Internal Revenue Service

Department of the Treasury

Washington, DC 20224

200108043

UIC: 4975.04-00

Contact Person:

Telephone Number:

In Reference to:
T:EP:RA:T3 ID:50-03192

Date:
NOV 27 2000

Attn:

LEGEND:

Company A:

Company B:

Company C:

Company D:

State E:

State F:

Government
Organization G:

Plan X:

Date 1:

Date 2:

Date 3:

Date 4:

Date 5:

Month 1:

Percentage 1:

Percentage 2:

Percentage 3:

Trustee W:

Threshold Price:

Actual Price:

240

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Dear :

This is in response to the request for letter ruling dated , , submitted on your behalf by your authorized representative, as supplemented by correspondence dated , and , in which you seek a letter ruling as to the consequences under section 1.46-8(e)(10) of the Income Tax Regulations of the transaction described herein. The following facts and representations support your ruling request.

During Month 1, 1997, Company B engaged in a corporate reorganization that formed two new corporations, Company A and Company D. Company D had previously operated as a division of Company B. As a result of this Month 1 reorganization, Company A became the parent of Company B and Company D.

Effective Month 1, 1997, Plan X was amended to make Company A a sponsoring employer thereof.

After Companies A and D were created in 1997, the stock of Companies A, B, and D satisfied the definition of "employer securities" as that term is used in Code section 409(l)(2). Additionally, Plan X exchanged its Company B stock for Company A stock. After said exchange, Plan X held only Company A stock.

Company A is a State E corporation which has its primary office in State F. Company A has no employees but is a holding company whose subsidiaries previously included Company B, Company C, and Company D. Until Date 1, approximately Percentage 1 of the outstanding stock of Company D was owned by Company A. On Date 1, Company D made an initial public offering (IPO) of its stock. As a result of the IPO, Company A owned approximately Percentage 2 of the outstanding stock of Company D. Company D stock is now publicly traded on the Nasdaq National Market System. Prior to the IPO, none of the stock of either Company A, Company B, Company C, or Company D was publicly traded.

Plan X was established on Date 2. Trustee W is the trustee of Plan X. The Plan X Administrative Committee is a three member committee appointed by Company A. Plan X has never covered employees of either Company C or Company D. Furthermore, as noted above, Company A has never had any employees. Until Date 3, Plan X held only stock of Company A. Company A had only one class of stock, and Plan X held approximately Percentage 3 of that stock. Plan X is not a tax credit employee stock ownership plan (TRASOP).

Prior to the Date 1 IPO of Company D stock, the Plan X Administrative Committee and Company B were aware that the IPO would cause Company D stock to become the only "employer securities" under Code section 409(l) with respect to Plan X. A number of possible courses of action were discussed. However, the Plan X Administrative Committee was also aware, prior to the Date 1 IPO, that the Directors of Company A and its subsidiaries planned a major corporate reorganization, the result of which would be that Plan X would acquire Company B stock. As a result of the acquisition of Company B stock by Plan X, Company D stock would no longer constitute "employer securities" within the meaning of Code section 409(l) with respect to Plan X. Furthermore, the Administrative

Committee of Plan X was aware, as of the date of the Date 1 IPO, that certain steps relating to the corporate reorganization were imminent.

The Plan X Administrative Committee was aware that the above-referenced corporate reorganization would, in all probability, be completed within one (1) year of the Date 1 IPO. However, since the reorganization required approval by the Internal Revenue Service and a "no action" letter from Government Organization G, the Administrative Committee was also aware that the reorganization could not be completed within 90 days of the Date 1 IPO. Furthermore, as the Plan X Administrative Committee also understood, the reorganization was contingent upon Company D acquiring at least 90% of the fair market value of the net assets of Company A. The price of Company D stock had to remain above the Threshold Price in order for this condition to be met. On Date 5, 2000, the price of Company D stock was Actual Price per share which exceeded the per share Threshold Price.

As noted above, Company A stock has not ever been publicly traded. Thus, there was no possibility that Plan X could convert Company A stock to Company D stock during the period between the Date 1 IPO and the date of the above-referenced corporate reorganization. Furthermore, immediately following the Date 1 IPO, the price of Company D stock fluctuated greatly due, in part, to the "high tech" nature of Company D's business. Finally, the Plan X Administrative Committee could not direct the Trustee thereof to acquire Company D stock at that time because the Trust did not have any liquid assets to make such acquisition of Company D stock.

On Date 4, 1999, Company A requested a letter ruling from the Service concerning the proposed plan of reorganization. As noted above, within two weeks of Date 4, 1999, this request for letter ruling was filed with the Service. This specific letter ruling request regarding the reinvestment period was filed within 90 days of the Date 1 IPO.

On April 27, 2000, the Service issued a letter ruling approving the above-referenced plan of reorganization.

On July 21, 2000, Company A received its requested "no action" letter from Government Organization G. Several days later, on Date 5, 2000, the price of Company D stock was above the required threshold. Thus, on Date 5, 2000, Plan X acquired all of the outstanding stock of Company B in exchange for a portion of its Company A stock pursuant to step (ii) of the above-referenced plan of reorganization. This acquisition of Company B stock by Plan X was approved by the Plan Administrator of Plan X. It is represented that the acquisition was for "adequate consideration", as such term is defined in sections 3(18)(B) and 408(e) of the Employee Retirement Income Security Act of 1974 (ERISA).

Accordingly, effective Date 5, 2000, Company B stock constitutes "employer securities" within the meaning of Code section 409(l) with respect to Plan X. Date 5, 2000, occurred 272 days after Date 1.

The plan of reorganization, referenced above, in which Company A and Company D entered, is described in section 368(a)(1)(C) of the Internal Revenue

Code. Pursuant to said plan, Company A exchanged substantially all of its assets for Company D stock. This transfer was part of a series of integrated transactions pursuant to the above-mentioned plan of reorganization. As part of the reorganization, Company A divested itself of its Company B and its Company C stock. And as noted above, as part of the reorganization, Company A transferred all Company B stock to Plan X as a partial redemption of Company A stock held by Plan X.

After Company A divested itself of its Company B stock, Company B was no longer in a controlled group with either Company A or Company D. Company A intends to liquidate since the reorganization is complete. Company A will distribute, in complete liquidation, its Company D common stock to Company A shareholders in proportion to their respective ownership of Company A stock. No other property will be distributed to Company A shareholders. Thus, as a result of the reorganization, Company B will be the sole sponsoring employer of Plan X.

Plan X will continue to be designed to invest primarily in employer securities after the reorganization is completed. In order to continue as an ESOP after the reorganization, Plan X will be required to invest in Company B stock because said stock constitutes the only employer securities under Plan X.

Based on the above facts and representations, the following letter ruling is requested:

> That if the 90-day reinvestment period of section 1.46-8(e)(10) of the Income Tax Regulations applies to Plan X, then the Commissioner of the Internal Revenue Service shall extend said reinvestment period pursuant to his authority found in the regulations so that any and all sales and exchanges of Company A stock by Plan X following the IPO of Company D Stock, referenced above, and the reinvestment of the proceeds of such sales in, or the receipt in such exchanges of either Company B or Company D stock, may take place over a period commencing on Date 1 and ending on Date 5, 2000, 272 days later, without resulting in the failure of Plan X to satisfy the requirement of section 4975(e)(7) of the Internal Revenue Code that Plan X be designed to invest primarily in employer securities.

With respect to your ruling request, Code section 4975(e)(7) provides, generally, that an employee stock ownership plan (ESOP) is a defined contribution plan which is a qualified stock bonus plan, or a stock bonus plan and a money purchase plan, both of which are qualified under Code section 401(a), which is designed to invest primarily in "qualifying employer securities" as defined in Code section 4975(e)(8).

Code section 4975(e)(8) defines a "qualifying employer security" as an employer security within the meaning of Code section 409(l). Code section 409(l) provides that the term "employer securities" means common stock issued by the employer (or by a corporation which is a member of the same controlled group within the meaning of section 1563(a) determined without regard to

sections 1563(a)(4) and 1563(e)(3)(C)), which is "readily tradable on an established securities market".

Code section 409(l)(2) provides a special rule where there is no readily tradable common stock of the employer, or within the controlled group of employers. Under such circumstances, "employer securities" under the plan shall be the common stock issued by the employer, or by a corporation which is a member of the same controlled group, that has a combination of voting power and dividend rights equal to or exceeding that of the class of common stock of the employer having the greatest voting power and the class of stock having the greatest dividend rights.

Code section 1563(a)(1) provides that a parent-subsidiary controlled group exists where one or more chains or corporations are connected through stock ownership with a common parent corporation, if stock possessing at least 80 percent of the total combined voting power of all classes of stock entitled to vote, or at least 80 percent of the total value of shares of all classes of stock of each of the corporations, except the common parent corporation, is owned by one or more of the other corporations, and the common parent owns stock possessing at least 80 percent of the total combined voting power of all classes of stock entitled to vote or at least 80 percent of the total value of shares of all classes of stock of at least one of the other corporations in the chain. In computing such voting power or value percentage, stock owned by other corporations in the chain is excluded.

Code section 409(l)(4)(B) provides, with regard to the term "controlled group of corporations" under Code section 1563(a)(1), that if the common parent owns directly stock possessing at least 50 percent of the voting power of all classes of stock and at least 50 percent of each class of nonvoting stock in a first tier subsidiary, such subsidiary (and all other corporations below it in the chain which would meet the 80 percent test of section 1563(a) if the first tier subsidiary were the common parent) shall be treated as includible corporations.

Section 1.46-8(e)(10) of the Income Tax Regulations provides that the requirement that a tax-credit ESOP be designed to invest primarily in employer securities is a continuing obligation. Therefore, a transaction changing the status of a corporation as an employer may require the conversion of certain plan assets into other securities. Section 1.46-8(e)(10) further provides that cash or other assets derived from the disposition of employer securities held by a TRASOP must be reinvested in new employer securities not later than the ninetieth day following the date of disposition. However, the Commissioner may grant an extension of the period for reinvestment in employer securities depending on the facts and circumstances of each case.

In this case, prior to the IPO, none of the stock of either Company A or any of its subsidiaries was publicly traded. Thus, prior to the IPO, the common stock of Company A fell within the definition of "employer securities" under Code section 409(l)(2) although that stock was not publicly traded. As a result of the IPO, however, Company D has become "readily tradable" and, therefore, Company D stock satisfied the definition of "employer securities" under Code section 409(l)(1) with respect to Plan X. Because Company A stock

was not publicly traded, said stock no longer constituted "employer securities" within the meaning of Code section 409(l) with respect to Plan X.

However, as described above, the corporations referenced in this ruling intended to reorganize as of Date 1 in such a manner that Company B and Company D would no longer be members of a controlled group but would be unrelated entities even under the expanded definition of "controlled group" found in Code section 409(l)(4)(B). Furthermore, as noted above, the corporations have, in fact, reorganized. After the reorganization, Company B is the sole employer sponsoring Plan X. Thus, after the reorganization, Company B common stock is the only "employer securities" with respect to Plan X. Furthermore, as part of the series of integrated transactions constituting the reorganization, Plan X on Date 5, 2000, acquired all of the stock of Company B.

In situations, such as this, where, as a result of an integrated transaction which involved a corporate reorganization described in Code section 368, all of the employer securities held in Plan X, an ESOP described in Code section 4975(e)(7), which is not a TRASOP, lose their Code section 409(l) qualified status, but later, as a result of actions taken to effectuate the reorganization, the subject employer securities are reinvested in securities which attain Code section 409(l) status, it is appropriate to apply the principles underlying section 1.46-8(e)(10) of the regulations to determine Code section 409(l) qualified status of the subject employer securities during said transaction.

Based on the facts and circumstances in this case, the Service believes that it was reasonable for the subject stock not to be reinvested in qualified employer securities until Date 5, 2000, which date was 272 days after the date of the Date 1 IPO referenced herein.

Therefore, with respect to your ruling request, we conclude as follows:

That the 90-day reinvestment period of section 1.46-8(e)(10) of the Income Tax Regulations applies to the above-described transaction involving stock held in Plan X, an ESOP which is not a TRASOP. Furthermore, the Commissioner of the Internal Revenue Service extends said reinvestment period pursuant to his authority found in the regulations so that any and all sales and exchanges of Company A stock by Plan X following the IPO of Company D Stock, referenced above, and the reinvestment of the proceeds of such sales in, or the receipt in such exchanges of either Company B or Company D stock, may take place over a period commencing on Date 1 and ending on Date 5, 2000, 272 days later, without resulting in the failure of Plan X to satisfy the requirement of section 4975(e)(7) of the Internal Revenue Code that Plan X be designed to invest primarily in employer securities.

This ruling letter is based on the assumption that Plan X is otherwise qualified under Code sections 401(a), 409, and 4975(e)(7) at all times relevant thereto.

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

A copy of this ruling letter has been sent to your authorized representative pursuant to a power of attorney on file in this office.

Sincerely yours,

Frances V. Sloan

Frances V. Sloan
Manager, Group 3
Tax Exempt and Governmental
Entities Division