30 T.C. 1251 (1958)

A plan of complete liquidation for tax purposes is considered adopted on the date shareholders formally approve the resolution, not the date of informal board actions or intentions, unless the sale of assets precedes shareholder approval.

Summary

The Virginia Ice and Freezing Corporation (the "Petitioner") sold two properties at a loss before a formal shareholder vote approving a plan of complete liquidation. The IRS disallowed the loss, claiming the sales fell within the 12-month period of liquidation under section 337 of the Internal Revenue Code, and therefore, no loss could be recognized. The U.S. Tax Court ruled in favor of the Petitioner, determining that the plan of complete liquidation was not adopted until the shareholders' formal approval. The court emphasized that, in the absence of a sale of assets *after* the shareholder's vote, the formal shareholder vote determines the adoption date of the liquidation plan.

Facts

Virginia Ice and Freezing Corporation was a Virginia corporation that owned and operated ice plants. Due to declining business, the board of directors discussed liquidation. On October 1 and 4, 1954, the corporation sold two ice plants at a loss. On October 1, the board entered a notice in the minute book for a meeting on October 11 to consider liquidation. On October 11, the board recommended liquidation to the stockholders. On October 22, 1954, the stockholders approved the liquidation, and authorized the corporation to sell assets. The corporation filed a tax return claiming a loss on the October sales, which the IRS disallowed, arguing the sales were part of a liquidation plan.

Procedural History

The Commissioner of Internal Revenue determined a tax deficiency based on the disallowance of the loss from the sale of the two properties. The Petitioner contested this determination in the United States Tax Court, arguing that the sales occurred prior to the adoption of a plan of liquidation.

Issue(s)

1. Whether the corporation had adopted a plan of complete liquidation before the sales of the properties on October 1 and 4, 1954.

2. If no plan was adopted, can the corporation recognize a loss on the sale of the assets?

Holding

1. No, because the plan of complete liquidation was not adopted until October 22, 1954, when the shareholders approved it.

2. Yes, because the sales occurred before the plan of liquidation was adopted, therefore, the loss could be recognized.

Court's Reasoning

The court analyzed the application of Section 337 of the Internal Revenue Code of 1954, which provides that no gain or loss is recognized to a corporation from the sale or exchange of property within a 12-month period following the adoption of a plan of complete liquidation. The court focused on the date of adoption of the plan. Citing the regulations, the court stated, "Ordinarily the date of the adoption of a plan of complete liquidation by a corporation is the date of adoption by the shareholders of the resolution authorizing the distribution of all the assets of the corporation." The court found that the formal adoption occurred on October 22, when shareholders voted to approve the plan. The Court held that the board's actions before the formal shareholder vote did not constitute adoption of a plan for purposes of Section 337. The court found that the board's actions did not represent a binding decision, and the shareholder vote was required to finalize the plan. The court rejected the Commissioner's argument that the plan was informally adopted earlier due to the board's actions, even though the directors might have anticipated shareholder approval based on past proxy voting patterns. The court noted that the sales occurred before the date on which the shareholders formally adopted the plan of liquidation.

Practical Implications

This case highlights the importance of the formal shareholder vote in determining the date of adoption of a plan of complete liquidation under Section 337. Attorneys should advise clients to clearly document the date of adoption, usually by the shareholder resolution. It clarifies that the date is not based on informal discussions or anticipated future actions. This has implications for tax planning, as the timing of asset sales relative to the adoption of the liquidation plan can significantly impact the tax consequences. Corporate lawyers should advise clients on the importance of timing asset sales strategically in relation to the formal adoption of a liquidation plan to realize or avoid recognition of gains or losses. The ruling underscores the need to adhere to the statutory requirements and regulations when undertaking liquidations to ensure desired tax outcomes. The IRS and courts closely scrutinize liquidations to prevent abuse.

The case is frequently cited in tax law and business planning contexts to understand how Section 337 impacts corporate liquidations, particularly regarding the timing of transactions and the required corporate procedures.