J. Ungar, Inc., 26 T.C. 348 (1956)

A corporation that assigns the right to receive income to its shareholder as part of a liquidating dividend, but remains in existence to pay liabilities, is still subject to the anticipatory assignment of income doctrine and must recognize income when the income is subsequently received by the shareholder.

Summary

J. Ungar, Inc., a corporation acting as a commission broker, liquidated and distributed its assets, including the right to collect commissions on unshipped orders, to its sole shareholder. The IRS determined that the corporation was still taxable on the commissions when the shareholder received them, applying the anticipatory assignment of income doctrine. The Tax Court agreed, finding that the corporation continued to exist for tax purposes during the liquidation process because it retained assets to satisfy its liabilities. The court held that the corporation had performed all necessary services to earn the income and its assignment of the right to receive the income did not shield it from taxation. This case highlights the ongoing tax obligations of a corporation during liquidation, even after ceasing active business.

Facts

J. Ungar, Inc. (the Corporation) was a commission broker for foreign exporters that reported income on an accrual basis, recognizing income from commissions only after merchandise shipment. In 1950, the sole stockholder decided to liquidate the corporation. The corporation adopted a liquidation plan and made liquidating distributions, including a distribution of the right to collect commissions on unshipped orders to the stockholder. The corporation did not report the commissions collected by the stockholder as income. The corporation filed a certificate of dissolution with the state, but continued the process of liquidation. The IRS determined the commissions were taxable income to the corporation under the anticipatory assignment of income doctrine.

Procedural History

The Commissioner of Internal Revenue determined a deficiency in the corporation’s income tax. The corporation contested the deficiency in the United States Tax Court. The Tax Court ruled in favor of the Commissioner.

Issue(s)

1. Whether the corporation, reporting income on an accrual basis, must recognize income from brokerage commissions when the right to those commissions was distributed to its shareholder as a liquidating dividend, but the corporation continued to exist for tax purposes while settling its liabilities.

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Holding

1. Yes, because the corporation remained a taxable entity and had already earned the income, so the anticipatory assignment of income doctrine applied.

Court’s Reasoning

The court applied the anticipatory assignment of income doctrine, which dictates that the assignor of income, not the assignee, is taxed on the income when the assignor has already earned it. The court noted that the corporation had not yet shipped the goods, but all services necessary to earn the commissions had been performed before the assignment to the shareholder. The court found that the corporation remained a taxable entity during the liquidation process because it retained assets (cash) to pay off its liabilities, even after filing a certificate of dissolution. The court cited the regulation, which stated, “A corporation having an existence during any portion of a taxable year is required to make a return.” The court reasoned that the corporation’s continued existence meant that it could not escape taxation on the income that it had earned. The court distinguished the case from instances where the corporation had completely dissolved before income was realized, and had no continuing existence.

Practical Implications

This case is significant for its focus on the application of the anticipatory assignment of income doctrine during corporate liquidations. It underscores that the mere filing of a certificate of dissolution does not automatically end a corporation’s tax liability, especially if the corporation retains assets to settle liabilities. This case serves as a reminder that even during liquidation, a corporation must carefully consider the timing of income recognition. If a corporation in liquidation assigns the right to income, but has performed the services necessary to earn that income, the corporation, not the assignee, will likely be taxed on the income when the assignee later receives it. Corporate planners must understand that simply distributing assets before income realization is insufficient to avoid taxation; they must also ensure the complete cessation of the corporation’s existence for tax purposes.

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