2 T.C. 531 (1943)

A corporation cannot avoid tax liability on the sale of its assets by formally distributing the assets to its shareholders, who then complete the sale that the corporation had already negotiated.

Summary

Court Holding Company orally agreed to sell its property. Before executing a written contract, the corporation's shareholders were advised that a corporate sale would trigger significant taxes. The corporation then distributed the property to its shareholders as a liquidating dividend, and the shareholders immediately sold the property to the same buyer under the same terms. The Tax Court held that the sale was, in substance, made by the corporation and that the corporation was liable for the tax on the gain. The court reasoned the liquidation was merely a step in an overall plan to avoid corporate taxes.

Facts

Court Holding Company (CHC) was a Florida corporation whose primary asset was an apartment building. The Millers, husband and wife, owned all of CHC's stock. CHC orally agreed to sell the apartment to the Fines for $54,500. Before a written sales agreement was finalized, CHC's attorney advised the Millers that the corporation would incur substantial income tax liability from the sale. To avoid this, CHC distributed the apartment building to the Millers as a liquidating dividend.

Procedural History

The Commissioner of Internal Revenue assessed deficiencies against Court Holding Company, arguing the sale was made by the corporation, not the shareholders. The Tax Court upheld the Commissioner's determination, finding that the liquidation was merely a step in a plan to avoid corporate taxes.

Issue(s)

Whether a sale of property, formally executed by shareholders after a corporate liquidation, should be treated as a sale by the corporation when the corporation had previously negotiated the sale and taken steps to complete it, all for the primary purpose of tax avoidance.

Holding

Yes, because the transfer of property from the corporation to the shareholders, followed by the sale, was merely a step in an overall plan to avoid corporate taxes; the substance of the transaction indicated that the corporation made the sale.

Court's Reasoning

The Tax Court applied the principle that the substance of a transaction, rather than its form, controls for tax purposes. The court emphasized that CHC had already negotiated the sale terms and even received a partial payment before the liquidation occurred. The court found that "the Millers were carrying out the agreement made by the corporation and not an agreement made by themselves individually." Citing *Gregory v. Helvering*, 293 U.S. 465 (1935), the court stated that formal devices, such as the liquidation, undertaken solely for tax avoidance, "may not be given effect." The court distinguished *Falcon Co., 41 B.T.A. 1128* a case where the corporation had not entered any contract before liquidation.

The court stated:

"Consummation of the oral agreement was the substantive purpose. The resolutions of February 23 and the consequent transfer of title to the Millers were unnecessary to its accomplishment, or to the accomplishment of any purpose save that of tax avoidance. They were formal devices to which resort was had only in the attempt to make the transaction appear to be other than what it was. As such, they may not be given effect. *Gregory v. Helvering*, 293 U.S. 465; *Minnesota Tea Co. v. Helvering*, 302 U.S. 609; *Griffiths v. Helvering*, 308 U.S. 355."

Practical Implications

Court Holding Co. establishes the principle that a corporation cannot use a liquidating distribution to shareholders as a means to avoid taxes on a sale the corporation had already arranged. This case is frequently cited in tax law to support the IRS's authority to disregard the form of a transaction when it is clear that the substance is a corporate sale. This decision highlights the importance of considering the economic realities of a transaction, not just the legal formalities. Later cases have distinguished *Court Holding Co.* when the shareholders genuinely conducted independent negotiations after receiving the distributed assets. However, the case remains a significant precedent for applying the step-transaction doctrine to prevent tax avoidance schemes involving corporate liquidations and sales.