## *Engasser v. Commissioner of Internal Revenue, T.C. Memo. 1958-146*

Property held primarily for sale to customers in the ordinary course of a taxpayer's trade or business is considered ordinary income property, even if unimproved and sold in bulk.

### Summary

August Engasser, a home builder, sold a 5.5-acre parcel of unimproved land to his closely held corporation. The IRS determined the profit from this sale should be taxed as ordinary income, not capital gain, arguing the land was held primarily for sale to customers in the ordinary course of his business. The Tax Court agreed with the IRS, finding that Engasser's business included buying and selling real estate as part of his home construction activities, and the intent behind holding the land was ultimately for sale in that business, even though it was sold in bulk to his own corporation before houses were built.

### Facts

Petitioner, August Engasser, was engaged in the home construction business with his son, Charles, through partnerships and a corporation. Engasser purchased 5.5 acres of unimproved land in Amherst, New York, in December 1949. He did not improve the land, but the town paved streets through it, increasing its value. In August 1952, Engasser sold the land to Layton-Cornell Corporation, a company owned by him, his wife, and son. Engasser and his son had been buying lots, building houses on them, and selling them since 1946. Lots were purchased in Engasser's name, and the partnerships or corporation would build houses. During partnership periods, Engasser conveyed lots directly to buyers. During the corporate period, Engasser conveyed lots to the corporation, which then conveyed to buyers after houses were built. The corporation had received about 35 lots from Engasser at its formation.

### Procedural History

The Commissioner of Internal Revenue determined that the gain from the sale of the Amherst property was ordinary income. Engasser contested this determination in the Tax Court, arguing for long-term capital gain treatment.

### Issue(s)

1. Whether the gain of $44,100 realized by the petitioner from the sale of the Amherst property in 1952 is taxable as ordinary income or long-term capital gain under Section 117 of the Internal Revenue Code of 1939?

### Holding

1. No. The Tax Court held that the gain is taxable as ordinary income because the

Amherst property was held by the petitioner primarily for sale to customers in the ordinary course of his trade or business.

**Court's Reasoning**

The court reasoned that the central question is factual: whether the property was held primarily for sale to customers in the ordinary course of trade or business. The court emphasized that Engasser and his son were in the business of general contracting and home construction, consistently buying lots, building houses, and selling them. Although the Amherst property was sold unimproved and in bulk to his corporation, the court found that the original intent in purchasing the land was to eventually build houses on it for sale, consistent with his established business practice. The court stated, "The record clearly shows that the Amherst property was purchased, as were all of the other properties, with the intent and purpose of constructing houses for sale thereon." The court dismissed Engasser's arguments that the Amherst property was different because it was unimproved acreage and sold before houses were built, stating, "We see no merit in either of these distinctions." The court found the factual pattern similar to *Walter H. Kaltreider, 28 T.C. 121*, where taxpayers were deemed in the real estate business when their corporation sold houses and lots that the taxpayers owned and subdivided. The court concluded, "After considering the facts and circumstances present we have concluded and found as a fact that the property in question was held primarily for sale to customers in the ordinary course of trade or business. The gain on its sale, therefore, is ordinary income."

**Practical Implications**

This case highlights that the intent and purpose for which property is held, particularly at the time of acquisition, is crucial in determining its tax treatment upon sale. Even if land is sold in bulk or unimproved, if the taxpayer's primary business involves developing and selling similar properties, the gain from the sale is likely to be treated as ordinary income. This case is a reminder that simply selling property to a related entity does not automatically convert ordinary income property into a capital asset. The court's focus on the taxpayer's ongoing business activities and the intended use of the property demonstrates a practical approach to classifying real estate gains, emphasizing substance over form. Legal professionals should advise clients in real estate development to carefully document their intent for acquiring and holding property to ensure appropriate tax treatment, especially when dealing with sales to related entities.

 