Internal Revenue Service

Department of the Treasury

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Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:

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May 18, 2000

Distributing =

Number: **200033034** Release Date: 8/18/2000

Controlled =

State X =

<u>A</u> =

B =

C =

business $\underline{m} =$

business n =

Date 1 =

This letter replies to a request for rulings, dated February 1, 2000, on the federal income tax consequences of a proposed transaction concerning § 355 of the Internal Revenue Code. We received additional information in letters dated March 27, April 3, and May 8, 2000. The information submitted for consideration is summarized below.

Distributing, a State \underline{X} corporation, is the common parent of an affiliated group that files a consolidated return. Distributing has a single class of voting common stock outstanding which is held by three individuals: \underline{A} , his ex-wife \underline{B} , and \underline{A} 's sister, \underline{C} . Distributing conducts business \underline{m} , and until Date 1, which is approximately three years prior to the date of this letter, Distributing also conducted business \underline{n} . On Date 1, Distributing contributed the assets of business \underline{n} to Controlled, a wholly owned subsidiary, in exchange for Controlled stock and the assumption of the liabilities of business \underline{n} (the "Date 1 Exchange"). Presently, \underline{A} and \underline{B} operate business \underline{m} with little or no involvement in business \underline{n} while \underline{C} operates business \underline{n} with little or no involvement in business \underline{m} . Distributing and Controlled each use the accrual method of

accounting.

We have received financial information indicating that business \underline{m} and business \underline{n} have had gross receipts and operating expenses representative of the active conduct of a trade or business for each of the past five years.

 \underline{A} , \underline{B} , and \underline{C} wish to focus their efforts exclusively on the business with which they are most involved. Specifically, \underline{A} and \underline{B} wish to concentrate on business \underline{m} , and \underline{C} wishes to concentrate on business \underline{n} . Accordingly, it has been proposed that \underline{C} exchange all of her Distributing stock for all of the Controlled stock held by Distributing.

The following representations have been made in connection with the proposed transaction:

- (a) The fair market value of the Controlled stock to be received by <u>C</u> approximately equals the fair market value of the Distributing stock surrendered by <u>C</u> in the exchange.
- (b) No part of the consideration to be distributed by Distributing will be received by a shareholder as a creditor, employee, or in any capacity other than that of a shareholder of the corporation.
- (c) The five years of financial information submitted on behalf of Distributing is representative of the corporation's present operations, and there have been no substantial operational changes since the date of the last financial statements submitted.
- (d) The five years of financial information concerning business <u>n</u> submitted on behalf of Controlled is representative of the corporation's present operations, and there have been no substantial operational changes since the date of the last financial statements submitted.
- (e) Following the transaction, Distributing and Controlled will each continue the active conduct of its business, independently and with its separate employees.
- (f) The distribution of stock of Controlled is being carried out for the following corporate business purpose: to allow Distributing's shareholders to focus their efforts exclusively on the business with which they are most involved. The distribution of the stock of Controlled is motivated, in whole or substantial part, by this corporate business purpose.
- (g) There is no plan or intention by the shareholders of Distributing to sell, exchange, transfer by gift, or otherwise dispose of any of their stock in either Distributing or Controlled subsequent to the proposed transaction.

- (h) There is no plan or intention by either Distributing 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 § 4.05(1)(b) of Rev. Proc. 96-30.
- (i) There is no plan or intention to liquidate Distributing or Controlled, to merge either corporation with any other corporation, or to sell or otherwise dispose of the assets of either corporation subsequent to the transaction, except in the ordinary course of business.
- (j) No property will be transferred to Controlled and no liabilities will be assumed by Controlled in connection with the proposed transaction.
- (k) No intercorporate debt will exist between Distributing and Controlled at the time of, or subsequent to, the distribution of Controlled stock.
- (I) 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. Furthermore, Distributing's excess loss account with respect to the Controlled stock, if any, will be included in income immediately before the distribution.
- (m) Payments made in connection with all continuing transactions between Distributing and Controlled will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.
- (n) 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 percent or more of the combined voting power of all classes of stock of either Distributing or Controlled, or stock possessing 50 percent or more of the total value of all classes of stock of either Distributing or Controlled.
- (o) No gain or loss was recognized on the Date 1 Exchange.

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

- (1) <u>C</u> will recognize no gain or loss (and no amount will be included in the income of <u>C</u>) upon the receipt of the Controlled stock in exchange for all of her Distributing stock, as described above (§ 355(a)(1)).
- (2) Distributing will recognize no gain or loss upon the distribution of all of its Controlled stock (§ 355(c)).

- C 's basis in her Controlled stock will equal her aggregate basis in the (3)Distributing stock surrendered in the exchange (§ 358(a)(1)).
- The holding period of the Controlled stock received by C will include the holding (4) period of the Distributing stock surrendered in the exchange, provided that the Distributing stock is held as a capital asset on the date of the exchange (§ 1223(1)).
- (5) The allocation of, and adjustments to, earnings and profits between Distributing and Controlled will be made in accordance with § 312(h) and §§ 1.312-10(b) and 1.1502-33 of the Income Tax Regulations.

No opinion was requested, and no opinion is expressed, concerning the tax treatment of the Date 1 Exchange. We also 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.

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

Each affected taxpayer must attach a copy of this letter to the taxpayer's federal income tax return for the tax year in which the transaction covered by this ruling letter is consummated.

We have sent a copy of this letter to the taxpayer pursuant to the power of attorney on file in this office.

> Sincerely yours, Assistant Chief Counsel (Corporate)

Assistant to the Chief, Branch 3

By: Michael J. Wilder