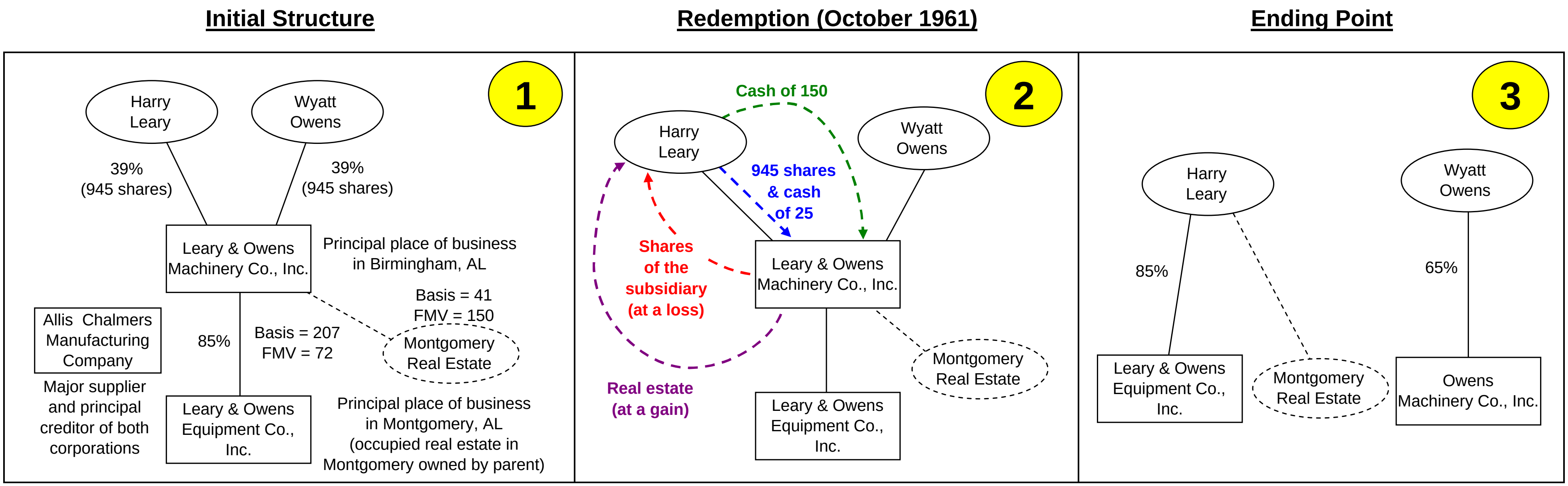
**Owens Machinery Co. v. Commissioner**
**54 T.C. 877 (1970)**

# In-Kind Redemption Not a Section 311 Distribution






Owens Machinery Company, Inc., ("OMC") was organized under the laws of the State of Alabama, on March 22, 1945, as Leary & Owens Machinery Company, Inc. On March 1, 1962 the name of OMC was changed to Owens Machinery Company, Inc. The principal business activity of OMC was the selling, servicing and repairing of heavy construction equipment. The principal supplier of OMC was Allis Chalmers Manufacturing Company. As of January 1, 1961 the outstanding capital stock of OMC consisted of 2,400 shares of common stock with the par value of $100 per share. On such date Harry J. Leary, president, and Wyatt Owens, vice president, each owned 945 shares of OMC's stock.

OMC owned 85% of a subsidiary corporation, Leary & Owens Equipment Company, Inc. The subsidiary engaged in substantially the same business as OMC in a different location and also occupied real estate owned by OMC. During 1961 certain differences arose between Harry J. Leary and Wyatt Owens, the principal stockholders of OMC. An agreement was entered into on October 18, 1961 between OMC and Mr. Leary which provided that OMC would transfer the stock of its subsidiary to Mr. Leary in exchange for 945 shares of its stock plus $25,000, and OMC would transfer the occupied real property to Mr. Leary for the sum of $150,000.

The fair market value of OMC's stock, as of October 18, 1961, was $50 per share and OMC's basis for the 85% of Leary & Owens Equipment Company, Inc. was $206,960. The basis of the Montgomery property was $40,763.17. The IRS argued to treat the exchange of the subsidiary's stock as two separate transactions, namely, a sale in part of the subsidiary's stock for $25,000 and a distribution by OMC with respect to its stock under section 311 as to the balance of the subsidiary's stock. Unless the transaction was fragmented the IRS impliedly recognized that the transaction could not be characterized as a distribution by OMC "with respect to its stock."

The Tax Court stated that it knew of no rule which would warrant "fragmenting" such transaction to treat it as an exchange for stock of part of the stock and a sale for cash of the balance. It must be treated as a single exchange of stock for stock and cash. The cash payment was a significant element of the total consideration received by OMC, namely, $25,000 out of a total consideration of $72,250. It was not a situation in which a relatively insignificant cash adjustment is made to avoid the issuance of fractional shares. The payment of $25,000 was a necessary element of the transaction. Since the exchange herein involved included both OMC's stock and cash, it did not constitute a distribution by OMC with respect to its stock within the meaning of section 311 .