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CC:CORP:B03  
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Date:  
July 29, 2011

**LEGEND:**

Parent =

Distributing =

Controlled =

Foreign Sub 1 =

Foreign Sub 2 =

Foreign Sub 3 =

Business A =

Business B =

Date 1 =

Date 2 =

State A =

Country a =

b =

Continuing  
Arrangements =

Dear :

This letter responds to your letter dated May 13, 2011, requesting rulings under §§355 and 368 and related provisions with respect to a proposed transaction described below (the “Proposed Transaction”). The information submitted in that request and in subsequent correspondence is summarized below.

The rulings contained in this letter are based on 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 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 Distribution (defined below): (i) satisfies the business purpose requirement of Treas. Reg. §1.355-2(b); (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 Treas. Reg. §1.355-2(d)); and (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 Treas. Reg. §1.355-7).

## **FACTS**

Parent is a privately held State A corporation and the common parent of an affiliated group of corporations filing a consolidated federal income tax return with its eligible members (the “Parent Group”). Parent owns all the stock of Distributing, a State A corporation, which has a single class of common stock outstanding and is a member of the Parent Group. Distributing owns all the stock of Controlled, a State A corporation, as well as all of the stock of Foreign Sub 1, and Foreign Sub 2, both Country a corporations. Distributing is directly, and indirectly through a number of wholly owned

disregarded entities, engaged in Business A. Since Date 1, Controlled has been directly engaged in Business B. Prior to Date 1, and as described more fully below, Controlled and Distributing directly, and indirectly through a number of wholly owned disregarded entities, conducted Business B.

Both Business A and Business B are capital intensive and require large amounts of debt to fund their respective operations. Distributing's current lines of credit contain provisions (the "Distributing Debt Covenants") that constrain Distributing's business operations.

The taxpayer has submitted financial information indicating that the Business A operations conducted by Distributing have had gross receipts and operating expenses representing the active conduct of a trade or business for each of the past five years and that the Business B operations conducted by Distributing and Controlled before Date 1 and by Controlled after Date 1 have had gross receipts and operating expenses representing the active conduct of a trade or business for each of the past five years.

Parent has determined that the separation of Business B from Business A will serve a number of corporate business purposes (see representation below), and, accordingly, the following proposed transaction has been partially consummated. Steps (v) through (viii) will occur on the same day.

## **PROPOSED TRANSACTION**

- (i) On Date 1, Distributing contributed assets associated with Business B ("Business B domestic assets" that exclude Country a Business B assets that Foreign Sub 1 currently holds) to Controlled in constructive exchange for Controlled stock, liabilities assumed, and the Controlled Debt in the form of a note (the "Initial Contribution"). Comprised of previously existing liabilities associated with Business B, the Controlled Debt was created in the Initial Contribution.
- (ii) On Date 2, Foreign Sub 1 formed Foreign Sub 3, a Country a corporation, as a wholly owned subsidiary with cash necessary to meet minimum capital requirements ("Formation of Foreign Sub 3").
- (iii) Foreign Sub 1 will transfer all of its Country a Business B assets to Foreign Sub 3 and Foreign Sub 3 will assume related liabilities in constructive exchange for additional Foreign Sub 3 stock (the "Country a Exchange"). After this Step (iii), Foreign Sub 3 will have an outstanding liability owed to Foreign Sub 2 (the "Foreign Sub 3 Debt").

- (iv) All of the stock of Foreign Sub 3 will be transferred to Distributing in a transaction under Country a law. Parent has represented that the value of Foreign Sub 3 will be approximately \$b.
- (v) Distributing will transfer additional Business B assets and all of the stock of Foreign Sub 3 to Controlled in constructive exchange for additional Controlled stock (the "Secondary Contribution," and together with the Initial Contribution, the "Contributions").
- (vi) Distributing and Parent will enter into a purchase agreement (the "Purchase Agreement") pursuant to which Distributing will issue cash to Parent which Parent must then use to purchase the stock of Controlled (as outlined in Steps (vii) and (viii) below).
- (vii) Pursuant to the Purchase Agreement, Distributing will declare and issue a cash dividend (the "Dividend") to Parent in an amount equal to the value of Controlled.
- (viii) Pursuant to the Purchase Agreement, Parent will use the Step (vii) Dividend to purchase all of the stock of Controlled from Distributing (the "Purchase"). Steps (vii) and (viii) may be referred to as the "Distribution".

In connection with the Distribution, Distributing and Controlled will enter into certain agreements concerning continuing business arrangements relating to Business A and Business B (the "Continuing Arrangements"). In addition, Controlled intends to refinance the Controlled Debt and the Foreign Sub 3 Debt within two years of the Distribution. In the event Controlled has difficulty accessing debt from third parties after the Distribution (that is, in the event of an unanticipated tightening of the credit markets), it is possible Controlled might not be able to refinance the Controlled Debt or the Foreign Sub 3 Debt within two years of the Distribution and that it might be required to borrow additional funds from Parent or other members of the Parent Group, including Distributing, from time to time as needed to fund its operations.

## **REPRESENTATIONS**

- a) The Initial Contribution was made in connection with the Proposed Transaction. The purpose of the Secondary Contribution was solely to facilitate the Proposed Transaction.
- b) No part of the stock to be distributed by Distributing in the Distribution will be received by Parent as a creditor, employee, or in any capacity other than that of a shareholder of Distributing.

- c) 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”, which includes Controlled) as defined in §355(b)(3)(B), as one corporation.
- d) The five years of financial information submitted on behalf of Business A conducted by Distributing (a member of the Distributing SAG) are 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.
- e) But for limited acquisitions that the taxpayer describes as permissible expansions of Business A under Treas. Reg. § 1.355-3(b)(3)(ii), the Distributing SAG neither acquired Business A nor acquired control of an entity conducting Business A 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) in whole or in part. Through the five-year period ending on the date of the Distribution, the Distributing SAG has been the principal owner of the goodwill and significant assets of Business A and will continue to be the principal owner following the Distribution.
- f) The five years of financial information submitted on behalf of Business B conducted by Distributing and Controlled (both members of the Distributing SAG) before the Initial Contribution and by Controlled after the Initial Contribution, are 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.
- g) Controlled neither acquired Business B nor acquired control of an entity conducting Business B 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) in whole or in part. Through the five-year period ending on the date of the Distribution, the Distributing SAG, which includes Controlled, has been the principal owner of the goodwill and significant assets of Business B and Controlled will continue to be the principal owner following the Distribution.
- h) Except for the Continuing Arrangements, following the Distribution, Distributing and Controlled will continue the active conduct of their respective businesses, independently and with their separate employees.
- i) The Distribution will be carried out for the corporate business purposes of i) significantly reducing Business B’s cost of capital, ii) allowing Business B to better manage its costs and more accurately price its products, and iii) eliminating the competition for capital between Business A and Business B. The Distribution is motivated, in whole or in part, by one or more of these corporate business purposes.

- j) There is no plan or intent 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 after the Distribution, except in the ordinary course of business.
- k) The Distribution is not being used principally as a device for the distribution of the earnings and profits of Distributing, Controlled, or both.
- l) For purposes of §355(d), immediately after the Distribution, Parent (determined after applying §355(d)(7)) will not 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 five-year period (determined after applying §355(d)(6)) ending on the date of the Distribution.
- m) For purposes of §355(d), immediately after the Distribution, Parent (determined after applying §355(d)(7)) will not 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 five-year period (determined after applying §355(d)(6)) ending on the date of the Distribution or (ii) attributable to distributions on Distributing stock or securities that were acquired by purchase (as defined in §§355(d)(5) and (8)) during the five-year period (determined after applying §355(d)(6)) ending on the date of the Distribution.
- n) Except for one of the Continuing Arrangements, payments made in 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 arms' length.
- o) No two parties to the Distribution are investment companies as defined in §368(a)(2)(F)(iii) and (iv).
- p) Immediately after the Distribution (as defined in §355(g)(4)), neither Distributing nor Controlled will be a disqualified investment corporation (within the meaning of §355(g)(2)).
- q) The Distribution is not part of a plan or series of related transactions (within the meaning of Reg. § 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 either corporation).
- r) The liabilities assumed (within the meaning of §357(d)), if any, by Controlled, as well as the Controlled Debt, were incurred in the ordinary course of business and are associated with the assets being transferred.

- s) The total fair market value of the assets transferred by Distributing to Controlled in the Contributions will exceed the sum of: (i) the amount of any liabilities assumed (within the meaning of §357(d)) by Controlled in connection with the exchange, if any (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, including the Controlled Debt. The fair market value of the assets of Controlled will exceed the amount of its liabilities immediately after the exchange.
- t) No investment credit determined under §46 has been (or will be) claimed with respect to any of the property transferred, and to be transferred, from Distributing to Controlled in the Contributions.
- u) Except for the Controlled Debt, and for indebtedness that may be created in the ordinary course of business in connection with the Continuing Arrangements, no intercorporate debt will exist between Distributing and Controlled at the time of, or subsequent to, the Distribution. The indebtedness owed by Controlled to Distributing after the Distribution will not constitute stock or securities.
- v) Parent, Distributing, and Controlled will each pay their own expenses, if any, incurred in connection with the Distribution.
- w) The Purchase Agreement, Dividend, and Purchase were structured solely to avoid the Distributing Debt Covenants. The Dividend and Purchase are intended to create a circular flow of cash between Parent and Distributing and to be disregarded for Federal income tax purposes.
- x) Parent has no plan or intention to dispose of the stock of Distributing or Controlled or to engage in any transaction that would result in Distributing or Controlled ceasing to be members of the Parent Group.
- y) Parent has no plan or intention to sell or otherwise dispose of the stock of Foreign Sub 3 or any of its assets, after the Distribution.

## **RULINGS**

- (1) For Federal income tax purposes, steps (vii) and (viii) will be disregarded and Distributing will be treated as having distributed all of its Controlled stock to Parent. See Rev. Rul. 83-142, 1983-2 C.B. 68.
- (2) The Contributions followed by the Distribution will constitute a reorganization within the meaning of §368(a)(1)(D). Distributing and Controlled each will be a “party to a reorganization” within the meaning of §368(b).

- (3) The Controlled Debt will be treated as “other property” for purposes of §361(b). See Rev. Rul. 80-228, 1980-2 C.B. 115.
- (4) The Controlled Debt will be allocated to each of the assets transferred in the Contributions in proportion to each asset’s relative fair market value under the principles of Rev. Rul. 68-55, 1968-1 C.B. 140 (as amplified by Rev. Rul. 85-164, 1985-2 C.B. 117). Distributing will recognize gain, but not loss, to the extent the amount of the Controlled Debt allocated to each asset exceeds such asset’s adjusted basis at the time of the Contributions (§361).
- (5) The gain recognized by Distributing from the Contributions will be deferred under the principles of Treas. Reg. §1.1502-13.
- (6) Controlled will recognize no gain or loss upon the Contributions (§1032(a)).
- (7) Controlled's basis in each of the assets received in the Contributions will be equal to the basis of the asset in the hands of Distributing immediately prior to the Contributions increased by an amount equal to the gain, if any, recognized by Distributing on the transfer (§362(b)).
- (8) Controlled's holding period in each of the assets received will include the period during which Distributing held the assets (§1223(2)).
- (9) Distributing will recognize no gain or loss upon the Distribution (§361(c)).
- (10) Parent will recognize no gain or loss (and no amount will be includible in its income) upon the receipt of Controlled stock in the Distribution (§355(a)(1)).
- (11) The aggregate basis of the Controlled stock in the hands of Parent immediately after the Distribution will equal the aggregate basis of the Distributing stock held by Parent immediately before the Distribution, allocated between the stock of Distributing and Controlled in proportion to the fair market value of each immediately following the Distribution in accordance with Reg. §1.358-2(a).
- (12) Parent’s holding period in the Controlled common stock received in the Distribution will include the holding period of the common stock of Distributing with respect to which the Distribution is made, provided that Parent held such Distributing common stock as a capital asset on the date of the Distribution (§1223(1)).
- (13) Earnings and profits will be allocated between Distributing and Controlled in accordance with §312(h) and Reg. §1.312-10(a).



**CAVEATS**

No opinion was requested and no opinion is expressed about the Formation of Foreign Sub 3 in Step (ii), above, or the Country a Exchange in Step (iii), above, or 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.

This ruling is directed only to the taxpayer requesting 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 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 ruling letter.

In accordance with the power of attorney on file in this office, a copy of this ruling letter will be sent to your authorized representative.

Sincerely,

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Joanne M. Fay  
Assistant Branch Chief, Branch 3  
Office of Associate Chief Counsel (Corporate)

cc: