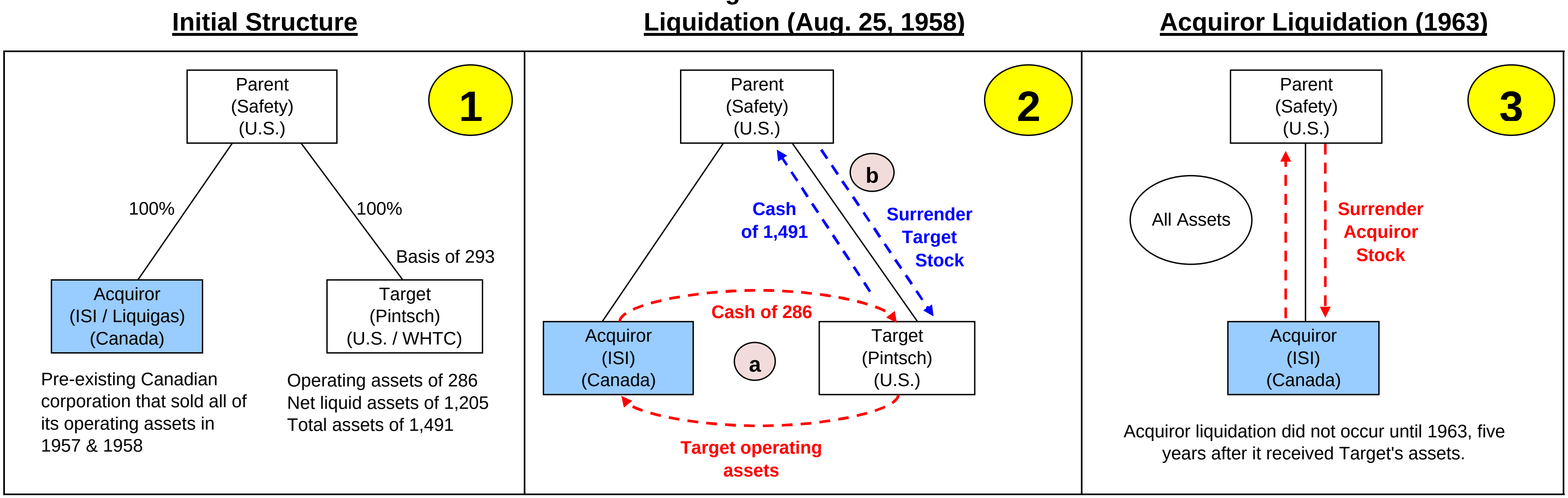
American Manufacturing Co. v. Commissioner
55 T.C. 204 (1970)

Outbound D Reorganization



The Commissioner argued that the full 1,491 received by Parent should be included in income as a dividend under sections 301(a) and 316(a), in part from Target and in part from Acquiror. In the alternative, the Commissioner argued that the 1,491 was received as part of a reorganization under section 368(a)(1)(D) and that the gain realized should be taxable under section 356(a)(2) as a dividend. The Taxpayer argued that the 1,491 was a nontaxable distribution in a section 332 liquidation of Target.

Prior cases dealing with liquidation-reincorporation have never considered the application of the reorganization provisions and the dividend provisions to transactions where section 332 is purportedly involved. In determining whether a reorganization has occurred in the liquidation-reincorporation area, "the situation must be considered as it existed at the beginning and end of a series of steps." The Tax Court held that the purported section 332 liquidation was a step in a D reorganization and that the distribution was "in connection with" the reorganization. The 1,491 therefore was not a section 301 distribution, but should be recharacterized as a dividend to the extent provided by section 356(a)(2).

In similar circumstances in Davant, the Fifth Circuit rationalized that since there was a complete identity of shareholders, the earnings and profits of both Target and Acquiror should be considered in determining the amount of distributions taxable as a dividend under section 356(a)(2). Here, the Tax Court held that only Target's earnings and profits should be considered in determining the amount of gain to be recharacterized as a dividend. The gain on the transaction was 1,198 (1,491 - 293), and Target's earnings and profits amounted to 1,235. Thus, the entire gain is taxable as a dividend under section 356(a)(2). The Tax Court also held that gain must be recognized by Target on its outbound transfer of assets under sections 367(a) and 361 because Target did not receive an advance ruling on the transfer.