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Department of the Treasury

Washington, DC 20224

Person to Contact:

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Refer Reply To:
CC:CORP:3-PLR-100611-02
Date:
June 25, 2002

Re:

Distributing 1 =

Distributing 2 =

Controlled =

State X =

Sub 1 =

Sub 2 =

Sub 2 LLC =

Y =

Z =

Trust A =

A	=
Sibling	=
$b	=
c	=
d	=
$e	=
$f	=
g	=
$h	=
i	=
$j	=
k	=
l	=
m	=
n	=
$o	=
$p	=
q	=
r	=
Bank Debt	=
Business R	=
Business S	=
Business T	=

Business U =

Location R =

Location S =

Year =

Date 1 =

Date 2 =

Date 3 =

Family Group 1 =

Family Group 2 =

Family Group 3 =

Dear :

We respond to your December 28, 2001, request for rulings on certain federal income tax consequences of a proposed transaction. Additional information was submitted in letters dated March 12, May 3, May 30, and June 6, 2002. The information submitted is summarized below.

Summary of Facts

Distributing 2 is the common parent of a group of corporations whose includible affiliates join in filing a consolidated federal income tax return. Distributing 2 has three classes of stock outstanding: 1) noncumulative, nonvoting preferred stock, 2) nonvoting Class A common stock, and 3) voting Class B common stock. The stock is beneficially owned by the widow and descendants of A (deceased). Many of the shares are actually owned directly and through various partnerships and trusts created for the benefit of the family groups headed by each child of A. In addition, Trust A owns the majority of the Class B shares. The trust agreement for Trust A provides that on the death of A, which occurred on Date 1, $b would be set aside for the grandchildren of A with the remainder of the trust being divided into equal shares for the benefit of A's children.

Distributing 2 owns c percent (which is greater than 80 percent) of the stock of Distributing 1. The remaining shares are held by a few unrelated minority shareholders. Distributing 1 owns all of the stock of Sub 1. Sub 1 owns d percent of Sub 2. The remaining shares of Sub 2 are owned by the public. Although Sub 1 does not own a majority of Sub 2 stock, it has effective control.

Distributing 2 is a holding company that does not conduct an active trade or business directly but relies on its ownership of Distributing 1 to satisfy the active trade or business requirement of § 355(b). Distributing 1 conducts Business R, Business S, Business T, and Business U. You have submitted financial information indicating that the conduct of these businesses each have generated gross receipts and operating expenses representing the active conduct of a trade or business for each of the past five years.

During the past five years the following transfers of Distributing 2 stock have occurred. First, in connection with a Date 2 settlement of certain claims against Sibling (one of A's children), Distributing 2 issued debentures in an aggregate amount of $e, with a debenture in the amount of $f issued to Trust A in redemption of g shares of Distributing Class B common stock (the Trust Debenture) and the remaining $h in debentures issued to the family groups in redemption of the i shares of Distributing 2 Class A stock held by each family group (the Shareholder Debentures). In addition, on Date 3, Distributing 2 issued additional debentures totaling $j to members of Family Group 2 in redemption of k shares of Distributing 2 Class A common stock (the Family Group 2 Debentures). Second, in the later half of Year, the Family Group 1 and Family Group 3 limited partnerships terminated, Distributing 2 stock was distributed to the partners, and the recipients re-contributed to new limited family partnerships (the Partnership Transfers).

Proposed Transaction

The shareholders of Distributing 2, especially the family groups and entities collectively known as Z, have had serious disputes with and concerning the management practices of Sibling and the operation of the businesses conducted by Distributing 1. These disputes have resulted in litigation. The following transaction has been proposed to settle the disputes:

(i) Sub 1 will merge into Sub 2 LLC, a newly formed single member LLC wholly-owned by Distributing 1. Sub 2 LLC will be disregarded for Federal income tax purposes (Sub 1 Liquidation or Merger);

(ii) Distributing 1 will borrow approximately $p from an outside lender or lenders (the Bank Debt) to complete certain corporate projects and to equalize values of Z's interests in Distributing 2 and Controlled;

(iii) Distributing 1 will form a single member LLC, Y LLC, and transfer assets from Business R (including Location R) and Business S (including Location S) to Y LLC. Y LLC will assume the Bank Debt to equalize values. Y LLC will be disregarded for Federal income tax purposes;

(iv) Sub 2 LLC will distribute all of its assets, other than its Sub 2 stock and

Z's share in the Sub 2 dividends, to Distributing 1;

(v) Distributing 1 will organize Controlled as a State X corporation and contribute to it all of its interest in Y LLC and Sub 2 LLC in exchange for q shares of Controlled nonvoting Class A common stock and r shares of Controlled voting Class B common stock (the Contribution);

(vi) Trust A will be divided into l separate trusts, one for each of the m children of A and each of the n grandchildren of A, all beneficiaries of Trust A. The tax consequences of this trust separation will be the subject of a separate private letter ruling request. The separation, if approved, will occur immediately before, and on the same day as, the distributions described below;

(vii) Distributing 1 will distribute all of its Controlled stock pro rata to its shareholders (the First Distribution);

(viii) Distributing 2 will distribute all of its Controlled stock to Z in exchange for all of their Distributing 2 stock (the Second Distribution). For each share of Distributing 2 Class A or Class B common stock surrendered by a member of Z, each shareholder will receive an equivalent share of Controlled Class A or Class B common stock; and

(ix) Distributing 2 will redeem all of the preferred stock held by Z for $o a share.

Representations

Distributing 2 has made the following representations concerning the Sub 1 Liquidation:

(a) Distributing 1, on the date of adoption of the plan for the Merger, and at all times until the Merger is completed, will be the owner of at least 80 percent of the single outstanding class of Sub 1 stock.

(b) No shares of Sub 1 stock will have been redeemed during the three years preceding the adoption of the Merger plan.

(c) The Merger will take place within a single taxable year of Sub 1.

(d) Effective as of the date of the Merger, the corporate existence of Sub 1 will cease under state law.

(e) Sub 1 will retain no assets following the Merger.

(f) Sub 1 will not have acquired assets in any nontaxable transaction at any time, except for acquisitions occurring more than 3 years prior to the date of adoption of the plan of Merger.

(g) Other than the possible transfers of Sub 2 LLC interests to Controlled, followed by the First and Second Distributions, no assets of Sub 1 have been or will be disposed of by either Sub 1 or Distributing 1, except for dispositions in the ordinary course of business and dispositions occurring more than three years prior to adoption of the plan of Merger.

(h) Other than the possible transfers of Sub 2 LLC interests to Controlled, the Merger will not be preceded or followed by the reincorporation in, or transfer or sale to, a recipient corporation (Recipient) of any of the businesses or assets of Sub 1, if persons holding, directly or indirectly, more than 20 percent in value of the Sub 1 stock also hold, directly or indirectly, more than 20 percent in value of the stock in Recipient. For purposes of this representation, ownership will be determined by application of the constructive ownership rules of § 318(a) as modified by § 304(c)(3).

(i) Prior to adoption of the Merger plan, no assets of Sub 1 will have been distributed in kind, transferred, or sold to Distributing 1, except for (i) transactions occurring in the normal course of business and (ii) transactions occurring more than 3 years prior to adoption of the Merger plan.

(j) Sub 1 will report all earned income represented by assets that will be deemed distributed to Distributing 1, such as receivables being reported on a cash basis, unfinished construction contracts, commissions due, etc.

(k) The fair market value of the assets of Sub 1 will exceed its liabilities both at the date of the adoption of the plan of Merger and immediately prior to the time the Merger occurs.

(l) There is no intercorporate debt existing between Distributing 1 and Sub 1 and none has been canceled, forgiven, or discounted, except for transactions that occurred more than three years prior to the date of adoption of the Merger plan.

(m) Distributing 1 is not an organization that is exempt from federal income tax under § 501 or any other provision of the Code.

(n) All other transactions undertaken contemporaneously with, in anticipation of, in conjunction with, or in any way related to, the proposed Merger of Sub 1 have been fully disclosed.

Distributing 2 has made the following representations concerning the First

Distribution and Second Distributions:

(o) No part of the consideration to be distributed by Distributing 1 or Distributing 2 will be received by a shareholder as a creditor, employee, or in any capacity other than that of a shareholder of the corporation.

(p) The fair market value of the Controlled stock and other consideration to be received by Z will be approximately equal to the fair market value of the Distributing 2 stock surrendered by Z in the exchange.

(q) The five years of financial information submitted on behalf of Distributing 1 is representative of Distributing 1's present operations, and with regard to Distributing 1, there have been no substantial operational changes since the date of the last financial statements submitted.

(r) Immediately after the Second Distribution, at least 90 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).

(s) Immediately after the First and Second Distributions, the fair market value of the assets that comprise each directly operated business of Distributing 1 and Controlled being relied upon to meet the active trade or business test of § 355(b) will, in each instance, equal or exceed five percent of the total fair market value of the gross assets of the company directly operating such business.

(t) Following the transaction, Distributing 1, Distributing 2, and Controlled each will continue the active conduct of its businesses, independently and with its separate employees.

(u) The First and Second Distributions are carried out for one or more of the following corporate business purpose: to resolve shareholder disputes pursuant to a settlement agreement. The First and Second Distributions are motivated, in whole or substantial part, by this corporate business purpose.

(v) Other than the Second Distribution, there is no plan or intention by 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 transaction.

(w) There is no plan or intention by the shareholders or security holders of Distributing 2 to sell, exchange, transfer by gift, or otherwise dispose of any of their stock in, or securities of, either Distributing 2 or Controlled after the transaction.

(x) There is no plan or intention by either 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 § 4.05(1)(b) of Rev. Proc. 96-30, 1996-1 C.B. 696, 705.

(y) There is no plan or intention to liquidate Distributing 1, Distributing 2, or Controlled, to merge either corporation into any other corporation, or to sell or otherwise dispose of the assets of any of these corporations after the transaction, except in the ordinary course of business.

(z) The total adjusted bases and the fair market value of the assets transferred to Controlled by Distributing 1 each equals or exceeds the sum of the liabilities assumed (as determined under § 357(d)) by Controlled .

(aa) Except for the Bank Debt, the liabilities assumed in the transaction (as determined under § 357(d)) 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.

(bb) No intercorporate debt will exist between Distributing 1 or Distributing 2 and Controlled at the time of, or subsequent to, the distributions of the Controlled stock.

(cc) Immediately before the First and Second Distributions, 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, 1995-2 I.R.B. 6, and as currently in effect; §1.1502-13 as published by T.D. 8597). Further, Distributing 1 and/or Distributing 2’s excess loss account with respect to the Controlled stock, if any, will be included in income immediately before the distribution (see § 1.1502-19).

(dd) Payments made in connection with all continuing transactions, if any, between Controlled and either Distributing 1 or Distributing 2 will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm’s length.

(ee) No two parties to the transaction are investment companies as defined in § 368(a)(2)(F)(iii) and (iv).

(ff) The distributions are 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 total value or total combined voting power of all classes of stock of Distributing 1, Distributing 2 or Controlled.

(gg) There was no agreement, understanding, arrangement, or substantial negotiations concerning the First Distribution or the Second Distribution at the time of (i) the redemptions of Distributing 2 stock in connection with the Date 2 settlement, or within six months thereafter, (ii) the transfers of Distributing 2 stock as a result of the termination of the Family Group 1 and Family Group 3 limited partnerships or within six months thereafter, or (iii) the re-contribution of such stock to new family limited partnerships, or within six months thereafter.

Rulings

Based solely on the information submitted and representations made, we rule on the Sub 1 Liquidation as follows:

(1) The Sub 1 Merger will qualify as a distribution by Sub 1 to Distributing 1 in complete liquidation of Sub 1 under § 332 and § 1.332-2(d).

(2) No income, gain or loss will be recognized by Distributing 1 on its deemed receipt of the assets and liabilities of Sub 1 in the Sub 1 Merger (§ 332(a)).

(3) No income, gain or loss will be recognized by Sub 1 on the Sub 1 Merger (§§ 336(d)(3), 337(a) and 337(b)).

(4) The basis Distributing 1 will have in each asset deemed received from Sub 1 as a result of the Sub 1 Merger equals the basis of that asset in the hands of Sub 1 immediately before the Sub 1 Merger (§ 334(b)(1)).

(5) The holding period Distributing 1 will have in each asset deemed received from Sub 1 as a result of the Sub 1 Merger includes the period during which that asset was held by Sub 1 (§ 1223(2)).

(6) Distributing 1 will succeed to and take into account the items of Sub 1 described in § 381(c), subject to the conditions and limitations specified in §§ 381, 382, 383 and 384 and the regulations thereunder (§ 381(a); § 1.381(a)-1).

(7) Distributing 1 will succeed to and takes into account the earnings and profits, or deficit in earnings and profits, of Sub 1 as of the date of the Sub 1 Merger (§ 381(c)(2)(A); § 1.381(c)(2)-1). Any deficit in the earnings and profits of Sub 1 or Distributing 1 will be used only to offset earnings and profits accumulated after the date of the Sub 1 Merger (§ 381(c)(2)(B)). Notwithstanding the above, to the extent that Sub 1's earnings and profits are reflected in Distributing 1's earnings and profits, the Sub 1 earnings

and profits to which Distributing 1 succeeds must be adjusted to prevent duplication (§ 1.1502-33(a)).

Based solely on the information submitted and representations made, we rule on the First and Second Distributions as follows:

(8) The Contribution by Distributing 1 to Controlled, followed by the pro-rata distribution of the Controlled stock to Distributing 1's shareholders will qualify as a reorganization within the meaning of § 368(a)(1)(D). Distributing 1 and Controlled each will be a "party to the reorganization" within the meaning of § 368(b).

(9) No gain or loss will be recognized by Distributing 1 in the Contribution in exchange for Controlled stock (§§ 361(a) and 357(a)).

(10) No gain or loss will be recognized by Controlled on the Contribution in exchange for Controlled stock (§ 1032(a)).

(11) The basis of each asset received by Controlled in the Contribution will equal the basis of that asset in the hands of Distributing 1 immediately before the Contribution (§ 362(b)).

(12) The holding period of each asset received by Controlled in the Contribution will include the holding period of that asset in the hands of Distributing 1 (§ 1223(2)).

(13) Distributing 1 will recognize no gain or loss on the First Distribution (§§ 355(c), 355(d), 355(e), 361(c)(1)) and Rev. Rul. 62-138, 1962-2 C.B. 95).

(14) No gain or loss will be recognized by (and no amount will be included in the income of) Distributing 2 or the minority shareholders on the First Distribution (§ 355(a)(1)).

(15) The aggregate basis of the Distributing 1 stock and the stock of Controlled in the hands of each Distributing 1 shareholder after the First Distribution will equal the basis of the Distributing 1 stock held by the shareholder immediately before the First Distribution. This aggregate basis will be allocated between the Distributing 1 and Controlled stock in proportion to the fair market values of the Distributing 1 and Controlled stock immediately after the First Distribution in accordance with § 1.358-2(a)(2) (§§ 358(a)(1), (b) and (c)).

(16) The holding period of the Controlled stock received by each Distributing 1 shareholder in the First Distribution will include the holding period of the Distributing 1 stock on which the First Distribution will be made, provided the Distributing 1 stock is held as a capital asset on the date of the First Distribution (§ 1223(1)).

(17) Proper allocation of earnings and profits between Distributing 1 and Controlled will be made under §§ 1.312-10(a) and 1.1502-33.

(18) No gain or loss will be recognized by Distributing 2 on the distribution of Controlled stock to Z in exchange for their Distributing 2 stock (§§ 355(c), 355 (d), 355(e), § 1.355-7T(d)(4) of the Income Tax Regulations, and Rev. Rul. 62-138, 1962-2 C.B. 95).

(19) Z will recognize no gain or loss on their receipt of Controlled stock in exchange for Distributing 2 stock in the Second Distribution (§ 355(a)).

(20) Z's basis in the Controlled stock after the Second Distribution will equal the basis of the Distributing 2 stock surrendered in exchange therefor (§ 362(b)).

(21) The holding period of the Controlled stock received by Z will include the holding period of the Distributing 2 stock surrendered in the exchange, provided the Distributing 2 stock is held as a capital asset on the date of the Second Distribution (§ 1223(1)).

(22) Proper allocation of earnings and profits between Distributing 2 and Controlled will be made under §§ 1.312-10(b) and 1.1502-33.

No opinion is requested and no opinion is expressed concerning steps (iii), (iv), (vi), and (ix) above. Additionally, 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. Specifically, we express no opinion on the tax consequences or characterization upon the issuance of the Trust Debenture, the Shareholders Debentures, and the Family Group 2 Debenture or the Partnership Transfers.

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. See § 12.04 of Rev. Proc. 2002-1, 2002-1 I.R.B. 1, 50, which discusses in greater detail the revocation or modification of ruling letters. However, when the criteria in § 12.05 of Rev. Proc. 2002-1 are satisfied, a ruling is not revoked or modified retroactively except in rare or unusual circumstances.

This ruling is directed only to the taxpayer 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 ruling letter be attached to the federal income tax return of each party 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, a copy of this letter has been sent to the taxpayer.

Sincerely yours,

Filiz A. Serbes

Filiz A. Serbes
Chief, Branch 3
Office of Associate Chief Counsel (Corporate)

cc: