

Internal Revenue Service

Department of the Treasury
Washington, DC 20224

Number: **200446011**

Release Date: 11/12/04

Index Number: 337.14-00, 368.01-00,
512.00-00, 1502.13-00

Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:CORP:B06 – PLR-120309-04

Date:

July 19, 2004

In Re:

LEGEND

Subdivision =

Member =

Target =

Acquiring =

X =

Entity =

State A =

Date 1 =

Date 2 =

Date 3 =

PLR-120309-04

Date 4 =

Date 5 =

Date 6 =

Business A =

Business B =

c =

d =

e =

\$f =

Dear

This letter responds to your March 31, 2004 request for rulings regarding certain Federal income tax consequences of a proposed transaction. The information submitted for consideration is summarized below.

SUMMARY OF FACTS

Subdivision is a political subdivision of State A. Through Entity, Subdivision operates Business A.

Member is a State A non-stock, non-member corporation exempt from tax under section 501(c)(3) of the Internal Revenue Code. Its exempt purpose is to support Subdivision. Subdivision appoints a majority of the members of the Board of Directors of Member, and other members of Member's Board are officers of Subdivision. Pursuant to Member's Articles of Incorporation, upon dissolution of Member and the winding up of its affairs, the assets of Member are to be distributed exclusively to Subdivision, so long as Subdivision remains a political subdivision of State A when such distributions are to be made.

PLR-120309-04

Target, a State A non-stock, single-member corporation that was incorporated on Date 1, is a holding company that was formed for the purpose of acquiring and holding the stock and debt obligations of Acquiring. Target is the common parent of an affiliated group (the “Target Group”) that files a consolidated federal income tax return using the accrual method of accounting for book and income tax purposes and having an annual accounting period that starts on Date 2 and ends on Date 3. Acquiring is the only other member of the Target Group. Target’s only assets are the Acquiring Common Stock, the Acquiring Preferred Stock, and the Notes (defined below).

Target’s sole member is Member. Member has the exclusive right to vote on the election, appointment or removal of the members of Target’s Board of Directors. In addition, Member may receive distributions from Target and is entitled to all of the assets of Target upon its dissolution.

Acquiring, a State A corporation engaged in Business B, is a wholly-owned subsidiary of Target and is included on the Target Group’s consolidated return. Acquiring was originally incorporated in State A on Date 4 as X, changing its name to Acquiring effective Date 5.

Acquiring has one class of common stock outstanding (“Acquiring Common Stock”) and one class of preferred stock outstanding (“Acquiring Preferred Stock”). Acquiring has outstanding c shares of Acquiring Common Stock and d shares of Acquiring Preferred Stock, all of which is owned by Target. Additionally, there are e demand promissory notes (collectively, the “Notes”) on which Acquiring is debtor and Target is creditor. As of Date 6, the aggregate amount of indebtedness represented by the Notes was approximately \$f.

PROPOSED TRANSACTION

For what have been represented to be valid business reasons, the following steps are proposed (collectively, the “Proposed Transaction”):

- (i) Pursuant to an Agreement and Plan of Merger in accordance with State A law (“Plan of Merger”), Target will merge with and into Acquiring with Acquiring surviving (the “Merger”). State A law and the Plan of Merger will provide that the following steps occur simultaneously as part of the Merger: (a) Member will exchange its membership interest in Target solely in return for newly issued Acquiring common stock, (b) all of the assets and liabilities of Target will become the assets and liabilities of Acquiring, and (c) Target will cease its separate legal existence for all purposes. As part of the Merger, Acquiring will cancel the Acquiring Common Stock, Acquiring Preferred Stock and the Notes formerly held by Target.

PLR-120309-04

- (ii) Shortly after the Merger, Acquiring will amend and restate its articles of incorporation to convert Acquiring to a not-for-profit stock corporation and qualify as a tax-exempt entity under section 501(c)(3) (the "Conversion").
- (iii) Immediately following the Conversion, Member will transfer all of the outstanding Acquiring stock to Subdivision.

As a result of the Proposed Transaction, Subdivision will own 100% of the outstanding stock of Acquiring. Acquiring will continue to conduct its Business B subsequent to the Proposed Transaction.

REPRESENTATIONS

The following representations have been made in connection with the Proposed Transaction:

- (a) The fair market value of the Acquiring stock received by Member will be approximately equal to the fair market value of the Target membership interest surrendered in the exchange.
- (b) At least 50% of the proprietary interest in Target will be exchanged for Acquiring stock and will be preserved within the meaning of Treas. Reg. section 1.368-1(e).
- (c) Acquiring has no plan or intention to reacquire any of its stock issued in the Proposed Transaction.
- (d) Acquiring has no plan or intention to sell or otherwise dispose of any of the assets of Target acquired in the Proposed Transaction, except for dispositions made in the ordinary course of business. However, the Conversion will cause a deemed disposition of Acquiring's assets pursuant to Treas. Reg. section 1.337(d)-4(a).
- (e) The liabilities of Target assumed by Acquiring and the liabilities to which the transferred assets of Target are subject were incurred by Target in the ordinary course of business.
- (f) Following the Merger, Acquiring will continue its historic business. Target's historic business, which consists of Acquiring Common Stock, Acquiring Preferred Stock, and the Notes, will necessarily be cancelled in the Merger.

PLR-120309-04

- (g) Acquiring, Target, and Member will pay their respective expenses, if any, incurred in connection with the Proposed Transaction, except that Acquiring will assume (by operation of law) and pay Target's expenses not paid before the Merger occurs.
- (h) There is no intercorporate indebtedness existing between Target and Acquiring that was issued or acquired or will be settled at a discount.
- (i) No two parties to the Proposed Transaction are investment companies as defined in section 368(a)(2)(F)(iii) and (iv).
- (j) Target is not under the jurisdiction of a court in a title 11 or similar case within the meaning of section 368(a)(3)(A).
- (k) The fair market value of the assets of Target transferred to Acquiring will equal or exceed the sum of the liabilities assumed by Acquiring plus the amount of liabilities, if any, to which the transferred assets are subject.
- (l) The total adjusted basis of the assets of Target transferred to Acquiring will equal or exceed the sum of Target's liabilities assumed by Acquiring, plus the amount of liabilities, if any, to which the transferred assets are subject.
- (m) Member's membership interest in Target is not "debt-financed property" within the meaning of section 514.

RULINGS

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

- (1) Provided the Merger qualifies as a statutory merger under State A law, the Merger will constitute a reorganization within the meaning of section 368(a)(1)(A). Acquiring and Target will each be a "party to the reorganization" within the meaning of section 368(b).
- (2) Target will recognize no gain or loss upon the transfer of its assets to Acquiring solely in exchange for shares of Acquiring stock and the assumption of liabilities by Acquiring. Sections 361(a) and 357(a).
- (3) Target will recognize no gain or loss on the distribution of the Acquiring stock to Member. Section 361(c)(1).

PLR-120309-04

- (4) No gain or loss will be recognized by Member upon its receipt of Acquiring stock solely in exchange for Member's membership in Target. Section 354(a).
- (5) The basis of the Acquiring stock received by Member will be the same as the basis of the Target membership interest surrendered in exchange therefor. Section 358(a)(1).
- (6) The holding period of the Acquiring stock received by Member will include the period during which the Target membership interest surrendered in exchange therefor was held, provided that the Target membership interest was held as a capital asset by Member on the date of the exchange. Section 1223(1).
- (7) No gain or loss will be recognized by Acquiring upon Acquiring's receipt of Target's assets in exchange for shares of Acquiring stock and the assumption of Target's liabilities. Section 1032(a).
- (8) No net amount of income, gain, or loss will be recognized by Target and Acquiring in the aggregate upon the extinguishment of Acquiring's indebtedness to Target. Treas. Reg. Section 1.1502-13(g).
- (9) Member, a section 501(c)(3) organization, will not incur unrelated business taxable income as a result of the transfer of Acquiring stock to Subdivision. Section 512(b)(5).
- (10) Acquiring will succeed to and take into account the items of Target described in section 381(c). These items will be taken into account by Acquiring subject to the applicable conditions and limitations specified in sections 381, 382, 383, and 384 and the Treasury Regulations thereunder. Section 381(a) and Treas. Reg. Section 1.381(a)-1.
- (11) Upon Acquiring's change from a taxable to a tax-exempt entity, Acquiring will be treated as if, immediately before the change in status becomes effective, it sold all of its assets for fair market value to a tax-exempt entity in a transaction in which Acquiring recognizes any gain or loss. Such assets will not include any of the Acquiring stock or Acquiring indebtedness held by Target before the Merger, because such stock and indebtedness will cease to exist when acquired by Acquiring. Treas. Reg. Section 1.337(d)-4(a)(1) and (2).

CAVEAT

No opinion is expressed about the tax treatment of the proposed transaction under other provisions of the Code and regulations or about the tax treatment of any

PLR-120309-04

conditions existing at the time of, or effects resulting from, the proposed transaction that are not specifically covered by the above rulings.

PROCEDURAL STATEMENTS

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Internal Revenue Code provides that it may not be used or cited as precedent.

A copy of this letter must be attached to the federal income tax return of each taxpayer involved in the taxable year in which the transaction is consummated.

We have sent copies of this letter to the taxpayer, as designated on the power of attorney on file in this office.

Sincerely yours,

Reginald Mombrun
Assistant to the Branch Chief, Branch 6
Office of Associate Chief Counsel
(Corporate)