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**Internal Revenue Service**

Department of the Treasury

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Washington, DC 20224

Person to Contact:

CC:DOM:CORP:4 PLR-114216-99
Date:
September 27, 1999

FCorp 1 =

FCorp 2 =

FCorp 3 =

USCorp 4 =

FCorp 5 =

USCorp 6 =

USCorp 7 =

USCorp 8 =

USPship 1 =

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USPship 2 =

FNewco 1 =

USNewco 2 =

Business A =

Business B =

Business C =

Business D =

Property =

Name =

Country E =

Country F =

Dear :

This letter responds to your April 27, 1999 request for rulings on certain federal income tax consequences of a proposed transaction. The information in that request and in later correspondence is summarized below. The rulings contained in this letter are based on facts and representations submitted by the taxpayers under penalties of perjury. The Internal Revenue Service may require verification of this information as part of the audit process.

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## Summary of Facts

FCorp 1 wholly owns FCorp 2 indirectly. Both are Country E corporations. FCorp 2 wholly owns FCorp 3, a Country E corporation, and FCorp 3 wholly owns USCorp 4 indirectly. FCorp 5, a Country F corporation unrelated to the FCorp 1 group, wholly owns USCorp 6. USCorp 6 wholly owns USCorp 7. USCorp 8 is owned equally by FCorp 5 and USPship 1. USPship 2 is owned 49.5 percent each by USPship 1 and USCorp 7 and one percent by USCorp 8, the general partner.

FCorp 3 conducts Business A and Business B, and USCorp 4 conducts Business C.

USPship 2 is primarily engaged in Business D (similar to Business B) and has entered into a number of management agreements (the "Management Agreements") that entitle USPship 2 to a percentage of the gross revenue as a base fee and to incentives keyed to revenues in excess of certain specified base amounts. Most of the Management Agreements give USPship 2 a right to acquire the underlying Property, and some of the Management Agreements include a termination fee payable to USPship 2 in the event the owner of the subject Property terminates the Management Agreement or sells the underlying Property.

## Proposed Transaction

To permit FCorp 3 to combine its Business B with Business D of USPship 2, the parties propose the following transaction:

(i) FCorp 3 will, through a series of steps some of which are transitory, contribute its Business B assets to FNewco 1, a newly formed Country E corporation, for FNewco 1 stock ("Contribution 1A") and transfer the FNewco 1 stock to FCorp 2 in a transaction intended to be tax-free under the laws of Country E (altogether, the "Country E Distribution").

(ii) FCorp 5 will transfer its 50 percent interest in USCorp 8 to USCorp 6, and USCorp 6 will contribute the 50 percent interest to USCorp 7.

(iii) USCorp 7 will contribute its 50 percent interest in USCorp 8 and 49.5 percent interest in USPship 2 to FNewco 1 in exchange for FNewco 1 class K stock ("Contribution 1B").

(iv) USPship 1 will contribute its 50 percent interest in USCorp 8 and 49.5 percent interest in USPship 2 to FNewco 1 in exchange for FNewco 1 class H stock ("Contribution 1C" and, together with Contribution 1A and Contribution 1B, "Contribution

1").

(v) FNewco 1 will contribute the USCorp 8 stock and the 99 percent interest in USPship 2 to newly formed USNewco 2 in exchange for USNewco 2 common stock ("Contribution 2A").

(vi) USCorp 4 will contribute its Business C assets to USNewco 2 in exchange for USNewco 2 nonvoting preferred stock and the assumption by USNewco 2 of related liabilities ("Contribution 2B" and, together with Contribution 2A, "Contribution 2").

**Representations**

The following representations are made by FCorp 2 and FCorp 3 for Contribution 1A, by USCorp 7 for Contribution 1B, by USPship 1 for Contribution 1C, by FNewco 1 for Contribution 2A, and by USCorp 4 for Contribution 2B (collectively, the "Contributions," and each, a "Contribution"). Hereinafter, the transferee of a Contribution is a "Transferee," and the transferor of a Contribution is a "Transferor."

(a) No stock or securities will be issued for services rendered to or for the benefit of any Transferee in connection with the Contributions, and no stock or securities will be issued for indebtedness of any Transferee that is not evidenced by a security or for interest on indebtedness of any Transferee that accrued on or after the beginning of the holding period of the Transferor(s) for the debt.

(b) Any patents or patent applications will qualify as "property" within the meaning of § 351 of the Internal Revenue Code. Each Transferor will transfer all substantial rights in such patents or patent applications within the meaning of § 1235.

(c) No Transferor will retain any significant power, right, or continuing interest, within the meaning of § 1253(b), in the franchises, trademarks, or trade names being transferred.

(d) None of the stock to be transferred in any Contribution is "section 306 stock" within the meaning of § 306(c).

(e) No Contribution is the result of the solicitation by a promoter, broker, or investment house.

(f) No Transferor will retain any rights in the property transferred to a Transferee.

(g) The adjusted basis and the fair market value of the assets transferred in Contribution 1 and Contribution 2 will, in each instance, equal or exceed the amount of

any liabilities assumed (as determined under § 357(d)) by the Transferee.

(h) Any liabilities of a Transferor that will be assumed (as determined under § 357(d)) by its Transferee were incurred in the ordinary course of business and are associated with the assets to be transferred.

(i) There is no indebtedness between any Transferee and its Transferor, and there will be no indebtedness created in favor of any Transferor as a result of any Contribution.

(j) The transfers and exchanges in Contribution 1 and Contribution 2 will occur, in each case, under a plan agreed upon before the transaction in which the rights of the parties are defined.

(k) All the transfers contemplated by Contribution 1 and Contribution 2 will occur, in each case, on approximately the same date.

(l) There is no plan or intention on the part of any Transferee to redeem or otherwise reacquire any stock or indebtedness issued in any Contribution.

(m) Taking into account any issuance of additional shares of Transferee stock; any issuance of stock for services; the exercise of any Transferee stock rights, warrants, or subscriptions; a public offering of Transferee stock; and the sale, exchange, transfer by gift, or other disposition of any Transferee stock received in the Contribution, the Transferors will be in "control" of the Transferee under § 368(c).

(n) Each Transferor will receive stock approximately equal to the fair market value of the property transferred by it to the Transferee.

(o) Other than as described above, each Transferee will remain in existence and retain and use the property transferred to it in a trade or business.

(p) There is no plan or intention by any Transferee to dispose of the transferred property other than by (i) Contribution 2 and (ii) dispositions in the normal course of business operations.

(q) Each of the parties to Contribution 1 or Contribution 2 will pay its own expenses, if any, incurred in connection with the Contribution.

(r) No Transferee will be an investment company under § 351(e)(1) and § 1.351(c)(1)(ii) of the Income Tax Regulations.

(s) No Transferor is under the jurisdiction of a court in a title 11 or similar case (under § 368(a)(3)(A)), and no stock or securities received in any Contribution will be used to satisfy the indebtedness of such debtor.

(t) No Transferee will be a "personal service corporation" under § 269A.

(u) The value of the stock received in exchange for accounts receivable will be equal to the net value of the accounts transferred (i.e., the face amount of the accounts receivable previously included in income less the reserve for bad debts).

(v) FNewco 1, a foreign corporation within the meaning of §§ 7701(a)(3) and 7701(a)(5), will not be a controlled foreign corporation within the meaning of § 957(a) ("CFC") at any time from the date of its formation through the date of Contribution 2A. FNewco 1 is not, nor will become as a result of the transaction, a passive foreign investment company as defined in § 1297 ("PFIC").

(w) Business B is an active trade or business that has been conducted outside the U.S. by FCorp 3 for more than 36 months before the proposed transfers within the meaning of § 1.367(a)-3(c)(3). At the time of the proposed transfers, there will be no intention on the part of USCorp 7, USPship 1, or FNewco 1 to dispose of or discontinue Business B.

(x) At the time of the proposed transfers, taking into account the rules of § 1.367(a)-3(c), the fair market value of Business B owned by FNewco 1 will be greater than the fair market value of USNewco 2 .

(y) USNewco 2 will satisfy the reporting requirements of § 1.367(a)-3(c)(6).

(z) Based upon ruling (18) that the Management Agreements will be U.S. real property interests ("USRPIs") within the meaning of § 897(c), each of USNewco 2 and USCorp 8 will be a U.S. real property holding corporation ("USRPHC") within the meaning of § 897(c)(2), and the stock of each of USNewco 2 and USCorp 8 will be a USRPI within the meaning of § 897(c)(1)(A)(ii).

(aa) Based upon ruling (18), the transfer of the partnership interests in USPship 2 by FNewco 1 will be treated as a transfer by FNewco 1 of the USRPI's held by USPship 2 pursuant to § 897(g).

(bb) None of the Country E entities affected by the Country E Distribution, including but not limited to FCorp 1, FCorp 2, and FCorp 3, will be a USRPHC within the meaning of § 897(c)(2) at any time during the five-year period ending on the completion of the Country E Distribution, and will not be a USRPHC immediately

thereafter.

(cc) None of the Country E entities affected by the Country E Distribution, including but not limited to FCorp 1, FCorp 2, and FCorp 3, will be a CFC within the meaning of § 957(a) at any time during the five-year period ending on the completion of the Country E Distribution and will not be a CFC immediately thereafter. None of the Country E entities affected by the Country E Distribution, including but not limited to FCorp 1, FCorp 2, and FCorp 3, will be a PFIC within the meaning of § 1297(a) at any time during the five-year period ending on the completion of the Country E Distribution, and will not be a PFIC immediately thereafter.

(dd) Fifty percent or less of both the total voting power and the total value of the stock of FNewco 1 will be received, directly or indirectly, in the aggregate, by USCorp 7 and USPship 1 in connection with their Contributions to FNewco 1 within the meaning of § 1.367(a)-3(c)(1)(i).

(ee) Fifty percent or less of both the total voting power and the total value of the stock of FNewco 1 will be owned, directly or indirectly, in the aggregate, by U.S. persons that are either officers or directors of USNewco 2 or that are five-percent target shareholders, within the meaning of § 1.367(a)-3(c)(1)(ii).

(ff) Each of USCorp 7 and USPship 1 will be a five-percent transferee shareholder within the meaning of § 1.367(a)-3(c)(1)(iii)(B). Each of USCorp 7 and USPship 1 will enter into a five-year gain recognition agreement in the form provided in § 1.367(a)-8 with respect to the USNewco 2 stock such shareholders are deemed to have exchanged, respectively, for FNewco 1 stock in connection with the indirect stock transfer rule under §§ 1.367(a)-3(d)(1)(vi) and 1.367(a)-3(d)(2)(vi).

(gg) In connection with one or more steps of the transactions described in the ruling request, there will be no transfer or other disposition of tangible or intangible property, directly or indirectly, by USPship 2 or USCorp 8 to FNewco 1.

(hh) Any royalty payments on licenses of USPship 2's or USCorp 8's intangible assets to FNewco 1 will be based on fair market value consideration and on terms and conditions that are consistent with standards for § 482.

(ii) Immediately before and after the date of Contribiution 1C, all of the partners of USPship 1 will be United States persons within the meaning of § 7701(a)(30).

(jj) FNewco 1 will meet the filing requirements of § 1.897-5T(d)(1)(iii).

(kk) USCorp 6 is a USRPHC both prior to and after its respective receipt of the

USCorp 8 stock as a capital contribution from FCorp 5. USCorp 6 will comply with the filing requirements of § 1.897-5T(d)(1)(iii).

**Rulings**

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

Contribution 1 Rulings

(1) Contribution 1A, Contribution 1B, and Contribution 1C each will be a transfer of property under § 351(a).

(2) No gain or loss will be recognized by FCorp 2, USCorp 7, or USPship 1 in Contribution 1 (§§ 351(a) and (c) and 357(a)).

(3) No gain or loss will be recognized by FNewco 1 in Contribution 1 (§ 1032).

(4) The basis of each asset received by FNewco 1 in Contribution 1 will equal the basis of that asset in the hands of FCorp 2, USCorp 7, or USPship 1 immediately before Contribution 1 (§ 362(a)).

(5) The holding period of each asset received by FNewco 1 in Contribution 1 will include the period during which FCorp 2, USCorp 7, or USPship 1 held that asset (§ 1223(2)).

(6) The basis of the FNewco 1 stock received by FCorp 2, USCorp 7, and USPship 1 in Contribution 1 will in each case equal the basis of the assets transferred in exchange therefor (§ 358(a)(1)).

(7) The holding period of the FNewco 1 stock received by FCorp 2, USCorp 7 and USPship 1 will in each case include the period during which FCorp 2, USCorp 7, or USPship 1 held the transferred assets (§ 1223(1)).

Contribution 2 Rulings

(8) No gain or loss will be recognized by FNewco 1 or USCorp 4 in Contribution 2 (§§ 351(a) and 357(a)).

(9) No gain or loss will be recognized by USNewco 2 in Contribution 2 (§ 1032).

(10) The basis of each asset received by USNewco 2 in Contribution 2

will equal the basis of that asset in the hands of FNewco 1 or USCorp 4 immediately before Contribution 2 (§ 362(a)).

(11) The holding period of each asset received by USNewco 2 in Contribution 2 will include the holding period of that asset in the hands of FNewco 1 or USCorp 4 (§ 1223(2)).

(12) The basis of the USNewco 2 stock received by FNewco 1 and USCorp 4 in Contribution 2 will in each case equal the basis of the assets transferred in exchange therefor (§ 358(a)(1)).

(13) The holding period of the USNewco 2 stock received by FNewco 1 and USCorp 4 will in each case include the period during which FNewco 1 or USCorp 4 held the transferred assets (§ 1223(1)).

Section 367 Rulings

(14) For purposes of § 367(a), the transfer of the interests in USPship 2 and the USCorp 8 stock by USCorp 7 in exchange for FNewco1 stock followed by FNewco 1's transfer of such assets to USNewco 2 will be treated as a transfer by USCorp 7 of its limited partnership interests in USPship 2 and the USCorp 8 stock to USNewco 2 in exchange for USNewco 2 stock, and a subsequent transfer by USCorp 7 of its deemed ownership of USNewco 2 stock to FNewco 1 in exchange for FNewco 1 stock in an exchange described in § 354 (§ 1.367(a)-3(d)(2)(vi)). Upon the filing by USCorp 7 of a five-year gain recognition agreement pursuant to § 1.367(a)-8, no gain or loss will be recognized by USCorp 7 under § 367(a) on the transfer of the USNewco 2 stock (§ 1.367(a)-3(b)(1)(ii), (c)(1)).

(15) For purposes of § 367(a), the transfer of the interests in USPship 2 and the USCorp 8 stock by USPship 1 in exchange for FNewco1 stock followed by FNewco 1's transfer of such assets to USNewco 2 will be treated as a transfer by USPship 1 of its limited partnership interests in USPship 2 and the USCorp 8 stock to USNewco 2 in exchange for USNewco 2 stock, and a subsequent transfer by USPship 1 of its deemed ownership of USNewco 2 stock to FNewco 1 in exchange for FNewco 1 stock in an exchange described in § 354 (§ 1.367(a)-3(d)(2)(vi)). Upon the filing by USPship 1 of a five-year gain recognition agreement pursuant to § 1.367(a)-8, no gain or loss will be recognized by USPship 1 under § 367(a) on the transfer of the USNewco 2 stock (§ 1.367(a)-3(b)(1)(ii), (c)(1)).

(16) For purposes of § 367(d), the transfer of intangible assets by USCorp 7 to FNewco 1 will be treated as a transfer by USCorp 7 of intangible assets to USNewco 2 in exchange for USNewco 2 stock, and a subsequent transfer by USCorp 7 of its

deemed ownership of USNewco 2 stock to FNewco 1 in exchange for FNewco 1 stock (§§ 1.367(d)-1T(a) and 1.367(a)-3(d)(3) Ex. 8.). The application of the foregoing would not trigger the anti-abuse rule under § 1.367(d)-1(g)(6) in this instance. Thus, § 367(d) does not apply to the transfer of the intangibles.

(17) For purposes of § 367(d), the transfer of intangible assets by USPship 1 to FNewco 1 will be treated as a transfer by USPship 1 of intangible assets to USNewco 2 in exchange for USNewco 2 stock, and a subsequent transfer by USPship 1 of its deemed ownership of USNewco 2 stock to FNewco 1 in exchange for FNewco 1 stock (§§ 1.367(d)-1T(a) and 1.367(a)-3(d)(3) Ex. 8.). The application of the foregoing would not trigger the anti-abuse rule under § 1.367(d)-1(g)(6) in this instance. Thus, § 367(d) does not apply to the transfer of the intangibles.

Section 897 Analysis and Ruling

Section 897(a) taxes the disposition of interests in real property by foreign taxpayers as effectively connected income under §§ 871 and 882. Under § 897(c)(1), U.S. real property interests include certain interests in real property in the United States. Section 1.897-1(d)(2)(i) generally provides that an interest in real property other than solely as a creditor includes any direct or indirect right to share in the appreciation in the value, or in the gross or net proceeds or profits generated by, the real property. Further, § 1.897-1(d)(2)(ii)(B) generally provides that an option, a contract, or a right of first refusal to acquire any interest in real property (other than solely as a creditor) will itself constitute an interest in real property other than solely as a creditor. Finally, § 1.897-1(d)(2)(ii)(E) generally provides that a right to payment of a commission, brokerage fee, or similar charge will constitute an interest other than solely as a creditor if the total amount of the payment is contingent upon appreciation, proceeds, or profits of the real property occurring or arising after the date of the transaction with respect to which the professional services giving rise to the payment were rendered.

(18) The Management Agreements owned by USPship 2 are U.S. real property interests (see §§ 897(c)(1)(A) and 1.897-2(d)(2)). Provided that FNewco 1 satisfies the filing requirements of § 1.897-5T(d)(1)(iii) as modified by Notice 89-57, 1989-1 C.B. 698, no gain or loss shall be recognized under § 897(e) upon FNewco 1's transfer of the USPship 2 partnership interest and the USCorp 8 stock to USNewco 2 (see §§ 897(a) and 1.897-6T(a)(1)).

**Caveats**

We express no opinion on the tax effects of the transaction under other provisions of the Code and regulations, or the tax effects of any condition 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 regarding (i) qualification of the Country E Distribution under § 355, (ii) whether the Name is considered to be property in Country E and, consequently, whether there will be a transfer of property in connection with the use of the Name by FNewco 1 to which § 367 or 482 is applicable absent the payment of consideration by FNewco to USPship 2, (iii) the application of § 897 (e) and (g) on any § 708 termination resulting from the transfer of the partnership interests in USPship 2 by FNewco 1 to USNewco 2, or (iv) the application of § 897(e) and § 1.897-6T(a)(1) to the transfer of the USCorp 8 stock by FCorp 5 to USCorp 6. Also, see § 1445 and the regulations thereunder for the withholding responsibilities of USCorp 6 and USNewco 2.

**Procedural Matters**

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

A copy of this letter should be attached to the federal income tax return of each affected taxpayer for the year in which the transactions covered by this letter are completed.

Under a power of attorney on file in this office, a copy of this letter is being sent to your authorized representative.

Sincerely,
Assistant Chief Counsel
(Corporate)

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