12 T.C. 49 (1949)

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A foreign corporation is not considered to be ‘engaged in trade or business within the United States’ under Section 231(b) of the Internal Revenue Code if its U.S. activities are primarily clerical and routine, even if those activities are extensive and useful.

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Summary

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Scottish American Investment Co. and related entities challenged the Commissioner’s determination of income tax deficiencies, arguing they were resident foreign corporations engaged in trade or business within the U.S. The Tax Court ruled against the companies, finding that despite maintaining a U.S. office, their core investment decisions were made in Scotland, and the U.S. office primarily handled routine clerical tasks. Therefore, they were not considered to be ‘engaged in trade or business’ in the U.S. within the meaning of the relevant tax code.

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Facts

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The petitioners, investment trusts organized under British law with principal offices in Edinburgh, Scotland, invested funds for income. They established a U.S. office in Jersey City, New Jersey, managed by an assistant secretary who was a CPA. All decisions regarding securities purchases and sales and investment policies were made by the home offices in Scotland. The U.S. office maintained records, collected dividends, executed proxies, made reports to the home office, paid local expenses, and prepared tax returns. The assistant secretary had the authority to withdraw funds up to $5,000 per month. The reduction in dollar volume was due to the British government requisitioning securities.

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Procedural History

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The Commissioner determined deficiencies in the petitioners' income tax for 1942 and 1943. The petitioners challenged this determination in the Tax Court, arguing they were resident foreign corporations engaged in trade or business within the United States. The Tax Court previously addressed these companies under earlier Revenue Acts, finding they had an office or place of business in the U.S., but did not determine if they were engaged in business. The Supreme Court affirmed the finding that the taxpayers had "an office or place of business" in the US but didn't rule on if they were engaged in "trade or business".

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Issue(s)

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Whether, during 1942 and 1943, the petitioners were 'engaged in trade or business within the United States' under Section 231(b) of the Internal Revenue Code, as amended by the Revenue Act of 1942, thus qualifying them as resident foreign corporations for tax purposes.

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Holding

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No, because the petitioners' activities in the U.S. were primarily clerical and routine, and the key investment decisions were made in Scotland. The activities, though regular, didn't constitute carrying on a business within the United States as defined by the tax code.

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Court's Reasoning

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The court emphasized that the core business decisions regarding investments were made in Scotland. The activities of the U.S. office were largely routine and clerical, similar to functions previously performed by banks. The court noted the legislative intent behind the 1942 amendment to Section 231(b) was to narrow the scope of what constituted 'engaged in trade or business' and to prevent foreign corporations

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from easily qualifying as resident corporations merely by establishing a U.S. office. The court cited previous language used in opinions that the US office “was used for the regular transaction of business” and “performed vital functions in the taxpayers’ investment trust business.” However, the court reasoned that while the functions were regular, they do not “warrant the conclusion that the business of petitioners was carried on in the United States within the meaning of section 231(b) as qualified by section 211(b).” The court distinguished the case from others where resident agents had discretion in effecting transactions. The court concluded that the real business of the petitioners was “the cooperative management in Scotland of British capital” and the US office was merely “helpfully adjunct.” Judge Opper dissented, citing the Supreme Court’s previous ruling that the American office

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