17 T.C. 1625 (1952)

Accumulated earnings of a corporation do not survive a Section 77B reorganization where assets are acquired by a new corporation whose stock is acquired by creditors of the old corporation, excluding stockholders.

Summary

This case addresses whether distributions from a corporation (Fisher Corporation) constituted taxable dividends. The Tax Court held that the accumulated earnings of its predecessor (Fisher Company) were not acquired by Fisher Corporation in a Section 77B reorganization because the creditors of the old company became the equitable owners before the reorganization, effectively distributing the earnings to them. Therefore, the *Commissioner v. Sansome* doctrine, which generally allows accumulated earnings to carry over in reorganizations, does not apply in Section 77B reorganizations where creditors displace stockholders as equity owners.

Facts

Carl G. Fisher Corporation (Fisher Corporation) was formed in 1935 following the reorganization of The Carl G. Fisher Company (Fisher Company) under Section 77B of the National Bankruptcy Act. Fisher Company, primarily a holding company, had guaranteed bonds of Montauk Beach Development Corporation. When Montauk defaulted, Fisher Company, unable to pay its obligations under the guaranty, filed for reorganization. The reorganization plan provided for the creation of Fisher Corporation to which the assets of Fisher Company were transferred. Stock in Fisher Corporation was issued primarily to the creditors of Fisher Company, including the Montauk bondholders. The stockholders of Fisher Company received no stock in the new corporation. In 1940, distributions were made to the stockholders of Fisher Corporation. The Commissioner treated these distributions as fully taxable dividends. F.R. Humpage and the Estate of Carl Fisher, stockholders of Fisher Corporation, challenged this determination, arguing that Fisher Corporation had no accumulated earnings and profits from which to pay a dividend.

Procedural History

The Commissioner of Internal Revenue determined deficiencies in the income tax of F.R. Humpage and the Estate of Carl G. Fisher for the calendar year 1940. The taxpayers petitioned the Tax Court for a redetermination of these deficiencies. The Tax Court consolidated the proceedings for hearing and report.

Issue(s)

Whether the accumulated earnings and profits of The Carl G. Fisher Company were acquired by Carl G. Fisher Corporation in a Section 77B reorganization, such that the distributions to stockholders of Carl G. Fisher Corporation in 1940 constituted taxable dividends.

© 2025 SCOTUSreports.com. All rights reserved.

Holding

No, because the creditors of the old corporation became the beneficial owners of the assets before the reorganization was complete, effectively distributing the earnings to them before the new corporation was formed.

Court's Reasoning

The Tax Court reasoned that the *Sansome* doctrine, which generally provides that accumulated earnings and profits of a predecessor corporation carry over to a successor corporation in a tax-free reorganization, does not apply to a Section 77B reorganization where the creditors of the old corporation become the equitable owners of its assets. Citing *Helvering v. Alabama Asphaltic Limestone Co.*, the court emphasized that when creditors take steps to enforce their demands against an insolvent debtor, they effectively step into the shoes of the old stockholders. The court stated, "When the equity owners are excluded and the old creditors become the stockholders of the new corporation, it conforms to realities to date their equity ownership from the time when they invoked the processes of the law to enforce their rights of full priority. At that time they stepped into the shoes of the old stockholders." Because the creditors became the beneficial owners of the assets of Fisher Company prior to the transfer of those assets to Fisher Corporation, any accumulated earnings and profits were distributed to them at that time, and were not available to be carried over to Fisher Corporation. The court distinguished *Sansome* and its progeny, noting that those cases involved voluntary tax-free reorganizations or liquidations, whereas this case involved a bankruptcy proceeding where creditors ousted stockholders to enforce their rights.

Practical Implications

This case clarifies that the *Sansome* doctrine does not automatically apply to all corporate reorganizations, especially those under Section 77B of the Bankruptcy Act (or its successors). In situations where creditors take control of a company's assets through legal processes, they are treated as having received the accumulated earnings before the formal reorganization. This impacts how distributions from the newly reorganized entity are treated for tax purposes. The decision emphasizes a substance-over-form approach, looking at the actual control and ownership of assets, not just the formal steps of the reorganization. Later cases involving similar insolvency reorganizations must consider whether the creditors effectively became the equitable owners prior to the transfer of assets to the new corporation. This case also highlights the importance of analyzing the specific facts and circumstances of each reorganization to determine whether the *Sansome* doctrine applies.

© 2025 SCOTUSreports.com. All rights reserved.