4 T.C. 820 (1945)

Distributions made by a corporation during the process of liquidation are treated as distributions in partial liquidation under Section 115(i) of the Revenue Acts of 1934, 1936, and 1938, and are includible in the recipient's income under Section 115(c) of those acts.

Summary

The petitioner received distributions from a company during its liquidation between 1935 and 1938 and argued that these distributions should be treated as distributions from capital under Section 115(d) of the Revenue Acts. The Commissioner argued that the distributions were part of a series in complete cancellation or redemption of the company's stock, thus qualifying as distributions in partial liquidation under Section 115(i) and taxable under Section 115(c). The Tax Court held that the distributions were indeed part of a liquidation process and thus taxable as distributions in partial liquidation, regardless of whether stock certificates were surrendered or canceled at the time of distribution.

Facts

- The company's primary purpose, as stated in its articles of incorporation, was to liquidate the assets of the Bankers Joint Stock Land Bank of Milwaukee, Wisconsin.
- From 1932 to 1938, the company actively disposed of these assets, converting them into cash for distribution to its stockholders.
- The company's assets decreased from approximately $13 million in 1932 to about $4.5 million in 1938.
- The company made distributions of the sums realized from converting its assets into cash; most were designated as "liquidating dividends."
- No shares were surrendered or canceled when these distributions were made, nor were there endorsements of the distributions on the stock certificates.

Procedural History

The Commissioner determined that the distributions received by the petitioner were includible in his income as amounts distributed in partial liquidation. The petitioner appealed to the Tax Court, arguing that the distributions should be treated as distributions from capital. The Tax Court reviewed the case and upheld the Commissioner's determination.

Issue(s)

1. Whether the distributions received by the petitioner from the company during the taxable years 1935 to 1938 were distributions in partial liquidation within the meaning of Section 115(i) of the Revenue Acts of 1934, 1936, and 1938.
2. Whether these distributions were includible in the petitioner's income in the

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full amounts under Section 115(c) of those acts.

Holding

1. Yes, because the distributions were "one of a series of distributions in complete cancellation or redemption" of the company's stock, made during a period when the company was actively liquidating its assets.
2. Yes, because distributions in partial liquidation are treated as in part or full payment in exchange for stock, and the gains are recognized and included in income under Section 115(c).

Court's Reasoning

The Court reasoned that the company was in the process of liquidation during the period in which the distributions were made, as evidenced by its stated purpose and continuous efforts to dispose of assets and convert them into cash for distribution. The Court cited *T. T. Word Supply Co., 41 B. T. A. 965, 980*, stating that liquidation involves winding up affairs by realizing upon assets, paying debts, and appropriating profits/losses, requiring a manifest intention to liquidate, a continuing purpose to terminate affairs, and activities directed thereto. The Court noted that the company's actions met these requirements. The Court also emphasized that the character of the distributions should be determined based on the circumstances at the time they were made. "Each of the distributions here in question seems to have been one of a series of distributions intended to be in complete cancellation or redemption of all of the stock of the corporation when the series was completed." Even though shares were not surrendered or cancelled, and even if the company altered its course later, the tax character of previous liquidating distributions remained unchanged.

Practical Implications

This case clarifies the tax treatment of corporate distributions made during the process of liquidation. It highlights that the intent and actions of the corporation during the distribution period are key factors in determining whether the distributions qualify as partial liquidation. Legal practitioners must carefully analyze the corporation's activities, stated purposes, and distribution patterns to accurately classify these distributions for tax purposes. The case confirms that the absence of contemporaneous share surrender or cancellation does not preclude a distribution from being treated as a distribution in partial liquidation. This ruling has been applied in subsequent cases to determine the tax consequences of distributions made during corporate reorganizations and dissolutions.

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