

Internal Revenue Service

Department of the Treasury

Index Number: 0355.01-01, 0368.04-00

Washington, DC 20224

Number: **199903014**

Person to Contact:

Release Date: 1/22/1999

Telephone Number:

Refer Reply To:

CC:DOM:CORP:4 PLR-108978-98

Date:

October 22, 1998

Distributing =

Controlled =

Business A =

Group A =

Group B =

x =

y =

Dear

This letter responds to your April 3, 1998 request for rulings on certain federal income tax consequences of a proposed transaction. The information provided in that request and in later correspondence is summarized below.

Distributing conducts Business A and is owned x percent by Group A and y percent by Group B.

Financial information has been submitted indicating that Distributing had gross income and operating expenses representing the conduct of an active business during each of the past five years.

Serious disputes regarding the best way to operate Business A have arisen between Group A and Group B. The disputes are having an adverse effect on the day-to-day operations of Distributing. To allow Group A and Group B to go their own ways and cause their corporations to conduct Business A in the way each Group thinks best, the following transaction has been proposed:

- (i) Distributing will transfer certain Business A assets to newly formed Controlled in exchange for Controlled stock (the "Contribution").
- (ii) Distributing will distribute all of the Controlled stock to the members of Group B in exchange for all of the Distributing stock held by each member of Group B (the "Distribution").

The taxpayer has made the following representations concerning the proposed transaction:

- (a) The fair market value of the Controlled stock received by each shareholder of Distributing will be approximately equal to the fair market value of the Distributing stock surrendered by the shareholder in the exchange.
- (b) No part of the consideration to be distributed by Distributing will be received by a shareholder as a creditor, employee, or in any capacity other than that of a shareholder the corporation.
- (c) The five years of financial information submitted on behalf of Distributing is representative of the corporation's present operations, and with regard to such corporation, there have been no substantial operational changes since the date of the last financial statement submitted.
- (d) Following the Distribution, Distributing and Controlled will each continue,

independently and with its separate employees, the active conduct of its share of all the integrated activities of the business conducted by Distributing prior to consummation of the transaction.

- (e) The Distribution is being carried out for the purposes set forth above. The Distribution is motivated, in whole or substantial part, by one or more of these corporate business purposes.
- (f) There is no plan or intention by the shareholders of Distributing to sell, exchange, transfer by gift, or otherwise dispose of any of their stock in either Distributing or Controlled after the Distribution.
- (g) There is no plan or intention by either Distributing or Controlled, directly or through any subsidiary corporation, to purchase any of its outstanding stock after the Distribution, other than through stock purchases meeting the requirements of § 4.05(1)(b) of Rev. Proc. 96-30.
- (h) There is no plan or intention to liquidate either Distributing or Controlled, to merge either corporation with any other corporation, or to sell or otherwise dispose of the assets of either corporation after the Distribution, except in the ordinary course of business.
- (i) The income tax liability for the taxable year in which investment credit property (including any building to which § 47(d) applies) is transferred will be adjusted pursuant to § 50(a)(1) or (a)(2) (or § 47, as in effect before amendment by Public Law 101-508, Title 11, 104 Stat. 1388, 536 (1990), if applicable) to reflect an early disposition of the property.
- (j) No intercorporate debt will exist between Distributing and Controlled at the time of, or subsequent to, the Distribution.
- (k) No two parties to the transaction are investment companies as defined in § 368(a)(2)(F)(iii) and (iv) of the Internal Revenue Code.
- (l) Payments made in connection with all continuing transactions, if any, between Distributing and Controlled, will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's-length.
- (m) Distributing is not an S corporation (within the meaning of § 1361(a)), and there is no plan or intention by Distributing or Controlled to make an S corporation election pursuant to § 1362(a).
- (n) Distributing neither accumulated its receivables nor made extraordinary payments of its payables in anticipation of the Contribution and

Distribution.

Based solely on the information submitted and the representations set forth above, we rule as follows:

- (1) The Contribution, followed by the Distribution, will be a reorganization under § 368(a)(1)(D). Distributing and Controlled will each be "a party to a reorganization" under § 368(b).
- (2) No gain or loss will be recognized by Distributing on the Contribution (§ 361(a)).
- (3) No gain or loss will be recognized by Controlled on the Contribution (§ 1032(a)).
- (4) The basis of each asset received by Controlled will equal the basis of that asset in the hands of Distributing immediately before the transfer (§ 362(b)).
- (5) The holding period of each asset received by Controlled will include the period during which Distributing held the asset (§ 1223(2)).
- (6) No gain or loss will be recognized by (and no amount will otherwise be included in the income of) any member of Group B on the Distribution (§ 355(a)(1)).
- (7) The basis of the Controlled stock received by each member of Group B will equal the basis of the Distributing stock that member surrendered in exchange therefor (§ 358(a)(1)).
- (8) No gain or loss will be recognized by Distributing on the Distribution (§ 361(c)(1)).
- (9) The holding period of the Controlled stock received by each member of Group B will include the holding period of the Distributing stock exchanged therefor, provided the Distributing stock is held as a capital asset on the date of the Distribution (§ 1223(1)).
- (10) As provided in § 312(h), proper allocation of earnings and profits between Distributing and Controlled will be made under § 1.312-10(a).

We express no opinion about the tax treatment of the transaction under any other section of the Code or regulations or the tax treatment of any conditions existing at the time of, or effects resulting from, the transaction that are not specifically covered

in the above rulings.

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 should be attached to the federal income tax return of each taxpayer involved for the taxable year in which the transaction is consummated.

Under the power of attorney on file in this office, copies of this letter are being sent to the taxpayer and the second named authorized representative.

Sincerely yours,

Assistant Chief Counsel (Corporate)

By: _____
Vicki J. Hyche
Chief, Branch 4

