3 T.C. 1076 (1944)

A corporation that liquidates its assets and ceases operations de facto, even if its charter technically remains active, must file a tax return for the fractional part of the year it was operational, with income annualized, but is not subject to a reduction in excess profits tax credit for capital reductions occurring at liquidation.

Summary

Kamin Chevrolet Co. liquidated its assets on June 30, 1940, but did not formally dissolve its corporate charter. The Commissioner of Internal Revenue treated the filed excess profits tax return as covering only January 1 to June 30, 1940, and annualized the income. The Commissioner also reduced the excess profits tax credit based on a net capital reduction resulting from the liquidation. The Tax Court held that the Commissioner correctly treated the return as covering a fractional year and annualizing income, but erred in reducing the excess profits credit, as the capital reduction occurred on the last day of the taxable period.

Facts

Kamin Chevrolet Co. was a Pennsylvania corporation. On June 24, 1940, the stockholders agreed to dissolve and wind up the company's affairs. On June 29, 1940, the corporation distributed all its assets to its stockholders, subject to liabilities. The corporation continued to technically exist under Pennsylvania law because its charter was not surrendered. After June 30, 1940, the corporation had no capital, income, or expenses.

Procedural History

Kamin Chevrolet Co. filed an excess profits tax return for the calendar year 1940. The Commissioner treated the return as one made for the period January 1 to June 30, 1940, and determined a deficiency. The taxpayer petitioned the Tax Court for a redetermination of the deficiency.

Issue(s)

1. Whether the Commissioner erred in interpreting the return filed as a return for a fractional part of the year 1940 and placing the same on an annual basis.
2. Whether the Commissioner erred in deducting for excess profits tax credit an amount representing 6 percent of the net capital reduction.

Holding

1. No, because the corporation underwent a *de facto* dissolution when it liquidated its assets and ceased operations, making a fractional-year return appropriate.
2. Yes, because the capital reduction occurred on the last day of the short taxable

year; therefore, there was no capital reduction during the taxable year that would justify reducing the excess profits tax credit.

Court's Reasoning

The court reasoned that even though Kamin Chevrolet Co. technically existed for the entire year, it had a *de facto* dissolution on June 30, 1940. The Court emphasized that the corporation was an "empty shell" after that date. Citing 26 U.S.C. § 48, the court stated that "Taxable year" includes a return made for a fractional part of a year. The court then applied 26 U.S.C. § 711 (a) (3), which provides that if the taxable year is a period of less than twelve months, the excess profits net income for such taxable year shall be placed on an annual basis. The court stated, "There appears to us to be no basis for the petitioner's contention… We think it clear that it was the intention of Congress to apply the excess profits credit for a 12-month period against the net income of a 12-month period." However, regarding the capital reduction, the court noted that § 711(a)(3)(A) states, "The tax shall be such part of the tax computed on such annual basis as the number of days in the short taxable year is of the number of days in the twelve months ending with the close of the short taxable year." The court concluded that because the capital reduction occurred precisely when the corporation was completely liquidated on June 30, there was no occasion to reduce the excess profits tax credit.

Practical Implications

This case provides guidance on how to treat the taxable year of a corporation that liquidates but does not formally dissolve. It clarifies that a *de facto* dissolution is sufficient to trigger fractional-year reporting requirements. It also highlights the importance of matching the timing of capital reductions with the correct taxable year when calculating excess profits tax credits. Subsequent cases will need to examine when a corporation's activities have ceased sufficiently to constitute a *de facto* dissolution. Tax advisors must consider the timing of liquidations carefully to optimize tax credits and minimize liabilities. This case illustrates a narrow interpretation that benefits taxpayers, as the excess profits credit was not reduced because the liquidation occurred at the end of the period.

