

Internal Revenue Service

memorandum

CC:CORP:4:PRENO-120891-03
CBWell

date: September 17, 2003

to: Manager, Exempt Organizations, Rulings and Agreements
Technical Group 3, T:EO:RA:T:3
Attn: Michael Seto

from: ^{SJD} Sean P. Duffley, Assistant to the Chief, CC:CORP:4

subject: [REDACTED]

This is in response to your request for assistance in connection with a ruling request submitted by the above taxpayer. The following is for inclusion in your reply to the taxpayer.

LEGEND

- Coop Parent = [REDACTED]
- Coop Subsidiary = [REDACTED]
- State A = [REDACTED]
- Utility B = [REDACTED]
- Asset C = [REDACTED]
- D = [REDACTED]
- Agency = [REDACTED]
- E = [REDACTED]
- F = [REDACTED]

G	=	[REDACTED]
H	=	[REDACTED]
Date 1	=	[REDACTED]
Date 2	=	[REDACTED]
Date 3	=	[REDACTED]
Year 1	=	[REDACTED]
Year 2	=	[REDACTED]

This letter responds to your request for rulings on certain federal income tax consequences of a proposed transaction. The information submitted in such request and in subsequent correspondence is summarized below.

FACTS

Coop Parent is a corporation organized on Date 1 pursuant to the State A cooperative statute. Coop Parent is engaged in Utility B. On Date 2, the Internal Revenue Service granted Coop Parent exemption from federal income taxation as an organization described in section 501(c)(12) of the Internal Revenue Code. Coop Parent remained exempt until Year 1, when it failed to satisfy the requirement that 85 percent or more of its income consist of amounts collected from members for the sole purpose of meeting losses and expenses. Coop Parent reclaimed its exemption in Year 2 and has retained such status since that time.

On a date prior to Date 3, Coop Parent organized Coop Subsidiary as a one-member subsidiary cooperative pursuant to the State A cooperative statute. On Date 3, the Internal Revenue Service granted Coop Subsidiary exemption from federal income taxation as an organization described in section 501(c)(12). Coop Subsidiary has maintained its tax-exempt status from Date 3 to the present.

Coop Parent formed Coop Subsidiary for the purpose of financing the construction of Asset C. In connection with the construction of Asset C, Coop Parent loaned \$D to Coop Subsidiary, which amount Coop Parent had borrowed from Agency and from E (the "Construction Debt"). Approximately \$F of the Construction Debt remains unsatisfied. Coop Subsidiary also owes Coop Parent \$G for certain capital improvements Coop Parent made on Coop Subsidiary's behalf, and an additional \$H representing miscellaneous indebtedness (hereafter, all such indebtedness owed by Coop Subsidiary to Coop Parent is referred to as the "Coop Subsidiary Indebtedness").

For valid business reasons, Coop Parent proposes the complete liquidation of Coop Subsidiary into Coop Parent (the "Liquidation"). Upon approval of the proposed transaction by Agency and issuance of this private letter ruling by the Internal Revenue Service, Coop Subsidiary will adopt a plan of liquidation pursuant to which Coop Subsidiary will distribute all of its assets and liabilities to Coop Parent and will be dissolved under applicable State A law.

REPRESENTATIONS

The taxpayer has made the following representations with respect to the proposed transaction:

(a) Coop Parent and Coop Subsidiary each has satisfied all the requirements to be classified as a cooperative for federal income tax purposes.

(b) Neither Coop Parent nor Coop Subsidiary has engaged in activities that would give rise to unrelated business taxable income within the meaning of sections 511 through 514.

(c) On the date of adoption of the plan of liquidation, and at all times until the final liquidating distribution is completed, Coop Parent's membership interest in Coop Subsidiary will constitute the sole equity interest in Coop Subsidiary.

(d) All distributions from Coop Subsidiary to Coop Parent pursuant to the plan of complete liquidation will be made within a single taxable year of Coop Subsidiary.

(e) As soon as the first liquidating distribution has been made, Coop Subsidiary will cease to be a going concern and its activities will be limited to winding up its affairs, paying its debts, and distributing its remaining assets to its sole equity holder Coop Parent.

(f) Coop Subsidiary will retain no assets following the final liquidating distribution.

(g) Coop Subsidiary will not have acquired assets in any nontaxable transaction at any time, except for acquisitions occurring more than 3 years prior to the date of adoption of the plan of liquidation.

(h) No assets of Coop Subsidiary have been, or will be, disposed of by either Coop Subsidiary or Coop Parent except for dispositions in the ordinary course of business and dispositions occurring more than 3 years prior to adoption of the plan of liquidation.

(i) The liquidation of Coop Subsidiary will not be preceded or followed by the reincorporation in, or transfer or sale to, a recipient corporation (Recipient) of any of the

businesses or assets of Coop Subsidiary, if persons holding, directly or indirectly, more than 20 percent in value of the equity interest in Coop Subsidiary also hold, directly or indirectly, more than 20 percent in value of the equity interest in Recipient. For purposes of this representation, ownership will be determined by application of the constructive ownership rules of section 318(a) of the Code as modified by section 304(c)(3).

(j) Prior to adoption of the plan of liquidation, no assets of Coop Subsidiary will have been distributed in kind, transferred, or sold to Coop Parent, except for (i) transactions occurring in the normal course of business and (ii) transactions occurring more than 3 years prior to adoption of the liquidating plan.

(k) Coop Subsidiary will report all earned income represented by assets that will be distributed to Coop Parent such as receivables being reported on a cash basis, commissions due, etc.

(l) The fair market value of the assets of Coop Subsidiary will exceed its liabilities both at the date of the adoption of the plan of complete liquidation and immediately prior to the time the first liquidating distribution is made.

(m) All other transactions undertaken contemporaneously with, in anticipation of, in conjunction with, or in any way related to, the proposed liquidation of Coop Subsidiary have been fully disclosed.

LAW

Section 332(a) provides that no gain or loss shall be recognized on the receipt by a corporation of property distributed in a complete liquidation of another corporation. Section 332(b) sets forth various requirements that must be met in order for a distribution to be considered in complete liquidation for purposes of section 332.

Section 1.332-7 of the Income Tax Regulations provides, in part, that if section 332(a) is applicable to the receipt of the subsidiary's property in complete liquidation, then no gain or loss shall be recognized to the subsidiary upon the transfer of such properties even though some of the properties are transferred in satisfaction of the subsidiary's indebtedness to its parent. However, any gain or loss realized by the parent corporation on such satisfaction of indebtedness, shall be recognized to the parent corporation at the time of the liquidation.

Section 337(a) provides that no gain or loss shall be recognized to the liquidating corporation on the distribution to the 80-percent distributee of any property in a complete liquidation to which section 332 applies.

Section 337(b)(1) provides that if a corporation is liquidated in a liquidation to which section 332 applies, and on the date of the adoption of the plan of liquidation,

such corporation was indebted to the 80-percent distributee, then for purposes of section 337 and 336, any transfer of property to the 80-percent distributee in satisfaction of such indebtedness shall be treated as a distribution to such distributee in such liquidation.

Section 337(b)(2)(A) generally provides that sections 337(a) and (b)(1) shall not apply where the 80-percent distributee is an organization (with limited exception not relevant on these facts) which is exempt from the tax imposed by Chapter 1.

Section 337(d) authorizes the Secretary to prescribe regulations as may be necessary or appropriate to carry out the purposes of the amendments made by subtitle D of title VI of the Tax Reform Act of 1986, including regulations to ensure that such purposes may not be circumvented through the use of a tax-exempt entity. The legislative history concerning a 1988 amendment to section 337(d) explains that the grant of authority in section 337(d) "includes rules to require the recognition of gain if appreciated property of a C corporation is transferred to . . . a tax-exempt entity in a carryover basis transaction that would otherwise eliminate corporate level tax on the built-in appreciation." S. Rep. No. 445, 100th Cong., 2d Sess. 66 (1988) (footnote omitted).

Section 1.337(d)-4(a)(1) sets forth the general rule that if a taxable corporation transfers all or substantially all of its assets to one or more tax-exempt entities, the taxable corporation must recognize gain or loss immediately before the transfer as if the assets transferred were sold at their fair market values.

RULINGS

Section 3.01(29) of Rev. Proc. 2003-3, 2003-1 I.R.B. 113, 115, provides that the Service will not rule on the qualification of a transaction as a tax-free liquidation under section 332, unless the Service determines that there is a significant issue that is not clearly and adequately addressed by published authority. In such a case, the Service will rule on the entire transaction, and not just the significant issue. In addition to rulings and under sections 332 and 337, the taxpayer has requested a ruling on whether section 337(b)(2)(A) applies to the complete liquidation of a tax-exempt subsidiary into its tax-exempt parent under section 332.

Based solely on the information submitted and representations provided, we rule as follows:

(1) Provided that the requirements of section 332(b) are met, no gain or loss will be recognized by Coop Parent upon the receipt of the assets and liabilities of Coop Subsidiary in the Liquidation. Section 332(a). Any gain or loss realized by Coop Parent on the satisfaction of the Coop Subsidiary Indebtedness shall be recognized. §1.332-7.

(2) No gain or loss will be recognized by Coop Subsidiary on the distribution of its assets to, or the assumption of liabilities by, Coop Parent. Sections 337(a), 337(b) and 336(d)(3). In particular, section 337(b)(2)(A) will not apply to the Liquidation.

(3) Coop Parent's basis in each asset received from Coop Subsidiary as a result of the Liquidation will be the same as the basis of that asset in the hands of Coop Subsidiary immediately before the Liquidation. Section 334(b)(1).

(4) Coop Parent's holding period in each asset received from Coop Subsidiary as a result of the Liquidation will include the period during which that asset was held by Coop Subsidiary. Section 1223(2).

(5) Coop Parent will succeed to and take into account the items of Coop Subsidiary described in section 381(c), subject to the conditions and limitations specified in sections 381, 382, 383, and 384 and the regulations thereunder. Section 381(a) and §1.1381(a)-1.

CAVEATS

The rulings contained in this letter are based upon the information and representations submitted by the taxpayer and accompanied by a penalties of perjury statement executed by an appropriate party. Although this office has not verified any of the materials submitted in support of the request for rulings, it is subject to verification on examination.

We express no opinion about the tax treatment of the transaction under other provisions of the Code and regulations or about the tax treatment of any conditions at the time of, or effects resulting from, the transaction that are not specifically covered by the above ruling.

PROCEDURAL STATEMENTS

This ruling is directed only to the taxpayer who requested 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.

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