***O. B. M. v. Commissioner, 52 T. C. 426 (1969)***

A corporation must diligently attempt to determine and distribute all assets except those retained to meet claims to qualify for non-recognition of gain under Section 337.

**Summary**

In O. B. M. v. Commissioner, the Tax Court ruled that O. B. M. failed to comply with Section 337(a) of the Internal Revenue Code, which allows non-recognition of gain on liquidating distributions if all assets are distributed within 12 months, except those retained to meet claims. O. B. M. did not distribute all its assets, including a claim against New York City and Tidewater stock, within the required period. The court found that O. B. M. did not make a diligent effort to ascertain the value of these assets or the amount of contingent liabilities, thus failing to meet Section 337's requirements. Consequently, O. B. M. was taxable on the gain from Tidewater's liquidation, and its shareholders were liable as transferees for the resulting tax deficiencies.

**Facts**

O. B. M. adopted a plan of complete liquidation on June 22, 1962. By June 23, 1962, O. B. M. had not distributed all its assets, retaining cash, insurance claims, the tug DuBois II, a claim against New York City from the O'Brien-Quist joint venture, and Tidewater stock. O. B. M. 's liabilities included accounts payable, an insured damage claim, and a judgment for unpaid general business tax totaling $7,950. The claim against New York City had a minimum settlement value of $15,000, yet O. B. M. 's officers believed it worthless without making a diligent effort to assess its value. Similarly, they considered the Tidewater stock worthless, despite its potential for future distributions. O. B. M. received liquidating distributions from Tidewater exceeding its basis in the stock, triggering a taxable gain.

**Procedural History**

O. B. M. petitioned the Tax Court to challenge the Commissioner's determination that it failed to meet Section 337(a)'s requirements for non-recognition of gain. The Commissioner also asserted transferee liability against O. B. M. 's shareholders for the resulting tax deficiencies. The Tax Court heard the case and issued its opinion in 1969, finding for the Commissioner on both issues.

**Issue(s)**

1. Whether O. B. M. complied with Section 337(a) by distributing all its assets within 12 months, except those retained to meet claims?
2. Whether O. B. M. 's shareholders are liable as transferees for O. B. M. 's tax deficiencies?

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## Holding

1. No, because O. B. M. failed to make a diligent effort to determine the value of the claim against New York City and the Tidewater stock, and did not distribute all assets as required by Section 337(a).
2. Yes, because the liquidating distributions to the shareholders were made without full and adequate consideration, leaving O. B. M. insolvent, and New York law imposes liability on shareholders for the corporation's debts in such cases.

## Court's Reasoning

The Tax Court applied Section 337(a) of the Internal Revenue Code, which requires a corporation in liquidation to distribute all its assets within 12 months, except those retained to meet claims, to qualify for non-recognition of gain. The court found that O. B. M. did not meet this requirement because it failed to diligently ascertain the value of the claim against New York City and the Tidewater stock. The court noted that the claim had a minimum settlement value of $15,000, and the Tidewater stock had potential value due to future distributions. The court rejected O. B. M. 's argument that a good-faith belief in the worthlessness of these assets was sufficient, stating, "a taxpayer who is seeking to qualify for the tax benefit of section 337 must establish more diligence in attempting to meet the requirements of the section. " The court also found that O. B. M. 's officers did not make a serious effort to determine the amount of contingent liabilities. For the transferee liability issue, the court applied New York Debtor and Creditor Law, which imposes liability on shareholders for the corporation's debts when distributions are made without full and adequate consideration, leaving the corporation insolvent.

## Practical Implications

This decision emphasizes the importance of due diligence in corporate liquidations under Section 337. Corporations must make a serious effort to determine the value of all assets and the amount of all liabilities to qualify for non-recognition of gain. A good-faith belief in the worthlessness of assets is insufficient; corporations must actively investigate and document their efforts. This case also serves as a reminder of the potential transferee liability for shareholders receiving liquidating distributions, especially when the corporation becomes insolvent. Practitioners should advise clients to thoroughly document the liquidation process, including asset valuations and liability assessments, to avoid similar tax consequences. Subsequent cases, such as Commissioner v. Stern, have clarified the procedural aspects of transferee liability under Section 6901, but the substantive requirements for shareholder liability remain governed by state law.

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