

## Internal Revenue Service

## Department of the Treasury

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Person to Contact:

Telephone Number:

Refer Reply To:

**CC:CORP:BR:06-PLR-165603-01**

Date:

**April 4, 2002**

### LEGEND

Corp 1 =

Corp 2 =

Corp 3 =

State A =

Area 1 =

#a =

#b =

#c =

#d =

#e =

#f =

#g =

Business 1 =

Business 2 =

Business 3 =

Business 4 =

Business 5 =

Business 6 =

a =

b =

c =

d =

e =

f =

g =

h =

i =

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j =

Date 1 =

Date 2 =

Period 1 =

Dear

This letter is in reply to your letters dated November 30, 2001, January 24, 2002, February 1, 2002 and February 15, 2002.

Corp 1, a State A corporation, is a diversified company with many active businesses serving a variety of industries for over #a years. Corp 1 members own more than #b percent of the single class of Corp 1 stock. Tax exempt organizations own the remaining stock.

Corp 1 directly engages in numerous active businesses. Corp 1 has directly engaged in Business 2, Business 3, Business 4, and Business 5 for more than five years. These five-year active businesses directly operated by Corp 1 constitute well in excess of five percent of Corp 1's net and gross assets and will comprise more than five percent after the transaction, described below. Recently, Corp 1 sold Business 1, a directly conducted five-year business. The distribution of the proceeds of the sale of Business 1 is the subject of this ruling request. Corp 1 also engages in businesses that it conducted for less than five years. Within the past five years, Corp 1 acquired all of the stock of Corp 3, a corporation that engages in Business 6.

Before the sale described below, Corp 1 conducted the business associated with Business 1. Corp 1 started Business 1 in Period 1. Business 1 owned and actively managed over #c acres of a properties in Area 1. Business 1 was a separate and active business. It generated income and incurred expenses and it had its own management separate and distinct from Corp 1's other business operations. Also, Business 1 had its own office, equipment, and employees that performed various direct business functions such as: sales management, negotiation of a lease agreements, land security and surveying, management and control of b, and investigation of the purchase/sale of various a properties. For cost efficiency purposes, Corp 1's d sector and corporate offices performed certain administrative functions of Business 1. Business 1 was separately accounted for with its own separate internally prepared financial statements.

On Date 1 (closing date), Corp 1 sold #a percent of Business 1 to Corp 2 an unrelated purchaser. This sale constituted a sale of the e and f of the real estate attributable to Business 1, as well as a sale of g, h, and i. The purchaser also hired the employees of Business 1. The transaction was an "asset sale" for #d in cash. Corp 1 immediately invested the proceeds, on a temporary basis in a segregated account, in order to preserve the funds received.

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Upon receipt of a favorable ruling from the Service, Corp 1's Board of Directors will approve and adopt a plan of partial liquidation providing for the distribution of the net proceeds attributable to the sale of the Business 1. In the same or the next succeeding tax year, pursuant to the plan of partial liquidation, Corp 1 will distribute all of the net proceeds (after expenses and taxes) attributable to Business 1 pro rata to the Corp 1 shareholders (the "Proposed Distribution"). Corp 1 estimates the amount of the Proposed Distribution to be #e.

Corp 1 has not used any of the cash from the sale of the Business 1 in any manner except that Corp 1 has placed the cash in an identified and segregated separate investment custodial account, as managed by a financial adviser. Corp 1 will not distribute any assets representing income earned on this account pursuant to the plan of partial liquidation. No substituted assets will be distributed. There is no plan or intention to completely liquidate Corp 1. As of Date 2, Corp 1 has #f stock options outstanding. These options have been issued to one employee of Corp 1. As of Date 2, #g of these options can be exercised by the employee. None of these options have been exercised by the employee.

The following representations have been made in connection with the proposed transaction.

- (a) Throughout the five-year period prior to Date 1, Corp 1 was engaged in many different active businesses serving a variety of industries. Business 1 was a separate active business and a division of Corp 1. Business 1, as well as Corp 1's other businesses which Corp 1 will continue after the Proposed Distribution, will each qualify as a five-year trade or business.
- (b) The sales proceeds to be distributed are proceeds from the sale of business assets that Corp 1 actively used in the Business 1 and are not attributable to an expansion reserve, a mere business decline, or a mere decrease in working capital. None of the sales proceeds are proceeds from the sale of assets that, directly or indirectly, are or were idle, passive or investment assets.
- (c) The Proposed Distribution will be consummated during the taxable year in which the plan of partial liquidation is adopted or in the succeeding taxable year.
- (d) Following the Proposed Distribution, Corp 1 will not retain any portion of the sales proceeds attributable to Business 1.
- (e) All distributions to Corp 1 shareholders in the Proposed Distribution will be made with cash coming solely from the proceeds of the sale of Business 1. Corp 1 has not used any of the cash that it will distribute pursuant to the Proposed Distribution in any manner, except that Corp 1 placed the cash in identified and segregated liquid short-term investments. Corp 1

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will not distribute any assets representing income earned on these accounts pursuant to the Proposed Distribution. Corp 1 has not used any of the proceeds from the sale of Business 1 in any of its remaining business activities. Corp 1 will not distribute any substituted assets.

- (f) Corp 1 will distribute proceeds pro rata to the Corp 1 shareholders. Although Corp 1 shareholders will not surrender any Corp 1 shares in the proposed Distribution, each shareholder will compute gain or loss on a deemed redemption under the principles set forth in Rev. Rul. 77-245, 1977-2, C.B. 105.
- (g) There are no declared but unpaid dividends on the stock to be redeemed by Corp 1.
- (h) There is no plan or intention to completely liquidate Corp 1.
- (i) Corp 1 has no plan or intention to reenter Business 1 or to expand its continuing business operations other than through normal internal growth, except that it is actively negotiating the acquisition of companies involved in business activities unrelated to those of Business 1.
- (j) Corp 1 shareholders have no plan or intention to reinvest any of the amount distributed in the Proposed Distribution transaction in Corp 1.
- (k) The Proposed Distribution will not be preceded or followed by the reincorporation or transfer of such cash to a recipient corporation where persons holding more than 20 percent in value of the stock of Corp 1 also hold more than 20 percent in value of the stock of the recipient corporation. For purposes of this representation, ownership will be determined by application of the constructive ownership rules of section 318 of the Code as modified by section 304(c)(3).
- (l) None of the amounts distributed by Corp 1 in the Proposed Distribution will be received by a Corp 1 shareholder as a debtor, creditor, employee, or in some capacity other than that of a Corp 1 shareholder.
- (m) Corp 1 will adjust the terms of its outstanding options to eliminate the dilutive effect on the value of these options caused by distributing assets in a partial liquidation without actually redeeming shares of Corp 1 stock.

Based solely on the information submitted and on the representations set fourth above, we hold as follows:

- (a) The distribution of the net proceeds from the sale of Business 1 will be treated as a distribution in partial liquidation under section 302(e)(1) of the Code provided such distribution is made in the taxable year in which the

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plan is adopted or in the next succeeding year. Section 1.346-1(a)(2) of the Income Tax Regulations.

- (b) The maximum amount considered to be distributed in the partial liquidation with respect to the sale of Business 1 equals the sales proceeds received by Corp 1 relating to Business 1, reduced by all the liabilities (including taxes and expenses) of Corp 1 incurred in connection with the sale and the Proposed Distribution. This amount will not include any earned or accrued investment earnings on the sales proceeds. See Rev. Rul. 60-232, 1960-2 C.B. 115; Rev. Rul. 71-250, 1971-1 C.B. 112; Rev. Rul. 76-279, 1976-2 C.B. 99; Rev. Rul. 76-289, 1976-2 C.B. 100.
- (c) If the amount distributed to the Corp 1 shareholders in the proposed transaction exceeds the maximum amount considered distributed in the partial liquidation (see ruling b above), each shareholder of Corp 1 or each person considered to hold Corp 1 stock under section 302(e)(5), as relevant, will be treated as receiving the same ratio of that maximum amount and any excess. Such excess distribution will be treated as a distribution of property under section 301(c)(1) and section 316.
- (d) In the case of non-corporate shareholders, distributions made pursuant to the plan of partial liquidation to the extent indicated in ruling (b) above will be treated as is in full payment for the stock constructively redeemed. Section 302(a). Such shareholders will recognize gain or loss to the extent of the difference between the amount distributed in partial liquidation and the adjusted basis of the shares deemed surrendered, as provided in ruling (e) below, in exchange therefore. Provided that the stock is a capital asset in the hands of the exchanging shareholder and that section 341(a) (relating to collapsible corporations) is not applicable, gain or loss, if any, will be considered capital gain or loss subject to the provisions and limitations of subchapter P of Chapter 1 of the Code.
- (e) For purposes of Rulings (a) and (d) above, the number of shares that will be considered to have been redeemed regardless of the number of shares actually surrendered for the purposes of determining gain or loss will be determined in accordance with the principles set forth in Rev. Rul. 77-245, 1977-2, C.B. 105. To the extent that the fair market value of the distributions in partial liquidation received by a shareholder exceeds the fair market value of the Corp 1 stock deemed surrendered in exchange therefor, the additional shares considered redeemed pursuant to Rev. Rul. 77-245 will be determined in accordance with the principles set forth in Rev. Rul. 68-348, 1968-2, C.B. 141 and Rev. Rul. 85-48, 85-1 C.B. 126.
- (f) Corp 1 will recognize no gain or loss on the distribution of cash in partial liquidation. Section 311(a).

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No opinion is expressed about the tax treatment of the proposed transaction under other provisions of the Code and regulations or about the tax treatment of any conditions existing at the time of, or effects resulting from, the proposed transaction that are not directly covered by the above rulings.

This ruling letter is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent. A copy of this letter should be attached to the federal income tax returns of the taxpayers involved for the taxable year in which the transaction covered by this ruling letter is consummated.

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

Sincerely yours  
Steven Hankin  
Senior Technician Reviewer, Branch 6  
Office of Associate Chief Counsel  
(Corporate)