

Background Facts
<p>This case is before us for the second time on a petition to review a decision of 647*647 the Tax Court, reported in 1948, 10 T.C. 1080. Petitioners have sought, by invoking the doctrine of Gregory v. Helvering, 1935, 293 U.S. 465, 55 S.Ct. 266, 79 L.Ed. 596, 97 A.L.R. 1355, to avoid the tax consequences of a transaction falling within the literal language of the statutory definition of a "reorganization". I.R.C. § 112(g) (1) (D), 26 U.S.C.A. § 112(g) (1) (D). On the first petition, we vacated the Tax Court's decision, reported in 1946, 6 T. C. 455, and remanded the case for further proceedings. 1 Cir., 1947, 160 F.2d 839. The factual background has been clarified on the remand.</p> <p>John B. Lewis died in 1930, and John D. Lewis, Inc., a Rhode Island corporation (hereinafter called the old company), was organized in 1931 to take over the business which the decedent had operated. The common stock was issued to the trustees under decedent's will, and had a basis of \$435,000 in their hands. Petitioners are the surviving trustees.</p> <p>The old company was engaged in three different lines of business in 1941: the manufacture of synthetic resins, the manufacture of chemicals for the textile industry, and the distribution of chemicals. In July, 1941, the synthetic resin business and the chemical distributing business were sold for a total of approximately \$325,000 in cash and marketable securities. At that time petitioners, who were directors of the old company, tried to sell the chemical manufacturing business too, but their efforts were unsuccessful. They decided to continue operating this business until they could dispose of it at a fair price, but they did not want to leave the old company's liquid assets at the risk of the chemical manufacturing business. Advice of counsel was sought as to how to distribute the liquid assets so as to incur a minimum tax. The decision was reached to transfer the operating assets of the chemical manufacturing business to a new corporation in exchange for its stock and to distribute this stock, together with the old company's liquid assets, in liquidation of the old company.</p> <p>Steps were then taken to carry this decision into effect. On December 27, 1941, the directors of the old company voted to transfer to a corporation to be organized (hereinafter called the new company) all the assets of the old company, other than cash in excess of \$90,000 and securities, in consideration of the issuance to the old company of the capital stock of the new company and the assumption by the latter of the old company's liabilities. This action of the directors was ratified by the shareholders on the same day. On December 29, 1941, the new company was incorporated under the laws of Rhode Island. At 11 A.M. on that day, the old company made the transfer of assets to the new company in exchange for its stock, and at 11:30 A.M. the directors of the old company voted to liquidate that company by distributing its remaining assets, including the stock of the new company, to the shareholders of the old company in cancellation of the old company's outstanding shares. Immediately thereafter the shareholders of the old company ratified this action, and it was carried out. The Tax Court found that the gain realized by petitioners, as trustees, on this exchange was \$66,107.30, and this amount was not disputed by petitioners. The cash distributed to petitioners exceeded this sum, and the undistributed earnings or profits of the old company accumulated since 1931 also exceeded it.</p> <p>The Tax Court found that "there was no interruption of [the chemical manufacturing] business and no change of location, policy, personnel, officers, or directors, but no salaries were paid to the officers. The new company continued to conduct the chemical manufacturing business until the latter part of 1944, when the Hercules Powder Co. purchased the bulk of its assets. The new company was liquidated and dissolved in 1945. The 1941 transfer of assets from the old company to the new company in exchange for the latter's stock was undertaken for reasons germane to the continuance of the corporate business. There was a business purpose in the transaction, and the plan which was adopted and carried out effected a genuine reorganization of corporate business, with a continuity of the enterprise 648*648 and continuity of interests therein under a modified corporate structure."</p> <p>On the fiduciary income tax return of the Estate of John B. Lewis for the year 1941, petitioners reported the gain on the exchange of the old company's shares as a long-term capital gain under I.R.C. §§ 115(c) and 117, 26 U.S.C.A. §§ 115(c), 117, realized upon the complete liquidation of the old company. The Commissioner determined a deficiency on the grounds that the liquidating distribution to petitioners by the old company was made pursuant to a plan of reorganization; that under § 112(c) (1) the gain was recognized in full since it was less than the value of the "boot", that is, the cash and securities (other than the stock of the new company) distributed; and that since the distribution had the effect of a dividend, it was taxable as such pursuant to § 112(c) (2). On the basis of the above findings, the Tax Court sustained the Commissioner. This decision of the Tax Court is now before us on review.</p>

Analysis
Although petitioners' intention was to dispose of the chemical manufacturing business eventually, the fact that a going business was transferred and operated left the new company and petitioners, its shareholders, in a position where they stood to gain or lose from operations just as before the transfer; if business conditions warranted it, the business could have been continued indefinitely.

Rule
"the essence of [a statutory reorganization] is a continuance of the proprietary interests in the continuing enterprise under modified corporate form, the transaction being deemed insufficiently closed economically to justify a tax at the time, except in so far as the stockholder gets something in addition to stock or securities in the reorganized company."

Analysis
What is controlling is that in both the "popular and economic sense,"[5] and the intentment of the statute, considerations of "boot" aside,[6] gain or loss is not sufficiently crystallized for recognition by the mere transfer of a going business to another corporation for operation indefinitely; "the collective interests still remained in solution." Helvering v. Gregory, 2 Cir., 1934, 69 F.2d 809, 811. Hence, the transaction was within the statute.

Rule
§ 112(g) (1) (D): "The term 'reorganization' means * * * (D) a transfer by a corporation of all or a part of its assets to another corporation if immediately after the transfer the transferor or its shareholders or both are in control of the corporation to which the assets are transferred".

Conclusion
The controlling factor which we have concluded brings this case within the statute is that a basic element of the plan was the continuance of the chemical manufacturing business in the corporate shell of the new company, with the gain (were it not for the "boot") not having sufficiently crystallized for recognition, because the collective interests of the shareholders "still remained in solution."

Conclusion
The decision of the Tax Court is affirmed.