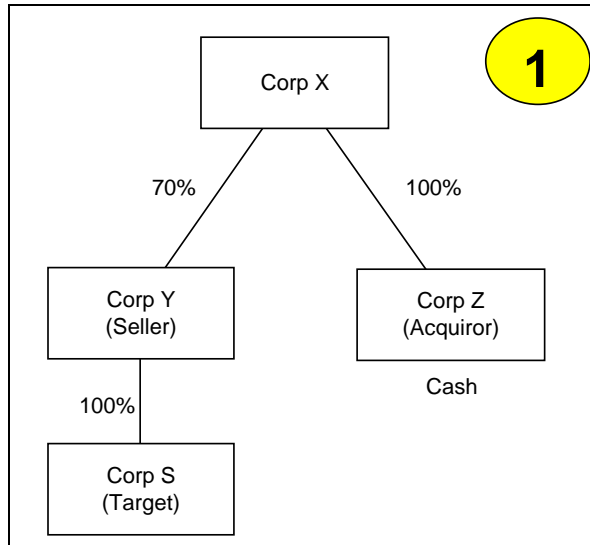
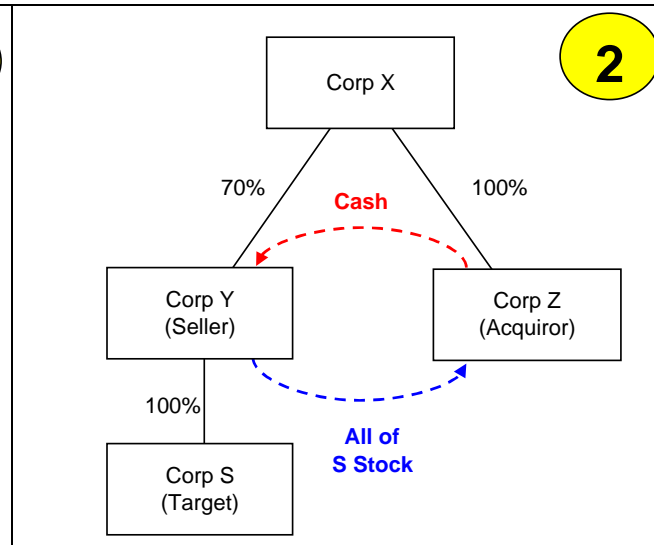


**Classic 304 Transaction**

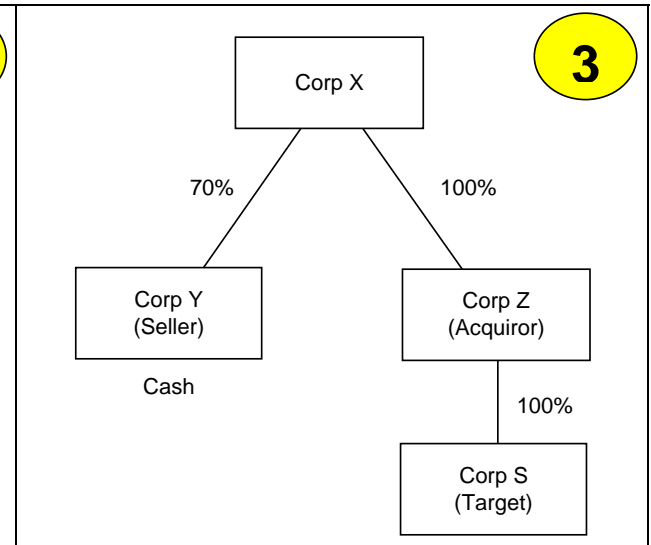
**Initial Structure**



**Sale of Stock**



**Ending Point**



Corporation X owns 70 percent of the stock of corporation Y and 100 percent of the stock of corporation Z. Y sold all of the stock of its wholly owned subsidiary, S, to Z for cash. Section 304(a)(1) provides that for purposes of section 302 and section 303, if one or more persons are in control of each of two corporations and in return for property, one of the corporations acquires stock in the other corporation from the person so in control, then such property shall be treated as a distribution in redemption of the stock of the corporation acquiring such stock. In any such case, the stock so acquired shall be treated as having been transferred by the person from whom acquired, and having been received by the corporation acquiring it, as a contribution to the capital of such corporation.

Section 304(c)(1) provides that for purposes of section 304 control means the ownership of stock possessing at least 50 percent of the total combined voting power of all classes of stock entitled to vote, or at least 50 percent of the total value of shares of all classes of stock. Section 304(c)(2) makes section 318(a) (relating to the constructive ownership of stock) applicable to section 304, with certain modifications, for the purposes of determining control under section 304(c)(1).

Y actually owned 100 percent of the stock of S before the transaction and by the application of section 318(a)(3)(C) (relating to the constructive ownership by a corporation of stock owned by its parent corporation) Y is considered to have owned all of the stock of Z before the transaction. Accordingly, since Z acquired the stock of S for cash from a person (Y) in control of both the issuing corporation (S) and the acquiring corporation (Z), the transaction is considered to be an acquisition of stock by a related corporation within the meaning of section 304(a)(1) and thus a redemption of the stock of Z, the acquiring corporation.