



A, an individual, who owns all of the stock of X corporation, purchased all of the stock of Y corporation for 250x dollars. 200x dollars of the purchase price was borrowed by A from a bank. Subsequently, A transferred the Y stock to X in return for the assumption by X of A's liability to the bank in the amount of 200x dollars and additional X stock. The assumption of the liability by X relieved A of all liability thereon. At the time of the transfer, the Y stock had a fair market value of 400x dollars and an adjusted basis in the hands of A of 250x dollars. During the time that A held the Y stock, A exercised all the rights of ownership of the stock including managing the operations of Y and receiving dividends therefrom. At the time of the transfer of the Y stock to X, X had earnings and profits in excess of 200x dollars.

Section 304(a)(1) is applicable, and not section 357(a), to that portion of the transaction in which the liability is assumed. Section 351(a) will be applied to that portion of the transaction in which stock of X is received. Since section 304(a)(1) is applicable, the assumption by X of A's liability to the bank in the amount of 200x dollars is treated as a distribution in redemption of the X stock subject to the provisions of section 302.