

Internal Revenue Service

Department of the Treasury

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Person to Contact:

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Date:

April 16, 2002

LEGEND:

Distributing =

Controlled =

Corporation A =

Corporation B =

Corporation C =

Business A =

Business B =

Shareholder 1 =

Shareholder 2 =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Date 6 =

Date 7 =

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Date 8 =

a =

b =

c =

d =

e =

f =

Dear

This letter responds to your request for rulings regarding certain federal income tax consequences of a proposed transaction. The information submitted in that request and in later correspondence is summarized below.

SUMMARY OF FACTS

Distributing is a domestic corporation that is the common parent of an affiliated group of corporations that files a consolidated federal income tax return. Distributing has two classes of stock issued and outstanding. One class of Distributing stock is publicly traded.

Distributing is indirectly engaged in Business A through its wholly owned subsidiary Corporation A. Corporation A is indirectly engaged in Business A through its wholly owned subsidiaries Corporation B and Corporation C. Corporation B and Corporation C, respectively, each are directly engaged in Business A. In addition, Distributing is indirectly engaged in Business B through its subsidiary Controlled.

By agreement dated Date 1, and amended as of Date 2, Distributing and Corporation A agreed to engage in a tax-free merger transaction (the "Merger"). The taxpayer has represented that the Merger, which became effective on Date 3, qualified as a tax-free reorganization. In the Merger, a wholly owned subsidiary of Distributing merged with and into Corporation A with Corporation A surviving as a wholly owned subsidiary of Distributing. The shareholders of Corporation A stock exchanged their Corporation A stock for shares of Distributing stock that represented less than a percent (by vote and value) of the outstanding stock of Distributing immediately after the Merger.

Controlled was formed by Distributing on Date 4 as a wholly owned subsidiary. On Date 5, Distributing transferred to Controlled the assets constituting Business B, and

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Controlled assumed the liabilities relating thereto in a transaction that the taxpayer has represented qualified for nonrecognition of gain or loss. On Date 6, Controlled sold b shares of its common stock to the public in a partial initial public offering (the "IPO"). Subsequent to the IPO, Distributing owned (and continues to own) c shares of Controlled common stock – the sole class of issued and outstanding Controlled stock – representing approximately d percent of the e shares of Controlled common stock outstanding as of Date 7. Controlled stock is publicly traded.

Distributing and Controlled will have entered into a Tax Sharing Agreement ("Tax Sharing Agreement") that will be in effect at the time of, and subsequent to, the Distribution (as defined herein).

Financial information has been received which indicates that Distributing's Business A and Controlled's Business B each has had gross receipts and operating expenses representative of the active conduct of a trade or business for each of the past five years.

Business A and Business B are substantially different, incompatible businesses, and their present coexistence within the same affiliated group creates management, systematic and other problems that can only be resolved through a complete separation of the two businesses. Distributing has presented documentation, including internal reports and reasoned analyses of an outside financial advisor and independent analysts, as well as other materials, to substantiate the corporate business purpose for the complete separation of Business A from Business B.

PROPOSED TRANSACTION

Accordingly, to enhance the success of Business A and Business B by enabling Distributing and Controlled to resolve the management and systematic and other problems that arise by the operation of the two businesses within a single affiliated group, the following transaction is proposed: Distributing will distribute all of the shares of Controlled common stock held by Distributing (representing at least 80 percent of the sole class of issued and outstanding shares of Controlled stock) to the holders of Distributing's common stock, pro rata, in proportion to their ownership of Distributing (the "Distribution"), and cash will be distributed in lieu of fractional shares on the effective date of the Distribution (the "Distribution Date"). The Distribution will take place on or after Date 8. Before the Distribution, Controlled may redeem up to approximately f percent of its stock that is held by Distributing.

REPRESENTATIONS

Distributing has made the following representations regarding the proposed transaction:

- (a) The indebtedness, if any, owed by Controlled to Distributing after the Distribution will not constitute stock or securities.

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- (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, Corporation A, Corporation B and Corporation C is representative of each corporation's present operation, and with regard to each such corporation, there have been no substantial operational changes since the date of the last financial statements submitted.
- (d) Immediately after the Distribution, at least 90 percent of the fair market value of the gross assets of Distributing will consist of the stock of its controlled subsidiary Corporation A.
- (e) Immediately after the Distribution, at least 90 percent of the fair market value of the gross assets of Corporation A will consist of the stock of Corporation A's controlled subsidiaries Corporation B and Corporation C, each of which is a corporation that is engaged in the active conduct of a trade or business as defined in section 355(b)(2).
- (f) The Business A assets directly held by Corporation B have a fair market value that is at least 5 percent of the total fair market value of Corporation B's gross assets.
- (g) The Business A assets directly held by Corporation C have a fair market value that is at least 5 percent of the total fair market value of Corporation C's gross assets.
- (h) The five years of financial information submitted on behalf of Controlled 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.
- (i) The Business B assets directly held by Controlled have a fair market value that is at least 5 percent of the total fair market value of Controlled's gross assets.
- (j) Following the Distribution, Distributing (through Corporation A, Corporation B and Corporation C) and Controlled will each continue the active conduct of its business, independently and with its separate employees.
- (k) The Distribution is being carried out for the following corporate business purpose: to effect fit and focus. The Distribution is motivated, in whole or substantial part, by the foregoing corporate business purpose.

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- (l) There is no plan or intention by any shareholder who owns 5 percent or more of the stock of Distributing, and the management of Distributing, to its best knowledge, is not aware of any plan or intention on the part of any particular remaining shareholder or security holder of Distributing to sell, exchange, transfer by gift, or otherwise dispose of any stock in, or securities of, either Distributing or Controlled after the Distribution. Notwithstanding the foregoing, Shareholder 1 and Shareholder 2 may in the future determine to dispose of or purchase any such stock in the normal course of their respective businesses as investment advisors based upon decisions as to existing market conditions and the needs of investors they represent.
- (m) 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 Distribution, other than through stock purchases meeting the requirements of section 4.05(1)(b) of Rev. Proc. 96-30.
- (n) There is no plan or intention to liquidate either Distributing or Controlled, to merge either corporation with any other corporation, or to sell or otherwise dispose of the assets of either corporation after the Distribution, except in the ordinary course of business.
- (o) For purposes of section 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 Distributing stock entitled to vote, or 50 percent or more of the total value of shares of all classes of Distributing stock, that was acquired by purchase (as defined in sections 355(d)(5) and (8)) during the five-year period (determined after applying section 355(d)(6)) ending on the Distribution Date.
- (p) For purposes of section 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 Controlled stock entitled to vote, or 50 percent or more of the total value of shares of all classes of Controlled stock, that either (i) was acquired by purchase (as defined in sections 355(d)(5) and (8)) during the five-year period (determined after applying section 355(d)(6)) ending on the Distribution Date or (ii) is attributable to distributions on Distributing stock that was acquired by purchase (as defined in sections 355(d)(5) and (8)) during the five-year period (determined after applying section 355(d)(6)) ending on the Distribution Date.
- (q) The Distribution is not part of a plan or series of related transactions (within the meaning of section 355(e)) pursuant to which one or more persons has acquired or will acquire, directly or indirectly, stock

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possessing 50 percent or more of the total combined voting power of all classes of stock of either Distributing or Controlled entitled to vote, or stock possessing 50 percent or more of the total value of all classes of stock of either Distributing or Controlled.

- (r) There was no agreement, understanding, arrangement or substantial negotiations concerning the Distribution at the time of the Merger or within six months thereafter, or at the time of the IPO or within six months thereafter.
- (s) Distributing neither accumulated its receivables nor made extraordinary payment of its payables in anticipation of the Distribution.
- (t) Except with respect to obligations arising out of certain disclosed continuing relationships, no intercorporate debt will exist between Distributing and Controlled at the time of, or subsequent to, the Distribution.
- (u) Immediately before the Distribution, items of income, gain, loss, deduction and credit will be taken into account as required by applicable intercompany transaction regulations (See sections 1.1502-13 and 1.1502-14 as in effect before the publication of T.D. 8597, 1995-2 C.B. 147, and as currently in effect, section 1.1502-13 as published by T.D. 8597). Further, Distributing's excess loss account, if any, with respect to Controlled stock will be included in income immediately before the Distribution. (See section 1.1502-19).
- (v) Payments made in connection with all continuing transactions, if any, 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.

RULINGS

- (1) No gain or loss will be recognized by (and no amount will be included in the income of) Distributing's shareholders upon the receipt of Controlled common stock from Distributing pursuant to the Distribution. Section 355(a)(1).
- (2) No gain or loss will be recognized by Distributing upon the distribution of Controlled common stock to Distributing's shareholders pursuant to the Distribution. Section 355(c)(1).
- (3) The aggregate basis of the Distributing stock and the Controlled common stock in the hands of Distributing's shareholders after the Distribution will be the same as the aggregate basis of the Distributing stock in the hands of Distributing's shareholders immediately before the Distribution,

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allocated between the Distributing stock and the Controlled common stock in proportion to the fair market values of each in accordance with sections 1.358-2(a)(2), (a)(4). See also sections 358(a)(1), (b)-(c).

- (4) The holding period of the Controlled common stock to be received by the Distributing shareholders will include the holding period of their Distributing stock, provided that the Distributing stock is held as a capital asset on the Distribution Date. Section 1223(1).
- (5) The payment of cash in lieu of fractional shares in Controlled will be treated as if the fractional shares were distributed and then redeemed by Controlled. The cash payment will be treated as having been received as a distribution in full payment in exchange for the stock considered redeemed, as provided in section 302(a). See Rev. Rul. 66-365, 1966-2 C.B. 116; Rev. Proc. 77-41, 1977-2 C.B. 574.
- (6) Earnings and profits will be allocated between Distributing and Controlled in accordance with sections 312(h), 1.312-10(b) and 1.1502-33(e).
- (7) Payments made by Distributing to Controlled or by Controlled to Distributing under the Tax Sharing Agreement that (i) have arisen or will arise for a taxable period ending before the Distribution or for a taxable period beginning on or before and ending after the Distribution and (ii) will not become fixed or ascertainable until after the Distribution will be treated as occurring immediately before the Distribution.

CAVEATS

No opinion is expressed about the tax treatment of the transaction under any other provision of the Code or Regulations, or the tax treatment of any conditions existing at the time of, or effects resulting from, the transaction that are not specifically covered by the above rulings. In particular, no opinion is expressed concerning the tax consequences associated with:

- (a) the merger that Distributing and Corporation A entered into on Date 3, pursuant to an agreement dated Date 1, and which was amended on Date 2;
- (b) Distributing's transfer to Controlled on Date 5 of the assets constituting Business B and Controlled's assumption of the liabilities relating thereto; or
- (c) the proposed redemption of Controlled stock which may occur before the Distribution.

PROCEDURAL STATEMENTS

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

A copy of this letter must be attached to the federal income tax return of each taxpayer involved for the taxable year in which the transaction is consummated.

In accordance with the Power of Attorney on file with this office, the original of this letter is being sent to the taxpayer's authorized representative.

Sincerely yours,
Alfred C. Bishop, Jr.
Branch Chief, Branch 6
Associate Chief Counsel (Corporate)