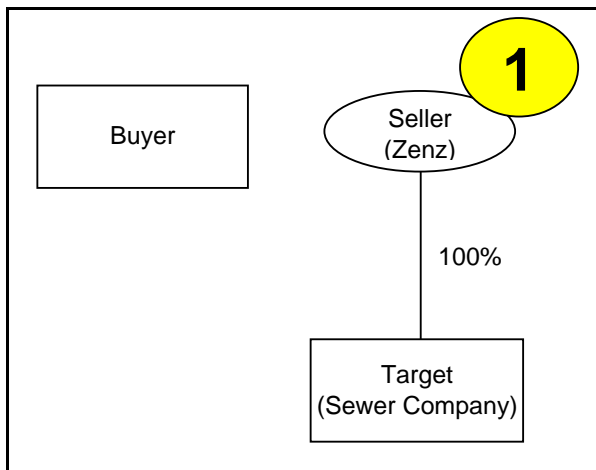


**Zenz v. Quinlivan**  
**213 F.2d 914 (6th Cir. 1954)**

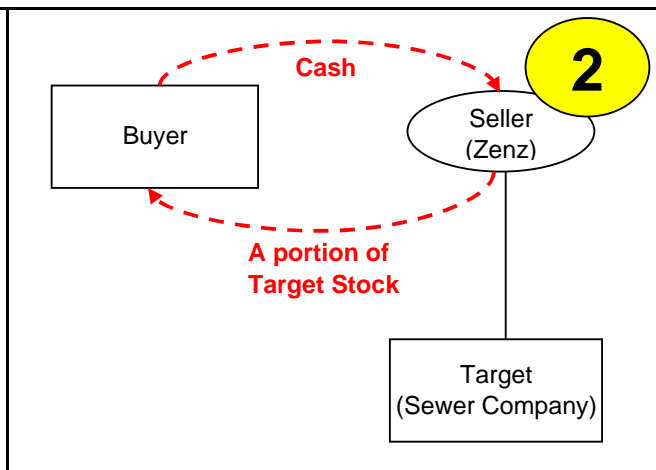
**Stock Disposition -  
 Part Sale & Part Redemption**

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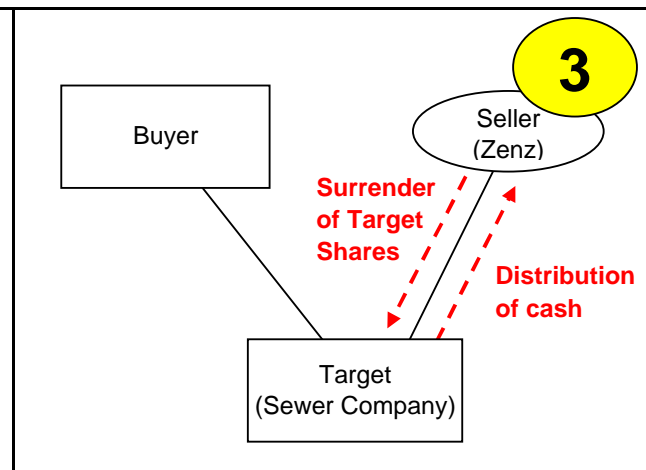
**Initial Structure**



**Stock Acquisition**



**Stock Redemption (3 Weeks Later)**



The issue in the case was whether Zenz should receive capital gain treatment on the redemption (step 3 above) or whether the distribution should be treated as dividend income. The District Court had held that it should be dividend. The Sixth Circuit reversed, stating:

The basic precept underlying the capital gains theory of taxation as distinguished from ordinary income tax is the concept that a person who has developed an enterprise in which earnings have been accumulated over a period of years should not be required to expend the ordinary income tax rate in the one year when he withdraws from his enterprise and realizes his gain. . . .

We cannot concur with the legal proposition enunciated by the District Court that a corporate distribution can be essentially equivalent to a taxable dividend even though that distribution extinguishes the shareholder's interest in the corporation. To the contrary, we are satisfied that where the taxpayer effects a redemption which completely extinguishes the taxpayer's interest in the corporation, and does not retain any beneficial interest whatever, that such transaction is not the equivalent of the distribution of a taxable dividend as to him.

In Rev. Rul. 55-745, the IRS announced that for purposes of section 302(b)(3), it would follow the decision in Zenz. See also Rev. Rul. 75-447 in which the Zenz rationale was applied to section 302(b)(2). At the time of Zenz's transaction, the redemption was able to strip out 100% of Target's E&P. However, section 312(n)(7) now provides for a proportionate reduction in E&P.

**Ending Point**

