***B.L. and S. v. Commissioner, 31 T.C. 116 (1958)***

The court determines whether a corporate withdrawal constitutes a loan or a dividend based on the facts, considering the parties' intent, the existence of a repayment obligation, and the economic substance of the transaction.

**Summary**

The case concerns the tax treatment of funds withdrawn by B. L. and S. from East Flagler Corporation. The IRS contended these withdrawals were taxable dividends because East Flagler had accumulated earnings and profits. The taxpayers argued the withdrawals were loans. The court examined the economic reality of the transactions, including the parties' intent, the presence of formal loan documentation, and the source of the funds. The Tax Court held that the withdrawals constituted loans, not dividends, emphasizing that the intent of the parties, the formal characteristics of the transactions (like the promissory note), and the subsequent conduct supported this conclusion. This decision underscores the importance of substance over form in tax law and the need for a thorough factual analysis to determine the true nature of a transaction.

**Facts**

B. L. and S. (taxpayers) owned East Flagler Corporation. In 1949, East Flagler borrowed $175,000 from West Flagler, another company controlled by B. L. and S.. East Flagler then advanced $152,000 to B. L. and S. The IRS characterized the $152,000 advance as a dividend distribution because East Flagler had accumulated earnings. A prior withdrawal of $323,000 in 1947 was also treated by the IRS as a loan. B. L. and S. executed a joint note for $475,000, the sum of the two advances. The funds were used to acquire East Flagler's stock. The corporation's books recorded both withdrawals as loans receivable. B. L. and S. had substantial assets of their own and intended to repay the withdrawals.

**Procedural History**

The Commissioner of Internal Revenue determined that the withdrawals made by B. L. and S. were taxable distributions. The taxpayers, B. L. and S., contested this determination in the United States Tax Court. The Tax Court reviewed the facts and evidence presented by both sides to determine whether the withdrawals were loans or dividends.

**Issue(s)**

Whether the withdrawal of $152,000 by B. L. and S. from East Flagler on April 13, 1949, constituted a loan or a distribution of corporate earnings taxable as a dividend.

**Holding**

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Yes, the withdrawal of $152,000 was a loan because the taxpayers intended a loan, the transactions had the formal characteristics of a loan, and they acted consistently with the loan’s terms.

**Court’s Reasoning**

The court found that the withdrawal of $152,000 was a loan, not a dividend, based on the facts and circumstances. The court emphasized that

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