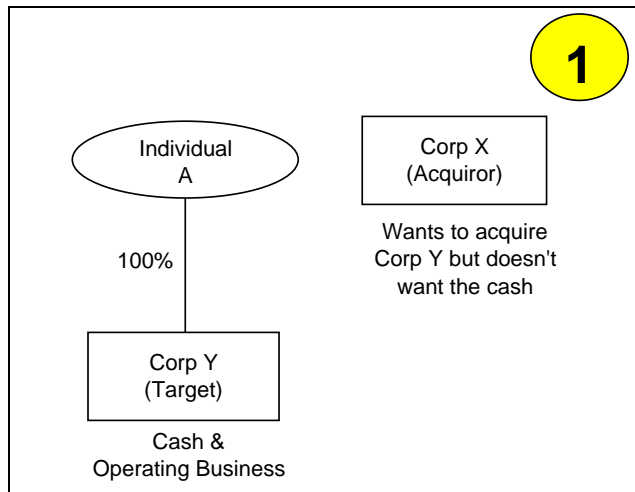
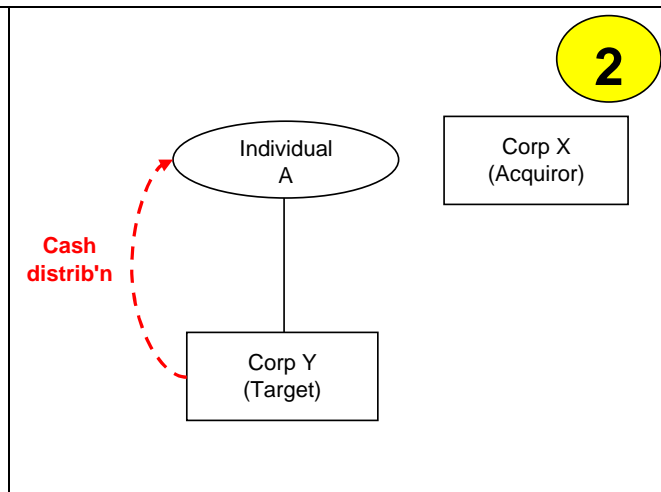


**Pre-Sale Distribution: 301 Distribution,
Liquidation Proceeds, or Sales Proceeds**

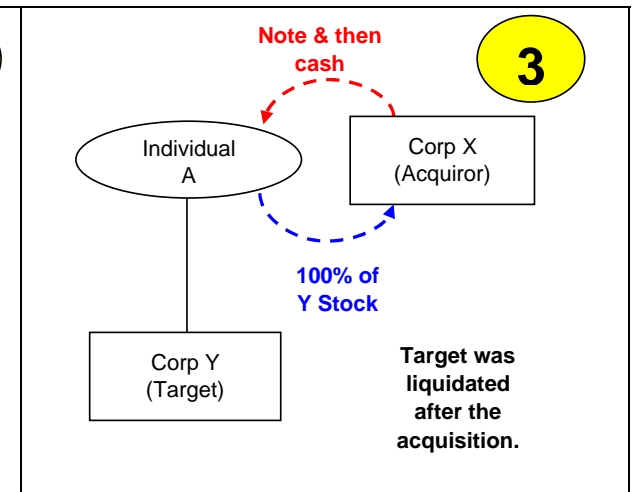
Initial Structure



Distribution (November 1, 1974)



Stock Acquisition (November 2, 1974)



A, an individual, owned all of the stock of Y corporation. X corporation entered into negotiations with A to buy for cash all of the stock of Y. In negotiating the purchase price of the Y stock, X stated that it did not want to purchase, in effect, the large amount of cash held by Y. A then offered to have Y distribute the cash to A with the understanding that X would then buy the Y stock. On November 1, 1974, Y declared and paid a cash dividend of the unwanted cash to A who surrendered no stock. At that time, X was under no legal obligation to purchase A's Y stock. Y had earnings and profits in excess of the amount of the distribution. On November 2, 1974, A and X executed an agreement for the sale of the Y stock to X for a fixed dollar amount. Pursuant to the agreement X acquired all of A's stock in Y and designated new officers and directors of Y who adopted a formal plan of complete liquidation of Y pursuant to which all of the property of Y was distributed to X in complete cancellation and redemption of the stock of Y. After the liquidation of Y, X paid A the agreed price of the Y stock with funds borrowed from an unrelated lender.

The issue was whether (a) the cash distribution to A was a distribution to which section 301 applies, or (b) the cash distribution was received by A in complete liquidation of Y so that the amounts would be treated as a full payment in exchange for Y stock under section 331(a)(1), or (c) the cash distribution was part of the purchase price paid by X to A for the Y stock and thus treated under sections 1001 and 1002 as in part payment for the Y stock.

The payment of the dividend did not reduce X's obligation to pay the agreed upon purchase price. Thus, the distribution was not considered a part of the purchase price paid by X to A for the Y stock. Moreover, since A was not the owner of any Y stock on the date of the adoption of the plan of liquidation of Y, the distribution was not considered as received by A in complete liquidation of Y. The distribution was taxable to A under section 301. Compare *Waterman Steamship Corporation v. Commissioner*, 430 F.2d 1185 (5th Cir. 1970), cert. denied 401 U.S. 939 (1970) and *Casner v. Commissioner*, 450 F.2d 379 (5th Cir. 1977).

Ending Point

