

Internal Revenue Service

Department of the Treasury

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Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:
CC:CORP:B02-PLR-109315-00
Date:
October 24, 2000

LEGEND:

- Foreign Parent =
- Distributing 1 =
- Distributing 2 =
- Controlled =
- Controlled
Subsidiary 1 =
- Controlled
Subsidiary 2 =
- State T =
- State U =
- Country V =
- Country W =
- Country X =
- Country Y =
- Industry Z =
- Business A =
- Business B =
- Business C =
- Business D =
- Business E =
- Business F =

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Dear:

This letter responds to your Authorized Representatives' letter dated April 26, 2000, in which you requested rulings under section 355 of the Internal Revenue Code. Additional information regarding your request has been submitted in letters dated July 27, August 7, August 9, August 18, September 12, September 27, and October 17, 2000. The material information submitted for consideration is summarized below.

Foreign Parent is a Country V corporation engaged in Industry Z. Distributing 2, a wholly-owned subsidiary of Foreign Parent, is a State U corporation. Distributing 2 is a holding company for operations located in Countries W, X, and Y and is the common parent for the U.S. affiliated group. Distributing 2 is engaged in Businesses A, B, C, D, E, and F indirectly, through its subsidiaries. Each of these businesses has been conducted for more than five years.

Distributing 1, a State U corporation, is a wholly-owned subsidiary of Distributing 2. Distributing 1 is actively engaged in Businesses A, B, C, D, E, and F. Each of these businesses has been conducted for more than five years. Controlled is to be a State U corporation and will be formed for the purpose of restructuring Business F. After the proposed transaction, Controlled will be engaged in Business F through its wholly-owned subsidiaries.

Controlled Subsidiary 1, a State U corporation, is a wholly-owned subsidiary of Distributing 1. Controlled Subsidiary 1 has been directly engaged in Business F for each of the past five years. Controlled Subsidiary 2, a State T corporation, is a wholly-owned subsidiary of Distributing 1. Controlled Subsidiary 2 has been directly engaged in Business F for each of the past five years.

The taxpayer has supplied financial information which indicates that Distributing 1, Distributing 2, Controlled Subsidiary 1, and Controlled Subsidiary 2 have been conducting businesses that have had gross receipts and operating expenses representative of the active conduct of such businesses for each of the past five years.

The management of Distributing 1 has determined that Businesses A and F cannot achieve their full potential as part of the Distributing 1 affiliated group due to management and systemic problems arising in their operation. Since Business A represents a larger share of Distributing 1's overall sales, management has been heavily influenced by the business model appropriate to Business A. As a result, the current structure impedes the investment in research and development necessary to succeed in Business F and the ability to make and implement decisions essential to the Business F operations.

Accordingly, in order to resolve these problems, the taxpayer has proposed the following transaction:

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- (1) Distributing 1 will contribute all of the issued and outstanding stock of Controlled Subsidiary 1 and Controlled Subsidiary 2 to Controlled in exchange for all of the issued and outstanding stock of Controlled.
- (2) Distributing 1 will then distribute all of the issued and outstanding stock of Controlled to Distributing 2 ("Distribution 1").
- (3) Distributing 2 will then distribute all of the issued and outstanding stock of Controlled to Foreign Parent ("Distribution 2").

The following additional representations have been made in connection with Step 1 of the proposed transaction:

- (a) The five years of financial information submitted on behalf of Distributing 1, Controlled Subsidiary 1, and Controlled Subsidiary 2 is representative of their present operations, and with regard to such corporations, there have been no substantial operational changes since the date of the last financial statements submitted.
- (b) The proposed transaction does not involve the vertical division of a single business or the separation of two or more businesses. There is no planned or intended substantial reduction in the business activity of Distributing 1 or Controlled.
- (c) The total adjusted gross bases and the fair market value of the assets to be transferred to Controlled by Distributing 1 each equals or exceeds the sum of the liabilities assumed by Controlled plus any liabilities to which the transferred assets are subject.
- (d) The liabilities assumed in step 1 of 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.

The following additional representations have been made in connection with Step 2 of the proposed transaction:

- (e) No part of the consideration to be distributed by Distributing 1 will be received by the shareholder of Distributing 1 as a creditor, employee, or in any capacity other than that of a shareholder of Distributing 1.
- (f) There is no plan or intention on the part of the shareholders of Distributing 1 to sell, exchange, transfer by gift, or otherwise dispose of any of their stock in either Distributing 1 or Controlled after the proposed transaction, except: (i) Foreign Parent will contribute Controlled to its wholly-owned

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subsidiary, Foreign Holdco, and then, possibly, to a wholly-owned subsidiary of Foreign Holdco, and (ii) Distributing 2 will contribute Distributing 1 to its wholly-owned U.S. subsidiary, New Capco.

- (g) Immediately after the distribution, at least ninety percent of the fair market value of the gross assets of Controlled 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).
- (h) Immediately after the distribution, at least ninety percent of the fair market value of the gross assets of Distributing 2 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).
- (i) The proposed transaction does not involve the vertical division of a single business or the separation of two or more businesses. There is no planned or intended substantial reduction in the business activity of Distributing 2.
- (j) The distribution of the stock of Controlled is being undertaken for the following corporate business purpose: to enhance the success of the business by enabling the corporations to resolve management and systemic problems that arise by the taxpayer's operation of different businesses within a single corporation or affiliated group. The distribution of the stock of Controlled is motivated, in whole or substantial part, by such corporate business purpose.
- (k) There is no plan or intention to issue, redeem, or dispose of any of the Controlled stock except as described above at paragraph (f).
- (l) There is no plan or intention by Distributing 1, Distributing 2, or Controlled, directly or through any subsidiary corporation, to purchase any of its outstanding stock after the transaction, other than through stock purchases meeting the requirements of Section 4.05(1)(b) of *Rev. Proc. 96-30*.
- (m) There is no plan or intention to liquidate Distributing 1, Distributing 2, or Controlled; to merge any of these corporations with any other corporation; or to sell or otherwise dispose of any of the assets of these corporations except (i) in the ordinary course of business and (ii) as described above at paragraph (f).
- (n) Neither Distributing 1 nor Distributing 2 accumulated its receivables nor made extraordinary payment of its payables in anticipation of the

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proposed transaction.

- (o) No shareholder of Distributing 1 or Distributing 2 will hold immediately after the distribution disqualified stock within the meaning of § 355(d)(3) which constitutes a 50% or greater interest in Distributing 1, Distributing 2, or Controlled.
- (p) The distribution is not part of a plan or series of related transactions (within the meaning of § 355(e)) pursuant to which one or more persons will acquire, directly or indirectly, stock possessing 50% or more of the combined voting power of all classes of stock entitled to vote of either Distributing 1, Distributing 2, or Controlled, or stock possessing 50% or more of the total value of all classes of stock of either Distributing 1, Distributing 2, or Controlled.
- (q) No intercorporate debt will exist between Distributing 1, Distributing 2, and Controlled at the time of, or subsequent to, the distribution of the Controlled stock, except as may arise from the shared treasury function operated out of Distributing 1. Any such intercorporate debt will not constitute stock or securities.
- (r) 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. Further, Distributing 1's and Distributing 2's excess loss account, if any, with respect to the Controlled stock will be included in income immediately before the distribution (See § 1.1502-19).
- (s) Payments made in connection with all continuing transactions, if any, between Distributing 1, Distributing 2, and Controlled will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.
- (t) None of the parties to the transaction is an investment company as defined in section 368(a)(2)(F)(iii) and (iv).

The following additional representations have been made in connection with Step 3 of the proposed transaction:

- (u) No part of the consideration to be distributed by Distributing 2 will be received by the shareholder of Distributing 2 as a creditor, employee, or in any capacity other than that of a shareholder of Distributing 2.
- (v) There is no plan or intention on the part of the shareholders of Distributing

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2 to sell, exchange, transfer by gift, or otherwise dispose of any of their stock in either Distributing 1, Distributing 2, or Controlled after the proposed transaction, except as described above at paragraph (f).

- (w) Neither Distributing 2 nor Controlled has been or will be a “United States real property holding corporation” (“USRPHC”), as defined in § 897(c)(2), at any time during the five-year period ending on the date of Distribution 2, and neither Distributing 2 nor Controlled will be a USRPHC immediately after Distribution 2.

Based solely upon the information submitted and the representations made, we rule as follows:

- (a) The transfer by Distributing 1 to Controlled of the stock of Controlled Subsidiary 1 and Controlled Subsidiary 2, solely in exchange for all of the issued and outstanding stock of Controlled, followed by the distribution of all of the Controlled stock to Distributing 2 will be a reorganization within the meaning of section 368(a)(1)(D) of the Code. Distributing 1 and Controlled will each be “a party to the reorganization” within the meaning of section 368(b).
- (b) Distributing 1 will recognize no gain or loss upon the transfer of the stock of Controlled Subsidiary 1 and Controlled Subsidiary 2 to Controlled in exchange for the stock of Controlled (section 361(a)).
- (c) Controlled will recognize no gain or loss upon the receipt of the stock of Controlled Subsidiary 1 and Controlled Subsidiary 2 in exchange for the stock of Controlled (section 1032(a)).
- (d) The basis of the stock of Controlled Subsidiary 1 and Controlled Subsidiary 2 received by Controlled in the transaction will be the same as the basis of such property in the hands of Distributing 1 immediately prior to their transfer to Controlled (section 362(b)).
- (e) The holding period of the stock of Controlled Subsidiary 1 and Controlled Subsidiary 2 received by Controlled in the transaction will include the period during which such property was held by Distributing 1 (section 1223(2)).
- (f) Distributing 2 will recognize no gain or loss (and no amount will be included in the income of Distributing 2) upon the receipt of the Controlled stock (section 355(a)(1)).
- (g) Distributing 1 will recognize no gain or loss upon the distribution of the

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Controlled stock to Distributing 2 (section 361(c)).

- (h) The aggregate basis of the Controlled stock and the Distributing 1 stock in the hands of Distributing 2 immediately after the distribution to Distributing 2 will be the same as the basis of the Distributing 1 stock in the hands of Distributing 2 immediately prior to the distribution (section 358(a)(1) and section 1.358-1(a)). Such aggregate basis will be allocated between the Distributing 1 stock and the Controlled stock in proportion to the relative fair market value of each corporation's stock in accordance with section 1.358-2(a)(2) of the Income Tax Regulations (section 358(b)).
- (i) The holding period of the Controlled stock received by Distributing 2 will include the holding period of the Distributing 1 stock held by Distributing 2 with respect to which the distribution will be made, provided that the Distributing 1 stock is held as a capital asset on the date of the distribution (section 1223(1)).
- (j) As provided in section 312(h), proper allocation of earnings and profits between Distributing 1 and Controlled will be made under sections 1.312-10(a) and 1.1502-33 of the Income Tax Regulations.
- (k) Foreign Parent will recognize no gain or loss (and no amount will be included in the income of Foreign Parent) upon the receipt of the Controlled stock (section 355(a)(1)).
- (l) Distributing 2 will recognize no gain or loss upon the distribution of the Controlled stock to Foreign Parent (section 355(c)).
- (m) The aggregate basis of the Controlled stock and the Distributing 2 stock in the hands of Foreign Parent immediately after the distribution to Foreign Parent will be the same as the basis of the Distributing 2 stock in the hands of Foreign Parent immediately prior to the distribution (section 358(a)(1) and section 1.358-1(a)). Such aggregate basis will be allocated between the Distributing 1 stock and the Controlled stock in proportion to the relative fair market value of each corporation's stock in accordance with section 1.358-2(a)(2) of the Income Tax Regulations (section 358(b)).
- (n) The holding period of the Controlled stock received by Foreign Parent will include the holding period of the Distributing 2 stock held by Foreign Parent with respect to which the distribution will be made, provided that the Distributing 2 stock is held as a capital asset on the date of the distribution (section 1223(1)).
- (o) As provided in section 312(h), proper allocation of earnings and profits

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between Distributing 2 and Controlled will be made under sections 1.312-10(a) and 1.1502-33 of the Income Tax Regulations.

- (p) Distributing 2 will not recognize gain or loss under section 367(e)(1) on the distribution of Controlled stock to Foreign Parent (section 1.367(e)-1(c)).

No opinion is expressed or implied 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. The rulings contained in this letter are predicated upon the facts and representations submitted by the Taxpayer and accompanied by a penalties of perjury statement executed by an appropriate party. This office has not verified any of the materials submitted in support of the request for a ruling. Verification of the information, representations, and other data may be required as part of the audit process.

This ruling letter is directed only to the taxpayer(s) requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

A copy of this letter should be attached to the federal income tax return(s) of the taxpayer(s) involved for the taxable year in which the transaction covered by this ruling letter is consummated.

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

Sincerely,
Associate Chief Counsel (Corporate)
by Lewis K Brickates
Assistant to the Branch Chief, Branch 2