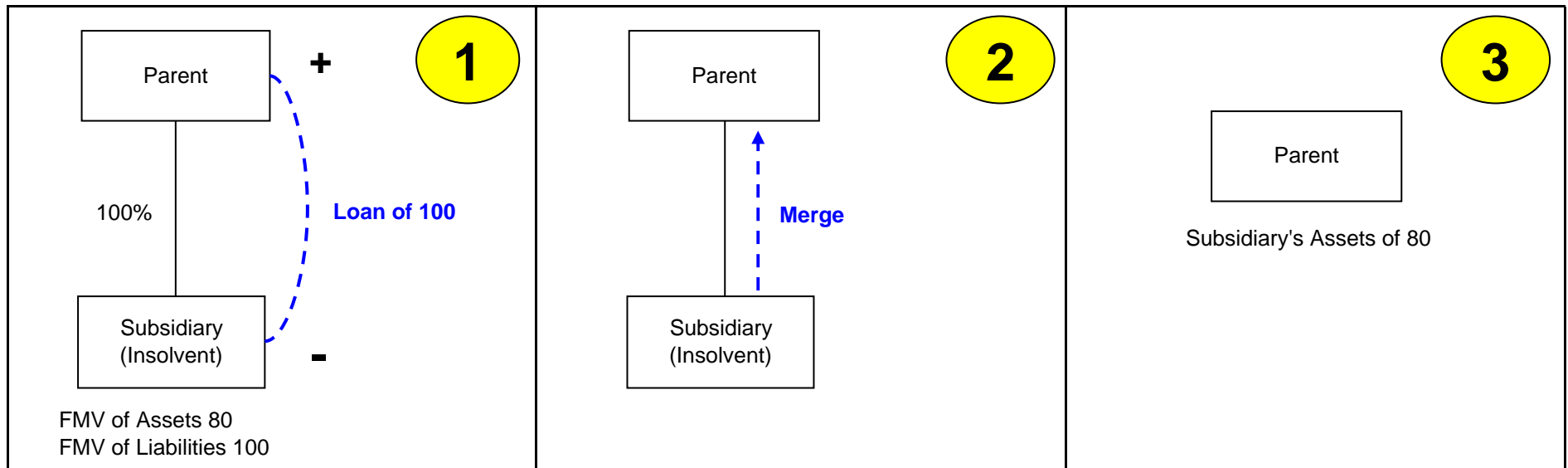


**Upstream Merger of Insolvent Subsidiary**

**Initial Structure**

**Upstream Merger**

**Ending Point**



Parent was a bona fide creditor of Subsidiary. Subsidiary was insolvent. Subsidiary merged into Parent. Under the applicable state merger statutes, the transfer of assets from Subsidiary to Parent was made in satisfaction of the indebtedness. Since all of the property of Subsidiary is worth less than the debt, no part of the transfer is attributable to the stock interest of Parent. The transaction is therefore neither a nontaxable distribution under section 332 nor a tax-free "reorganization" under section 368(a)(1)(A).

Parent is entitled to a bad debt deduction to the extent provided in section 166. Dollar amounts shown above were not included in the Revenue Ruling -- they have been added for illustrative purposes.