Fisher v. Commissioner, 62 T. C. 73 (1974)

Stock received in lieu of a cash dividend in a reorganization transaction is taxable as a dividend under section 301.

Summary

In Fisher v. Commissioner, the Tax Court ruled that 1,614 shares of Ashland stock received by J. Robert Fisher were taxable as a dividend under section 301. Fisher had agreed to exchange his stock in Fisher Chemical Co. for 168,800 shares of Ashland stock but modified the agreement to receive additional shares instead of a cash dividend. The court found this modification constituted a separate transaction from the reorganization, thus the additional shares were not part of the tax-free exchange but were a taxable dividend.

Facts

J. Robert Fisher agreed to exchange his 100 shares of Fisher Chemical Co. for 168,800 shares of Ashland Oil & Refining Co. ‘s voting preferred stock on November 18, 1966. The agreement initially allowed for dividends to accrue after December 15, 1966. However, due to concerns over the tax implications, the agreement was amended on December 9, 1966, to provide that if the closing occurred after December 15, Fisher would receive 1,614 additional shares instead of a cash dividend for one quarter. The closing took place on December 16, 1966, and Fisher received a total of 170,414 shares.

Procedural History

The Commissioner of Internal Revenue determined deficiencies in Fisher’s 1966 and 1967 federal income taxes, asserting that the 1,614 additional shares constituted a taxable dividend. Fisher petitioned the Tax Court for a redetermination of the deficiencies. The parties agreed that if the additional shares were taxable, the tax would apply to 1967. The Tax Court held that the additional shares were taxable as a dividend.

Issue(s)

1. Whether the 1,614 shares of Ashland stock received by Fisher were part of the consideration for the reorganization under section 368(a)(1)(B) or a separate transaction taxable as a dividend under section 301.

Holding

1. No, because the additional shares were received in lieu of a cash dividend and constituted a separate transaction from the reorganization, making them taxable as a dividend under section 301.

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Court’s Reasoning

The court analyzed the modification to the original agreement, concluding it constituted a separate transaction from the reorganization. The court applied sections 305(a) and 305(b)(2), noting that Fisher effectively elected to receive stock instead of a cash dividend. The court emphasized that the policy of the tax law is to prevent the transformation of ordinary income into part of a tax-free transaction. The court distinguished this case from others involving recapitalizations or redemptions, where stock received in lieu of dividends was not treated as taxable, because here the additional shares were not part of the original reorganization plan but a subsequent modification. The court rejected Fisher’s argument that the additional shares should be treated as part of the tax-free exchange, as they were received in exchange for surrendering his right to a cash dividend.

Practical Implications

This decision impacts how stock received in lieu of dividends in reorganization transactions is treated for tax purposes. It clarifies that such stock is not automatically part of a tax-free exchange but may be taxable as a dividend if it represents a separate transaction. Practitioners must carefully structure reorganization agreements to avoid unintended tax consequences. The ruling reinforces the principle that attempts to convert ordinary income into capital gains or part of a tax-free transaction will be scrutinized by the IRS. Subsequent cases have cited Fisher when analyzing the tax treatment of stock distributions in corporate reorganizations.

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