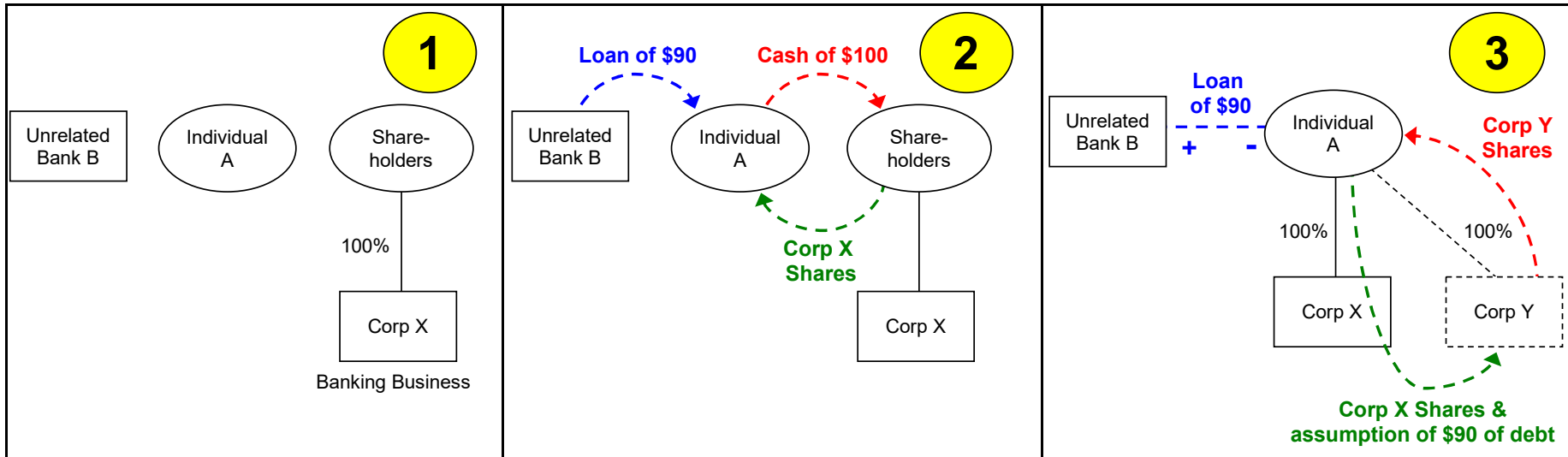


Shareholder Treated As Agent To Borrow Funds For Corp

Initial Structure

Borrowing & Purchase of Shares

Contribution & Liability Assump.



X is a corporation engaged in the general banking business that has solely common stock outstanding. In order to acquire indirect ownership of X through a bank holding company and to satisfy the appropriate banking rules and regulations, A, an individual who previously owned no X stock, devised the following plan. A first borrowed money from an unrelated financial institution B to acquire 90% of the X stock, pledging the X stock as security. A acquired the remaining 10% of X stock with his personal funds. A then formed Y, a new corporation, to be operated as a bank holding company, and immediately transferred all the X stock to Y. In exchange therefor, Y issued to A all of its stock and assumed the indebtedness incurred by A. The assumption by Y was done with the agreement of B and operated to release A from any liability with respect to the borrowed funds.

Section 351 applies to the transfer by A of the X stock to Y in exchange for the Y stock because A was in control of Y (as defined in section 368(c)) immediately after the exchange. If A had first formed Y and then had caused Y to borrow money from B so that Y would have directly acquired the 90% of the shares of X stock, there would have been no need for an assumption of the indebtedness by Y. In substance, there was no plan or intention for A to either own the X stock, or to repay the loan proceeds which were used to acquire that stock. Thus, for federal income tax purposes, A will be treated for this part of the transaction as a mere intermediate agent employed solely to satisfy non-tax related rules and regulations and the assumption of the indebtedness will be disregarded. Consequently, neither section 357(a) nor section 304(a)(1) have any application to the transaction since there is no assumption of a liability and also no "property" is distributed by Y, the acquiring-transferee corporation, within the meaning of section 304(a)(1).

Ending Point

