets to Controlled 2 in exchange for the stock of Controlled 2, then distributed stock of Controlled 2 to S4 and S14 in exchange for S4's and S14's respective interests in Distributing 2 stock and finally distributed any remaining stock of Controlled 2 to Distributing 1.
- (p) The transfer of the Contributed A Assets to Controlled 2 followed by the distribution of the stock of Controlled 2 will be a reorganization within the meaning of §368(a)(1)(D). Distributing 2 and Controlled 2 will each be a "party to the reorganization" within the meaning of §368(b).
- (q) No gain or loss will be recognized by Distributing 2 on the transfer of the Contributed A Assets to Controlled 2 in exchange for Controlled 2 stock or the

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- assumption by Controlled 2 of Distributing 2's liabilities. Sections 361(a) and 357(a).
- (r) No gain or loss will be recognized to Controlled 2 on its receipt of the Contributed A Assets in exchange for shares of Controlled 2 stock. Section 1032.
  - (s) Controlled 2's basis in the Contributed A Assets received from Distributing 2 will equal the basis of the Contributed A Assets in the hands of Distributing 2 immediately before the transfer of such Contributed A Assets to Controlled 2. Section 362(b).
  - (t) The holding period of the Contributed A Assets transferred by Distributing 2 to Controlled 2 will include the period during which Distributing 2 held the Contributed A Assets. Section 1223(2).
  - (u) No gain or loss will be recognized by Distributing 2 on the distribution of all of the Controlled 2 stock to Distributing 1, S4 and S14. Section 361(c).
  - (v) No gain or loss will be recognized by and no amount will be included in the income of Distributing 1, S4 or S14 upon their receipt of Controlled 2 stock. Section 355(a)(1).
  - (w) The aggregate tax basis of the Distributing 2 stock and the Controlled 2 stock in the hands of Distributing 1 will be equal to the aggregate tax basis of the Distributing 2 stock held by Distributing 1 immediately before the Internal Spin-Off, allocated in proportion to the fair market value of each. The tax basis of the Controlled 2 stock in the hands of S4 and S14 will be equal to the basis of the Distributing 2 stock surrendered in exchange therefor. Section 358(a)(1) and (b); Treas. Reg. §1.358-2(a).
  - (x) Assuming that the Distributing 2 stock held by Distributing 1, S4 and S14 is a capital asset in their hands, the holding period of the Controlled 2 stock received by Distributing 1, S4 and S14 will include their holding period for the Distributing 2 stock. Section 1223(1).
  - (y) As provided in §312(h), following distribution of the stock of Controlled 2, proper allocation of earnings and profits will be made between Distributing 2 and Controlled 2 in accordance with Treas. Reg. §1.312-10(a).

#### Treatment of Stock Options and Other Stock-Based Employee Benefits

- (z) The holders of Current Distributing Options will not realize any income upon the receipt of Adjusted Distributing Options and Controlled 1 Options pursuant to the External Spin-Off. Section 83.

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- (aa) Amounts includible in the gross income of an optionee upon the exercise of a nonqualified Adjusted Distributing Option or a nonqualified Controlled 1 Option or upon the disqualifying disposition of stock acquired under an Adjusted Distributing ISO or a Controlled 1 ISO will be deductible by the corporation that is the optionee's employer at the time of exercise (or was the more recent employer in the case of an optionee whose employment terminated prior to such exercise) assuming the optionee was employed by that corporation since the date the options were granted to the optionee. No opinion is expressed concerning situations where the optionee was not employed by the same corporation since the date the options were granted to the optionee. Section 83(h).
- (bb) Distributing 1 will not recognize any gain or loss upon the transfer of Controlled 1 common shares to an employee of Distributing 1 who exercises a Controlled 1 Option, and Controlled 1 will not recognize any gain or loss upon the transfer of Distributing 1 common shares to an employee of Controlled 1 who exercises an Adjusted Distributing Option. Sections 83 and 1032; Rev. Rul. 2002-1, 2002-2 I.R.B. 268.
- (cc) Neither the adjustment of Current Distributing Options to constitute Adjusted Distributing Options nor the substitution of Controlled 1 Options for Current Distributing Options pursuant to the External Spin-Off will cause any such options to fail to satisfy the performance goal requirements of §162(m) and Treas. Reg. §1.162-27(e)(2). Section 162(m).
- (dd) Neither the adjustment of Current Distributing Options intended to qualify as incentive stock options to constitute Adjusted Distributing ISOs nor the substitution of Controlled 1 ISOs for Current Distributing Options intended to qualify as incentive stock options pursuant to the External Spin-Off will constitute a modification, extension or renewal of these incentive stock options within the meaning of §424(h)(3) of the Code and therefore will not constitute the grant of new options. Section 424(h)(3).
- (ee) Amounts includible in the gross income of a holder of Outstanding Distributing Restricted Stock or Controlled 1 Restricted Stock upon the vesting of such restricted stock (if an election under §83(b) was not timely made with respect to the grant of such restricted stock) will be deductible by the corporation that is the holder's employer at such time (or was the more recent employer in the case of a holder whose employment terminated prior to such time) assuming the employee was employed by such corporation since the date the stock was granted. No opinion is expressed concerning situations where the holder of option was not employed by the same corporation from the date of grant. Section 83(h).
- (ff) The discount at which an employee purchased a Distributing 1 common share

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under Plan O prior to the External Spin-Off will be allocated between such Distributing 1 common share and the number of Controlled 1 common shares received pursuant to the External Spin-Off with respect to such Distributing 1 common share in the same proportion as the basis of such Distributing 1 common share prior to the External Spin-Off is allocated between the Distributing 1 common share and the number of Controlled 1 common shares received pursuant to the External Spin-Off with respect to a Distributing 1 common share. Section 423.

- (gg) Amounts includible in the gross income of an employee or former employee of Distributing 1 or Controlled 1 after the External Spin-Off upon the disqualifying disposition of a Distributing 1 common share acquired under Plan O prior to the External Spin-Off or a Controlled 1 common stock received pursuant to the External Spin-Off with respect to a Distributing 1 common share acquired under Plan O prior to the External Spin-Off will be deductible by the corporation that is the employer or former employee's employer at the time of the disqualifying disposition (or was the most recent employer in the case of a holder whose employment terminated prior to such time) assuming the employee was employed by such corporation since the date the stock was granted. No opinion is expressed concerning situations where the holder of option was not employed by the same corporation from the date of the grant. Sections 421 and 423.
- (hh) Distributing 1 will not recognize any gain or loss upon the transfer of Controlled 1 common shares after the External Spin-Off to an employee of Distributing 1 who is entitled to receive such shares under a Distributing Deferred Compensation Plan, and Controlled 1 will not recognize any gain or loss upon the transfer of Distributing 1 common shares after the External Spin-Off to an employee of Controlled 1 who is entitled to receive such shares under a Controlled 1 Deferred Compensation Plan. Sections 83 and 1032; Rev. Rul. 2002-1, 2002-2 I.R.B. 268.
- (ii) Amounts includible in the gross income of an employee or former employee of Distributing 1 or Controlled 1 after the External Spin-Off upon the receipt of Distributing 1 common shares and/or Controlled 1 common shares under a Distributing Deferred Compensation Plan or a Controlled 1 Deferred Compensation Plan will be deductible by the corporation that is the employee's employer in the taxable year in which an amount attributable to such contribution is includible in income as compensation. Section 83(h).

Except as specifically ruled above, no opinion is expressed regarding the transaction under any other provision of the Code. Specifically, we express no opinion regarding the following:

- (i) The tax consequences of the Facilitating Transactions;

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- (ii) The qualification of the incentive stock options under §422 of the Code;
- (iii) The qualification of the employee stock purchase plan under §423 of the Code;
- (iv) Whether the Controlled 1 Options issued to employees of Distributing 1 meet the requirements of §162(m)(4)(C).
- (v) No opinions have been requested and none are provided about the federal income tax consequences of Taxpayer's proposed foreign restructuring transactions. In particular, no opinion is expressed about the application of Code §367(b) (i.e. Treas. Reg. §1.367(b)-5(d)) to the Internal Spin-off or the application of Code §1248.
- (vi) No opinion is expressed about the effectiveness of the election by Holdco or by any other foreign entity under Treas. Reg. §301.7701-3 to be treated as a disregarded entity.
- (vii) Whether any or all of the above-referenced foreign corporations are passive foreign investment companies (within the meaning of §1297(a)). If it is determined that any or all of the above-described foreign corporations are passive foreign investment companies, no opinion is expressed with respect to the application of Code §§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 any other provision of the Code.
- (viii) The rulings contained in this letter are predicated upon the facts and representations submitted by the taxpayer and accompanied by a penalties of perjury statement 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. See §12.04 of Rev. Proc. 2000-1, 2000-1 I.R.B. 4, which discusses in greater detail the revocation or modification of ruling letters. However, when the criteria in §12.05 of Rev. Proc. 2000-1 are satisfied, a ruling is not revoked or modified retroactively except in rare or unusual circumstances.

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.

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A copy of this letter must be attached to any income tax return to which it is relevant.

Sincerely,

Lisa A. Fuller  
Assistant to the Chief  
CC:CORP:1