2 T.C. 586 (1943)

Income derived from contracts assigned to a taxpayer who owns substantially all the stock of a corporation that is party to those contracts is taxable to the taxpayer, even if the income is subsequently assigned to a third party.

Summary

Ronald Mattox, owning almost all the stock of The Ronald Mattox Company, assigned income from contracts with Alvin H. Huth, Inc. and Richard V. Reineking to his wife. The Commissioner of Internal Revenue determined that this income was taxable to Mattox despite the assignments. The Tax Court agreed with the Commissioner, holding that the payments, in effect, were corporate distributions to Mattox, taxable to him because of his ownership of the corporation. The court reasoned that Mattox's control over the corporation meant the income was essentially his before the assignment.

Facts

Ronald Mattox, a certified public accountant, organized The Ronald Mattox Company in 1927. He owned 93-95 of the 100 shares of the company's stock. The company engaged in fraternity and sorority accounting. In 1936, the company contracted with Alvin H. Huth, Inc., assigning its accounting contracts in Lafayette and West Lafayette, Indiana, to Huth in exchange for a percentage of Huth's net income. In 1938, Mattox and the company entered into a contract with Richard V. Reineking, assigning fraternity and sorority accounting contracts in Bloomington and Green Castle, Indiana, to Reineking for a percentage of net income. Mattox then assigned the income streams from both the Huth and Reineking contracts to his wife, Louise Mattox.

Procedural History

The Commissioner of Internal Revenue determined deficiencies in Mattox's income tax for fiscal years 1938, 1939, and 1940, adding income paid to Louise Mattox under the assignments to his taxable income. Mattox contested this adjustment, arguing the income was properly taxable to his wife. The Tax Court upheld the Commissioner's determination, finding the income taxable to Ronald Mattox.

Issue(s)

Whether income from contracts payable to the petitioner, which he assigned to his wife, is taxable to the petitioner when the contracts were initially derived from a corporation in which the petitioner owns substantially all the stock.

Holding

Yes, because the payments made to Mattox under the contracts and then passed to

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his wife were effectively corporate distributions and are taxable to him as the controlling shareholder.

Court’s Reasoning

The court reasoned that the payments from Huth and Reineking were essentially payments for the corporation’s property and business. Because Mattox owned substantially all the stock, the payments were, in substance, distributions from the corporation to him. The court emphasized that Mattox treated the corporation as his alter ego. Even though the contracts stipulated payment to Mattox individually, the court looked to the substance of the transaction. The court distinguished this case from cases involving assignments of trust income, noting that Mattox retained ownership of the corporate shares, thereby maintaining control over the income-producing asset. As the court noted, the payments were being made “because he was substantially the owner of all the stock of the corporation.”

Practical Implications

This case illustrates the importance of the assignment of income doctrine and its intersection with corporate distributions. It reinforces that taxpayers cannot avoid tax liability by assigning income derived from property they control, particularly when that property is a closely held corporation. This case teaches that courts will look beyond the form of a transaction to its substance, especially when a taxpayer attempts to shift income to a related party while retaining control over the underlying income-producing asset. Legal practitioners must carefully analyze similar arrangements to determine if the assignment has economic substance or is merely a tax avoidance strategy. Subsequent cases have cited *Mattox* for the principle that assignments of income from closely held corporations may be disregarded for tax purposes when the assignor retains control over the corporation.

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