**Internal Revenue Service**

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Department of the Treasury
Washington, DC 20224

Third Party Communication: None
Date of Communication: Not Applicable

Person To Contact:
, ID No.
Telephone Number:

Refer Reply To:
CC:CORP:B02
PLR-106035-05
Date:
May 20, 2005

Legend

| | |
|---|---|
| A | = |
| Distributing | = |
| DE or Controlled | = |
| K | = |
| $G | = |
| Business W | = |
| State X | = |
| State Y | = |
| State Z | = |
| Date1 | = |
| Date2 | = |
| Date3 | = |
| Date 4 | = |
| Date 5 | = |

Dear :

This letter responds to your January 26, 2005, request for rulings on certain federal income tax consequences of a proposed transaction. The information provided in that request and in later correspondence is summarized below.

The rulings contained in this letter are based upon facts and representations submitted by the taxpayer and accompanied by penalties of perjury statements executed by an appropriate party. This office has not verified any of the material submitted in support of

the request for rulings. Verification of the information, representations, and other data may be required as part of the audit process.

In particular, this office has not reviewed any information pertaining to, and has made no determination regarding, whether the transaction described below satisfies the business purpose requirement of §1.355-2(b) of the Income Tax Regulations, whether the distribution described below is used principally as a device for the distribution of earnings and profits of Distributing or Controlled or both (see § 355(a)(1)(B) of the I.R.C. and § 1.355-2(d)), or whether any distribution described below is part of a plan (or series of related transactions) pursuant to which one or more persons will acquire directly or indirectly stock representing a 50-percent or greater interest in Distributing or Controlled (see § 355(e) and §1.355-7). Moreover, no opinion is expressed on the application of § 1031 to the transaction described below or to the validity of any subchapter S election.

Distributing is a State X S corporation that uses the accrual method of accounting. A owns all of Distributing's single class of voting common stock, which is the only stock of Distributing that is issued and outstanding. DE, which was formed on Date 4, is a State Z limited liability company that is disregarded as separate from its owner for federal income tax purposes under §301.7701-3. Distributing owns all of the membership interests of DE.

Distributing has been engaged in each of two businesses, Business W and Business R, for more than five years. The financial information submitted by Distributing indicates that Business W and Business R each has had gross receipts and operating expenses representing the active conduct of a trade or business for each of the past 5 years. Since Date 4, Distributing has operated Business R through DE. Within the last five years, Distributing sold property used in Business R, and through DE, acquired similar property that continued to be used in Business R, in a transaction intended to qualify as a nontaxable like-kind exchange under § 1031.

It has been represented that Distributing's key employee, K, is actively engaged in the management of Business W. Distributing wishes to allow K to acquire a significant voting interest in an entity engaged solely in Business W. In order to achieve that goal, the following transaction has been proposed to separate Business R from Distributing:

(i) A Form 8832, "Entity Classification Election" will be filed to treat DE (hereinafter referred to as "Controlled") as an association taxable as a corporation for federal income tax purposes under §301.7701-3. As a result of this election, Distributing will be deemed to contribute all of the assets and liabilities of Business R to Controlled in exchange for 100 percent of Controlled's equity interests (the "Controlled stock") (the "Contribution").

(ii) Distributing will distribute all of the Controlled stock to A (the "Distribution" or "Spin-off").

(iii) K will acquire a significant amount of Distributing's common stock within one year of the issuance of this letter.

The parties have made the following representations concerning the proposed transaction.

(a) Distributing, Controlled, A, and K each will pay its, or his own expenses, if any, incurred in the transaction.

(b) No part of the consideration to be distributed by Distributing will be received by A as a creditor, employee, or in any capacity other than that of a shareholder of Distributing.

(c) Following the transaction, Distributing and Controlled will each continue the active conduct of its business, independently and with its separate employees, except that Distributing and Controlled will share the services of A. Distributing and Controlled will each pay A directly for the value of his services.

(d) The Spin-off is being carried out for the following business purpose: to facilitate the acquisition by K of a significant stock interest in Distributing. The distribution of the Controlled stock in the Spin-off is motivated, in whole or substantial part, by this business purpose.

(e) The Spin-off is not being used principally as a device for the distribution of the earnings and profits of Distributing or Controlled or both.

(f) The total adjusted basis and the fair market value of the assets transferred to Controlled by Distributing (1) each equal or exceed the sum of any liabilities assumed (as determined under § 357(d)) by Controlled, and (2) any liabilities assumed (as determined under § 357(d)) in the transaction were incurred in the ordinary course of business and are associated with the assets being transferred.

(g) No intercorporate debt will exist between Distributing and Controlled at the time of, or after, the Distribution.

(h) No two parties to the transaction are investment companies as defined in § 368(a)(2)(F)(iii) and (iv).

(i) The five years of financial information submitted on behalf of Business W and Business R represents the present operation of each, and there have been no substantial material operational changes since the date of the last financial statements submitted.

(j) There is no plan or intention to liquidate 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 transaction, except in the ordinary course of business.

(k) Within a period not to exceed one year from the date of issuance of a favorable letter ruling, K shall acquire by purchase from Distributing and/or by gift from A, as described below, no less than twenty-five percent (25%) of all shares of Distributing stock issued and outstanding as of the date of issuance of the ruling; provided, however that K shall in no event be permitted to acquire more than forty-nine percent (49%) of all shares of Distributing stock then issued and outstanding.

(l) A may, but shall not be required to, make gifts of stock in Distributing to K. In the event that A shall make gifts of stock to K, the aggregate value of such gifts shall not exceed $G as determined by a qualified independent appraisal; such gifts shall be included in the calculation set forth above in (k).

(m) Payments made in 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.

(n) There is no acquisition of stock of Distributing or Controlled (including any predecessor or successor of any such corporation) that is part of a plan or series of related transactions (within the meaning of Reg. §1.355-7T) that includes the distribution of the stock of Controlled**.**

(o) The Distribution will not be a disqualified distribution (as defined in § 355(d)(2)) because immediately after the Distribution: (i) no person (determined after applying § 355(d)(7)) will hold disqualified stock (defined in § 355(d)(3)) in Distributing that will constitute a 50 percent or greater interest (defined in § 355(d)(4)) in Distributing, and (ii) no person (determined after applying § 355(d)(7)) will hold disqualified stock (defined in § 355(d)(3)) in Controlled that will constitute a 50 percent or greater interest (defined in § 355(d)(4)) in Controlled.

Based solely on the information submitted and the representations set forth above, we rule as follows with respect to the proposed Contribution and Distribution:

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

(2) No gain or loss will be recognized by Distributing upon the Contribution. Sections 357(a) and 361(a).

(3) No gain or loss will be recognized by Controlled upon the Contribution in exchange for Controlled stock. Section 1032(a).

(4) The basis of each asset received by Controlled will equal the basis of such asset in the hands of Distributing immediately prior to the Contribution. Section 362(b).

(5) Controlled's holding period for each asset received in the Contribution will include the period during which such asset was held by Distributing. Section 1223(2).

(6) Distributing will recognize no gain or loss on the Distribution. Section 361(c)(1).

(7) A will recognize no gain or loss (and no amount will be included in A's income) upon the receipt of the Controlled stock in the Spin-off. Section 355(a)(1).

(8) The aggregate basis of the Distributing and Controlled stock in the hands of Distributing's sole shareholder, A, will equal A's basis in the Distributing stock held immediately before the Distribution, allocated between the Distributing stock and the Controlled stock in proportion to the relative fair market value of each in accordance with §1.358-2(a)(2). Section 358(a)(1),(b) and (c)).

(9) The holding period of Controlled stock received by Distributing's shareholder in the Distribution will include the holding period of the Distributing stock with respect to which the Distribution will be made, provided that such Distributing stock is held as a capital asset on the date of the Distribution. Section 1223(1).

(10) Proper allocation of earnings and profits and the accumulated adjustments account between Distributing and Controlled immediately before the transaction will be made in accordance with §§ 312(h), 1.312-10(a) and 1.1368-2(d)(3).

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. Moreover, no opinion is expressed 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 (as provided above), no opinion is expressed regarding: (i) whether the Distribution satisfies the business purpose requirement of §1.355-2(b); (ii) whether the proposed transaction is used

principally as a device for the distribution of the earnings and profits of the distributing corporation or the controlled corporation or both (see § 355(a)(1)(B) and §1.355-2(d));

and (iii) whether the Distribution and an acquisition or acquisitions are part of a plan (or series of related transactions) under § 355(e)(2)(A)(ii).

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

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representatives.

A copy of this letter must be attached to any income tax return to which it is relevant.

Sincerely,

_____
Alison G. Burns
Chief, Branch 2
Office of the Associate Chief Counsel
(Corporate)