

IRS Letter Rulings and TAMs (1954-1997), UIL No. 7701.00-00 Definitions, Letter Ruling 9008035, (Nov. 24, 1989), Internal Revenue Service, (Nov. 24, 1989)

Letter Ruling 9008035, November 24, 1989

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Definitions

[Code Sec. 7701]

In a letter of May 10, 1989, you asked us to rule that income and gains derived under the following circumstances from the sale of pulp constitute "qualifying income" within the meaning of section 7704(d)(1)(E) of the Internal Revenue Code.

FACTS

Directly and through its subsidiaries, X, a domestic corporation, grows and cuts timber, extracts pulp from cut timber, and produces paper and containerboard. Y, a subsidiary of X, owns and operates a mill that extracts pulp from cut timber using the kraft process, and sells the pulp to paper producers.

The kraft pulping process separates cellulose fibers (pulp) from the other components of cut timber, lignin and bark. Either the mill or an outside producer begins the process by debarking logs (cut timber) and chipping the logs into wood chips. In a pressure vessel known as a digester, the mill dissolves the lignin from the chips in a steam-heated solution of water and chemicals. The mill then washes the separated cellulose fibers in water and passes the wet pulp solids ("brown stock") through knotters, which catch any undigested chips ("knots"). The brown stock is then bleached, cleaned, dried, baled, and sold in bulk to producers of paper.

X intends to cause Y to transfer this pulp mill to a limited partnership (Partnership), of which Y will be the general partner. X will cause units representing interests in Partnership to be listed on Exchange, an established securities market, where they will be sold in a registered offering and will be readily tradeable.

LAW AND DISCUSSION

Section 7704(a) of the Code generally treats publicly traded partnerships as corporations. Section 7704(b) defines "publicly traded partnership," in part, as any partnership if interests in that partnership are traded on an established securities market.

Section 7704(c)(1) of the Code exempts a publicly traded partnership from treatment as a corporation for any taxable year if the partnership met the gross income requirements of section 7704(c)(2) for that taxable year and every preceding taxable year beginning after December 31, 1987, during which the partnership was in existence. A partnership meets the gross income requirements of section 7704(c)(2) for any taxable year if 90 percent or more of the partnership's gross income for that taxable year consists of qualifying income.

Interests in partnership will be traded on an established securities market. Therefore, partnership will be a publicly traded partnership and will be treated as a corporation unless 90 percent or more of its gross income

for the taxable year consists of qualifying income.

Section 7704(d)(1)(E) of the Code defines "qualifying income," in part, as income and gains derived from the processing of any mineral or natural resource (including timber), and from transportation of natural resources.

We conclude that the pulping of cut timber constitutes the processing of a natural resource within the meaning of section 7704(d)(1)(E) of the Code, and that partnership will derive qualifying income from the manufacture and sale of pulp.

PROCEDURAL MATTERS

We express no opinion about the federal tax consequences of any aspect of this transaction other than the points expressly considered. We direct this ruling only to the taxpayer who requested it. Under section 6110(j) of the Code, it may not be used or cited as precedent.

As you requested in the power of attorney you filed with us, we are sending a copy of this letter to X.