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Person to Contact:

Telephone Number:

Refer Reply To:
CC:CORP:B06-PLR-132631-02
Date:
September 6, 2002

Distributing =

- DSub1 =
- DSub2 =
- DSub3 =
- DSub4 =
- DSub5 =
- DSub6 =
- DSub7 =
- DSub8 =
- DSub9 =
- DSub10 =
- DSub11 =
- DSub12 =
- DSub13 =
- DSub14 =
- DSub15 =
- DSub16 =
- DSub17 =
- DSub18 =
- DSub19 =

Controlled =

- X1 =
- X2 =
- X3 =

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Y1 =

Y2 =

X1 Corp =

X2 Corp =

X3 Corp =

Y1 Corp =

Y2 Corp =

b =

c =

d =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Dear

This letter responds to your letter dated June 13, 2002, requesting rulings under I.R.C. §§ 368 and 355. Additional information was received in a letter dated August 1, 2002. The information submitted in your letters is summarized below.

Distributing is a holding company that is the common parent of an affiliated group of corporations filing a consolidated Federal income tax return. As of Date 3, it has one class of stock outstanding comprised of b shares of common stock. This stock is owned by approximately c shareholders of record on Date 2. Of these shareholders, d own 5% or more of such stock.

Distributing is indirectly engaged in the following businesses: X1, X2 and X3 (the "X Business"), and Y1 and Y2 (the "Y Business"). The X1 business is primarily conducted by X1 Corp. The X2 business is primarily conducted by X2 Corp. The X3 business is primarily conducted by X3 Corp. The Y1 business is primarily conducted by Y1 Corp. The Y2 business is primarily conducted by Y2 Corp.

Distributing acquired the stock of Y1 Corp on Date 1 in a taxable transaction. The distribution described below ("Distribution") will not occur until after Date 4. Thus, at the time of the Distribution, Distributing will have owned all of the stock of Y1 Corp for more than five years.

Distributing owns all of the stock of DSub1 through DSub19, X3 Corp, Y1 Corp and Y2 Corp. DSub3 owns all of the stock of X1 and DSub10 owns all of the stock of X2 Corp.

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Distributing has documented that the Distribution will allow Controlled to: (1) more efficiently finance the growth of the X Business through the issuance of equity securities, by means of an initial public offering ("IPO"), and (2) optimize Controlled's capital structure, thus facilitating the opportunity for Controlled to obtain debt financing at a lower cost. In order to effectuate its business purposes, Distributing will undertake the following series of steps:

- (1) Distributing will incorporate Controlled and will own all of its outstanding stock.
- (2) Distributing, through certain of its subsidiaries, will transfer land and other minor assets to Y2 Corp.
- (3) Distributing will transfer to Y1 Corp all of the stock of DSub1, DSub2 and Y2 Corp.
- (4) Distributing will transfer to DSub3 all of the stock of DSub4 through DSub9. DSub3 will transfer all of the stock of all of these entities to X1 Corp.
- (5) Distributing will transfer to X3 Corp all of the stock of DSub17, DSub18 and DSub19.
- (6) Distributing currently intends to draw down on one or more of its line of credits and use the cash proceeds to acquire shares of its stock from one or more of its shareholders, including its larger shareholders.
- (7) Distributing will transfer to Controlled all of the stock of DSub3, DSub10 through 16 and X3 Corp, as well as some assets, in exchange for all of the stock of Controlled and the assumption by Controlled of an appropriate amount of liabilities of Distributing, including the liability for the line(s) of credit drawn down by Distributing in the preceding step. Simultaneously, Controlled intends to borrow funds from an unrelated third party and will distribute the loan proceeds to Distributing.
- (8) Distributing will deposit any cash received from Controlled in the preceding step into a segregated account and, prior to the IPO described below or possibly afterwards (but prior to the distribution of the stock of Controlled), it intends to use these funds solely to buy back additional shares of its stock.
- (9) Controlled will issue no more than 19.9% of Controlled stock to public investors in an IPO.
- (10) Within 12 months following the IPO and the receipt of a favorable private letter ruling from the IRS, Distributing will distribute all of its shares of stock of Controlled pro rata to the Distributing shareholders.

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Each of the transfers described in steps (2) - (5) is intended to qualify under I.R.C. § 351(a).

The following representations have been made in connection with the proposed transaction:

- (a) The total adjusted bases and the fair market value of the assets transferred to Controlled by Distributing each equals or exceeds the sum of the liabilities assumed by Controlled (as determined under section 357(d)).
- (b) The liabilities assumed in the transaction (as determined under section 357(d)) were incurred in the ordinary course of business and are associated with the assets being transferred.
- (c) Neither Distributing nor Controlled will accumulate its receivables nor make extraordinary payment of its payables in anticipation of the Distribution.
- (d) Other than trade account indebtedness created in the ordinary course of business through continuing transactions at terms comparable to those which could be obtained in an arm's-length transaction, and payables created for all transitional services negotiated at arm's-length, no intercorporate debt will exist between Distributing and Controlled at the time of, or subsequent to, the Distribution.
- (e) Subsequent to the Distribution, it is anticipated that Distributing and Controlled will share a number of administrative services for a transitional period not to exceed 12 months.
- (f) Immediately before the Distribution, items of income, gain, loss, deduction and credit will be taken into account as required by the applicable intercompany transaction regulations (See Treas. Reg. sections 1.1502-13 and 1.1502-14 as in effect before the publication of T.D. 8597, 1995-32 I.R.B. 6, and as currently in effect; Treas. Reg. section 1.1502-13 as published by T.D. 8597). Further, Distributing's excess loss account with respect to DSub3, DSub10, X1 Corp, X2 Corp, and X3 Corp, if any, will be included in income before the Distribution (See Treas. Reg. section 1.1502-19).
- (g) Payments made in connection with all continuing transactions after the Distribution, if any, between Distributing and Controlled, X1 Corp, X2 Corp, X3 Corp, DSub3 or DSub10, will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's-length.
- (h) Neither Distributing nor Controlled is an investment company as defined in section 368(a)(2)(F)(iii) and (iv).

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- (i) The indebtedness owed by Controlled to Distributing after the Distribution, if any, will not constitute "stock or securities" within the meaning of section 355.
- (j) No part of the consideration to be distributed by Distributing will be received by a shareholder of Distributing as a creditor, employee or in any capacity other than that of a shareholder of Distributing.
- (k) The payment of cash in lieu of fractional shares of Controlled common stock is solely for the purpose of avoiding the expense and inconvenience to Controlled of issuing fractional shares and does not represent separately bargained for consideration. The total cash consideration that will be paid in the transaction to the shareholders instead of issuing fractional shares of Controlled common stock will not exceed one percent of the total consideration that will be issued in the transaction to the shareholders. The fractional share interests of each shareholder will be aggregated and no shareholder will receive cash in an amount greater than one full share of Controlled common stock.
- (l) The five years of financial information provided on behalf of Y1 Corp is representative of its present operations, and with regard to such corporation, there have been no substantial operational changes since the date of the last financial statements submitted.
- (m) Immediately after the Distribution, at least 90 percent of the fair market value of the gross assets of Distributing will consist of the stock and securities of Y1 Corp, which is a wholly owned corporation engaged in the active conduct of a trade or business as defined in section 355(b)(2).
- (n) The five years of financial information provided on behalf of X1 Corp, X2 Corp and X3 Corp is representative of each corporation's present operations, and with regard to each such corporation, there have been no substantial operational changes since the date of the last financial statements submitted.
- (o) Immediately after the Distribution, at least 90 percent of the fair market value of the gross assets of Controlled will consist of the stock and securities of DSub3, DSub10 and X3 Corp. X3 Corp is a wholly owned first tier corporation engaged in the active conduct of a trade or business as defined in section 355(b)(2).
- (p) Immediately after the Distribution, at least 90 percent of the fair market value of the gross assets of DSub3 will consist of the stock and securities of X1 Corp, which is a wholly owned corporation engaged in the active conduct of a trade or business as defined in section 355(b)(2).
- (q) Immediately after the Distribution, at least 90 percent of the fair market value of the gross assets of DSub10 will consist of the stock and securities of X2 Corp,

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which is a wholly owned corporation engaged in the active conduct of a trade or business as defined in section 355(b)(2).

- (r) Immediately after the Distribution, the gross assets of the active business conducted by each of Y1 Corp, X1 Corp, X2 Corp and X3 Corp (as defined in section 355(b)(2)) will, in each case, have a fair market value that is at least 5 percent of the total fair market value of that corporation's assets.
- (s) Following the Distribution, Y1 Corp, X1 Corp, X2 Corp and X3 Corp will each continue the active conduct of its business, independently and with its separate employees.
- (t) The distribution of Controlled is primarily carried out for the corporate business purpose of improving Controlled's financing structure, including its ability to effectively and efficiently raise a significant amount of capital on more favorable terms including raising capital in an IPO. The Distribution is motivated, in whole or substantial part, by this corporate business purpose.
- (u) There is no plan or intention by any shareholder who owns 5 percent or more of the stock of Distributing, and the management of Distributing, to its best knowledge, is not aware of any plan or intention on the part of any remaining shareholder or security holder to sell, exchange, transfer by gift or otherwise dispose of any of their stock in, or securities of, either Distributing or Controlled after the Distribution.
- (v) 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 section 4.05(1)(b) of Rev. Proc. 96-30. However, prior to the Distribution, Distributing may acquire shares of its own stock using the proceeds of the loan it intends to obtain together with any money that may be transferred to it by Controlled and representing the proceeds of Controlled's intended third party borrowing.
- (w) 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.
- (x) Distributing, Controlled, and their respective shareholders will each pay their own expenses, if any, incurred in connection with the Distribution.
- (y) No Distributing shareholder or shareholders will hold immediately after the Distribution disqualified stock within the meaning of section 355(d)(3), which

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constitutes a 50 percent or greater interest in Distributing or Controlled.

- (z) For purposes of section 355(d), immediately after the Distribution, no person (determined after applying section 355(d)(7)) will hold stock possessing 50 percent or more of the total combined voting power or 50 percent or more of the total value of shares of all classes of Distributing stock, that was acquired by purchase (as defined in section 355(d)(5) and (8)) during the five year period (determined after applying section 355(d)(6)) ending on the date of the Distribution.
- (aa) For purposes of section 355(d), immediately after the Distribution, no person (determined after applying section 355(d)(7)) will hold stock possessing 50 percent or more of the total combined voting power or 50 percent or more of the total value of shares of all classes of Controlled stock, that was acquired by purchase (as defined in section 355(d)(5) and (8)) during the five year period (determined after applying section 355(d)(6)) ending on the date of the Distribution.
- (bb) The Distribution is not a part of a plan or series of related transactions (within the meaning of section 355(e)), pursuant to which one or more persons will acquire directly or indirectly stock possessing fifty percent or more of the total combined voting power of all classes of stock of either Distributing or Controlled, or stock possessing fifty percent or more of the total value of all classes of stock of either Distributing or Controlled.

Based solely on the information submitted and the representations made, we have concluded that:

- (1) The transfer by Distributing of the stock of DSub3, DSub10 through DSub16, X3 Corp, as well as some assets, to Controlled in exchange for all of the Controlled voting common stock and the assumption by Controlled of certain liabilities, followed by the pro rata distribution by Distributing of all of the Controlled stock to the Distributing shareholders, will constitute a reorganization within the meaning of section 368(a)(1)(D) of the Internal Revenue Code. 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 upon its receipt of Controlled stock in exchange for the transfer of assets to, and the assumption of liabilities by, Controlled. Section 361(a) and (b)(1) and section 357(a).
- (3) No gain or loss will be recognized by Controlled upon its receipt of assets in exchange for its issuance of shares of Controlled stock. Section 1032(a).

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- (4) Controlled's basis in the assets received from Distributing will equal the basis of such asset in the hands of Distributing immediately prior to the transfer. Section 362(b).
- (5) The holding period of each asset received by Controlled from Distributing will include the period during which Distributing held such asset. Section 1223(2).
- (6) Distributing will not recognize gain or loss upon the Distribution of the stock in Controlled to the Distributing shareholders. Sections 355(c), 355(d), 355(e), and 361(c)(1).
- (7) No gain or loss will be recognized to (and no amounts will be included in the income of) the Distributing shareholders upon their receipt of Controlled stock. Section 355(a)(1).
- (8) The aggregate basis of the Distributing stock and the Controlled stock in the hands of the Distributing shareholders after the Distribution will equal the aggregate adjusted basis of the Distributing stock held immediately before the Distribution, allocated in proportion to the fair market value of each under Treas. Reg. section 1.358-2(a)(2).
- (9) The holding period of the Controlled stock received by the Distributing shareholders will, in each instance, include the holding period of the Distributing stock with respect to which the Distribution will be made, provided that the Distributing stock is held as a capital asset on the day of the Distribution. Section 1223(1).
- (10) As provided in section 312(h), proper allocation of earnings and profits between Distributing and Controlled will be made in accordance with Treas. Reg. sections 1.312-10(a) and 1.1502-33.
- (11) The payment of cash in lieu of fractional shares of Controlled common stock will be treated for Federal income tax purposes as if the fractional shares were distributed as part of the Distribution and then sold. Any gain or loss will be treated as capital gain or loss, provide such fractional shares of stock will be held as capital assets on the date of the Distribution. Rev. Proc. 77-41, 1971-2 C.B. 574, Section 1221 and 1222.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. In particular, no opinion is expressed concerning the tax consequences of steps (2) - (5).

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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.

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

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

Sincerely,

Reginald Mombrun _____

Reginald Mombrun
Assistant to the Branch Chief, Branch 6
Office of Associate Chief Counsel
(Corporate)