

**Internal Revenue Service**

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Department of the Treasury

Washington, DC 20224

[Third Party Communication:

Date of Communication: Month DD, YYYY]

Person To Contact:

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Refer Reply To:

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PLR-106965-05

Date: June 27, 2005

Legend

Parent =

Distributing 1 =

Distributing 2 =

Controlled 1 =

Controlled 2 =

Controlled 3 =

Business A =

Business B =

Country X =

Date 1 =

Dear

This ruling is in reply to your representative's letter dated January 31, 2005 for rulings concerning the Federal income tax consequences of a proposed transaction. Additional information was submitted in letters dated April 1, April 3 and June 8. The material information submitted for consideration is substantially as set forth below.

The rulings contained in this letter are based on 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 rulings. Verification of the information, representations and other data may be required as part of the audit process. Moreover, no information provided by the taxpayer has been reviewed and no determination has been made regarding whether the proposed transaction: (i) satisfies the business purpose requirement of § 1.355-2(b) of the Income Tax Regulations, (ii) is used principally as a device for the distribution of the earnings and profits of the distributing corporation or the controlled corporation or both (see § 355(a)(1)(B) of the Internal Revenue Code and § 1.355-2(d)), or (iii) is part of a plan (or series of related transactions) pursuant to which one or more persons will acquire directly or indirectly stock representing a 50-percent or greater interest in the distributing corporation or the controlled corporation (see § 355(e)(2)(A)(ii) and § 1.355-7T).

Parent, a publicly held corporation with two classes of stock outstanding (class A common stock and class B common stock), is formed under the laws of Country X. Parent is directly engaged in Business A and owns numerous subsidiaries that are engaged in Business A or Business B either directly or through its subsidiaries. Parent owns all the stock of Distributing 1 and Controlled 3. Distributing 1, a holding company engaged in Business A and Business B through its subsidiaries, is the common parent

of an affiliated group of corporations, including Distributing 2 and Controlled 2, that file a consolidated Federal income tax return. Controlled 3 is a corporation formed under the laws of Country X and has one class of common stock outstanding. Distributing 2 is engaged in Business A and Business B, and Controlled 2 and Controlled 3 are engaged in Business B.

We have received information that Parent, Distributing 2, Controlled 2 and Controlled 3 each have had gross receipts and operating expenses representing the active conduct of a trade or business for each of the past five years.

For what has been represented as a valid business purpose, the taxpayer has proposed the following transaction which will be completed by Date 1:

- (i) Distributing 2 will form Controlled 1 and contribute all of its assets relating to Business B to Controlled 1 in exchange for Controlled 1 stock and the assumption by Controlled 1 of certain of the liabilities related to those assets (the "First Contribution").
- (ii) Distributing 2 will distribute all the outstanding shares of Controlled 1 to Distributing 1 (the "First Distribution").
- (iii) Distributing 1 will distribute all the outstanding shares of Controlled 1 and Controlled 2 to Parent (the "Second Distributions").
- (iv) Parent will contribute the stock of Controlled 1 and Controlled 2 (received in step (iii), above), as well as certain assets relating to Business B, to Controlled 3 in constructive exchange for additional stock of Controlled 3 and the assumption of certain liabilities (the "Second Contribution").
- (v) Parent, the sole shareholder of Controlled 3, will approve a resolution amending the certificate of incorporation of Controlled 3 so that it will have two classes of stock (class A common stock and class B common stock) that mirror the capital structure of Parent. After the amendments Parent will exchange all of its Controlled 3 common stock for shares of new Controlled 3 class A common stock and class B common stock such that Parent will have the same number of shares of new class A and class B common stock of Controlled 3 that it currently has outstanding with its own shareholders (together the "Exchange"). It has been represented that the Exchange will qualify under § 368(a)(1)(E).
- (vi) Parent will distribute all of the outstanding shares of new Controlled 3 stock to its shareholders (the "Third Distribution").

Following the proposed transaction the Distributing 1 consolidated group will consist only of assets used in the conduct of Business A.

Also, in connection with the proposed transaction, Controlled 1, Controlled 2 and Controlled 3 may enter into short term agreements with Parent, or subsidiaries related to Parent, concerning certain administrative services (the "Transitional Agreements").

The taxpayer has made the following representations in connection with the First Contribution and the First Distribution:

- (a) No part of the consideration to be distributed by Distributing 2 will be received by Distributing 1 as a creditor, employee, or in any capacity other than that of a shareholder of the corporation.
- (b) The five years of financial information submitted on behalf of Distributing 2 represents the corporation's present operations. There have been no substantial operational changes since the date of the last financial statements submitted.
- (c) Following the First Distribution, Distributing 2 and Controlled 1 will each continue the active conduct of its respective business, independently and with its separate employees, except for the Transitional Agreements.
- (d) The First Distribution is being carried out to facilitate the Third Distribution. The distribution of Controlled 1 stock is motivated, in whole or substantial part, by this corporate business purpose.
- (e) The transaction is not used principally as a device for the distribution of the earnings and profits of Distributing 2, Controlled 1, or both.
- (f) There is no acquisition of stock of Distributing 2 or Controlled 1 (including any predecessor or successor of any such corporation) that is part of a plan or series of related transactions (within the meaning of § 1.355-7T) that includes the distribution of the Controlled 1 stock.
- (g) The total adjusted bases and fair market value of the assets transferred to Controlled 1 by Distributing 2 equals or exceeds the sum of the liabilities assumed by Controlled 1 plus any liabilities to which the transferred assets are subject.
- (h) The liabilities assumed and liabilities to which the transferred assets are subject were incurred in the ordinary course of business and are associated with assets being transferred.
- (i) Except for some short-term accounts payable for internal services that may have been rendered but not yet paid by Controlled 1 at the time of the

First Distribution, no intercorporate debt will exist between Distributing 2 and Controlled 1 at the time of, or subsequent to, the First Distribution .

- (j) Immediately before the First Distribution, items of income, gain, loss, deduction, and credit will be taken into account as required by the applicable intercompany transaction regulations. Further, Distributing 2's excess loss account with respect to the Controlled 1 stock, if any, will be included in income immediately before the First Distribution.
- (k) Payments made in connection with all continuing transactions between Distributing 2 and Controlled 1 will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.
- (l) No two parties to the First Distribution are investment companies as defined in § 368(a)(2)(F)(iii) and (iv).

The taxpayer has made the following representations in connection with the Second Distributions:

- (aa) No part of the consideration to be distributed by Distributing 1 will be received by Parent as a creditor, employee, or in any capacity other than that of a shareholder of the corporation.
- (bb) The five years of financial information submitted on behalf of Distributing 2, Controlled 1 and Controlled 2 represents each corporations' respective present operations. There have been no substantial operational changes since the date of the last financial statements submitted.
- (cc) Immediately after the Second Distributions, at least 90% of the fair market value of the gross assets of Distributing 1 will consist of stock and securities of controlled corporations that are engaged in the active conduct of a trade or business as defined in § 355(b)(2).
- (dd) Following the Second Distribution, Distributing 1, Controlled 1 and Controlled 2 will each continue the active conduct of its respective business, independently and with its separate employees, except for the Transitional Agreements.
- (ee) The Second Distributions are being carried out to facilitate the Third Distribution. The distributions of stock of Controlled 1 and Controlled 2 are motivated, in whole or substantial part, by this corporate business purpose.

- (ff) The transaction is not used principally as a device for the distribution of the earnings and profits of the Distributing 1, Controlled 1, or Controlled 2, or both.
- (gg) There is no acquisition of stock of Distributing 1, Controlled 1 or Controlled 2 (including any predecessor or successor of any such corporation) that is part of a plan or series of related transactions (within the meaning of § 1.355-7T) that includes the distributions of the controlled corporations stock.
- (hh) Except for some short-term accounts payable for internal services that may have been rendered but not yet paid by Controlled 1 or Controlled 2 at the time of the Second Distributions, no intercorporate debt will exist between Parent, Controlled 1 and Controlled 2 at the time of, or subsequent to the Second Distributions.
- (ii) Immediately before the Second 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 excess loss account with respect to Controlled 1 stock, if any, and Controlled 2 Stock, if any, will be included in income immediately before the Second Distribution.
- (jj) Payments made in connection with all continuing transactions, if any, between Distributing 1 and its subsidiaries and Controlled 1 or Controlled 2 will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.
- (kk) No parties to the Second Distributions are investment companies as defined in Code §§ 368(a)(2)(F)(iii) and (iv).
- (ll) Distributing 1 will not be a United States real property holding corporation as defined in § 897(c)(2) at the time of the Second Distribution.

The taxpayer has made the following representations in connection with the Second Contribution and Third Distribution:

- (aaa) No part of the consideration to be distributed by Parent will be received by any shareholder as a creditor, employee, or in any capacity other than that of a shareholder of the corporation.
- (bbb) The five years of financial information submitted on behalf of Parent and Controlled 3 represents the corporations' present operations. There have been no substantial operational changes since the date of the last financial statements submitted.

- (ccc) Following the Third Distribution, Parent and Controlled 3 will each continue the active conduct of its respective business, independently and with its separate employees except for the Transitional Agreements.
- (ddd) The Third Distribution is carried out for the following corporate business purpose: to permit senior management to focus exclusively on achieving the distinctive and complex strategic business plan of either Business A or Business B, but not both. The distributions are motivated, in whole or in substantial part, by this corporate business purpose.
- (eee) The transaction is not used principally as a device for the distribution of the earnings and profits of Parent or the Controlled 3 or both.
- (fff) There is no acquisition of stock of Parent or Controlled 3 (including any predecessor or successor of any such corporation) that is part of a plan or series of related transactions (within the meaning of § 1.355-7T) that includes the distribution of the controlled corporation stock.
- (ggg) The total adjusted bases and fair market value of the assets transferred to Controlled 3 by Parent equals or exceeds the sum of the liabilities assumed by Controlled 3 plus any liabilities to which the transferred assets are subject.
- (hhh) The liabilities assumed and liabilities to which the transferred assets are subject were incurred in the ordinary course of business and are associated with assets being transferred.
- (iii) Except for some short-term accounts payable for internal services that may have been rendered but not yet paid by Controlled 1, Controlled 2 or Controlled 3 at the time of the Third Distribution, no intercorporate debt will exist between Parent and Controlled 3 at the time of, or subsequent to, the Third Distribution.
- (jjj) Payments made in connection with all continuing transactions between Parent (and its subsidiaries) and Controlled 3 (and its subsidiaries) will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.
- (kkk) No two parties to the Third Distribution are investment companies as defined in §§ 368(a)(2)(F)(iii) and (iv).
- (III) Neither Controlled 1 nor Controlled 2 will be a United States real property holding corporation as defined in § 897(c)(2) as it relates to the Second Contribution.

Based solely on the information and representations set forth herein, we rule as follows for the First Contribution and the First Distribution:

- (1) The First Contribution followed by the First Distribution will be a reorganization within the meaning of § 368(a)(1)(D). Distributing 2 and Controlled 1 will each be a “party to the reorganization” within the meaning of § 368(b).
- (2) Distributing 2 will recognize no gain or loss upon the First Contribution (§§ 361(a) and 357).
- (3) Controlled 1 will recognize no gain or loss upon the First Contribution (§1032(a)).
- (4) Controlled 1’s basis for each asset received in the First Contribution will equal the basis of that asset in the hands of Distributing 2 immediately prior to the transfer (§ 362(b)).
- (5) Controlled 1’s holding period for each asset received in the First Contribution will include the period during which Distributing 2 held such asset (§ 1223(2)).
- (6) Distributing 2 will recognize no gain or loss upon the First Distribution (§ 361(c)).
- (7) Distributing 1 will recognize no gain or loss and no amount will be includible in its income upon the First Distribution (§ 355(a)(1)).
- (8) The holding period of the Controlled 1 stock received by Distributing 1 in the First Distribution will include the holding period of the Distributing 2 stock, provided that Distributing 1 held the Distributing 2 stock as a capital asset on the date of the First Distribution (§ 1223(1)).
- (9) Earnings and profits will be allocated between Distributing 2 and Controlled 1 in accordance with §§ 1.312-10(a) and 1.1502-33.

Based solely on the information and representations set forth herein, we rule as follows for the Second Distributions:

- (10) Distributing 1 will recognize no gain or loss upon the Second Distributions (§ 355(c)).

- (11) Parent will recognize no gain or loss and no amount will be included in its income upon the receipt of the Controlled 1 and Controlled 2 stock (§ 355(a)(1)).
- (12) Distributing 1 will recognize no gain or loss upon the Second Distributions (§§ 367(e) and 1.367(e)-1(c)).
- (13) The aggregate basis of the Distributing 1, Controlled 1 and Controlled 2 stock held by Parent after the Second Distributions will equal the basis of the Distributing 1 stock held by Parent immediately before the Second Distribution, allocated in proportion to the fair market value of the Distributing 1, Controlled 1 and Controlled 2 stock in accordance with § 1.358-2(a)(2) (§358(a), (b), and (c)).
- (14) The holding period of the Controlled 1 stock and Controlled 2 stock received by Parent in the Second Distributions will include the holding period of the Distributing 1 stock on which the Second Distributions will be made, provided that Parent holds the Distributing 1 stock as a capital asset on the date of the Second Distributions (§ 1223(1)).

Based solely on the information and representations set forth herein, we rule as follows for the Second Contribution and Third Distribution:

- (15) The Second Contribution followed by the Third Distribution will constitute a reorganization within the meaning of § 368(a)(1)(D). Parent and Controlled 3 will each be a “party to the reorganization” within the meaning of § 368(b).
- (16) Parent will recognize no gain or loss upon the Second Contribution (§§ 361(a) and 357).
- (17) Controlled 3 will recognize no gain or loss upon the Second Contribution (§1032(a)).
- (18) Controlled 3’s basis for each asset received in the Second Contribution will equal the basis of that asset in the hands of Parent immediately prior to the Second Contribution (§ 362(b)).
- (19) Controlled 3’s holding period for each asset received in the Second Contribution will include the period during which Parent held such asset (§ 1223(2)).
- (20) Parent will recognize no gain or loss upon the Third Distribution (§ 361(c)).

- (21) The shareholders of Parent will recognize no gain or loss and no amount will be includible in their income upon the Third Distribution (§ 355(a)(1)).
- (22) The holding period of the Controlled 3 stock received by each shareholder of Parent in the Third Distribution will include the holding period of the Parent stock, provided that shareholder of Parent held the Parent stock as a capital asset on the date of the Third Distribution (§ 1223(1)).

No opinion is expressed about the tax treatment of the proposed transactions under other provisions of the Code or regulations or the tax treatment of any conditions existing at the time of, or effects resulting from, the proposed transactions that are not specifically covered by the above rulings. In particular, no opinion is expressed regarding: (i) whether the First Distribution, Second Distributions or Third Distribution satisfy the business purpose requirement of § 1.355-2(b); (ii) whether the proposed transaction is used principally as a device for the distribution of earnings and profits of the distributing corporations or the controlled corporations or both (see § 355(a)(1)(B) and § 1.355-2(d)); and (iii) whether the First Distribution, Second Distributions or Third Distribution and an acquisition or acquisitions are part of a plan (or series of related transactions) under § 355(e)(2)(A)(ii). Additionally, no opinion is expressed as to whether the transaction described in step (v) qualifies as a reorganization under § 368(a)(1)(E).

This ruling is directed on to the taxpayer 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 must be attached to any income tax return to which it is relevant.

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

Sincerely,  
Mark J. Weiss  
Mark J. Weiss  
Acting Assistant to the Chief, Branch 6  
Office of Associate Chief Counsel  
(Corporate)