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Internal Revenue Service

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Department of the Treasury

Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:
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Date:
June 30, 1999

Distributing =

Controlled =

Sub 1 =

Sub 2 =

Sub 3 =

Foreign Sub 4 =

Foreign Sub 5 =

LLC =

Business A =

Business B =

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Business B1 =

Business B2 =

Business C =

Business D =

Date A =

Date B =

c =

Year =

This letter responds to your February 23, 1999 request for rulings on certain aspects of the proposed transactions described below.

The rulings contained in this letter are predicated upon the facts and representations submitted by the taxpayer and accompanied by a penalty of perjury executed by an appropriate party. This office has not verified any of the material submitted in support of the request for a ruling. Verification of the factual information, representations, and other data may be required as part of the audit process.

Summary of Facts

Publicly traded Distributing is the common parent of a consolidated group that engages in Business A, Business B, Business C, and Business D. Distributing directly conducts Business A and Business B (which consists of Business B1 and Business B2) but may sell part or all of Business A. Distributing wholly owns Sub 1, Sub 2, Sub 3, and Foreign Sub 4. Sub 2 wholly owns Foreign Sub 5. Sub 1 conducts Business C directly and Business D through wholly owned LLC.

We have received financial information indicating that Business D, which will be conducted by Distributing, and Business B, which will be conducted by Controlled, had gross receipts and operating expenses representing the active conduct of a trade or business for each of the past five years.

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Business C and Business D (the "Related Businesses") differ significantly from Business B in the nature of customers served, product type and development, and business regulation. Because these competing differences have forced management continually to weigh the needs of the Related Businesses against those of Business B, neither business has been able to realize its full potential. Accordingly, Distributing proposes to separate the Related Businesses from Business B and by doing so allow the management of each to fully focus on the policies and practices appropriate to its business.

Proposed Transactions

To accomplish this separation, Distributing has undertaken the following series of transactions (the "Proposed Transactions" or the "Transactions"):

(i) Effective Date B, Sub 1 transferred the assets of Business D to LLC in exchange for the lone ownership interest in LLC.

(ii) Sub 1 will transfer its interest in LLC to Distributing, either as a dividend or in exchange for other property.

(iii) Sub 2 will transfer the Foreign Sub 5 stock to Distributing.

(iv) Distributing will transfer Business B (consisting of Business B1 and Business B2, and including the stock of Sub 3, Foreign Sub 4, and Foreign Sub 5) to newly formed Controlled in exchange for all of the Controlled stock and the assumption by Controlled of related liabilities.

(v) Controlled will borrow approximately c dollars in cash from one or more unrelated lenders and immediately use this amount to pay down outstanding debt owed by Distributing to one or more unrelated creditors (step (iv) and (v) together, the "Contribution").

(vi) Distributing will distribute all of the Controlled stock to its shareholders, pro rata (the "Distribution"). Cash will be distributed in lieu of any fractional share interests.

After the Proposed Transactions, Controlled will engage directly in Business B, and Distributing will engage directly in Business D and indirectly in Business C.

Representations

Distributing makes the following representations concerning the Proposed Transactions:

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(a) Any indebtedness owed by Controlled to Distributing after the Distribution will not constitute stock or securities.

(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 Distributing.

(c) The five years of financial information submitted on behalf of Distributing's Business B and Sub 1's Business D represents, in each case, the corporation's present operation of such business, and with regard to such business, there have been no substantial operational changes since the date of the last financial statements submitted.

(d) Following the Transactions, Distributing and Controlled each will continue the active conduct of its business, independently and with its separate employees.

(e) The Distribution is being carried out to permit the management of the Related Businesses and the management of Business B each to focus on the policies and practices appropriate to its business. The Distribution is motivated, in whole or substantial part, by this and other corporate business purposes.

(f) There is no plan or intention by any shareholder who owns five 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 Transactions.

(g) 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 Transactions, other than through stock purchases meeting the requirements of § 4.05(1)(b) of Rev. Proc. 96-30, 1996-1 C.B. 696, 705.

(h) 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 Transactions, except in the ordinary course of business.

(i) The total adjusted basis and the fair market value of the assets transferred to Controlled by Distributing equals or exceeds, in each case, the sum of (i) the liabilities assumed by Controlled, (ii) any liabilities to which the transferred assets are subject, and (iii) the fair market value of any property (including money) received by Distributing from Controlled and distributed by Distributing to its shareholders or creditors in

pursuance of the plan of reorganization.

(j) The liabilities assumed in the Transactions 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.

(k) Except for short-term indebtedness incurred in the ordinary course of business and short-term indebtedness arising from the transactions described above, no intercorporate debt will exist between Distributing and Controlled at the time of, or after, the Distribution.

(l) Immediately before the Distribution, any 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 of the Income Tax Regulations and § 1.1502-14 as 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 Distributing may have in the stock of Controlled will be included in the income of Distributing immediately before the Distribution as required by the applicable regulations (see § 1.1502-19).

(m) Payments made in any 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.

(n) No two parties to the Transactions are investment companies as defined in § 368(a)(2)(F)(iii) and (iv) of the Internal Revenue Code.

(o) The payment of cash in lieu of fractional shares of Controlled will be 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 total cash consideration to be paid in lieu of fractional shares of Controlled stock will not exceed one percent of the total consideration that will be issued in the Transactions to Distributing shareholders. 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.

(p) 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 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.

(q) Both before and after the Transactions, no foreign person will own a five percent or greater interest in Distributing.

Rulings

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

(1) The Contribution, followed by the Distribution, will be a reorganization under § 368(a)(1)(D). Distributing and Controlled each will each be "a party to a reorganization" under § 368(b).

(2) No gain or loss will be recognized by Distributing on the Contribution (§§ 357(a), 361(a), and 361(b)(3)).

(3) No gain or loss will be recognized by Controlled on the Contribution (§ 1032(a)).

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

(5) The holding period of each asset received by Controlled in the Contribution will include the period during which that asset was held by Distributing (§ 1223(2)).

(6) No gain or loss will be recognized by Distributing on the Distribution (§ 361(c)(1)).

(7) No gain or loss will be recognized by (and no amount will otherwise be included in the income of) any shareholder of Distributing on receipt of Controlled stock in the Distribution (§ 355(a)(1)).

(8) The aggregate basis of the Distributing stock and the Controlled stock in the hands of each Distributing shareholder after the Distribution (including any fractional share interests to which the shareholder is entitled) will equal the aggregate basis of the Distributing stock held by such shareholder immediately before the Distribution, allocated between the Distributing and Controlled stock in proportion to the fair market value of each in accordance with § 1.358-2(a)(2) (§ 358(a)(1), (b)(2), and (c)).

(9) The holding period of the Controlled stock received by each shareholder of Distributing will include the period during which the Distributing shareholder has held the Distributing shares on which the Distribution is made, provided the Distributing stock is held as a capital asset on the date of the Distribution (§ 1223(1) and (1)((B)).

(10) As provided in § 312(h), proper allocation of earnings and profits between Distributing and Controlled will be made under § 1.312-10(a).

(11) If cash is received by a Distributing shareholder in lieu of a fractional share of Controlled stock, Distributing will be treated as distributing the fractional share to the shareholder, and the shareholder will be treated as selling the fractional share (§ 1001). The shareholder's gain or loss will be measured by the difference between the basis of the fractional share, as determined in ruling (8), above, and the amount of cash received. If the Controlled stock qualifies as a capital asset in the hands of the shareholder, the gain or loss will be a capital gain or loss subject to the provisions and limitations of Subchapter P of Chapter 1 of the Code.

(12) Provided that (i) Distributing satisfies the requirements of § 1.367(e)-1T(c)(2)(i) of the Temporary Income Tax Regulations (and the reporting requirement described in § 1.367(e)-1T(c)(2)(iii)), and (ii) Distributing does not know or have reason to know that any shareholder of Distributing who is not a qualified U.S. person (as defined in § 1.367(e)-1T(b)(1)(i)) is a five percent shareholder (as described in § 1.367(e)-1T(c)(2)(ii)), no gain will be recognized by Distributing under § 367(e)(1) with respect to the Distribution.

(13) The earnings and profits of Foreign Sub 4 to the extent attributable to such stock under § 1.1248-2 or § 1.1248-3 (whichever is applicable) which were accumulated in taxable years of such foreign corporation beginning after December 31, 1962, during the period Distributing held the Foreign Sub 4 stock (or was considered as holding it by reason of the application of § 1223) while Foreign Sub 4 was a controlled foreign corporation shall be attributable to the Foreign Sub 4 stock in the hands of Controlled (§ 1.1248-1(a)(1)).

(14) The earnings and profits of Foreign Sub 5 to the extent attributable to such stock under § 1.1248-2 or § 1.1248-3 (whichever is applicable) which were accumulated in taxable years of such foreign corporation beginning after December 31, 1962, during the period Distributing held the Foreign Sub 5 stock (or was considered as holding it by reason of the application of § 1223) while Foreign Sub 5 was a controlled foreign corporation shall be attributable to the Foreign Sub 5 stock in the hands of Controlled (§ 1.1248-1(a)(1)).

Caveats

No opinion is expressed about the tax treatment of the Transactions 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 Transactions that are not specifically covered by the above rulings. In particular, no opinion is expressed about the tax treatment of (a) the LLC formation described above in step (i), (b) the LLC transfer

described above in step (ii), or (c) the transfer of Foreign Sub 5 by Sub 2 described above in step (iii) (see § 1.1248-1(a) for rules on gain recognition from a sale or exchange of stock of certain foreign corporations).

This ruling has no effect on any earlier documents and 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 taxpayer involved in the Transactions must attach a copy of this ruling letter to the taxpayer's federal income tax return for the taxable year in which the Transactions are completed.

Under a power of attorney on file in this office, a copy of this ruling letter will be sent to the taxpayer.

Sincerely yours,

Assistant Chief Counsel (Corporate)

By: Wayne T. Murray

Wayne T. Murray
Senior Technician/Reviewer
Branch 4