28 T.C. 756 (1957)

A contract received in a corporate liquidation can have a fair market value for tax purposes, even if the payments under the contract are contingent.

Summary

In this tax court case, the Commissioner of Internal Revenue determined deficiencies against several petitioners based on their tax treatment of several transactions, most notably the valuation of contracts received from dissolved corporations. The court addressed issues related to the inclusion of certain payments to a water company, the fair market value of contracts distributed in corporate liquidations, the deductibility of a payment made by a former shareholder to satisfy corporate tax liability, and the validity of a joint tax return. The court sided with the Commissioner on the valuation of the contracts, holding that the contracts had a fair market value at the time of distribution, even though their future value was contingent on the amount of water sold.

Facts

Several corporations, in which the petitioners were stockholders, were in the business of subdividing land and constructing houses. To provide water service, they contracted with a water company to extend waterlines, paying for the extensions. The water company agreed to make payments to the corporations based on a percentage of its gross revenue from water sales to the homes for a period of 10 years. The corporations included the water line costs as part of the cost of the houses sold. Upon dissolution of the corporations, the water contracts were distributed to the stockholders. The Commissioner determined that the contracts had a fair market value at the time of distribution. In another matter, one of the petitioners, Albert Gersten, paid a tax liability of a dissolved corporation, and the issue was whether his payment to the IRS was correctly characterized as a nonbusiness bad debt. Lastly, the petitioners were residing in California, and Albert Gersten obtained a Mexican divorce and remarried, and filed a joint tax return with his new wife for 1950.

Procedural History

The cases were heard in the U.S. Tax Court. The Commissioner assessed deficiencies against the taxpayers. The taxpayers contested the assessments. The Tax Court heard the cases and issued an opinion addressing each issue raised. The decision determined the tax implications of payments made to a water company, the value of contracts distributed upon corporate liquidation, the deductibility of a payment made by a former shareholder, and the validity of a joint tax return after a divorce in California and remarriage in Mexico. Decisions were entered based on the court’s findings.

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Issue(s)

1. Whether payments made by the corporations to the water company for the construction of the waterlines were properly included in computing the cost of the houses sold.

2. What value, if any, was attributable to the water company contracts when distributed to stockholders in liquidation, and specifically if such contracts had an ascertainable fair market value.

3. Whether a payment by Albert Gersten to satisfy a tax liability of a dissolved corporation resulted in a fully deductible loss under I.R.C. § 23(e)(2).

4. Whether Albert Gersten and his new wife, Bernice, were entitled to file a joint income tax return for the year 1950 after a divorce and remarriage in Mexico.

5. Whether the business of J. Richard Company was

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