16 T.C. 1163 (1951)

A corporation does not realize taxable income when it distributes property, including growing crops, to its stockholders as a dividend in kind or in liquidation, even if the property's fair market value exceeds the consideration received from the stockholders.

Summary

Burrell Groves, Inc. sold its citrus grove and operating assets to its stockholders, the Burrells, who then formed a partnership to manage the grove. The Commissioner of Internal Revenue argued that the fair market value of the fruit on the trees at the time of the sale should be treated as ordinary income to the corporation. The Tax Court disagreed, holding that the transaction was either a bona fide sale (as the corporation reported) or a distribution in liquidation, neither of which resulted in taxable income to the corporation for the value of the unharvested crop. The court emphasized that the IRS cannot unilaterally reallocate income under Section 45 without properly raising the issue in pleadings.

Facts

Burrell Groves, Inc. (petitioner) was a Florida corporation operating a citrus grove. Eugene and Alice Burrell owned all its outstanding stock. They wanted to dissolve the corporation and operate the grove as individuals but were advised that liquidation would trigger significant taxes. Instead, they purchased the grove from the corporation based on an independent appraisal of $187,590, paying a small amount in cash and the balance with a note and mortgage. The sale included the land, trees, equipment, and a growing crop of fruit. The Burrells then formed a partnership to manage the grove and sell the fruit.

Procedural History

Burrell Groves, Inc. reported the sale as an installment sale and paid capital gains tax on the initial payment. The Commissioner determined a deficiency, arguing that the fair market value of the fruit ($87,918.75) should be treated as ordinary income. The Tax Court reversed the Commissioner's determination.

Issue(s)

Whether the Commissioner properly determined that the fair market value of the unharvested fruit on trees at the time of sale to the stockholders should be included as ordinary taxable income to the corporation.

Holding

No, because the transaction was either a bona fide sale, in which the corporation already reported the capital gain, or a distribution in liquidation, which does not result in taxable gain to the corporation for the distribution of assets.

Court's Reasoning

The Tax Court found that the Commissioner's attempt to reallocate income under Section 45 was improper because the issue was not adequately raised in the pleadings or during the initial determination. The court stated that it found "no basis, either in issues raised or on the record made, for any application of section 45." The court reasoned that once the grove was transferred, the corporation no longer had any interest in the crop. If the transfer was a bona fide sale, the corporation had already reported the capital gain. If the transfer was a distribution in liquidation, the corporation did not realize any gain from distributing assets to its stockholders, citing *United States v. Cumberland Public Service Co., 338 U.S. 451* and *General Utilities Operating Co. v. Helvering, 296 U.S. 200*.

Practical Implications

This case illustrates that a corporation generally does not recognize gain or loss when it distributes property to its shareholders as a dividend or in liquidation. It also shows the importance of proper pleadings when the IRS seeks to reallocate income under Section 45. The IRS must clearly state its intent to apply Section 45. The case also distinguishes itself from situations where the question is whether a portion of the *selling price* is allocable to the growing crop, which would be ordinary income. Here, the IRS sought to tax an amount *over and above* the selling price, which the court rejected. Later cases distinguish this ruling by emphasizing that the transfer must genuinely be a sale or distribution, and not a disguised attempt to shift income.

