

The following facts and representations have been submitted under penalties of perjury in support of the rulings requested:

Company A, a publicly traded company, maintains Plan M, a profit-sharing plan intended to be qualified under section 401(a), that includes a qualified cash or deferred arrangement under section 401(k) and an employee stock ownership plan under section 4975(e)(7). One investment option under Plan M is Fund Q, which is invested primarily in Company A common stock. Fund Q is intended to qualify as an employee stock ownership plan under sections 401(a) and 4975(e)(7). Plan M is the subject of a favorable determination letter dated Date 1, indicating that Plan M is qualified under section 401(a) and satisfies the requirements of section 4975(e)(7). Plan M uses the average cost method described in § 1.402(a)-1(b)(2)(ii)(d)(1) to determine the cost basis of the shares of Company A common stock in Fund Q.

Company A undertook a series of internal restructuring transactions to separate Business H. As a result of the internal restructuring, the U.S. assets and liabilities of Business H, the U.S. operations of Business H, and a substantial majority of the subsidiaries operating the non-U.S. operations of Business H were held by Company C, a wholly owned indirect subsidiary of Entity E, which was, in turn, a wholly owned entity of Company A. Thereafter, Company A converted Entity E to Company B, the controlled corporation in the spinoff.

On Date 2, Company A spun off $x\%$ of the common stock of Company B to Company A's public common stock shareholders (Spinoff). Company A employees in Business H were transferred to Company C prior to the Spinoff and were no longer within Company A's controlled group within the meaning of section 414(b), (c), (m), or (o) following the Spinoff. Company A intends to dispose of the retained $y\%$ of Company B common stock within z days following the Spinoff in satisfaction of Company A debt obligations.

In connection with the Spinoff, Plan M, as a shareholder of Company A common stock through Fund Q, acquired Company B common stock, resulting in Plan M participants having investments in both Company A common stock and Company B common stock. On Date 3, the fiduciary of Plan M retained Advisor K to serve as an independent fiduciary with respect to the Company B common stock that was acquired by Plan M in connection with the Spinoff. Within five days following the Spinoff, Fund R was formed, and the shares of Company B common stock held by Fund Q were transferred to Fund R. Plan M participants are permitted to trade units out of Fund R under the normal Plan M trading rules and reinvest the proceeds in Fund Q or any other Plan M investment alternative, but Plan M participants are not permitted to make any new investments in Fund R.

Advisor K has full responsibility with respect to the Company B common stock received by Plan M held in Fund R. Advisor K indicated that it is likely to decide to sell the Company B common stock by liquidating the Company B common stock within

approximately one year from the formation of Fund R. It is expected that Advisor K will temporarily invest the proceeds from the sales of Company B common stock in cash and other short-term investments, holding these investments in Fund R. The sales proceeds will then be reinvested in another Plan M investment alternative, which may include Fund Q.

Advisor K prepared a report that explains that the sale of Company B common stock and reinvestment in Company A common stock within Fund Q may exceed 90 days. Advisor K stated that when constructing a sales strategy, the variables it considers include the size of the non-employer stock fund and the average daily trading volume of the common stock held in the fund, noting that it tries to minimize the market impact of its sales activity, which generally means keeping directed sales to less than 15% of the common stock's average daily trading volume. The report notes that the following two situations may cause a final sales period to exceed 90 days: (1) a depressed trading volume over a long period of time after the commencement of the final sales period, and (2) a market event that occurs in the middle of the final sales period which may cause Advisor K to delay its sales process for an extended period of time. The report also notes that Company A retained $y\%$ of the shares of Company B common stock, which means that the trading volume of Company B common stock will be lower than would be the case if 100% of the shares were distributed. Based on Advisor K's assessment of these factors and recognizing possible market volatilities, Advisor K thinks it would be advisable to have the time limit for reinvesting Company B common stock into Company A common stock extended beyond 90 days to up to 180 days from the date of sale of Company B common stock.

On Date 4, Company A received a private letter ruling from the Office of Associate Chief Counsel (Corporate), ruling that Company A common stock shareholders will recognize no gain or loss (and no amount will be includible in income) upon the receipt of Company B common stock in the Spinoff under section 355(a) and that the aggregate basis of Company A shares of common stock and Company B shares of common stock in the hands of Company A's public shareholders immediately after the Spinoff will be the same as the aggregate basis of the Company A common stock held by Company A's public shareholders immediately before the Spinoff, allocated between Company A common stock and Company B common stock in proportion to the fair market value of each in accordance with § 1.358-2(a)(2).

Rulings Requested

Based on the facts and representations, the following rulings are requested:

1. Shares of Company B common stock acquired by Plan M for the benefit of Plan M participants (whether current employees, former employees, or beneficiaries) as a result of the Spinoff constitute "securities of the employer corporation" for purposes of section 402(e) and the exclusion of net unrealized appreciation from income under section 402(e).

2. For purposes of determining net unrealized appreciation under section 402(e), the basis of the Company A common stock and Company B common stock held by Plan M immediately after the Spinoff will be determined by allocating the section 402 basis in the shares of Company A common stock immediately before the Spinoff between the Company A shares of common stock and the Company B shares of common stock immediately after the Spinoff in proportion to their relative fair market value, in accordance with the rules of section 358.
3. With respect to any Plan M participant who elects to divest from Fund R and immediately reinvest the proceeds in Company A common stock through Fund Q, such sale and reinvestment shall constitute an exchange of “securities of the employer corporation” for purposes of section 402(j), so that the determination of net unrealized appreciation shall be made without regard to such sale.
4. With respect to any Plan M participant who is divested from Company B common stock in connection with the termination or liquidation of Fund R by Company A or Plan M fiduciaries and reinvested in Company A stock through Fund Q, such sale and reinvestment shall constitute an exchange of “securities of the employer corporation” for purposes of section 402(j), so that the determination of net unrealized appreciation shall be made without regard to such sale and without regard to any temporary investment of Company B stock sales proceeds in short-term investments.
5. Pursuant to the authority granted by section 402(j)(2)(B), if Plan M undertakes the sale of some or all of the Company B shares of common stock, the 90-day period for reinvesting the Company B common stock sales proceeds in Company A common stock through Fund Q shall be extended up to 180 days from the date of sale.

Law and Analysis

Section 402(e)(4)(A) provides, in pertinent part, that for purposes of sections 402(a) and 72, in the case of a distribution other than a lump sum distribution, the amount actually distributed to any distributee from a trust described in section 402(a) shall not include any net unrealized appreciation in securities of the employer corporation attributable to amounts contributed by the employee.

Section 402(e)(4)(B) states, in pertinent part, that for purposes of sections 402(a) and 72, in the case of any lump sum distribution which includes securities of the employer corporation, there shall be excluded from gross income the net unrealized appreciation attributable to that part of the distribution which consists of securities of the employer corporation.

Section 402(e)(4)(E)(ii) provides, in pertinent part, that for purposes of section 402(e), the term “securities of the employer corporation” includes securities of a parent or subsidiary corporation (as defined in subsections (e) and (f) of section 424) of the employer corporation.

Section 1.402(a)-1(b)(2)(i) provides that, with respect to a trust described in section 401(a) that is tax exempt under section 501(a), the amount of net unrealized appreciation in securities of the employer corporation that are distributed by the trust is the excess of the market value of such securities at the time of distribution over the cost or other basis of such securities to the trust.

Section 1.402(a)-1(b)(2)(ii) sets forth the manner in which the cost or other basis to the trust of a distributed security of the employer corporation is calculated for the purpose of determining the net unrealized appreciation on such security.

Section 1.402(a)-1(b)(3) sets forth certain special rules for determining the net unrealized appreciation on securities of the employer corporation that are attributable to employee contributions.

Under § 1.402(a)-1(d)(2), neither employee salary deferrals made pursuant to a cash or deferred arrangement nor matching contributions are treated as employee contributions for purposes of section 402(e)(4).

In Rev. Rul. 73-29, 1973-1 CB 198, securities of an employer corporation held by its qualified plan were transferred to the qualified trust of an unrelated corporation when the first employer sold part of its business and transferred some of its employees to an unrelated corporation. The Internal Revenue Service held that shares of stock of the seller corporation distributed from the buyer’s qualified trust to employees of the buyer corporation who were former employees of the seller corporation were securities of the employer corporation and will always be securities of the employer corporation even after those shares and the employees in whose accounts they were held were transferred to an unrelated corporation.

Section 402(j) provides, in pertinent part, that for the purposes of section 402(e)(4), in the case of any transaction in which either (A) the plan trustee exchanges the plan’s securities of the employer corporation for other such securities or (B) the plan trustee disposes of securities of the employer corporation and uses the proceeds of such disposition to acquire securities of the employer corporation within 90 days (or such longer period as the Secretary of the Treasury may prescribe), the determination of net unrealized appreciation shall be made without regard to such transaction.

Company B was a wholly owned subsidiary of Company A before and at the time of the Spinoff. Section 424(f) provides, in part, that the term “subsidiary corporation” means any corporation (other than the employer corporation) in an unbroken chain of corporations beginning with the employer corporation if each of the corporations other

than the last corporation in the unbroken chain owns stock possessing 50 percent or more of the total combined voting power of all classes of stock in one of the other corporations in such chain. Section 402(e)(4)(E)(ii) provides that the term “securities of the employer corporation” includes securities of a parent or subsidiary corporation (as defined in subsections (e) and (f) of section 424). Because Company B was a wholly owned subsidiary of the “employer corporation” before and at the time of the Spinoff, those shares of Company B common stock constitute “securities of the employer corporation” within the meaning of section 402(e)(4)(E).

Pursuant to and simultaneously with the Spinoff, Company B ceased to be a subsidiary of Company A. However, the shares of Company B common stock distributed to Plan M pursuant to the Spinoff represent part of the pre-Spinoff value of Company A common stock.

The distribution of the shares of Company B common stock with respect to the shares of Company A common stock held by Plan M is similar to the facts in Rev. Rul. 73-29 because the securities of an employer corporation (in this case, the shares of Company B common stock) held by the qualified plan of a related corporation (in this case, Company A) are ultimately held by the qualified plan of an unrelated corporation (Company A, after the Spinoff was consummated). In Rev. Rul. 73-29, shares of stock of the seller corporation transferred to the buyer’s qualified trust as part of the transaction and then distributed from the buyer’s qualified trust to employees of the buyer corporation who were former employees of the seller corporation were securities of the employer corporation at the time contributed and remained employer securities even after those shares and the employees in whose account they were held were transferred to an unrelated corporation.

Therefore, the shares of Company B common stock acquired by Plan M for the benefit of Plan M participants (whether current employees, former employees, or beneficiaries) as a result of the Spinoff constitute “securities of the employer corporation” for purposes of section 402(e) and the exclusion of net unrealized appreciation from income under section 402(e).

Company A received a private letter ruling from the Office of Associate Chief Counsel (Corporate) ruling that Company A common stock shareholders will recognize no gain or loss (and no amount will be includible in income) upon the receipt of shares of Company B common stock in the Spinoff under section 355(a) and that the aggregate basis of shares of Company A common stock and shares of Company B common stock in the hands of Company A’s public shareholders immediately after the Spinoff will be the same as the aggregate basis of the Company A common stock held by Company A’s public shareholders immediately before the Spinoff, allocated between the shares of Company A common stock and the shares of Company B common stock in proportion to the fair market value of each in accordance with § 1.358-2(a)(2).

Section 1.402(a)-1(b)(2)(i) provides that the amount of net unrealized appreciation in securities of the employer corporation that are distributed by the trust is the excess of the market value of such securities at the time of the distribution over the cost or other basis of such securities to the trust.

Therefore, for purposes of determining net unrealized appreciation under section 402(e), the basis of the shares of Company A common stock and shares of Company B common stock held by Plan M immediately after the Spinoff is determined by allocating the section 402 basis in the shares of Company A common stock immediately before the Spinoff between the shares of Company A common stock and the shares of Company B common stock immediately after the Spinoff in proportion to their relative fair market value, in accordance with § 1.358-2(a)(2).

Section 402(j) provides, in pertinent part, that for purposes of section 402(e)(4), in the case of any transaction in which either (A) the plan trustee exchanges the plan's securities of the employer corporation for other such securities or (B) the plan trustee disposes of securities of the employer corporation and uses the proceeds of such disposition to acquire securities of the employer corporation within 90 days (or such longer period as the Secretary of the Treasury may prescribe), the determination of net unrealized appreciation shall be made without regard to such transaction. In the present case, to the extent there is a disposition of Company B common stock followed by the immediate reinvestment of the proceeds in Company A common stock, such exchange or disposition will constitute an exchange of "securities of the employer corporation" for purposes of section 402(j)(2) so that the determination of net unrealized appreciation shall be made without regard to such exchange or disposition.

As discussed above, we have concluded that the shares of Company B common stock received by Plan M as a result of the Spinoff are securities of the employer corporation as defined in section 402(e). The disposition of Company B common stock followed by the reinvestment of the proceeds in Company A common stock is thus a disposition of securities of the employer corporation followed by a reinvestment of the proceeds in securities of the employer corporation.

Therefore, to the extent any Plan M participant who is divested from Company B common stock in connection with the termination or liquidation of Fund R by Company A or Plan M fiduciaries and reinvested in Company A common stock through Fund Q, such sale and reinvestment shall constitute an exchange of "securities of the employer corporation" for purposes of section 402(j), so that the determination of net unrealized appreciation shall be made without regard to such sale, provided that the transactions are completed within the required time frame. According to the submission of your authorized representative, interim investments of the proceeds from Plan M's sales of shares of Company B common stock may be made in cash or other short-term investments. As discussed below, the period for the reinvestment of these proceeds in Company A common stock may be as long as 180 days. Because of the

length of time which may be needed to implement the reinvestment, we do not find that the placement of the proceeds into an interim investment alters this conclusion.

Section 402(j), by its terms alone, does not expressly permit participant-directed transactions. The legislative history (see Senate Report No. 99-313, at 1040 (1986)), however, indicates that section 402(j) applies to transactions that are in the exercise of fiduciary duty or are required by the Employee Retirement Income Security Act of 1974 and requires a participant-directed trustee to act in accordance with participant directions. Therefore, it is appropriate for participant-directed dispositions and acquisitions of employer securities to be covered by section 402(j), provided that the transactions are completed within the required time frame.

Therefore, with respect to any Plan M participant who elects to divest from Fund R and immediately reinvest the proceeds in Company A common stock through Fund Q, such sale and reinvestment would constitute an exchange of "securities of the employer corporation" for purposes of section 402(j), so that the determination of net unrealized appreciation would be made without regard to such sale.

Your authorized representative has submitted a report prepared by Advisor K that explains that the sale of Company B common stock and reinvestment in Company A common stock may exceed 90 days and that it thinks it would be advisable to have the time limit for reinvesting Company B common stock into Company A common stock extended beyond 90 days to up to 180 days from the date of sale of Company B common stock. Advisor K's assessment was based on several factors that it identified in its report, including that (1) it tries to minimize the market impact of its sales activity, which generally means keeping directed sales to less than 15% of the common stock's average daily trading volume; (2) there may be a depressed trading volume over a long period of time after the commencement of the final sales period; (3) a market event that occurs in the middle of the final sales period may cause the sales process to be delayed for an extended period of time; and (4) Company A retained $y\%$ of the shares of Company B common stock, which means that the trading volume of Company B common stock will be lower than would be the case if 100% of the shares were distributed. Because prudent management of the reinvestment may require a period of time longer than the 90 days provided in section 402(j)(2)(B), an extension of the 90-day reinvestment period is not unreasonable under the facts and circumstances described above.

Therefore, if Plan M undertakes the sale of some or all of the shares of Company B common stock, the 90-day period for reinvesting the Company B common stock sales proceeds in Company A common stock through Fund Q shall be extended up to 180 days from the date of sale.

Rulings

Therefore, with respect to your ruling requests, we conclude that:

1. Shares of Company B common stock acquired by Plan M for the benefit of Plan M participants (whether current employees, former employees, or beneficiaries) as a result of the Spinoff constitute “securities of the employer corporation” for purposes of section 402(e) and the exclusion of net unrealized appreciation from income under section 402(e).
2. For purposes of determining net unrealized appreciation under section 402(e), the basis of the shares of Company A common stock and shares of Company B common stock held by Plan M immediately after the Spinoff will be determined by allocating the section 402 basis in the shares of Company A common stock immediately before the Spinoff between the shares of Company A common stock and the shares of Company B common stock immediately after the Spinoff in proportion to their relative fair market value, in accordance with the rules of section 358.
3. With respect to any Plan M participant who elects to divest from Fund R and immediately reinvest the proceeds in Company A common stock through Fund Q, such sale and reinvestment shall constitute an exchange of “securities of the employer corporation” for purposes of section 402(j), so that the determination of net unrealized appreciation shall be made without regard to such sale.
4. With respect to any Plan M participant who is divested from Company B common stock in connection with the termination or liquidation of Fund R by Company A or Plan M fiduciaries and reinvested in Company A stock through Fund Q, such sale and reinvestment shall constitute an exchange of “securities of the employer corporation” for purposes of section 402(j), so that the determination of net unrealized appreciation shall be made without regard to such sale and without regard to any temporary investment of Company B stock sales proceeds in cash and other short-term investments.
5. Pursuant to the authority granted by section 402(j)(2)(B), if Plan M undertakes the sale of some or all of the shares of Company B common stock, the 90-day period for reinvesting the Company B common stock sales proceeds in Company A common stock through Fund Q shall be extended up to 180 days from the date of sale.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalties of perjury statement executed by an appropriate party, as specified in Rev. Proc. 2021-1, 2021-1 IRB 1, § 7.01(16)(b). This office has not verified any of the material submitted in support of the request for rulings, and such material is subject to verification on examination. The Associate office will revoke or modify a letter ruling and apply revocation retroactively if there has been a misstatement or omission of controlling facts; the facts at the time of

the transaction are materially different from the controlling facts on which the rulings was based; or, in the case of a transaction involving a continuing action or series of actions, the controlling facts change during the course of the transaction. See Rev. Proc. 2021-1, § 11.05.

Except as specifically set forth above, no opinion is expressed or implied concerning the federal tax consequences of any aspect of any transaction or item discussed or referenced in this letter ruling.

This ruling letter is based on the assumption that Plan M is qualified under section 401(a), Fund Q meets the requirements of sections 401(a)(35) and 4975(e)(7), and Plan M's related trust is tax-exempt under section 501(a) at all relevant times.

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 authorized representative.

Sincerely,

John T. Ricotta
Chief, Qualified Plans Branch 3
Office of Associate Chief Counsel
(Employee Benefits, Exempt Organizations,
and Employment Taxes)

cc: