

Internal Revenue Service

Department of the Treasury

Number: **200345007**

Washington, DC 20224

Release Date: 11/07/2003

Index Numbers: 708.00-00; 721.00-00;
722.00-00; 1223.00-00;
7704.00-00

Person to Contact:

Telephone Number:

Refer Reply To:

CC:PSI:B01 - PLR-113113-03

Date:

August 7 2003

In Re:

Legend:

X =

State =

A Unit =

B Unit =

C Unit =

D Unit =

E Unit =

a =

b =

D1 =

Dear :

This responds to your letter dated February 20, 2003, requesting rulings concerning the creation of new membership interest units in X and the conversion of the existing membership interest units into the newly created membership interest units.

Facts

According to the representations made, X is a State LLC taxed as a partnership for Federal tax purposes. X began operations on D1. X has more than a members. There are currently b shares of A Units outstanding.

X intends to (1) designate A Unit as B Unit, (2) create C Unit, D Unit, and E Unit, each of which has different rights, preferences, privileges, and restrictions from one another and (3) allow its members to convert, on a one-to-one basis, (i) B Units into C Units, D Units, or E Units, (ii) C Units into E Units, (iii) D Units into C Units or E Units, and (iv) E Units into C Units.

The following has been further represented. X is not a publicly traded partnership as defined under § 7704 of the Internal Revenue Code. Each member's proportionate share in X's capital will remain the same after the planned conversion of the membership interests. The conversion will not change each member's proportionate share of X's liabilities.

X has requested the following rulings.

(1) No gain or loss is recognized by the members of X as a result of the designation of A Units as B Units, the conversion of B Units into C Units, D Units, or E Units, the conversion of C Units into E Units, the conversion of D Units into C Units or E Units, and the conversion of E Units into C Units.

(2) No termination of X occurs under § 708, regardless whether more than 50 percent of the membership interests are converted.

(3) No gain or loss is recognized by any converting members.

(4) The adjusted basis of a converting member is not affected by the conversion.

(5) There is no change in a converting member's holding period for the member's membership interest under § 1223(1).

(6) The designation of A Units as B Units and the subsequent conversions of units do not constitute an issuance of additional units as described in § 1.7704-1(e)(4)(i) of the Procedure and Administration Regulations.

Law and Analysis

Section 741 provides when a partnership interest is sold or exchanged, the transferor partner recognizes gain or loss.

Under § 1001, if there is a sale or other disposition of property, the entire amount of the gain or loss realized thereunder will be recognized, unless another section of subtitle A provides for nonrecognition.

Under § 721, no gain or loss is recognized by a partnership or any of its partners upon the contribution of property to the partnership in exchange for an interest therein.

Section 708 provides that a partnership continues if it is not terminated. A partnership terminates only if (1) no part of any business, financial operation, or venture of the partnership continues to be carried on by any of its partners in a partnership, or (2) within a 12-month period there is a sale or exchange of 50 percent or more of the total interest in partnership capital and profits.

Section 722 generally provides that the basis of an interest in a partnership acquired by a contribution of property equals the transferor partner's adjusted basis in the contributed property.

Section 1223(1) provides that the holding period of property received in exchange for other property includes that holding period of the property exchanged, if the property received has the same basis (in whole or in part) as the property exchanged.

Under § 731, if a partnership distributes money to a partner, than that partner will generally recognize gain only to the extent that the amount of money distributed (or deemed distributed) exceeds the adjusted basis of the partner's interest in the partnership immediately before the distribution.

Under § 733, if there is a distribution by a partnership to a partner and if there is no liquidation of that partner's interest, then the adjusted basis of that partner's interest in the partnership must be reduced (but not below zero) by the amount of money distributed to the partner.

Section 752(a) states, in part, that any increase in a partner's share of a partnership's liabilities is considered to be a contribution of money by the partner to the partnership.

Section 752(b) states, in part, that any decrease in a partner's share of a partnership's liabilities is considered to be a distribution of money by the partnership to the partner.

Rev. Rul. 84-52, 1984-1 C.B. 158, addressed the circumstance where a general partnership interest was converted into a limited partnership interest in the same partnership. Each partner's total percent ownership interest in the partnership remained the same after the conversion. Rev. Rul. 84-52 holds, in part, that the partnership was not terminated because the conversion was not a sale or exchange for

§ 708 purposes. Rev. Rul. 84-52 also holds that there is no change in the adjusted basis of any partner's interest in the partnership provided that each partner's share of the liabilities remained unchanged. Furthermore, Rev. Rul. 84-52 states that under § 1223(1), there will be no change to the holding period of any partner's total interest in the partnership.

Under § 1.7704-1(e)(1), for purposes of § 7704(b) and § 1.7704-1, transfers pursuant to a closed end redemption plan (as defined in § 1.7704-1(e)(4)) are disregarded in determining whether interests in a partnership are readily tradable on a secondary market or the substantial equivalent thereof.

Section 1.7704-1(e)(4) provides that for purposes of § 1.7704-1(e)(1)(viii), a redemption or repurchase agreement (as defined in § 1.7704-1(e)(3)) is a closed end redemption plan only if – (i) The partnership does not issue any interest after the initial offering (other than the issuance of additional interests prior to August 5, 1988); and (ii) No partner or person related to any partner (within the meaning of § 267(b) or 707(b)(1)) provides contemporaneous opportunities to acquire interests in similar or related partnerships which represent substantially identical investments.

Based on the facts provided and the representations made, we conclude the following.

(1) No gain or loss will be recognized by the members of X as a result of the designation of A Units as B Units, the conversion of B Units into C Units, D Units, or E Units, the conversion of C Units into E Units, the conversion of D Units into C Units or E Units, and the conversion of E Units into C Units, on a one-to-one basis.

(2) No termination of X will occur under § 708, regardless whether more than 50 percent of the existing membership interest units are converted into other newly created membership interest units.

(3) No gain or loss will be recognized by any converting members upon the proposed conversions of their existing membership interest units.

(4) Provided that there will be no change in the members' shares of X's liabilities as a result of the conversions, the adjusted basis of a converting member will not be affected by the conversion.

(5) Pursuant to § 1223(1), there will be no change to the holding period of any member's membership interest in X.

(6) The designation of A Units as B Units and the subsequent conversions of units will not constitute an issuance of additional units as described in § 1.7704-1(e)(4)(i) of the Procedure and Administration Regulations.

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.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) 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 taxpayer.

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.

Sincerely,

David R. Haglund
Senior Technician Reviewer, Branch 1
Office of the Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures:

Copy of this letter

Copy for §6110 purposes