

Internal Revenue Service

Department of the Treasury
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Person To Contact: _____, ID No.

Telephone Number:

Refer Reply To:
CC:CORP:4
PLR-117174-21

Date:
February 18, 2022

Legend

Distributing =

Controlled =

Business A =

Distributing Business =

Controlled Business =

Transferred Assets =

Retained Assets =

Family A =

PLR-117174-21

4

Family B

=

a

=

b

=

Dear

:

This letter responds to your letter dated August 2, 2021, as supplemented by additional letters dated February 15, 2022 and February 17, 2022, requesting rulings on certain federal income tax consequences of a series of transactions (the “Proposed Transaction,” as defined below). The material information submitted in that request and subsequent correspondence is summarized below.

This letter is issued pursuant to Rev. Proc. 2017-52, 2017-41 I.R.B. 283, as amplified and modified by Rev. Proc. 2018-53, 2018-43 I.R.B. 667, regarding one or more “Covered Transactions” under section 355 and/or section 368 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 penalties of perjury statement executed by an appropriate party. This office has not verified any of the materials 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 the Proposed Transaction: (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 Treas. Reg. § 1.355-2(d)); or (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, 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 Treas. Reg. § 1.355-7).

Summary of Facts

Distributing is a closely held corporation that operates Business A. Distributing has made an election under section 1362(a) to be treated as a subchapter S corporation (within the meaning of section 1361(a)). Distributing has a single class of common stock outstanding. Family A directly owns a percent of the issued and outstanding stock of Distributing. Family B indirectly owns b percent of the issued and outstanding stock of Distributing through various domestic eligible entities (within the meaning of Treas. Reg. § 301.7701-3(a)) that are disregarded as entities separate from their owner for U.S. federal income tax purposes.

For purposes of satisfying the active trade or business requirements of section 355(b) with respect to the Proposed Transaction (as defined below), Distributing will rely on the Distributing Business, and Controlled will rely on the Controlled Business. Distributing has submitted financial information in accordance with Rev. Proc. 2017-52 indicating

that the Distributing Business and Controlled Business have had gross receipts and operating expenses representing the active conduct of a trade or business for each of the past five years.

Proposed Transaction

For what are represented to be valid business reasons, Distributing proposes to engage in the following transactions (collectively, the "Proposed Transaction"):

1. Distributing will form a new limited liability company, Controlled, and elect to treat Controlled as a qualified subchapter S subsidiary (a "QSub") as of the date of formation. Controlled will have a single class of stock outstanding, all of which will be directly owned by Distributing.
2. Distributing will transfer the Transferred Assets to Controlled solely in exchange for stock of Controlled and the assumption by Controlled of liabilities associated with the Transferred Assets (the "Contribution").
3. Distributing will distribute all of the stock of Controlled to the Family A shareholders in complete redemption of the Family A shareholders' respective shares of Distributing (the "Distribution").
4. Effective immediately after the Distribution, Controlled will elect to be classified as a subchapter S corporation for U.S. federal income tax purposes.

In connection with the Proposed Transaction, Distributing and Controlled may enter into a separation and distribution agreement, and a tax matters agreement, that will continue after the completion of the Proposed Transaction in order to effectively transition to separate operations.

Representations

Except as set forth below, Distributing has made all of the representations in section 3 of the Appendix to Rev. Proc. 2017-52 with respect to the Proposed Transaction:

1. Distributing has made the following alternative representations: 3(a), 8(a), 11(a), 15(a), 22(a), 31(a), and 41(b).
2. Distributing has not made the following representations, which do not apply to the Proposed Transaction: 5, 6, 20, 24, 25, 35, 36, 37, 38, 39, and 40.
3. Distributing cannot make Representation 42 but has represented that: "All of the shareholders of Distributing are U.S. persons."

Distributing has made all of the representations in section 3.04 of Rev. Proc. 2018-53

with respect to the Proposed Transaction, except Representation 6, which does not apply to the Proposed Transaction.

Rulings

1. The Contribution, together with the Distribution, will qualify as a reorganization and distribution pursuant to sections 368(a)(1)(D) and 355. Distributing and Controlled will each be a “party to the reorganization” within the meaning of section 368(b).
2. No gain or loss will be recognized by Distributing on the Contribution. Sections 357(a) and 361(a).
3. No gain or loss will be recognized by Controlled on the Contribution. Section 1032(a).
4. The basis in each asset received by Controlled from Distributing in the Contribution will equal the basis of the asset in the hands of Distributing immediately before the Contribution. Section 362(b).
5. The holding period in each asset received by Controlled from Distributing in the Contribution will include the period during which such asset was held by Distributing. Section 1223(2).
6. No gain or loss will be recognized by Distributing upon its distribution of the stock of Controlled on the Distribution. Section 361(c).
7. No gain or loss will be recognized by (and no amount otherwise will be included in the income of) the shareholders of Distributing upon the receipt of Controlled stock in exchange for their Distributing stock. Section 355(a)(1).
8. Each participating shareholder’s aggregate basis in its Controlled stock immediately after the Distribution will equal such shareholder’s aggregate basis in the Distributing stock surrendered in the Distribution and will be allocated among the shares received in the manner described in Treas. Reg. § 1.358-2(a). Section 358(a)(1) and (b)(1).
9. Each participating shareholder’s holding period in its Controlled stock received in the Distribution will include the holding period of the Distributing stock held by such shareholder, provided that such Distributing stock was held as a capital asset on the date of the Distribution. Section 1223(1).
10. Distributing’s accumulated adjustment account immediately before the transaction will be allocated between Distributing and Controlled in a manner similar to the manner in which Distributing’s earnings and profits will be allocated under section 312(h) in accordance with Treas. Reg. § 1.1368-2(d)(3). Treas. Reg. §§ 1.312-10(a) and 1.1368-2(d)(3).

11. The Distribution will cause a termination of Controlled's QSub election because Controlled will cease to be a wholly owned subsidiary of a subchapter S corporation. For all U.S. federal income tax purposes, Controlled will be treated as a new corporation acquiring all of its assets and assuming all of its liabilities from Distributing immediately before the termination of Controlled's QSub election in exchange for the stock of Controlled pursuant to Treas. Reg. § 1.1361-5(b)(1)(i) and section 1361(b)(3)(B) and (C).

12. Distributing's momentary ownership of the stock of Controlled, as part of the reorganization under section 368(a)(1)(D), will not cause Controlled to have an ineligible shareholder for any portion of its first taxable year under section 1361(b)(1)(B), and will not, in itself, render Controlled ineligible to elect to be a subchapter S corporation for its first taxable year. If Controlled otherwise meets the requirements of a small business corporation under section 1361, Controlled will be eligible to make a subchapter S election under section 1362(a) for its first taxable year, provided that such election is made effective immediately upon the Distribution.

Caveats

Except as expressly provided herein, no opinion is expressed or implied about the tax treatment of the Proposed Transaction under any other provisions of the Code or regulations, or the tax treatment of any conditions existing at the time of, or effects resulting from, the Proposed Transaction that are not specifically covered by the above rulings.

Procedural Statements

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 should be attached to the federal 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 on and control number (PLR-117174-21) of this letter ruling.

Sincerely,

Brian R. Loss
Senior Technician Reviewer, Branch 4
Office of Associate Chief Counsel (Corporate)

cc: