

Internal Revenue Service

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Person To Contact: _____ , ID No.

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Refer Reply To:
CC:CORP:B03
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Date:
September 26, 2007

Distributing 1 =

Distributing 2 =

Controlled =

State X =

Business A =

Business B =

y =

Product =

Entity =

Guarantees =

Transition Services
Agreement =

Dear

We respond to your representative's letter dated May 25, 2007, requesting rulings as to the Federal income tax consequences of a proposed transaction. Additional information was submitted in letters dated June 7, June 14, June 18, June 21, July 12, July 19, August 10, August 29, September 10, September 12, September 19, and September 25, 2007. The information submitted is summarized below.

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. This Office has not verified any of the material submitted in support of the request for rulings. Verification of the information, representations, and other data may be required as part of the audit process. In particular, this Office has not reviewed any information pertaining to, and has made no determination regarding, whether the Internal Distribution or the External Distribution (each described below): (i) satisfies the business purpose requirement of § 1.355-2(b) of the Income Tax Regulations; (ii) is used principally as a device for the distribution of the earnings and profits of the distributing corporation or the controlled corporation or both (see § 355(a)(1)(B) of the Internal Revenue Code and § 1.355-2(d)); and (iii) is part of a plan (or series of related transactions) pursuant to which one or more persons will

acquire directly or indirectly stock representing a 50-percent or greater interest in the distributing corporation or the controlled corporation (see § 355(e) and § 1.355-7).

STATEMENT OF FACTS

Distributing 1, a State X corporation, is the common parent of an affiliated group of corporations that files a consolidated Federal income tax return. Distributing 1 has one class of stock outstanding which is widely held and publicly traded. Distributing 1 is indirectly engaged through its subsidiaries in Business A and Business B. Distributing 2, a State X corporation, is a wholly owned subsidiary of Distributing 1. Controlled, a State X corporation, is a wholly owned subsidiary of Distributing 2. Controlled was formed to effectuate the proposed transaction.

Distributing 1 has determined that the management and regulatory requirements of Business B's operations are substantially different from those of Business A. Accordingly, Distributing 1 has determined that the proposed transaction is necessary to allow Distributing 1 to focus on its core strategies and grow Business A, while permitting Business B to focus on its own growth in a separate publicly traded corporation.

The information provided indicates that Business A and Business B each has had gross receipts and operating expenses representing the active conduct of a trade or business for each of the five years preceding the proposed transaction.

PROPOSED TRANSACTION

The taxpayer proposes the following transaction (the "Proposed Transaction"):

- (i) Distributing 2 will contribute Business B to Controlled solely in exchange for Controlled stock (the "Contribution"). Entity, a limited liability company wholly owned by Distributing 2, invoices many of the third party customers of Business B. Certain intercompany receivables (the "Receivables") representing amounts invoiced by Entity to customers will not be settled as of the date of the Proposed Transaction. The Receivables will be reclassified as third party trade receivables and retained by Controlled. As amounts are collected from customers, Entity will transfer these amounts to Controlled in satisfaction of the Receivables.
- (ii) Distributing 2 will distribute all of the stock of Controlled to Distributing 1 (the "Internal Distribution").
- (iii) Distributing 1 will distribute all of the stock of Controlled to its shareholders on a pro-rata basis (the "External Distribution").

Distributing 2 will retain certain healthcare liabilities in the amount of \$y which relate to retired employees who have worked for Business B.

Distributing 1 and the Business B entities will work together to secure the release of existing cross-guarantees (the "Guarantees"). To the extent that they are unable to secure a release of one or more of the Guarantees, Distributing 1 or Controlled, as appropriate, will continue to be a guarantor. However, Distributing 1 and Controlled each agree to satisfy its respective primary obligations, and do not expect that either entity will be called upon to satisfy any obligation in its guarantor capacity.

Distributing 1 and Controlled will agree to continue certain transitional arrangements and practices for a limited period of time following the Proposed Transaction. These agreements include a Transition Services Agreement under which the Distributing 1 group will provide certain administrative and other services to Controlled for a period of no longer than 12 months. Controlled will pay fair market rates for these services.

The Distributing 1 group currently purchases Product from Business B to satisfy its obligations with third party customers under long-term Product supply agreements. The Distributing 1 group will attempt to obtain third-party consents to assign such supply agreements to Controlled. Supply agreements, where consent cannot be obtained, will continue under their existing terms. The Distributing 1 group will continue to invoice the customers under such supply agreements and will remit payment to Controlled upon receipt from the customer.

Under two agreements, the Distributing 1 group sources Product from Controlled properties. Following the Proposed Transaction, Controlled will supply Product to the Distributing 1 group under these agreements at fair market value rates.

REPRESENTATIONS

The following representations have been made regarding the Contribution:

- (a) The total adjusted basis and the fair market value of the assets transferred to Controlled in the Contribution will equal or exceed the sum of (i) the total liabilities assumed (within the meaning of § 357(d)) by Controlled, and (ii) the total amount of any money and the fair market value of any other property (within the meaning of § 361(b)) received by Distributing 2 and transferred to its creditors in connection with the reorganization.
- (b) The liabilities assumed (within the meaning of § 357(d)) by Controlled in the Contribution were incurred in the ordinary course of business and are associated with the assets being transferred.
- (c) The total fair market value of the assets transferred to Controlled in the Contribution will exceed the sum of (i) the amount of any liabilities assumed

(within the meaning of § 357(d)) by Controlled in connection with the exchange, (ii) the amount of any liabilities owed to Controlled by Distributing 2 that are discharged or extinguished in connection with the exchange, and (iii) the amount of any cash and the fair market value of any other property (other than stock and securities permitted to be received under § 361(a) without the recognition of gain) received by Distributing 2 in connection with the exchange. The fair market value of the assets of Controlled will exceed the amount of its liabilities immediately after the exchange.

- (d) The aggregate fair market value of the assets transferred to Controlled in the Contribution will equal or exceed the aggregate adjusted basis of these assets.

The following representations have been made regarding the Internal Distribution:

- (e) No part of the stock to be distributed by Distributing 2 in the Internal Distribution will be received by Distributing 1 as a creditor, employee, or in any capacity other than that of a shareholder of Distributing 2.
- (f) With respect to the Internal Distribution, the five years of financial information submitted on behalf of Distributing 2 regarding Business A (conducted primarily through limited liability companies classified as disregarded entities for Federal tax purposes) is representative of the present operations of such business, and there have been no substantial operational changes since the date of the last financial statements submitted.
- (g) With respect to the Internal Distribution, the five years of financial information submitted on behalf of Controlled regarding Business B (conducted primarily through limited liability companies classified as disregarded entities for Federal tax purposes) is representative of the present operations of such business, and there have been no substantial operational changes since the date of the last financial statements submitted.
- (h) Following the Internal Distribution, the Distributing 2 and Controlled will each continue the active conduct of its respective business, independently and with its respective employees.
- (i) The Internal Distribution is being carried out to facilitate the External Distribution. The Distribution of the stock and securities of Controlled is motivated, in whole or substantial part, by this corporate business purpose.
- (j) There is no plan or intention to liquidate Distributing 2 or Controlled, to merge either corporation with any other corporation, or to sell or otherwise dispose of the assets of either corporation after the Internal Distribution, except in the ordinary course of business.

- (k) The Internal Distribution is not being used principally as a device for the distribution of the earnings and profits of Distributing 2, Controlled, or both.
- (l) For purposes of § 355(d), immediately after the Internal Distribution, no person (determined after applying § 355(d)(7)) will hold stock possessing 50 percent or more of the total combined voting power of all classes of Distributing 2 stock entitled to vote, or 50 percent or more of the total value of shares of all classes of Distributing 2 stock, that was acquired by purchase (as defined in § 355(d)(5) and (8)) during the five-year period (determined after applying § 355(d)(6)) ending on the date of the Internal Distribution.
- (m) For purposes of § 355(d), immediately after the Internal Distribution, no person (determined after applying § 355(d)(7)) will hold stock possessing 50 percent or more of the total combined voting power of all classes of Controlled stock entitled to vote, or 50 percent or more of the total value of shares of all classes of Controlled stock, that was either (i) acquired by purchase (as defined in § 355(d)(5) and (8)) during the five-year period (determined after applying § 355(d)(6)) ending on the date of the Internal Distribution or (ii) attributable to distributions on Distributing 2 stock or securities that were acquired by purchase (as defined in § 355(d)(5) and (8)) during the five-year period (determined after applying § 355(d)(6)) ending on the date of the Internal Distribution.
- (n) No two parties to the Internal Distribution are investment companies as defined in § 368(a)(2)(F)(iii) and (iv).
- (o) The Internal Distribution is not part of a plan or series of related transactions (within the meaning of § 1.355-7) pursuant to which one or more persons will acquire directly or indirectly stock representing a 50-percent or greater interest (within the meaning of § 355(d)(4)) in Distributing 2 or Controlled (including any predecessor or successor of either corporation).
- (p) At the time of the Internal Distribution, no member of the Distributing 1 group will have an excess loss account in the Controlled stock or in the stock of any Controlled subsidiary.
- (q) The allocation of basis under § 358 that will occur in connection with the Internal Distribution will not result in the Controlled stock having a higher basis than it had immediately before the Internal Distribution.

The following representations have been made regarding the External Distribution:

- (r) Except for the Receivables, no intercorporate debt will exist between Distributing 1 (and its affiliates) and Controlled (and its affiliates) at the time of, or subsequent to, the External Distribution.
- (s) No part of the stock to be distributed by Distributing 1 in the External Distribution will be received by a Distributing 1 shareholder as a creditor, employee, or in any capacity other than that of a shareholder of Distributing 1.
- (t) With respect to the External Distribution, the five years of financial information submitted on behalf of Distributing 2 (a member of the Distributing 1 SAG) regarding Business A is representative of the present operations of the business, and there have been no substantial operational changes since the date of the last financial statements submitted. Distributing 2 is, and immediately after the External Distribution will be, affiliated with Distributing 1 within the meaning of § 1504(a), without regard to § 1504(b).
- (u) With respect to the External Distribution, the five years of financial information submitted on behalf of Controlled regarding Business B (conducted primarily through limited liability companies classified as disregarded entities for Federal tax purposes) is representative of the present operations of such business, and there have been no substantial operational changes since the date of the last financial statements submitted.
- (v) Following the External Distribution, the Distributing 1 SAG and Controlled will each continue the active conduct of its respective business, independently and with its respective employees.
- (w) The External Distribution is being carried out for the following corporate business purpose: to allow Distributing 1 and Controlled to each focus on its own core business. The Distribution of the stock and securities of Controlled is motivated, in whole or substantial part, by this corporate business purposes.
- (x) There is no plan or intention to liquidate Distributing 1 or Controlled, to merge either corporation with any other corporation, or to sell or otherwise dispose of the assets of either corporation after the External Distribution, except in the ordinary course of business.
- (y) The External Distribution is not being used principally as a device for the distribution of the earnings and profits of Distributing 1, Controlled, or both.
- (z) For purposes of § 355(d), immediately after the External Distribution, no person (determined after applying § 355(d)(7)) will hold stock possessing 50 percent or more of the total combined voting power of all classes of Distributing 1 stock entitled to vote, or 50 percent or more of the total value of shares of all

classes of Distributing 1 stock, that was acquired by purchase (as defined in § 355(d)(5) and (8)) during the five-year period (determined after applying § 355(d)(6)) ending on the date of the External Distribution.

- (aa) For purposes of § 355(d), immediately after the External Distribution, no person (determined after applying § 355(d)(7)) will hold stock possessing 50 percent or more of the total combined voting power of all classes of Controlled stock entitled to vote, or 50 percent or more of the total value of shares of all classes of Controlled stock, that was either (i) acquired by purchase (as defined in § 355(d)(5) and (8)) during the five-year period (determined after applying § 355(d)(6)) ending on the date of the External Distribution or (ii) attributable to distributions on Distributing 1 stock or securities that were acquired by purchase (as defined in § 355(d)(5) and (8)) during the five-year period (determined after applying § 355(d)(6)) ending on the date of the External Distribution.
- (bb) Payments made in connection with all continuing transactions, if any, between Distributing 1 (and its affiliates) and Controlled (and its affiliates), will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.
- (cc) No two parties to the External Distribution are investment companies as defined in § 368(a)(2)(F)(iii) and (iv).
- (dd) Neither Distributing 1 nor Controlled will be a disqualified investment corporation (within the meaning of § 355(g)(2)).
- (ee) The External Distribution is not part of a plan or series of related transactions (within the meaning of § 1.355-7) pursuant to which one or more persons will acquire directly or indirectly stock representing a 50-percent or greater interest (within the meaning of § 355(d)(4)) in Distributing 1 or Controlled (including any predecessor or successor of either corporation).
- (ff) Immediately before the External Distribution, items of income, gain, loss, deduction, and credit will be taken into account as required by the applicable intercompany transaction regulations. Any excess loss account in the Controlled stock (or a member may have in the stock of another member that is required to be taken into account by § 1.1502-19) will be included in income immediately before the External Distribution to the extent required by regulations (see § 1.1502-19).
- (gg) The payment of cash in lieu of fractional shares, if any, of Controlled stock will be solely for the purpose of avoiding the expense and inconvenience of issuing and maintaining fractional shares and will not represent separately

bargained for consideration. The total cash consideration that will be paid in connection with the External Distribution in lieu of fractional shares of Controlled stock is not intended to exceed one percent of the total consideration that will be distributed to holders of Distributing 1 stock in the Distribution. Any fractional share interests will be aggregated, and it is intended that no Distributing 1 shareholder will receive cash in lieu of fractional shares in an amount equal to or greater than the value of one full share of Controlled.

RULINGS

Based solely on the information submitted and representations made, we rule as follows regarding the Contribution:

- (1) The Contribution, followed by the Internal Distribution, will be a reorganization under § 368(a)(1)(D). Distributing 2 and Controlled will each be “a party to a reorganization” under § 368(b).
- (2) No gain or loss will be recognized by Distributing 2 in the Contribution (§§ 361(a) and 357(a)).
- (3) No gain or loss will be recognized by Controlled in the Contribution (§ 1032(a)).
- (4) Controlled's basis in each asset received from Distributing 2 will equal the basis of that asset in the hands of Distributing 2 immediately before the Contribution (§ 362(b)).
- (5) Controlled's holding period in each asset contributed will include the period during which such asset was held by Distributing 2 (§ 1223(2)).

Based solely on the information submitted and representations made, we rule as follows regarding the Internal Distribution:

- (6) No gain or loss will be recognized by Distributing 2 in the Internal Distribution (§ 361(c)(1)).
- (7) No gain or loss will be recognized by (and no amount will otherwise be included in the income of) Distributing 1 on receipt of the Controlled stock from Distributing 2 in the Internal Distribution (§ 355(a)(1)).
- (8) The aggregate basis of the Controlled stock and Distributing 2 stock in the hands of Distributing 1 will be the same as the aggregate tax basis of the Distributing 2 stock held by Distributing 1 immediately before the Internal Distribution allocated in proportion to the fair market value of each (§ 358(a)(1) and (b) and § 1.358-2(a)(2)).

- (9) Distributing 1's holding period in the Controlled stock received in the Internal Distribution will include the holding period of the stock of Distributing 2 with respect to which the Internal Distribution is made, provided that Distributing 1 held such Distributing 2 stock as a capital asset on the date of the Internal Distribution (§ 1223(1)).
- (10) Distributing 2 and Controlled will allocate their earnings and profits, if any, in accordance with § 312(h) and § 1.312-10(a).

Based solely on the information submitted and representations made, we rule as follows regarding the External Distribution:

- (11) No gain or loss will be recognized by Distributing 1 in the External Distribution (§ 355(c)(1)).
- (12) No gain or loss will be recognized by (and no amount will otherwise be included in the income of) the Distributing 1 shareholders on receipt of the Controlled stock from Distributing 1 in the External Distribution (§ 355(a)(1)).
- (13) The aggregate basis of the Controlled stock and Distributing 1 stock in the hands of each Distributing 1 shareholder will be the same as the aggregate tax basis of the Distributing 1 stock held by such shareholder immediately before the Internal Distribution allocated in proportion to the fair market value of each (§ 358(b) and (c) and § 1.358-2(a)(2)). If a Distributing 1 shareholder that purchased or acquired shares of Distributing 1 stock on different dates or at different prices is not able to identify which particular share of Controlled stock is received with respect to a particular share of Distributing 1 stock, the stockholder may designate which share of Controlled stock is received with respect to a particular share of Distributing 1 stock, provided the terms of the designation are consistent with the terms of the distribution. (§ 1.358-2(a)(2)(vii)).
- (14) Each Distributing 1 shareholder's holding period in the Controlled stock received in the External Distribution will include the holding period of the stock of Distributing 1 with respect to which the External Distribution is made, provided that the shareholder held such Distributing 1 stock as a capital asset on the date of the External Distribution (§ 1223(1)).
- (15) Distributing 1 and Controlled will allocate their earnings and profits, if any, in accordance with § 312(h), § 1.312-10(b), and § 1.1502-33(e)(3).

We express no opinion about the tax treatment of any transaction described above under other provisions of the Code and regulations or the tax treatment of any condition existing at the time of, or effect resulting from, any of these transactions that is

not specifically covered by the above rulings. In particular, no opinion is requested and no opinion is expressed regarding the tax consequences of Distributing 2's retention of retiree healthcare liabilities as described above.

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

A copy of this ruling letter must be attached to the Federal income tax return of each party involved for the taxable year in which the transaction covered by this letter is consummated. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their returns that provides the date and control number of the letter ruling.

Pursuant to the power of attorney on file in this Office, copies of this letter are being sent to Distributing 1's authorized representatives.

Sincerely,

Ross E. Poulsen
Assistant to the Branch Chief, Branch 3
Office of Associate Chief Counsel (Corporate)

cc: