American Participations-Trust, 10 T.C. 144 (1948)

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A fixed investment trust is not taxable as a corporation if the trustee's powers are limited to preserving trust property, collecting income, and distributing it to beneficiaries, without the power to vary investments significantly.

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Summary

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American Participations-Trust sought a determination that it should not be classified as an association taxable as a corporation. The IRS argued that the trust had the power to reinvest proceeds and vary investments. The Tax Court held that the trust was not taxable as a corporation because the trustee's powers were limited to preserving the trust property, collecting income, and distributing it to beneficiaries. The crucial factor was whether the trustee had the power to vary the investment of certificate holders.

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Facts

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The American Participations-Trust was created as a fixed investment trust. The trust indenture specified a portfolio of 34 stocks, with each portfolio unit consisting of one share of each stock. The trustee had the power to sell undesirable stocks, but the key issue was whether they had the power to reinvest the proceeds to vary the initial fixed investment.

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Procedural History

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The Commissioner of Internal Revenue determined that American Participations-Trust was an association taxable as a corporation. The Tax Court reviewed the Commissioner's determination.

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Issue(s)

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Whether American Participations-Trust should be classified as an association taxable as a corporation, based on the powers granted to the trustee under the trust indenture.

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Holding

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No, because the powers granted to the trustee were limited to preserving trust property, collecting income, and distributing it to the beneficiaries, without the power to vary the investment of certificate holders in a manner that constitutes doing business.

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Court’s Reasoning

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The court relied on the principles established in *Morrissey v. Commissioner*, which defined characteristics of a business trust taxable as a corporation, including a continuing entity, centralized management, continuity uninterrupted by death, transferability of beneficial interests, and limited liability. The court distinguished this case from *Commissioner v. North American Bond Trust Co.*, where the trustee had the power to vary the investment, which led to its classification as a taxable association. The court emphasized that the powers granted in the trust indenture, not just the extent to which they are used, determine the classification. The court also emphasized that Section 7.01 of the trust indenture had to be read in conjunction with Section 11.11 which defined a unit as consisting of one share each of the specified corporations. According to the court, the trustee could not increase the number of shares of any portfolio unit. Quoting *Chase National Bank*, the court stated that if activities are limited to “weeding out whatever became unsound for investment and retaining the remainder” it prevents the trusts from “being, or becoming, more than what are sometimes called strict investment trusts.”

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