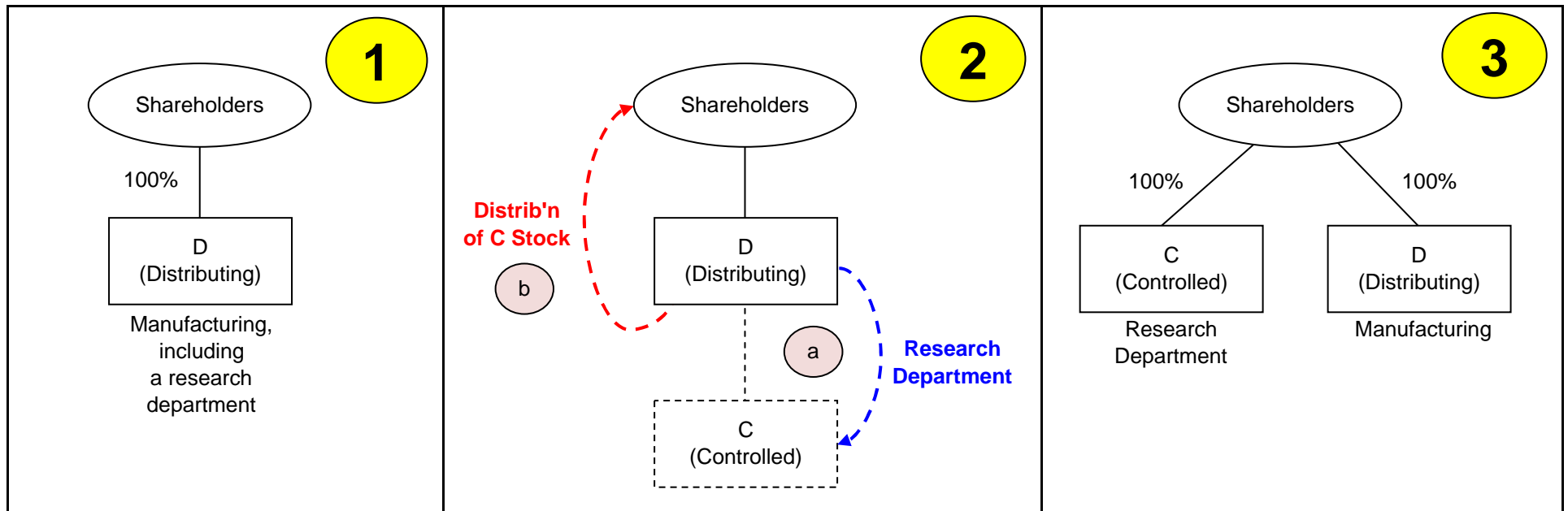


**Spin-Off -- Horizontal  
 Division-- Research**

**Initial Structure**

**Contribution / Spin-Off**

**Ending Point**



For more than five years, D has engaged in the active conduct of manufacturing and sale of household products. Throughout this period, D has maintained a research department for use in connection with its manufacturing activities. The research department has 30 employees actively engaged in the development of new products. D transfers the research department (which has significant assets and goodwill) to new subsidiary C and distributes the C stock to the D shareholders. After the distribution, C continues its research operations on a contractual basis with several corporations, including D. D and C both satisfy the requirements of section 355(b). The result is the same if, after the distribution, C continues its research operations but furnishes its services only to D. However, see §1.355-2(d)(2)(iv)(C) (related function device factor) for possible evidence of device.