7 T.C. 211 (1946)

r
r

A subsidiary corporation formed for legitimate business purposes and conducting substantial business activity will be recognized as a separate entity for tax purposes, even if wholly owned by a parent corporation.

r
r

Summary

r

Rhode Island Hospital Trust Company (the petitioner) formed Rimnik Corporation as a subsidiary to manage and dispose of foreclosed real estate. Rimnik bought properties from the petitioner and sustained operating losses. In 1941, Rimnik purchased and retired shares of its stock held by the petitioner. The Commissioner argued that Rimnik was a sham and its separate entity should be disregarded, thus disallowing the petitioner's claimed loss on the stock retirement. The Tax Court held that Rimnik was a legitimate entity, and the petitioner could deduct the loss. The court also held the liquidation was not pre-planned, therefore Section 112(b)(6) did not apply.

r
r

Facts

r

r

r

- Prior to 1932, the petitioner made mortgage loans secured by real estate.

  r

- Due to the depression, many loans defaulted, requiring foreclosure.

  r

- In 1932, Rimnik Corporation was formed as a subsidiary to acquire, manage, and dispose of foreclosed properties.

© 2025 SCOTUSreports.com. All rights reserved.

r

- The petitioner owned all of Rimnik’s stock.

r

- Rimnik purchased mortgages or properties from the petitioner, often at the face amount of the mortgage.

r

- Rimnik sustained substantial operating losses due to a falling real estate market.

r

- In 1941, Rimnik purchased and retired 805 shares of its stock held by the petitioner to reduce capitalization.

r

- In December 1944, the petitioner sold a portion of its Rimnik stock to an outside party.

r

- Shortly after, Rimnik was liquidated and dissolved.

r

r

r
r

Procedural History

r

The Commissioner of Internal Revenue determined a deficiency against the petitioner for the 1941 tax year, disallowing a claimed long-term capital loss from the stock retirement. The petitioner contested the disallowance in the Tax Court.

r
r

Issue(s)

© 2025 SCOTUSreports.com. All rights reserved.

r

r

r

1. Whether Rimnik Corporation was a mere sham whose separate corporate entity may be ignored for tax purposes.

   r

2. Whether the petitioner’s basis for gain or loss on the Rimnik stock was its original cost, adjusted for capital contributions and losses.

   r

3. Whether Section 112(b)(6) of the Internal Revenue Code (regarding non-recognition of gain or loss in complete liquidation of a subsidiary) applied to the 1941 stock retirement.

   r

r

r
r

Holding

r

r

r

1. No, because Rimnik was formed for a legitimate business purpose and conducted substantial business activity.

   r

2. Yes, because the petitioner’s cost was the proper basis, absent evidence that Rimnik paid inflated prices for assets.

   r

3. No, because there was no plan of complete liquidation at the time of the 1941 stock retirement.

© 2025 SCOTUSreports.com. All rights reserved.

r

r

r
r

Court’s Reasoning

r

r

r

- The court distinguished *Higgins v. Smith*, emphasizing that disregarding a corporate entity requires finding it to be a

© 2025 SCOTUSreports.com. All rights reserved.