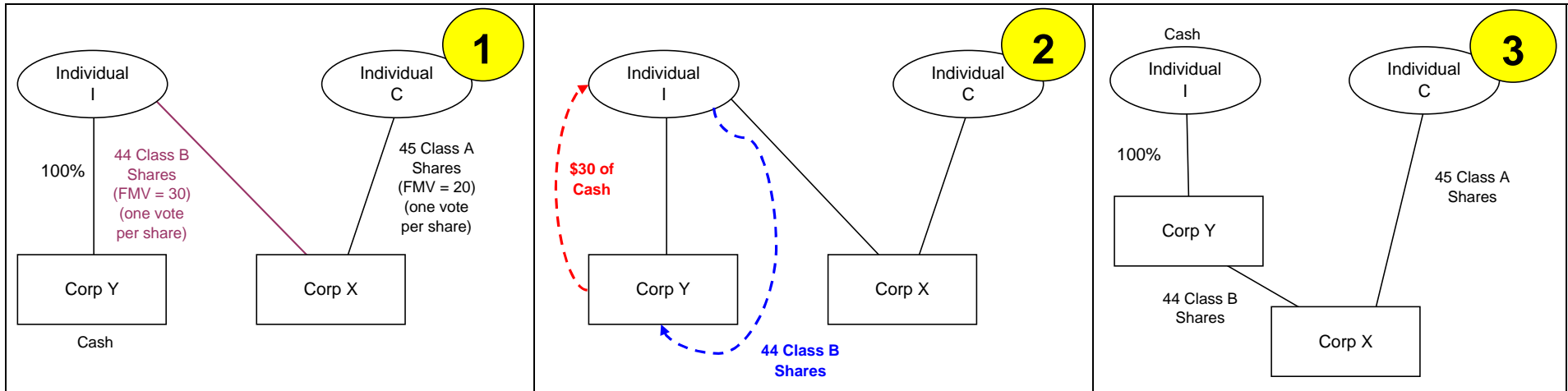


Initial Structure

Sale of Stock

Ending Point



I owned all of the outstanding stock of corporation Y. I and C, a person not related to I, together owned all the outstanding stock of corporation X. I owned the X Class B stock (44 shares) and C owned the X Class A stock (45 shares). The fair market value of the 44 shares of X Class B stock held by I was 30x dollars, and the fair market value of the 45 shares of X Class A stock held by C was 20x dollars. Thus, I owned 60 percent (30/50) of the aggregate fair market value of the X stock outstanding. The Class A stock and the Class B stock each had one vote per share. Thus, I held less than 50 percent of the vote in X (44/89). The difference in value between the Class A stock and the Class B stock was due to differences in dividend and liquidation rights.

Y purchased I's X stock for 30x dollars cash, the stock's fair market value. I was in control of Y because I owned all of the outstanding Y stock immediately before the transaction. Because I owned stock in X possessing only 44 votes out of a total of 89 votes, I did not satisfy the voting power test of section 304(c)(1). The value test of section 304(c)(1) is determined in an aggregate manner, and I was in control of X because I owned 60 percent of the total value of the X stock outstanding. If, however, the value test were determined in a class-by-class manner, then I was not in control of X because I did not own any of the X Class A stock.

The fact that the statute bases the value test of section 304(c)(1) on the total value of shares implies that the test is applied in an aggregate manner rather than in a class-by-class manner. See Rev. Rul. 87-88, 1987-2 C.B. 81 (concluding that if a corporation has more than one class of common stock outstanding, the provisions of section 302(b)(2)(C) are applied in an aggregate manner and not in a class-by-class manner). Moreover, construing the value test as involving a class-by-class approach would render that test meaningless. Under such a construction, the value test could be satisfied only when the voting power test is also satisfied. Thus, control would exist if, and only if, the voting power test is met. Therefore, for purposes of section 304(c)(1), the determination of the total value of the X stock must be made by aggregating all of the outstanding classes of X stock.

Because I owned X Class B stock having a value of at least 50 percent of the total value of all of the outstanding X stock, I am in control of X for purposes of section 304(c)(1), even though I owned none of the X Class A stock. Under section 304(a) and (b), the 30x dollars I received from Y is treated as a distribution in redemption of stock in Y, and this redemption is tested under section 302(b) by reference to the stock of X. Under sections 304(b)(1) and 318(a)(2)(C), I's equity interest in X is not decreased and, therefore, paragraphs (1), (2), and (3) of section 302(b) do not apply. Accordingly, this deemed redemption is described in section 302(d), and not section 302(a).