

**Internal Revenue Service**

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Date:  
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Legend

Distributing =

Controlled =

Oldco =

Sub 1 =

Entity 1 =

Entity 2 =

Exchange =

Debt =

Plan 1 =

Plan 2 =

Business X =

Segment X =

Business Y =

Receivables =

Shareholder 1 =

Shareholder 2 =

Individual 1 =

Individual 2 =

Officer =

Date U =

Date V =

Date W =

Date X =

Date Y =

Date Z =

a =

b =

c =

d =

e =

f =

Dear :

This letter responds to your November 13, 2009, request for rulings as to the federal income tax consequences of a Proposed Transaction (as defined below). The information received in that request and in subsequent correspondence is summarized below.

The rulings contained in this letter are based upon facts and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. This office has not verified any of the material 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. In particular, this office has not reviewed any information pertaining to, and has made no determination regarding whether the Distribution (as defined below): (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 (the "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) and § 1.355-7).

### Summary of Facts

Distributing is the common parent of an affiliated group of corporations filing a consolidated federal income tax return. Distributing was incorporated on Date U, as part of a restructuring transaction described in a prior private letter ruling (issued Date V) and is the successor to Oldco. The prior restructuring was consummated on Date W. Oldco is now a wholly owned subsidiary of Distributing.

Distributing has a single class of common stock, a shares of which are issued and outstanding. The Distributing stock is publicly traded on the Exchange. As of Date X, Distributing had b shareholders who owned five percent or more of the common stock of Distributing. In particular, Shareholders 1 and 2 each own c shares of Distributing common stock. Distributing has outstanding certain Debt.

Distributing maintains two stock-based employee compensation plans. Plan 1 provides for grants of (i) incentive and nonqualified stock options; (ii) stock appreciation rights; (iii) restricted stock; (iv) restricted stock units; and (v) other stock or cash-based incentive awards. The maximum aggregate number of shares of common stock that may be issued under this plan is d shares (approximately e of which remain available as of Date Y). Under Plan 2, employees, excluding executive officers, can elect to have a specified amount of wages withheld to purchase Distributing common stock at a specified discount.

Distributing wholly owns Sub 1, Entity 1 and Entity 2. Each of Entity 1 and Entity 2 is a disregarded entity for U.S. federal tax purposes.

Prior to the Proposed Transaction, Distributing is engaged, through disregarded entities and corporations, in Businesses X and Y.

Financial information has been submitted indicating that Segment X (a business line of Business X) and Business Y each has had gross receipts and operating expenses representing the active conduct of a trade or business for each of the past five years.

Business Y is adversely impacting Distributing's Business X operations. Distributing's management believes that the separation of Business X from Business Y is necessary to eliminate the negative effects of Business Y (the "Business Purpose").

### **Proposed Transaction**

To separate Business Y from Business X, the taxpayer proposes the following series of transactions (the "Proposed Transaction"):

- 1) By exchanging \$f of cash for f shares of common stock, Distributing formed Controlled on Date Z as a wholly-owned subsidiary.
- 2) Distributing will transfer to Controlled the following assets:
  - a) Cash to be used in Business Y;
  - b) the stock of Sub 1;
  - c) 100% of the membership interests in Entity 1;
  - d) 100% of the membership interests in Entity 2;
  - e) Receivables; and

- f) certain trade names and other similar intellectual property related to Business Y.

Together, these assets are referred to as the Business Y Assets. This step is hereinafter referred to as the Contribution.

- 3) Distributing will distribute the stock of Controlled to the Distributing shareholders on a pro rata basis. Although the exact distribution ratio has not yet been decided and will not be finally decided until completion of the Proposed Transaction, it is anticipated that the Distributing shareholders will receive one share of Controlled stock for every two shares of Distributing stock that they own. Cash will be issued in lieu of fractional shares. This step is hereinafter referred to as the Distribution.

It is anticipated that after the Distribution, there will be certain continuing relationships between Distributing and Controlled. Following the Distribution, Shareholders 1 and 2, as well as Individuals 1 and 2 (each of Individual 1 and 2 is an officer and member of the Distributing board of directors), will continue to serve on the board of directors of Distributing, along with Distributing's five independent directors. It is contemplated that Shareholders 1 and 2, and Individuals 1 and 2, will serve on Controlled's board of directors, along with five new independent directors who will not overlap with any of Distributing's current independent directors. In addition, other than the position of Officer, it is anticipated that there will be no overlap between the officers of either Distributing or Controlled.

Distributing and Controlled will enter into several agreements, including a tax sharing agreement, an information technology agreement, and a shared services agreement (together, the "Agreements"). Pursuant to the information technology agreement, Distributing will provide certain services to Controlled for a period of one year or less. Controlled will reimburse Distributing for the costs of the services provided. Pursuant to the shared services agreement, Distributing will provide certain administrative functions to Controlled that are not core revenue or operational functions and for which duplication of costs is not justified. The term of the shared services agreement will be indefinite, and Controlled will reimburse Distributing for the costs incurred in providing the services. Either party to the shared services agreement will be able to terminate the agreement with 60-days notice where the termination is without cause and without notice where the termination is for cause. Finally, Distributing will continue to sublease office space to Entity 1 under the same terms as the underlying third-party lease.

It is anticipated that Controlled will implement a stock-based employee compensation plan similar to Plan 1, but will not implement a plan similar to Plan 2.

### **Representations**

The following representations are made regarding the Proposed Transaction:

- 1) The indebtedness, if any, owed by Controlled to Distributing immediately after the Proposed Transaction will not constitute stock or securities.
- 2) No part of the consideration to be distributed by Distributing will be received by the Distributing shareholders as a creditor, employee, or in any other capacity other than that of a shareholder of Distributing.
- 3) In applying § 355(b)(2)(A) regarding the active conduct of a trade or business, Distributing will treat all members of its separate affiliated group (the "Distributing SAG"), as defined in § 355(b)(3)(B), as one corporation.
- 4) The five years of financial information submitted on behalf of Segment X conducted by the Distributing SAG is representative of its present operations, and with regard to such operations, there have been no substantial operational changes since the date of the last financial statements submitted.
- 5) The five years of financial information submitted on behalf of Business Y to be conducted by Controlled is representative of its present operations, and with regard to such operations, there have been no substantial operational changes since the date of the last financial statements submitted.
- 6) Except as described above with respect to certain shared services, following the Proposed Transaction, the Distributing SAG and Controlled will each continue, independently and with its separate employees, the active conduct of Segment X and Business Y, respectively, as conducted prior to the Proposed Transaction.
- 7) Neither Segment X nor control of an entity conducting this business will have been acquired during the five-year period ending on the date of the Distribution in a transaction in which gain or loss was recognized (or treated as recognized under proposed § 1.355-3) in whole or in part. Throughout the five-year period ending on the date of the Distribution, the Distributing SAG will have been the principal owner of the goodwill and significant assets of Segment X and will continue to be the principal owner following the Distribution.
- 8) Neither Business Y nor control of an entity conducting this business will have been acquired during the five-year period ending on the date of the Distribution in a transaction in which gain or loss was recognized (or treated as recognized under proposed § 1.355-3) in whole or in part. Throughout the five-year period ending on the date of the Contribution, the Distributing SAG will have been the principal owner of the goodwill and significant assets of Business Y. Following the Proposed Transaction, Controlled will be the principal owner of the goodwill and significant assets of Business Y.

- 9) The Distribution is carried out for the Business Purpose. The Distribution is motivated, in whole or substantial part, by one or more corporate business purposes.
- 10) The Proposed Transaction is not used principally as a device for the distribution of the earnings and profits of Distributing or Controlled or both.
- 11) For purposes of § 355(d), immediately after the Proposed Transaction, no person (determined after applying § 355(d)(7)) will hold stock possessing 50% or more of the total combined voting power of all classes of Distributing stock entitled to vote, or 50% or more of the total value of shares of all classes of Distributing stock, that was acquired by purchase (as defined in § 355(d)(5) and (8)) during the 5-year period (determined after applying § 355(d)(6)) ending on the date of the Proposed Transaction.
- 12) For purposes of § 355(d), immediately after the Proposed Transaction, no person (determined after applying § 355(d)(7)) will hold stock possessing 50% or more of the total combined voting power of all classes of Controlled stock entitled to vote, or 50% or more of the total value of shares of all classes of Controlled stock, that was either (i) acquired by purchase (as defined in § 355(d)(5) and (8)) during the 5-year period (determined after applying § 355(d)(6)) ending on the date of the Proposed Transaction, or (ii) attributable to distributions on Distributing stock that was acquired by purchase (as defined in § 355(d)(5) and (8)) during the 5-year period (determined after applying § 355(d)(6)) ending on the date of the Proposed Transaction.
- 13) The Proposed Transaction is not part of a plan or series of related transactions (within the meaning of § 1.355-7) pursuant to which one or more persons will acquire directly or indirectly stock representing a 50% or greater interest (within the meaning of § 355(d)(4)) in Distributing or Controlled (including any predecessor or successor of any such corporation).
- 14) The total fair market value of the assets transferred to Controlled by Distributing will exceed the sum of (i) the total liabilities assumed, if any, (within the meaning of § 357(d)) by Controlled in connection with the exchange, (ii) the amount of any liabilities owed to Controlled by Distributing that are discharged or extinguished in connection with the exchange, and (iii) the amount of cash and the fair market value of any other property (other than stock and securities permitted to be received under § 361(a) without the recognition of gain) received by Distributing in connection with the exchange. The fair market value of the assets of Controlled will exceed the amount of its liabilities immediately after the exchange.
- 15) The total adjusted basis of the assets transferred to Controlled by Distributing will exceed the total liabilities assumed, if any, (within the meaning of § 357(d)) by Controlled.

- 16) The liabilities, if any, assumed (within the meaning of § 357(d)) by Controlled were incurred in the ordinary course of business and are associated with the assets being transferred.
- 17) Except for indebtedness that may be created in the ordinary course of business or in connection with the Agreements described above, no indebtedness will exist between Distributing and Controlled at the time of, or subsequent to, the Proposed Transaction.
- 18) Immediately before the Proposed Transaction, 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 in effect before the publication of T.D. 8597, 1995-2 C.B. 147, and as currently in effect; § 1.1502-13 as published by T.D. 8597). Further, any excess loss account of a member in the stock of another member that is required to be taken into account by § 1.1502-19 will be included in income, as appropriate.
- 19) Payments made in connection with all continuing transactions between Distributing and Controlled will be as agreed to under the Agreements.
- 20) Neither Distributing nor Controlled is an investment company as defined in § 368(a)(2)(F)(iii) and (iv).
- 21) Immediately after the Proposed Transaction (taking into account § 355(g)(4)), either (i) neither Distributing nor Controlled will be a disqualified investment corporation (within the meaning of § 355(g)(2)), or (ii) no person will hold a 50% or greater interest (within the meaning of § 355(g)(3)) in the stock of Distributing or Controlled that such person did not hold immediately before the Proposed Transaction.
- 22) Distributing, Controlled, and the shareholders of Distributing will each pay their own expenses, if any, incurred in connection with the Proposed Transaction.
- 23) The payment of cash in lieu of fractional shares of Controlled stock is solely for the purpose of avoiding the expense and inconvenience to Controlled of issuing fractional shares and does not represent separately bargained-for-consideration. The fractional share interests of each Distributing shareholder will be aggregated, and no Distributing shareholder will receive cash in an amount equal to or greater than the value of one full share of Controlled stock.

### **Rulings**

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



- a) The Contribution, followed by the Distribution, will be a reorganization within the meaning of § 368(a)(1)(D). Distributing and Controlled will each be “a party to a reorganization” under § 368(b).
- b) Distributing will recognize no gain or loss on the transfer of the Business Y Assets to Controlled in exchange for Controlled stock and Controlled’s assumption of debt, if any, (§§ 357(a) and 361(a)).
- c) Controlled will recognize no gain or loss on the issuance of Controlled stock in exchange for the Business Y Assets (§ 1032(a)).
- d) Controlled’s basis in the Business Y Assets received from Distributing will equal the basis of such assets in the hands of Distributing immediately before their transfer to Controlled (§ 362(b)).
- e) Controlled’s holding period in the Business Y Assets received from Distributing will include the period during which Distributing held such assets (§ 1223(2)).
- f) Distributing will recognize no gain or loss on the distribution of the Controlled stock to its shareholders in the Distribution (§ 361(c)).
- g) The Distributing shareholders will recognize no gain or loss (and will include no amount of income) on the receipt of the Controlled stock in the Distribution (§ 355(a)(1)).
- h) A Controlled shareholder that receives cash in lieu of a fractional share of Controlled stock will recognize gain or loss measured by the difference between the amount of cash received and the basis of such fractional share (§ 1001). Provided the fractional share interest is a capital asset in the hands of the recipient shareholder, the gain or loss will constitute capital gain or loss subject to the provisions and limitations of Subchapter P of Chapter 1 of the Code (§§ 1221 and 1222).
- i) The aggregate basis of the Distributing stock and the Controlled stock in the hands of the Distributing shareholders immediately after the Proposed Transaction will be the same as the aggregate basis of the Distributing stock held by such shareholders immediately before the Proposed Transaction, allocated in proportion to the fair market value of each in accordance with § 1.358-2(a)(2) (§ 358(a), (b) and (c)).
- j) Each Distributing shareholder’s holding period in the Controlled stock received in the Proposed Transaction will include the holding period of the Distributing stock with respect to which the stock is received, provided that the shareholder holds

such Distributing stock as a capital asset on the date of the Proposed Transaction (§ 1223(1)).

- k) Distributing and Controlled will allocate their earnings and profits in accordance with § 312(h) and §§ 1.312-10(a) and 1.1502-33(e)(3).

### **Caveats**

No opinion is expressed about the tax treatment of the Proposed Transaction 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 Transaction that are not specifically covered by the above rulings. In particular, this office has not reviewed any information pertaining to and has made no determination regarding whether the Distribution: (i) satisfies the business purpose requirement of § 1.355-2(b), (ii) is used principally as a device for the distribution of the earnings and profits of Distributing or Controlled or both (see § 355(a)(1)(B) and § 1.355-2(d)), (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 Distributing or Controlled (see § 355(e) and § 1.355-7).

### **Procedural Statements**

This ruling letter is directed only 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 ruling letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of this letter ruling.

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,

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Lewis K Brickates  
Chief, Branch 4  
Office of Associate Chief Counsel  
(Corporate)