

Vern Realty, Inc. v. Commissioner, 58 T. C. 1005 (1972)

A corporation must distribute all its assets, less assets retained to meet claims, within 12 months of adopting a plan of complete liquidation to qualify for nonrecognition of gain under IRC section 337(a).

Summary

Vern Realty, Inc. , adopted a plan of complete liquidation on February 15, 1968, and sold its office building the following month. The proceeds were deposited into a corporate savings account, but not distributed to shareholders until March 13, 1969. The corporation also owned an apartment building, which was not distributed or set aside for claims until after the 12-month period. The Tax Court held that Vern Realty did not comply with IRC section 337(a) because it failed to distribute all its assets within the required 12 months, thus the gain from the office building sale was taxable.

Facts

Vern Realty, Inc. , a Rhode Island corporation, was organized on July 8, 1959, to rent real estate. On February 15, 1968, its shareholders adopted a plan of complete liquidation. On March 15, 1968, the corporation sold an office building for \$66,500 and deposited the net proceeds of \$38,000 into a corporate savings account. An apartment building, purchased in 1967, was not rented and remained unsold until March 10, 1969, when it was transferred to shareholder Ronald Nani in satisfaction of a debt. The savings account funds were not distributed to shareholders until March 13, 1969.

Procedural History

The Commissioner of Internal Revenue determined a deficiency in Vern Realty's income tax for the fiscal year ending June 30, 1968, due to the gain from the office building sale. Vern Realty filed a petition with the United States Tax Court, which heard the case and issued its decision on September 21, 1972, holding for the Commissioner.

Issue(s)

1. Whether Vern Realty, Inc. , distributed all of its assets, less assets retained to meet claims, within the 12-month period following the adoption of its plan of complete liquidation under IRC section 337(a).

Holding

1. No, because Vern Realty did not distribute its assets within the required 12-month period. The office building sale proceeds were not distributed until after the 12-month period, and the apartment building was not set aside for claims within the

same timeframe.

Court's Reasoning

The court focused on the strict requirements of IRC section 337(a), which mandates that all assets, except those retained to meet claims, must be distributed within 12 months of adopting a plan of complete liquidation for nonrecognition of gain to apply. The court found no evidence that the office building sale proceeds were constructively received by shareholders within the 12-month period, as they remained in the corporation's savings account. Additionally, the court noted that the apartment building was not specifically set apart for the payment of claims within the 12-month period. The court rejected the argument that a shareholder resolution alone was sufficient to effect a distribution, emphasizing that actual distribution or a clear intent to distribute must be shown. The court's decision underscores the importance of timely and proper asset distribution in corporate liquidations.

Practical Implications

This decision clarifies that for a corporation to benefit from the nonrecognition of gain under IRC section 337(a), it must strictly adhere to the 12-month distribution requirement. Legal practitioners should ensure that clients planning corporate liquidations understand the necessity of timely asset distribution and proper documentation of any assets retained for claims. The ruling impacts how similar cases should be analyzed, emphasizing the need for clear evidence of distribution or intent to distribute. It also highlights potential pitfalls in the liquidation process that can lead to unexpected tax liabilities. Subsequent cases have continued to apply this strict interpretation of the 12-month rule, reinforcing its significance in tax planning for corporate liquidations.