Lansing Broadcasting Co. v. Commissioner, 52 T. C. 299 (1969)

Liquidating distributions are considered 'exchanges of stock' under IRC § 1372(e)(5), potentially terminating a corporation's Subchapter S election if they exceed 20% of gross receipts.

Summary

Lansing Broadcasting Co. received a liquidating distribution from Chief Pontiac Broadcasting Co. , which it argued should not be considered 'personal holding company income' under IRC § 1372(e)(5). The Tax Court held that such distributions are treated as 'exchanges of stock' under IRC § 331(a)(1), and thus, when combined with other passive income, exceeded 20% of Lansing's gross receipts, terminating its Subchapter S election for 1962. The court emphasized the consistency of this treatment with the purpose of Subchapter S to limit its application to corporations with significant operating income.

Facts

Lansing Broadcasting Co. owned 53. 625% of Chief Pontiac Broadcasting Co. 's stock. In 1962, Chief Pontiac sold its assets and distributed the proceeds to shareholders in complete liquidation. Lansing received distributions totaling $233,404. 22 over several dates in 1962 and 1963. Lansing had elected Subchapter S status in 1958 and reported the distribution as long-term capital gain. The IRS argued that this gain, along with other passive income, exceeded 20% of Lansing's gross receipts, terminating its Subchapter S election.

Procedural History

The Commissioner of Internal Revenue determined deficiencies in Lansing's income taxes for 1962-1964 due to the termination of its Subchapter S election. Lansing petitioned the Tax Court for a redetermination of these deficiencies. The Tax Court upheld the Commissioner's determination, ruling that the liquidating distribution constituted an 'exchange of stock' under IRC § 1372(e)(5), leading to the termination of Lansing's Subchapter S election effective January 1, 1962.

Issue(s)

1. Whether the liquidating distribution received by Lansing Broadcasting Co. from Chief Pontiac Broadcasting Co. constitutes 'gross receipts derived from sales or exchanges of stock or securities' under IRC § 1372(e)(5).

Holding

1. Yes, because under IRC § 331(a)(1), liquidating distributions are treated as amounts received in exchange for stock, and thus fall within the definition of 'exchanges of stock' in IRC § 1372(e)(5).

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Court’s Reasoning

The court relied on IRC § 331(a)(1), which treats liquidating distributions as payments in exchange for stock. This interpretation aligns with the legislative purpose of Subchapter S, which aims to limit its application to corporations with significant operating income rather than passive investment income. The court found no inconsistency between § 331(a)(1) and Subchapter S, emphasizing that the taxable income of an electing corporation must be computed as if no election had been made. The court also noted the legislative history and purpose of § 1372(e)(5) to restrict Subchapter S to corporations with substantial operating income. The court rejected Lansing’s argument that the regulation under § 1. 543-1(b)(5)(i) should limit the interpretation of ‘exchanges of stock’ to exclude liquidating distributions, finding the statutory language broad enough to include such distributions.

Practical Implications

This decision impacts how liquidating distributions are treated for Subchapter S corporations, requiring careful consideration of such distributions in maintaining Subchapter S status. Practitioners must account for all passive income, including liquidating distributions, when calculating gross receipts under § 1372(e)(5). The ruling underscores the importance of aligning corporate activities with the operational focus intended by Subchapter S. Subsequent cases have followed this precedent, reinforcing the inclusion of liquidating distributions as ‘exchanges of stock’ for Subchapter S termination analysis.

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