

**Internal Revenue Service**

Department of the Treasury

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Person to Contact:

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Refer Reply To:

CC:TEGE:EB:QP2- PLR-106104-03

Date:

June 12, 2003

LEGEND

Taxpayer =

Company =

ESOP =

X Shares =

Dear :

This responds to your letter requesting a ruling, under the facts described below, that the reporting of purchases of qualified replacement property filed with Taxpayer's 2002 income tax return will be treated as having substantially complied with the requirements of section 1.1042-1T of the Temporary Income Tax Regulations in connection with the sale of stock of the Company to the employee stock ownership plan (ESOP) maintained by the Company.

Taxpayer is an individual filing an income tax return on a calendar year basis.

We will assume for purposes of this ruling request that common stock of the Company constitutes qualified securities within the meaning of section 1042(c)(1) of the Code and that the ESOP is qualified under section 401(a) and meets the requirements of section 4975(e)(7).

On October 3, 2001, Taxpayer sold X shares of common stock of the Company to the ESOP. As a result of the sale, Taxpayer realized a gain.

Taxpayer represents that when the 2001 income tax return was filed, he attached a statement electing nonrecognition treatment under section 1042 as well as a statement of consent pursuant to section 1042(b) signed by the President of the Company whereby the Company agreed to be bound by the terms of sections 4978 and 4979A.

Taxpayer arranged for a large investment bank to acquire qualified replacement property on his behalf and to manage the resulting portfolio for him. However, Taxpayer had difficulty obtaining timely information from the investment bank during the replacement period. At one point, the investment bank refused to provide a list of the required information. Taxpayer moved his account from the investment bank to a local stock broker who provided the information required for the statements of purchase. Taxpayer made 276 purchases of qualified replacement property during the qualified replacement period. The statement of purchase containing individual information for each of these purchases was signed by the Taxpayer and notarized within 30 days of the final purchase of qualified replacement property. The notarized statement of purchase was filed with the Taxpayer's timely filed 2002 income tax return.

You have requested a ruling that, based on the specific facts of this case, the reporting of purchases of qualified replacement property filed with Taxpayer's 2002 income tax return will be treated as substantially complying with the notarized statement of purchase requirement of section 1.1042-1T, A-3(b) and (c) of the Temporary Income Tax Regulations.

Section 1042(a) of the Code provides that a taxpayer or executor may elect in certain cases not to recognize long-term capital gain on the sale of "qualified securities" to an ESOP (as defined in section 4975(e)(7)) or eligible worker owned cooperative if the taxpayer purchases "qualified replacement property" (as defined in section 1042(c)(4)) within the replacement period of section 1042(c)(3) and the requirements of section 1042(b) and section 1.1042-1T of the Temporary Income Tax Regulations are satisfied.

A sale of "qualified securities" meets the requirements of section 1042(b) if: (1) the qualified securities are sold to an ESOP (as defined in section 4975(e)(7)), or an eligible worker owned cooperative; (2) the plan or cooperative owns (after application of 318(a)(4)), immediately after the sale, at least 30 percent of - a) each class of outstanding stock of the corporation (other than stock described in section 1504(a)(4)) which issued the securities, or (b) the total value of all outstanding stock of the corporation (other than stock described in section 1504(a)(4)); (3) the taxpayer files with the Secretary a verified written statement of the employer whose employees are covered by the ESOP or an authorized officer of the cooperative consenting to the application of section 4978 and 4979A with respect to such employer or cooperative; and (4) the taxpayer's holding period with respect to the qualified securities is at least 3 years (determined as of the time of the sale).

Section 1042(c)(1) provides that the term "qualified securities" means employer securities (as defined in section 409(l)) which are issued by a domestic C corporation that has no stock outstanding that is readily tradable on an established securities

market; and

were not received by the taxpayer in a distribution from a plan described in section 401(a), or in a transfer pursuant to an option or other right to acquire stock to which section 83, 422 or 423 applied.

The taxpayer must purchase "qualified replacement property" within the "replacement period" which is defined in section 1042(c)(3) as the period which begins 3 months before the date on which the sale of qualified securities occurs and ends 12 months after the date of such sale.

Section 1042(c)(4)(A) defines "qualified replacement property" (QRP) as any security issued by a domestic operating corporation which did not, for the taxable year preceding the taxable year in which such security was purchased, have passive investment income (as defined in section 1362(d)(3)(D)) in excess of 25 percent of the gross receipts of such corporation for such preceding taxable year; and is not the corporation which issued the qualified securities which such security is replacing or a member of the same controlled group of corporations (within the meaning of section 1563(a)(1)) as such corporation.

Section 1.1042-1T (Q&A-3) of the Temporary Income Tax Regulations states that the election shall be made in a "statement of election" attached to the taxpayer's income tax return filed on or before the due date (including extensions of time) for the taxable year in which the sale occurs.

Section 1.1042-1T (Q&A-3) of the Temporary Income Tax Regulations states that the "statement of election" shall provide that the taxpayer elects to treat the sale of securities as a sale of qualified securities under section 1042(a), and shall contain the following information:

- (1) A description of the qualified securities sold, including the type and number of shares;
- (2) The date of the sale of the qualified securities;
- (3) The adjusted basis of the qualified securities;
- (4) The amount realized upon the sale of the qualified securities;
- (5) The identity of the ESOP or worker-owned cooperative to which the qualified securities were sold;
- (6) If the sale was part of a single interrelated transaction under a prearranged agreement between taxpayers involving other sales of qualified securities, the names and taxpayer identification numbers of the other taxpayers under the agreement and the number of shares sold by the other taxpayers.

Section 1.1042-1T (Q&A-3) of the Temporary Income Tax Regulations further provides that if the taxpayer has purchased qualified replacement property at the time of the election, the taxpayer must attach as part of the statement of election a "statement of purchase" describing the qualified replacement property, the date of the purchase, and the cost of the property, and declaring such property to be qualified replacement property with respect to the sale of qualified securities. The statement of purchase must be notarized no later than 30 days after the purchase.

With respect to the present ruling request, Taxpayer had difficulty obtaining the required information from the investment bank originally entrusted with making purchases of qualified replacement property. After moving the investments to another stock broker Taxpayer was able to obtain the required information. All purchases of QRP were made within the qualified replacement period with respect to the ESOP sale. The statement of purchase encompassing information on all the purchases was notarized within 30 days of the date of the final purchase of QRP.

Therefore, based on the specific facts of this case and representations made by the Taxpayer, we conclude that the filing of the notarized statement of purchase as described above with the Taxpayer's 2002 income tax return will be treated as substantially complying with the notarized statement of purchase requirement of section 1.1042-1T, A-3(b) and (c) of the Temporary Income Tax Regulations.

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.

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.

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

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 yours,

Robert D. Patchell  
Chief, Qualified Plans Branch 2  
Division Counsel/Associate Chief Counsel  
(Tax Exempt and Government Entities)

Enclosures:

Copy for 6110 purposes

CC: