

Internal Revenue Service

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Department of the Treasury
Washington, DC 20224

Third Party Communication: None
Date of Communication: Not Applicable

Person To Contact:
, ID No.

Telephone Number:

Refer Reply To:
CC:CORP:B02
PLR-124160-19

Date:
April 14, 2020

Legend

Distributing =

Shareholder L =

Shareholder
M =

Shareholder
N =

Shareholder
O =

Shareholder P =

a =

b =

c =

d =

e =

f =

g =

h =

i =

i =

State A =

Business A =

Controlled 1
Assets =

Controlled 2
Assets =

Controlled 3
Assets =

Controlled 4
Assets =

Segment 1 of
Business A =

Segment 2 of
Business A =

Segment 3 of =
Business A

Segment 4 of =
Business A

Dear :

This letter responds to your October 4, 2019, request submitted by your authorized representative, requesting rulings on certain federal income tax consequences of a proposed transaction (defined below, the “Proposed Transaction”). The information provided in that request and in later correspondence is summarized below.

This letter is issued pursuant to Rev. Proc. 2017-52, 2017-42 I.R.B. 283, regarding one or more “Covered Transactions” under section 355 of the Internal Revenue Code (the “Code”). This Office expresses no opinion as to any issue not specifically addressed by the rulings below.

The rulings contained in this letter are based on facts 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.

This office has made no determination regarding whether any of the Distributions (as defined below): (i) satisfies the business purpose requirement of Treas. Reg. § 1.355-2(b); (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 section 355(a)(1)(B) and § 1.355-2(d)); or (iii) is part of a plan (or a 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, or any predecessor or successor of the distributing corporation or the controlled corporation, within the meaning of Treas. Reg. § 1.355-8 (see section 355(e)(2)(A)(ii) and § 1.355-7).

Summary of Facts

Distributing is a State A corporation that was formed on Date 1 and made an election under § 1362(a) to be an S corporation effective as of one day after Date 1. Distributing has a single class of common stock that is owned as follows: Shareholder L, Shareholder M, and Shareholder P each own a%; Shareholder N owns b%; and Shareholder O owns c%. Collectively, Shareholder L, Shareholder M, Shareholder N, Shareholder O, and Shareholder P are referred to as the “Shareholders.”

The Shareholders are siblings. Shareholder M is the President of Distributing. The Shareholders are all members of the board of directors of Distributing and there are no other board members. Shareholder L, Shareholder M, and Shareholder P manage Distributing.

Distributing is a calendar year taxpayer and uses the cash method of accounting. Distributing is directly engaged in Business A. The financial information submitted by Distributing indicates that Distributing has had gross receipts and operating expenses representing the active conduct of a trade or business for each of the past five years.

Proposed Transaction

The Shareholders have significant differences of opinion as to the management and operation of Business A and desire to split the assets and operate separate portions of Business A independently. Therefore, Distributing proposes to engage in the following transaction (the "Proposed Transaction"):

- (i) In order to equalize the value of the stock of the new Controlled entities to be formed, Shareholder N and Shareholder O will contribute cash to Distributing in exchange for additional stock in Distributing (the "Share Equalizations"). Shareholder N will contribute \$d to Distributing. Shareholder O will contribute \$e to Distributing. Following the Share Equalizations, the stock of Distributing will be owned as follows: Shareholder L, Shareholder M, and Shareholder P will each own f%; Shareholder N will own g%; and Shareholder O will own h%. The above contributions and changes to Shareholder ownership are approximate and will be finally determined at the time of the Contributions and Distributions.
- (ii) Distributing will distribute \$i and other property with a value of \$j to Shareholder P in exchange for all of Shareholder P's Distributing stock (the "Redemption").
- (iii) Distributing will form Controlled 1, Controlled 2, Controlled 3, and Controlled 4 as a State A corporation (each, a "Controlled"). Each Controlled will have outstanding one class of voting common stock .
- (iv) Distributing will transfer the Controlled 1 Assets, which include assets used to conduct Segment 1 of Business A, to Controlled 1 in exchange for the Controlled 1 stock and the assumption by Controlled 1 of the liabilities associated with the transferred assets ("Contribution 1").
- (v) Distributing will transfer the Controlled 2 Assets, which include assets used to conduct Segment 2 of Business A, to Controlled 2 in exchange for the Controlled 2 stock and the assumption by Controlled 2 of the liabilities associated with the transferred assets ("Contribution 2").

- (vi) Distributing will transfer the Controlled 3 Assets, which include assets used to conduct Segment 3 of Business A, to Controlled 3 in exchange for the Controlled 3 stock and the assumption by Controlled 3 of the liabilities associated with the transferred assets (“Contribution 3”).
- (vii) Distributing will transfer the Controlled 4 Assets, which include assets used to conduct Segment 4 of Business A, to Controlled 4 in exchange for the Controlled 4 stock and the assumption by Controlled 4 of the liabilities associated with the transferred assets (“Contribution 4”). Contribution 1, Contribution 2, Contribution 3, and Contribution 4, each a “Contribution”, and collectively, the “Contributions”).
- (viii) Distributing will distribute, Controlled 1 stock to Shareholder L in exchange for all of Shareholder L’s stock in Distributing (“Distribution 1”), Controlled 2 stock to Shareholder M in exchange for all of Shareholder M’s stock in Distributing (“Distribution 2), Controlled 3 stock to Shareholder N in exchange for all of Shareholder N’s stock in Distributing (“Distribution 3”), and Controlled 4 stock to Shareholder O in exchange for all of Shareholder O’s stock in Distributing (“Distribution 4”). (Distribution 1, Distribution 2, Distribution 3, and Distribution 4, are each a Distribution, and collectively, the “Distributions”).
- (ix) Distributing will be liquidated as part of the reorganization.
- (x) Immediately after the Distributions, Controlled 1, Controlled 2, Controlled 3, and Controlled 4 will each make an election under § 1362(a) to be treated as a subchapter S corporation (within the meaning of section 1361(a)) and will have one class of voting stock outstanding.

Representations

With respect to each Contribution and Distribution, Distributing has made all of the representations in section 3 of the Appendix to Rev. Proc. 2017-52, except as set forth below:

- (1) Distributing has made the following alternative representations set forth in section 3 of the Appendix to Rev. Proc. 2017-52:

Representations 3(a); 8(a); 11(a); 15(a); 22(a); 31(a); 41(b).

- (2) Distributing has not made the following representations, which do not apply to the Proposed Transaction:

Representations 4; 5; 6; 19; 20; 25; 35; 36; 37; 38; 39; 40.

- (3) Distributing makes no modified representations other than to the extent necessary to take into account the definitions in section 2.02 and 2.11 of the Appendix to Rev. Proc. 2017-52.

Distributing makes the following additional representations with respect to the Redemption:

1. There are no outstanding options or warrants to purchase Distributing stock, nor are there any outstanding debentures or other obligations that are convertible into Distributing stock or would be considered Distributing stock.
2. No notes or other obligations of Distributing will be distributed to Shareholder P.
3. No Distributing shareholder has been or will be obligated to purchase any of the redeemed stock.
4. The Redemption is part of the Proposed Transaction.
5. There have been no redemptions, issuances, or exchanges by Distributing of its stock in the past 5 years.
6. Except as described in the Proposed Transaction, Distributing has no plan or intention to issue, redeem, or exchange additional share of its stock.
7. Shareholder P is not related, within the meaning of section 318, to any remaining Distributing shareholder.
8. None of the stock to be redeemed was acquired by Shareholder P within the 10-year period preceding the redemption from a person whose stock would be attributed under section 318(a) to Shareholder P at the time of redemption.
9. After the Redemption, Shareholder P will not have any interest in Distributing, including an interest as officer, director, or employee. Shareholder P will not be a creditor as described in section 1.302-4(d) and will not have constructive ownership under section 318(a)(1).
10. At the time of the exchange, the fair market value of the consideration to be received by Shareholder P will be approximately equal to the fair market value of the Distributing stock to be exchanged.
11. The price to be paid for the redeemed Distributing stock will not result in a loss with respect to those shares.

12. There are no declared but unpaid dividends, or funds set apart for dividends, on any of the stock to be redeemed in the Redemption.

Rulings

Based solely on the information and representation submitted, we rule as follows on the Redemption:

- (1) Distributing will recognize gain, if any, with respect to the property distributed by Distributing to effect the Redemption (§ 311(b)(1)).
- (2) The Redemption will be treated as a complete termination of Shareholder P's interest in Distributing within the meaning of section 302(b)(3). The amount distributed in the Redemption will be treated as a distribution in full payment in exchange for stock surrendered as provided in section 302(a).

Based solely on the information and representations submitted, we rule as follows on each Contribution and Distribution:

- (3) Each Contribution, together with its respective Distribution, followed by the liquidation of Distributing will qualify as a reorganization within the meaning of § 368(a)(1)(D). Distributing, Controlled 1, Controlled 2, Controlled 3, and Controlled 4 each will be a "party to a reorganization" within the meaning of § 368(b).
- (4) Distributing will not recognize gain or loss on the Contributions. §§ 361(a) and 357(a).
- (5) Neither Controlled 1, Controlled 2, Controlled 3 nor Controlled 4 will recognize gain or loss on its respective Contribution. § 1032(a).
- (6) The basis in each asset received from Distributing by each Controlled in its respective Contribution will equal the basis of that asset in the hands of Distributing immediately before the Contribution. § 362(b).
- (7) Each Controlled's holding period in each asset received from Distributing in the respective Contribution will include the period during which Distributing held that asset. § 1223(2).
- (8) Distributing will not recognize any gain or loss on the Distributions. § 361(c)(1).
- (9) Shareholder L, Shareholder M, Shareholder N, and Shareholder O will not recognize gain or loss (and no amount will be otherwise included in income) upon the receipt of their respective Controlled stock. § 355(a)(1).

- (10) The aggregate basis of the Controlled stock received by each Shareholder immediately after its respective Distribution will equal the Shareholder's aggregate basis in the Distributing stock surrendered in the Distribution, allocated in the manner described in § 1.358-2. § 358(a) and (b).
- (11) The holding period of the Controlled stock received by each Shareholder will include the holding period of the Distributing stock with respect to which the Distribution is made, provided that the Distributing stock is held as a capital asset on the date of the Distribution. § 1223(1).
- (12) Earnings and profits, if any, will be allocated between each Controlled in accordance with § 312(h) and Treas. Reg. § 1.312-10(a).
- (13) Distributing's accumulated adjustment account immediately before the transaction will be allocated between each Controlled in a manner similar to the manner in which earnings and profits are allocated under § 312(h) in accordance with Treas. Reg. § 1.1368-2(d)(3) (§§ 1.312-10(a) and 1.1368-2(d)(3)).
- (14) Provided that Distribution 1, Distribution 2, Distribution 3, and Distribution 4 are undertaken immediately after Contribution 1, Contribution 2, Contribution 3, and Contribution 4, Distributing's momentary ownership of the stock of Controlled 1, Controlled 2, Controlled 3, and Controlled 4, as part of the reorganization under section 368(a)(1)(D), will not cause Controlled 1, Controlled 2, Controlled 3, or Controlled 4 to have an ineligible shareholder for any portion of their respective first taxable year under section 1361(b)(1)(B) and will not, in itself, render Controlled 1, Controlled 2, Controlled 3, or Controlled 4 ineligible to elect to be a subchapter S corporation for its respective first taxable year.

Caveats

Except as expressly provided herein, no opinion is expressed or implied concerning the tax treatment of the Proposed Transaction under any provision of the Code and regulations or the tax treatment of any condition existing at the time of, or effects resulting from, the Proposed Transaction that are not specifically addressed by this letter. In particular, no opinion is expressed regarding:

- (i) Whether any Distribution satisfies the business purpose requirement of § 1.355-2(b);
- (ii) Whether any Distribution is used principally as a device for the distribution of earnings and profits of Distributing or Controlled or both;
- (iii) Whether any Distribution and an acquisition or acquisitions are part of a plan (or a series of related transactions) under § 355(e)(2)(A)(ii);

- (iv) Whether any Distributing is a valid S Corporation; and
- (v) Whether any Controlled is otherwise eligible to be an S Corporation.

Procedural Matters

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

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number (PLR-124160-19) of this letter ruling.

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

Sincerely,

Richard K. Passales
Senior Counsel (Branch 4)
Office of Associate Chief Counsel (Corporate)

cc: