

Rev. Proc. 96-30

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### SECTION 1. PURPOSE

This revenue procedure updates Rev. Proc. 86-41, 1986-2 C.B. 716, which sets forth in a checklist questionnaire the information that must be included in a request for rulings under § 355, relating to the nonrecognition of gain or loss on distributions of stock and securities of controlled corporations.

### SECTION 2. BACKGROUND

This checklist is intended to facilitate the filing and processing of ruling requests under § 355. It specifies information and representations to be included so that the requests will be as complete as possible when initially filed. Nevertheless, because the information and representations necessary to rule on a particular transaction depend upon all the facts and circumstances, the Service may require information or representations in addition to those set forth in this revenue procedure.

The general procedures of the Internal Revenue Service with respect to the issuance of letter rulings and determination letters by the National Office are outlined in the first revenue procedure published each year (the “**annual revenue procedure**”). *See, e.g.*, Rev. Proc. 96–1, 1996–1 I.R.B. 8. The Service also publishes a revenue procedure, generally in the first Internal Revenue Bulletin of the year, which provides a list of those areas of the Code under the jurisdiction of the Associate Chief Counsel (Domestic) for which the Service will not issue advance letter rulings. *See, e.g.*, Rev. Proc. 96–3, 1996–1 I.R.B. 82. The Service periodically updates these revenue procedures, along with this checklist questionnaire.

Careful attention to all requirements of the most recent revenue procedures, including this checklist questionnaire, will aid in the timely processing of ruling requests. Failure to submit the requisite information and representations will often delay consideration of the transaction and the issuance of a letter ruling.

This revenue procedure substantially modifies Rev. Proc. 86–41. The principal changes are to add to, delete, or modify the information and representations requested, and to add an appendix that provides guidelines with respect to ruling requests involving certain corporate business purposes. This document also revokes section 3.01(23) of Rev. Proc. 96–3, which sets forth “no rule” positions regarding certain corporate business purposes.

This section describes the information and representations to be provided in a § 355 ruling request. The presentation of the information and representations in the ruling request should follow the organization of this section and use appropriate descriptive headings. Taxpayers are welcome to provide a narrative description of the transaction to supplement (but not substitute for) the presentation requested in this section.

A ruling request should address each item in this section and provide all facts relevant to the transaction. If an item is not applicable, so state and briefly explain why.

Standard representations are set forth throughout this section and are highlighted by the word “representation” in boldface type. The representations are necessary to ensure that specific statutory and judicial requirements, and administrative ruling guidelines relating thereto, are satisfied. Each representation should be submitted in the language requested. If a representation cannot be submitted exactly as requested, an explanation must be given. Deviation from the language of the representations should be avoided, except as required by the facts being described. Unnecessary variations may delay processing the ruling request and will not be accepted unless reasons satisfactory to the Service are submitted.

The terms “**Distributing**” and “**Controlled**” in this document refer to the “**distributing corporation**” and “**controlled corporation**” as described in § 355(a)(1)(A). References to the term “**distribution**” include a distribution of stock or securities of Controlled with respect to Distributing stock, an exchange of Distributing stock or securities for Controlled stock or securities, or some combination thereof, as the context requires.

Requests for information and representations regarding Distributing or Controlled include, as the context requires, a request for information (or representations) regarding a successor of Distributing or Controlled. For example, if Distributing will merge with an acquiring corporation after the distribution, the representation requested in section 4.03(8) of this revenue procedure (that is, Distributing will continue to conduct its business) should be modified to include a similar representation under penalties of perjury by the acquiring corporation regarding the continuing conduct of Distributing’s business after the merger, in addition to Distributing’s representation. Similarly, the representation requested in section 4.05(1) of this revenue procedure (that is, there is no plan or intention by the Distributing shareholders to dispose of their shares in Distributing), should be modified to include a similar representation regarding dispositions of acquiring corporation shares by the Distributing shareholders. If a taxpayer believes that information regarding, or a representation by, a successor is inappropriate or should be modified, the taxpayer must explain why.

.01

(1) **Identification.** State the name, employer identification number, and place and date of incorporation of Distributing and Controlled. If Controlled is not in existence, state its proposed name and place of incorporation. If Distributing joins in the filing of a consolidated federal income tax return, provide the name and employer identification number of the common parent corporation of the affiliated group.

(2) **Jurisdiction.** Identify the District Office that has or will have examination jurisdiction over the return of Distributing (sometimes referred to below as the “**taxpayer**”) and of Controlled.

(3) **Taxable year.** State the last day of the taxable year of Distributing and Controlled.

.02

(1) **Capital structure of Distributing and Controlled immediately prior to the distribution.**

### SECTION 3. CHANGES

### SECTION 4. INFORMATION TO BE INCLUDED IN REQUESTS FOR RULINGS UNDER § 355

Distribution includes exchanges

Successors of Distributing or Controlled

Information regarding Distributing and Controlled

Ownership of interests in Distributing and Controlled

Under a separate heading for each corporation, provide the following information with respect to the stock and securities of Distributing and Controlled that will be outstanding immediately prior to the distribution:

**Description of stock**

(a) A complete description of each class of stock, setting forth the rights and privileges of each class, including voting or nonvoting rights, dividend and liquidation preferences or limitations, and whether classified as common or preferred stock.

**Shareholdings**

(b) A list of the number of shares and the percentage of each class of stock owned by each shareholder prior to the distribution. However, if the corporation has more than 100 shareholders, the taxpayer need only list those shareholders owning 5 percent or more of any class of stock, and state the total number of other shareholders together with the total number of shares and the percentage that these other shareholders own of each class of stock.

**Description of agreements**

(c) A description of any existing, planned, or intended agreements, such as a voting trust, affecting the rights of any shareholder. However, if the corporation has more than 100 shareholders, the taxpayer need only describe agreements affecting shareholders owning directly, or as a result of the agreement, controlling, 5 percent or more of any class of stock.

**Description of securities**

(d) A description of any securities and all other outstanding interests (bonds, debentures, notes, warrants, options, puts, etc.) and a brief explanation as to whether any of these items should be considered a stock interest.

**Foreign shareholders**

**(2) Foreign shareholders.** If Distributing has any foreign shareholders, state whether: (i) Distributing or Controlled was a United States real property holding corporation (as defined in § 897(c)(2)) at any time during the 5-year period ending on the date of the distribution, and (ii) Distributing or Controlled will be a United States real property holding corporation immediately after the distribution. *See* § 367(e)(1) and § 897. In addition, if Distributing is publicly traded, provide a list of all foreign persons owning 5 percent or more of Distributing stock either before or after the distribution. If Distributing is not publicly traded, provide a list of all foreign persons owning stock of Distributing either before or after the distribution. *See* section 4.08(7) of this revenue procedure for additional information regarding foreign parties.

**Stock, securities, and property being distributed**

**(3) Description of stock, securities, and other property being distributed.**

**(a) Stock.** State the number of shares and percentage of each class of stock of Controlled being distributed. In addition, if preferred stock is being distributed and it is contended that this stock is not “section 306 stock,” within the meaning of § 306(c), fully explain the reasons for this contention.

**(b) Securities.** State the principal amount of each series of securities of Controlled being distributed.

**(c) Other property.** Provide complete details as to any property, other than stock and securities of Controlled, to be distributed or received in the transaction including, but not limited to, cash, stock rights, warrants, or the payment of expenses incurred in connection with the transaction (*see* § 356).

**Date of distribution**

**(d) Timing.** State the date of the distribution and whether all the stock, securities, and other property will be distributed on that date. If all the stock, securities, and other property are not being distributed on the same date, state the approximate length of, and the reasons for, the delay in the distribution.

**Control**

**(e) Planned stock issuance, etc.** Describe any planned or intended stock issuances, redemptions, or dispositions of Controlled shares. Explain the effect of any of these transactions on the distribution-of-control requirement of § 355(a)(1)(D), and if property is being transferred from Distributing to Controlled, the effect on the control-immediately-after requirement of § 368(a)(1)(D).

**Obtaining control**

**(f) Obtaining control.** State whether Distributing has modified or will modify its ownership of Controlled stock, such as in a recapitalization, within the 5-year period preceding the distribution with the result that Distributing obtained or will obtain control of Controlled, as defined in § 368(c). Provide complete details, including the information requested in section 4.08(8) of this revenue procedure, with respect to such modifications.

**Post-distribution ownership of interests in Controlled by Distributing**

**(4) Ownership of stock and securities in Controlled immediately after the distribution.**

**(a) Interests in Controlled to be held by Distributing** (*see* § 1.355-2(e) of the Income Tax Regulations).

**(i) Retention of stock, securities, or options.** State the number of shares and percentage of each class of stock in, and the principal amount of each series of securities of, Controlled to be held by Distributing after the distribution and the length of time Distributing will hold this interest. Describe any options that Distributing will hold after the distribution to acquire stock in Controlled and the length of time Distributing will hold these options.

Post-distribution ownership of interests in Controlled by shareholders of Distributing

(ii) **Retention of debt.** If Controlled will be indebted to Distributing after the distribution of Controlled stock, submit the following **REPRESENTATION**: *The indebtedness owed by the controlled corporation to the distributing corporation after the distribution of the controlled corporation stock will not constitute stock or securities.*

(iii) **Purpose for Distributing holding stock, securities, or options in Controlled.** If Distributing will hold stock, securities, or options in Controlled after the distribution, explain the reasons therefor and why this should not be viewed as in pursuance of a plan having as one of its principal purposes avoiding federal income tax. See Appendix B of this revenue procedure regarding favorable rulings with respect to the retention of stock, securities, or options. State whether a distribution of all the stock or securities of Controlled would be treated to any extent as a distribution of “other property” under § 356.

(b) **Interests in Controlled to be held by shareholders of Distributing.**

(i) **Distribution or exchange.** State whether the distribution of Controlled stock will be pro rata or non pro rata with respect to the shareholders of Distributing. Fully describe the transaction between Distributing and its shareholders.

(ii) **Stock ownership.** State the number of shares and the percentage of each class of stock outstanding in Distributing and Controlled that will be owned by each shareholder immediately after the distribution. However, if there will be more than 100 shareholders immediately after the distribution, the taxpayer need only list those shareholders who will own 5 percent or more of any class of stock, and state the expected total number of other shareholders together with the expected total number of shares and the expected percentage that these other shareholders will own of each class of stock.

(iii) **Securities.** Identify any shareholders of Distributing receiving securities of Controlled and state the principal amount of each series of securities to be received in the transaction. With respect to each shareholder, state the principal amount of each series of Distributing securities to be surrendered in the transaction, or, if no securities are being exchanged, so state. See § 1.355-2(f)(1).

(iv) **Surrender of stock.** If one or more Distributing shareholders will surrender Distributing stock in the transaction, submit the following **REPRESENTATION**: *The fair market value of the controlled corporation stock and other consideration to be received by each shareholder of the distributing corporation will be approximately equal to the fair market value of the distributing corporation stock surrendered by the shareholder in the exchange.*

Post-distribution ownership of interests in Controlled by security holders of Distributing

(c) **Interests in Controlled to be held by security holders of Distributing.** Identify those security holders of Distributing receiving Controlled stock, the total number of shares of each class of stock being received, and the principal amount of the securities of Distributing being exchanged. Identify those security holders of Distributing receiving securities of Controlled, the principal amount being received by each holder, and the principal amount of the securities of Distributing being exchanged. See § 1.355-2(f)(1). If no securities are being exchanged, so state. If the securities are, or, immediately after the distribution, will be, held by more than 100 security holders, identify only those security holders that will own 5 percent or more of the outstanding shares of any class of Controlled stock or of any outstanding series of Controlled securities immediately after the distribution.

(d) **Receipt of consideration other than with respect to stock or securities.**

(i) **Shareholder in dual capacity.** Submit the following **REPRESENTATION**: *No part of the consideration to be distributed by the distributing corporation will be received by a shareholder as a creditor, employee, or in any capacity other than that of a shareholder of the corporation.*

(ii) **Security holder in dual capacity.** If consideration will be distributed to security holders, submit the following **REPRESENTATION**: *No part of the consideration to be distributed by the distributing corporation will be received by a security holder as an employee or in any capacity other than that of a security holder of the corporation.*

(iii) **Other transfers.** State whether the shareholders or security holders of Distributing will transfer or surrender any property in the transaction other than stock or securities of Distributing. If so, provide full details.

.03

Information concerning the businesses of Distributing and Controlled (see generally § 1.355-3)

(1) **Description of businesses.** Describe each line of business engaged in by Distributing, Controlled, and their respective subsidiaries, whether or not the business will be relied upon to meet the requirements of § 355(b). Note which corporations are engaged in each line of business.

Distributing's Active Businesses

(2) **Distributing's Active Businesses.** Submit a complete description of each trade or business that will be relied upon to meet the requirements of § 355(b) (an “Active Business”), that is conducted directly by Distributing, and that will be retained by Distributing. Provide the following information with respect to each such Active Business:

Employee information

(a) **Active conduct during the preceding 5-year period.** Provide all information necessary to establish that the Active Business is a trade or business that has been actively conducted for the entire 5-year period ending on the date of the distribution (within the meaning of § 1.355-3(b)(2) and (3)). In general, the description should conclusively show that substantial managerial and operational activities have been directly carried on by the Active Business during each of the past 5 years.

(b) **Employee information.** If the Active Business employed fewer than 50 full-time employees during any of the past 5 years, submit separate lists for each of the past 5 years showing the job titles of the Active Business' employees, the function (managerial, operational, or other) of each position, and the number of persons employed in each position. Include a brief description of the type of duties performed by each category of employee during each of these years.

Nonemployee information

(c) **Nonemployee information.** If Distributing is required to submit the employee information specified in section 4.03(2)(b) of this revenue procedure with respect to an Active Business, also state whether Distributing uses persons who are not employees, such as independent contractors. If so, include a brief description of the duties they perform, and the percentage of the activities they perform for the Active Business.

Continuous ownership of Active Businesses conducted during 5-year period

(d) **Continuous ownership of an Active Business during the preceding 5-year period.** State whether the Active Business has been continuously conducted, within the meaning of § 1.355-3(b), by Distributing for the 5-year period ending on the date of distribution. Give the date Distributing commenced conduct of the Active Business or acquired the Active Business. If an Active Business has not been continuously conducted by Distributing for such 5-year period, *see* section 4.03(6) of this revenue procedure.

Change in business during 5-year period

(e) **Change in business.** Describe any substantial change during the preceding 5-year period in the type of business activity conducted or the method of conducting business, such as substantial changes in: products or services offered, production capacity, assets owned or used, technology employed, sales or distribution channels, or locations. If the preceding 5-year period includes any time during which there was no business activity, or a significant amount of time during which there was a substantial reduction in business activity, identify the period of time, the type and amount of business activity during this period, and the reasons for the cessation or reduction in activity.

Separation of real property, intellectual property, or other intangible property from user

(f) **Separation of real property, intellectual property, or other intangible property from user.** State whether all or a portion of any real property, intellectual property, or other intangible property historically occupied or used by one business will be separated in the transaction from that business. If so, describe the property. State whether the business formerly using the property will continue to use the property after the transaction, and the terms upon which it will be allowed to use the property. Describe any other planned use of the property after the transaction. Explain the reason for separating the ownership of the property from its historic user.

Balance sheets

(g) **Balance sheets.** Provide a copy of the most recent balance sheet of Distributing (including all applicable notes). The balance sheet should not be limited to assets and liabilities of Distributing's Active Businesses. Also submit any consolidated balance sheets prepared for financial accounting purposes that include Distributing.

Profit and loss statements

(h) **Profit and loss statements.** Submit separate unconsolidated profit and loss statements (including all applicable notes) for each of the past 5 years for each Active Business. The statements must show that each business has had gross receipts and operating expenses (including employee expenses such as payroll withholding taxes) representative of the active conduct of a trade or business for each of the past 5 years. Submit the following **REPRESENTATION:** *The 5 years of financial information submitted on behalf of the distributing corporation 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.*

Description of Active Businesses transferred to Controlled

(3) **Description of Active Businesses being transferred by Distributing to Controlled.** If, in connection with the plan, Distributing transfers all or part of the assets of one or more of its Active Businesses (*see* § 1.355-3(c), example (4)) to either a newly formed or pre-existing Controlled, identify and submit a complete description of each Active Business or part of an Active Business being transferred. Submit the information and representation required by section 4.03(2)(a) through (h) of this revenue procedure for each such Active Business, or part of an Active Business, being transferred. If property will be transferred from Distributing to Controlled, submit a pro forma balance sheet for Controlled reflecting the transfer of assets to Controlled and all liabilities to be assumed or to which the property transferred will be subject.

Description of pre-existing Controlled's Active Businesses

(4) **Pre-existing Controlled's Active Businesses.** If Controlled is a pre-existing corporation, submit a complete description of each Active Business conducted directly by Controlled.

Submit the information and representation required by section 4.03(2)(a) through (h) of this revenue procedure with respect to each such Active Business, treating references to Distributing as references to Controlled, as appropriate.

Indirect conduct of trade or business

(5) **Indirect conduct of trade or business through ownership of stock in other corporations.** If either Distributing or Controlled is not directly engaged in an Active Business but will be so engaged indirectly through ownership of stock and securities in one or more corporations controlled by it (“**Other Corporations**”) immediately after the distribution, submit the information and representation required by sections 4.03(2)(a) through (h) of this revenue procedure (treating, for this purpose, each Other Corporation as Distributing or Controlled, as appropriate). In addition, if Distributing or Controlled is not directly engaged in an Active Business, submit the following **REPRESENTATION**: *Immediately after the distribution, at least 90 percent of the fair market value of the gross assets of [insert the name of the corporation so indirectly engaged] will consist of the stock and securities of controlled corporations that are engaged in the active conduct of a trade or business as defined in § 355(b)(2). See section 3.04 of Rev. Proc. 77–37, 1977–2 C.B. 568, 570.*

Active Businesses acquired during 5-year period

(6) **Changes in ownership of an Active Business during the 5-year period ending on the date of distribution.** If an Active Business that is directly conducted by Distributing, Controlled, or an Other Corporation has been acquired by that corporation during the 5-year period ending on the date of distribution, identify the Active Business that was acquired and provide the following information with respect to that Active Business:

(a) **Identity.** Identify the party from whom the business was acquired, and the transferor’s relationship, if any, to Distributing or its shareholders.

(b) **Date.** State the date the business was acquired and the period of time the business had been previously conducted by Distributing’s, Controlled’s, or Other Corporation’s predecessor in interest.

(c) **Transaction.** Describe the transaction in which the business was acquired. For example, was the business acquired in a reorganization under § 368(a)(1), by purchase, or by some other means? If a letter ruling was issued with respect to the transaction, attach a copy.

(d) **Consideration.** State the consideration given in the acquisition.

(e) **Gain or loss.** State whether gain or loss was recognized, in whole or in part, to any party to the transaction and whether the basis of the assets acquired was determined, in whole or in part, by reference to the transferor’s basis.

(7) **Stock ownership during the preceding 5-year period (see § 355(b)(2)(D)).**

Stock continuously owned during 5-year period

(a) **Stock of Controlled or Other Corporations continuously owned during the preceding 5-year period.** Identify Controlled and Other Corporations whose shares have been continuously held by Distributing or Controlled for the 5-year period ending on the date of distribution.

(b) **Stock of Controlled or Other Corporations acquired by Distributing, Controlled, or Other Corporations during the preceding 5-year period.** If the stock of Controlled or Other Corporations has been acquired by Distributing, Controlled, or Other Corporations during the 5-year period ending on the date of the distribution, identify the stock that was acquired and provide the following information with respect to that stock:

(i) **Identity.** Identify the party from whom the stock was acquired and the transferor’s relationship, if any, to Distributing or its shareholders.

(ii) **Date and consideration.** State the date the stock was acquired and the consideration given in the acquisition.

(iii) **Transaction.** Describe the transaction in which the stock was acquired. For example, was the stock acquired in a § 368(a)(1) reorganization, by purchase, or by some other means? State whether control was acquired in a transaction in which Distributing transferred cash or other liquid or inactive assets to Controlled. See section 4.01(31) of Rev. Proc. 96–3. If a letter ruling was issued with respect to the transaction, attach a copy.

(iv) **Gain or loss.** State whether gain or loss was recognized, in whole or in part, to any party to the transaction and whether the basis of the stock acquired was determined, in whole or in part, by reference to the transferor’s basis.

Stock acquired during 5-year period

Other changes in ownership during 5-year period

(c) **Other changes in ownership.** Provide complete details concerning any change in ownership of the stock of Distributing, Controlled, or Other Corporations during the 5-year period ending on the date of the distribution that is not fully described under section 4.03(7)(b) of this revenue procedure. For this purpose, a change of ownership includes, but is not limited to, acquisitions, redemptions, recapitalizations, stock dividends, and sales. Information regarding sales of stock to which the issuing corporation was not a party need not be provided if: (i) the sale occurred on a recognized stock exchange or in an established market; and (ii) both the purchaser and the seller held less than 5 percent of the corporation’s stock both before and after the sale.

Continuation of business

**(8) Continuation of business.** If the transaction involves the vertical division of a single Active Business, submit the following **REPRESENTATION**: *Following the transaction, the distributing and controlled corporations will each continue, independently and with its separate employees, the active conduct of its share of all the integrated activities of the business conducted by the distributing corporation prior to consummation of the transaction.* If the transaction involves the separation of two or more Active Businesses, submit the following **REPRESENTATION**: *Following the transaction, the distributing and controlled corporations will each continue the active conduct of its business, independently and with its separate employees.* Additionally, if, following the transaction, Distributing and Controlled will share the services of any employees, identify these employees, specify the services to be performed, the length of time the employees will be shared, the compensation arrangements, and explain why the services of these employees will be shared.

In addition, describe any planned or intended substantial reduction in business activity for any Active Business. Generally, a substantial reduction in business activity does not include a vertical division of a single Active Business where Distributing and Controlled together continue all of the integrated activities of the Active Business.

Business purpose (see generally § 1.355-2(b))

.04

**(1) Detailed Description.** Describe in detail each purpose (whether or not a corporate business purpose) for the distribution of the stock of Controlled.

**(2) Corporate Business Purposes.** Explain which purposes described in section 4.04(1) of this revenue procedure are corporate business purposes within the meaning of § 1.355-2(b)(2) (“Corporate Business Purposes”). Describe how each Corporate Business Purpose is a real and substantial nonfederal tax purpose germane to the business of Distributing, Controlled, or the affiliated group (as defined in § 1.355-3(b)(4)(iv)) to which Distributing belongs. In addition, explain the business exigencies that require the distribution at this time. Submit the following **REPRESENTATION**: *The distribution of the stock, or stock and securities, of the controlled corporation is carried out for the following corporate business purposes: [list these Corporate Business Purposes]. The distribution of the stock, or stock and securities, of the controlled corporation is motivated, in whole or substantial part, by one or more of these corporate business purposes.*

Alternative transactions

**(3) Alternative transactions.** Explain why each Corporate Business Purpose cannot be achieved through a nontaxable transaction that does not involve the distribution of stock of Controlled and which is neither impractical nor unduly expensive. For example, in appropriate cases, possible alternative transactions might include the transfer of assets to a partnership or limited liability company. If a Corporate Business Purpose can be achieved through a nontaxable alternative transaction that would be impractical or unduly expensive, fully describe the reason the alternative transaction would be impractical or the additional expense that would be incurred by using the alternative transaction instead of the proposed transaction. An alternative transaction that will cause the loss of a favorable special tax status, such as an existing S corporation election, will ordinarily be viewed as unduly expensive.

Appendix A

**(4) Cross reference to Appendix A.** Appendix A of this revenue procedure provides guidelines that the Service will use, for ruling purposes, in evaluating whether a distribution satisfies the corporate business purpose requirement in certain situations and specifies information to be submitted with respect to the following business purposes: key employee, stock offering, borrowing, cost savings, fit and focus, competition, facilitating an acquisition of Distributing, facilitating an acquisition by Distributing or Controlled, and risk reduction. The business purposes described in Appendix A of this revenue procedure are not an exclusive list of Corporate Business Purposes for which the Service will issue a favorable ruling. If a purpose for the transaction is not described in Appendix A of this revenue procedure, the taxpayer should follow section 4.04 of this revenue procedure to establish that the distribution satisfies the corporate business purpose requirement.

Non-Corporate Business Purposes

**(5) Non-Corporate Business Purposes.**

**(a) General.** If the transaction will enable Distributing, Controlled, or Other Corporations to effect a reduction in federal taxes, or if it appears that the transaction will achieve one or more other non-Corporate Business Purposes, the taxpayer must convince the Service by clear and convincing evidence that the distribution is motivated in whole or substantial part by one or more Corporate Business Purposes in order to obtain a favorable ruling.

Shareholder planning

**(b) Shareholder planning.** State whether a purpose for the distribution is to facilitate the personal planning (such as estate planning or gifts) of any shareholder. If the answer is in the affirmative, provide the details.

Special tax status

**(c) Special tax status.** State whether Distributing, Controlled, or any Other Corporation is, plans to become, will cease to be, or will become eligible to become an S corporation, real estate investment trust, insurance company, bank, savings and loan, controlled foreign corporation, or other corporation with a special federal tax status. If so, describe the special tax status and the date it was or will become effective, will cease to be effective, or when the

|   |  |
|---|--|
| Description of any reduction in federal taxes                     | <p>corporation will become eligible. If either Distributing or Controlled will be eligible to elect S corporation status after the distribution, <i>see</i> Appendix C.</p> <p>(d) <b>Reduction in federal taxes.</b> Describe any reduction in federal taxes of Distributing, Controlled, or any Other Corporations that can reasonably be expected to result from the transaction. For this purpose, nonrecognition of income or gain to the shareholders or corporation resulting from the application of § 355 or § 361 is disregarded.</p>  |
| Representation regarding potential non-Corporate Business Purpose | <p>(e) <b>Representation.</b> In order to lessen the Service's concern about a potential non-Corporate Business Purpose, the taxpayer, in appropriate cases, may wish to represent that it will engage in a specific course of action (such as making or not making an election) that obviates the potential avoidance of federal taxes or other non-Corporate Business Purpose.</p>   |
| Substantiation  | <p>(6) <b>Substantiation of business purpose.</b></p> <p>(a) <b>Documentation.</b> The taxpayer must provide substantiation of one or more Corporate Business Purposes that motivate the transaction in whole or substantial part. The type and extent of the substantiation will necessarily vary depending on the described business purpose and facts of the particular case. Accordingly, the taxpayer should submit documentation that provides factual support for the Corporate Business Purposes. The Service recognizes that a particular transaction may be undertaken for more than one Corporate Business Purpose. Generally, satisfying the requirements of this section 4.04(6) of this revenue procedure with respect to one Corporate Business Purpose that motivates the transaction, in substantial part, will suffice in such cases.</p>  |
| Third party documentation   | <p>(b) <b>Third party documentation.</b> If the transaction is being undertaken at the request of, or pursuant to the advice or analysis of, persons other than Controlled or Distributing, explain fully. Provide documentation of such third party requests, advice, or analysis to substantiate the business purpose for the distribution. Such documentation should include an explanation of the third party's qualifications to speak to the matter.</p> <p>Business purposes for which third party documentation may be necessary include, for example, risk reduction, cost savings, facilitating a stock offering or borrowing, obtaining regulatory relief, improving credit, and preserving a franchise. Third party documentation prepared specifically for submission with the taxpayer's ruling request must contain an acknowledgement that the documentation will be submitted to the Internal Revenue Service for use in determining the federal tax consequences of the transaction.</p>   |
| Regulatory filings  | <p>(7) <b>Additional documents.</b></p> <p>(a) <b>Regulatory filings.</b> Provide copies of any proxy statements, information statements, or prospectuses filed or prepared in connection with the distribution or any related transaction. List and briefly describe any other documents that have been or will be filed with (or prepared for) any federal, state, local, or foreign regulatory body (such as the Securities and Exchange Commission) by the taxpayer in connection with the distribution. The Service may request copies of some or all such documents in the course of analyzing the ruling request.</p>   |
| Material prepared for directors                                   | <p>(b) <b>Material prepared for directors.</b> Attach a copy of any materials that relate to the purpose for the distribution and were prepared for or presented to the taxpayer's board of directors, and any relevant portions of the board's minutes.</p>   |
| Communications to shareholders and employees                      | <p>(c) <b>Communications to shareholders and employees.</b> Attach a copy of any press releases relating to the distribution. Attach copies of any letters or memoranda relating to the distribution that the taxpayer or its officers sent to the taxpayer's shareholders. In addition, attach copies of the taxpayer's written statements to its employees that discuss any purpose for the distribution.</p>  |
| Device ( <i>see generally</i> § 1.355-(2)(d))                     | <p>.05</p> <p>(1) <b>Dispositions of stock or securities.</b></p> <p>(a) <b>Representation.</b> Submit the following <i>REPRESENTATION: There is no plan or intention by the shareholders or security holders of the distributing corporation to sell, exchange, transfer by gift, or otherwise dispose of any of their stock in, or securities of, either the distributing or controlled corporation after the transaction.</i> For publicly traded companies, the taxpayer may instead submit the following <i>REPRESENTATION: There is no plan or intention by any shareholder who owns 5 percent or more of the stock of the distributing corporation, and the management of the distributing corporation, to its best knowledge, is not aware of any plan or intention on the part of any particular remaining shareholder or security holder of the distributing corporation to sell, exchange, transfer by gift, or otherwise dispose of any stock in, or securities of, either the distributing or controlled corporation after the transaction.</i></p> |
| Purchases of stock by Distributing or Controlled                  | <p>(b) <b>Permitted purchases.</b> For ruling purposes, the Service will treat purchases by either Distributing or Controlled of its stock after the transaction as not violating the device requirement of § 355(a)(1)(B) provided that:</p> <p>(i) there is a sufficient business purpose for the stock purchase;</p>  |

- (ii) the stock to be purchased is widely held;
- (iii) the stock purchases will be made in the open market; and
- (iv) there is no plan or intention that the aggregate amount of stock purchases will equal or exceed 20 percent of the outstanding stock of the corporation.

Submit the following **REPRESENTATION**: *There is no plan or intention by either the distributing corporation or the controlled corporation, 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 section 4.05(1)(b) of Rev. Proc. 96-30.*

If the stock purchases do not meet the requirements of this paragraph (b), the Service will consider ruling on whether the purchases violate the device requirement of § 355(a)(1)(B) after considering all of the facts and circumstances of each case.

(c) **Other dispositions.** If a plan or intent to dispose exists (including stock purchases that meet the requirements of section 4.05(1)(b) of this revenue procedure), provide the following information:

(i) **Detailed description.** Give complete details concerning the transaction, including any agreements existing between the parties and the number of shares of each class of stock or the amount of each series of securities that will be disposed of by each shareholder or security holder.

(ii) **Consideration.** State the consideration to be received by each shareholder or security holder.

(iii) **Evidence of nondevice.** Explain any special circumstances indicating why the disposition should not be viewed as a device, such as proportionate sales of Distributing and Controlled stock by the shareholder.

(2) **Absence of earnings and profits.** If the taxpayer contends that the distribution should not be considered to be a device because of an absence of earnings and profits (*see* § 1.355-2(d)(5)(ii)), submit the following **REPRESENTATIONS**:

(a) *The distributing corporation and the controlled corporation have no accumulated earnings and profits at the beginning of their respective taxable years;*

(b) *The distributing corporation and the controlled corporation will have no current earnings and profits as of the date of the distribution;*

(c) *No distribution of property by the distributing corporation immediately before the transaction would require recognition of gain resulting in current earnings and profits for the taxable year of the distribution; and*

(d) *The distributing corporation is not aware of, nor is the distributing corporation planning or intending, any event that will result in the distributing corporation or the controlled corporation having positive current or accumulated earnings and profits after the distribution.*

(3) **Non pro rata distribution.** State whether all or any part of the distribution, if considered taxable, would qualify as an exchange under § 302(a) or § 303(a).

(4) **Investment and inactive assets.** Under a separate heading for each corporation, provide the following information with respect to Distributing, Controlled, or Other Corporations:

(a) **Detailed description.** Provide a description and valuation of the investment assets, and other assets that are not related to the reasonable needs of the Active Businesses of Distributing, Controlled, or Other Corporations; and

(b) **Explanation.** Explain why Distributing, Controlled, or Other Corporations will hold these assets.

(5) **Liquidation or sale of assets.** Submit the following **REPRESENTATION**: *There is no plan or intention to liquidate either the distributing or controlled corporation, to merge either corporation with any other corporation, or to sell or otherwise dispose of the assets of either corporation after the transaction, except in the ordinary course of business.* Alternatively, describe the subsequent transaction.

.06 The taxpayer must explain how the continuity of interest requirement will be satisfied. Generally, the Service will view this requirement as satisfied if one or more persons who, directly or indirectly, were the owners of the enterprise prior to the distribution own, in the aggregate, 50 percent or more of the stock in each of the modified corporate forms in which the enterprise is conducted after the separation. In appropriate cases, the Service may require a continuity of interest representation from the taxpayer.

.07 Explain in detail why the distribution of Controlled stock, or of Controlled stock and securities, will not be a disqualified distribution within the meaning of § 355(d)(2). Generally, the explanation should set forth facts establishing that, taking into account the application of § 355(d)(6), (7), and (8), immediately after the distribution: (i) no person holds disqualified stock in Distributing that constitutes a 50 percent or greater interest in Distributing; and (ii) no person holds disqualified stock in Controlled that constitutes a 50 percent or greater

Information regarding  
planned dispositions of  
stock or securities

Absence of earnings and  
profits

Distribution qualifying as  
an exchange  
Investment assets

Liquidation or sale of  
assets

Continuity of shareholder  
interest (*see generally*  
§ 1.355-2(c))

Disqualified distribution

interest in Controlled. It is not necessary for the taxpayer to submit information accounting for all of the stock of Distributing or Controlled if, by providing information with respect to a smaller amount of stock, it can establish that the distribution will not be a disqualified distribution.

.08

**(1) Transfers and transactions between Distributing and Controlled.**

**(a) Contributions to capital.** Provide complete details concerning any transfers of property by Distributing to Controlled in anticipation of or in connection with the transaction. For ruling purposes, such transfers ordinarily will be treated as occurring in connection with a reorganization pursuant to § 368(a)(1)(D). If a transfer of property from Distributing to Controlled will not qualify as a reorganization pursuant to § 368(a)(1)(D), and the taxpayer contends that § 351 applies to the transaction, submit the information and representations specified in Rev. Proc. 83-59, 1983-2 C.B. 575, as modified or superseded, or explain why an item is not being submitted.

**(b) Liabilities.** If Controlled is assuming liabilities or receiving assets subject to liabilities, submit the following **REPRESENTATIONS**:

(i) *The total adjusted bases and the fair market value of the assets transferred to the controlled corporation by the distributing corporation each equals or exceeds the sum of the liabilities assumed by the controlled corporation plus any liabilities to which the transferred assets are subject; and*

(ii) *The liabilities assumed in the transaction and the liabilities to which the transferred assets are subject were incurred in the ordinary course of business and are associated with the assets being transferred.*

**(c) Investment credit property.** If any property is being transferred between Distributing and Controlled, state whether any investment credit determined under § 46 has been (or will be) claimed with respect to any of such property. If the answer is in the affirmative, submit the following **REPRESENTATION**: *The income tax liability for the taxable year in which investment credit property (including any building to which § 47(d) applies) is transferred will be adjusted pursuant to § 50(a)(1) or (a)(2) (or § 47, as in effect before amendment by Public Law 101-508, Title 11, 104 Stat. 1388, 536 (1990), if applicable) to reflect an early disposition of the property.* Alternatively, explain why no increase in tax will be required under § 50 (or § 47, as in effect before such amendment) as a result of the transaction.

**(d) Matching of income and deductions.** State the overall method of accounting of Distributing and Controlled. Further, state whether the transaction involves or will result in a situation in which one party recognizes income but another party recognizes the deductions associated with such income or one party owns property but another party recognizes the income associated with such property. *See, for example*, Notice 95-53, 1995-44 I.R.B. 21. If one or more parties use the cash method of accounting, explain the extent to which any actions have been or will be taken that are not in the ordinary course of business and that might affect the timing or the amount of any income or deduction to be recognized by a cash basis party to the transaction. *See, for example*, Rev. Rul. 80-198, 1980-2 C.B. 113. In addition, submit a statement as to whether any income items, such as accounts receivable, or any items resulting from a sale, exchange or disposition that would have resulted in income to Distributing, or any items of expense, will be transferred to Controlled. If any of these items are being transferred, fully explain. Further, submit the following **REPRESENTATION**: *The distributing corporation neither accumulated its receivables nor made extraordinary payment of its payables in anticipation of the transaction.* If Distributing uses the cash method of accounting or a similar method and Controlled uses the accrual method or a similar method, a closing agreement will be required unless the taxpayer submits the following **REPRESENTATION**: *No income items, including accounts receivable or any item resulting from a sale, exchange or disposition of property, that would have resulted in income to the distributing corporation, and no items of expense will be transferred to the controlled corporation if the distributing corporation has earned the right to receive the income or could claim a deduction for the expense under the accrual or similar method of accounting.*

**(2) Indebtedness.**

**(a) Cancellation of indebtedness.** If any indebtedness has been or will be cancelled in connection with the transaction, give complete details concerning the principal amount of the indebtedness, the circumstances under which it arose, and the date and method under which the indebtedness will be discharged.

**(b) Continuing indebtedness.** Submit the following **REPRESENTATION**: *No intercorporate debt will exist between the distributing corporation and the controlled corporation at the time of, or subsequent to, the distribution of the controlled corporation stock.* Alternatively, submit a full description of all existing, planned, or intended debt between Distributing and

Miscellaneous

Contributions to capital

Section 351

Liabilities

Investment credit  
recapture representation

Matching of income and  
deductions

Debt cancellation

Intercorporate  
indebtedness

Controlled, including complete details as to principal amounts, terms, and reasons for the issuance. Include copies of any instruments evidencing the intercorporate indebtedness. If any debt exists between Controlled, as debtor, and Distributing, as creditor, state whether such debt arose in connection with a transfer of assets by Distributing to Controlled. If so, explain the circumstances.

**Consolidated transactions**

(3) **Consolidated transactions.** If Distributing joins in the filing of a consolidated federal income tax return, submit the following **REPRESENTATION:** *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 § 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; § 1.1502-13 as published by T.D. 8597). Further, Distributing's excess loss account with respect to the Controlled stock will be included in income immediately before the distribution (See § 1.1502-19).*

**Future intercorporate transactions**

(4) **Continuing transactions between Distributing and Controlled (or two or more controlled corporations).** Describe in detail any continuing, planned, or intended transactions between Distributing and Controlled following the distribution, either directly or indirectly (such as through a partnership), or between an Other Corporation and a corporation from which it will be separated. In addition, submit the following **REPRESENTATION:** *Payments made in connection with all continuing transactions, if any, between the distributing and controlled corporations, will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.*

**Investment company**

(5) **Investment company.** If assets are transferred by Distributing to Controlled, or if liabilities owed by Controlled to Distributing are cancelled, submit the following **REPRESENTATION:** *No two parties to the transaction are investment companies as defined in § 368(a)(2)(F)(iii) and (iv).*

**Consideration received by Distributing**

(6) **Transfers of money or property to Distributing.** Set forth all consideration received by Distributing, including distributions by Controlled to Distributing, in connection with the transaction. Describe any receipt of money or property by Distributing from Controlled in contemplation of the distribution (other than in the ordinary course of business).

**Foreign corporation**

(7) **Foreign corporation.** State whether Distributing, Controlled, or any Other Corporation is a foreign corporation and whether any such foreign corporation is a passive foreign investment corporation (as defined in § 1296(a)), or a controlled foreign corporation (as defined in § 957) both before and after the distribution. See §§ 367(b), 367(e)(1), 897, and 1248(f).

**Other transactions**

(8) **Other transactions.** State whether there have been, or will be, any related transactions, and, if so, describe these other transactions and fully explain their relationship to, and impact on, the present transaction. Even if the transaction is thought to be unrelated, provide full details if it is contemplated that any stock is to be issued or redeemed by Distributing, Controlled, or Other Corporations, other than that already described as being distributed pursuant to the plan. Provide a description of any plan or intention to issue, redeem, or alter any rights in, such as voting rights, shares of stock of Distributing, Controlled, or Other Corporations.

**Plan of reorganization and other relevant documents**

(9) **Plan of reorganization and other relevant documents.** Submit a copy of the plan of reorganization or distribution. Alternatively, state why a copy is not available. In addition, submit a copy of any indemnification and tax sharing agreements to which Distributing or Controlled is a party.

If these or any other documents requested in this revenue procedure become available after filing the ruling request, submit copies as soon as possible.

**Requested rulings**

(10) **Requested rulings.** List the rulings being requested in the exact wording desired, and provide statutory, regulatory, or other authority for their issuance.

**Presubmission conference**

(11) **Presubmission conference.** Prior to submitting a § 355 ruling request, the taxpayer may request a conference with the Office of Assistant Chief Counsel (Corporate). A presubmission conference is particularly recommended if the transaction does not satisfy all of the requirements or relevant guidelines of this revenue procedure. The taxpayer must submit a description of the transaction, including the name of the taxpayer, and a memorandum of the issues to be discussed at the conference, at least three business days before the conference. The taxpayer must provide a power of attorney for each representative attending the conference. In appropriate cases, the Service will consider conducting the presubmission conference by telephone. For additional information regarding presubmission conferences, see the annual revenue procedure referred to in section 2 of this revenue procedure and contact the Office of the Assistant Chief Counsel (Corporate) at (202) 622-7710 (not a toll-free call).

## SECTION 5. EFFECT ON OTHER DOCUMENTS

.01 Rev. Procs. 91–63, 91–62, and 86–41 are superseded. Section 3.01(23) of Rev. Proc. 96–3 is revoked.

.02 The item relating to the § 355 Checklist Questionnaire in section 9.01 of Rev. Proc. 96–1 is amended to read as follows: Rev. Proc. 96–30, 1996–19 I.R.B. 8.

.03 Section 9.02 of Rev. Proc. 96–1 is modified to replace the reference to Rev. Proc. 91–63 with a reference to section 4.05(1)(b) of Rev. Proc. 96–30.

## SECTION 6. EFFECTIVE DATE

This revenue procedure will apply to all ruling requests postmarked, or, if not mailed, received, on or after June 5, 1996. However, the Service may ask the taxpayer to submit information specified in this revenue procedure for any ruling requests submitted prior to that date. The revocation of section 3.01(23) of Rev. Proc. 96–3 is effective on date May 6, 1996. The Service will entertain ruling requests on the business purposes listed in Appendix A of this revenue procedure whether the ruling request arrives before, on, or after the publication date of this revenue procedure.

## DRAFTING INFORMATION

The principal author of this revenue procedure is Dean P. Lekos of the Office of Assistant Chief Counsel (Corporate). For further information regarding this revenue procedure, contact Mr. Lekos on (202) 622-7550 or Mr. Howard W. Staiman on (202) 622-7750 (not toll-free calls).

## APPENDIX A

### SECTION 1. BUSINESS PURPOSE GUIDELINES

Appendix A provides guidelines that the Service will use, for ruling purposes, in evaluating whether a distribution satisfies the corporate business purpose requirement in certain situations. These guidelines apply in addition to the requirements specified in section 4.04 of this revenue procedure.

The business purposes described in this Appendix A are not an exclusive list of Corporate Business Purposes for which the Service will issue a favorable ruling. If a purpose for the transaction is not described in Appendix A of this revenue procedure, the taxpayer should follow section 4.04 of this revenue procedure to establish that the distribution satisfies the corporate business purpose requirement. The failure of a transaction to meet the guidelines in this Appendix A does not, in and of itself, mean that the distribution is not carried out for a Corporate Business Purpose. Moreover, the Service will consider requests for rulings that do not satisfy the guidelines in this Appendix A and may rule favorably in appropriate circumstances. Conversely, although a transaction may fall within the literal language of these guidelines, the Service will not issue a favorable ruling unless it is satisfied that the transaction is motivated, in whole or substantial part, by a real and substantial nonfederal tax purpose germane to the business of Distributing, Controlled, or the affiliated group to which Distributing belongs, and that the purpose cannot be achieved through a nontaxable transaction that does not involve the distribution of Controlled stock and which is neither impractical nor unduly expensive. The Service will continue to evaluate the guidelines in this Appendix A and may modify them when appropriate.

The Service recognizes that a particular transaction may be motivated, in whole or substantial part, by more than one business purpose described in this Appendix A. Generally, in such cases, satisfying the guidelines for one Corporate Business Purpose that motivates the transaction, in substantial part, will suffice.

A reference to Distributing or Controlled includes, as the context requires, a reference to Other Corporations (as defined in section 4.03(5) of this revenue procedure), or to a corporation that will be formed as part of the transaction.

### SECTION 2. SPECIFIC CORPORATE BUSINESS PURPOSES

#### .01 Key Employee.

(1) **General.** To establish that a Corporate Business Purpose for the distribution is to provide an equity interest in a business of Distributing or Controlled to a current or prospective employee, or employees, ordinarily, the taxpayer must demonstrate to the satisfaction of the Service that:

(a) The transfer of Distributing or Controlled stock to this employee, or these employees, will accomplish a real and substantial purpose germane to the business of Distributing, Controlled or the affiliated group (as defined in § 1.355–3(b)(4)(iv)) to which Distributing belongs. Among other things, the taxpayer must explain why the individual, or each individual, is considered a key employee, and why it is necessary to give the individual, or each individual, an equity interest of the type and amount proposed in the transaction.

(b) Generally within one year of the distribution, the employee, or the employees as a group, will receive a significant amount, in terms of percentage and value, of voting stock of either Distributing or Controlled. (An acquisition of a significant percentage of stock may not be required, however, if it would be prohibitively expensive for the employee,

or employees, to acquire a significant percentage of stock.) The taxpayer must state when the employee, or employees, will acquire the stock and fully describe the terms and method of acquisition (for example, purchase, compensation, or exercise of an option).

(c) The objective to be accomplished by transferring stock to the employee, or employees, cannot be accomplished by an alternative nontaxable transaction that does not involve the distribution of Controlled stock and which is neither impractical nor unduly expensive. (For example, the Service generally will consider that it is unduly expensive to create a controlled corporation that would terminate an existing S corporation election. In such cases, however, the taxpayer must demonstrate why another nontaxable transaction, such as the transfer of assets to a partnership or limited liability company, is neither impractical nor unduly expensive.) Where the taxpayer contends that a transaction involving a distribution will provide the employee, or employees, voting power representing a meaningful voice in the governance of their employer's business that is not available through an alternative transaction, the Service will consider such cases on a case-by-case basis, taking into account factors such as the distribution of voting power among the shareholders, family relationships, and competing economic interests.

**(2) Options and restricted stock.** The Service will scrutinize closely situations in which stock issued to the employee, or employees is subject to an option or restriction.

**(3) Stock ownership plans.** The principles of section 2.01(1) and (2) of this Appendix A also apply if a business purpose is to transfer Distributing or Controlled stock to an employee stock ownership plan described in § 4975(e)(7) (an "ESOP"), treating the ESOP as a group of key employees. Other plans relating to employee stock ownership will be considered on a case-by-case basis.

**.02 Stock offering.** To establish that a Corporate Business Purpose for the distribution is to facilitate a stock offering, ordinarily, the taxpayer must demonstrate to the satisfaction of the Service that:

(1) The issuing corporation needs to raise a substantial amount of capital in the near future to fund operations, capital expenditures, acquisitions, the retirement of indebtedness, or other business needs.

(2) The stock offering will raise significantly more funds per share (net of transaction costs of the distribution), or is otherwise more advantageous, if Distributing and Controlled are separated in connection with the offering. The taxpayer ordinarily must submit substantiation in the form of an analysis based on the professional judgment of persons qualified to speak to such matters. The analysis should be supported by data involving comparable corporations, businesses, and stock offerings and should compare the expected results of an offering, taking into account the proposed distribution, with the expected results of an offering by Distributing or Controlled without the distribution. Generally, the Service will acknowledge (without extensive substantiation) that an offering of publicly traded stock by a widely held corporation with no significant shareholders will raise more funds per share than an offering by the same corporation in the position of a controlled subsidiary.

(3) The funds raised in the stock offering will, under all circumstances, be used for the business needs of Distributing, Controlled, or the affiliated group (as defined in § 1.355-3(b)(4)(iv)) to which Distributing belongs. The taxpayer should explain when and how the funds will be used in satisfying such business needs.

(4) The stock offering will be completed within one year of the distribution.

(5) If the stock of a corporation with one or more significant shareholders will be purchased by a limited number of investors who require the distribution as a condition of their participation, the Service may require appropriate substantiation from these investors.

**.03 Borrowing.** To establish that a Corporate Business Purpose for the distribution is to facilitate borrowing, ordinarily, the taxpayer must demonstrate to the satisfaction of the Service that:

(1) Distributing or Controlled needs to raise a substantial amount of capital in the near future to fund operations, capital expenditures, acquisitions, or other business needs.

(2) The separation will enable Distributing or Controlled to borrow significantly more money or borrow on significantly better nonfinancial terms. The taxpayer ordinarily must submit substantiation, such as an analysis based on the professional judgment of persons qualified to speak to such matters.

(3) The funds raised in the borrowing will, under all circumstances, be used for the business needs of Distributing, Controlled, or the affiliated group (as defined in § 1.355-3(b)(4)(iv)) to which Distributing belongs. The taxpayer should explain when and how the funds will be used in satisfying such business needs.

(4) The borrowing will be completed within one year after the distribution.

If the distribution will enable Distributing or Controlled to borrow money at a lower cost, see section 2.04 of this Appendix A, relating to cost savings.

**.04 Cost savings.** To establish that a Corporate Business Purpose for the distribution is cost savings, ordinarily, the taxpayer must demonstrate to the satisfaction of the Service that the distribution will produce significant cost savings. Ordinarily, the taxpayer's submission should include analysis based on the professional judgment of persons qualified to speak to this matter (such as the taxpayer's insurer for insurance savings, an investment banker for lower borrowing costs, or, in appropriate cases, the taxpayer's employees). The analysis must explain the savings and why the savings cannot be achieved through a nontaxable transaction that does not involve the distribution of stock of Controlled and which is neither impractical nor unduly expensive.

Significant cost savings generally are projection period cost savings equal to at least one percent of the base period net income of Distributing's affiliated group. Projection period cost savings are the total anticipated future cost savings to

Distributing, Controlled, and their affiliated group for the 3-year period following the distribution, reduced by the transaction costs of the distribution and any anticipated additional direct or indirect costs to Distributing, Controlled and their affiliated group, all of which are computed on an after-tax basis. For this purpose, all savings (whether or not from the same source) and all additional costs to Distributing, Controlled, and their affiliated group are aggregated. Base period net income is the total net consolidated financial income of Distributing's affiliated group for the 3-year period preceding the distribution, all of which is computed on an after-tax basis, using generally accepted accounting principles. The taxpayer may choose to use the 5-year periods preceding and following the distribution for the base period and projection period instead of 3-year periods. Members of an affiliated group are determined in accordance with § 1.355-3(b)(4)(iv). In the case of foreign tax savings, explain the extent to which the foreign tax that is expected to be saved would have resulted in foreign tax credits or foreign tax credit carryovers for federal tax purposes.

The Service may apply different guidelines in various situations, including the following:

- (1) Projection period cost savings will not equal one percent of base period net income.
- (2) Net income for one or more of the 3 (or 5) years preceding the distribution is nominal or is affected by extraordinary or nonrecurring items of gain, loss, income or deduction, or there is a loss for any year.
- (3) Controlled stock will be distributed to a member of Distributing's affiliated group.
- (4) There are cost savings from the reduction of both federal and nonfederal taxes. In certain situations, a purpose of reducing nonfederal taxes is not a Corporate Business Purpose. *See* § 1.355-2(b)(2).

#### **.05 Fit and Focus.**

(1) **General.** This section 2.05 of Appendix A provides guidelines for a ruling request in which a Corporate Business Purpose for the distribution is that the separation will enhance the success of the businesses by enabling the corporations to resolve management, systemic, or other problems that arise (or are exacerbated) by the taxpayer's operation of different businesses within a single corporation or affiliated group. Except as provided in section 2.05(2) of this Appendix A, the Service ordinarily will rule with respect to pro rata as well as non pro rata distributions.

(2) **Significant shareholder or nonpublicly traded.** If Distributing is not publicly traded (or is publicly traded, but has a significant shareholder), the Service ordinarily will not rule unless the distribution:

- (a) is a non pro rata distribution to enable a significant shareholder or shareholder group to concentrate on a particular business (*see* example (2) of § 1.355-2(b)(5)), or
- (b) effects an internal restructuring within an affiliated group (members of an affiliated group are determined in accordance with § 1.355-3(b)(4)(iv)).

(3) **Significant shareholder defined.** A significant shareholder is any person who is directly or indirectly, or together with related persons, the owner of 5 percent or more of any class of stock of Distributing or Controlled and who actively participates in the management or operation of Distributing or Controlled. If the taxpayer contends that a person meeting or exceeding this 5 percent threshold does not actively participate in management or operations, the taxpayer should submit details supporting the taxpayer's contention.

(4) **Substantiation.** Documentary substantiation satisfactory to the Service is essential. The documentation should describe in detail the problems associated with the current corporate structure and demonstrate why the distribution will lessen or eliminate these problems. Internal reports and studies, and analyses based upon the professional judgment of persons qualified to speak to such matters (such as investment bankers or management consultants), are examples of documentation that may provide adequate substantiation. Reports by securities analysts or similar materials may also be helpful. However, in the case of a non pro rata distribution made to enable a significant shareholder or shareholder group to concentrate on a particular business, the Service ordinarily will not require third party documentation or detailed studies.

(5) **Special scrutiny.** In evaluating the ruling request, the Service will scrutinize closely the following situations:

(a) **Continuing relationship.** Any continuing relationship between Distributing and Controlled to determine if such relationship is consistent with the stated business purpose. Examples of continuing relationships include common directors, officers, or key employees, the provision of goods or services to the other company, or commonly-owned property.

(b) **Cross ownership.** Except for cases involving an internal restructuring of an affiliated group, any direct or indirect continuing interest in both Distributing and Controlled by a significant shareholder or, in the case of a nonpublicly traded corporation, any other shareholder. For example, if the purpose of the distribution is to allow a significant shareholder to concentrate on a particular business, the Service ordinarily will require, as a condition of ruling, that the separating shareholders not maintain interests (including interests as employees or directors) in both Distributing and Controlled after the distribution. Exceptions will be made on a case-by-case basis, taking into account the extent and nature of the interest in each corporation.

(c) **Certain internal restructurings.** Any internal restructuring in which the distributee is not entitled to eliminate, exclude, or receive a 100 percent dividends-received deduction with respect to, a distribution from Distributing, such as a transaction involving a foreign corporation.

#### **.06 Competition.**

(1) **General.** To establish that a Corporate Business Purpose for the distribution is to resolve the taxpayer's problems with customers or suppliers who object to Distributing or Controlled being associated with a business that competes with the customer or supplier, ordinarily, the taxpayer must demonstrate to the satisfaction of the Service that:

(a) One or more customers or suppliers have significantly reduced (or will significantly reduce) their purchases from, or sales to (or, for potential customers or suppliers, have not made any purchases from, or sales to), Distributing or Controlled because of the competing business.

(b) Because of the distribution, these customers or suppliers will significantly increase (or not implement a planned significant reduction in) their purchases from, or sales to, Distributing or Controlled after the distribution.

(c) These customers or suppliers do not object to the Distributing shareholders' ownership of stock of Controlled after the distribution.

(d) Sales to these customers, or purchases from these suppliers, will represent a meaningful amount of sales or purchases by Distributing or Controlled after the distribution.

(2) **Substantiation.** The taxpayer must submit substantiating evidence. In most cases, corroboration from customers or suppliers will be required.

**.07 Facilitating an acquisition of Distributing.** To establish that a Corporate Business Purpose for the distribution is to tailor Distributing's assets to facilitate a subsequent tax-free acquisition of Distributing by another corporation (the "acquiring corporation"), ordinarily, the taxpayer must demonstrate to the satisfaction of the Service that:

(1) The acquisition will not be completed unless Distributing and Controlled are separated.

(2) The acquisition cannot be accomplished by an alternative nontaxable transaction that does not involve the distribution of Controlled stock and is neither impractical nor unduly expensive.

(3) The acquiring corporation is not related to Distributing or Controlled. If the taxpayer contends that the Service should rule favorably, notwithstanding the fact that the acquiring corporation is related to Distributing or Controlled, explain the relationship and why the Service should disregard the relationship.

(4) The acquisition will be completed, and, except in unusual circumstances, will be completed within one year of the distribution.

**.08 Facilitating an acquisition by Distributing or Controlled.** To establish that a Corporate Business Purpose for the distribution is to tailor Distributing's assets or Controlled's corporate structure to facilitate a subsequent tax-free acquisition of another corporation (the "target corporation") by Distributing or Controlled, ordinarily, the taxpayer must demonstrate to the satisfaction of the Service that:

(1) The combination of the target corporation with Distributing or Controlled will not be undertaken unless Distributing and Controlled are separated.

(2) The acquisition cannot be accomplished by an alternative nontaxable transaction that does not involve the distribution of Controlled stock and is neither impractical nor unduly expensive.

(3) The target corporation is not related to Distributing or Controlled. If the taxpayer contends that the Service should rule favorably, notwithstanding the fact that the target corporation is related to Distributing or Controlled, explain the relationship and why the Service should disregard the relationship.

(4) The acquisition will be completed, and, except in unusual circumstances, will be completed within one year of the distribution.

**.09 Risk Reduction.** If a Corporate Business Purpose for the distribution is to significantly enhance the protection of one or more businesses (the "other businesses") from the risks of another business (the "risky business"), the factors the Service will consider, and the taxpayer should address, include:

(1) The nature and magnitude of the risks faced by the risky business. The taxpayer must submit information regarding the claims history of the risky business, or of the typical risk experience of similar businesses in that industry.

(2) Whether the assets and insurance associated with the risky business are sufficient to meet reasonably expected claims arising from the conduct of the risky business. The taxpayer must submit the book value and approximate fair market value of the net assets, including intangibles, of the risky business. Describe any other factors, such as liabilities that are not included on the taxpayer's balance sheet, that affect the value of the net assets of the risky business. The taxpayer must submit information as to the taxpayer's current insurance coverage and discuss the availability and cost of additional insurance. Facts regarding the cost and availability of insurance generally will require third party substantiation. If affordable insurance is available, but a separation of the businesses would reduce the cost, see section 2.04 of this Appendix A, relating to cost savings.

(3) Whether, under applicable law, the distribution will significantly enhance the protection of the other businesses from the risks of the risky business and, whether, under applicable law, an alternative nontaxable transaction that does not involve the distribution of Controlled stock and which is neither impractical nor unduly expensive (for example, creating a parent/subsidiary or holding company structure) would provide similar protection. See example (3) of § 1.355-2(b)(5). The taxpayer's submission should include an analysis of the law and the application of the law to the relevant facts of the proposed transaction. An opinion of counsel may be required. It is not necessary for the taxpayer to establish conclusively that, under applicable law, the proposed transaction will afford adequate protection or that an alternative transaction would not afford adequate protection. However, the taxpayer must convince the Service that, based on objective analysis of the law and its application to the facts, risk reduction is a real and substantial purpose for the transaction.

## APPENDIX B

### SECTION 1. RULING REQUESTS INVOLVING RETENTION OF STOCK OR OPTIONS BY DISTRIBUTING

.01 The Service will issue favorable rulings regarding the application of § 355(a)(1)(D)(ii), relating to the retention by Distributing of stock or options in Controlled, to transactions in which Controlled stock will be widely held if Distributing establishes that the following requirements are satisfied:

(1) A sufficient business purpose exists for the retention of the stock, options, and any stock acquired on the exercise of the options.

(2) None of Distributing's directors or officers will serve as directors or officers of Controlled as long as Distributing retains the stock, options, or any stock acquired on the exercise of the options. Under appropriate facts and circumstances, the Service may issue a favorable ruling in cases in which the directors or officers of Distributing will serve as directors or officers of Controlled. For example, the Service may issue a favorable ruling if a director or officer of Distributing serves as a director or officer of Controlled solely to accommodate Controlled's business needs.

(3) The retained stock, options, and any stock acquired upon exercise of the options will be disposed of as soon as a disposition is warranted consistent with the business purpose specified in section 1.01(1) of this Appendix B, but in any event, not later than 5 years after the distribution.

(4) Distributing will vote the retained stock and any stock acquired on exercise of the options in proportion to the votes cast by Controlled's other shareholders. For example, if after the distribution the other shareholders of Controlled vote 70 percent in favor of a matter and 30 percent against, Distributing would be required to vote the stock 70 percent in favor and 30 percent against the matter.

.02 In other cases, the Service may issue favorable rulings, based upon all relevant facts and circumstances, regarding the application of § 355(a)(1)(D)(ii). For example, the Service will rule favorably if the transaction is covered by Rev. Rul. 75-321, 1975-2 C.B. 123.

## APPENDIX C

### SECTION 1. REPRESENTATIONS REGARDING S CORPORATION STATUS

.01 This Appendix C contains representations regarding S corporation status that the taxpayer may submit to lessen the Service's concerns about the potential avoidance of federal taxes. These representations may be submitted if either Distributing or Controlled will be eligible to elect S corporation status after the distribution. If either Distributing or Controlled will be eligible to elect S corporation status after the distribution, but the taxpayer does not submit any of the representations in this Appendix C, please explain. The taxpayer's failure to submit any of the representations will not prevent the Service from issuing a favorable ruling if it is satisfied that the distribution is motivated in whole or substantial part by one or more Corporate Business Purposes. On the other hand, there may be cases where the submission of one of the representations will not conclusively establish that the transaction does not have the potential for the avoidance of federal taxes.

**(1) No S elections. REPRESENTATION:** *The distributing corporation is not an S corporation (within the meaning of § 1361(a)), and there is no plan or intention by the distributing or controlled corporation to make an S corporation election pursuant to § 1362(a).*

**(2) Distributing and Controlled will elect S corporation status. REPRESENTATION:** *The distributing corporation is not an S corporation (within the meaning of § 1361(a)), but immediately before the distribution, the distributing corporation will be eligible to make an S corporation election pursuant to § 1362(a). The distributing and controlled corporations will elect to be an S corporation pursuant to § 1362(a) on the first available date after the distribution, and there is no plan or intent to revoke or otherwise terminate the S corporation election of either the distributing or controlled corporation.*

**(3) Distributing is an S corporation. REPRESENTATION:** *The distributing corporation is an S corporation (within the meaning of § 1361(a)). The controlled corporation will elect to be an S corporation pursuant to § 1362(a) on the first available date after the distribution and there is no plan or intent to revoke or otherwise terminate the S corporation election of either the distributing or controlled corporation.*