

**Internal Revenue Service**

Number: **200545001**

Release Date: 11/10/2005

Index Numbers: 368.04-00, 355.01-00

Department of the Treasury

Washington, DC 20224

Third Party Communication: None

Date of Communication: Not Applicable

Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:CORP:4

PLR-104686-05

Date:

August 12, 2005

LEGEND:

Distributing =

Controlled =

Group Parent =

FSub 1 =

FSub 2 =

Domestic Parent =

Target Holdco =

Business A =  
Date 1 =  
Date 2 =  
Date 3 =  
State A =  
State B =  
State C =  
State D =  
State E =  
State F =  
a =  
b =  
c =  
d =  
e =  
f =  
g =  
h =

Dear :

This letter responds to your January 20, 2005 letter requesting rulings on certain federal income tax consequences of a completed transaction. The information provided in that letter and in later correspondence is summarized below.

The rulings contained in this letter are based on facts and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. This office has not verified any of the material submitted in support of the request for rulings. Verification of the information, representations, and other data may be required as part of the audit process. Moreover, this office has not reviewed any information pertaining to, and has made no determination regarding, whether the Distribution (described below): (i) satisfies the business purpose requirement of § 1.355-2(b) of the Income Tax Regulations; (ii) is used principally as a device for the distribution of earnings and profits of the distributing corporation or the controlled corporation or both (see § 355(a)(1)(B) of the Internal Revenue Code and § 1.355-2(d)); and (iii) is part of a plan (or series of related transactions) pursuant to which one or more persons will acquire directly or indirectly stock representing a 50-percent or greater interest in the distributing corporation or the controlled corporation (see § 355(e) and § 1.355-7).

### Summary of Facts

Group Parent (a foreign corporation) is the common parent of a corporate group composed of various domestic and foreign corporations engaged in Business A. Group Parent wholly owns FSub 1, which has conducted Business A directly since Date 1. FSub 1 wholly owns FSub 2. FSub 2 wholly owns Domestic Parent.

Domestic Parent is a domestic holding company and the common parent of an affiliated group of corporations that files a consolidated federal income tax return. Domestic Parent conducts Business A indirectly through subsidiaries.

Before Date 2, Distributing was wholly owned by Target Holdco. On Date 2, Domestic Parent acquired all of the outstanding stock of Distributing (except for certain shares owned by directors of Distributing described below) in a two-step transaction. First, Domestic Parent formed a wholly-owned subsidiary which merged into Target Holdco ("Merger 1"). In Merger 1, Target Holdco's shareholders received cash in exchange for their Target Holdco stock and Target Holdco became a wholly owned subsidiary of Domestic Parent. Second, Target Holdco merged into Domestic Parent ("Merger 2"). The taxpayer treated Merger 1 as an acquisition of the stock of Target Holdco for cash and Merger 2 as a liquidation of Target Holdco under § 332. Following Merger 2 and immediately before the Distribution, Domestic Parent owned a shares (representing approximately b percent) of Distributing's voting common stock, its sole class of stock outstanding ("Distributing Common Stock"). The remaining c shares (representing approximately d percent) of Distributing Common Stock were owned by directors of Distributing in satisfaction of certain non-tax federal law requirements.

Distributing directly conducts Business A, principally through offices located in States A, B, C, D, E and F. Domestic Parent believes that the transfer of Distributing's

Business A located in States E and F into a separate organization will permit Domestic Parent to replicate its successful model of regionally focused and managed operations.

Financial information has been received indicating that Business A (as conducted by FSub 1) has had gross receipts and operating expenses representing the active conduct of a trade or business for each of the past five years.

### **Completed Transaction**

To effect the separation of Distributing's Business A located in States A, B, C, and D from Distributing's Business A located in States E and F, the following transaction was completed on Date 3:

(i) Distributing contributed its Business A assets located in States E and F and cash in the amount of approximately \$e to newly formed Controlled in exchange for all of Controlled's common stock (the "Controlled Common Stock"), all of Controlled's Preferred Stock (the "Controlled Preferred Stock") and Controlled's assumption of the liabilities of the transferred business (the "Contribution"). Taxpayer represents that the Controlled Preferred Stock is not nonqualified preferred stock within the meaning of § 351(g)(2). Distributing immediately transferred f shares of its Controlled Preferred Stock (representing approximately g percent of the Controlled Preferred Stock outstanding) directly to the five initial members of Controlled's board of directors to satisfy certain non-tax federal law requirements (the "Preferred Stock Transfer").

(ii) Immediately after the Contribution and the Preferred Stock Transfer, Distributing distributed to Domestic Parent all of its Controlled Common Stock and all of its Controlled Preferred Stock (the "Distribution"). No securities or other property of Controlled was distributed in the Distribution. It is expected that the number of directors of Controlled will increase and that each new director will be granted h shares of Controlled Preferred Stock, which will reduce the percentage of Controlled Preferred Stock held by Domestic Parent, but not below 80 percent.

Following the Distribution, Distributing has continued to conduct Business A in States A, B, C, and D, and Controlled has conducted the Business A formerly conducted by Distributing in States E and F.

### **Representations**

The taxpayer has made the following representations regarding the Contribution and the Distribution:

(a) Any indebtedness owed by Controlled to Distributing after the Distribution did not constitute stock or securities.

(b) No part of the consideration distributed by Distributing was received by a shareholder as a creditor, employee, or in any capacity other than that of a shareholder of the corporation.

(c) The five years of financial information submitted on behalf of Business A (as conducted by FSub 1) is representative of the corporation's present operation, and with regard to such corporation, there have been no substantial operational changes since the date of the last financial statements submitted.

(d) Following the transaction, Distributing and Controlled have each continued, independently and with its separate employees, the active conduct of its share of all the integrated activities of the business conducted by Distributing before consummation of the transaction.

(e) The Distribution was carried out for the following corporate business purposes: to more easily align the business of, and marketing efforts associated with, Distributing's Business A located in States E and F with the highly successful regional management and marketing strategy that Domestic Parent's corporate group currently employs. The Distribution was motivated, in whole or substantial part, by one or more of these corporate business purposes.

(f) The transaction was not used principally as a device for the distribution of the earnings and profits of Distributing or Controlled or both.

(g) The total adjusted basis and the fair market value of the assets transferred to Controlled by Distributing in the Contribution each equaled or exceeded the sum of the liabilities assumed (as determined under § 357(d)) by Controlled.

(h) The liabilities assumed (as determined under § 357(d)) by Controlled in the Contribution were incurred in the ordinary course of business and were associated with the assets transferred.

(i) No intercorporate debt existed between Distributing and Controlled at the time of, or after, the Distribution. However, Distributing and Controlled may engage in certain transactions that are customary between affiliated corporations engaged in Business A.

(j) Immediately before the Distribution, items of income, gain, loss, deduction, and credit were taken into account as required by the applicable intercompany transaction regulations (see § 1.1502-13 and § 1.1502-14 as in effect before the publication of T.D. 8597, 1995-2 C.B. 147, and as currently in effect; § 1.1502-13 as published by T.D. 8597). At the time of the Distribution, Distributing did not have an excess loss account in the Controlled stock.

(k) Payments made in connection with all continuing transactions, if any, between Distributing and Controlled have been and will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.

(l) No two parties to the transaction are investment companies as defined in § 368(a)(2)(F)(iii) and (iv).

(m) None of the shares of Controlled Preferred Stock distributed in the Distribution were nonqualified preferred stock (as defined in § 351(g)(2)).

(n) For purposes of § 355(d), immediately after the Distribution, no person (determined after applying § 355(d)(7)) held stock possessing 50 percent or more of the total combined voting power of all classes of Distributing stock entitled to vote 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 § 355(d)(5) and (8) and by application of § 1.355-6(b)(2)(iii)) during the five-year period (determined after applying § 355(d)(6)) ending on the date of the Distribution.

(o) For purposes of § 355(d), immediately after the Distribution, no person (determined after applying § 355(d)(7)) held stock possessing 50 percent or more of the total combined voting power of all classes of Controlled stock entitled to vote or 50 percent or more of the total value of shares of all classes of Controlled stock that was either (i) acquired by purchase (as defined in § 355(d)(5) and (8)) during the five-year period (determined after applying § 355(d)(6)) ending on the date of the Distribution, or (ii) attributable to distributions on Distributing stock that was acquired by purchase (as defined in § 355(d)(5) and (8)) during the five-year period (determined after applying § 355(d)(6)) ending on the date of the Distribution.

(p) Pursuant to § 355(e)(2)(C), the Distribution was not part of a plan or series of related transactions (within the meaning of § 1.355-7) pursuant to which one or more persons will acquire directly or indirectly stock representing a 50-percent or greater interest (within the meaning of § 355(d)(4)) in Distributing or Controlled (including any predecessor or successor of any such corporation).

### **Rulings**

Based solely on the information submitted and the representations made, we rule as follows on the Contribution and the Distribution:

(1) The Contribution, followed by the Distribution, qualified as a reorganization under § 368(a)(1)(D). Distributing and Controlled were each a "party to a reorganization" under § 368(b).

(2) No gain or loss was recognized by Distributing on the Contribution (§§ 357(a) and 361(a)).

(3) No gain or loss was recognized by Controlled on the Contribution (§ 1032(a)).

(4) The basis of each asset received by Controlled in the Contribution equals the basis of that asset in the hands of Distributing immediately before its transfer (§ 362(b)).

(5) The holding period of each asset received by Controlled in the Contribution will include the period during which Distributing held that asset (§ 1223(2)).

(6) No gain or loss was recognized by Distributing on the Distribution (§ 361(c)).

(7) No gain or loss was recognized by (and no amount will otherwise be included in the income of) Domestic Parent on its receipt of Controlled stock in the Distribution (§ 355(a)(1)).

(8) The aggregate basis of the Distributing stock and the Controlled stock in the hands of Domestic Parent after the Distribution will equal the aggregate basis of the Distributing stock held by Domestic Parent immediately before the Distribution, allocated between the stock of Distributing and Controlled in proportion to the relative fair market value of each immediately following the Distribution in accordance with § 1.358-2(a)(2) (§ 358(b) and (c)).

(9) The holding period of the Controlled stock received by Domestic Parent in the Distribution includes the holding period of the Distributing stock on which the Distribution was made, provided the Distributing stock was held as a capital asset on the date of the Distribution (§ 1223(1)).

(10) Earnings and profits, if any, will be allocated between Distributing and Controlled in accordance with §§ 312(h) and 1.312-10(a).

### **Caveats**

We express no opinion about the tax treatment of any transaction described above under other provisions of the Code and regulations or the tax treatment of any condition existing at the time of, or effects resulting from, the completed transaction that are not specifically covered by the above rulings. In particular, no opinion is expressed regarding: (i) whether the Distribution satisfied the business purpose requirement of § 1.355-2(b); (ii) whether the transaction was used principally as a device for the distribution of the earnings and profits of Distributing or Controlled or both (see § 355(a)(1)(B) and § 1.355-2(d)); (iii) whether the Distribution and an acquisition or acquisitions are part of a plan (or series of related transactions) under § 355(e)(2)(A)(ii); (iv) whether the Controlled Preferred Stock is § 306 stock; and (v) the Preferred Stock Transfer.

**Procedural Matters**

This ruling letter 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.

Each taxpayer involved in this transaction should attach a copy of this ruling letter to the taxpayer's federal income tax return for the taxable year in which the transaction was completed.

Under the power of attorney on file in this office, a copy of this letter is being sent to your authorized representatives.

Sincerely,

---

Richard K. Passales  
Senior Counsel, Branch 4  
Office of Associate Chief Counsel  
(Corporate)