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THE CASE OF THE UNDISTRIBUTED EARNED SURPLUS

THE ancient sage Ben Zakai, when expounding the laws of false weights and measures, is said to have exclaimed: "Woe unto us if we tell them, and woe unto us if we don't tell them. If we tell them, they will learn how to circumvent the law, and if we don't tell them, they will say the sages are without learning in these matters." [1] Commentators on the income tax laws must, in these days, share the same feeling of frustration. Yet the example of the great sage in expounding the law must be followed.

Lawyers who are familiar with the tax dilemmas of their clients will rank high the problem of the undistributed earned surplus of the one man, or family-owned, corporation. Despite war time taxes, including excess profits taxes, which often drained nearly 90% of the net profits of corporations into the federal treasury, and despite liberal salaries paid to officers, and even occasional dividends to the stockholders, many companies accumulated large cash surpluses and, in many cases not yet affected by the recession, are continuing to do so. The stockholders whose enterprise produced these luxurious growths of monetary rewards find themselves in a sorry predicament. Should the corporation declare the surplus in dividends, it would surely be consumed in personal income taxes.[2] On the other hand, to allow the surplus to remain unused in the corporate treasury is to expose it to the hazards of business, to deprive one of its present enjoyment, and to run the risk of substantial depletion thereof by the application of Section 102 of the Internal Revenue Code,[3] or the possible revival of some form of undistributed

[1] TALMUD, TRACTATE BABA BATHRA, p. 89b.

[2] Under existing rates, the tax levied by the Federal Government on a dividend of $200,000 received by a stockholder would be in excess of $150,000; and for sums in excess of $200,000, the income tax would approximate 90% of the dividend received. See Internal Revenue Code, Sections 11 and 12.

[3] As to the problems raised by Section 102, see Cary, *Accumulations Beyond the Reasonable Needs of the Business: The Dilemma of Section 102(c)*, 60 HARV. L. REV. 1282 (1947).

profits tax.[4] No Scylla or Charybdis could be more disheartening.

The simplest procedure is, of course, the complete liquidation of the corporation. By this process, the cash surplus as well as all the other assets of the corporation are distributed to the stockholders who may thereupon pay a capital gain tax on the excess of the proceeds from liquidation over the base cost of the stock.[5] The good will of the corporation as well as its future earning power are in that case, however, lost to the stockholders. This untoward result is averted where there are several classes of stock and the cash surplus, or a substantial part thereof, can be utilized to redeem an entire class of stock, leaving the corporation in a position to carry on the business.[6] Or, where there are several stockholders, it is possible for the corporation to cancel or redeem all of the stock of one of the stockholders who would, in such event, be liable only for a capital gain tax.[7] But if only a percentage of the stock of all the stockholders, or even of one stockholder is redeemed or cancelled, the cash received by the stockholder will normally be treated as a dividend.[8] No doubt, there are situations in which the

[4] The Internal Revenue Act of 1936, §§ 14, 27, 49 STAT. 1648-1756 (1936), imposed a tax on undistributed profits. This was dropped in subsequent revenue acts.

[5] INT. REV. CODE §§ 115(c), 115(d); U. S. Treas. Reg. 111, § 29.115-5.

[6] *Ibid.*, § 115(i); U. S. Treas. Reg. 111, § 29.115-5; White v. United States, 305 U. S. 281 (1938); Helvering v. Weaver, 305 U. S. 293 (1938).

[7] ". . . , a cancellation or redemption by a corporation of all of the stock of a particular shareholder, so that the shareholder ceases to be interested in the affairs of the corporation, does not effect a distribution of a taxable dividend." U. S. Treas. Reg. 111, § 29.115-9.

[8] *Ibid.* See also INT. REV. CODE § 115(g) providing that if a corporation cancels or redeems its stock in such manner as to be equivalent to a dividend, it will be taxed as such. In the second circuit, it had been held that distribution of accumulated earnings in cancellation of stock could never be "essentially equivalent" to a dividend. Di Nobili Cigar Co. v. Commissioner, 143 F. 2d 436 (2d Cir. 1937). But this proposition has been discarded *sub silentia*, Kirschenbaum v. Commissioner, 155 F. 2d 23, 24 (2d Cir. 1946), *cert. denied*, 329 U. S. 726 (1946). In this case, the court said, "What other test will satisfy the language of Section 115(g) we need not now attempt to say; perhaps the section covers all cancellations or redemptions which result in the distribution of accumulated earnings." This language can hardly be squared with Section 115(i) which defines "amounts distributed in partial liquidation" as any distributions made by a corporation "in complete liquidation or redemption of part of its stock." This proposition, that is, that stock cancelled or redeemed by a corporation out of accumulated earnings is equivalent to a dividend under Section 115(g) is said to rest on the decision of the Supreme Court

purchase by the corporation of a part of the stock of one or even of all of the stockholders might be dictated by motives other than the avoidance of the tax on dividends. Where such a good business reason exists, there is room for the argument that the distribution is not a dividend but a mere sale of stock to the corporation and the proceeds should, therefore, be taxed as a capital gain.

Basically, the line between taxation of the stockholders' receipts as dividends, on the one hand, or proceeds of the sale on the other, must depend upon whether the stockholder is actually parting with something when he surrenders his stock to the corporation. Where all the stockholders of a corporation surrender the same percentage of stock to the corporation, it is plain that no essential differences in their relationship to the corporate entity are effected; but where the percentages surrendered are not uniform among stockholders, an actual change in the relationship between them results, and there is ground for the opinion that in such cases the distribution should not be regarded as a dividend.

Recently, the Tax Court has held [9] that the sale of stock by a stockholder to a wholly owned subsidiary of a corpora-

in Commissioner v. Estate of Bedford, 325 U. S. 283 (1945). But that case arose under the provisions of Section 112 and involved a reorganization consisting of a recapitalization in which the stockholders received in exchange for their old stock, new stock plus cash. As the cash was derived from accumulated net earnings, the court held that it was equivalent to a dividend under the provisions of Section 112. Explicitly, the court held that Section 115(i) was not involved. "Respondent, however, claims that this distribution more nearly has the effect of a 'partial liquidation' as defined in Section 115(i). But the classifications of Section 115, which governs 'Distributions of Corporations' apart from reorganizations, were adopted for another purpose. They do not apply to a situation arising within Section 112. The definition of a 'partial liquidation' in Section 115(i) is specifically limited to use in Section 115. To attempt to carry it over to Section 112 would distort its purpose." But the circuit court in the *Kirschenbaum* case, *supra,* dismisses this distinction with the statement that the Supreme Court's interpretation of the phrase "equivalent to a dividend" in Section 112 is binding upon the lower courts in interpreting Section 115(i), in spite of the Supreme Court's caveat that the two sections have different purposes.

Moreover, where the corporation purchases its stock and holds same in the treasury for resale the circuit court in the *Kirschenbaum* case, *supra* at 25, reiterated its holding in Alpers v. Commissioner, 126 F. 2d 58 (2d Cir. 1942), that the acquired shares were neither "cancelled or redeemed" and, therefore, not within Section 115(i). It is noteworthy that this dictum is from an opinion written by Judge Learned Hand, who dissented in the *Alpers* case, *supra.*

[9] Trustees of Common Stock of John Wanamaker, etc. v. Commissioner of Internal Revenue, 11 T. C. 365 (1948).

tion does not result in a taxable dividend, even if the sale to the corporation itself would have involved such a determination. The opinion of the Tax Court makes it clear that the decision is made necessary by the language of the statute itself. In principle, it is difficult to see any reason for the distinction between the sale of stock to the corporation and the sale to its wholly owned subsidiary whose funds are entirely available to the corporation.

Where the stockholders sell their stock outright to a third party, there is, of course, no difficulty about treating the proceeds as a capital gain. Practical obstacles, however, to such sales are evident. It is difficult, in the first place, to find purchasers who are willing to buy the stock in companies which have accumulated large surpluses. The burden with regard thereto, in such cases, is simply transferred from the seller to the purchaser. Even where a sale of that sort could be made, say to a competitive company which might have some use for the corporate assets as well as its cash surplus, the seller could not expect to receive par for the frozen dollars in the corporate surplus. Of necessity, such sales partake of the nature of distress sales and do not realize what most people, who have toiled over the years to build up corporate enterprise, regard as fair value.

A wholly different result, however, is obtained where the sale of the corporate stock is made to an institution exempt under Section 101 of the Internal Revenue Act.[10] Such an institution can afford to pay par for the frozen dollars, to pay a fair price for the going concern value of the business, and can even afford to give the seller a net profit over the value of the assets. The reason for this ability so generously to deal with the business to be sold is that the tax exempt institution can forthwith withdraw the surplus, when it becomes the owner of the stock, as a dividend and being exempt from taxation can use the whole surplus to reimburse itself for the purchase price.[11] Moreover, under certain circum-

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[10] Finkelstein, *Freedom From Uncertainty in Income Tax Exemption*, 48 MICH. L. REV. 449 (1950).

[11] As I have shown elsewhere definitive rulings by the Supreme Court have not yet been made, despite the holding in Trinidad v. Sagrada Orden, 263 U. S. 578 (1924).

stances, it would seem that the tax exempt institution could operate the business without paying any income tax on its profits at all and could, therefore, use a portion of the profits to meet deferred payments on the purchase price of the stock or to reimburse itself for monies borrowed or advanced wherewith to complete the purchase.[12]

Indeed, the sale of the corporate stock to a tax exempt institution would seem to be a copper riveted method of translating the cash surplus into a fund in the hands of the stockholders subject only to a capital gain tax; and this would be so even if it were ultimately to be held that the business so purchased by the tax exempt institution were not tax exempt with respect to its future earnings.[13] The withdrawal of the surplus by the tax exempt institutional stockholder, as a dividend, would, under well settled doctrine, be necessarily tax exempt.[14]

Recently, the vogue of selling industrial concerns to tax exempt institutions has both become popular and attracted comment.[15] Where the purchase price is furnished by the tax exempt corporation out of its own treasury, or even where it derives from the surplus funds of the industrial company purchased, the transaction, from the tax point of view, is properly unimpeachable. But where the purchase price is largely deferred over a period of years, and is to be derived wholly, or in large measure, from future profits of the industrial company acquired, by the tax exempt entity, a difficult problem is presented both to the tax administrators and to the courts. By the process of forming special *ad hoc* foundations for each purchase, the sole assets of which are to be the stock of the industrial company purchased, the unequivocal undertaking of the foundation to pay the pur-

[12] Roche's Beach, Inc. v. Com. of Int. Rev., 96 F. 2d 776 (2d Cir. 1938); Com. of Int. Rev. v. Orton, 173 F. 2d 483 (6th Cir. 1949).

[13] Though the corporation acquired should ultimately be held to be taxable by refusal of the Supreme Court to follow the doctrine of the *Roche's Beach* case, *supra* note 12, and the adoption of the views expressed by Judge Learned Hand in his dissenting opinion in that case, there seems to be no basis for denying the ordinary incidents of a sale to a transaction whereby stockholders sell all or part of their stock to a tax exempt institution.

[14] This much can well be said to have been settled in the *Trinidad* case, *supra* note 11.

[15] *Ibid.* See also note 10 *supra.*

chase price is deprived of practical significance. Where the foundation agrees to make payments on account of the purchase price, and its only source of revenue will be income derived from the acquired industrial company, a strange series of results follows. The industrial company itself might escape taxation, and its profits, or a substantial portion thereof over a number of years, will come into the hands of the original stockholders, subject only to the capital gain tax. If such results are within the scope of congressional intent, all is well, for they can be firmly supported by economic policy. But if Congress does not intend to effect such a policy, it is clear that clarification is needed on the legislative level. For it would seem that without such clarification the proposed escape from the aforementioned taxpayers' dilemma must necessarily be deemed to be free from administrative or judicial condemnation.

A specific example will help to clarify the problem. A large university, whose income is clearly tax exempt, proposes to buy all the stock of a manufacturing corporation. The agreed purchase price is \$5,000,000, but the university is unwilling to risk either its funds or its credit in the enterprise. Let us assume that the manufacturing company has a cash surplus, above its business requirements, of \$1,000,000, and net profits, before taxes, annually of approximately \$500,000. There are several mechanisms which are customarily used in this type of situation, of which only one need be discussed. A new foundation is created by the university; its control is in the hands of the university authorities, and its charter provides that all its income must be utilized for the purposes of the university. The new foundation is endowed with but a most nominal capital, and it acquires the stock of the manufacturing company in consideration of its specific promise to pay \$5,000,000 therefor as follows: \$1,000,000 upon purchase, and the balance in sixteen annual installments of \$250,000 each. The first payment is made by the foundation by drawing out as a tax free dividend the entire cash surplus of the acquired company. The remaining payments will be made out of tax free dividends received by the foundation from future operations of the manufacturing company. If the manufacturing company is likewise tax exempt, as it may be under certain circumstances, the benefits to the parties will be immediate, otherwise, somewhat delayed. By this rather simple device, $5,000,000 of ordinary income has been converted into a capital gain.

The points of administrative attack on this device are few and singularly unimpressive. It might, of course, first be argued that we are not dealing here with a genuine sale.[16] But why not? Is it because the purchaser is made of straw, and its solemn undertaking to pay is without meaningful worth? But such transactions are everyday occurrences in business, particularly in the sale of real estate. The presence of an unequivocal obligation to pay is usually sufficient to denominate the transaction a sale. It has never been suggested that the purchaser must also be a man of means.

Of course, if it should be held that the dividends received by the foundation were not exempt from taxes, the plan would fail to achieve its purpose. But is such a holding within the realm of the probable? Clearly not. It has already been held by the Supreme Court of the United States, in a much cited and relied upon decision, that dividends received by a tax exempt corporation are exempt from the income tax.[17] What is there in the fact that the foundation controls and operates the business, to change the incidence of this rule? To be sure there is a factual difference and it is one that legislation may well deal with. But surely there is nothing here that the courts may seize upon as a basis for limiting the area of tax exemption of those institutions which are specifically exempted by Section 101 of the Internal Revenue Code.

Should it turn out that the encouragement of such sales is contra-indicated by a sound public policy, numerous legislative devices are available for their discouragement. For example, foundations formed in the future might be required to be of a certain age, say three to five years, before they could enjoy tax exemption; or limitations might be imposed

[16] Thal v. The Commissioner of Internal Revenue, 142 F. 2d 874 (6th Cir. 1944); Commissioner of Internal Revenue v. Hopkinson, 126 F. 2d 406, 409-10 (2d Cir. 1942); Commissioner of Internal Revenue v. Moore, 48 F. 2d 526 (10th Cir. 1931).

[17] Trinidad v. Sagrada Orden, *supra* note 11.

upon the powers of tax exempt corporations to incur obligations, or to manage, operate or control business concerns.

The discussion thus far has been of a method of solving the stockholder's tax dilemma, by the liquidation or sale of the enterprise.

Where the stockholder desires to remain an active participant in the business and to derive business benefits therefrom in the future, the sale of the stock or the liquidation of the corporation does not meet his requirements and the problem must squarely be faced as to whether or not there exists any form of reorganization which will have the effect of separating the cash surplus from the corporation and making it available to the stockholder or stockholders, and at the same time freeing it from the imposition of the tax on dividends.

It should, of course, be borne in mind that any plan of reorganization which has for its primary purpose the achievement of this end must necessarily fail. Mere compliance with the letter of the law will not avoid the tax under the current doctrines of the Supreme Court, unless there exists, at least in addition to the tax avoidance purpose, another business purpose which by itself would justify and explain the reorganization. What we are here saying to the taxpayer is this: You may not take advantage of the provisions for corporate reorganization contained in the Internal Revenue Code merely for the purpose of avoiding a tax on dividends. But, if you have a genuine business purpose which would justify your reorganization on its own merits, the incidental avoidance of the tax on dividends will not be an insurmountable hazard. In such cases, it is suggested that the tax might be avoided if the court could be convinced that a genuine business purpose is being served.[18]

It is not difficult to devise a plan of reorganization which will comply with the letter of Section 112 of the Internal Revenue Code and which will effectively separate the

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[18] Darrell, *Recent Developments in Non-Taxable Reorganizations and Stock Dividends*, 61 HARV. L. REV. 958 (1948).

cash surplus from the operating company and make the cash available to the stockholders without subjecting the transaction to any tax at all. The definition of the term "reorganization" in Section 112 [19] permits the transfer of all or part of the assets of a corporation to another corporation without the recognition of gain or loss if, immediately after such transfer, the transferor corporation, *or its stockholders,* are in control of the transferee corporation. Thus, if a corporation with a large, but not needed cash surplus, should transfer all of its assets, exclusive of such cash surplus, to a new corporation formed for the purpose, and the new corporation, in consideration of such transfer, should distribute its stock among the stockholders of the transferor corporation, a non-taxable reorganization would take place within the letter of the statute, and would comply with the provisions of Section 112(g), as well as Section 112(b)(4) of the Internal Revenue Code.[20] Prior to the doctrine of *Helvering v.*

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[19] INT. REV. CODE § 112(g), defining a "reorganization," provides, in part, as follows: "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, ..."

[20] INT. REV. CODE § 112(b)(4) provides that "No gain or loss shall be recognized if a corporation a party to a reorganization, exchanges property, in pursuance of the plan of reorganization, solely for stock or securities in another corporation a party to the reorganization."

This language is not sufficient to cover the hypothetical case suggested in the text, where a corporation transfers property to another corporation, and the stock of the transferee is issued directly to the stockholders of the transferor corporation. But since the definition of "Reorganization" in Section 112(g)(1)(D) includes a case where there is "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," it has been held that such a transaction is covered by Sections 112(b)(4) and 112(g). Clyde Baron, Inc. v. Com. of Int. Rev., 4 T. C. 1107, 1118, 1119 (1945). But *quaere,* does this decision give proper consideration to the history of the statute? The Revenue Act of 1932, 47 Stat. 169 (1932), contained an old provision, numbered Section 112(g), as follows: "If there is distributed, in pursuance of a plan of reorganization, to a shareholder in a corporation a party to the reorganization, stock or securities in such corporation or in another corporation a party to the reorganization, without the surrender by such shareholder of stock or securities in such a corporation, no gain to the distributee from the receipt of such stock or securities shall be recognized." This language precisely covered the hypothetical case instanced in the text. But Section 112(g) of the 1932 Act was omitted from all subsequent acts. Referring to this section, the Report of the House Committee on Ways and Means in the 73rd Congress (2d session), 14, stated: ". . . the Committee recommends that Section 112(g) be omitted from the bill. This paragraph provides that a corporation, by means

Gregory,[21] it would not have been thought that such a transaction would be taxable under any statutes, and the transferor corporation might, upon the completion of the transaction, be retained by the stockholders as a personal holding company, as a vehicle for making new investments not within the scope of the old investments; or it might be liquidated and the cash distributed to the stockholders on a capital gain basis. All this was possible in the halcyon pre-New Deal, pre-depression, pre-Roosevelt days, when finance had learned, as one jurist put it,[22] to improve on the resourcefulness of Becky Sharp by learning to live on no reported income at all, without in any way reducing its revenues. But in these days, much more than mere compliance with the provisions of the statute is required before a reorganization is permitted to be tax exempt by the courts. It must also appear that the reorganization has a "business purpose," that is, a logical reason for its effectuation, other than the saving of some tax dollars. It has, however, not yet been held that the tax saving motive must be entirely absent. The furthest the statute has gone is to condemn transactions where the "primary motive" is the avoidance of the tax.[23] *Non constat.* But where other good and valid motives exist for entering into the transaction, the mere fact that tax avoidance is also one of the motives, as long as it is not the primary motive, will not prevent the exemption from accruing.

The reader will not find it difficult at this point to reconstruct the very words of the conference between the tax lawyer and his client. The lawyer will be pointing out that the plan of reorganization, while completely tax exempt by the express language of the statute, can, nevertheless, not hope to achieve its purpose unless some entirely valid and in-

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of a reorganization, may distribute to its shareholders stock or securities in another corporation a party to the reorganization without any tax to the shareholders. By this method, corporations have found it possible to pay what would otherwise be taxable dividends, without any taxes on their shareholders. The Committee believes that this means of avoidance should be ended."

[21] 293 U. S. 465 (1935).

[22] PECORA, WALL STREET UNDER OATH 189 (1939).

[23] Thus, in INT. REV. CODE § 112(k), the tax exemption is denied if "the principal purpose" of the taxpayer is to "avoid federal income tax." See also PAUL, SELECTED STUDIES IN FEDERAL TAXATION 290 *et seq.* (2d ser. 1938).

dependent motive for embarking on the plan is primarily responsible for its being undertaken. The client, mindful of the necessity for protecting his reputation for integrity, will be saying that he has long been wanting to rearrange his affairs in this way quite independently of any tax considerations. Pressed, he will point out that he is getting on in years and that he has been thinking of passing some of the responsibility on to younger shoulders; and, of course, it is necessary to give them some stock interest in the company in order to motivate their resourcefulness. Before this can be done, however, it seems idle to have so much cash in the company treasury, as the cost of the stock would then be beyond the reach of the young people. Or a proposed merger with another company cannot be arranged because of the presence of the embarrassing cash surplus. Or the stockholders wish to invest in another business, not connected with the old business, and to the risk of which the assets of the old business ought not to be subjected. Other situations of like import will arise in the mind of either the lawyer or his client, and the unanswered question in each case will be: Is this a business purpose of which the court spoke as the *sine qua non* of a valid tax free reorganization?

It was freely predicted,[24] after the decision by the Supreme Court in *Gregory v. Helvering*, that the effect of the decision would not be a change in the law, but merely a burden upon the ingenuity of counsel. "Business purposes" would have to be found and indicated to the court where prior thereto a mere literal compliance with the statute would have been deemed sufficient.

Presumably, however, there may be a perfectly valid business reason for a reorganization which is significant for the stockholders of a corporation, but of no consequence whatsoever to the corporation as an entity, or to the conduct of its business. The question is thereupon presented, whether such a "business purpose" is condemned by the rule in *Gregory v. Helvering*. The dissenting opinion in the

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[24] Sandberg, *Income Tax Subsidy to "Reorganization,"* 38 COL. L. REV. 98, 116 (1938). "Cases like *Chisholm v. Commissioner* and *Bremer v. White* indicate that the net result of the principle, so startling and revolutionary when first announced, may be merely to require greater artistry of the tax lawyer."

Bazley [25] case would seem to indicate that the dissenting justices were of the opinion that the business purpose referred to in *Gregory v. Helvering* was any business purpose, whether that of the corporation or of its stockholders, as distinguished from the corporation. In that case, the dissenting opinion pointed out that a perfectly valid business purpose of the stockholders did, in fact, exist.[26] Strangely enough, the majority did not affirmatively deal with this point of view. In the prevailing opinion, no attempt was made to distinguish between the business purpose of the corporation and the business purpose of the stockholders. Instead, the court contented itself with holding that the purported recapitalization in the *Bazley* case, which complied with the statute "as inert language," [27] was not the kind of recapitalization to which tax exemption was afforded by the statute. Indeed, in so far as there is any expression of opinion from the court as to the meaning of the words "business purpose," the indications are that the requirement may be satisfied even if the business purpose be that only of the stockholders, and one in which the corporate entity as such has no interest. Thus, the Supreme Court, through Mr. Justice Reed, in two cases involving the exchange of stock of a corporation for its bonds, said: "There is not present in either situation the wholly useless temporary compliance with statutory literalness which this court condemned as futile, as a matter of law, in *Gregory v. Helvering.* The demonstrated possibility of sales by the holders of the obligations to persons other than stockholders *alone* proves the differentiation." [28] In these cases, a family owned corporation issued interest bearing, unsecured obligations which were distributed to the stockholders, mainly in exchange for their capital stock. The precise problem involved in the cases was whether payments of interest on these obligations were deductible by the corporation as an expense, or whether

[25] Bazley v. Commissioner, 331 U. S. 737 (1937), *affirming* 155 F. 2d 237 (3d Cir. 1946). Mr. Justice Douglas and Mr. Justice Burton dissented for reasons stated in the joint dissent of Judges Maris and Goodrich below.
[26] *Ibid.*, 155 F. 2d at 245.
[27] See majority opinion in the *Bazley* case, *supra* note 25.
[28] John Kelley Co. v. Com. of Int. Rev., 326 U. S. 521, 525-6 (1946).

the Commissioner was correct in holding, in one case at least, that the distributions were, in effect, dividends. However, while the precise point here discussed was not involved, namely, the propriety of exchanging stock of a corporation for its bonds within the safeguards afforded by Section 112 of the Internal Revenue Code, nevertheless, the language quoted above indicates that the court was of the opinion that where the bonds are freely salable by the stockholders to others than stockholders, that circumstance alone distinguishes the case from *Gregory v. Helvering*. This, of course, would be a facile mode of syphoning the cash surplus, on a capital gain basis, by the ultimate redemption of the bonds.

It is difficult to square the language thus quoted above with the holding in the *Bazley* case, for in the latter case, too, the stockholders received bonds of the corporation, and the stockholders were free to sell the bonds to others than stockholders. Yet this consideration, which was said by the Supreme Court "alone" to differentiate the case from *Gregory v. Helvering,* was held not to be sufficient to endow the transaction with the statutory exemption. Under these circumstances, it is small wonder that applications for rulings in situations of this kind are not dealt with sympathetically on the administrative level. Nor have we been promised by the court any relief on the judicial level. Rather, we are told that: "The search for relevant meaning is often satisfied not by a futile attempt at abstract definition, but by pricking a line through concrete applications. Meaning frequently is built up by assured recognition of what does not come within the concept, the content of which is in controversy." [29] There is always, however, the danger that the line so pricked, may degenerate into a series of unrelated points through which no line, Euclidian or non-Euclidian, could be drawn.

While it may seem a virtue to the Supreme Court that no specific definitions are provided, either by Congress, or the court, the business man and the administrative officials are left, by the absence of definitions, with no guide to the

[29] *Ibid.*

perplexed. Courageous taxpayers who are willing to risk all for the purpose of trying out a theory on a new state of facts by testing it with the conscience of the court, are encountered infrequently, and, as a result, the points through which the line of application is pricked are remotely spaced.

No doubt the ancient sage with whom we started was more wise than we are. His dilemma was simple compared with ours. He knew what the law is—we, alas, do not.

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