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Distributing =

State A =

Shareholder A =

Shareholder B =

Controlled =

Business A =

Supplier =

Dear :

This letter responds to a letter dated July 21, 2003, requesting rulings concerning the federal income tax consequences of a proposed transaction. The information submitted in that and subsequent correspondence is summarized below.

Distributing, a State A corporation, is a C corporation that uses the accrual method of accounting and a January 31 year end. Distributing is primarily engaged in Business A. Distributing has outstanding common stock, 50 percent held by

Shareholder A and 50 percent held by Shareholder B. Shareholders A and B have been engaged in both the managerial and operational activities of Distributing for many years.

Controlled, a State A corporation, uses the accrual method of accounting and a calendar year. Controlled has outstanding solely a single class of common stock. At present, 80 percent of the outstanding stock in Controlled is held by Distributing, and 20 percent is held by Shareholder B. Directly, and through Distributing, Shareholders A and B have been engaged in both the managerial and operational activities of Controlled for many years. Distributing has submitted financial and employee information that indicates that both Distributing and Controlled had gross receipts and operating expenses representative of the active conduct of a trade or business for each of the past 5 years.

Shareholders A and B have substantial differences as to how the businesses of Distributing and Controlled should be run. It is now desired to separate Distributing and Controlled for the purpose of eliminating management conflict. Distributing's management believes the separation of Distributing and Controlled will enable the two companies to function more effectively as a result of each having its own consistent business strategy.

The parties intend to undertake the following transaction:

> Distributing will distribute all the Controlled stock it holds (80% of all the outstanding stock in Controlled) to Shareholder B in exchange for the surrender by Shareholder B of all his stock in Distributing. (Following this transaction, Shareholder A will own all the outstanding stock in Distributing and Shareholder B will own all the outstanding stock in Controlled.)

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

(a) Distributing, Controlled, and each of the shareholders will each pay their own expenses in the transaction.

(b) The fair market value of the Controlled stock received by Shareholder B will approximately equal the fair market value of the Distributing stock surrendered by Shareholder B in exchange therefor.

(c) No part of the Controlled stock received by Shareholder B is being received by Shareholder B as a creditor, employee, or in any capacity other than that of a shareholder of Distributing.

(d) The 5 years of financial information submitted on behalf of Distributing and Controlled with regard to each corporation's Business A is representative of that corporation's present operations and, for each corporation, there has been no substantial operational changes since the date of the last financial statements submitted.

(e) Following the transaction, Distributing and Controlled will each continue, independently and with its own separate employees, the active conduct of its Business A

(f) The distribution of Controlled stock is being undertaken for the corporate business purposes of ending the present management disagreements and achieving a consistent business strategy for both Distributing and Controlled. The distribution of Controlled stock is motivated in substantial part by these business purposes.

(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 transaction, 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 by either Shareholder A or Shareholder B to sell, exchange, transfer by gift or otherwise dispose of any of their stock in either Distributing or Controlled after the proposed transaction.

(i) 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, except for dispositions in the ordinary course of business.

(j) No intercorporate debt will exist between Distributing and Controlled at the time of the proposed transaction, or subsequent thereto, except for any temporary accounts payable that may arise in the course of routine business transactions between the companies.

(k) Once the proposed transaction is consummated, it is not anticipated that any substantial business transactions will occur between Distributing and Controlled. However, with regard to any inter-company transactions that do occur, all payments between Distributing and Controlled will be for fair market value based on terms and conditions arrived at by the parties bargaining at arms length.

(l) Immediately after the distribution, no person will hold, directly or indirectly, disqualified stock, (within the meaning of § 355(d)(3)) in Distributing or Controlled that constitutes a 50 percent or greater interest (within the meaning of § 355(d)(4)) in Distributing or Controlled.

(m) The proposed transaction is not part of a plan or series of related transactions (within the meaning of § 355(e)) pursuant to which one or more persons will acquire, directly or indirectly, stock representing a 50 percent or greater interest (as defined in § 355(d)(4)) in Distributing or Controlled.

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

(1) No gain or loss will be recognized to Distributing upon the distribution to Shareholder B of 80% of the stock in Controlled (§ 361(c)(1)).

(2) No gain or loss will be recognized to (and no amount will be included in the income of) Shareholder B upon the receipt of Controlled stock (§ 355(a)).

(3) The basis of the Controlled stock received by Shareholder B will be equal to the basis of the Distributing stock surrendered in exchange therefor (§ 358(a)(1)).

(4) The holding period of the Controlled stock received by Shareholder B will include the period during which such shareholder held the Distributing stock exchanged therefor, provided that the Distributing stock is a capital asset in the hands of the shareholder on the date of the exchange (§ 1223(1)).

(5) As provided in § 312(h), proper allocation of earnings and profits between Distributing and Controlled will be made under § 1.312-10(b) of the Income Tax Regulations.

No opinion is expressed about the tax treatment of the proposed transaction under other provisions of the Code and regulations or about the tax treatment of any conditions existing at the time of, or effects resulting from, the transaction that are not specifically covered by the above rulings.

This ruling is directed only to the taxpayers who requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with a power of attorney on file in this office, a copy of this letter is being sent to the taxpayer's representative.

It is important that a copy of this letter be attached to the federal income tax returns of the taxpayers involved for the taxable year in which the transaction covered by this letter is consummated.

Sincerely,

_*Debra L. Carlisle*________
Debra L. Carlisle
Chief, Branch 5
Office of Associate Chief Counsel
(Corporate)

cc: