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Person To Contact:
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May 23, 2006

LEGEND

Corporation =
State =
a =
b =
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d =
e =
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g =

Dear :

We received a letter dated November 7, 2005 from your authorized representative requesting rulings regarding the application of § 216 of the Internal Revenue Code. This letter responds to that request.

The represented facts are as follows. Corporation is a cooperative housing corporation organized under the laws of State. Corporation owns land and a building, which consists of a residential units and a ground floor that contains b commercial unit and a parking garage. Currently, c shares of common stock of Corporation are issued and outstanding, out of a total of d authorized shares. All of the outstanding common stock has been allocated to the residential units. No stock has been allocated to the commercial unit or the garage. The total square footage of the residential units is e. The square footage of the commercial unit is f.

Corporation proposes to allocate g shares of its authorized but unissued stock to the commercial unit (New Shares). Corporation represents that the shares allocated to the commercial unit will bear a reasonable relationship to the ratio of the value of

Corporation's equity in the commercial unit to the value of the Corporation's equity in the land, building and garage.

The proprietary lease will entitle the purchaser of the additional shares attributable to the commercial unit to occupy the unit for dwelling purposes solely by reason of the ownership of such shares. The owner of the commercial unit will be entitled to install facilities in commercial unit for cooking, sleeping, and sanitation normally found in residence.

Corporation further proposes to form a limited liability company (LLC) with Corporation as the sole member. Corporation will transfer the New Shares to LLC, and then distribute all of the membership interests in LLC pro rata to Corporation's tenant-stockholders. LLC will elect to be classified as a partnership.

Corporation represents that the local zoning law and building regulations currently permit modification of the commercial unit to residential use as a matter of right. Corporation submits facts and representations to show that it would be reasonable to convert the commercial unit to residential use. The size and location of the commercial unit are such that, with certain modifications, it could be converted into residential apartments. The cost of adding sleeping and cooking facilities to the commercial unit would be approximately 20 percent of the fair market value the commercial unit would have if it was sold as a residential unit.

You have specifically requested the following rulings:

(1) Initially, LLC will be treated as a disregarded entity. Accordingly, Corporation will be treated as the owner for federal tax purposes of the New Shares held by LLC. The distribution by Corporation of the LLC interests will be treated as a distribution by Corporation of the LLC assets (the New Shares). Immediately after the distribution, the stockholders of Corporation will be treated as contributing the New Shares to LLC. Unless it elects otherwise, LLC will be treated as a partnership for federal tax purposes following the distribution of the New Shares to Corporation's stockholders.

(2) The issuance of shares allocated to the Commercial unit and the possible nonresidential use of the commercial unit will not prevent Corporation from qualifying as a cooperative housing corporation under § 216(b).

(3) For purposes of § 216(b)(1)(D), the income Corporation receives from LLC will be income derived from tenant-stockholders.

(4) The deemed distribution by Corporation of the New shares will not be treated as a distribution to the tenant-stockholders to which § 301 applies by reason of § 305(b) or (c) but will constitute a distribution to which § 305(a) applies. Thus, the

distribution will not result in taxable income to any of the Corporation's shareholders. Further, the basis of the stock in Corporation held by a shareholder immediately prior to the distribution of the shares will be allocated between the stock immediately prior to the distribution of the shares and the New Shares deemed received in the distribution in proportion to the fair market value of the stocks of each immediately after the distribution in accordance with § 307(a).

(5) No gain or loss will be recognized to Corporation upon the deemed distribution of the New Shares, in accordance with § 311(a).

(6) The deemed transfer to LLC by Corporation's shareholders of their newly received shares will have no adverse effect upon any of the above conclusions.

Ruling Request 1

Section 301.7701-3(a) of the Procedure and Administration Regulations provides that a business entity that is not classified as a corporation under § 301.7701-2(b)(1), (3), (4), (5), (6), (7), or (8) (an eligible entity) can elect its classification for federal tax purposes. An eligible entity with at least two members can elect to be classified as either an association (and thus a corporation under § 301.7701-2(b)(2)) or a partnership, and an eligible entity with a single owner can elect to be classified as an association or to be disregarded as an entity separate from its owner. Elections are necessary only when an eligible entity does not want to be classified under the default classification or when an eligible entity chooses to change its classification.

Section 301.7701-3(b)(1) provides that, unless it elects otherwise, a domestic eligible entity is (i) a partnership if it has two or more members; or (ii) disregarded as an entity separate from its owner if it has a single owner.

In Rev. Rul. 99-5, 1999-1 C.B. 434, Situation 1, LLC, which for federal tax purposes is disregarded as an entity separate from its owner, is converted to a partnership when the new member, B, purchases an interest in the disregarded entity from the owner, A. B's purchase of 50% of A's ownership interest in LLC is treated as the purchase of a 50% interest in each of the LLC's assets which are treated as held directly by A for federal tax purposes. Immediately thereafter, A and B are treated as contributing their respective interests in those assets to a partnership in exchange for ownership interests in the partnership.

Initially, LLC will be treated as an entity disregarded from its owner. Accordingly, Corporation will be treated as the owner for federal tax purposes of the New Shares held by LLC. The distribution by Corporation of the LLC interests will be treated as a distribution by Corporation of the LLC assets (New Shares). Immediately after the distribution, the stockholders of Corporation will be treated as contributing the New

Shares to LLC. Unless it elects otherwise, LLC will be treated as a partnership for federal tax purposes.

Ruling Requests 2 & 3

Section 216(b)(1) provides that the term “cooperative housing corporation” means a corporation - (A) having one and only one class of stock outstanding, (B) each of the stockholders of which is entitled, solely by reason of his ownership of stock in the corporation, to occupy for dwelling purposes a house, or an apartment in a building, owned or leased by such corporation, (C) no stockholder of which is entitled (either conditionally or unconditionally) to receive any distribution not out of earnings and profits of the corporation except on a complete or partial liquidation of the corporation, and (D) 80 percent or more of the gross income of which for the taxable year in which the taxes and interest described in § 216(a) are paid or incurred is derived from tenant-stockholders.

Section 216(b)(2) provides that the term “tenant-stockholder” means a person who is a stockholder in a cooperative housing corporation, and whose stock is fully paid-up in an amount not less than an amount shown to the satisfaction of the Secretary as bearing a reasonable relationship to the portion of the value of the corporation’s equity in the houses or apartment building and the land on which situated which is attributable to the house or apartment which such person is entitled to occupy.

Section 1.216-1(e)(2) provides, in relevant part, that in order to qualify as a “cooperative housing corporation” under § 216, each stockholder of the corporation, whether or not the stockholder qualifies as a tenant-stockholder under §§ 216(b)(2) and 1.216-1(f), must be entitled to occupy for dwelling purposes an apartment in a building or a unit in a housing development owned or leased by such corporation. The stockholder is not required to occupy the premises. The right as against the corporation to occupy the premises is sufficient. Such right must be conferred on each stockholder solely by reasons of his or her ownership of stock in the corporation. That is, the stock must entitle the owner thereof either to occupy the premises or to a lease of the premises. The fact that the right to continue to occupy the premises is dependent upon the payment of charges to the corporation in the nature of rentals or assessments is immaterial.

Rev. Rul. 74-241, 1974-1 C.B. 68, provides that, for purposes of § 216(b)(1)(B), the term “apartment in a building” means an independent housekeeping unit consisting of one or more rooms containing facilities for cooking, sleeping, and sanitation normally found in a principal residence.

Rev. Rul. 90-35, 1990-1 C.B. 48, provides that Rev. Rul. 74-241 does not require that a unit presently contain all the facilities normally found in a principal residence in order to constitute an apartment in a building for purposes of § 216(b)(1)(B). A unit will

be treated as meeting that definition if: (1) the stockholder is entitled to convert the unit to an apartment, as defined in Rev. Rul. 74-241, solely by reason of ownership of stock in the cooperative housing corporation; (2) the conversion of the unit would be reasonable under all the facts and circumstances, including structural feasibility and cost; and (3) the applicable zoning, building, and fire codes permit both the conversion and residential use of the unit as a matter of right.

Applying the above standards to the facts and representations submitted and subject to the limitation below and based solely upon those representations, we conclude that provided Corporation satisfies the requirements of § 216(b)(1)(A), (C), and (D), neither the issuance of stock by Corporation to be allocated to the commercial unit nor the possible nonresidential use of the unit will prevent Corporation from qualifying as a cooperative housing corporation within the meaning of § 216(b)(1).

We also conclude that for purposes of § 216(b)(1)(D), the income Corporation receives from LLC will be income derived from tenant-stockholders provided that the fully paid-up requirement of § 216(b)(2) is met.

Ruling Requests 4 & 5

Section 305(a) provides that except as otherwise provided, gross income does not include the amount of any distribution of the stock of a corporation made by such corporation to its shareholders with respect to its stock.

Section 305(b) provides that distributions in lieu of money, disproportionate distributions, distributions of common stock and preferred stock, distributions on preferred stock and distributions of convertible preferred stock are treated as § 301 distributions of property.

Under §§ 305(c) and 1.305-7, a change in conversion ratio, a change in redemption price, a difference between redemption price and issue price, a redemption which is treated as a distribution to which § 301 applies, or any transaction having a similar effect on the interest of any shareholder may be treated as a distribution with respect to any shareholder whose proportionate interest in the earnings and profits or assets of the corporation is increased by such change, difference, redemption, or similar transaction.

Section 307(a) provides that if a shareholder in a corporation receives its stock ("new stock") in a distribution to which § 305(a) applies, then the basis of such new stock and of the stock with respect to which it is distributed ("old stock"), respectively, shall, in the shareholder's hands, be determined by allocating between the old stock and the new stock the adjusted basis of the old stock.

Section 1.307-1(a) provides that if a shareholder receives stock as a distribution on stock previously held and under § 305 such distribution is not includible in gross

income, the basis of the stock with respect to which the distribution was made shall be allocated between the old and new stocks in proportion to the fair market values of each on the date of distribution.

Section 311(a) provides that no gain or loss shall be recognized to a corporation on the distribution (not in complete liquidation) with respect to its stock, of its stock.

Section 301.7701-2(a) provides that if an entity is disregarded, its activities are treated in the same manner as a sole proprietorship, branch, or division of the owner.

Since LLC will be a disregarded entity, § 301.7701-2(a) will treat Corporation as the owner of LLC's assets, i.e. the New Shares. As such, Corporation's distribution of the LLC shares will be treated as a distribution of the New Shares. Because of Corporation's pro-rata distribution of common stock to its tenant-stockholders, the recipients of the LLC shares will not include the shares into gross income under § 305(a). Under §§ 307(a) and 1.307-1(a), the tenant-stockholders will allocate basis between their previously held shares and the New Shares in proportion to the fair market values of each on the date of distribution. Finally, there will be no gain or loss to Corporation on the distribution of its common stock under § 311(a).

Accordingly, we conclude that the deemed distribution by Corporation of the New Shares will not be treated as a distribution to the tenant-stockholders to which § 301 applies by reason of § 305(b) or (c) but will constitute a distribution to which § 305(a) applies. Thus, the distribution will not result in taxable income to any of the Corporation's shareholders. Further, the basis of the stock in Corporation held by a tenant-stockholder immediately prior to the deemed distribution by Corporation of the New Shares will be allocated between the Corporation stock held immediately prior to the distribution and the New Shares received in the distribution in proportion to the fair market value of the stocks of each immediately after the distribution in accordance with § 307(a).

We also conclude that the deemed distribution by Corporation of the New Shares will not result in the recognition of gain or loss by Corporation under § 311(a).

Ruling Request 6

Based on the information submitted and representations made we conclude that the transfer to a newly formed LLC by Corporation's shareholders of their newly received shares will have no adverse affect upon Ruling Requests 1, 2, 3, 4, or 5.

Except as expressly provided herein, we express or imply no opinion concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. Further, we express or imply no opinion whether Corporation otherwise meets the requirements of § 216.

Specifically, we express or imply no opinion as to whether Corporation meets the requirements of § 216(b)(2) concerning whether the stock bears a reasonable relationship to the portion of the value of the Corporation's equity in the building and land which is attributable to the unit which the purchaser is entitled to occupy.

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

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.

In accordance with the power of attorney on file with this office, we are sending copies of this letter to your authorized representatives. A copy of this ruling must be attached to any income tax return to which it is relevant.

Sincerely,

/s/

Joseph H. Makurath
Senior Technician Reviewer, Branch 7
Office of Associate Chief Counsel (Passthroughs
& Special Industries)