Office of Chief Counsel
Internal Revenue Service

# memorandum

CC:WR:NCA:SF:TL-N-612-98
JPThurston

date: JUN 0 1 1999

to: Assistant Chief Counsel (Field Service) CC:DOM:FS

from: District Counsel, Northern California District, San Francisco

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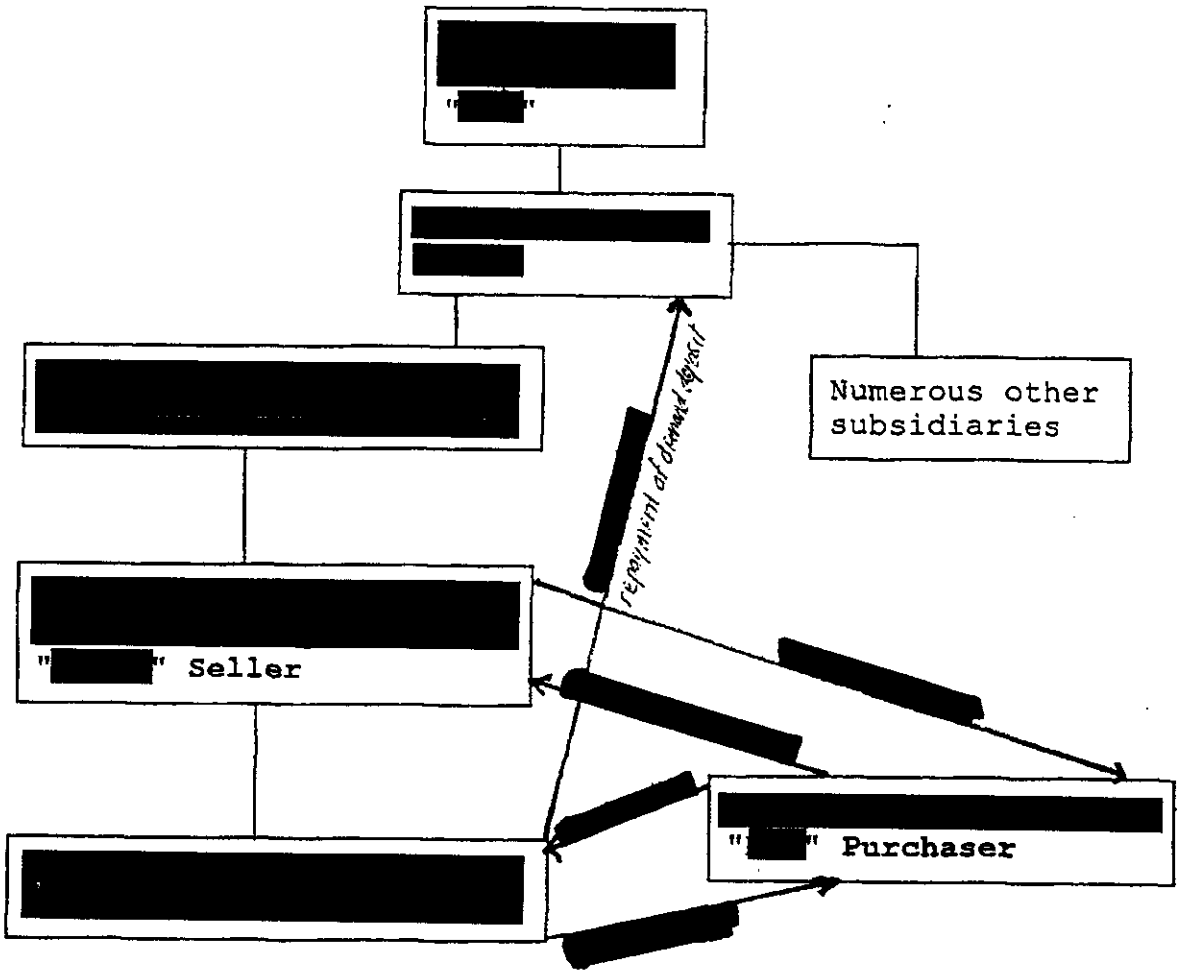
subject: **Request for Post-Review of Significant Advice**
**Review of** [redacted]

We request post-review of oral advice we offered the [redacted] audit team. The audit team requested our advice on the tax consequences of a sale of an [redacted] subsidiary to a third party purchaser.

We believe this advice qualifies for post-review under CCDM (35)3(19)4(4)because the advice involves the application of well-settled principles of law to the facts.

We have attached a copy of a Notice of Proposed Adjustment ("NPA")prepared by the [redacted] audit team setting forth facts and copies of relevant documents along with a proposed adjustment. We have been advised by the [redacted] audit team the NPA will not be issued to the taxpayer based in part upon the advice we offered.

Following is a diagram of the facts as set forth in the NPA:




On , sold to for Dollars(" ") . The sale resulted in a capital loss claimed on the consolidated income tax return of in the amount of $ . The transaction was structured in two steps. First, subscribed to stock in in the amount of . used the capital to extinguish it sole liability, a demand deposit from . Second, purchased for all of the remaining stock of .

The proposed to characterize the equity subscription by as part of the purchase price received by for the stock of . The asserted that the value of the assets acquired by was consistent with a purchase price of instead of the reflected in the sales agreement. The states that the demand deposit of should have been included in the asset pool of .

We orally advised the audit team that the NPA position fails to take into consideration that the [redacted] was at all times both an asset and a liability. It was a liability payable to [redacted] before the demand deposit was paid off and it was a liability payable to [redacted], as a shareholder, after it was paid off. At no time did [redacted] have a net book value of [redacted] as asserted in the [redacted]. In fact, the net book value of [redacted] at closing was [redacted].

Moreover, to adopt the position taken in the [redacted] it would be necessary to attribute receipt of the [redacted] paid to [redacted] in satisfaction of the demand note as in substance received by [redacted] as part of the purchase price. The note payable to [redacted] would need to be disregarded. However, the $[redacted] appears to be legitimate debt of [redacted] payable to [redacted] and no evidence is cited to the contrary.

The [redacted] could be considered part of the purchase price if [redacted] had been liable to [redacted] for the demand deposit. But there is no evidence that this was the case.

We advised that we did not think that the [redacted] equity subscription by [redacted] followed by the satisfaction of [redacted]'s [redacted] in indebtedness to [redacted] should be recharacterized as a payment of part of the purchase price by [redacted] to [redacted] for its [redacted] stock.

Please call Jim Thurston at (415) 744-9201 if you have any questions.

James P. Thurston

JAMES P. THURSTON
Special Litigation Assistant

Attachment
cc: Assistant Regional Counsel (TL)
(without attachment)