199941044

Internal Revenue Service

Department of the Treasury

Index Numbers: 0351.00-00, 0355.00-00, 0355.01-00, 0367.00-00, 0368.04-00,

Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:
CC:DOM:CORP:4 PLR-105919-99
Date:
July 15, 1999

Parent =

Sub 1 =

Sub 2 =

Foreign Distributing 1 =

Distributing 2 =

Foreign Distributing 3 =

Foreign Controlled 1 =

Foreign Controlled 2 =

Foreign Controlled 3 =

3/4

Transitory Corporation =

Newco-shell =

Business X =

Business Y =

Country A =

Country B =

Country C =

a =

Date b =

Date c =

Date d =

Date e =

Date f =

Date g =

h =

i =

j =

k =

Date l =

We reply to your March 12, 1999 request for rulings on certain federal income tax consequences of a proposed transaction.

The rulings contained in this letter are predicated upon the 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 a ruling. Verification of the information, representations, and other data may be required as part of the audit process.

Summary of Facts

Publicly traded Parent is the parent of an affiliated group that comprises both domestic and foreign corporations and conducts, among others, Business X and Business Y. Parent joins with its includible affiliates in filing a consolidated federal income tax return.

Before the transactions described below, Parent wholly owned Sub 1, Sub 2, Foreign Distributing 1, Distributing 2, and Foreign Distributing 3. Foreign Distributing 1 wholly owned Foreign Controlled 1, and Distributing 2 wholly owned Foreign Controlled 2.

Foreign Distributing 1, Distributing 2, and Foreign Distributing 3 each conducts Business X . Foreign Controlled 1, Foreign Controlled 2, and Foreign Distributing 3 each conducts Business Y.

We have received financial information indicating that Business X, as conducted by Foreign Distributing 1, Distributing 2, and Foreign Distributing 3, and Business Y, as conducted by Foreign Controlled 1, Foreign Controlled 2, and Foreign Distributing 3, each has had gross receipts and operating expenses representing the active conduct of a trade or business for each of the past five years.

Approximately a percent of the Business Y current production is used by Parent in Business X. Business Y is attempting to increase its sales to unrelated parties, but potential customers are reluctant to purchase Business Y products while it and Business X are both owned by Parent. To overcome this problem, Parent proposes to associate all of the Business Y assets with Sub 1 and distribute the stock of Sub 1 to certain of its stockholders (the "Proposed Distribution"). On Date b, the Internal Revenue Service issued to Parent a private letter ruling concluding that the Proposed Distribution would qualify for nonrecognition treatment under § 355 of the Internal Revenue Code. The transactions described in the present letter are designed to move

foreign Business Y assets to Sub 1 before the Proposed Distribution occurs.

The Country A Transaction

(i) On Date c, Sub 2 acquired Newco-shell, and Newco-shell elected under § 301.7701-3 of the Income Tax Regulations to be disregarded as an entity separate from Sub 2 for U.S. federal tax purposes.

(ii) On Date d, Foreign Distributing 1 transferred its Foreign Controlled 1 stock to Newco-shell for no consideration in a Country A demerger.

(iii) On Date e, Parent transferred its Sub 2 stock to Sub 1 in exchange for Sub 1 stock in a transaction intended to qualify under §351(a).

Country A Transaction Representations

The taxpayer has made the following representations concerning this transaction (based on the characterization of steps (i) through (iii) above by ruling (1) below):

(a) No part of the consideration distributed by Foreign Distributing 1 was received by Parent as a creditor, employee, or in any capacity other than that of a shareholder of Distributing 1.

(b) The five years of financial information submitted on behalf of Foreign Distributing 1 and Foreign Controlled 1 represents the present operation of each corporation, and with regard to each corporation, there have been no substantial operational changes since the date of the last financial statements submitted.

(c) Following the transaction, Foreign Distributing 1 and Foreign Controlled 1 each will continue the active conduct of its business, independently and with its separate employees.

(d) Distribution A (defined below at ruling (1)(a)) was carried out to increase the amount of Business Y that Sub 1 conducts with unrelated parties. Distribution A was motivated, in whole or substantial part, by this corporate business purpose.

(e) There is no plan or intention by Parent to sell, exchange, transfer by gift, or otherwise dispose of any of its stock in Foreign Distributing 1 or Foreign Controlled 1 after Distribution A except as part of the overall transaction, and Sub 2 has no plan or intention to sell, exchange, transfer by gift, or otherwise dispose of any stock in, or securities of Foreign Controlled 1 after step (ii) above.

(f) There is no plan or intention by either Foreign Distributing 1 or Foreign

Controlled 1, 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.

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

(h) No intercorporate debt existed between Foreign Distributing 1 and Foreign Controlled 1 at the time of, or after, Distribution A other than trade payables arising in the ordinary course of business.

(i) Except during a transition period expected to last one year or less, payments made in all continuing transactions between Foreign Distributing 1 and Foreign Controlled 1 will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.

(j) Neither Foreign Distributing 1 nor Foreign Controlled 1 is an investment company as defined in § 368(a)(2)(F)(iii) and (iv).k) The Country A Transaction 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 Foreign Distributing 1 or Foreign Controlled 1 entitled to vote, or stock possessing 50 percent or more of the total value of all classes of stock of either Foreign Distributing 1 or Foreign Controlled 1.

(k) Parent will treat the deemed transfer of Foreign Controlled 1 stock to Sub 2 as qualifying under § 351(a).

(l) Parent will treat its transfer of Sub 2 stock to Sub 1 as qualifying under § 351(a).

Country A Transaction Rulings

Based solely on the information submitted and the representations set forth above, and provided that the requirements of paragraph (c) and (d) of § 7.367(b)-1 of the Temporary Income Tax Regulations and all the conditions and requirements of § 7.367(b)-4 through § 7.367(b)-12 are satisfied, we rule as follows on the Country A Transaction:

(1) For federal income tax purposes, the transactions described above in steps (i) through (iii) are treated as if (a) Foreign Distributing 1 had distributed all the stock of

Foreign Controlled 1 to Parent ("Distribution A"), (b) Parent had transferred the stock of Foreign Controlled 1 to Sub 2 in exchange for stock of Sub 2, and (c) Parent had transferred the stock of Sub 2 to Sub 1 in exchange for stock of Sub 1 (see Rev. Rul. 77-191, 1977-1 C.B. 94).

(2) No gain or loss was recognized by (and no amount was otherwise included in the income of) Parent on the receipt of Foreign Controlled 1 stock (§ 355(a)(1)).

(3) No gain or loss was recognized by Foreign Distributing 1 on Distribution A (§ 355(c)).

(4) The holding period of Foreign Controlled 1 stock received by Parent includes the holding period of the Foreign Distributing 1 stock on which Distribution A was made, provided the Foreign Distributing 1 stock was held as a capital asset on the date of Distribution A (§ 1223(1) and (1)(B)).

(5) Distribution A is an exchange to which § 7.367(b)-10(c) applies, and the requirements of paragraphs (d) through (h) of § 7.367(b)-10 must be satisfied.

(6) If Parent recognizes no gain under § 1248 by virtue of the contribution of the stock of Foreign Controlled 1 to the capital of Sub 2, the earnings and profits of Foreign Controlled 1, to the extent attributable to such stock under § 1.1248-2 or 1.1248-3 (whichever is applicable), which were accumulated in taxable years beginning after December 31, 1962 and during the period in which Foreign Controlled 1 was a controlled foreign corporation, shall be attributable to such stock now held by Sub 2 through Newco-shell (see § 1248-1(a)(1)).

The Country B Transaction

(iv) On Date e:

(a) Distributing 2 distributed the Foreign Controlled 2 stock to Parent ("Distribution B").

(b) Parent transferred the Foreign Controlled 2 stock to Sub 2 in a transaction intended to qualify under § 351(a).

(c) Parent transferred the Sub 2 stock to Sub 1 in a transaction intended to qualify under § 351(a).

Country B Transaction Representations

The taxpayer has made the following representations concerning Distribution B:

(m) No part of the consideration distributed by Distributing 2 was received by Parent as a creditor, employee, or in any capacity other than that of a shareholder of Distributing 2.

(n) The five years of financial information submitted on behalf of Distributing 2 and Foreign Controlled 2 represents the present operations of each corporation, and with regard to each corporation, there have been no substantial operational changes since the date of the last financial statements submitted.

(o) Following the transaction, Distributing 2 and Foreign Controlled 2 each will continue the active conduct of its business, independently and with its separate employees.

(p) Distribution B was carried out to increase the amount of Business Y that Sub 1 conducts with unrelated parties. Distribution B was motivated, in whole or substantial part, by this corporate business purpose.

(q) There is no plan or intention by Parent to sell, exchange, transfer by gift, or otherwise dispose of any of its stock in Distributing 2 or Foreign Controlled 2 after Distribution B except as part of the overall transaction, and Sub 2 has no plan or intention to sell, exchange, transfer by gift, or otherwise dispose of any stock in, or securities of Foreign Controlled 2 after step (iv)(b) above.

(r) There is no plan or intention by either Distributing 2 or Foreign Controlled 2, 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.

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

(t) No intercorporate debt existed between Distributing 2 and Foreign Controlled 2 at the time of, or after, Distribution B.

(u) Except during a transition period expected to last one year or less, payments made in all continuing transactions between Distributing 2 and Foreign Controlled 2

will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.

(v) Neither Distributing 2 nor Foreign Controlled 2 is an investment company as defined in § 368(a)(2)(F)(iii) and (iv).

(w) The Country B Transaction 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 2 or Foreign Controlled 2 entitled to vote, or stock possessing 50 percent or more of the total value of all classes of stock of either Distributing 2 or Foreign Controlled 2.

(x) Parent will treat its transfer of Foreign Controlled 2 stock to Sub 2 as qualifying under § 351(a).

Country B Transaction Rulings

Based solely on the information submitted and the representations set forth above, and provided that the requirements of paragraph (c) and (d) of § 7.367(b)-1 and all the conditions and requirements of § 7.367(b)-4 through 7.367(b)-12 are satisfied, we rule as follows on Distribution B:

(7) No gain or loss was recognized by (and no amount was included in the income of) Parent on Distribution B (§ 355(a)(1)).

(8) No gain or loss was recognized by Distributing 2 on Distribution B (§ 355 (c)).

(9) The basis of Foreign Controlled 2 stock in the hands of Parent will be the lesser of the adjusted basis of that stock in the hands of Distributing 2 or the substituted basis allocated to Foreign Controlled 2's stock in accordance with § 1.358-2(a)(2) (§ 1248(f)(2); Notice 87-64, 1987-2 C.B. 375).

(10) The holding period of Foreign Controlled 2 stock received by Parent will be the greater of the holding period of the Foreign Controlled 2 stock in the hands of Distributing 2 or the holding period of Distributing 2 stock in the hands of Parent (§ 1248(f)(2); Notice 87-64).

(11) Section 1248(f)(1) will not apply to Distribution B (§ 1248(f)(2); Notice 87-64).

(12) If Parent recognizes no gain under section 1248 by virtue of the

contribution of the stock of Foreign Controlled 2 to the capital of Sub 2, the earnings and profits of Foreign Controlled 2, to the extent attributable to such stock under § 1.1248-2 or 1.1248-3 (whichever is applicable), which were accumulated in taxable years beginning after December 31, 1962 and during the period in which Foreign Controlled 2 was a controlled foreign corporation, shall be attributable to such stock now held by Sub 2 (see § 1248-1(a)(1)).

The Country C Transaction

(v) On Date f, Sub 2 formed a transitory Country C corporation ("Transitory Corporation").

(vi) On Date g:

(a) Foreign Distributing 3 transferred its Business Y assets to newly formed Foreign Controlled 3 in exchange for the Foreign Controlled 3 stock and the assumption by Foreign Controlled 3 of related liabilities.

(b) Parent contributed h dollars in cash to Sub 1, Sub 1 contributed the cash to Sub 2, and Sub 2 contributed the cash to Transitory Corporation.

(c) Transitory Corporation transferred an j dollar note (the "Transitory Note") and j dollars in cash to Foreign Controlled 3 in exchange for newly issued Foreign Controlled 3 stock.

(d) Transitory Corporation purchased the remaining Foreign Controlled 3 stock from Foreign Distributing 3 for k dollars fair market value in cash.

(e) Foreign Distributing 3 distributed to Parent the k dollars in cash received in step (vi)(d) above.

(vii) On Date l, Transitory Corporation was merged downstream into Foreign Controlled 3, and the Transitory Note was canceled.

Country C Transaction Representations

The taxpayer has made the following representations concerning the transaction (based on the characterization of steps (v) through (vii) above by ruling (13) below):

(y) No part of the consideration distributed by Foreign Distributing 3 was received by Parent as a creditor, employee, or in any capacity other than that of a shareholder of Foreign Distributing 3.

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(z) The five years of financial information submitted on behalf of Foreign Distributing 3 for Business X and Business Y represents the present operations of each business, and with regard to each, there have been no substantial operational changes since the date of the last financial statements submitted.

(aa) Following the transaction, Foreign Distributing 3 and Foreign Controlled 3 each will continue the active conduct of its business, independently and with its separate employees.

(bb) The Country C Transaction was carried out to increase the amount of Business Y that Sub 1 conducts with unrelated parties. The Country C Transaction was motivated, in whole or substantial part, by this corporate business purpose.

(cc) There is no plan or intention by Parent to sell, exchange, transfer by gift, or otherwise dispose of any of its stock in Foreign Distributing 3 or Foreign Controlled 3 after Distribution C except as part of the overall transaction, and Sub 2 has no plan or intention to sell, exchange, transfer by gift, or otherwise dispose of any stock in, or securities of Foreign Controlled 3 after the Country C Transaction.

(dd) There is no plan or intention by either Foreign Distributing 3 or Foreign Controlled 3, 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.

(ee) There is no plan or intention to liquidate either Foreign Distributing 3 or Foreign Controlled 3, to merge either corporation with any other corporation, or to sell or otherwise dispose of the assets of either corporation after the transaction, except in the ordinary course of business.

(ff) The total adjusted basis and the fair market value of the assets transferred to Foreign Controlled 3 by Foreign Distributing 3 each equals or exceeds the sum of the liabilities assumed by Foreign Controlled 3 plus the liabilities to which the transferred assets are subject.

(gg) The liabilities assumed in the transaction 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.

(hh) No intercorporate debt existed between Foreign Distributing 3 and Foreign Controlled 3 at the time of, or after, the distribution of the Foreign Controlled 3 stock.

(ii) Except during a transition period expected to last one year or less, payments made in all continuing transactions between Foreign Distributing 3 and Foreign

Controlled 3 will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.

(jj) Neither Foreign Distributing 3 nor Foreign Controlled 3 is an investment company as defined in § 368(a)(2)(F)(iii) and (iv).

(kk) The Country C Transaction 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 Foreign Distributing 3 or Foreign Controlled 3, or stock possessing 50 percent or more of the total value of all classes of stock of either Foreign Distributing 3 or Foreign Controlled 3

(ll) Parent will treat the deemed transfer of Foreign Controlled 3 stock to Sub 1 as qualifying under § 351(a).

Country C Transaction Rulings

Based solely on the information submitted and the representations set forth above, and provided that the requirements of paragraphs (c) and (d) of § 7.367(b)-1 and all the conditions and requirements of § 7.367(b)-4 through 7.367(b)-12 are satisfied, we rule as follows on the Country C Transaction:

(13) For federal income tax purposes, the transactions described above in steps (v) through (vii) are treated as if (a) Foreign Distributing 3 had transferred its Business Y assets to newly formed Foreign Controlled 3 in exchange for Foreign Controlled 3 stock and the assumption by Foreign Controlled 3 of related liabilities ("Contribution C"), (b) Foreign Distributing 3 had distributed the stock of Foreign Controlled 3 to Parent ("Distribution C"), (c) Parent had transferred the stock of Foreign Controlled 3 and j dollars in cash to Sub 1 in exchange for stock of Sub 1, (d) Sub 1 had transferred the stock of Foreign Controlled 3 and j dollars in cash to Sub 2 in exchange for stock of Sub 2, and (e) Sub 2 had contributed j dollars in cash to Foreign Controlled 3 (see Rev. Rul. 77-191).

(14) Contribution C, followed by Distribution C, is a reorganization under §368(a)(1)(D). Foreign Distributing 3 and Foreign Controlled 3 each was "a party to a reorganization" under § 368(b).

(15) No gain or loss was recognized by Foreign Distributing 3 on Contribution C (§§ 361(a) and 357(a)).

(16) No gain or loss was recognized by Foreign Controlled 3 on Contribution C (§ 1032(a)).

(17) The basis of each Business Y asset received by Foreign Controlled 3 equals the basis of that asset in the hands of Foreign Distributing 3 immediately before Contribution C (§ 362(b)).

(18) The holding period of each Business Y asset received by Foreign Controlled 3 includes the period during which that asset was held by Foreign Distributing 3 (§ 1223(2)).

(19) No gain or loss was recognized by (and no amount was otherwise included in the income of) Parent on its receipt of the Foreign Controlled 3 stock in Distribution C (§ 355(a)(1)).

(20) No gain or loss was recognized by Foreign Distributing 3 on Distribution C (§ 361(c)).

(21) The holding period of the Foreign Controlled 3 stock received by Parent includes the holding period of the Foreign Distributing 3 stock on which Distribution C was made, provided the Foreign Distributing 3 stock was held as a capital asset on the date of Distribution C (§ 1223(1) and (1)(B)).

(22) Distribution C is an exchange to which section 7.367(b)-10(c) applies, and the requirements of paragraphs (d) through (h) of section 7.367(b)-10 must be satisfied.

(23) If Parent recognizes no gain under § 1248 by virtue of the contribution of the stock of Foreign Controlled 3 to the capital of Sub 1, the earnings and profits of Foreign Controlled 3, to the extent attributable to such stock under § 1.1248-2 or 1.1248-3 (whichever is applicable), which were accumulated in taxable years beginning after December 31, 1962 and during the period in which Foreign Controlled 3 was a controlled foreign corporation, shall be attributable to such stock now held by Sub 1 (see § 1248-1(a)(1)).

(24) If Sub 1 recognizes no gain under § 1248 by virtue of the contribution of the stock of Foreign Controlled 3 to the capital of Sub 2, the earnings and profits of Foreign Controlled 3, to the extent attributable to such stock under § 1.1248-2 or 1.1248-3 (whichever is applicable), which were accumulated in taxable years beginning after December 31, 1962 and during the period in which Foreign Controlled 3 was a controlled foreign corporation, shall be attributable to such stock now held by Sub 2 (see § 1248-1(a)(1)).

Caveats

We express no opinion on the tax effects of the transactions under any other provisions of the Code or regulations, or the tax effects of any condition existing at the

time of, or effect resulting from, the transactions that is not specifically covered in the above rulings. In particular, we express no opinion regarding:

(a) The election by Newco-shell under § 301.7701-3 as described above in step (i);

(b) Apart from the rulings given above, the U.S. tax consequences of Foreign Distributing 1's transfer of the stock of Foreign Controlled 1 to Newco-shell;

(c) Whether the transfer by Parent of Sub 2 stock to Sub 1 described above in ruling (1)(c) and step (iii) and (iv)(c) qualified under § 351(a);

(d) Whether the transfer by Parent of Foreign Controlled 1 stock to Sub 2 described above in ruling (1)(b) qualified under § 351(a);

(e) Whether the transfer by Parent of Foreign Controlled 2 stock to Sub 2 described above in step (iv)(b) qualified under § 351(a);

(f) Whether the transfer by Parent of Foreign Controlled 3 stock and cash to Sub 1 described above in ruling (13)(c) qualified under § 351(a);

(g) Whether the transfer by Sub 1 of Foreign Controlled 3 stock and cash to Sub 2 described above in ruling (13)(d) qualified under § 351(a);

(h) Whether the transfer by Sub 2 of cash to Foreign Controlled 3 described above in ruling (13)(e) qualified under § 351(a); and

(i) The tax treatment of payments made between parties during the transition periods referred to in representations (i), (t), and (gg).

Temporary or final regulations pertaining to one or more issues addressed in this ruling letter (including regulations under § 358(g)) have yet to be adopted. Therefore, this ruling letter may be revoked or modified if adopted temporary or final regulations are inconsistent with any conclusions reached herein. See section 12.04 of Rev. Proc. 99-1, 1999-1 I.R.B. 6, 47, which addresses in greater detail when a ruling will be revoked or modified. However, when the criteria in section 12.05 of Rev. Proc. 99-1 are satisfied, a ruling is seldom revoked or modified retroactively, except in rare or unusual circumstances.

Procedural Statements

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

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Each taxpayer involved in these transactions should 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.

In accordance with the power of attorney on file in this office, a copy of this letter is being sent to the taxpayer and a second authorized representative.

Sincerely yours,

Assistant Chief Counsel (Corporate)

By: Wayne T. Murray
Wayne T. Murray
Senior Technician/Reviewer
Branch 4