O. B. M. , Inc. v. Commissioner, 52 T. C. 619 (1969)

For non-recognition of gain under IRC section 337, a corporation must diligently attempt to distribute all its assets within 12 months of adopting a liquidation plan, except those retained to meet claims.

Summary

O. B. M. , Inc. , adopted a plan of complete liquidation in 1961 but failed to distribute all its assets within the required 12-month period as per IRC section 337. The company retained assets like a lawsuit claim and stock in Tidewater, believing them worthless, but did not make a diligent effort to ascertain their value. The Tax Court held that O. B. M. did not meet section 337's requirements, thus recognizing the gain from Tidewater's liquidation. Additionally, O. B. M. 's shareholders were held liable as transferees for the corporate tax deficiencies.

Facts

O. B. M. , Inc. , ceased operations in 1958 and held significant assets including stock in Tidewater Dredging Corp. On June 23, 1961, O. B. M. adopted a plan of complete liquidation, aiming to distribute all assets within 12 months except those needed to meet claims. By June 23, 1962, O. B. M. had not distributed all its assets, retaining cash, insurance claims, the tugboat DuBois II, a lawsuit claim against New York City, and Tidewater stock. The lawsuit had a settlement offer of $15,000, and Tidewater continued to make distributions post-liquidation.

Procedural History

The Commissioner of Internal Revenue asserted deficiencies against O. B. M. for the taxable years 1961, 1962, and 1963, and also against individual shareholders as transferees. The case was heard in the United States Tax Court, which found for the respondent, determining that O. B. M. did not qualify for non-recognition of gain under section 337 and that the shareholders were liable as transferees.

Issue(s)

1. Whether O. B. M. , Inc. , distributed all its assets within 12 months of adopting its plan of complete liquidation, less assets retained to meet claims, as required by IRC section 337.
2. Whether the individual shareholders are liable as transferees for the deficiencies asserted against O. B. M.

Holding

1. No, because O. B. M. did not make a diligent attempt to determine the value of retained assets and distribute them as required by section 337.
2. Yes, because the shareholders received distributions without full and adequate

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consideration, leaving O. B. M. insolvent, and thus are liable for O. B. M. ‘s tax deficiencies under New York law.

Court’s Reasoning

The court emphasized that section 337 requires a corporation to distribute all its assets within 12 months, except those retained to meet claims. O. B. M. failed to meet this requirement because it did not diligently attempt to determine the value of the lawsuit claim and Tidewater stock. The court rejected the argument that a good-faith belief in the worthlessness of these assets was sufficient without due diligence. The court noted that the lawsuit had a known settlement value of at least $15,000, and the Tidewater stock had potential value due to subsequent distributions. Furthermore, O. B. M. did not make a serious effort to ascertain the amounts of contingent claims that might justify retaining assets. Regarding transferee liability, the court applied New York debtor and creditor law, finding that the shareholders were liable for O. B. M. ‘s tax deficiencies due to receiving distributions that left the corporation insolvent.

Practical Implications

This decision underscores the importance of diligent asset valuation and distribution in corporate liquidations under IRC section 337. Corporations must actively assess the value of all assets, including those considered worthless, to comply with the statute. The ruling also affects how similar cases are analyzed, emphasizing the need for corporations to document efforts to meet claims and to distribute assets. For legal practitioners, this case highlights the necessity of advising clients on the requirements of section 337 and the potential for transferee liability. Subsequent cases have applied this ruling to reinforce the need for thorough asset management in liquidations. Businesses must be aware of the tax implications of retaining assets beyond the statutory period and the potential for shareholder liability if the corporation becomes insolvent.

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