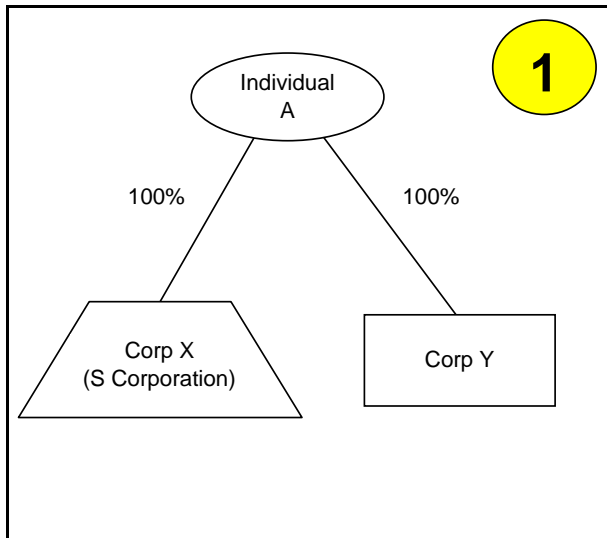
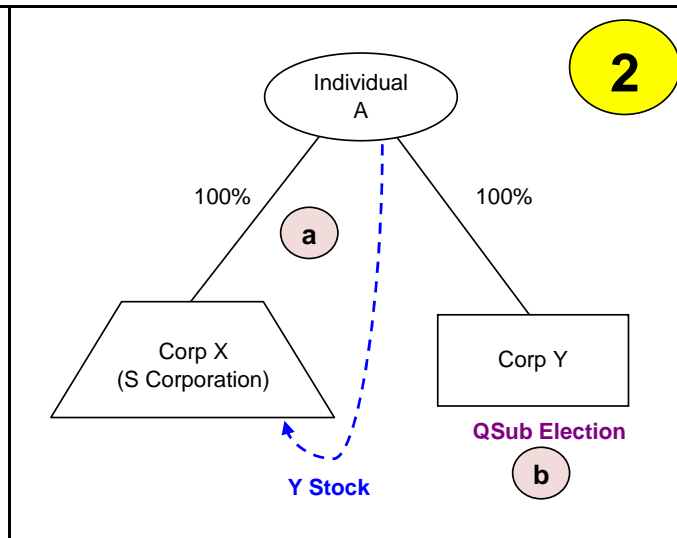


**Contribution & QSub Election  
(Drop & Check)**

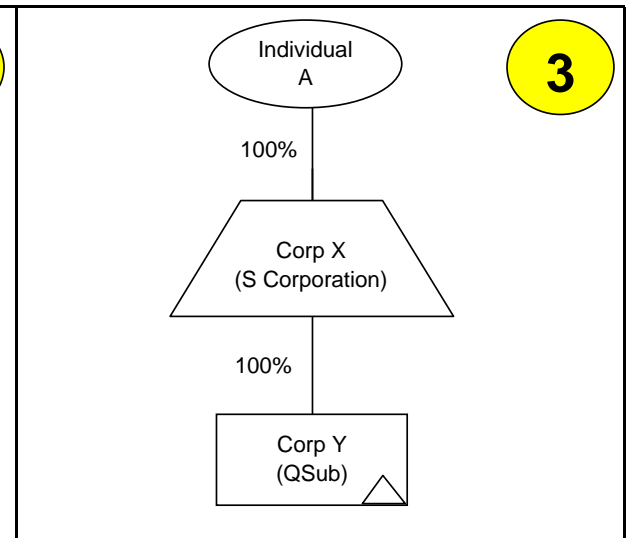
Initial Structure



Contribution & QSub Election



Ending Point



Individual A, pursuant to a plan, contributes all of the outstanding stock of Y to his wholly owned S corporation, X, and immediately causes X to make a QSub election for Y. The transaction is a reorganization under section 368(a)(1)(D), assuming the other conditions for reorganization treatment (e.g., continuity of business enterprise) are satisfied. The example indicates that if the sum of the amount of liabilities of Y treated as assumed by X exceeds the total of the adjusted basis of the property of Y, then section 357(c) applies and such excess is considered as gain from the sale or exchange of a capital asset or of property which is not a capital asset, as the case may be. However, section 357(c)(1)(B) was amended in 2004 as part of the American Jobs Creation Act. Section 357(c)(1)(B) now only applies to D reorganizations that are part of a section 355 spin-off / split-off / split-up type transaction. See Rev. Rul. 2007-8.

This transaction is very similar to a classic "drop and check" transaction in the international arena where an entity is contributed down and a check the box election is made.

△ Means "flow-thru" for U.S. tax purposes

▱ Means "S" Corporation