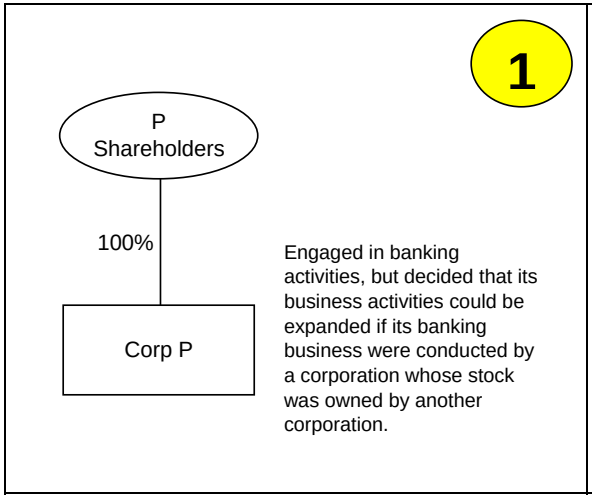
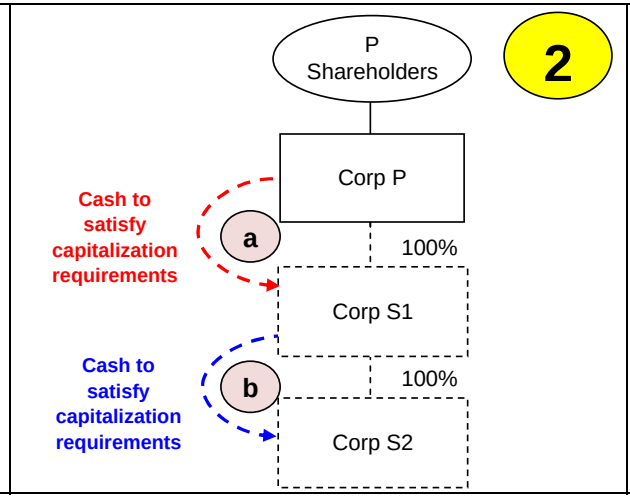
Revenue Ruling 77-428
Situation 1

Downstream Forward Triangular Merger

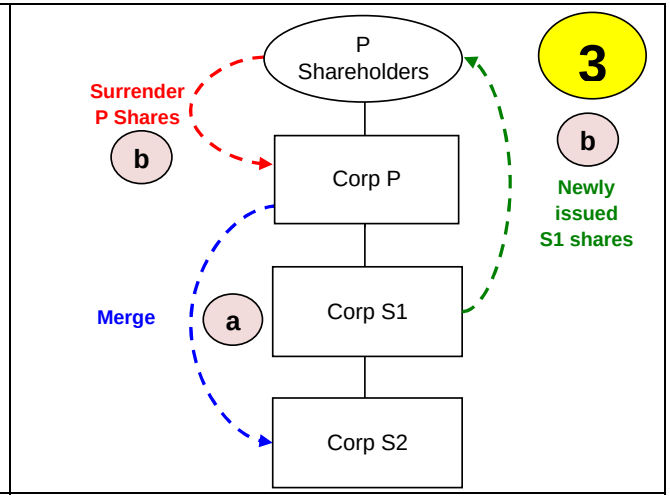
Initial Structure



Creation of Subsidiaries



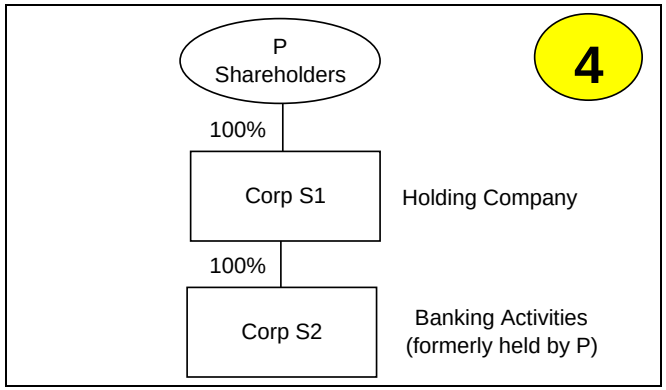
Downstream Forward Triangular Merger



P is a corporation chartered under state law that has been engaged in the commercial banking business for a number of years. P, for good business reasons, decided that its business activities could be expanded if its banking business were conducted by a corporation whose stock was owned by another corporation. The other corporation could then engage in related nonbanking activities, such as selling insurance to borrowers and leasing personal property, activities that could not be engaged in directly by P under state law. To accomplish this, P caused corporation S1 to be organized as a wholly owned subsidiary. S1 then caused corporation S2 to be organized as a wholly owned subsidiary. Other than the cash received from P to satisfy capitalization requirements, the only asset of S1 was the stock of S2, and the only asset of S2 was the cash received from S1 to satisfy capitalization requirements.

Pursuant to a plan of merger, P merged with and into S2 under the applicable state laws with S2 being the surviving corporation. On the effective date of the merger, each share of P stock held by the P shareholders was exchanged for a share of newly issued S1 stock. Thus, as a result of the merger, all the assets and business of P became the assets and business of S2, the P shareholders became the shareholders of S1, and S1 then engaged in the nonbanking activities described above.

Ending Point



Section 368(a)(2)(D) provides, in part, that the acquisition by one corporation, in exchange for stock of a corporation which is in control of the acquiring corporation, of substantially all of the properties of another corporation which in the transaction is merged into the acquiring corporation will not disqualify a transaction under section 368(a)(1)(A) if such transaction otherwise qualifies as a statutory merger and no stock of the acquiring corporation is used in the transaction. Reg. 1.368-2(b)(2) provides that this provision applies whether or not the controlling corporation (or the acquiring corporation) is formed immediately before the merger, in anticipation of the merger, or after preliminary steps have been taken to merge directly into the controlling corporation. While Reg. 1.368-2(b)(2) does not specifically provide for the formation of both the controlling and acquiring corporation, or for the acquiring of a related corporation, there is nothing in the legislative history of the enactment of section 368(a)(2)(D) to indicate that section was not intended to apply where such was the case. Accordingly, the merger of P with and into S2 qualifies as a reorganization under section 368(a)(1)(A) by reason of section 368(a)(2)(D) even though S1 and S2 were newly organized corporations and even though a related corporation was acquired in the transaction. See Rev. Rul. 72-274 in which a similar transaction was treated as a reorganization under section 368(a)(1)(A) by reason of section 368(a)(2)(D).