***26 T.C. 151 (1956)***

When a stock sale agreement provides that a dividend will be declared and used to reduce the purchase price, the dividend is taxable to the seller if the seller owned and controlled the shares at the time the dividend was declared, even if the agreement was executed on the same day.

**Summary**

The U.S. Tax Court addressed whether a dividend declared on stock was taxable income to the seller or the buyers of the stock. The agreement for sale was executed on the same day the dividend was declared, but made payable to shareholders of record on the day before the sale. The agreement stipulated that the dividend would reduce the purchase price. The court held that the dividend was taxable as ordinary income to the seller because the seller owned and controlled the shares when the dividend was declared and paid to the seller. The court also addressed an issue regarding standard deductions, finding that the taxpayers were entitled to the standard deduction even though they incorrectly took some deductions from gross income.

**Facts**

Clarence W. Miller owned the majority of Tiny Tot Safety Table Company stock. On July 29, 1950, Miller entered into a contract to sell his stock to Raymond S. Miller and Frank Nowatzki. The contract stipulated that a dividend would be declared and used to reduce the purchase price. On the same day, the board of directors declared a dividend payable to shareholders of record on July 28, 1950. The sale agreement was also finalized on July 29, 1950. The dividend checks were issued on August 7, 1950, and the stock assignment was executed on August 4, 1950. C.W. Miller received the dividend, and in their tax returns, the buyers did not report the dividend as income, while C.W. Miller reported the sale as a long-term capital gain.

**Procedural History**

The Commissioner of Internal Revenue determined deficiencies and penalties against C.W. Miller and the buyers. The Tax Court consolidated the cases. The primary issue was whether the dividend was taxable to the seller (C.W. Miller) or the buyers. The Tax Court ruled in favor of the Commissioner, concluding that the dividend was taxable to C.W. Miller. The court also addressed issues regarding the proper calculation of income and deductions, and penalties.

**Issue(s)**

1. Whether the dividend declared on the stock was taxable income to the seller (C.W. Miller) or the buyers.

2. Whether certain deductions from gross income were properly taken on the C.W.

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Miller’s 1950 return.

3. Whether the respondent properly disallowed the $1,000 standard deduction from adjusted gross income.

**Holding**

1. Yes, because the seller owned and controlled the shares when the dividend was declared and made payable to him.

2. No, the deductions from gross income were improperly taken.

3. Yes, the petitioners were entitled to the standard deduction because they elected to take the standard deduction on their return.

**Court’s Reasoning**

The court focused on when the ownership of the stock effectively transferred. The court distinguished this case from prior cases (e.g., *Moore v. Commissioner*) where the stock was held in escrow or used as collateral and the buyer had control of the stock at the time the dividend was declared. Here, the court found that the seller retained control of the stock when the dividend was declared. The court noted that the formal assignment of the stock occurred after the dividend was declared. Additionally, the board minutes and the contract itself supported the conclusion that the sale wasn’t immediately effective. The court emphasized that the dividend was declared payable to the seller, who owned and controlled the shares at the time, and that the dividend was then used to reduce the purchase price. The court held that the form of the transaction, including the timing of the assignment and the directors’ actions, indicated that the seller remained in control at the time the dividend was declared, and thus the seller was liable for the taxes. The court cited the statement from *Northern Trust Co. of Chicago v. United States*, “Clearly the income is that of the beneficial owner of the stock…”

**Practical Implications**

This case highlights the importance of accurately determining the timing of the transfer of ownership in stock sale transactions for tax purposes. Specifically, the economic realities of the transaction, rather than the mere form, are considered by the courts. Tax lawyers must carefully draft agreements to reflect the intent of the parties regarding the transfer of beneficial ownership and control of the stock. This case warns against attempting to manipulate the timing of dividend declarations and stock sales to avoid tax liabilities, as the substance of the transaction will likely govern. Later cases would likely cite this case for its emphasis on the importance of who owns the stock at the time the dividend is declared.

**Meta Description**

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The Miller case clarifies when a stock dividend is taxed to the seller or buyer, focusing on control and ownership at the time of the dividend declaration, with implications for structuring stock sale agreements.

**Tags**

Miller v. Commissioner, U.S. Tax Court, 1956, Dividend, Stock sale, Ownership, Timing of transfer

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