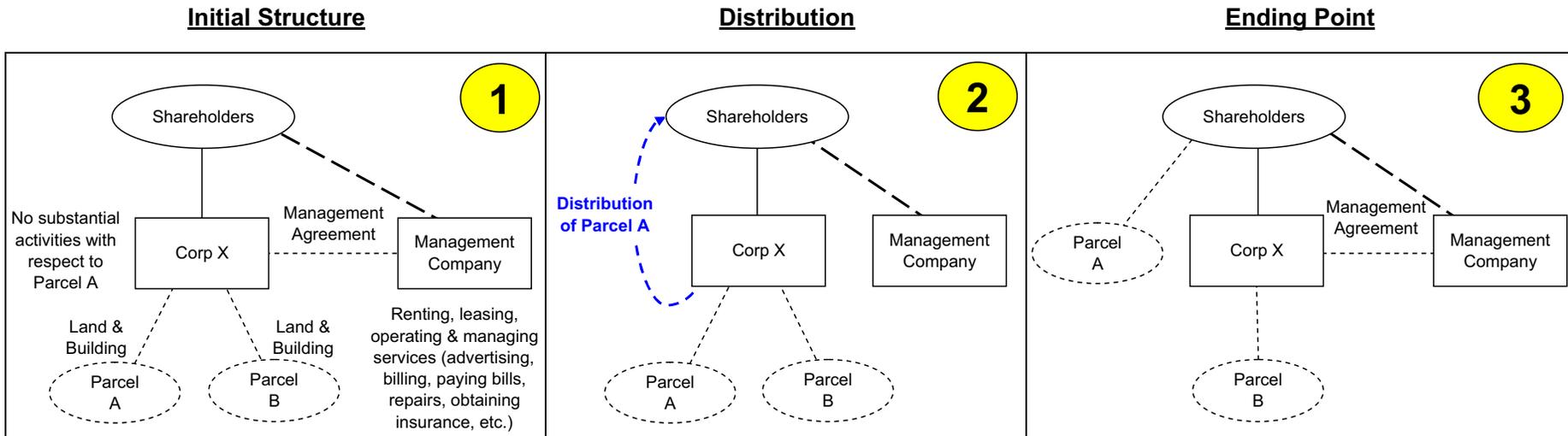


No Partial Liquidation on Distribution of Real Estate



X corporation owned two parcels of real property (parcel A and parcel B), each consisting of land and a building thereon. X has only one class of stock outstanding. Both parcel A and parcel B are leased. Under both leases, the lessee is required to pay all real estate taxes and similar assessments and is responsible for all interior maintenance and the operation of the building's equipment. Both parcel A and parcel B are the subject of a management agreement whereby another corporation, wholly owned by one of X's shareholders, provides renting, leasing, operating, and managing services. These services include advertising, billing, paying bills (including mortgages), taking care of all phases of repairs and alterations (such as hiring employees and purchasing supplies), obtaining insurance, and enforcing the terms of all contracts.

X distributed parcel A pro rata to its shareholders in redemption of a part of their stock. X had accumulated earnings and profits in excess of the fair market value of parcel A. The issue in the ruling was whether a genuine contraction of X's business results since X itself engaged in no substantial activities with respect to parcel A, or with respect to parcel B, which is retained by X. Section 331(a)(2) provided that amounts distributed in partial liquidation of a corporation (as defined in section 346) shall be treated as in part or full payment in exchange for the stock. Section 346(a)(2) provided, in part, that a distribution shall be treated as in partial liquidation of a corporation if it is not essentially equivalent to a dividend, is in redemption of a part of the stock of the corporation pursuant to a plan, and occurs within the taxable year in which the plan is adopted or within the succeeding taxable year. [partial liquidations are now only relevant for purposes of section 302(b)(4)]

Reg. § 1.346-1(a) states that a distribution that will qualify as a distribution in partial liquidation of a corporation under section 346(a)(2) is one that results from a genuine contraction of the corporate business, such as the distribution of unused insurance proceeds recovered as a result of a fire which destroyed part of the business causing a cessation of a part of its activities. For purposes of finding that a genuine contraction of a business has occurred for purposes of section 346(a)(2), there must be a substantial reduction of activities performed by the corporation making the distribution. In the instant case, there was no substantial reduction in activities because X under its lease and its management contract has no substantial activities to perform. Thus, the distribution does not constitute a genuine contraction of X's business within the meaning of section 346(a)(2).