Internal Revenue Service

Department of the Treasury

Washington, DC 20224

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Person to Contact:

Telephone Number:

Refer Reply To:
CC:CORP:4 - PLR-121811-02
Date:
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Legend

Controlled =

Acquiror =

New Parent =

Company 3 =

Sub 39 =

Distributing Subsidiary Preferred Stock =

Controlled Common Stock =

Controlled Class A Common Stock =

Date I =

Date J =

Date K =

Date L =

Date M =

h =

i =

j =

Dear :

This letter responds to your April 12, 2002 request that we supplement our letter ruling dated June 27, 2001 (PLR-127793-01) (the “Prior Letter Ruling”). The information submitted in that request and in later correspondence is summarized below. Capitalized terms not defined in this ruling have the meanings originally assigned them in the Prior Letter Ruling.

The Prior Letter Ruling addresses certain federal income tax consequences of a distribution of stock of a controlled corporation and related transactions.

Supplemental Facts

Distributing currently has two classes of stock outstanding: Distributing Common Stock and Distributing Subsidiary Preferred Stock. Distributing subsidiaries own all of the Distributing Subsidiary Preferred Stock outstanding. None of the other classes of Distributing stock described in the Prior Letter Ruling are currently outstanding. At the time of the Splint-Off (as defined below), Distributing will have two additional classes of stock outstanding: Distributing Exchangeable Preferred Stock (as defined below) and New Distributing Subsidiary Preferred Stock (as defined below).

On Date K, Company 3 acquired an interest in Sub 39, a company indirectly and beneficially owned by Distributing. In connection with that transaction, Distributing agreed to purchase all of the remaining shares of Company 3 from its shareholders upon the occurrence of a specified condition. On Date L, Distributing issued h shares of Distributing Common Stock for cash to satisfy a portion of its obligations to the Company 3 shareholders (the “New Issuances”).

On Date M, Distributing acquired all of the Target 2 stock in exchange for approximately i percent of the Distributing Common Stock outstanding immediately after the acquisition (the "Target 2 Acquisition").

On Date I, Acquiror made an unsolicited offer to combine with Business C. On Date J, Distributing and Acquiror agreed to combine Controlled, a newly formed subsidiary of Distributing that will own the assets and liabilities of Business C, with Acquiror. Specifically, Controlled and Acquiror will conduct their respective businesses under a recently formed, holding corporation ("New Parent"), which will own all of the stock of Controlled and Acquiror.

The separation of Business C from Business A and Business B is motivated by compelling business reasons. First, the coexistence of Business A, Business B, and Business C as separate divisions within the Distributing affiliated group is responsible for substantial management, systemic, and other problems that will be alleviated by the separation of Distributing and Controlled. Second, the separation will facilitate the combination of Controlled and Acquiror.

Proposed Transaction

To accomplish the combination of Controlled and Acquiror, certain of the transactions described in the Prior Letter Ruling will not be completed as originally contemplated. Specifically, the public offering of Distributing Business C Common Stock will not be consummated and the pro rata distribution to holders of Distributing Common Stock of Distributing Business B Common Stock may occur within one year of shareholder approval or thereafter, depending on market conditions. In addition, the separation of Business A and Business B from Business C will not be completed in the manner described in the Prior Letter Ruling. Instead, the following steps have been or are intended to be undertaken (the "Proposed Transaction"):

(i) Distributing completed the Distributing Restructuring.

(ii) Distributing will contribute all of the assets that constitute Business C to newly formed Controlled in exchange for Controlled's assumption of liabilities related to the transferred assets and in exchange for Controlled Common Stock, Controlled Class A Common Stock, and cash (steps (ii) and (iv), collectively, the "Contribution").

(iii) Controlled may borrow from an unrelated party and use the proceeds to repay existing intercompany debt owed by Controlled or one of Controlled's subsidiaries to Distributing or one of Distributing's subsidiaries. Any intercompany debt so repaid was incurred before Date J. Any intercompany debt not repaid will be contributed to the capital of Controlled or one of Controlled's subsidiaries.

(iv) In connection with the transaction, a certain amount of existing

Distributing debt will be allocated to Controlled and Controlled will assume or otherwise incur an equal amount of debt (the "Controlled Debt"). The Controlled Debt will be allocated to Controlled through a combination of the mechanisms described below and in step (iii) above. First, before step (ii), Controlled will be added as a co-obligor to certain series of existing Distributing debt instruments. Mechanically, this will be accomplished through an exchange offer pursuant to which holders of certain series of existing Distributing debt instruments can exchange such debt instruments for Distributing debt instruments of a like principal amount and with substantially identical terms, except that Controlled would be added as a co-obligor (the Distributing debt instruments relinquished or received pursuant to the exchange offer, collectively, the "Existing Distributing Debt"). In connection with the Splint-Off, the Existing Distributing Debt will be exchanged for debt instruments of Controlled (the "New Debt Instruments" and the "Debt Exchange"). Second, Controlled will incur new debt and, pursuant to the plan of reorganization, transfer the proceeds of such borrowing to Distributing, which, in turn, will apply the proceeds to repay existing debt (the "Cash Boot Transaction").

(v) Controlled will be recapitalized such that sufficient shares of Controlled Common Stock and Controlled Class A Common Stock will be available to effect the Splint-Off.

(vi) Distributing will issue shares of two new classes of exchangeable preferred stock: (1) Distributing Exchangeable Preferred Stock will be issued to Acquiror in exchange for shares of Distributing Common Stock held by Acquiror, and (2) New Distributing Subsidiary Preferred Stock will be issued in exchange for shares of Distributing Subsidiary Preferred Stock held by Distributing subsidiaries that will not be transferred to Controlled in connection with the Splint-Off. Shares of Distributing Exchangeable Preferred Stock and New Distributing Subsidiary Preferred Stock will not participate in the Splint-Off or the Mergers (as defined below).

(vii) Distributing will distribute pro rata to the holders of Distributing Common Stock its entire interest in the Controlled Common Stock (the "Spin-Off"), except for shares of Controlled Common Stock transferred to the holder of Distributing Special Debt Securities in the event the Distributing Special Debt Securities Exchange described in step (viii) below is consummated.

(viii) In the Distributing Special Debt Securities Exchange, the holder of Distributing Special Debt Securities will exchange such securities for shares of Controlled Common Stock. If the Distributing Special Debt Securities Exchange cannot be accomplished, Distributing and Acquiror will seek to transfer the obligations under the Distributing Special Debt Securities from Distributing to Controlled (the "Distributing Special Debt Securities Transfer") on the Splint-Off date. The Distributing Special Debt Securities Transfer would be structured as follows: (a) Controlled would issue new debt instruments (the "Controlled Special Debt Securities") to Distributing, with terms substantially similar to the Distributing Special Debt Securities, as part of the exchange

described in step (ii) above, and (b) Distributing would transfer the Controlled Special Debt Securities to the holder of Distributing Special Debt Securities in exchange for such securities. If neither the Distributing Special Debt Securities Exchange nor the Distributing Special Debt Securities Transfer occurs, Controlled will borrow an amount of cash equal to the fair market value of the Distributing Special Debt Securities and will transfer the borrowing proceeds to Distributing which, in turn, will transfer such cash to its creditors as described in step (iv) above.

(ix) Distributing will redeem the Distributing Subsidiary Preferred Stock in exchange for Controlled Class A Common Stock (the "Split-Off" and together with the Spin-Off, the "Splint-Off").

(x) Following the Splint-Off, in a transaction intended to qualify as a tax-free exchange under § 351: (i) a newly formed subsidiary of New Parent will merge into Controlled (the "Controlled Merger") and (ii) a newly formed subsidiary of New Parent will merge into Acquiror (the "Acquiror Merger" and both mergers, collectively, the "Mergers"). In the Controlled Merger, Controlled shareholders will receive New Parent stock representing more than 50 percent of the vote and value of the New Parent stock outstanding immediately after the Mergers.

(xi) Following the Splint-Off and the Mergers, (i) Distributing may effect a reverse stock split (the "Distributing Stock Split") and (ii) New Parent may, subject to shareholder approval, effect a reverse/forward stock split (the "New Parent Stock Split"). Provided Distributing elects to effect the Distributing Stock Split, it may offer holders of Distributing Common Stock who would own less than a specified number of Distributing Common Stock the opportunity to participate in a voluntary sale program (the "Odd-Lot Sale Program") pursuant to which eligible holders could sell their shares of Distributing Common Stock for cash in the open market. In no event will the shares sold pursuant to the Odd-Lot Sale Program exceed j percent of the Distributing Common Stock outstanding.

Representations

Distributing affirms the representations in the Prior Letter Ruling, except that (i) representation (t) is no longer relevant, (ii) representations (x) and (y) are new, and (iii) the following representations (lettered as shown in the Prior Letter Ruling) are revised to read in their entirety as follows:

(a) The fair market value of the Controlled Class A Common Stock received by each holder of Distributing Subsidiary Preferred Stock in the Split-Off will approximately equal the fair market value of the Distributing Subsidiary Preferred Stock surrendered in exchange therefor.

(c) No part of the consideration distributed by Distributing in connection with

the Debt Exchange, the Distributing Special Debt Securities Exchange, or the Distributing Special Debt Securities Transfer will be received by a security holder as an employee or in any capacity other than that of a Distributing security holder. The Distributing Special Debt Securities qualify as securities of Distributing for federal income tax purposes. In the event the Distributing Special Debt Securities Transfer is consummated, the Controlled Special Debt Securities will qualify as securities of Controlled for federal income tax purposes.

(d) The five years of financial information submitted on behalf of Distributing (regarding Business A and Business B) and Controlled (regarding Business C as conducted by Distributing before the Contribution) represents the present operations of each business, and with regard to each business, there have been no substantial operational changes since the date of the last financial statements submitted.

(e) Following the Splint-Off, the gross assets of Business A and Business B directly conducted by Distributing will have a fair market value equal to at least five percent of the total fair market value of the gross assets of Distributing.

(f) Following the Splint-Off, the Directly Conducted Business C Systems (i) will have a fair market value that is equal to at least five percent of the total fair market value of the gross assets of Controlled, or (ii) will represent at least (a) 5.1 percent of the aggregate revenues of Controlled and its subsidiaries, (b) 5.5 percent of the total customers of Controlled and its subsidiaries, and (c) 5.1 percent of the total employees of Controlled and its subsidiaries, or (iii) will satisfy both (i) and (ii). Consequently, immediately after the Splint-Off, the Directly Conducted Business C Systems will not be *de minimis* compared with the other assets or activities of Controlled and its subsidiaries.

(g) Following the Splint-Off, Distributing and Controlled each will continue, independently and with its separate employees, the active conduct of Business A and Business B, and Business C, respectively. New Parent does not intend to cause Controlled to modify its activities after the Mergers in a manner that would cause Controlled to cease to be engaged in the active conduct of a trade or business.

(h) The Splint-Off is being carried out for the following corporate business purposes: (i) to alleviate management, systemic, and other problems that arise from (or are exacerbated by) the coexistence of Business A, Business B, and Business C as separate divisions within the Distributing affiliated group, and (ii) to facilitate the acquisition of Controlled by New Parent. The Splint-Off is motivated, in whole or substantial part, by these corporate business purposes.

(i) No shareholder owns more than five percent (by vote or value) of Distributing, and the Distributing management, to its best knowledge, is not aware of any plan or intention on the part of any shareholder or security holder of Distributing to

sell, exchange, transfer by gift, or otherwise dispose of any stock in, or securities of, New Parent, Distributing or Controlled after the Splint-Off, other than: (i) exchanges of Controlled Common Stock for New Parent common stock, (ii) any dispositions by Acquiror of Distributing Common Stock required pursuant to the merger agreement among New Parent, Distributing, Controlled and Acquiror (the "Merger Agreement"), (iii) in ordinary market trading, (iv) pursuant to the Distributing Stock Split and the Odd-Lot Sale Program, or (v) pursuant to the New Parent Stock Split.

(k) Except as contemplated by the Merger Agreement, 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 Splint-Off (with the exception of dispositions by Distributing or Controlled of certain assets with a value not greater than 30 percent of the value of all of such corporation's assets, any consideration from which will be used by the disposing corporation to pay down its debt, to fund the capital requirements of its business activities, or for other corporate business purposes), except in the ordinary course of business.

(l) Any cash, New Debt Instruments or Controlled Special Debt Securities received by Distributing from Controlled as a result of the Contribution will be transferred by Distributing to its creditors pursuant to the plan of reorganization.

(r) Payments made in connection with 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 arm's length.

(x)(1) At the time of the Target 2 Acquisition or within six months thereafter, there was no "agreement, understanding, arrangement or substantial negotiations" concerning the Splint-Off.

(2) The proceeds of the public offering of Distributing Common Stock on Date L are intended to satisfy a portion of Distributing's pre-existing obligation to the public shareholders of Company 3, which pre-existing obligation results from agreements that were entered into more than two years before the Splint-Off and at such time, or within six months thereof, there was no "agreement, understanding, or substantial negotiations" concerning the Splint-Off." The Splint-Off is not motivated by a business purpose to facilitate the New Issuances, and the Splint-Off will occur at approximately the same time and in similar form regardless of the New Issuances.

(3) The holder of the Distributing Special Debt Securities acquired such securities from Distributing more than two years before the expected date of the Splint-Off in a transaction which is not part of a plan (or series of related transactions) that includes the Splint-Off.

(y) The Mergers will qualify as a tax-free exchange by the shareholders of Controlled and Acquiror under § 351.

Rulings

Based on the information and representations submitted with the original and supplemental requests, we reaffirm the rulings and caveats set forth in the Prior Letter Ruling, except that the following rulings are revised to read in their entirety as follows:

(7) No gain or loss will be recognized by (and no amount will otherwise be included in the income of) the holders of Distributing Common Stock or Distributing Subsidiary Preferred Stock on the Splint-Off (§ 355(a)(1)).

(9) A shareholder who receives Controlled Class A Common Stock in the Split-Off will have an aggregate adjusted basis in the Controlled Class A Common Stock immediately after the Split-Off equal to the aggregate adjusted basis of the shareholder's Distributing Subsidiary Preferred Stock surrendered in the Split-Off (§ 358(a)(1)).

(11) The holding period of Controlled Class A Common Stock received by a shareholder in the Split-Off will include the holding period of the Distributing Subsidiary Preferred Stock surrendered in exchange therefor, provided the Distributing Subsidiary Preferred Stock is held as a capital asset on the date of the Split-Off (§ 1223(1)).

(14) No gain or loss will be recognized by (and no amount will otherwise be included in the income of) a holder of Distributing Special Debt Securities on the exchange of the Distributing Special Debt Securities (i) for Controlled Common Stock in the Distributing Special Debt Securities Exchange, or (ii) for Controlled Special Debt Securities in the Distributing Special Debt Securities Transfer, provided that the Distributing Special Debt Securities surrendered in the Distributing Special Debt Securities Transfer have an aggregate principal amount equal to the aggregate principal amount of the Controlled Special Debt Securities received (§ 355(a)(1)).

(15) No gain or loss will be recognized by Distributing on the Debt Exchange, the Distributing Special Debt Securities Transfer, or the Cash Boot Transaction (§§ 361(a), 361(b)(3) and 361(c)(3)).

(16) The acquisition of shares of (i) Distributing Common Stock in connection with (a) the Target 2 Acquisition and (b) the New Issuances, and (ii) Controlled Common Stock pursuant to the Distributing Special Debt Securities Exchange, are not acquisitions that are part of a plan or series of related transactions (within the meaning of § 355(e)) which includes the Splint-Off. The Controlled Common Stock and Controlled Class A Common Stock will be “qualified property” for purposes of §§ 355(c) and 361(c)(2).

Caveats

We express no opinion about 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. In particular, no opinion is expressed on

(i) the Mergers described in step (x); and

(ii) the stock exchanges described in step (vi).

Procedural Statements

This supplemental letter 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 this transaction should attach a copy of this letter, along with a copy of the Prior Letter Ruling, to the taxpayer's federal income tax return for the taxable year in which the Proposed Transaction is completed.

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

Sincerely,

Richard K. Passales
Senior Counsel, Branch 4
Office of Associate Chief Counsel
(Corporate)