

Internal Revenue Service

Department of the Treasury

Number: **200143029**
Release Date: 10/26/2001
Index Number: 0355.00-00

Washington, DC 20224

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Refer Reply To:

CC:CORP:B05 PLR-130872-01

Date:

July 31, 2001

In re:

Parent =

Distributing =

Controlled 1 =

Controlled 2 =

Controlled 3 =

Business A =

Business B =

Sub 1 =

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Sub 2 =

Sub 3 =

State X =

This letter responds to your May 22, 2001, request for rulings on certain federal income tax consequences of a proposed transaction. The information submitted in this request and in subsequent correspondence, submitted on June 27, 2001, is summarized below.

Parent is a publicly traded corporation, principally engaged in Business A on a worldwide basis. Parent is the common parent of an affiliated group of corporations that file a U.S. federal income consolidated income tax return. Parent owns all of the outstanding stock of Distributing, a State X corporation. Distributing owns all of the outstanding stock of Controlled 1, Controlled 2, and Controlled 3, each of which is a State X corporation engaged in Business B. Distributing also owns all of the outstanding stock of Sub 1, Sub 2, and Sub 3.

Financial information has been submitted indicating that Distributing, Controlled 1, Controlled 2, and Controlled 3 have each had gross receipts and operating expenses representative of the active conduct of a trade or business for each of the last 5 years.

In order to reduce state income tax costs, the after tax income from Distributing's subsidiaries generally has not been distributed upstream to Distributing in the form of dividends. Distributing files income and/or franchise tax returns in most U.S. states. For state income tax purposes, dividend income that is received by Distributing is currently subject to taxation in a number of states that do not allow a corresponding deduction for dividends received. For state franchise tax purposes, Distributing is taxed in a number of states that include in the tax base the total equity of the company, including investments in subsidiaries. In order to finance the group's corporate operations, including future acquisitions, in the most state income tax efficient manner and to reduce Distributing's current and future state franchise tax expense, Distributing desires to create an organizational structure that will allow it to distribute the accumulated and future earnings of its subsidiaries and move the ownership of such subsidiaries to a newly created wholly owned subsidiary of Parent.

The Proposed Transaction

To accomplish this separation, Distributing has proposed the following transaction:

- (i) Parent will form a wholly owned U.S. subsidiary, Newco.
- (ii) Parent will contribute all of the stock of Distributing to Newco.
- (iii) Distributing will contribute all of the stock of Sub 1 and Sub 2 to Controlled 1.
- (iv) Distributing will contribute all of the stock of Sub 3 to Controlled 3.
- (v) Distributing will distribute all of the outstanding stock of Controlled 1, Controlled 2, and Controlled 3 to Newco.

Immediately following the completion of the proposed transaction, all of the stock of Distributing, Controlled 1, Controlled 2, and Controlled 3 will be directly owned by Newco, a wholly owned subsidiary of Parent. Following the proposed transaction, Distributing, Controlled 1, Controlled 2, and Controlled 3 will continue to carry on the same businesses and activities that they conducted prior to the transaction.

The Representations

In connection with the transaction, the following representations are made:

- (a) No part of the consideration to be distributed by Distributing will be received by Newco as a creditor, employee, or in any capacity other than that of a shareholder of the corporation.
- (b) The 5 years of financial information submitted on behalf of Distributing 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.
- (c) The 5 years of financial information submitted on behalf of Controlled 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) The 5 years of financial information submitted on behalf of Controlled 2 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.

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- (e) The 5 years of financial information submitted on behalf of Controlled 3 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.
- (f) The gross fair market value of Distributing's Business B assets presently constitutes and will constitute at the time of the Distribution at least 5 percent of the total gross fair market value of all the assets of Distributing. In addition, the gross fair market value of each of Controlled 1's, Controlled 2's, and Controlled 3's Business B assets constitutes and will constitute at the time of the Distribution at least 5 percent of the total gross fair market value of all the assets of Controlled 1, Controlled 2, and Controlled 3, respectively.
- (g) Following the transaction, Distributing, Controlled 1, Controlled 2, and Controlled 3 will each continue the active conduct of its business, independently and with its separate employees.
- (h) The distribution of the stock of Controlled 1, Controlled 2, and Controlled 3 is being carried out for the following corporate business purpose: the creation of a state tax efficient structure that will allow the distribution of the group's accumulated and future earnings for use by the parent company and reduce state tax franchise costs. The distribution of the stock of Controlled 1, Controlled 2, and Controlled 3 is motivated, in whole or substantial part, by this business purpose.
- (i) There is no plan or intention by the shareholders or security holders of Distributing to sell, exchange, transfer by gift, or otherwise dispose of any of their stock in, or securities of, either Distributing, Controlled 1, Controlled 2, or Controlled 3 after the transaction.
- (j) There is no plan or intention by Distributing, Controlled 1, Controlled 2, or Controlled 3, directly or through any subsidiary corporation, to purchase any of its outstanding stock after the transaction.
- (k) There is no plan or intention to liquidate either Distributing, Controlled 1, Controlled 2, or Controlled 3, 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.
- (l) Except for debt incurred in the ordinary course of business, no intercorporate debt will exist between Distributing and Controlled 1, Distributing and Controlled 2, or Distributing and Controlled 3, at the time

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of, or subsequent to, the distribution of the stock of Controlled 1, Controlled 2, and Controlled 3.

- (m) The indebtedness owed by Controlled 1, Controlled 2, or Controlled 3 to Distributing after the distribution of the stock of each controlled corporation will not constitute stock or securities in Controlled 1, Controlled 2, or Controlled 3, respectively.
- (n) 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 of the Income Tax Regulations 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). Further, Distributing does not have an excess loss account with respect to the Controlled 1, Controlled 2 or Controlled 3 stock.
- (o) Payments made in connection with all continuing transactions, if any, between Distributing and Controlled 1, Distributing and Controlled 2, and Distributing and Controlled 3, will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.
- (p) For purposes of § 355(d) of the Internal Revenue Code, immediately after the distribution, no person (determined after applying § 355(d)(7)) will hold stock possessing 50 percent or more of the total combined voting power of all classes of stock entitled to vote, or 50 percent or more of the total value of the shares of all classes of Distributing stock, that was acquired by purchase (as defined in §§ 355(d)(5) and (8)) during the 5-year period ending on the date of the distribution.
- (q) For purposes of § 355(d), immediately after the distribution, no person (determined after applying section 355(d)(7)) will hold stock possessing 50 percent or more of the total combined voting power of all classes of stock entitled to vote, or 50 percent or more of the total value of the shares of all classes of Controlled 1, Controlled 2, and Controlled 3 stock, that was acquired by purchase (as defined in sections 355(d)(5) and (8)) during the 5-year period ending on the date of the distribution.
- (r) The distribution is not part of a plan or series of related transactions pursuant to which one or more persons will acquire, directly or indirectly, stock possessing 50 percent or more of the total combined voting power of all classes of stock of either Distributing, Controlled 1, Controlled 2, or Controlled 3, or stock possessing 50 percent or more of the total value of all classes of stock of either Distributing, Controlled 1, Controlled 2, or

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Controlled 3, within the meaning of § 355(e).

- (s) None of Distributing, Controlled 1, Controlled 2, or Controlled 3 are investment companies as defined in § 368(a)(2)(F)(iii) and (iv).

The Rulings

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

- (1) The transfer by Distributing of the Sub 1 and Sub 2 stock to Controlled 1 solely in exchange for stock of Controlled 1 followed by the distribution of all the stock of Controlled 1 to Newco will qualify as a reorganization within the meaning of § 368(a)(1)(D). Distributing and Controlled 1 will each be a “party to a reorganization” within the meaning of § 368(b).
- (2) The transfer by Distributing of the Sub 3 stock to Controlled 3 solely in exchange for stock of Controlled 3 followed by the distribution of all the stock of Controlled 3 to Newco will qualify as a reorganization within the meaning of § 368(a)(1)(D). Distributing and Controlled 3 will each be a “party to a reorganization” within the meaning of § 368(b).
- (3) No gain or loss will be recognized by Distributing on the transfer of the Sub 1 and Sub 2 stock to Controlled 1 solely in exchange for Controlled 1 stock (§ 361(a)).
- (4) No gain or loss will be recognized by Distributing on the transfer of the Sub 3 stock to Controlled 3 solely in exchange for Controlled 3 stock (§ 361(a)).
- (5) No gain or loss will be recognized by Controlled 1 upon receipt of the Sub 1 and Sub 2 stock in exchange for Controlled 1 stock (§ 1032(a)).
- (6) No gain or loss will be recognized by Controlled 3 upon receipt of the Sub 3 stock in exchange for Controlled 3 stock (§ 1032(a)).
- (7) The basis of the Sub 1 and Sub 2 stock to be received by Controlled 1 will be equal to the basis of such stock in the hands of Distributing immediately before the transfer (§ 362(b)).
- (8) The basis of the Sub 3 stock to be received by Controlled 3 will be equal to the basis of such stock in the hands of Distributing immediately before the transfer (§ 362(b)).

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- (9) The holding period of the Sub 1 and Sub 2 stock in the hands of Controlled 1 will include the period during which such stock was held by Distributing (§ 1223(2)).
- (10) The holding period of the Sub 3 stock in the hands of Controlled 3 will include the period during which such stock was held by Distributing (§ 1223(2)).
- (11) No gain or loss will be recognized by Distributing upon the distribution of all of the stock of Controlled 1, Controlled 2, and Controlled 3 to Newco (§§ 355(c)(1) and 361(c)(1)).
- (12) No gain or loss will be recognized by (and no amount will be included in the gross income of) Newco upon its receipt of all of the stock of Controlled 1, Controlled 2, and Controlled 3 from Distributing (§ 355(a)(1)).
- (13) The aggregate basis of the Controlled 1, Controlled 2, Controlled 3, and Distributing stock in the hands of Newco immediately after the distribution will be the same as the aggregate basis of the Distributing stock held by Newco immediately before the distribution, allocated among the Controlled 1, Controlled 2, Controlled 3, and Distributing stock in proportion to the fair market value of each in accordance with § 1.358-2(a)(2) (§ 358(b)(2)).
- (14) The holding period of the Controlled 1, Controlled 2, and Controlled 3 stock received by Newco will include the holding period of the Distributing stock with respect to which the distribution will be made, provided that the Distributing stock is held as a capital asset on the date of the distribution (§ 1223(1)).
- (15) As provided in § 312(h), proper allocation of earnings and profits between Distributing, Controlled 1, Controlled 2, and Controlled 3 will be made under § 1.312-10(a) and (b).

Caveats

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

Procedural Matters

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

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

Pursuant to the power of attorney on file in this office, copies of this letter have been sent to the taxpayer's authorized representatives.

Sincerely yours,
Associate Chief Counsel (Corporate)
By: Debra Carlisle
Debra Carlisle
Chief, Branch 5