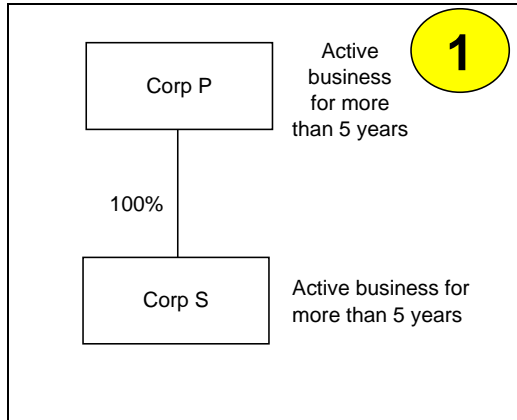


**Revenue Ruling 75-223
Situation 2**

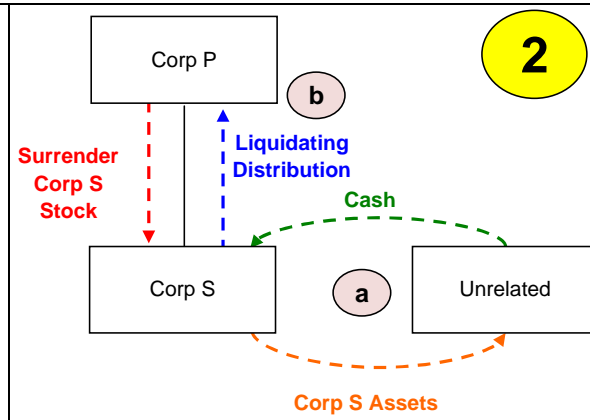
**Partial Liquidation With Sale
of Subsidiary's Assets**

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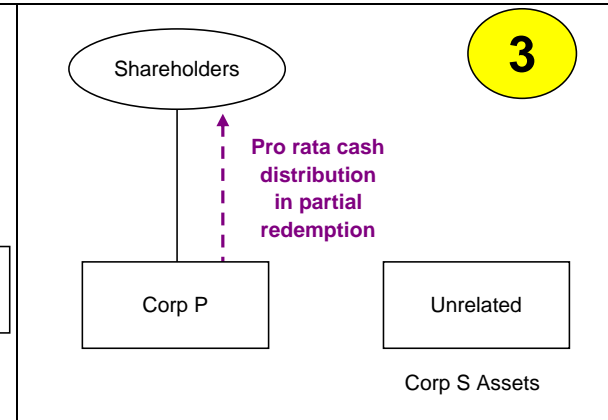
Initial Structure



Sale of Assets & Liquidation



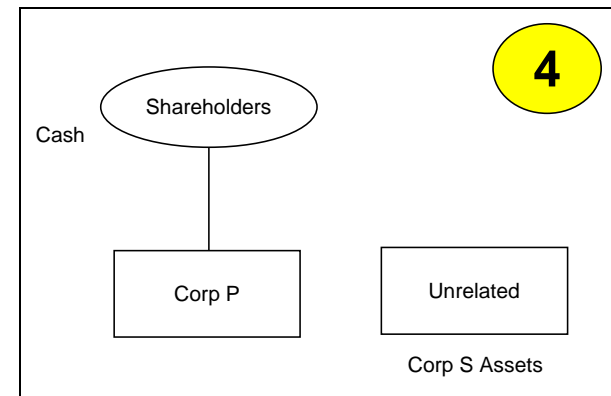
Distribution



Parent corporation P, and its wholly owned subsidiary corporation, S, have each been engaged in the active conduct of a trade or business for a period of more than five years and P has held all the stock of S throughout that period. A distribution by P of the assets used by S, or the proceeds of a sale of those assets, would have qualified as a partial liquidation under section 346(a)(2) if S's business activities had been conducted directly by P, for example, through a division, rather than through a subsidiary. S sells all its assets to an unrelated party and distributes the proceeds to P in complete liquidation under section 332. Pursuant to a plan, P distributes the sale proceeds pro rata to its shareholders in redemption of part of their stock in P. The distribution takes place within one year from the date of the adoption of the plan.

The issue presented is whether, and to what extent, the fact that a corporation has conducted a portion of its business activities through a subsidiary rather than directly precludes the application of section 346(a)(2). The business activities of a subsidiary are not generally considered to be business activities of its parent corporation. Under normal circumstances, the mere fact that one corporation owns all the stock of another corporation is not sufficient to attribute the business of the subsidiary to the parent corporation.

Ending Point



Under section 381, however, a parent corporation that liquidates a subsidiary under section 332 (when section 334(b)(2) does not apply) inherits, among other attributes, the earnings and profits, net operating loss carryovers, and accounting methods of the liquidated subsidiary. These attributes pass to the parent corporation whether the liquidating distribution consists of the operating assets of the subsidiary or the proceeds of a sale of those assets. Section 381, in effect, integrates the past business results of the subsidiary (as represented by its earnings and profits, net operating loss carryovers, etc.) with those of the parent corporation. For most practical purposes, the parent corporation, after the liquidation of the subsidiary, is viewed as if it had always operated the business of the liquidated subsidiary. Consequently, there is no meaningful distinction, for purposes of section 346(a)(2), between a corporation that distributes the assets of a division, or the proceeds of a sale of those assets, and a parent corporation that distributes assets of a subsidiary, or the proceeds of a sale of such assets, received from the subsidiary in a liquidation governed by sections 332 and 381. The fact that the distribution was attributable to assets that were used by a subsidiary rather than directly by the parent will not prevent the distribution from qualifying as a "genuine contraction of the corporate business" of the parent within the meaning of Reg. 1.346-1(a)(2).