31 T.C. 1286 (1959)

Profits from the sale of rental cars by an automobile dealer are considered ordinary income, not capital gains, if the cars were held primarily for sale to customers in the ordinary course of the dealer's business, even if they were rented for a period of time before sale.

Summary

In *Greene-Haldeman v. Commissioner*, the U.S. Tax Court addressed whether an automobile dealer's profits from selling rental cars should be taxed as capital gains or ordinary income. The dealer, Greene-Haldeman, rented cars before selling them as used cars. The court held that these profits were ordinary income because the cars were held primarily for sale to customers in the ordinary course of business, even though they were also used in a rental business. The court focused on factors such as the substantial and continuous nature of the sales, the dealer's intent to sell, and the integration of the rental car sales into its overall used car sales operations.

Facts

Greene-Haldeman, a large Chrysler-Plymouth dealer, operated a car rental business in addition to its sales of new and used cars. It rented cars on both short-term and long-term leases. Approximately 50% of the long-term rental contracts included purchase options for the lessees. The dealer obtained additional new cars by operating a car rental fleet. After the required rental period, typically six months for short-term rentals and one year for long-term rentals, the cars were sold either to the lessees or through the dealer's used-car department. The used-car department provided all services and facilities equally for all used cars. The dealer sold a substantial number of rental cars. The average gross profit per rental car sold was significantly higher than the profit from other used car sales.

Procedural History

The Commissioner of Internal Revenue determined deficiencies in Greene-Haldeman's income tax, reclassifying profits from the sale of rental cars as ordinary income rather than capital gains. Greene-Haldeman challenged this determination in the U.S. Tax Court.

Issue(s)

1. Whether profits from the sales of automobiles, previously acquired new and rented for varying periods of time, which were held for more than six months, constituted capital gains under Section 117(j) of the Internal Revenue Code of 1939.

Holding

1. No, because the court held that the profits from the sale of the rental cars were

taxable as ordinary income, not capital gains, under the Internal Revenue Code.

Court's Reasoning

The court applied the principle that whether property is held for sale in the ordinary course of business is a question of fact. The court considered several factors: the intent of the seller, the frequency, continuity, and substantiality of sales, and the extent of sales activity. The court noted that the dealer's sales of rental cars were frequent, continuous, and substantial, constituting a part of the dealer's everyday business operations. The sales were integrated with the dealer's other used-car sales activities. The dealer's acquisition, holding, and sale of rental cars were accompanied by the primary motive of selling them at retail for profit. The court referenced the Supreme Court's ruling in *Corn Products Co. v. Commissioner*, emphasizing that the capital asset provision of the tax code should not be applied to defeat the purpose of Congress to tax profits from everyday business operations as ordinary income. The court cited *Rollingwood Corp. v. Commissioner* and *S.E.C. Corporation v. United States* in its reasoning.

Practical Implications

This case is highly relevant for automobile dealers, rental companies, and other businesses that rent property before selling it. It underscores the importance of the intent behind the holding of the property. If a company acquires assets primarily for sale, even if there is an interim rental period, profits will likely be treated as ordinary income. The court's focus on the integration of the rental car sales into the dealer's overall used-car business activities is critical. For tax planning, businesses should carefully document the purpose for acquiring and holding assets and the extent to which sales activities are integrated with other operations. The *Greene-Haldeman* case continues to be cited as a key authority in determining whether income from the sale of business assets is taxed as ordinary income or capital gains. This case sets a precedent for how the courts view the primary purpose of the property held for sale.

