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Taxation - Income Tax - Liquidation of Dissolved Corporation by Trust

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requiring the docketing of a *lis pendens* before it would be a notice to an innocent purchaser, the final judgment remains unaffected by such a statute. Thus Virginia takes the anomalous position that although specifically abrogated by statute, the doctrine of Common Law *Lis Pendens* remains the basis for the rule that judgment is of itself notice.

It is obvious that the existence of unrecorded and undocketed judgments in actions to quiet title will not, as a practical matter, be apparent to a lawyer searching the records unless the records of the court in which the judgment was rendered are included within the scope of his search. It is suggested that a search of such records would be extremely burdensome, if not impossible, task for several reasons, some of which are:

(1) The concealed defect in the title under examination may crop up anywhere in the entire chain of conveyances.

(2) The name of *every* grantor and grantee will apparently have to be "run" in the court records, and the records in question are commonly not kept in alphabetical order.

(3) May quiet title actions involve numerous defendants but only the principal defendant's name appears in the captions by which the case is listed for index purposes.

(4) The indexes which exist are not designed for the task of facilitating a title search.

The effect of the decision is therefore to expose a serious defect in our recording statutes. It is apparent that remedial legislation is necessary.

ROBERT L. MCCONN

TAXATION — INCOME TAX — LIQUIDATION OF DISSOLVED CORPORATION BY TRUST — Plaintiff, a trust which was originally created as a liquidation vehicle for the assets of a dissolved corporation, was taxed by defendant, Collector of Internal Revenue, as a corporation with its consequent higher tax rate. In sustaining the lower court's affirmative decision for defendant's tax ruling it was *held*, that activities of the trustees were demonstrative of an entrepreneurial intent and of a commercial nature comprising more than mere incidents of liquidation. *Anderson v. Lamb*, 222 F.2d 176 (8th Cir. 1955).

Problems of determining whether trusts are, for the purposes of federal taxation, business trusts or "associations", and hence taxable as corporations,¹ have perplexed the courts ever since *Hecht v. Malley*.² There, the Supreme Court ruled that the trusts before them were business trusts or associations, and subject to the tax levied upon corporations because their trustees were, "associated together in much the same manner as directors in a corporation for the purpose of carrying on business enterprises",³ this being true "independently of the large measures of control exercised by the beneficiaries".⁴

The Circuit Court, although not citing *Hecht v. Malley*, joined with a majority of the courts in ruling that control was not the primary test but

1. §7701 (a) (b) Int. Rev. Code 1954, Public Law No. 591 (83rd Cong. 1954).

2. 265 U.S. 144 (1924).

3. *Ibid.* at 161.

4. *Ibid.*

that the "business enterprise" element was more revealing as to the actual status of the trust or association.⁵

Since the amount of control exercised over the trustees by the beneficiaries is no longer controlling, two established guideposts remain: (1) The similarity to a corporation, or formal "quasi-corporate structure" of the trust,⁶ and (2) the "business enterprise" test. The formal characteristics are of secondary importance, the important issue being whether the trust device is being used by a group of individuals to carry on a business for profit.⁷ Thus courts must necessarily probe into the history of a trust to determine its exact character when deciding a controversy identical or similar to that presented by the instant case.⁸

In light of the Federal Revenue Act,⁹ as applied by the courts,¹⁰ how best may the structure and functions of a liquidating trust be manipulated in order to avoid a fate similar to that of the purported trust involved in the instant case? It is obvious that all liquidating trusts are not taxable as "associations".¹¹ For example, the fact that trustees were empowered to enter into oil leases did not require the holding that the trust was organized for the purpose of carrying on a business.¹² In another instance a trust was not considered a business enterprise during the liquidation despite subdivision, improvement and sale of property when it was shown such property was too large for the market.¹³

It becomes apparent that the courts will allow the liquidating trustees a reasonable latitude to avoid sacrifice in the disposal, but where the facts show an aggressive continuation or enlargement of the business of the dissolved corporation it will be correspondingly categorized by the court.

ROBERT E. KEARNEY

5. *Accord*, Commissioner v. Vandegrift Realty & Invest. Co., 82 F.2d 387 (9th Cir. 1936); Trust No. 5833, Security-First National Bank v. Welch, 54 F.2d 323 (9th Cir. 1931) (dictum).

6. *Morrissey v. Commissioner*, 296 U.S. 344, 360 (1935) (dictum) (Five points of similarity to a corporation: (1) title is held by trustees as a continuous body during life of trust; (2) centralized management by trustees; (3) continuity or perpetual succession; (4) transferable shares; and (5) limited liability) (dictum).

7. *Commissioner v. Vandegrift Realty & Investment Co.*, 82 F.2d 387 (9th Cir. 1936).

8. See *Nee v. Linwood Securities Co.*, 174 F.2d 434 (8th Cir. 1949) (To be taxable as an association, the trust must (1) be initially created or have been thereafter utilized during the tax period involved, as a vehicle for carrying on a business enterprise, and it must (2) have characteristics under its written structure or in its adopted mode of operation resembling a corporate organization.).

9. 48 Stat. 771 (1934), 15 U.S.C. § 717a (1946).

10. *Porter v. Commissioner of Internal Revenue*, 130 F.2d 276 (9th Cir. 1942). Also See 2 Nossaman, *Trust Administration & Taxation*, §715. 267 (rev. ed., 1949). *Stevens, Corporations*, §7. 30 (2d. ed., 1949).

11. *E.g.*, *Fidelity Nat. Bank & Trust Co. v. Commissioner of Internal Revenue*, 37 B.T.A. 473 (1938) (Trustees were required to collect and turn assets into money and distribute the same from time to time as rapidly as was possible and consistent with the realization of fair prices therefor.)

12. *Nee v. Linwood Securities Co.*, 174 F.2d 434 (8th Cir. 1949).

13. *Girard Trust Co. v. Commissioner Internal Revenue*, 34 B.T.A. 1066 (1936).