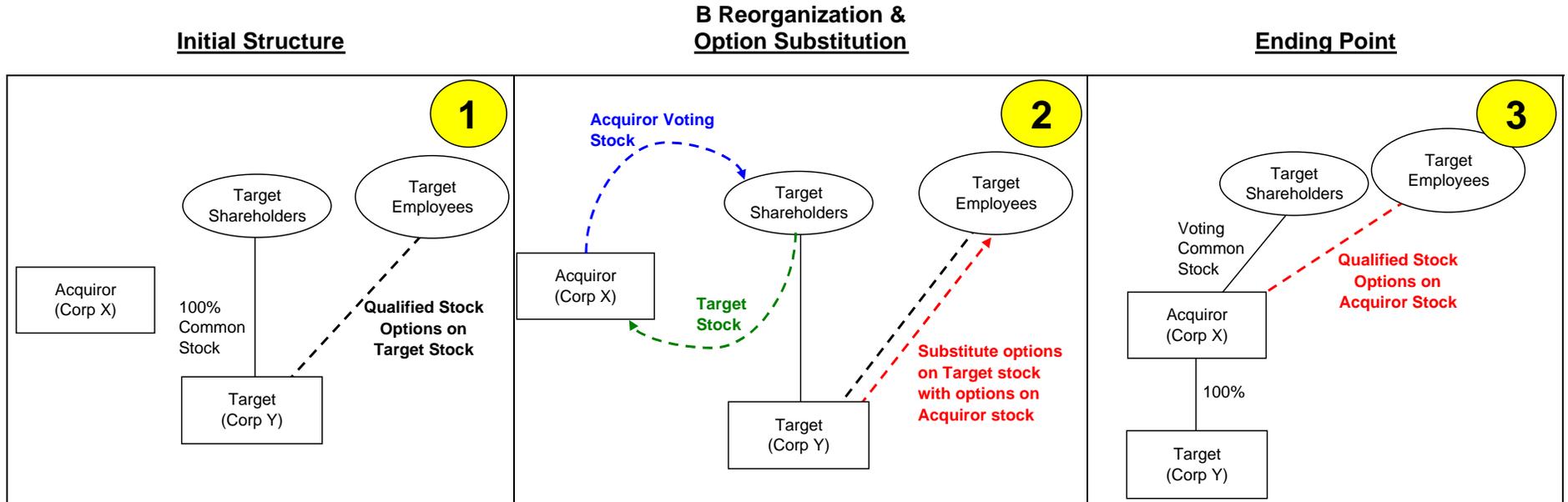


**B Reorganization:  
Substitution of Options**



Pursuant to a plan of reorganization, X corporation acquired all the outstanding stock of Y corporation from the Y shareholders in exchange for voting stock of X, the ratio of exchange being two shares of X stock for each share of the stock of Y based upon their fair market values at the time of the exchange. Y had outstanding qualified stock options (as defined in section 422(b)) to purchase Y stock. X substituted its own options for Y's outstanding qualified stock options when it acquired the Y stock in the exchange.

Some of the option holders of Y also owned stock of Y so that they received both X voting stock and X options in the transaction. The X options contained the same terms as the Y options except for relating to X stock with the number of shares being twice the number of shares of Y stock. The substitution of options was not a modification of the Y options, as defined in section 425(h)(3), so that it was not considered the granting of new options under section 425(h)(1).

Section 368(a)(1)(B) provides, in part, that a reorganization includes the acquisition by one corporation, in exchange solely for all or part of its voting stock, of stock of another corporation if, immediately after the acquisition, the acquiring corporation has control of such other corporation.

Although the substitution of options occurred as part of the overall transaction, the Y shareholders received exclusively X voting stock as consideration for the stock of Y. Shareholders owning stock of Y and who did not hold any Y options before the transaction did not receive options of X as a result of the transaction. Since the options contained the same terms as would have applied to the purchase of Y stock under the Y options, no additional benefits inured to the shareholders on the substitution of the options. Accordingly, in the instant case, only voting stock was utilized as consideration "in the acquisition of stock" within the meaning of section 1.368-2(c) of the regulations and the "solely for \* \* \* voting stock" requirement contained in section 368(a)(1)(B) is satisfied.