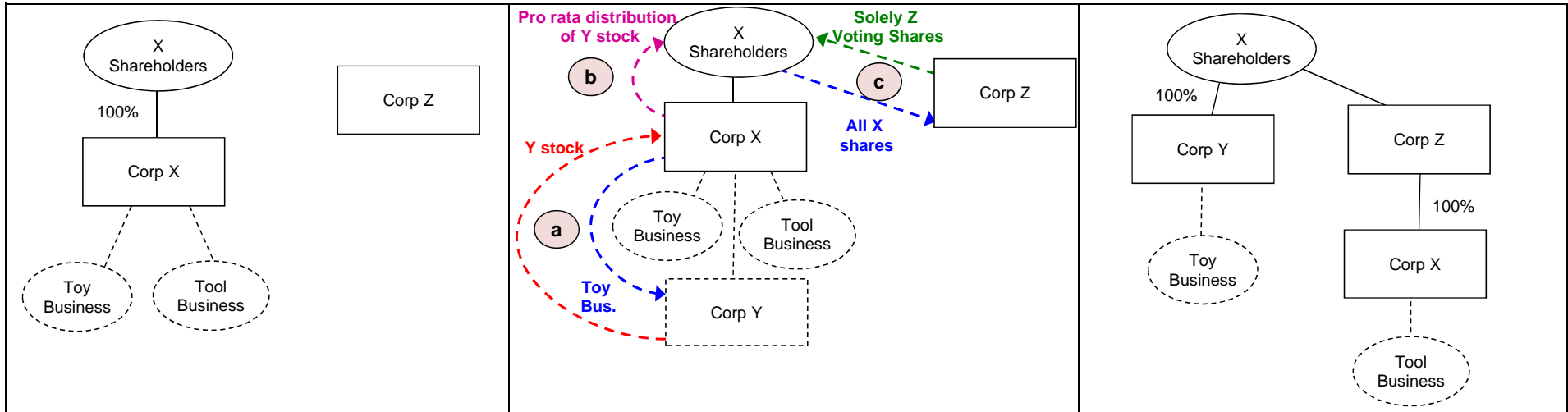


Spin-Off Followed by Stock-for-Stock Exchange Qualified as a "B" Reorganization

Initial Structure

Spin-Off (a & b) & B Reorganization (c)

Ending Point



Corporation X had been engaged in the active conduct of two businesses (toy manufacturing and hand tool manufacturing) for over five years. Corporation Z, an unrelated corporation, desired to acquire the stock of X but was only interested in having X conduct the hand tool manufacturing business. This was accomplished pursuant to a plan under which X transferred its toy manufacturing business, representing 23 percent of the assets of X, to a newly created corporation, Y, in exchange for all of the stock of Y which was distributed pro rata to the X shareholders in a transaction that qualified as a reorganization within the meaning of section 368(a)(1)(D) since the distribution of the Y stock met all of the requirements of section 355. Z then acquired all of the outstanding stock of X in exchange solely for voting common stock of Z. X remained in existence as a wholly owned subsidiary.

The exchange of the X stock for the Z stock is a reorganization within the meaning of section 368(a)(1)(B), which defines as a "reorganization" the acquisition by one corporation, in exchange solely for its voting stock, of stock of another corporation if, immediately after the acquisition, the acquiring corporation has control of such other corporation. The Y stock previously distributed to the X shareholders was not considered property received from Z in connection with the exchange of X stock for Z stock.