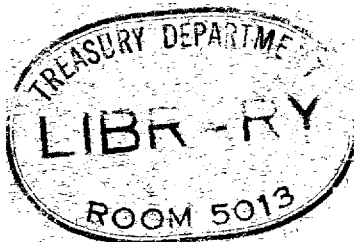


Treasury Department : : : Bureau of Internal Revenue

Internal Revenue Bulletin

Cumulative Bulletin VIII-2

JULY-DECEMBER, 1929



SPECIAL ATTENTION is directed to the cautionary notice on this page that published rulings of the Bureau do not have the force and effect of Treasury Decisions and that they are applicable only to facts presented in the published case

Treasury Department : : : : Bureau of Internal Revenue

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The rulings reported in the Internal Revenue Bulletin are for the information of taxpayers and their counsel as showing the trend of official opinion in the administration of the Bureau of Internal Revenue; the rulings other than Treasury Decisions have none of the force or effect of Treasury Decisions and do not commit the Department to any interpretation of the law which has not been formally approved and promulgated by the Secretary of the Treasury. Each ruling embodies the administrative application of the law and Treasury Decisions to the entire state of facts upon which a particular case rests. It is especially to be noted that the same result will not necessarily be reached in another case unless all the material facts are identical with those of the reported case. As it is not always feasible to publish a complete statement of the facts underlying each ruling, there can be no assurance that any new case is identical with the reported case. As bearing out this distinction, it may be observed that the rulings published from time to time may appear to reverse rulings previously published.

Officers of the Bureau of Internal Revenue are especially cautioned against reaching a conclusion in any case merely on the basis of similarity to a published ruling, and should base their judgment on the application of all pertinent provisions of the law and Treasury Decisions to all the facts in each case. These rulings should be used as aids in studying the law and its formal construction as made in the regulations and Treasury Decisions previously issued.

In addition to publishing all Internal Revenue Treasury Decisions, it is the policy of the Bureau of Internal Revenue to publish all rulings and decisions, including opinions of the General Counsel for the Bureau of Internal Revenue, which, because they announce a ruling or decision upon a novel question or upon a question in regard to which there exists no previously published ruling or decision, or for other reasons, are of such importance as to be of general interest. It is also the policy of the Bureau to publish all rulings or decisions which revoke, modify, amend, or affect in any manner whatever any published ruling or decision. In many instances opinions of the General Counsel for the Bureau of Internal Revenue are not of general interest because they announce no new ruling or no new construction of the revenue laws but simply apply rulings already made public to certain situations of fact which are without special significance. It is not the policy of the Bureau to publish such opinions. Therefore, the numbers assigned to the published opinions of the General Counsel for the Bureau of Internal Revenue are not consecutive. No unpublished ruling or decision will be cited or relied upon by any officer or employee of the Bureau of Internal Revenue as a precedent in the disposition of other cases. Unless otherwise specifically indicated, all published rulings and decisions have received the consideration and approval of the General Counsel for the Bureau of Internal Revenue.

UNITED STATES GOVERNMENT PRINTING OFFICE, WASHINGTON : 1930

ANNOUNCEMENT OF 1930 BULLETIN SERVICE.

The Internal Revenue Bulletin service for 1930 will consist of weekly bulletins and semiannual cumulative bulletins.

The weekly bulletins will contain the rulings and decisions to be made public and all Treasury Department decisions (known as Treasury decisions) pertaining to Internal Revenue matters. The semiannual cumulative bulletins will contain all rulings and decisions (including Treasury decisions) published during the previous six months.

The complete Bulletin service may be obtained, on a subscription basis, from the Superintendent of Documents, Government Printing Office, Washington, D. C., for \$2 per year.

New subscribers and others desiring to obtain the 1919, 1920, and 1921 Income Tax Service may do so from the Superintendent of Documents at prices as follows: Digest of Income Tax Rulings No. 19 (containing digests of all rulings appearing in Cumulative Bulletins 1 to 5, inclusive), 50 cents per copy; Cumulative Bulletins Nos. 1 to 5, containing in full all rulings published since April, 1919, to and including December, 1921, as follows: No. 1, 30 cents; No. 2, 25 cents; No. 3, 30 cents; No. 4, 30 cents; No. 5, 25 cents.

Persons desiring to obtain the one issue of Sales Tax Bulletin for 1920, Bulletin ST-1-20, and the Cumulative Bulletins for January-June and July-December, 1921, may procure them from the Superintendent of Documents at 15 cents and 5 cents each, respectively, per copy.

Persons desiring to obtain the Internal Revenue Bulletin service for the years 1922, 1923, 1924, 1925, 1926, 1927, 1928, and 1929 may do so at prices as follows:

Cumulative Bulletin I-1 (January-June, 1922)	40 cents
Cumulative Bulletin I-2 (July-December, 1922)	30 cents
Cumulative Bulletin II-1 (January-June, 1923)	30 cents
Cumulative Bulletin II-2 (July-December, 1923)	40 cents
Cumulative Bulletin III-1 (January-June, 1924)	50 cents
Cumulative Bulletin III-2 (July-December, 1924)	50 cents
Digest No. 13 (January, 1922-December, 1924)	60 cents
Cumulative Bulletin IV-1 (January-June, 1925)	40 cents
Cumulative Bulletin IV-2 (July-December, 1925)	35 cents
Digest No. 17 (January-December, 1925)	25 cents
Cumulative Bulletin V-1 (January-June, 1926)	40 cents
Cumulative Bulletin V-2 (July-December, 1926)	30 cents
Digest No. 21 (January-December, 1926)	15 cents
Cumulative Bulletin VI-1 (January-June, 1927)	40 cents
Cumulative Bulletin VI-2 (July-December, 1927)	40 cents
Digest No. 22 (January, 1925-December, 1927)	35 cents
Cumulative Bulletin VII-1 (January-June, 1928)	35 cents
Cumulative Bulletin VII-2 (July-December, 1928)	50 cents
Cumulative Bulletin VIII-1 (January-June, 1929)	50 cents
Cumulative Bulletin VIII-2 (July-December, 1929)	55 cents

All inquiries in regard to these publications and subscriptions should be sent to the Superintendent of Documents, Government Printing Office, Washington, D. C.

INTRODUCTORY NOTES.

The Internal Revenue Cumulative Bulletin VIII-2, in addition to all decisions of the Treasury Department (called Treasury decisions) pertaining to Internal Revenue matters, contains General Counsel's opinions, and rulings and decisions pertaining to income, estate, sales, capital stock, and miscellaneous taxes, as indicated on the title-page of this Bulletin, published in the weekly Bulletins (Volume VIII, Nos. 26 to 52, inclusive) for the period July 1 to December 31, 1929. It also contains a cumulative list of announcements relating to decisions of the United States Board of Tax Appeals published in the Internal Revenue Bulletin Service from December 22, 1924, to December 31, 1929.

Income Tax rulings are printed in four parts. Rulings under the Revenue Act of 1928 are published as Part I, the section headings corresponding with the sections of that law and the article headings corresponding with the article headings of Regulations 74. Rulings under the Revenue Act of 1926 are published as Part II, the section and article headings corresponding with the section and article headings of the Revenue Act of 1926 and Regulations 69. Rulings under the Revenue Act of 1924 are printed as Part III, the section and article headings corresponding with the section and article headings of the Revenue Act of 1924 and Regulations 65. Rulings under the Revenue Act of 1921 or earlier Acts are printed as Part IV, the section and article headings corresponding with the section and article headings of the Revenue Act of 1921 and Regulations 62.

ABBREVIATIONS.

The following abbreviations are used throughout the Bulletin:

- A, B, C, etc.—The names of individuals.
- A. R. M.—Committee on Appeals and Review memorandum.
- A. R. R.—Committee on Appeals and Review recommendation.
- B. T. A.—Board of Tax Appeals.
- C. B.—Cumulative Bulletin.
- Ct. D.—Court decision.
- C. S. T.—Capital Stock Tax Division.
- D. C.—Treasury Department circular.
- E. T.—Estate Tax Division.
- G. C. M.—General Counsel's memorandum.
- I. T.—Income Tax Unit.
- M, N, X, Y, Z, etc.—The names of corporations, places, or businesses, according to content.
- Mim.—Mimeographed letter.
- MS.—Miscellaneous Division.
- O. or L. O.—Solicitor's law opinion.
- O. D.—Office decision.
- Op. A. G.—Opinion of the Attorney General.
- S. T.—Sales Tax Division.
- S. M.—Solicitor's memorandum.
- Sol. Op.—Solicitor's opinion.
- S. R.—Solicitor's recommendation.

T.—Tobacco Division.

T. B. M.—Advisory Tax Board memorandum.

T. B. R.—Advisory Tax Board recommendation.

T. D.—Treasury decision.

x and y are used to represent certain numbers, and when used with the word "dollars" represent sums of money.

The practice of promulgating Treasury Decisions that embody court decisions relating to the internal revenue has been discontinued. Hereafter opinions of the courts, with appropriate headnotes for the information and guidance of taxpayers and officers and employees of the Bureau of Internal Revenue, will be published in the Internal Revenue Bulletin without formal approval and promulgation by the Secretary of the Treasury.

ANNOUNCEMENT RELATING TO BOARD OF TAX APPEALS DECISIONS.

Under the provisions of the Revenue Acts of 1924 and 1926, relating to appeals to the Board of Tax Appeals, the Commissioner may acquiesce in the decision of the Board or he may, if the appeal was heard by the Board prior to the passage of the 1926 Act, cause to be instituted a proceeding in court for the collection of any part of a tax determined by the Commissioner to be due but disallowed by the Board, provided that such proceeding is commenced within one year after final decision of the Board. As to appeals heard by the Board after the passage of the 1926 Act, the Commissioner may, within six months after the Board's decision is rendered, file a petition for a review of the decision by a Circuit Court of Appeals or by the Court of Appeals of the District of Columbia. In order that taxpayers and the general public may be informed as to whether or not the Commissioner has acquiesced in a decision of the Board of Tax Appeals disallowing a tax determined by the Commissioner to be due, announcement will be made in the weekly Bulletin at the earliest practicable date. Decisions so acquiesced in should be relied upon by officers and employees of the Bureau of Internal Revenue as precedents in the disposition of other cases before the Bureau.

For additional information which will be of assistance in the use of the Internal Revenue Bulletin service read the Introductory Notes to the latest Digest.

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BOARD OF TAX APPEALS.

CUMULATIVE LIST OF ANNOUNCEMENTS RELATING TO DECISIONS OF THE UNITED STATES BOARD OF TAX APPEALS PUBLISHED IN THE INTERNAL REVENUE BUL- LETIN SERVICE FROM DECEMBER 22, 1924, TO DECEM- BER 31, 1929, INCLUSIVE.

¹ VIII-52-4478

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¹ Ruling No. 4478 includes all acquiescence and nonacquiescence notices published in the Internal Revenue Bulletin service to and including December 31, 1929.

² Acquiescence relates to all issues except as to tentative tax.

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¹ Acquiescence relates to all issues except the third issue.² Estate tax decision; acquiescence relates only to 1912 trust.³ Acquiescence relates to issues involving officers' salaries and legal expenses.⁴ Acquiescence in decision in so far as it relates to inclusion in invested capital of (1) \$25,000 paid by taxpayer in 1915 for invention on which patents were pending, (2) \$600 for counsel fees.⁵ Acquiescence relates to first issue of decision.⁶ Estate tax decision.

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¹ Estate tax decision; acquiescence relates to third issue of decision.² Acquiescence relates to first issue of decision.³ Nonacquiescence notice in the case of Grosvenor Atterbury (C. B. IV-1, 4) recalled.

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¹ Acquiescence relates to second and third issues of decision.² Acquiescence relates only to issues involving computation of net income for 1918 and 1919 and excessive depreciation restored to income for 1918 and 1919.

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Blow et al., Adele M., administrators ¹	30077	16	872
Blow, George P., estate of ¹	30077	16	872
Bludworth, Mrs. W. M.....	6285	7	495
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¹ Estate tax decision.

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Boggs & Buhl, Inc.....	9269 18119	11	612
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Boyne City Lumber Co.....	10495	10	180
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¹ Estate tax decision.

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Brownell, Walter D.....	4937	4	1191
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¹ Estate tax decision.² Acquiescence relates to deduction of amounts expended for resurveying, maintaining, and marking boundaries of petitioner's property; and the cost of removing a boiler and installing a new one.

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¹ Acquiescence relates to issue 5, as to patent group No. 2, and issue 6.² Estate tax decision.³ Acquiescence relates to deduction of contribution to State Brewers' Association and affiliation with the Remar Co.

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Carney Coal Co. ⁵	{ 5562 8496 }	10	1397
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¹ Acquiescence does not relate to that part of decision involving application of Ayers decision (I. B. T. A., 1135).

² Estate tax decision.

³ Acquiescence relates to all issues of decision except fourth issue.

⁴ Acquiescence relates only to issues 2 and 4 in decision.

⁵ Acquiescence relates to issue No. 2 and with respect to fiscal year ended May 31, 1917, under issue No. 1.

⁶ Nonacquiescence notice in case of Carroll Chain Co. (C. B. IV-1, 4) recalled.

⁷ Acquiescence relates to cost of bank building, its physical life from date of acquisition, and March 1, 1913, value.

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Chartiers Creek Coal Co.-----	9652	10	984
Chatham & Phenix National Bank.-----	107	1	460
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Chicago Acceptance Co.-----	12764	12	150
Chicago Fire Brick Co.-----	11063	10	180
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Cleveland Home Brewing Co.-----	73	1	87
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Cleveland Trinidad Paving Co. of Delaware-----	17294	14	1209
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¹ Acquiescence in so far as decision determines that City Gas Co. of Norfolk and Virginia Railway & Power Co. were affiliated with each other.

² Acquiescence relates to issue as to whether proceeds of a note collected in 1919 represents income for that year; also decision as to fifth issue.

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College Point Boat Corporation.....	764	1	534
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¹ Acquiescence relates to allowance of officers' salaries.² Acquiescence relates to depreciation allowance.³ Estate tax decision.⁴ Acquiescence relates to all issues except Galloway note issue.

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¹ Estate tax decision.

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Davis Yarn Co., Inc.....	5497	8	299
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¹ Acquiescence relates only to determination of paid-in surplus at date of organization and rates of depreciation.

² Estate tax decision.

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	532		
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Derschug, John N. ³	18064	15	306
Des Cognets, sr., Louis.....	8112	7	286
Deshler Hotel Co.....	5025	7	158
Des Moines Improvement Co.....	8573	7	279
Detroit Egg Biscuit & Specialty Co.....	10563	9	1365
Detroit Opera House, Inc.....	13038	13	587
Detroit Vapor Stove Co.....	5663	4	1043
Deutsch, Julius W.....	3005	2	729
De Van & Co.....	8630	7	94
De Vaux, Norman.....	13574	14	205
De Ved, Sanford F.....	23968	15	1035
	29740		
De Vore, Fred F.....	19462	13	1376
Dewey, Mildred McLean.....	5040	9	1155
	10012		
Diamond Pillow, Feather & Down Co.....	12733	14	863
Dibble, Leon N., executor ¹	2528	6	732
Dibble, Louis N., estate of ¹	2528	6	732
Dicenso, Fellipo.....	13526	11	620
Dickey Grocery Co., L. Z.....	156	1	108
Dickinson, E. E.....	5193	8	722
Diesing, Fred D., executor.....	548	1	507
Dietrich, Gustav.....	8367	10	141
Dietrick, Herman T.....	9730	6	1371
Dill, Lewis.....	4563	3	65
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Dobson, James.....	863	1	1082
Dockum, Harry A.....	3874	11	39
Doerfler, Magdalen, beneficiary, etc.....	14551	13	921
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Donaghey Real Estate & Construction Co.....	1050	5	766
Donaldson Co., Inc., L. S.....	9974	12	271
Donaldson Iron Co.....	5762	9	1081
Donaldson Realty Co.....	25359	12	271
Donalson, Erle M., executor ¹	1629	6	455
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Dorn, Louis, estate of.....	11218	12	1102
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¹ Estate tax decision.² Acquiescence relates to first issue in decision.³ Acquiescence relates to issue 2 of decision.

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Dowling, Robert E.-----	11449	8	676
Downing Co., T. D.-----	2276	2	469
Dudley, W. S.-----	19392	15	570
Duffield et al., Divie B., executors-----	14954	14	1185
Duncan Co., J.-----	3152	9	1216
Dunn Co., John A.-----	7020	8	955
Dunn Manufacturing Co.-----	15815	14	225
Dunson Mills ¹ -----	17019	10	1150
Durabilt Steel Locker Co.-----	3121	5	239
Durkin, P. Frank-----	3644	4	743
Dustin, Annie M., estate of ² -----	8629	8	919
Dyer et al., George R., executors ³ -----	3351	5	711
E.			
Eagle Shoe Manufacturing Co., Inc.-----	5593	4	24
Earle, Ellis P.-----	13565	12	96
East Lynn Coal Co.-----	12515	13	116
East Market Street Hotel Co.-----	8664	11	796
Eastern Shoe Manufacturing Co.-----	12163	8	1169
Eastlack, James L.-----	4240	3	41
Eastland, Thomas B.-----	9762	10	1245
Eaton, Charles F.-----	2685	2	463
Eaton, Ezra Z.-----	2684	2	463
Eaton, Malcolm H.-----	2686	2	433
Eckstein, Elsie S.-----	679	2	19
Eckstein, Louis.-----	1171	2	19
Edgar, Clinton G.-----	9354	10	110
Edmonds, Jeanne, executrix-----	3940	4	967
Edmonds, John W., estate of-----	3940	4	967
Edmunds, J. M.-----	1842	1	998
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Egan & Hausman Co., Inc.-----	581	1	556
Eggink, Henry-----	6413	7	152
Ehrlich, jr., Franz, estate of-----	4695	4	483
Eimer & Amend-----	2270	2	603
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Electro Magnetic Tool Co.-----	7096	7	290
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Elias & Bro., Inc., G.-----	11954	10	508
Elkins, Luther-----	18036	12	1058
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Elliott, W. H.-----	10639	9	1404
Ellis, Wade H.-----	26136	15	1075
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Elm City Nursery Co.-----	6503	6	89
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Elsasser, Nelson A., executor ³ -----	11448	12	681
Empire State Finance Corporation-----	6805	6	1322

¹ Acquiescence relates to issue with respect to statute of limitations.² Estate tax decision; acquiescence relates to third issue of decision.³ Estate tax decision.

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Entress Brick Co.....	10006	9	588
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Evens & Howard Fire Brick Co.....	6797	8	867
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Faroll-Bittel Co.....	737	1	467
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¹ Estate tax decision.² Nonacquiescence notice in this case, published in Cumulative Bulletin IV-2, recalled.³ Estate tax decision; acquiescence relates to issue 1 of decision.

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Ficklen Tobacco Co., E. B.-----	10440	10	51
Fidelia Investment Co.-----	983	2	512
Fidelity-Philadelphia Trust Co., executor-----	27597	16	1214
Fidelity Trust Co.-----	4920	4	411
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First National Bank of Rock Rapids, Iowa-----	687	6	816
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Fleming, C. F., estate of ² -----	7212	9	419
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Foer Wall Paper Co.-----	10103	9	377
Foley, D. O.-----	13118	12	51
Fontius Shoe Co.-----	9944	7	1098
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Forrester, W. S.-----	10577	12	104
Forrester-Nace Box Co.-----	19064	12	104
Forstmann, Julius-----	2521	6	21

¹ Acquiescence relates to deduction of taxes on real estate and personal property.² Estate tax decision.

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Fruen Investment Co.....	1126	2	542
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Fulton, Guy.....	9362	11	641
Furst Bros. & Co.....	3362	2	960
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Galatis, Jerry.....	10747	8	213
Gallagher, Thomas P.....	21862	17	17
Gallen Paper Co.....	1377	5	76
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Galvin, John M., administrator.....	820	6	1088
Gambree, Wheeler B.....	3972	4	1234
Gamon Meter Co.....	395	1	1124

¹ Acquiescence relates to first issue of decision.² Estate tax decision.

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Georgia Car & Locomotive Co. ³	3131	2	986
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Gessell et al., Egbert G., executors ⁴	12394	3	441
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Giant Tire & Rubber Co.....	9412	3	334
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Gillen, Margaret.....	1785	2	1317
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Gillespie Coal Co.....	12509	1	967
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Gladly Manufacturing Co.....	227	10	165
Globe Outlet Co.....	14029	2	1290
Goellner Furniture Co.....	3500	7	860
Goerke Co., The.....	5992	15	199
Goethel Co., Alfred C.....	13273	7	955
Golconda Oil Co.....	10176	4	1073
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Goldberg, Louis M.....	11615	1	249
Goldberger, Leo G.....	243	12	874
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¹ Acquiescence relates to issue as to whether the income realized under agreements of December 14, 1918, is taxable in proportionable amounts to the several petitioners or whether such proportionate amounts are taxable one-half to the petitioners and one-half to their respective wives.

² Acquiescence does not relate to that part of decision involving application of Ayers decision (1 B. T. A., 1135).

³ Acquiescence relates only to issue 1 in decision.

⁴ Estate tax decision.

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Goodman, Emma E., estate of ¹	10124	12	823
Goodwin, C. H.....	21337	9	1209
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Goodyear, Charles A., estate of ¹	10304	11	833
Gopher Granite Co.....	6631	5	1216
Gordon Furniture Co.....	2470	3	311
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Gottfried, Hedwig B.....	8553	5	297
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Graft, George E.....	24631	8	1166
Gramercy Investing Co. of New York.....	{ 1356 2374 }	8	13
Gramercy Investing Co. of Pennsylvania.....	2373	8	13
Grand Rapids National Bank.....	{ 21116 19327 }	9 15	1119 1166
Grant, Helen M. W., estate of ¹	13792	13	174
Grant Construction Co., George J.....	2584	5	395
Grant Trust & Savings Co., trustee.....	3659	3	1026
Gras, Rudolph.....	2340	5	1163
Graves, George K.....	8113	7	286
Gray, jr., J. J.....	716	2	672
Gray, W. H.....	4552	6	347
Gray & Davis, Inc.....	143	1	222
Gray Printing Co., The.....	4503	4	1264
Graydon, Samuel.....	1477	2	552
Great Bear Spring Co. ³	10489	12	383
Great Northern Ry. Co. ⁴	{ 8433 11850 }	8	225
Green Oil Soap Co.....	3574	3	467
Greenbaum, Michael H.....	3836	2	979
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Greene Co., H. V.....	3127	5	442
Greenville Coal Co.....	3784	3	1323
Greenville Opera House Association.....	2311	5	887
Greenville Textile Supply Co.....	168	1	152
Greenwood Cemetery Association.....	3000	2	910
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Greylock Mills ⁵	11926	9	1281
Griesemer, Chester D.....	10827	10	386

¹ Estate tax decision.² Revokes nonacquiescence published in Cumulative Bulletin VI-1 at page 7.³ Acquiescence relates to depreciation and obsolescence adjustments.⁴ Acquiescence relates to all issues of decision except issue involving the question whether the company should accrue as income in the taxable years interest earned but not paid in those years on obligations of other corporations owned by it.⁵ Acquiescence in decision in so far as the Board holds that there is no deficiency for 1917.

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Grittman, Fred	16025	11	122
Grover, Arthur B.	1159	3	508
Guarantee Construction Co. ¹	1828 1848	2	1145
Guarantee Title & Trust Co.	6063	10	599
Guelph Hotel Corporation	1064	7	1043
Guenther, Paul	1755	2	105
Guggenheimer, H. Randolph	13625	9	418
Gurnee, Walter S., estate of	10441	12	1295
Gus Sun Booking Exchange Co.	10786	13	1066
Guterman & Sons Co., A. M.	10458	8	1187
Guterman Strauss Co.	234	1	243
H.			
Haas, Otto	3542	3	72
Hadaway, John B.	12717	13	986
Hadden, jr., et al., John Aspinwall, executors ²	9421	10	741
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Hagerstown Shoe & Legging Co.	463	1	666
Hagerty Shoe Co., P.	16023	15	1034
Hall, Charles Ward	11650	6	15
Hall et al., John S., executors	13552	16	71
Hall Co., Inc., F. A. ³	4612	3	1172
Hallahan, Stephen J.	6848	14	584
Hallam, Edwin C.	3582	2	1220
Hallenbeck, Harry C., estate of	12470	10	1034
Hallenbeck, John J., executor	12470	10	1034
Haller, Mary ⁴	14063 25751	14	488
Hamerslag, J. P.	13597	15	96
Hamerslag, Julian L.	13596	15	96
Hamilton & Chambers Co., Inc.	131	1	694
Hamilton Manufacturing Co.	2507	3	1045
Hammack, Rish Sons Co.	10516	6	1054
Hammerschmidt & Franzen Co.	13751	12	811
Hammersley, Charles E.	20501	16	68
Hammon, Hiram F., estate of ⁵	10914	10	43
Hammond, J. H.	11163	10	1036
Hampton Co.	2054	2	302
Hampton Cotton Mills	589	2	440
Hancock Construction Co. et al.	11758	11	800
Hancock Knitting Mills	16520	15	592
Haney and wife, Edgar P.	3486	5	1039
Hanly, W. W.	8516	6	613
Hansen, Hans C., estate of	6744	6	860
Hansen, H. Alfred, executor	6744	6	860
Hanson, Maud Hastings	5109	8	670
Harding Glass Co.	19708	15	621
Hardy, George W.	7981	5	981
Harmony Grove Mills, Inc.	4500	2	1200

¹ Acquiescence relates to fourth issue of decision.² Estate tax decision; nonacquiescence notice in this case published in Cumulative Bulletin VII-2, page 47, revoked.³ Nonacquiescence notice in the case of F. A. Hall Co., Inc. (C. B. V-1, 6), recalled.⁴ Acquiescence does not relate to deductibility of charitable contributions.⁵ Estate tax decision.

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Harris, Sam H.-----	8614	11	871
	9623		
Harris, William L., deceased, estate of ¹ -----	4426	5	41
Harris Amusement Co. of Michigan-----	17841	15	190
	17842		
Harris-Emery Co.-----	113	10	297
Harris Grocery Co., Inc., W. H.-----	3884	3	216
Harrolds Motor Car Co.-----	6184	5	429
	834	2	973
Hart Cotton Mills-----	9032	9	1062
	12781		
Hart, John W.-----	3916	7	211
Hartford & Connecticut Western R. R. Co.-----	2021	2	211
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Hartford Hat & Cap Co.-----	7400	7	714
Hartley, Harry-----	27725	16	1019
Hart-Wood Lumber Co.-----	2984	5	1171
Haskell, George S., estate of-----	4335	2	1300
Haskell, J. Amory, estate of-----	7102	6	890
Haskell, Kathryn M., executrix George S. Haskell estate-----	4335	2	1300
Hass, E. S. ² -----	14817	13	1352
Hastings, Alice M.-----	5106	8	670
Hastings, O. B.-----	5107	8	670
Hatzel & Buehler, Inc. ² -----	9501	10	993
	11454		
Haupt, Joseph J.-----	5781	6	1297
Hausmann, Louis, executor ¹ -----	5931	5	199
Hausmann, Theresa R., estate of ¹ -----	5931	5	199
Haverstick, Edward E.-----	9882	13	837
Hawkins, C. A.-----	418	6	1023
Hawks Nursery Co.-----	1469	1	1207
Hayes Textile Co., Inc.-----	844	4	1274
Haynes, Charles H., executor-----	9584	6	1166
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Hayslett, John-----	13119	12	51
Hazlett & Moss, Inc.-----	2247	2	154
Hearn, Benjamin F., estate of-----	10285	9	1362
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Heath, F. E.-----	6015	7	114
Heathcote, Bruce, administrator ¹ -----	11141	8	746
Heaton Construction Co., C. T.-----	11944	11	1302
	13695		
Heddon, Charles-----	15914	15	1372
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Heineman Lumber Co. ³ -----	10175	11	1224
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Heller et al., E. S., executors-----	4575	10	51

¹ Estate tax decision.² Acquiescence relates to second issue of decision.³ Acquiescence relates to issue as to market value on March 1, 1913, of timber owned on that date.

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Heyn, Otto P.....	7431	4	1256
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¹ Estate tax decision.² Acquiescence relates to first issue of decision.³ Acquiescence relates to third issue of decision.

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¹ Acquiescence relates to first issue of decision.² Estate tax decision.³ Acquiescence relates to third issue of decision.

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¹ Estate tax decision; acquiescence relates to issues concerning checking account, real estate, and pension fund.

² Estate tax decision.

³ Acquiescence relates to good-will and bad-debt issues.

⁴ Acquiescence does not relate to that part of decision involving application of Ayers decision (1 B. T. A., 1135).

⁵ Acquiescence relates to deduction of cost of wardrobe and traveling expenses.

⁶ Acquiescence relates only to issue 1 in decision.

⁷ Acquiescence does not apply to that part of decision relating to appeal of Guaranty Construction Co. (2 B. T. A., 1145).

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¹ Acquiescence does not relate to tentative tax issue.² Estate tax decision; acquiescence relates to value of stock.³ Estate tax decision.

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Jones Lumber Co.....	3275	5	1159
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¹ Estate tax decision.

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Kissel, Caroline T. ³ -----	21788	15	1270

¹ Acquiescence relates to depreciation and obsolescence adjustments.² Estate tax decision.³ Acquiescence relates to deduction of fees paid to attorneys.

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Knox, Seymour H., estate of-----	2936	3	143
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¹ Acquiescence relates to issue as to whether the income realized under agreements of December 14, 1918, is taxable in proportionate amounts to the several petitioners or whether such proportionate amounts are taxable one-half to the petitioners and one-half to their respective wives.

² Acquiescence relates to all issues except issue with respect to question of allowance of amortization in 1918 of costs incurred in 1919.

³ Acquiescence relates to all points of decision except that pertaining to the year 1919.

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¹ Estate tax decision.² Acquiescence relates to issue whether invested capital for 1919 should be reduced on account of the 1918 deficiency barred by the statute of limitations.³ Nonacquiescence notice in this case, published in Cumulative Bulletin IV-2, page 6, recalled.

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Lewis Co., Charles C.....	9918	16	61
Lewis-Hall Iron Works.....	3097	2	788
Lexington Realty Co.....	4639	12	850
Leydig, J. V.....	7109	15	124
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Libby & Blouin, Ltd.....	7416	4	910
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	2213		
Liberty Agency Co.....	6257	5	778
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Liberty Light & Power Co.....	3760	4	155
Lickumovitz, Morris.....	6842	4	1181
Lidstone Co., R. D.....	4133	9	447
Liebes & Co., H.....	14501	15	149
Liebman-Swaney Realty Co.....	8805	8	285
Life Saving Devices Co.....	2235	2	308
Liggett, J. T.....	3489	5	169
Lihue Plantation Co., Ltd.....	38	2	740
Lilly, V. T.....	13790	14	703
Limbert, Charles P., estate of.....	6725	9	24
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	12738		
Lincoln Cotton Mills.....	14541	15	680
	17624		
	30395	4	1245
Lindlahr Sanitarium, Inc.....	1619		
Lindsey-Long Coal & Lumber Co.....	11279	5	243
	11669		
Linn, Gus.....	1935	4	76
Lisk Manufacturing Co., Ltd. ²	10031	11	179
	11438		
	19050	15	1048
Lister, James R.....	3411	3	475
Little, Theodore W.....	10699	10	11
Live Stock National Bank.....	2467	7	413
Livermore, Norman B.....	6423	11	428
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Lloyd, Edward H.....	12092	15	82
Lloyd, William S.....	12093	15	82
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Lockport Paper Co.....	4872	9	601
Locks and Canals on Merrimack River, Proprietors of the.....	299	1	242
Lockwood, R. H., estate of.....	3843	4	1269
Loeb, Carl M.....	3082	8	787
	9191		
	9192	8	787
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	4061		

¹ Acquiescence relates to issues 3, 5, and 8 in decision.² Acquiescence relates to invested capital issue.

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Loftis, J. M. and J. S., administrators.....	7581	6	725
Loftis, S. T. A., deceased, estate of.....	7581	6	725
Logan & Bryan.....	4008	4	12
Loneragan, John E.....	6441	4	1209
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Long Island Foundry Co., Inc.....	2726	2	464
Loose, Ella C., executrix.....	8699	15	169
Loose, Jacob L., estate of.....	8699	15	169
Loper, H. T.....	10080	12	164
Lord, Elsie B.....	17189	9	807
Lord & Bushnell Co.....	{ 10597 12124 }	7	86
Lord Motor Car Co.....	4718	5	818
Los Angeles Cemetery Association.....	293	2	495
Los Angeles Towel Service Co.....	{ 8866 23391 }	9	665
Los Angeles Trust & Savings Bank.....	2818	6	850
Loughborough, J. F.....	8746	10	361
Louisiana Jockey Club, Inc.....	14654	13	752
Louisville Veneer Mills.....	10180	12	1352
Lovelace-Eubanks Lumber Co.....	15235	10	1174
Loveland, Russell V.....	1926	10	95
Lovett, Joanna, executrix estate of Thomas J. Lovett.....	2940	3	192
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Lozier, Charlotte C., estate of ²	7513	7	1050
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Lubell, Samuel L.....	26184	16	996
Luce Furniture Co.....	6536	9	1413
Lukins, F. W.....	2544	3	204
Luton Mining Co., Inc.....	13680	12	720
Lynch Construction Co.....	3375	3	313
Lynes, Emily A.....	7089	7	1085
Lynes, Samuel.....	7090	7	1085
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M.			
Mabel Elevator Co. ³	1110	2	517
MacAdam & Foster, Inc.....	10443	8	967
MacDonald-Kaitechuck Printing Co.....	279	4	996
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Mackay, Milton A.....	6833	11	569
MacKenzie, R. J., estate of ²	11141	8	740
MacMillan, H. R.....	6602	14	1367
Macmillan Co., The.....	5240	4	251

¹ Estate tax decision; acquiescence relates to all issues, except those involving deductions for executors' commissions, attorneys' fees, and miscellaneous administration expenses.

² Estate tax decision.

³ Nonacquiescence notice published in Cumulative Bulletin IV-2, page 6, recalled.

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Magnus, Mabce & Reynard, Inc.....	119	1	907
Maine Dairy Co.....	4675	4	375
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Mallinckrodt, sr., Edward ²	1750	4	1112
Mallinckrodt, sr., Edward, estate of.....	11032	14	323
Malone, Edwin B.....	5225	5	1226
Malter, Maurice.....	14502	14	1208
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Manierre, William R., deceased, estate of.....	3106	4	103
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Marble & Shattuck Chair Co.....	14091 14092 32033	13	657
Marigold Garden Co.....	1580	6	368
Marine Insurance Co., Ltd.....	2242	4	867
Markenheim Co., The.....	544	1	1240
Markle, Alvan.....	6208	10	763
Markle (II), George B., estate of.....	17780	10	763
Markle, jr. (III), George B.....	3799	10	763
Markle, sr., George B., estate of.....	17646	10	763
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Markowitz, Daniel S.....	20287	8	1100
Marks, H. Benjamin.....	10806	7	895
Marks, Isaac.....	10875	7	895
Marks, Joseph D.....	13912	14	87
Marks, Wilson.....	7132	6	729
Marlboro Fertilizer Co.....	3797	3	82
Marlin Grocery Co.....	15384	15	1080
Marsh, J. W.....	8419	12	1376
Marsh Fork Coal Co.....	10453	11	685
Marshall, Edward E.....	20308	10	1140
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Martin, Darwin D.....	3001	6	472
Maryott & Spencer Logging Co. et al.....	3341	10	1221
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Mather Paper Co. ³	1378	3	1
Mathews, W. B.....	10032	13	1133
Mathis Bros. Co.....	3861	9	338
Mattlage, Charles Henry.....	2116	3	242
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¹ Acquiescence relates to second issue of decision.² Acquiescence relates to first issue in decision.³ Nonacquiescence notice published in Cumulative Bulletin V-1, page 7, recalled.

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Mayer's, Inc.-----	3774	5	181
McAlester-Edwards Coal Co.-----	4490	10	1368
McBride, F. T., estate of ¹ -----	4885	8	435
McBride, Rose L., administratrix ¹ -----	4885	8	435
McCabe Co., M. J.-----	21	1	57
McCahill, Eugene P., administrator estate of Mary E. McCahill-----	2547	2	875
McCahill, Mary E., estate of-----	2547	2	875
McCallum, J. H.-----	14311	14	805
McCann Co., Inc., H. K.-----	{ 6578 8277 }	14	234
McCarthy, John Francis, estate of-----	17334	9	525
McCarthy, Walter R., executor-----	17334	9	525
McCarthy & Sons, Inc., John-----	354	1	1116
McCauley Co., C. R.-----	1273	1	937
McCloud, Charles A.-----	20405	13	311
McColgan, Adelaide, administratrix ¹ -----	3147	10	958
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McConnell, E. H.-----	3211	6	116
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McCoy-Brandt Machinery Co.-----	10733	8	909
McCreery, Henry F.-----	3557	4	967
McDonald, Mary E., executrix ¹ -----	3042	2	1295
McDonald, Mrs. Lyde-----	9336	9	1340
McDonald, Patrick J., estate of ¹ -----	3042	2	1295
McDonnell, Edward J.-----	6194	4	49
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McFetridge, Edward P.-----	11503	9	766
McFetridge, Georgiana-----	11210	9	759
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McGowin-Foshee Lumber Co. ² -----	10446	10	961
McGrath, B. R.-----	495	6	1089
McGrath Co., William-----	5317	10	177
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McKenna, James P.-----	121	1	326
McKinnon, L. E., estate of-----	2650	6	412
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McKnight, R. C.-----	10804	13	885
McLean, Caroline S.-----	1534	4	487
McMichael, Morgan J.-----	2221	4	266
McMillan Metal Co.-----	3841	2	797
McMullin, M. K., estate of-----	8015	12	425
McNaghten et al., Malcolm, executors-----	5846	13	871
McNeill, Robert H. ³ -----	17261	16	479
McWilliams, J. W.-----	{ 14977 25979 }	15	329
Mead et al., William W., executors-----	7228	6	752
Meade Cycle Co.-----	5756	10	887

¹ Estate tax decision.² Acquiescence relates to third issue of decision.³ Acquiescence relates to deduction of loss on account of worthless stock.

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Megeath, Samuel A.....	9248	5	1274
Megeath et al., George W.....	7118	5	1274
Meinel, Edward, estate of ¹	3098	6	341
Meinel, Ethel G., executrix ¹	3098	6	341
Meinhard, Carrie W.....	2100	3	612
Melick, J. J.....	7623	6	70
Melton, Alger.....	5699	7	717
Mephram, George S.....	1981	3	549
Mercantile Trust Co., executor ²	9528	13	85
Mercer, John W.....	8233	6	564
Merchants National Bank.....	8179	6	1167
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Meredith, E. T.....	1540	2	290
Meredith, G. W., estate of.....	4478	9	1374
Mereen-Johnson Machine Co.....	3531	5	400
Merges & Co., F.....	{ 11640 12438 }	11	444
Merillat, Charles H.....	10594	9	813
Merkle Broom Co.....	4953	3	1084
Mertz, Edward P.....	5695	5	694
Messenger Publishing Co.....	1569	2	30
Mesta Machine Co.....	2841	12	523
Metairie Cemetery Association.....	437	4	903
Metal Crafters, Inc.....	19842	15	583
Metasap Chemical Co.....	13569	12	1402
Metcalf, Edwin D., estate of.....	13348	13	236
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Metro Pictures Corporation of New England ³	4437	11	1271
Metro Pictures Film Exchange of Pennsylvania.....	747	1	721
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Meurer Steel Barrel Co., Inc.....	7749	7	64
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Meyer, Herman A., estate of.....	1062	4	686
Meyer & Bro. Co., F.....	5384	4	481
Meyrowitz, Emil B.....	3241	3	1327
Miami Beach Improvement Co.....	14869	14	10
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Michigan Trust Co. et al., executors.....	6725	9	24
Mickel, Tom E.....	440	5	979
Middleton Compress & Warehouse Co.....	1125	1	1145
Midland Coal Co.....	27	1	311
Midland National Life Insurance Co.....	28889	14	200
Midland Refining Co.....	{ 709 1983 }	2	292
Midwest Hotel Co.....	2933	5	121

¹ Estate tax decision.² Estate tax decision; acquiescence relates to issue regarding taxability of proceeds of life insurance in excess of \$40,000 exemption and issue as to bequest of works of art to or for the use of the Catholic Cathedral, St. Louis, Mo.³ Acquiescence relates to issues involving officers' salaries and legal expenses.⁴ Acquiescence relates to all issues except as to tentative tax.

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Miller, E. B.-----	3465	7	921
Miller, G. A.-----	4469	6	401
Miller, Jennie L., executrix-----	4397	11	854
Miller, John L., estate of-----	4397	11	854
Miller, Stanley R.-----	17002	12	702
Miller, Daybill & Co.-----	20267	15	13
Milliken, George W., estate of ¹ -----	10123	7	785
Milling Moore Mercantile Co.-----	7560	5	1060
Mills, Lucy M., estate of ¹ -----	1028	3	1016
Milwaukee Brass Manufacturing Co.-----	{ 3424 13542 21024 }	10	936
Milwaukee Woven Wire Works-----	8163	16	75
Miner & Frees Lumber Co.-----	10579	10	521
Miner Lithographing Co., E. C.-----	468	1	588
Minneapolis Sash & Door Co.-----	388	2	505
Minneapolis Syndicate-----	10163	13	1303
Minnesota Cement Construction Co.-----	6284	6	151
Mitchell Advertising Agency, Inc.-----	10351	10	1311
Mitchell Auto Co., A. P.-----	7597	10	1001
Mitten, Robert-----	10891	11	731
Moberly Oil Co.-----	3552	3	163
Mobile Delivery Co.-----	7124	8	1224
Mobile River Saw Mill Co.-----	8700	8	368
Mogg Coal & Coke Co.-----	12408	10	588
Moline Dispatch Publishing Co.-----	9235	11	934
Monarch Cooperage Co.-----	11590	13	929
Monarch Electric & Wire Co.-----	13405	12	158
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Monroe Cotton Mills-----	3310	6	172
Monroe Furniture Co., Ltd., et al.-----	2543	2	743
Moon, Annie-----	8675	6	385
Moon, O. L.-----	8674	6	385
Moore, Anna H., executrix ¹ -----	10542	13	864
Moore, George A.-----	14953	14	1185
Moore, H. B.-----	3544	8	749
Moore, L. C. ² -----	{ 3709 13907 }	11	979
Moore, William, estate of ¹ -----	10542	13	864
Moore Stave Co., Lucas E.-----	5146	5	1211
Moore & Scriver Co.-----	678	2	368
Mooros, Harry C.-----	4209	3	301
Moorhouse, Abraham, estate of ¹ -----	5101	8	964
Moorhouse et al., Mary Elizabeth, administrators ¹ -----	5101	8	964
Moors, John F.-----	1021	1	868
Mooyer, Christian, estate of ¹ -----	3404	2	723
Mooyer, Margaret A., executrix estate of Christian Mooyer, deceased ¹ -----	3404	2	723
Morefield and wife, W. H.-----	5721	4	394

¹ Estate tax decision.² Acquiescence relates to issue as to whether the income realized under agreements of December 14, 1913, is taxable in proportionate amounts to the several petitioners or whether such proportionate amounts are taxable one-half to the petitioners and one-half to their respective wives.

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Morris & Bailey Steel Co.....	9492	9	205
Morris & Cummings Dredging Co.....	9596	10	351
Morrison Woolen Co.....	9543	10	8
Morrison-Merrill & Co.....	4358	2	489
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Moser & Wacker, Inc.....	4475	4	1021
Mosher Manufacturing Co.....	1886	7	187
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Mosler, Moses, estate of ¹	17895	16	762
Mossberg Pressed Steel Corporation.....	8757	9	1161
Mossman, Yarnelle & Co. ²	{ 3269 11076 }	9	45
Mt. Vernon Car Mfg. Co.....	14207	13	810
Mt. Vernon National Bank.....	237	2	581
Moyse, Sidney G.....	5967	4	834
Mudd Motor Co., Ray F.....	1192	3	629
Mueller Metals Co.....	4395	3	169
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Multibestos Co.....	7598	6	1060
Mumper, Hewlings.....	14053	13	977
Munger, L. S.....	28479	16	168
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Munn Hotel Co.....	13819	14	93
Munson, Edgar, executor estate of Harriet A. Curtis, deceased.....	442	3	185
Murchison National Bank.....	608	1	617
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Murphy, Ray Slater, beneficiary.....	8191	9	521
Murphy Transfer & Storage Co.....	11554	7	1148
Musselman, C. H.....	160	1	41
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Mutual Chemical Co., of America.....	10083	12	578
Mutual Cotton Mills Co.....	16413	15	247
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Nabors Oil & Gas Co.....	7962	7	1091
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National Bank of Baltimore.....	3844	3	1038
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¹ Estate tax decision.² Acquiescence relates to issues decided adversely to the Commissioner, with the exception of issues involving deduction of tentative taxes in determining the earnings available for payment of dividends in 1918 and 1919.

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National Pneumatic Co.....	3651	5	637
National Sash & Door Co.....	5788	5	931
National Straw Works.....	5065	16	463
National Talking Machine Sales Corporation.....	5272	5	570
Naval Stores Equipment Co.....	13003	16	938
Nazareth Cement Co.....	2446	4	1121
Neapolitan Ice Cream Co.....	11793	8	437
Neill, James.....	9290	8	299
Nekonegan Paper Co.....	21064	16	1000
Neuberger, Max and Rudolph.....	{ 3035 3036 }	2	911
Neusteter Suit Co.....	4001	8	477
Nevins, Frank J.....	3344	12	866
Nevins, Frank J., administrator.....	3350	12	869
Nevins, Thomas F., estate of.....	3350	12	869
Newbold & Son Co., R. S.....	5698	7	471
New Century Color Plate Co.....	10986	10	1032
Newlyn Coal Co.....	9753	9	835
Newman, Lewis D.....	19138	9	158
Newman Theatre Co.....	3694	4	390
Newman, William C. ²	6530	10	158
Newmarket Co.....	1489	2	537
New Orleans Can Co.....	11994	7	1175
New Orleans, Texas & Mexico Ry. Co. ³	400	6	436
Newton, H. E.....	9626	7	1153
Newton, W. H.....	9627	7	1153
Newton Cotton Mills.....	10731	12	176
New York Blower Co.....	3861	9	338
New York, Brooklyn & Manhattan Beach Ry. Co.....	4945	3	606
New York, Ontario & Western Ry. Co.....	974	1	1172
New York Talking Machine Co.....	12363	13	154
Niagara Searchlight Co., Inc.....	9505	10	922
Nice Ball Bearing Co.....	2109	5	484
Nichols, A. M.....	12623	15	1155
Nichols, John W. T., estate of ⁴	9599	10	919
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Nichols Contracting Co.....	13399	15	102
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¹ Acquiescence does not relate to tentative tax issue.² Acquiescence does not relate to deduction of amount of bad debt ascertained to be worthless and charged off in 1920.³ Acquiescence relates to second issue of decision.⁴ Revokes nonacquiescence published in Cumulative Bulletin VII-1, page 39.

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North McAlester Coal Co.....	6831	5	200
North Street Trust.....	10545	6	947
Northeastern Oil & Gas Co.....	2231	5	332
	3525		
Northern Hotel Co.....	2768	3	1099
Northern Michigan Transportation Co.....	3168	3	255
Northern National Bank.....	16691	16	608
Northern Trust Co. et al., executors.....	4316	8	685
Northern Trust Co., executor ²	7127	9	96
Northwest Lumber Co.....	10650	9	1111
	15310		
Northwestern States Portland Cement Co. ³	5763	7	835
	10456		
Northwestern Yeast Co.....	1511	5	232
Northwood & Co., H.....	5122	4	697
Norton et al., Hiram S., executors ⁴	19038	16	1115
Norton, James E., estate of ⁴	19038	16	1115
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Norwood, Calif & Co.....	9	1	261
Noyes, Charles R., estate of ⁵	18486	16	519
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Oates, Mrs. Omer J.....	8393	8	981
O'Brien et al., Blanche, executors.....	25747	12	1195
	13042	10	682
O'Brien Leather Finish Corporation, Joseph.....	9630	8	521
Ocean Accident & Guarantee Corporation, Ltd.....	3114	6	1045
O'Connor & Co., J. J.....	1060	1	1021
O'Day Investment Co.....	16632	13	1230
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O'Hair, P. E., estate of.....	4184	3	1039
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Old Farmers Oil Co.....	2824	12	203
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Olsen Water & Towing Co.....	1908	1	1149
O'Meara, C. A.....	9822	11	101
O'Neill, John, estate of ⁴	5185	4	78
O'Neill, jr., et al., John J., executors ⁴	5185	4	78
O'Neill Machine Co.....	7922	9	567
Oppenheimer, Leon.....	9977	7	1156
	3317	6	1215
Opperman Coal Co.....	14729		
	15792		

¹ Acquiescence relates to third issue of decision.² Estate tax decision; acquiescence relates to trusts of 1912, 1919, and 1921.³ Acquiescence relates to first, second, third, fourth, and sixth issues of decision.⁴ Estate tax decision.⁵ Estate tax decision; acquiescence relates to issues 2 and 3 of decision.

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Paducah & Illinois R. R. Co.....	3028	2	1001
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Paget, J. H.....	4279	6	310
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Pantazas, James.....	3382	5	975
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	{ 5452		
Parker Wire Goods Co.....	12050	11	87
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¹ Acquiescence relates only to deduction of contribution to church building fund.² Acquiescence relates to issue 1 of decision.³ Acquiescence does not extend to that part of the Board's decision which purports to hold that section 704 (a) of the Revenue Act of 1923 is applicable to the case.

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¹ Estate tax decision.² Acquiescence relates to issues (c), (d), and (e).³ Acquiescence relates to issue as to value of good will for invested capital purposes for 1919.⁴ Acquiescence relates to that part of decision as to the purchase of taxpayer's own bonds at less than par which were held as an investment.⁵ Acquiescence does not relate to issue as to whether Phelps-Waters Co. was a transferee of Wisconsin Chemical Co.

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Piedmont Lumber Co.....	12828	14	778
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Pierce-Arrow Motor Car Co.....	893	2	396
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Pike County Coal Corporation ²	7189	4	625
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¹ Estate tax decision.² Acquiescence relates only to issue 1 in decision.

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Pratt, William B., estate of.....	8858	7	621
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¹ Estate tax decision.² Acquiescence relates to all issues except jurisdiction issue.³ Acquiescence relates only to issue 1 in decision.

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¹ Acquiescence relates to issue 1 of decision.² Estate tax decision.

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¹ Acquiescence relates to issues 2, 3, 4, 5, and 6 in decision.² Estate tax decision.³ Estate tax decision; acquiescence relates to issues 2 and 3 of decision.⁴ Acquiescence relates to issue concerning opening inventory at December 1, 1917.

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Scaife, William B., estate of.....	391	1	338
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¹ Estate tax decision; acquiescence relates to issue regarding taxability of proceeds of life insurance in excess of \$40,000 exemption and issue as to bequest of works of art to or for the use of the Catholic Cathedral, St. Louis, Mo.

² Acquiescence does not relate to issue involving "tentative tax" adjustment.

³ Acquiescence relates to affiliation for 1917 and inclusion of Savannah River Lumber Co. in consolidated group for 1918-1921.

⁴ Estate tax decision.

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Seneca Coal Mining Co.....	1049	2	513
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¹ Estate tax decision.² Acquiescence relates to issue as to whether certain income accruing to estate of petitioner's father was taxable income to petitioner.

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Sheane Auto Co., W. W.-----	5187	9	1317
Sheen, Jessie G.-----	543	6	114
Sheet Metal Construction Co., Inc.-----	5089	3	461
Sheffield Dentifrice Co. ¹ -----	11814	13	877
Sheldon Manufacturing Co., H.-----	12836	13	1296
Shelton et al., Charles B., executors ² -----	2161	3	809
Shepard, Stuart G.-----	17132	15	627
Sheridan Meat Co.-----	5493	10	211
Sheridan, Thomas F.-----	13698	4	1299
Sherman Stalter Co.-----	4313	4	23
Sherrod, Archibald.-----	22257	16	622
Sherrod, Henry Lambert.-----	22258	16	622
Sherwood, John W.-----	7748	8	103
Shiner Oil Mill & Manufacturing Co.-----	2875	11	805
Shipowners & Merchants Tugboat Co.-----	3955	4	403
Shope Brick Co.-----	6531	5	1042
Shotter, S. O. and Isabel, executors-----	3134	2	912
Shotter, S. P., deceased, estate of-----	3134	2	912
Shulthis, A. W., deceased, estate of-----	1827	2	1253
Shure Co., N.-----	3655	4	1181
Shutter, Marion D.-----	1316	2	23
Shuttleworth, Wollny Co., Inc.-----	1362	5	76
Sibley et al., John R., executors-----	24921	16	915
Sibley, Rufus A., estate of-----	24921	16	915
Sickles, Mrs. A.-----	10430	14	1259
Silk, Mrs. W. W.-----	10864	7	1256
Silk, W. W.-----	10864	7	1256
Silver & Co., Inc., William-----	9708	10	1329
Silverman, Alexander-----	10389	6	1328
Simmons Co.-----	1927	8	631
Simon, H. S.-----	4912	4	1078
Simon, Kate M.-----	9993	10	1186
Simonds Co., C. H.-----	267	1	105
Simons, jr., and wife, James A.-----	5329	5	480
Simons Brick Co. ³ -----	13973 24509 27247	14	878
Sinsheimer, Sidney W.-----	11068	7	1099
Skinker et al., Isabella N., executrices ² -----	11155	13	846
Skinker, Thomas K., estate of ² -----	11155	13	846
Slater, Chas. W.-----	4134	5	804
Slater, H. N., trust-----	8191	9	521
Slattery, Stephen J.-----	9312	9	1123
Sline, John T.-----	6752	9	1222
Smith, Bert K.-----	5329	5	480
Smith, Mrs. Bert K.-----	5329	5	480
Smith, Mrs. D. Sydney ⁴ -----	3262	4	385
Smith, Francis E.-----	1020	1	868
Smith, Harry A., executor ² -----	3098	6	341
Smith, Harry A. P.-----	2552	7	293
Smith, Theodore H.-----	1054	9	57
Smith, Walter T.-----	4841	4	397
Smith Insurance Service, Inc.-----	10901	9	284
Smith & Son Co., Lee S.-----	3328	3	343
Smith Machine Co., H. B.-----	7519	7	525
Smythe, Ernest E., estate of-----	12198	14	931

¹ Acquiescence relates to allocation of tax in consolidated return.² Estate tax decision.³ Acquiescence does not relate to contribution to the All Year Club.⁴ Revokes nonacquiescence published in Cumulative Bulletin VI-1 at page 8.

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Snyder, William J.-----	13186	11	807
Solof, J. W.-----	482	1	776
Solomon, Harry-----	20112	15	419
Somers Lumber Co.-----	2401	2	106
Sonenblick, David-----	3665	4	986
Sonora Bank & Trust Co.-----	7838	7	66
Sooy, Charles H.-----	2882	10	493
South Chicago Drug Co.-----	15157	13	1374
South Euclid Savings & Loan Co.-----	19508	14	1079
Southack, Augusta G., estate of-----	6359	3	1063
Southern Feed Co.-----	13587	6	736
Southern Press Cloth Mfg. Co.-----	13004	10	303
Southern Sand & Gravel Co., Inc.-----	6603	5	879
Spalding, Katherine A.-----	7302	7	588
Spang-Chalfant & Co., Inc.-----	10469	9	858
Speizer, Lena-----	2389	3	413
Spencer, Marion Parsons-----	22194	11	437
Spencer Lumber Co. et al., A. B.-----	7639	10	452
Sphar Brick Co.-----	2086	2	946
Spofford, Hannah M., administratrix of estate of Lucy M. Mills ¹ -----	1028	3	1016
Sporborg, William D., administrator-----	7914	8	1272
Sprague, Elizabeth S.-----	6740	8	173
Sprague Tire & Rubber Co.-----	4717	11	610
Spring Brook Ice Co.-----	12862	12	433
Springdale Cemetery Association-----	4169	3	223
Sprinkle, James L., estate of-----	10401	12	456
Squier, J. Bentley-----	12078	13	1223
Stafford, William F.-----	14313	14	1199
Stafford-Lowdon Co.-----	9088	7	1121
Staley, J. A.-----	6435	9	932
Staley, Wilmer C.-----	10750	9	1038
Stamey-Mackey Construction Co.-----	1271	4	383
Standard Brewery, Inc.-----	{ 10226 10492 }	10	374
Standard Gas Products Co.-----	9843	5	1221
Standard Marine Insurance Co., Ltd.-----	4822	4	853
Standard Refractories Co.-----	{ 3617 3618 }	6	24
Standard Silk Dyeing Co.-----	11694	9	648
Standifer Construction Corporation, G. M.-----	5550	4	525
Stanfield, Theodore-----	{ 3076 4056 }	8	787
Stanley, James T.-----	17323	15	158
Stanley Insulating Co.-----	2983	2	967
Stapley Co., Inc., O. S.-----	7685	13	557
Star Porcelain Co.-----	5002	4	989
Starck, Philip A., estate of ¹ -----	4051	3	514
Starck, Philip T., executor estate of Philip A. Starck ¹ -----	4051	3	514
Stark, Arthur L., estate of ¹ -----	10587	8	1150
Stark Brick Co.-----	12582	12	667
Starr, C. L.-----	12739	9	886
Starr, Howard W.-----	101	1	681
Starrett, Paul-----	6557	4	398

¹ Estate tax decision.

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Sterling Realty Co.....	6333	8	1000
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Stern, Louis.....	19376	5	870
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Strauss, David, estate of ¹	3877	9	1212
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Strong, Hewat & Co., Inc.....	5069	3	1035
Strong, J. E.....	1909	6	417
Strong, Stella.....	1909	6	417
Strother Lumber Co., G. F.....	15235	10	1174
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Stumer, Lois M.....	904	2	19
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Sugar Run Coal Mining Co.....	9236	11	587
Sugarland Industries.....	25063	15	1265
Suhr, Charles L.....	6406	4	1198
Sullivan Granite Construction Co.....	8790	6	703
Summit Wholesale Grocery Co.....	676	1	1040
Sumpter Valley Ry. Co.....	13145	10	1325
Sumter Coca-Cola Bottling Co.....	9079	7	890
Sunflower Packing Corporation.....	531	2	1104
Sunnyside Coal & Coke Co. ²	9442	9	984
Sunshine Cloak & Suit Co.....	11810	16	540
Superheater Co.....	8383	12	5
Superior Engraving Co.....	7949	8	861
	17814		
Superior Motor Parts Co. ²	10348	8	407

¹ Estate tax decision.² Acquiescence relates to second issue of decision.

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Swartz & Co., Inc., A. R.....	3688	5	264
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Sweeney, Jessie Gair, executrix ¹	6322	15	1287
Sweeney & James Co.....	{ 10266 19783 }	10	966
Sweet, Gertrude H.....	9240	8	404
Sweeten, P. P.....	4331	3	37
Swinehart Tire & Rubber Co.....	1436	2	223
Sydeco Photoplay Corporation.....	10221	7	445
Sylvan Electric Bath, Inc.....	7411	5	1293
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Tait, James ²	13908	11	979
Takamine Laboratory, Inc.....	3199	7	963
Talcott, Henrietta E., estate of ¹	16136	15	1025
Talcott et al., J. Frederick, executors ¹	16136	15	1025
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Taylor, P. L.....	10020	11	441
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Texarkana Cotton Oil Co., Inc.....	1888	1	1142
Texas Chemical Co.....	6360	11	390
Theis, jr., George.....	3958	3	1030
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¹ Estate tax decision.² Acquiescence relates to issue as to whether the income realized under agreements of December 14, 1918, is taxable in proportionate amounts to the several petitioners or whether such proportionate amounts are taxable one-half to the petitioners and one-half to their respective wives.

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Thorn, Susan K., estate of ² -----	18234	16	181
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315 West 97th Street Realty Co., Inc.-----	9898	10	368
Threefoot, K., estate of-----	521	9	499
Tibbs, William F.-----	21647	16	68
Tietz, Louise C., administratrix-----	9314	9	1123
Tietz, Robert M., estate of-----	9314	9	1123
Tift, Laver & Co., Inc.-----	12456	12	481
Tilford, Henry Morgan, deceased, estate of-----	3286	3	884
Tilt, C. A.-----	{ 18041 }	14	437
	19963		
Tilton, S. U., estate of-----	6378	8	914
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Title Insurance & Trust Co.-----	9195	11	288
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	2450		
Titusville Trust Co., executor-----	1508	3	868
Tivoli Theatre Co.-----	7452	6	610
Toccoa Furniture Co.-----	14429	12	804
Todd, C. Lee-----	1022	1	868
Todd, George W.-----	2959	3	327
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Tomfohrde, Andreas, estate of-----	9615	13	150
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Tonawanda Power Co.-----	3870		
	{ 6506 }	3	521
Topeka Tent & Awning Co.-----	3440		
Tower Co., A. J.-----	11402	16	101
Towns Hospital, Charles B.-----	2317	2	701
Townsend, Anna M. ¹ -----	20046	12	1343
Townsend, V. Ray ¹ -----	20047	12	1343
Townsend Lumber Co.-----	830	1	894
Toxaway Tanning Co.-----	{ 5084 }	5	371
	5694		
Trace Fork Mining Co.-----	16030	15	872
Tracy, Thomas H.-----	15152	15	1107
Transatlantic Clock & Watch Co.-----	4897	3	1064
Trathen, Mrs. J. Ries-----	8270	8	981
Treat Hardware Corporation-----	4524	6	768
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Tri County Light & Power Co.-----	2710	2	1165
Troost Avenue Cemetery Association-----	1114	4	1169
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Troy Manufacturing Co.-----	6585	7	119
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Tucker, E. G.-----	7863	13	932
Tucker, Genevieve-----	3470	2	796
Tunnelton Bank-----	11433	12	187
Turl Iron & Car Co., Inc.-----	9255	9	740

¹ Estate tax decision.² Estate tax decision; acquiescence relates to issue 1 of decision.³ Acquiescence does not relate to "tentative tax" issue.

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United States Refractories Corporation ³	5642	9	671
United States Tool Co.....	4650	3	492
United States Trust Co. of New York et al., executors ¹	7856	9	514
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United States Trust Co. of New York, executor ¹	15069	15	1366
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Universal Steel Co.....	26612	11	405
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¹ Estate tax decision.² Acquiescence relates to issue as to losses.³ Acquiescence relates to all issues except issue with respect to question of allowance of amortization in 1918 of costs incurred in 1919.

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Wallace Barnes Co.....	3653	10	1304
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¹ Estate tax decision; acquiescence relates to trusts of 1912, 1919, and 1921.² Estate tax decision.³ Acquiescence in so far as decision determines that City Gas Co. of Norfolk and Virginia Railway & Power Co. were affiliated with each other.

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Watterson Hotel Co.....	5792	13	943
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Webb, Stuart W.....	5591	5	366
Weber-Bunke-Lange Coal Co.....	9146	11	503
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Weeks Co., L. S.....	2604	6	300
Weill-Jamison Co., Inc.....	9645	13	1342
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Weingarten, David, estate of ³	10433	13	249
Weingarten, Melville D., executor ³	10433	13	249
Weis, A. W. D.....	11917	13	1284
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¹ Acquiescence does not relate to that part of decision involving application of the Ayers decision (1 B. T. A., 1135).

² Revokes nonacquiescence published in Cumulative Bulletin V-2, page 4.

³ Estate tax decision.

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Westergren, Inc., M. F.....	2723	5	1185
West Point Investment Co.....	300	1	436
West 28th Street Corporation.....	6032	4	147
West Virginia Coal Co.....	14790	16	378
Westermann & Pagano, Inc.....	3763	2	1308
Western American Oil Co. ¹	14452	10	17
Western Maryland Ry. Co. ²	6475	12	889
Western Star Milling Co.....	2852	5	109
Western Wheeled Scraper Co. ³	12001	14	496
Western Zinc Oxide Co.....	8604	7	972
Westland Co.....	19755	15	553
Wharton et al., Gerald A., executors ⁴	26439	13	302
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Wheary, George H.....	4799	5	829
Wheatley, James A. ⁵	9665	8	1246
Wheeler, D. E.....	21093	16	96
When Clothing Co.....	428	1	973
White, Asa L., estate of ⁴	12768	15	470
White, jr., James.....	5622	4	995
White, Julia A.....	5623	4	995
White, Robert P.....	5554	4	995
White et al., W. T., executors ⁴	12768	15	470
White Trust No. 1, R. H. and K. K.....	28141	15	1410
Whitehead, C. P.....	23948	11	461
Whitehouse Leather Products Co., Inc.....	10673	12	714
Whiteley, Burt H., estate of.....	8472	10	1385
Whiting, C. L., Inc.....	11046	7	1170
Whitman, Clarence.....	14110	16	197
Whitman, Nathaniel, deceased, estate of ⁶	1399	3	97
Whitman & Sons, Inc., Clarence.....	10316 15388	11	1192
Whitmeyer, Ella.....	3090	6	472
Whitmore, Alvah P.....	7086	5	1274
Whitson, Thomas J.....	3478	2	747
Whorton et al., Glen C., executors ⁴	3094	7	771
Whybrow, Clarence.....	609	1	725
Wickens Co.....	16476	16	968
Wickwire, Theodore H., estate of.....	5574	10	102
Wickwire et al., Theodore H., jr., executors.....	5574	10	102
Wiedemann Brewing Co., George.....	7955	4	664
Wiess, H. C.....	7615	7	467
Wiess, Olga.....	7637	7	467
Wigginton, George P.....	11425	9	1030
Wilbur, Loyd H.....	5636 10611	5	597
Wildermann Co., C.....	8289	8	771

¹ Acquiescence relates to second issue of decision.² Acquiescence relates to reduction by 2 per cent of income tax of taxpayer for calendar years 1918 and 1919.³ Acquiescence does not relate to that portion of decision which holds that section 284(c) of the Revenue Act of 1926 is applicable to the case.⁴ Estate tax decision.⁵ Acquiescence relates to item (2) of decision.⁶ Nonacquiescence notice in this case, published in Cumulative Bulletin IV-2, page 6, recalled.

ACQUIESCENCES—Continued.

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Wilhite et al., Hugh, executors and trustees-----	7462	11	85
Wilkins & Lange-----	10649	15	1183
	29037		
Wilkes, J. Frank-----	12024	11	717
Wilkes, J. Renwick-----	12023	11	717
Wilkes-Barre Lace Manufacturing Co.-----	452	1	467
Wilkins, L. H.-----	4208	6	593
Williams, Harry E.-----	4207	6	593
Williams, Robert W., executor of estate of Ellen C. Bonaparte-----	1652	1	1101
Williams Foundry & Machine Co.-----	10190	15	297
Williams Steamship Co.-----	8725	7	451
Williamson, Alexander B.-----	2343	2	747
Williamson & Rauers Co.-----	11292	12	476
Williamson Milling Co.-----	1042	5	814
Willis, Mrs. W. T.-----	15679	7	1256
Willis, W. T.-----	15679	7	1256
Wilson Bros. & Co.-----	8460	7	820
Wilson, Charles Scotto, estate of ¹ -----	4909	5	615
Wilson, F. H.-----	6911	12	403
Wilson, Fannie L., executrix ¹ -----	4909	5	615
Wilson Furniture Co.-----	11317	10	1294
Wilson, J. H.-----	18157	15	536
Winship, Charles N.-----	6754	10	237
Winter Garden, Inc.-----	8246	10	71
Wisconsin Hydro-Electric Co.-----	9601	10	933
Wolf, J. H. G.-----	2970	8	1121
Wolf Manufacturing Co.-----	8626	10	1161
Wolfe, Emma S., estate of ² -----	16149	15	835
Wolfe, Russel, executor ² -----	16149	15	835
Wolfe Co., Udolpho.-----	16010	15	485
Wolferman, Fred, executor ² -----	11291	10	285
Wolferman, Louis, estate of ³ -----	11291	10	285
Women's Apparel Co.-----	4001	8	477
Wood Bros. Thresher Co.-----	5877	4	43
Wood, Kay.-----	13014	11	740
Wood, T. J.-----	11029	9	1206
Woodliffe Silk Mills.-----	559	1	715
Woodruff Lumber Co.-----	7262	6	515
Woodruff & Son, John T.-----	6864	6	535
Woods & Sons Co., Joseph W.-----	9156	8	705
Woods Theatre Co., A. H.-----	11067	12	827
Woods, William Stone, estate of.-----	7462	11	85
Worcester Bank & Trust Co. et al., administrators.-----	14230	13	630
Wright, Herbert N., estate of.-----	14230	13	630
Wright, O. A., estate of.-----	12096	12	999
Wright, Pearl Ross, administratrix.-----	12096	12	999
Wright, W. Q.-----	4270	10	806
Wright's Automatic Tobacco Packing Machine Co.-----	1837	1	1260
Wyatt et al., Elizabeth C. R., executors.-----	17698	10	763
Wyman & Co., C. C.-----	10676	8	408
Wyoming Tie & Timber Co.-----	21370	9	1143
	24574		

¹ Estate tax decision.² Acquiescence relates to deduction of Pennsylvania and New Jersey inheritance taxes.³ Estate tax decision; acquiescence relates to first issue of decision.

ACQUIESCENCES—Continued.

Taxpayer.	Docket No.	Board of Tax Appeals.	
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Y.			
Yahola Sand & Gravel Co.....	2281	6	820
Yakima Hop Co.....	9527	8	441
Yale Brevda Paper Box Manufacturing Co.....	3353	2	900
Yellow Poplar Lumber Co.....	9894	12	1050
Yoder, Edward E.....	3220	3	1180
Yokohama Ki-Ito Kwaisha, Ltd.....	2653	5	1248
Yost & Herrell.....	2085	2	745
Young, I. F., estate of.....	7440	5	245
Young, May S., executrix ¹	3847	3	193
Young, Minal E., executor.....	4720	6	472
Young, S. Marsh.....	1839	2	457
Youngstown Bread Co.....	1333	2	402
Yunker Bros., Inc.....	5522	8	333
Yow, Frances White.....	5555	4	995
Z.			
Zeigen, Frederick, H.....	6426	10	844
Zenith Milling Co.....	5454	8	1279
Ziegler, jr., William.....	123	1	186
Zimmerman, E. W.....	2513	5	314
Zimmerman, Jennie E.....	2145	2	667
Zouri Drawn Metals Co.....	4908	8	853

¹ Nonacquiescence in this case, published in Cumulative Bulletin IV-2, page 6, is recalled.

The Commissioner does NOT acquiesce in the following decisions of the United States Board of Tax Appeals:

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A.			
Aitkin, A. King.....	13189	12	692
All America Cables, Inc. ¹	9092	10	213
Alling & Cory Co. ²	6606	7	574
Alsop, Edward B., estate of ³	6519	7	848
Alsop, Edward H., executor ³	6519	7	848
Amalgamated Sugar Co.....	6439	4	568
American Express Co.....	350	2	498
American Feature Film Co ¹	4437	11	1271
American Leather Products Co.....	10619	7	1043
American Seating Co. ⁴	4772	4	649
American Seating Co. ⁵	14676	14	328
American Steel Co.....	669	1	839
Ankeny, John D., executor ⁶	8904	9	1302
Ankeny, Levi, estate of ⁶	8904	9	1302

¹ Nonacquiescence relates to issue as to tentative tax.

² Nonacquiescence relates to third issue.

³ Estate tax decision; nonacquiescence relates only to 1917 trust.

⁴ Nonacquiescence in so far as it relates to inclusion in invested capital of the sum of \$198,716.37.

⁵ Nonacquiescence relates to second and third issues of decision.

⁶ Estate tax decision.

NONACQUIESCENCES—Continued.

Taxpayer.	Docket No.	Board of Tax Appeals.	
		Volume.	Page.
Archbold, John F., executor ¹ -----	8629	8	919
Arnold et al., John B. ² -----	20887	14	954
	20888		
	20889		
	20890		
Athens Brick & Tile Co.-----	12926	14	1359
	19339		
Atlantic Coast Line R. R. Co. ³ -----	10983	9	1193
Atlas Tack Co. ⁴ -----	11497	12	3
Audubon Park Realty Co.-----	9629	6	875
Auld, J. W.-----	12169	13	1213
Ayers & Co., L. S. ⁵ -----	1217	1	1135
B.			
Ball et al., Walter J., coexecutors-----	6858	8	180
Bamberg Cotton Mills Co.-----	9445	8	1236
	10104		
Bancker, jr., E. A.-----	18617	11	420
Bank of Duplin-----	12950	12	652
Bank of Italy, San Francisco, Calif-----	15810	13	1226
Bank of Topeka-----	18850	15	1301
Barnes et al., Charles G., executors-----	8624	8	360
	8625		
Barnes, jr., John, estate of-----	5266	7	924
Barnes, Joseph-----	9577	7	924
Barnes, Joseph, administrator-----	5266	7	924
Bartlett et al., Philip C. K., executors-----	23581	16	510
Bartlett, Herschel, estate of-----	23581	16	510
Barton, Mary L., trustee-----	12934	5	1008
Barton, Otis, estate of-----	12934	5	1008
Bates, E. W. (Mrs.)-----	18611	11	420
Beacon Coal Co. ⁶ -----	11894	9	280
Behlow Estate Co.-----	12670	12	1365
Belmont Iron Works-----	10454	6	722
Belowsky, Morris-----	9656	7	424
Belt Railway Co. of Chicago ⁷ -----	4289	9	304
Benedict, James A., estate of ⁸ -----	21621	16	438
Benson Lumber Co.-----	19519	9	593
Benson Timber Co.-----	16311	9	593
Berger, Mathilda W.-----	6110	10	747
Berger, Walter J.-----	6111	10	747
Berks Foundry & Manufacturing Co.-----	6998	5	756
Berlin Dye Works-----	15714	13	1354
Best Steel Castings Co.-----	8326	6	274
Biggs, sr., J. E.-----	15255	15	1092
Bingham, Robert W.-----	8823	8	603
Blair, W. A., estate of ⁸ -----	2440	4	959
Blair Co., J. C.-----	7147	11	673
Blaney, Edith H.-----	10613	13	1315

¹ Estate tax decision; nonacquiescence relates to first and second issues of decision.² Nonacquiescence relates to fraud penalties.³ Nonacquiescence relates to second issue of decision.⁴ Nonacquiescence relates to issue involving reduction of invested capital on account of dividend payment.⁵ This notice, which was originally published in Bulletin IV-41, page 1, was republished in Cumulative Bulletin V-1, page 6, for the reason that the case was erroneously included in the list of cases acquiesced in, published in Cumulative Bulletin IV-2, page 1.⁶ Nonacquiescence relates to first issue of decision.⁷ Nonacquiescence relates to issues involving Federal income taxes added to income for 1917, 1918, and 1919, in respect of which petitioner was entitled to be reimbursed by its tenant companies.⁸ Estate tax decision.

NONACQUIESCENCES—Continued.

Taxpayer.	Docket No.	Board of Tax Appeals.	
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Block, E. Bates.....	18792	11	420
Block, E. Bates, executor.....	18793	11	420
Block, Frank E., estate of.....	18793	11	420
Block & Kohner Mercantile Co.....	4576	4	673
Blossburg Mercantile Co.....	2880	4	690
Blumberg Bros. Co. ¹	12137	12	1021
Blydenburgh, Vail.....	9921	5	834
Boger & Crawford, Inc.....	14745	13	835
Bonwit Teller & Co.....	26037	10	1300
Bourne, Emily H., estate of ²	7883	8	582
Boyne City Lumber Co.....	4635	7	36
Brackenridge, George W., estate of.....	6515	11	148
Brawner, Alexander Harrison, estate of ³	16092	15	1122
Brawner, Frances, executrix ³	16092	15	1122
Brenneman, David E.....	8361	10	544
Brenneman, E. L. E.....	8323	10	544
Brenneman, Verna L.....	8324	10	544
Briant, E. S., administrator.....	8860	6	651
Brier Hill Collieries ⁴	11406 19365 28186 13557	12	500
Brittingham, Juan F.....	16535 18435	13	375
Brittingham, Juan G.....	18535	13	375
Bronson et al., James D., trustees ⁵	7702	7	127
Brown & Co., M.....	24864	9	753
Bryant & Stratton Commercial School, Inc.....	43	1	32
Buck, Truman, estate of ³	17660	13	415
Bullock, H. E.....	28612	16	451
Burges, Richard F.....	25908	17	275
Burke Electric Co. ⁶	1697	5	553
Burton, Lawrence Elmer.....	2689	5	99
Byck, W. S.....	2260	4	842
Byers, Howard Webster.....	10319	8	1191
C.			
Cadwalader, John, estate of.....	13296	15	1
Cadwalader, jr., et al., John, executors.....	13296	15	1
California Brewing Association ⁸	3903	5	347
Callaway, Fuller E.....	2264	4	842
Cambridge Ice Co.....	7282	9	156
Campbell, Archer Maynard.....	18320	6	60
Campbell, H. L.....	18321	8	1076
Campbell Co., John F.....	19591	15	458
Capitol Hotel Co. ⁷	6610 7134	4	441
Carbo Petroleum Co. ⁸	9524	12	166
Carey, C. W. ⁹	2432	6	539

¹ Nonacquiescence relates to first issue of decision.² Nonacquiescence does not relate to deductibility of New York inheritance tax.³ Estate tax decision.⁴ Nonacquiescence relates to depletion issue.⁵ Nonacquiescence relates to issues 1 and 2, and issue 5 as to patent group No. 1.⁶ Nonacquiescence relates to question of affiliation as to the companies included in the "units."⁷ Nonacquiescence relates only to that part of decision which relates to application of the Ayers decision (1 B. T. A., 1135).⁸ Nonacquiescence relates to fourth issue of decision.⁹ Nonacquiescence relates to issues 1 and 3 in decision.

NONACQUIESCENCES—Continued.

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Carney Coal Co. ¹	5562	10	1397
	8496		
Carruthers, Mabel G.....	25741	16	515
Central Savings Bank ²	5006	10	1408
Century Music Publishing Co.....	12840	12	647
Chadbourn & Moore.....	17066	16	961
Chapin, W. E.....	2267	4	842
Chapin Construction Co.....	3200	3	25
Chicago Portrait Co.....	21396	16	1129
City Button Works.....	15826	16	839
Clark, James B.....	11918	12	615
Cleveland, Painesville & Ashtabula R. R. Co.....	4927	4	637
Cleveland, Painesville & Eastern R. R. Co.....	4927	4	637
Cline, Mrs. Ella Pipes ³	6929	15	934
Cline, W. D. ³	6930	15	934
Clingan, Margaretta T.....	4227	6	8
Cohn & Sons Co., M. ⁴	7361	9	87
	9238		
Collins-McCarthy Candy Co.....	4302	4	1280
Colmer-Green Lumber Co. ⁵	20916	12	256
Connecticut & Passumpsic Rivers R. R. Co. ⁶	8424	8	492
	9100		
Connell, G. H.....	18405	15	1309
Connell, Mrs. G. H.....	18406	15	1311
Connelley, C. U.....	3363	4	359
Conover Co., S. A.....	3926	6	679
Consolidated Textile Corporation.....	15983	16	178
Conway, J. W.....	2263	4	842
Coon Valley State Bank ⁷	11352	13	132
Corbett & Stuart.....	11855	11	540
Cornelius Lumber Co.....	4273	5	215
Crabtree Co., E. B.....	5889	5	732
Crocker Co., H. S.....	4581	5	537
Cross Mountain Coal Co.....	1219	2	537
Crown Potteries Co.....	10043	12	1412
Cunningham-Beckemeier Supply Co.....	15838	14	992
Curran, Maurice J.....	793	5	180
D.			
D'Aramon, Henrietta.....	10644	7	600
Daily Pantagraph, Inc. ⁸	4126	9	1173
Daily Record Co.....	12058	13	458
Daniel, Charles R.....	20037	16	925
	22044		
Daniel, S. B.....	20036	16	925
Darby, Rufus C.....	2265	4	842

¹ Nonacquiescence relates to issue No. 1 in so far as it relates to fiscal year ended May 31, 1919.² Nonacquiescence relates to obsolescence issue.³ Nonacquiescence relates to deduction in 1919 of commissions incurred in sale of property; also decision as to fourth issue.⁴ Nonacquiescence relates to 25 per cent penalty for failure to file a return.⁵ Nonacquiescence relates to issue whether the consolidated return for 1919 started the running of the statute of limitations as to the Colmer-Green Lumber Co.⁶ Nonacquiescence relates to first issue of decision in so far as it holds that the income was not realized until the year in which the taxes became due and payable; and also to the second issue of decision.⁷ Nonacquiescence relates to issue involving loss of \$1,000 on Galloway note.⁸ Nonacquiescence relates only to issues involving reducing invested capital by reducing current earnings available for dividends by tax accrued for current year.

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Davis, Oscar-----	18625	11	420
Day, Henry M.-----	30198	12	161
De Forest, Julia N.-----	5857	4	1059
Deinert, sr., Oscar-----	6937	11	651
Deltos Grass Rug Co. ¹ -----	6926	7	811
Dennett, Fred-----	11498	7	1173
DeReuter, Ronald-----	6243	7	600
Derschug, John N. ² -----	18064	15	306
Desmond's, Inc.-----	14465	15	738
Dickerman & Englis, Inc.-----	4928	4	447
Dillon, John P.-----	10985	9	177
Doehne, George, estate of-----	9344	6	1071
Don, Harriet M., estate of ³ -----	5594	9	450
Dowling, Mary M.-----	2394	6	976
Duggan, Hanna, estate of ⁴ -----	4706	8	482
Duggan, James, executor ⁴ -----	4706	8	482
Duhme, Ophelia, estate of-----	6858	8	180
Duncan Coal Co., W. G.-----	12347	13	672
Dunson Mills ⁵ -----	17019	10	1150
Dustin, Annie M., estate of ⁶ -----	8629	8	919
Dwight & Lloyd Sintering Co.-----	120	1	179
E.			
Edgar Co., James-----	14606	16	120
Elkin, Dr. Wm. S.-----	18629	11	420
Emery et al., Earle C., executors-----	9766	9	328
Emery, jr., Lewis, estate of-----	9766	9	328
Esperson, Niels, estate of ⁴ -----	7071	11	1283
Esperson, Mrs. Niels (Mellie), executrix ⁴ -----	7071	11	1283
Excelsior-Leader Laundry Co.-----	9221	8	183
Extension Oil Co.-----	28764	16	1028
F.			
Fane, Evelyn Francis-----	16725	15	1332
Farmers Deposit National Bank and Affiliated Banks-----	6220	5	520
Farmers Loan & Trust Co., executor ⁷ -----	18234	16	181
Farmers' Loan & Trust Co., executor ⁴ -----	21621	16	438
Fidelity Trust Co. ⁸ -----	13638	13	109
Field, Marshall-----	11840	15	718
First National Bank of Duluth, administrator-----	{ 18502 18503 }	13	1096
First National Bank, Fresno, Calif.-----	15811	13	1226
First State Bank of Brackettville, Tex.-----	12876	9	975
First State Bank of Weimar-----	{ 12657 16011 }	10	396
First Trust & Savings Bank-----	11746	11	1034
Fitzgerald, Mary A.-----	810	5	178
Foster, Alice Fisher-----	10126	7	1137
Foster, James F., estate of ⁴ -----	11493	13	496

¹ Nonacquiescence relates to second issue in decision.² Nonacquiescence relates to issue 1 of decision.³ Nonacquiescence does not relate to deductibility of New York inheritance tax.⁴ Estate tax decision.⁵ Nonacquiescence relates to issue regarding jurisdiction.⁶ Estate tax decision; nonacquiescence relates to first and second issues of decision.⁷ Estate tax decision; nonacquiescence relates to issue 2 of decision.⁸ Nonacquiescence relates to issue concerning invested capital for 1920 and 1921.

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Francis, jr., Francis-----	16724	15	1332
Frank, William G., administrator-----	9344	6	1071
Franklin et al., Thomas H., executors and trustees-----	6515	11	148
Fresh Pond Ice Co.-----	7282	9	156
Fuller, jr., James W.-----	3068	7	28
G.			
Gallum, Albert F., trustee-----	6101	10	747
Garber, B. A. ² -----	3708	11	979
	14097		
Garber, M. C. ² -----	3710	11	979
	13909		
Gardner Governor Co. ³ -----	321	5	70
Garneau Co., Inc., Joseph-----	40	1	75
General Manifold & Printing Co.-----	14577	12	436
Georgia Car & Locomotive Co. ¹ -----	3131	2	986
Gibson, Kate Viola, estate of ⁴ -----	7402	7	1144
Gillette, Katharine K.-----	18754	14	580
Girard Trust Co., executor ⁴ -----	11298	10	1100
Girard Trust Co. et al., executors-----	23208	16	308
Glenn, Thomas K.-----	2262	4	842
Goddard, John N.-----	18621	11	420
Gong Bell Manufacturing Co.-----	17584	15	152
Gonzolus Creek Oil Co. (dissolved), trustees for creditors of-----	13393	12	310
Goodrum, jr., J. J.-----	18613	11	420
Gordon, Henry J.-----	13838	12	1191
Grandin, Florence-----	25740	16	515
Grandin, George W., trustee-----	25742	16	515
Grandin, Henry B.-----	25742	16	515
Graves et al., A. H., committee for creditors of Whittaker & Bacon-----	22631	12	124
Great Bear Spring Co. ⁵ -----	10489	12	383
Great Northern Ry. Co. ⁶ -----	8433	8	225
	11850		
Greene et al., Richard T.,*trustees-----	23973	15	401
Greck Condensed Buttermilk Co.-----	3691	7	79
Greylock Mills ⁷ -----	11926	9	1281
Guarantee Construction Co. ⁸ -----	1828	2	1145
	1848		
Guild Co., Inc., J. H.-----	8741	11	914
	9276	12	1244
Gulf States Steel Co.-----	18358		
	18359	14	393
Gwin, Earl S.-----	17983		

¹ Nonacquiescence relates to third issue of decision.² Nonacquiescence relates to issue as to whether the agreements of December 14, 1918, and the discharge thereof were productive of income taxable for the years involved, and, if so, to what extent.³ Nonacquiescence relates only to that part of decision which relates to application of the Ayers decision (1 B. T. A., 1135).⁴ Estate tax decision.⁵ Nonacquiescence does not relate to depreciation and obsolescence adjustments.⁶ Nonacquiescence relates to issue involving the question whether the company should accrue as income in the taxable years interest earned but not paid in those years on obligations of other corporations owned by it.⁷ Nonacquiescence in decision in so far as the Board holds that it has jurisdiction to determine the overpayment for 1917.⁸ Nonacquiescence relates to second issue of decision.

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Haller, Mary ¹ -----	{ 14063 25751	14	488
Hamilton, Harris & Co.-----	{ 4170 15687	12	735
Hamlet Ice Co.-----	25516	16	433
Hanlon, Mary E.-----	27251	16	809
Hannibal Missouri Land Co.-----	9084	9	1072
Harbour-Longmire Co.-----	6905	7	314
Harlan & Co., O. A.-----	1374	1	1027
Harriet Cotton Mills.-----	6228	5	734
Harris, Elizabeth H.-----	11820	11	420
Harris Oil Co., C. C.-----	8011	13	937
Harry Co., S. J.-----	1644	4	211
Hartmann, Charles.-----	18930	14	146
Haskell & Barker Car Co.-----	7009	9	1087
Hass, E. S. ² -----	14817	13	1352
Hatzel & Buehler, Inc. ³ -----	{ 9501 11454	10	993
Hawkins, Frank.-----	2572	4	842
Haynes, Elwood, estate of.-----	11724	13	796
Heineman Lumber Co. ⁴ -----	10175	11	1229
Heinrich, Samuel G., estate of.-----	2420	2	406
Hemlock Hollow Coal & Coke Co.-----	8837	10	1176
Henaghan, Elizabeth.-----	27252	16	809
Hendricks, Harmon W.-----	4554	4	1257
Henn, A. W., trustee.-----	4303	8	190
Hepburn, C. Fisher, estate of ⁵ -----	9690	11	1386
Hernance, H. P.-----	11192	11	420
Hershey Manufacturing Co.-----	{ 28862 32108	14	867
Herzog, Philip W.-----	6245	10	747
Hess Bros. ⁶ -----	8039	7	729
Hewitt Rubber Co.-----	325	1	424
Hickey, J. E.-----	19107	11	420
Higginbotham-Bailey-Logan Co. ⁷ -----	4691	8	566
Hinman, Thos. P.-----	18615	11	420
Hirsch & Co., Adolph.-----	3230	7	707
Hirsch-Weis Manufacturing Co.-----	30494	14	796
Hof Brau Co., The ⁸ -----	6134	6	442
Hoffman, Isabella C., estate of ⁹ -----	5338	3	1361
Hoffman et al., Meyer C., executors ⁵ -----			
Hoffmann, Frederick H.-----	3361	3	964
Holifield, Mary D. Moore.-----	10089	7	1302
Holyoke & Westfield R. R. Co.-----	8425	9	127
Home Builders Shipping Association.-----	7044	8	903
Home Laundry Co.-----	6047	4	45
Houston Belt & Terminal Ry. Co. ⁸ -----	8494	6	1364
Howard Co., J. W. & A. P.-----	19863	15	1096
Hulbert, Edmund D., estate of ⁹ -----	11204	12	818
Humphreys, E. C.-----	4069	9	656

¹ Nonacquiescence relates to issue concerning deductibility of charitable contributions.² Nonacquiescence relates to first issue of decision.³ Nonacquiescence relates to third issue in decision.⁴ Nonacquiescence relates to issue as to tentative tax.⁵ Estate tax decision.⁶ Nonacquiescence relates to second issue of decision.⁷ Nonacquiescence relates to first, second, and fourth issues of decision.⁸ Nonacquiescence relates to second and fourth issues of decision.⁹ Estate tax decision; nonacquiescence relates to issue concerning transfer of stock.

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Hunt, J. C.-----	19888	15	1388
Huntington, Annie-----	25807	15	851
Huntington, Wallace-----	25806	15	851
Hupfel Co., Inc., J. Chr. G. ¹ -----	9834	9	944
Hutchins Lumber & Storage Co. ² -----	3307	4	705
Hutchison, Charles ³ -----	8053	13	1187
Hynes, William J.-----	21382	16	1272
I.			
Illinois Merchants Trust Co., executor ⁴ -----	11204	12	818
Illinois Rural Credit Association-----	5058	3	1178
Independent Brewing Co. of Pittsburgh ⁵ -----	3242	4	870
Independent Brick Co.-----	8198	11	862
Indiana Harbor Belt R. R. Co.-----	{ 21550 37661 }	16	279
Indiana Rolling Mills Co.-----	12259	13	1141
Indiana Stove Works ⁶ -----	8148	8	1008
Indianapolis Street Ry. Co.-----	8787	7	397
Individual Towel & Cabinet Service Co.-----	{ 1231 12586 }	5	158
Inglewood Park Cemetery Association-----	3249	6	386
Inman, Edward H.-----	2501	4	842
Interurban Construction Co.-----	{ 7028 2687 }	5	1292
J.			
Jackson, Annette T. ⁷ -----	9001	11	1257
Jackson, George A. ⁷ -----	9002	11	1257
Jackson, Minnie L., estate of ⁸ -----	4219	3	832
Jackson, Willis K. ⁷ -----	9003	11	1257
Jackson & Tindle ⁷ -----	9000	11	1257
James, Arthur Curtiss ⁷ -----	2509	13	764
Jefferson Gas Coal Co.-----	{ 14951 33247 }	16	1135
Johnson et al., Homer S., executors ⁹ -----	9550	11	534
Johnson, Stephen O., estate of ⁹ -----	9550	11	534
Johnston, Mrs. E. V., deceased-----	14355	12	185
Johnston, R. H., heir at law-----	14355	12	185
K.			
Kalb, Louis-----	{ 19421 19422 }	15	865
Keen, Herbert Ide-----	8423	6	275
Keeney, George E., estate of-----	{ 11715 14424 }	15	715
Keeney, Raymond G., executor-----	{ 11715 14424 }	15	715
Keewis Realty Co., Inc. ¹⁰ -----	10489	12	383
Kehota Mining Co.-----	1117	3	885

¹ Nonacquiescence relates to obsolescence issue.² Nonacquiescence relates only to that part of decision which relates to application of the Ayers decision (1 B. T. A., 1135).³ Nonacquiescence relates to deduction of amount expended for "training" to keep in condition for "stunt" acting.⁴ Estate tax decision; nonacquiescence relates to issue concerning transfer of stock.⁵ Nonacquiescence relates only to issue 2 in decision.⁶ Nonacquiescence relates to second issue of decision.⁷ Nonacquiescence relates to tentative tax issue.⁸ Estate tax decision.⁹ Estate tax decision; nonacquiescence relates to trust instruments of 1918 and 1921.¹⁰ Nonacquiescence does not relate to depreciation and obsolescence adjustments.

NONACQUIESCENCES—Continued.

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Kissel, Caroline T. ¹	21788	15	1270
Kistler et al., Florence L., administrators ²	3707	11	979
	11986		
	18061		
Kistler, William F., estate of ²	3707	11	979
	11986		
	18061		
Kistler Land & Improvement Co. ³	12355	9	671
Kittery Realty Co.....	15114	14	569
	34274		
	4004		
Klein, Florence L. ⁴	4005	6	617
	6061		
	6102		
Klyman, E.....	10157	4	832
Kuhn, J. J.....	6753		
Kynett, Harold K.....	18631	11	420
	13190	12	692
L.			
Lancaster et al., John L., receivers.....	9863	9	365
Lancaster Lens Co. ⁵	11603	10	1153
Lawson, John S.....	6108	10	747
Leasing & Building Co.....	14423	16	105
Lee Live Stock Commission Co.....	280	7	532
Lee Shoe Co., Inc., John.....	10061	11	187
Levine Bros. Co., Inc. ⁶	6832	5	689
Ley & Co., Inc., Fred T.....	18168	9	749
Liberty Insurance Bank.....	5070	14	1428
Lieber et al., H. W., executors.....	9720	13	1175
Lightning Creek Oil & Gas Co.....	8584	9	1150
	23204		
	10031		
Lisk Manufacturing Co., Ltd. ⁷	11438	11	179
	19050	15	1048
	20440	15	806
Livezey, F. M.....	24414	8	1029
Lloyd, Ernest E.....	9295	7	1008
Lock, Moore & Co., Ltd.....	14325	14	228
Loetscher, Christian, estate of ⁸	14325	14	228
Loetscher et al., John A., executors ⁸	8465	13	446
Loewenstein Bros. Garment Co.....	23208	16	308
Ludington, Charles H., estate of.....			
M.			
McAvoy Co.....	9216	10	1017
McClung et al., Hu L., executors.....	12468	13	335

¹ Nonacquiescence relates to deduction of aliquot part of cost of improvements to certain property.² Nonacquiescence relates to issue as to whether the agreements of December 14, 1918, and the discharge thereof were productive of income taxable for the years involved, and, if so, to what extent.³ Nonacquiescence relates to issue with respect to question of allowance of amortization in 1918 on costs incurred in 1919.⁴ Nonacquiescence relates to question in decision pertaining to the year 1919.⁵ Nonacquiescence relates to the issue as to whether a return signed by the president and secretary was the return required by statute, the filing of which started the running of the statute of limitations.⁶ Nonacquiescence relates to issue 6 in decision.⁷ Nonacquiescence relates to depreciation issue.⁸ Estate tax decision; nonacquiescence relates to issues involving executors' commissions, attorneys' fees, and miscellaneous administration expenses.

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McCutchen, C. E.....	19819	16	569
McDonough, James B.....	21462	16	556
McGee, Nellie B.....	{ 13292 29938 }	13	1181
McGowin-Foshee Lumber Co. ²	10446	10	961
McMurtrie, Adnah.....	19740	8	1301
McNeill, Robert H. ³	17261	16	479
Magee Furnace Co. ⁴	5600	11	1216
Mahoning Coal R. R. Co.....	2202	4	923
Malley Co., Edward.....	9677	6	462
Mallinckrodt, jr., Edward.....	11031	14	194
Mallinckrodt, sr., Edward ²	1750	4	1112
Malta Temple Association.....	29476	16	408
Manhattan Brewing Co.....	693	6	952
Mann, Franklin P., estate of.....	6101	10	747
Maritime Securities Co. ⁵	324	2	188
Martin Advertising Agency, Inc., Mac.....	8115	11	162
Mathews, John E.....	9583	8	209
Matthiessen, jr., F. W.....	2125	2	921
Mercantile Trust Co., executor ⁶	9528	13	85
Merritt, Thomas A., estate of.....	{ 18502 18503 }	13	1096
Metro Pictures Corporation of New England ⁷	4437	11	1271
Mexican Telegraph Co. ⁷	9093	10	213
Mianus Motor Works, Inc.....	6052	5	435
Middlesex Ice Co. et al.....	7282	9	156
Mid-West Box Co.....	11066	11	1223
Miller, Clarence A.....	14087	13	1081
Moir, Harry C.....	19135	14	23
Moore, L. C. ⁸	{ 3709 13907 }	11	979
Moore Corporation, John C.....	18861	15	1140
Morgan, Brooks.....	18614	11	420
Morrell & Co., John.....	{ 15114 34274 }	14	569
Morsman, jr., Edgar M., administrator ⁹	17660	13	415
Morsman, Edgar M., estate of ⁹	32075	14	108
Morsman, jr., Edgar M., administrator ⁹	32075	14	108
Moser, Carl F.....	13473	12	672
Moser, George J.....	13475	12	672
Moser, Josephine T.....	13474	12	672
Moser, Julius C.....	13471	12	672
Mossman, Yarnelle & Co. ¹⁰	{ 3269 11076 }	9	45
M. S. C. Holding Corporation et al.....	4620	7	216

¹ Estate tax decision; nonacquiescence in so far as decision holds as nontaxable the value of property placed in trust under the instrument of July 27, 1918.

² Nonacquiescence relates to second issue of decision.

³ Nonacquiescence relates to deduction of commission paid to agents for negotiating lease.

⁴ Nonacquiescence relates to first issue of decision.

⁵ This notice, which was originally published in Bulletin IV-41, page 1, was republished in Cumulative Bulletin V-1, page 7, for the reason that the case was erroneously included in the list of cases acquiesced in published in Cumulative Bulletin IV-2, page 3.

⁶ Estate tax decision; nonacquiescence relates to deductibility of remainder value of the residuary estate bequeathed to charity.

⁷ Nonacquiescence relates to tentative tax issue.

⁸ Nonacquiescence relates to issue as to whether the agreements of December 14, 1918, and the discharge thereof were productive of income taxable for the years involved, and, if so, to what extent.

⁹ Estate tax decision.

¹⁰ Nonacquiescence relates to issue involving deduction of tentative taxes in determining the earnings available for payment of dividends in 1918 and 1919.

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Muller, Carl, estate of.....	9720	13	1175
Murphy et al., James C., executors ¹	4166	5	952
Myers, Long & Co.....	{ 12358 24511 }	14	460
N.			
National Bank of Topeka.....	18850	15	1301
National Piano Manufacturing Co. ²	{ 3333 20486 }	11	46
National Products Co.....	{ 6136 12120 }	7 11	632 511
National Refining Co. of Ohio et al., The.....	186	1	236
National Sugar Manufacturing Co.....	10605	7	577
National Tank & Export Co.....	3274	3	1217
Nelson, C. N., estate of ¹	7702	7	127
Neuman Co. et al., H. L.....	18348	16	533
Nevin, William L., executor ¹	31551	16	15
New Jersey Porcelain Co.....	29568	15	1059
Newman, Lillian D.....	15940	15	369
Newman, Lloyd D.....	15936	15	369
Newman et al., Lloyd D., executors.....	15939	15	369
Newman, Louis, estate of.....	15939	15	369
Newman, William C. ³	6530	10	158
New Orleans, Texas & Mexico Ry. Co. ⁴	400	6	436
Niles Fire Brick Co.....	2628	6	8
960 Park Ave. Co., Inc., et al.....	6978	7	216
Nolde & Horst Co. ⁵	9867	12	417
Nord Hop Ranch.....	6149	10	835
Nordholt, John B.....	3766	4	509
Norfolk Knitting Mills Corporation.....	4341	5	792
Northern Trust Co., executor ¹	2473	9	1310
Northern Trust Co., executor ⁶	7127	9	96
Northside Viaduct Co. ⁷	{ 11728 14200 }	9	468
Northwestern Improvement Co.....	12106	14	79
Northwestern States Portland Cement Co. ⁸	{ 5763 10456 }	7	835
Norton et al., Frank E., executors ⁹	5594	9	450
Norwich & Worcester R. R. Co.....	2020	2	215
Norwood Lumber Co.....	3785	6	341
Noyes, Charles R., estate of ¹⁰	18486	16	519
Nunnally, J. H.....	18627	11	420
Nunnally, Winship.....	18620	11	420
O.			
Ohio Falls Dye & Finishing Works.....	20395	16	1038
Oilbelt Motor Co.....	14700	16	831
Old Colony R. R. Co.....	7820	6	1025
Old Dominion Steamship Co.....	24462	16	264

¹ Estate tax decision.² Nonacquiescence relates to tentative tax issue.³ Nonacquiescence relates to deduction of amount of bad debt ascertained to be worthless and charged off in 1920.⁴ Nonacquiescence relates to issues 1 and 4 in decision.⁵ Nonacquiescence relates to first issue of decision.⁶ Estate tax decision; nonacquiescence relates to trust created on February 9, 1917.⁷ Nonacquiescence in so far as decision determines that Highland Park Co. and Northside Viaduct Co. were affiliated with Virginia Railway & Power Co.⁸ Nonacquiescence relates to fifth issue of decision.⁹ Nonacquiescence does not relate to deductibility of New York inheritance tax.¹⁰ Estate tax decision; nonacquiescence relates to issue 1 of decision.

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Olinda Gasoline Co.-----	{ 15799 19077 }	13	1050
Olinger Corporation-----	25469	9	170
Ortseifen, Adam ¹ -----	12900	14	1403
Ott, Will M.-----	13713	15	867
Ottley, John K.-----	18623	11	420
Ottumwa Serum Co.-----	{ 15114 34274 }	14	569
Oul Building and Loan Association-----	3865	6	1196
P.			
Pacific Coast Pipe Co. ² -----	7961	11	1329
Palmetto Coal Co.-----	{ 9478 18272 20306 }	11	154
Parrett, O. S.-----	6766	4	833
Paso Robles Mercantile Co.-----	11655	12	750
Pederson, Hans ³ -----	12329	14	1089
Pederson, Marie ³ -----	12328	14	1089
Peerless Woolen Mills.-----	12038	13	1119
Pelton, Honoro Gibson, executrix ⁴ -----	7402	7	1144
Peruna Co. ⁵ -----	{ 5102 12333 }	11	1180
Petaluma & Santa Rosa R. R. Co. ⁶ -----	13830	11	541
Phelps-Waters Co. ⁷ -----	19419	15	1166
Philadelphia Quartz Co.-----	6677	13	1146
Pietsch, Amy Lake, deceased, estate of ⁸ -----	5424	6	582
Pietsch, Walter G., executor ⁸ -----	5424	6	582
Pike County Coal Corporation ⁹ -----	7189	4	625
Pittsburgh Knife & Forge Co.-----	7464	6	1083
Pittsburgh Supply Co. ¹⁰ -----	18864	14	620
Pittsburgh Valve, Foundry & Construction Co.-----	9089	6	460
Potter, A. E.-----	7432	10	563
Powell Coal Co. ¹¹ -----	11945	12	492
Prescott et al., Oliver, executors ¹² -----	7883	8	582
Prescott, Wm. R.-----	18626	11	420
Prindible, John F.-----	15344	16	187
Prindible, Loretta H.-----	15345	16	187
Pritzlaff, Frederick C.-----	6109	10	747
Prosser, Seward.-----	8520	7	734
Providence & Worcester R. R. Co.-----	{ 6297 7775 }	5	1186
Provident Trust Co. et al., administrators ⁴ -----	4976	5	1004
Q.			
Quaker Maid, Inc.-----	11421	10	301

¹ Nonacquiescence does not relate to deduction of contribution to church building fund.² Nonacquiescence relates to issue 6 of decision.³ Nonacquiescence relates to issue (a).⁴ Estate tax decision.⁵ Nonacquiescence relates to issue as to whether the Board had jurisdiction to hear and determine a deficiency for 1920.⁶ Nonacquiescence relates to that part of decision as to the purchase of taxpayer's own bonds at less than par which were retired.⁷ Nonacquiescence relates to issue as to whether Phelps-Waters Co. was a transferee of Wisconsin Chemical Co.⁸ Nonacquiescence relates to fifth issue of decision.⁹ Nonacquiescence relates only to issue 2 in decision.¹⁰ Nonacquiescence relates to issue involving special assessment.¹¹ Nonacquiescence relates to jurisdiction issue.¹² Nonacquiescence does not relate to deductibility of New York inheritance tax.

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R.			
Randall, George W., estate of	5850	4	679
	6765		
Rauh & Sons Fertilizer Co., E. ¹	10720	12	468
Rebadow, Anna N.	15937	15	369
Red Salmon Canning Co.	4146	15	790
Reeb, M. A.	9847	8	759
Reese, J. H.	18404	15	1261
Reilly, Warren	5380	7	1327
Reliance Manufacturing Co.	6021	7	583
Remington Rand, Inc.	34726	11	773
Remington Typewriter Co.	2788	4	880
Renziehausen, Frederick C.	10658	8	87
Reynolds, Mary G., estate of	8625	8	360
Reynolds, Philip M., estate of	8624	8	360
Rhode Island Tool Co.	2832	3	180
Richfield Oil Co.	15799	13	1050
	19077		
Richmond Belt Ry. Co.	7218	13	1291
Rindge Land & Navigation Co.	3698	2	1179
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Robinson Co., A. M. ²	5652	5	1217
Robinson, Mrs. C. H.	8271	8	972
Rodenbough, Elizabeth McCahan, estate of ³	465	1	477
Rodenbough, Elmer E., executor of the estate of Elizabeth McCahan Rodenbough, deceased ³	465	1	477
Rolfe, Willard G., executor ⁴	18486	16	519
Root, Henry L., estate of ⁵	2825	5	696
Root, Susie M., executrix ⁵	2825	5	696
Rosenbaum Bros., Inc.	13050	11	736
Rosseter, John H.	6179	12	254
Roth, W. A.	6012	4	834
Rouse, Hempstone & Co., Inc. ⁶	7673	7	1018
	10987		
Ruf, Frank A., estate of ⁶	9528	13	85
S.			
St. Louis Malleable Casting Co. ⁷	5490	9	110
	15168		
St. Louis National Baseball Club	26798	15	1192
Saeger, Wilford C.	7562	9	890
Sage, Margaret Olivia, estate of	5882	6	36
	6988	16	1290
San Joaquin Fruit & Investment Co.	6989		
	20801	5	977
Sarfert, Max	3436		
Sass, Morris	6922	12	156
	14354	14	165
Savannah River Lumber Co. et al. ⁸	16130		
	26936		

¹ Nonacquiescence relates to issues 3 and 4 of decision.² Nonacquiescence relates to first issue in decision.³ Estate tax decision.⁴ Estate tax decision; nonacquiescence relates to issue 1 of decision.⁵ Nonacquiescence relates to final issue of decision.⁶ Estate tax decision; nonacquiescence relates to deductibility of remainder value of the residuary estate bequeathed to charity.⁷ Nonacquiescence relates to "tentative tax" issue.⁸ Nonacquiescence relates to affiliation of Savannah River Timber Co. and Port Wentworth Lumber Co. with group for 1918-1921.

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Schreier Co., Konrad.....	3600	9	407
Scully Syrup Co., D. B.....	10005	10	90
Seaboard National Bank of New York, N. Y., executor ¹	9690	11	1386
Seals, Victoria D. (Mrs.).....	18624	11	420
Sevier, Marion Shainwald ³	14410	14	709
Shaffer, C. B.....	9872	12	298
Shainwald, Marion D. ³	14410	14	709
Sheffield Dentifrice Co. ⁴	11814	13	877
Shillito Co., John.....	6187	8	665
Shillito Realty Co.....	6186	8	665
Siegel, Inc., Joe.....	1739	1	1113
Silver King Consolidated Mining Co. of Utah.....	15153	8	41
Simmons Gin Co.....	21523	16	793
Simons Brick Co. ⁵	{ 13973 24509 27247 }	14	878
Sinsheimer Bros., Inc.....	6498	5	918
Slocum et al., Herbert Jermain, executors.....	5882	6	36
Small, G. G.....	27976	16	658
Smith, Clarence C.....	3767	4	514
Smith Agricultural Chemical Co.....	13179	11	902
Smithers, Francis S., estate of ¹	665	1	1086
Sowers Manufacturing Co.....	14464	16	268
Standard Life Insurance Co. of America ⁶	{ 12475 25842 29779 }	13	13
Stange, A. H. ⁷	553	1	810
Stanton, jr., John, estate of ¹	5892		
Starbuck, A. E., administrator.....	11724	13	796
Stephens-Adamson Manufacturing Co.....	{ 13462 18641 25010 30443 }	16	41
Stetson & Ellison.....	8736	11	397
Stevens, H. G.....	16318	14	1120
Stevens & Thompson Paper Co.....	3501	5	1213
Stone, George L.....	10756	9	20
Stoney, Mary M. (Mrs.).....	18628	11	420
Strickland, D. F.....	40707	16	419
Strickland, Olive.....	40708	16	419
Strickland, D. F. and Olive.....	23159	16	419
Strong, B. R., estate of.....	12468	13	335
Sugg, J. D., estate of.....	8860	6	651
Sunlin, L. F.....	7483	6	1232
Sunnyside Coal & Coke Co. ⁸	9442	9	984

¹ Estate tax decision.² This case was inadvertently printed in Bulletin VIII-48 as having been acquiesced in by the Commissioner.³ Nonacquiescence relates to issue as to whether Board had jurisdiction to hear and determine deficiencies.⁴ Nonacquiescence relates to loss sustained through obsolescence of trade-mark.⁵ Nonacquiescence relates to contribution to the All Year Club.⁶ Nonacquiescence relates to issue involving the question of "reserve."⁷ Acquiescence notice in the case of A. H. Stange (C. B. IV-2, 4) recalled.⁸ Nonacquiescence relates to third issue of decision.

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Swift Co., C. J.-----	12315	12	974
T.			
Tait, James ² -----	13908	11	979
Temoyan et al., Annie, trustees-----	22239	16	923
Temoyan, Mrs. Hormig, estate of-----	22239	16	923
Texas & Pacific Ry. Co.-----	9863	9	365
Textile Mill Supply Co.-----	10382	8	145
Thomas, C. R.-----	7139	8	118
Thomas, Thomas E., estate of-----	4230	6	8
Thomas, W. Aubrey-----	4229	6	8
Thomas Coal Co. ³ -----	8098	10	639
Thorn, Susan K., estate of ⁴ -----	18284	16	181
Thorne, Neale & Co., Inc.-----	12491	13	490
Tighe, Anna M.-----	13472	12	672
Tindle, Frank T. ⁵ -----	8999	11	1257
Trippensee Manufacturing Co.-----	13261	15	15
Trumble Refining Co. of Arizona-----	11763	14	348
	17492		
	26434		
	32151		
Turners Falls Power & Electric Co.-----	26306	15	983
Turnure, George E.-----	10045	9	871
U.			
Underwood, Lucy C., estate of ⁶ -----	2473	9	1310
United States Merchants & Shippers Insurance Co. ⁷ -----	10439	13	164
United States Refractories Corporation ⁸ -----	5642	9	671
United States Trust Co. of New York et al., ex- ecutors of Francis S. Smithers, deceased ⁹ -----	665	1	1086
Upham, Roy-----	16105	16	950
V.			
Van Schaick, Ellen L., estate of ⁹ -----	7127	9	96
Van Zandt, Jacobs & Co.-----	6863	8	561
	11605		
Virginia Carolina Securities Corporation et al.-----	7484	6	84
Virginia Railway & Power Co. ¹⁰ -----	9040	9	468
	11731		
Von Ruck, Karl, estate of ^{6, 11} -----	16626	14	33

¹ Nonacquiescence relates to final issue of decision.² Nonacquiescence relates to issue as to whether the agreements of December 14, 1918, and the discharge thereof were productive of income taxable for the years involved, and, if so, to what extent.³ Nonacquiescence relates to second issue of decision.⁴ Estate tax decision; nonacquiescence relates to issue 2 of decision.⁵ Nonacquiescence relates to "tentative tax" issue.⁶ Estate tax decision.⁷ Nonacquiescence relates to premium reserve issue.⁸ Nonacquiescence relates to issue with respect to question of allowance of amortization in 1918 on costs incurred in 1919.⁹ Estate tax decision; nonacquiescence relates to trust created on February 9, 1917.¹⁰ Nonacquiescence in so far as decision determines that Highland Park Co. and Northside Viaduct Co. were affiliated with Virginia Railway & Power Co.¹¹ This case was inadvertently printed in Bulletin VIII-48 as having been acquiesced in by the Commissioner.

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Walcott Lathe Co.....	1142	2	1231
Walker, William Hall, estate of.....	23973	15	401
Walters, Frances W. (Mrs.).....	18616	11	420
Walworth, Charles W.....	8794	6	788
Wanamaker, John, estate of ¹	31551	16	15
Wardlaw, W. C.....	2261	4	842
Warner, Fred W.....	3713	5	963
Warren, Wm. C.....	18632	11	420
Washington Hotel Co. ²	{ 6609 7133 }	4	441
Washington Post Co.....	8085	10	1077
Weil, Joseph, estate of ¹	18960	15	965
Weil, Sophia, administratrix ¹	18960	15	965
Weissenbach, Minna K. ³	{ 4004 4005 6061 6102 10157 }	6	617
Western Exchange Bank.....	4967	12	66
Western Maryland Ry. Co. ⁴	6475	12	889
Western Wheeled Scraper Co. ⁵	12001	14	496
Wheatley, James A. ⁶	9665	8	1246
Whitehouse, Sybil.....	13220	7	600
Whitehurst et al., John L.....	12446	12	1416
Whitehurst, et al., Mary M.....	12447	12	1416
Wickersham, Chas. A.....	18612	11	420
Widener, George D.....	7723	8	651
Widener, Joseph E.....	{ 7724 7725 }	8	651
Wilshire Oil Co., Inc.....	3927	13	1150
Wilson, Elihu Clement.....	8500	11	963
Wilson, George B.....	8501	11	963
Wilson, William W.....	8502	11	963
Wilson Syndicate Trust.....	{ 12427 27808 }	14	508
Windfelder, John H., estate of ¹	4166	5	952
Winkler & Bro. Co., Isaac.....	{ 11932 13775 }	15	38
Winship, C. R.....	18618	11	420
Winship, Elizabeth T. (Mrs.).....	18630	11	420
Wire Wheel Corporation of America.....	26555	16	737
Wisconsin Bridge & Iron Co.....	13739	13	246
Wofford, G. T.....	12529	15	1225
Wolf et al., Max, trustees.....	6149	10	835

¹ Estate tax decision.² Nonacquiescence relates only to that part of decision which relates to application of the Ayers decision (1 B. T. A., 1135).³ Nonacquiescence relates to question in decision pertaining to the year 1919.⁴ Nonacquiescence relates to issues concerning contributions to Association of Railway Executives and accrual in calendar year 1919 of increased compensation for transportation of mail, awarded by Interstate Commerce Commission on December 23, 1919.⁵ Nonacquiescence relates to that portion of decision which holds that section 284(c) of the Revenue Act of 1926 is applicable to the case.⁶ Nonacquiescence relates to item (3) in decision.

NONACQUIESCENCES—Continued.

Taxpayer.	Docket No.	Board of Tax Appeals.	
		Volume.	Page.
Wolfe, Emma S., estate of ¹ -----	16149	15	835
Wolfe, Russel, executor ¹ -----	16149	15	835
Wolferman, Fred, executor ² -----	11291	10	285
Wolferman, Louis, estate of ² -----	11291	10	285
Woodruff, Ernest-----	2050	4	842
Woodruff, Geo. C.-----	18518	11	420
Woodruff, Jas. W.-----	18619	11	420
Woodward, David-----	2266	4	842
Woolston, Beulah H. J., estate of ³ -----	11298	10	1100
Worstell Co., Ltd-----	14707	15	413
Wright, Inc., Ben T.-----	12164	12	1149
W. T. & M. Co.-----	{ 8778 13093 }	11	722
Wyoming Central Association-----	{ 9965 20546 }	8	1064
Y.			
Yorkshire Creamery Co.-----	{ 15114 34274 }	14	569
York Ice & Milk Co.-----	18348	16	533
Young, James K., estate of ³ -----	4976	5	1004
Z.			
Zakon, William-----	5450	7	687
Zellerbach, Isadore-----	2028	2	1076
Zellerbach, Theresa-----	883	2	1076
Zinn, Arthur-----	2789	3	974
Zinn, Martin-----	3444	3	969

¹ Nonacquiescence relates to deduction of Connecticut and West Virginia inheritance taxes.² Estate tax decision; nonacquiescence relates to second issue of decision.³ Estate tax decision.

INCOME TAX RULINGS.—PART I.

REVENUE ACT OF 1928.

SUBTITLE B.—GENERAL PROVISIONS.

PART II.—COMPUTATION OF NET INCOME.

SECTION 22(a).—GROSS INCOME: GENERAL DEFINITION.

ARTICLE 58: Sale of stock and rights.

VIII-27-4259
G. C. M. 6374

REVENUE ACT OF 1928. -

The M Company issued to its stockholders of record on December 21, 1928, rights to purchase one 10-year convertible $4\frac{1}{2}$ per cent gold debenture bond, par value \$100, at 98 plus accrued interest, for each — shares of stock held on that date.

Held, such rights must be regarded as a dividend to the stockholders to the extent of their fair market value on the day of their issuance, and such fair market value is the basis for the determination of gain or loss from their subsequent sale.

An opinion is requested relative to the taxable status of rights issued by the M Company to A, which rights entitled him to subscribe for 10-year convertible $4\frac{1}{2}$ per cent gold debenture bonds of that corporation for less than par.

It appears the M Company issued to its stockholders of record on December 21, 1928, rights to purchase one 10-year convertible $4\frac{1}{2}$ per cent gold debenture bond, par value \$100, at 98 plus accrued interest, for each — shares of stock held on that date. On December 20, 1928, the stock of the M Company opened at 190, ranged between 190 and $193\frac{3}{4}$, and closed at $193\frac{3}{4}$. On December 21, 1928, the first day the stock sold ex-rights, it opened at 188, ranged between $189\frac{1}{2}$ and $186\frac{1}{4}$, and closed at 187; the rights on the same day opened at $5\frac{5}{8}$, ranged between $4\frac{7}{8}$ and $5\frac{5}{8}$, and closed at $4\frac{7}{8}$. A owned y shares of stock of the M Company; he received his rights and sold the same for approximately x dollars.

It is the contention of A that the issuance of the rights resulted in no income to him, but that, as a stockholder of the M Company, he received certain privileges in the form of rights, to which, regardless of their nature, he is entitled to allocate as a basis a certain portion of the cost of the stock in respect of which they were issued, in accordance with the method prescribed in article 58 of Regulations 74. It is true that A did receive the rights as a stockholder of the

M Company and purely as a result of that relationship. But this does not establish the validity of A's contention.

The issuance by a corporation of rights to subscribe to its own stock results in a dilution of the capital stock of the corporation and therefore is regarded as analogous to a stock dividend. (*Miles v. Safe Deposit & Trust Co. of Baltimore*, 259 U. S., 247, 42 S. Ct., 483; T. D. 3365, C. B. I-1, 72.) Such dilution requires the allocation of the basis of the old stock between the stock and rights in the manner prescribed in article 58 of Regulations 74. The issuance by a corporation of rights to purchase its bonds, or other securities owned by it, at a price lower than their fair market value results, however, in an entirely different situation. In such a case the right has a fair market value and constitutes a dividend, for to the extent of that value it effects a distribution of the surplus of the issuing corporation. A right to purchase stock of a second corporation owned by the issuing corporation has been held to be a dividend. (*Estate of Edwin D. Metcalf v. Commissioner*, 13 B. T. A., 236, affirmed by the Circuit Court of Appeals, Second Circuit, April 8, 1929, Ct. D. 58, C. B. VIII-1, 219.) A right to purchase rights received by the issuing corporation as a stockholder of a second corporation has also been held to be a dividend. (G. C. M. 926, C. B. VI-1, 133.) Debenture bonds of a corporation issued to its stockholders without cost must be regarded as a dividend to the extent of surplus earned after February 28, 1913. (*Doerschuck v. United States*, 274 Fed., 739, T. D. 3170, C. B. 4, 25.) Rights to purchase bonds at a price below par issued by a corporation to its stockholders must likewise be regarded as a dividend. Their issuance does not cause a stock dilution, but rather effects an immediate distribution of surplus.

In the instant case the M Company distributed rights which, because of the solid financial condition of the corporation, had a market value. Assuming that the M Company had on hand on December 21, 1928, a surplus earned since February 28, 1913, in an amount equal to or in excess of the total fair market value of all rights issued, such rights must be regarded as a dividend to the stockholders of that corporation to the extent of their fair market value on the day of their issuance. (*Estate of Metcalf v. Commissioner*, supra.) Such dividend is subject to surtax only. The fair market value of the rights on the day of their issuance is the basis for the determination of gain or loss from their subsequent sale by A.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

ARTICLE 58: Sale of stock and rights.

VIII-37-4348
I. T. 2494

REVENUE ACT OF 1928 AND PRIOR REVENUE ACTS.

Solicitor's Memorandum 1646 (C. B. III-1, 107), in so far as it holds that the entire selling price of the rights issued by a corporation to stockholders to subscribe for its bonds is income, is considered overruled by General Counsel's Memorandum 6374 (see on page 75), which holds, among other things, that the fair market value of such

rights on the day of their issuance when issued subsequent to February 28, 1913, is the basis in the hands of the stockholders for the determination of gain or loss from their subsequent sale.

ARTICLE 58: Sale of stock and rights.

VIII-45-4419
G. C. M. 7021

REVENUE ACT OF 1928.

Article 58 of Regulations 74 is not to be applied in determining the gain derived from sales of rights occurring in a taxable year prior to 1928, or in determining the basis of stock sold in a taxable year prior to 1928 in respect of which stock rights were issued prior to its sale.

An opinion is requested as to whether the last paragraph of article 58 of Regulations 74 may be applied retroactively to years prior to 1928.

The paragraph in question reads as follows:

The taxpayer may at his option include the entire proceeds from the sale of stock rights in gross income, in which case the basis for determining gain or loss from the subsequent sale of the stock in respect of which the rights were issued shall be the same as though the rights had not been issued.

A, the taxpayer, prior to 1920, acquired blocks of stock in the M Company, the N Company, the O Company, and the P Company. Each of these corporations during the years 1920 to 1926, inclusive, issued rights to subscribe to additional shares of its capital stock on certain terms and conditions. The taxpayer, upon receipt of his share of the rights, sold them and reported the entire proceeds as income for the year in which each sale took place. In 1927 the taxpayer sold some of his stock in each of the above-named corporations, and used the original cost per share as the basis for determining gain or loss from the sale. The revenue agent increased the gain derived from the stock sales in 1927 by adjusting the basis of the stock on account of the receipt and sale of rights in prior years. The taxpayer protests against this action, contending that the last paragraph of article 58 of Regulations 74, *supra*, must be retroactively applied, and that when so applied it permits the adoption of the basis he employed.

Section 62 of the Revenue Act of 1928 reads as follows:

The Commissioner, with the approval of the Secretary, shall prescribe and publish all needful rules and regulations for the enforcement of this title. [Title I, Income Tax.]

Pursuant to this authority, the Commissioner, with the approval of the Secretary, promulgated Regulations 74 (see article 1501 thereof), relating to the income tax under Title I of the Revenue Act of 1928; these regulations, however, are to be regarded as interpretative only of the provisions of Title I of the Revenue Act of 1928, and therefore as applicable only to those taxable years which are controlled by the provisions of that Act and title. Hence, article 58 of Regulations 74 is not to be applied in determining the gain derived from sales of rights occurring in a taxable year prior to 1928, or in determining the basis of stock sold in a taxable year prior to 1928 in respect of which stock rights were issued prior to its sale. The gain from the sales of rights received by the taxpayer in the

years 1920 to 1926, inclusive, should have been determined in accordance with the provisions of article 39 of Regulations 45 (1920 edition), as amended by Treasury Decision 3402 (C. B. I-2, 63), of article 39 of Regulations 62, as amended by Treasury Decision 3403 (C. B. I-2, 64), both amendments being promulgated October 18, 1922, and of article 39 of Regulations 65 and 69. The action of the revenue agent in adjusting the basis of the stock sold in 1927 on account of the prior receipt and sale of rights is therefore approved. (Cf. I. T. 2383, C. B. VI-2, 29, and I. T. 2417, C. B. VII-1, 59.)

While in the earlier taxable years here concerned the taxpayer reported as income the entire proceeds from the sale of the rights received in those years, in accordance with the then existing regulations, the amendments thereof were promulgated October 18, 1922, as a result of the decision of the Supreme Court of the United States in the case of *Miles v. The Safe Deposit & Trust Co. of Baltimore* (259 U. S., 247 (Ct. D. 29), T. D. 3365, C. B. I-1, 72), decided May 29, 1922, in ample time for the taxpayer to have protected his rights by the filing of claims for refund. His failure to do so can not justify a conclusion contrary to that expressed above. The reporting as income of the entire proceeds from the sales of rights received in the later taxable years was contrary to the then existing regulations, and as to those years the taxpayer must also be left to such relief as may be available to him through the filing of claims for refund.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

ARTICLE 58: Sale of stock and rights.

VIII-47-4431

I. T. 2509

REVENUE ACT OF 1928.

Method to be followed in the application of I. T. 2474 (C. B. VIII-1, 65) in the determination of the respective values of stock and rights where there is an established market value for the stock (including the rights) but none for the stock or rights separately on the date which determines the shareholders who are entitled to the rights.

The principles governing the distribution of rights entitling the shareholders to acquire shares of a character or preference different from that of the shares in respect of which the rights are issued are the same as in the case of the distribution of shares of stock of such different character or preference as a stock dividend. The apportionment in such case may, therefore, be made in accordance with article 600 (rule 2) of Regulations 74.

Advice is requested relative to certain questions arising in connection with the application of the ruling published as I. T. 2474, in which it was held that the date on which stock rights are considered to be issued, for the purpose of apportioning the cost or other basis of the stock between the stock and the rights under article 58 of Regulations 74, is the date of record on which the rights accrue to and vest in the shareholders as a property interest separate and distinct from the shares of stock in respect of which the rights are issued.

The question is raised as to the method to be followed in cases where there is an established market value for the stock (including

the rights) as of such record date but none for the stock or rights separately. Under such circumstances the respective values of the stock and rights on the record date can be satisfactorily determined by resort to a formula to which the Bureau has given recognition. (See article 39 of Regulations 65.) In accordance with the prescribed formula, all that is necessary is to take the aggregate value, on the date which determines the shareholders who are entitled to the rights, of that number of shares of stock the ownership of which entitles a shareholder to subscribe to 1 new share, add to such aggregate value the full amount of the subscription price required to be paid to acquire the new share of stock, and divide the sum by 1 plus the number of shares of stock whose aggregate value was used as a starting point. The quotient is the value attributable to 1 share of stock after the issuance of the rights, and the quotient less the subscription price is the value attributable to that number of rights which entitles a shareholder to subscribe to 1 new share of stock. The latter value divided by the number of rights involved is the value attributable to 1 right. The sum of the values attributable to a share of stock and a right under this formula will in all cases equal the value, on the date which determines the shareholders who are entitled to the rights, of a share of stock carrying with it the right created on that date. With the respective values of a share of stock and of a right on the date established, it is a simple matter to find the proper portion of the original cost or other basis of a share of stock which after the issuance of the stock right is assignable to the stock and to the right, respectively.

Inasmuch as the distribution of such rights is analogous to the distribution of additional shares of stock as a stock dividend, the principles governing the distribution of rights entitling the shareholders to acquire shares of a character or preference different from that of the shares in respect of which the rights are issued are the same as in the case of the distribution of shares of stock of such different character or preference as a stock dividend. The apportionment in such case may, therefore, be made in accordance with article 600 (rule 2) of Regulations 74. This is so because that rule follows the same principle of apportionment as is adopted in article 58 of Regulations 74, which article applies specifically to the procedure to be followed in every case where a corporation issues to its shareholders rights to subscribe to its stock, whether the rights entitle the shareholders to subscribe to shares of the same character or preference as the stock in respect of which the rights are issued or of a character or preference materially different from the stock in respect of which the rights are issued.

Where there are no sales of the stock or rights from which the respective values as of the record date may be determined and such values must be determined from other evidence, no general rule can be laid down as applicable to all such cases, and the respective values in any such case must be determined from the facts of the particular case.

ARTICLE 58: Sale of stock and rights.

VIII-50-4461
G. C. M. 7246

REVENUE ACT OF 1928.

The M Corporation was organized as an investment company. The stockholders of the O Company were given the first opportunity to purchase stock at 3*x* dollars per share, under warrants distributed by the M Corporation to stockholders of the O Company. Other than the fact that the directors of the M Corporation were directors of the O Company there was no connection between the two companies.

Held, that the entire proceeds of a sale of the warrants by a recipient constituted income subject both to normal tax and surtax; that where the rights were exercised, the basis of the stock so acquired was 3*x* dollars per share; that where warrants were purchased and combined with warrants directly received and then used to purchase stock, the basis of the stock was the cost of the purchased warrants plus the basis of the warrants directly received (zero) plus the subscription price of 3*x* dollars per share.

An opinion is requested relative to the treatment for income tax purposes of certain warrants issued by the M Corporation to stockholders of the O Company.

On April —, 1929, the O Company addressed to its stockholders a circular letter wherein it was stated that it appeared advantageous for the stockholders to unite in establishing a separate corporation to make investments in securities of other corporations. It was further stated that the M Corporation had been incorporated under the laws of the State of R, and that the stockholders of the O Company were to be given the first opportunity to purchase stock of the M Corporation.

On the same day the M Corporation addressed a circular letter to the stockholders of the O Company, wherein it offered to them the opportunity to purchase at 3*x* dollars per share *y* shares of its own no par common stock; it further stated that of the proceeds of the sale of the stock 2*x* dollars per share was to be capital and the remainder was to be paid-in surplus not available for dividends on the common stock. The terms of the offering were as follows:

Stockholders of the O Company are hereby offered the privilege of purchasing at 3*x* dollars per share, upon the terms and conditions hereinafter stated, on or before June —, 1929, a number of shares of the common stock of the M Corporation equal to one-half of the number of shares of stock of the O Company, registered in their respective names on its books at the close of business on May —, 1929.

The board of directors of the M Corporation consisted of the same individuals who comprised, in whole or in part, the board of directors of the O Company. Otherwise there was no connection between the O Company and the M Corporation. The M Corporation was organized separately and apart from the O Company. Furthermore, the O Company did not transfer any of its assets to the M Corporation either in exchange for stock or rights or otherwise. The surplus and earnings of the O Company were unaffected by the organization of the M Corporation and the distribution of warrants by the latter corporation evidencing the privilege of purchasing its stock.

The warrants evidencing the right to purchase the stock of the M Corporation were distributed by that corporation to all stockholders of record on the books of the O Company as of May —, 1929, as

soon as possible after that date, and said warrants became void after June —, 1929.

The Q Company asks to be advised how it should treat the warrants of the M Corporation for income tax purposes in the following cases:

- (1) Where the rights were sold.
- (2) Where the rights were exercised.
- (3) Where rights were purchased on the market and combined with those received on shares held.

From the foregoing it is clear that the capital, surplus, and undivided profits, if any, of the O Company were not affected by this transaction. No assets of the O Company were transferred to the M Corporation either in exchange for stock or rights in the latter corporation or otherwise. The O Company did not participate in the transaction except to furnish a list of its stockholders. Any rights or property of value received by the stockholders of the O Company did not constitute a dividend, as such rights or property did not effect a distribution of the surplus, if any, of the O Company. Furthermore, the rights did not work a dilution of the O Company's stock and therefore were not analogous to a stock dividend.

In substance, the transaction constituted a continuing offer to a certain designated group, i. e., the stockholders of the O Company and/or their assignees. By its terms the offer extended from May —, 1929, to June —, 1929. Ownership of the O Company's stock on May —, 1929, in itself fixed the identity of the offerees, but nothing more. Thereafter the stockholders, as of May —, 1929, held the privilege of accepting the offer of the M Corporation on or before June —, 1929. That privilege did not issue from the O Company to its stockholders as the result of the relationship of stockholder and corporation, but resulted to each stockholder from his status as offeree the moment the offer became effective. It was a property right owned by the offeree until exercised, sold, or allowed to expire. In this case the privilege or right of accepting the offer did not cost the offeree stockholder anything, and it therefore assumed a zero basis for the purpose of determining gain or loss from its subsequent disposition. (Section 113(a) of the Revenue Act of 1928.)

Under the circumstances and for the reasons stated, it is the opinion of this office that the entire proceeds of a sale of the warrants constituted income subject both to normal tax and surtax; that where the warrants were exercised, the basis of the stock so acquired was $3x$ dollars per share; that where warrants were purchased and combined with warrants directly received and then used to purchase stock, the basis of the stock was the cost of the purchased warrants plus the basis of the warrants directly received (zero) plus the subscription price of $3x$ dollars per share.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

ARTICLE 63: Improvements by lessees.

VIII-52-4479
T. D. 4282

INCOME TAX.

Article 63 of Regulations 74 amended.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, D. C.*To Collectors of Internal Revenue and Others Concerned:*

Article 63 of Regulations 74 is hereby amended to read as follows:

ART. 63. *Improvements by lessees.*—When buildings are erected or improvements made by a lessee in pursuance of an agreement with the lessor, and such buildings or improvements are not subject to removal by the lessee, the lessor may at his option report the income therefrom upon either of the following bases:

(a) The lessor may report as income at the time when such buildings or improvements are completed the fair market value of such buildings or improvements subject to the lease.

(b) The lessor may spread over the life of the lease the estimated depreciated value of such buildings or improvements at the expiration of the lease and report as income for each year of the lease an aliquot part thereof.

Except in cases where the lessor has exercised the option to report income upon basis (b), if the lease is terminated so that the lessor comes into possession or control of the property prior to the time originally fixed for the expiration of the lease, the lessor derives no income by reason thereof, and, just as when the lessor comes into possession or control of the property upon the expiration of the lease, the basis for determining gain or loss to the lessor from the subsequent sale or other disposition of the buildings or improvements and for depreciation in respect of such property is the amount previously reported as income by the lessor because of the erection of the buildings or improvements, except that if the buildings or improvements were acquired prior to March 1, 1913, the basis shall be their value subject to the lease when acquired or their value subject to the lease on March 1, 1913, whichever is greater. If the buildings or improvements are destroyed prior to the expiration of the lease, the lessor is entitled to deduct as a loss for the year when such destruction takes place the amount previously reported as income because of the erection of such buildings or improvements, less any salvage value subject to the lease to the extent that such loss is not compensated for by insurance or otherwise. If the buildings or improvements destroyed were acquired prior to March 1, 1913, the deduction shall be based on their value subject to the lease when acquired or their value subject to the lease on March 1, 1913, whichever is greater, less any salvage value subject to the lease to the extent that such loss is not compensated for by insurance or otherwise. (See articles 130 and 204.)

In all cases where the lessor has exercised the option to report income upon basis (b), if the lease is terminated so that the lessor comes into possession or control of the property prior to the time originally fixed for the expiration of the lease, the lessor derives additional income for the year in which the lease is so terminated to the extent that the value of such buildings or improvements when he becomes entitled to such possession exceeds the amount already reported as income on account of the erection of such buildings or improvements. No appreciation in value due to causes other than the termination of the lease shall be included. If the buildings or improvements are destroyed prior to the expiration of the lease, the lessor is entitled to deduct as a loss for the year when such destruction takes place the amount previously reported as income because of the erection of such buildings or improvements, less any salvage value subject to the lease to the extent that such loss is not compensated for by insurance or otherwise.

ROBT. H. LUCAS,

Commissioner of Internal Revenue.

Approved December 19, 1929.

OGDEN L. MILLS,

Acting Secretary of the Treasury.

SECTION 22(b).—GROSS INCOME: EXCLUSIONS FROM GROSS INCOME.

ARTICLE 87: Interest upon United States obligations.

VIII-48-4446
T. D. 4276

INCOME TAX.

Exemption of Treasury bills.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, D. C.

To Collectors of Internal Revenue and others concerned:

Attention is invited to the Act entitled "An Act to amend section 5 of the Second Liberty Bond Act, as amended," approved June 17, 1929 (Pub. No. 11, 71st Cong., H. R. 1648), which, among other things, authorizes the Secretary of the Treasury to issue Treasury bills on a discount basis, payable at maturity without interest. That Act amends section 5 of the Second Liberty Bond Act, as amended, to read as follows, the tax provisions being contained in subdivision (b) thereof:

SEC. 5. (a) That in addition to the bonds and notes authorized by sections 1 and 18 of this Act, as amended, the Secretary of the Treasury is authorized to borrow from time to time, on the credit of the United States, for the purposes of this Act, to provide for the purchase or redemption before maturity of any certificates of indebtedness or Treasury bills issued hereunder, and to meet public expenditures authorized by law, such sum or sums as in his judgment may be necessary, and to issue therefor (1) certificates of indebtedness of the United States at not less than par and at such rate or rates of interest, payable at such time or times as he may prescribe; or (2) Treasury bills on a discount basis and payable at maturity without interest. Treasury bills to be issued hereunder shall be offered for sale on a competitive basis, under such regulations and upon such terms and conditions as the Secretary of the Treasury may prescribe, and the decisions of the Secretary in respect of any issue shall be final. Certificates of indebtedness and Treasury bills issued hereunder shall be in such form or forms and subject to such terms and conditions, shall be payable at such time, not exceeding one year from the date of issue, and may be redeemable before maturity upon such terms and conditions as the Secretary of the Treasury may prescribe. Treasury bills issued hereunder shall not be acceptable before maturity in payment of interest or of principal on account of obligations of foreign governments held by the United States of America. The sum of the par value of such certificates and Treasury bills outstanding hereunder and under section 6 of the First Liberty Bond Act shall not at any one time exceed in the aggregate \$10,000,000,000.

(b) All certificates of indebtedness and Treasury bills issued hereunder (after the date upon which this subdivision becomes law) shall be exempt, both as to principal and interest, from all taxation (except estate and inheritance taxes) now or hereafter imposed by the United States, any State, or any of the possessions of the United States, or by any local taxing authority; and the amount of discount at which Treasury bills are originally sold by the United States shall be considered to be interest within the meaning of this subdivision.

(c) Wherever the words "bonds and notes of the United States," or "bonds and notes of the Government of the United States," or "bonds or notes of the United States" are used in the Federal Reserve Act, as amended, they shall be held to include certificates of indebtedness and Treasury bills issued hereunder.

The statement of the managers on the part of the House which accompanied the conference report (Rept. No. 17, 71st Cong., 1st sess.) accompanying H. R. 1648 shows that Congress intended that the

original discount rate at which a Treasury bill is issued should be regarded in the same way as the interest rate fixed by the security itself in the case of an interest-bearing obligation, and that the amount of the discount should be apportioned among the holders according to the periods of their holdings just as the interest on an interest-bearing obligation is apportioned. (See Sol. Op. 46, C. B. 3, p. 90.)

Accordingly, in the case of an original purchaser from the Government who holds a Treasury bill to maturity, the entire amount of the discount at which the bill was issued is exempt from income tax. If a bill is sold before maturity, each respective holder is entitled to treat as exempt from income tax that proportion of the amount of the discount at which the bill was issued which the number of days (computed on an actual calendar-day basis) the bill was owned by him bears to the total number of days (computed on an actual calendar-day basis) from the date of the issuance of the bill to the date of its maturity. In other words, the amount of the discount at which the bill was issued is to be apportioned among the holders according to the periods of their holdings. The gain from the sale or other disposition of a Treasury bill (that is, the excess of the amount realized therefrom less discount from the date of acquisition to the date of its disposition over the cost or other basis of the bill) is taxable as ordinary income. A loss from the sale or other disposition of a Treasury bill (that is, the excess of the cost or other basis of the bill over the amount realized therefrom less discount from the date of acquisition to the date of its disposition) is allowable as a deduction. There will be stated on each Treasury bill the amount of the discount at which it was issued.

The foregoing principles may be illustrated by the following examples:

Example 1: A 90-day Treasury bill is issued to A on March 17 for \$9,900. The bill has a maturity value of \$10,000 on the following June 15. A holds the bill to maturity. He may treat the entire amount of the discount, or \$100, as tax-exempt interest.

Example 2: A Treasury bill is issued to A as in example 1. A holds the bill until April 11 (25 days), on which date he sells it to B for \$9,927.78. B holds the bill to maturity (i. e., for 65 days). A is entitled to treat 25/90ths of the amount of the discount, or \$27.78, as tax-exempt interest, that amount being the proportion of the discount which the number of days A owned the bill (25) bears to the total number of days for which the bill was issued (90). Likewise, B is entitled to treat 65/90ths, or \$72.22, as tax-exempt interest.

Example 3: A Treasury bill is issued to A as in example 1. A holds the bill until May 1, when he sells it to B for \$9,962.50. B holds the bill to maturity. A is entitled to treat 45/90ths of the amount of the discount, or \$50, as tax-exempt interest. A realizes a taxable gain of \$12.50 in the transaction, computed as follows:

The amount A realizes from the sale is \$9,962.50, which includes \$50, representing discount to him. Therefore, \$9,962.50 less \$50, or \$9,912.50, is the amount A realizes from the sale in addition to the discount treated as tax-exempt interest. Since the bill cost A \$9,900, the amount of the gain is \$9,912.50 less \$9,900, or \$12.50.

B is also entitled to treat 45/90ths of the amount of the discount, or \$50, as tax-exempt interest. B sustains a deductible loss of \$12.50 in the transaction, computed as follows:

The amount B realizes upon the maturity of the bill is \$10,000, which includes \$50, representing discount to him. Therefore, \$10,000 less \$50, or \$9,950, is the amount B realizes upon the maturity of the bill in addition to the discount treated as tax-exempt interest. Since the bill cost B \$9,962.50, the amount of his deductible loss is \$9,962.50, less \$9,950, or \$12.50.

Example 4: A Treasury bill is issued to A as in example 1. A holds the bill until May 1, when he sells it to B for \$9,937.50. B holds the bill to maturity. A is entitled to treat 45/90ths of the amount of the discount, or \$50, as tax-exempt interest. A sustains a deductible loss of \$12.50 in the transaction, computed as follows:

The amount A realizes from the sale is \$9,937.50, which includes \$50 representing discount to him. Therefore, \$9,937.50 less \$50, or \$9,887.50, is the amount A realizes from the sale in addition to the discount treated as tax-exempt interest. Since the bill cost A \$9,900, the amount of his deductible loss is \$9,900 less \$9,887.50, or \$12.50.

B is also entitled to treat 45/90ths of the amount of the discount, or \$50, as tax-exempt interest. B realizes a taxable gain of \$12.50 in the transaction, computed as follows:

The amount B realizes upon the maturity of the bill is \$10,000, which includes \$50 representing discount to him. Therefore, \$10,000 less \$50, or \$9,950, is the amount B realizes upon the maturity of the bill in addition to the discount treated as tax-exempt interest. Since the bill cost B \$9,937.50, the amount of the gain is \$9,950 less \$9,937.50, or \$12.50.

(This Treasury decision is applicable only to the treatment of discount in the case of Treasury bills.)

ROBT. H. LUCAS,

Commissioner of Internal Revenue.

Approved November 22, 1929.

A. W. MELLON,

Secretary of the Treasury.

SECTION 23(a).—DEDUCTIONS FROM GROSS INCOME: EXPENSES.

ARTICLE 121: Business expenses.

VIII-49-4448

G. C. M. 7133

REVENUE ACT OF 1928.

Allowable expense deductions in the case of professional golf players who participate in tournaments considered for income tax purposes.

An opinion is requested as to what expenses may be allowed as deductions for income tax purposes in the case of professional golf players who participate in tournaments.

The professional golf players here under consideration travel throughout the United States, Canada, and Europe, competing in tournaments for cash prizes. They do not receive any guarantee and are not compensated for their expenses. The only income they receive from participation in the tournaments is the amount of prize

money they win in open competition. Their expenses include amounts paid for railroad fare, hotel accommodations, caddie hire, entry fees, golf clubs, balls, tees, and other equipment, as well as golf shoes, hose, sweaters, rain jackets, and other wearing apparel required in their work, and laundry.

A determination of the status of the expenses of a professional golf player participating in golf tournaments depends in the first instance upon whether the activities of a professional golf player come within the scope of section 23(a) of the Revenue Act of 1928, which reads in part as follows:

In computing net income there shall be allowed as deductions:

(a) *Expenses*.—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; traveling expenses (including the entire amount expended for meals and lodging) while away from home in the pursuit of a trade or business; and rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity.

Bouvier's Law Dictionary (Rawles Third Revision) defines business as "that which occupies the time, attention, and labor of men for the purpose of livelihood or profit, but it is not necessary that it should be the sole occupation or employment. It embraces everything about which the person can be employed." This definition has been followed with approval by the Supreme Court in the case of *Flint v. Stone Tracy Co.* (220 U. S., 107), the opinion noting also that "business is a very comprehensive term and embraces everything about which a person can be employed." The general tenor of this latter definition has been followed widely, as, for example, in Treasury Decision 1989; *Beickler v. Guenther* (121 Iowa, 419, 96 N. W., 895); *Territory v. Harris* (8 Mont., 140, 19 Pac., 286); *State v. Boston Club* (45 La. Ann., 585, 12 S., 895); *Goddard v. Chaffee* (84 Mass., 395). In the case of *State v. District Court* (138 Minn., 103, 164 N. W., 366), the court held that the term "trade" or "profession" of a person generally means that branch of the world's activities wherein he expends his usual everyday efforts to gain a livelihood.

From the foregoing it seems clear that the playing of golf for a consideration or compensation as a means of gaining a livelihood constitutes a trade or business. It is similar in some respects to the occupation of professional ball playing, which has been held to be a trade or calling in *Crook v. Commonwealth* (147 Va., 593, 136 S. E., 566).

The occupation of professional golf playing does not necessarily confine the player to a golf club where he may be employed as instructor, but permits him to engage in his occupation at other places where he may receive some compensation for his activities as a golf player. In giving public exhibitions of golf playing for a consideration, and in competing at professional golf tournaments for a prize, or for money, the professional golf player is merely pursuing his occupation in another place. In many instances professional golf players are not attached as instructors or experts to any particular golf club, but gain a livelihood solely by competition in tournaments or by giving exhibitions of skillful golf playing.

Since professional golf playing constitutes a trade or business, it comes within the scope of section 23(a) of the Revenue Act of 1928.

In Solicitor's Memorandum 1048 (C. B. 1, 101) it was held that "the test, therefore, is whether an expense is incurred primarily because of the business as the immediate cause inducing the expenditure." Applying this test to the instant case, it is clear that the immediate cause of an expenditure would be the business of professional golf playing in different localities which offer inducements to the golf player to exercise his skill.

An attorney traveling from home in the pursuit of his profession has been allowed to deduct his traveling expenses, including meals (Hamilton Ward, 8 B. T. A., 704). This decision was acquiesced in by the Commissioner (C. B. VII-1, 33). A university professor living in one city and going to another city to teach for a few weeks during his vacation period was allowed his traveling expenses, including meals and lodging, as deductible items in computing net income. (See I. T. 2481, on page 291.) Attention is also directed to the case of Walter F. Brown (13 B. T. A., 832), where the Board of Tax Appeals held that where a taxpayer accepted a Government position which required his presence and work in Washington about one-half the time and taxpayer retained his home and professional connections in a distant city, expenses for meals and lodging while in Washington were properly deductible as expenses incurred in carrying on a trade or business. This decision was acquiesced in by the Commissioner (C. B. VIII-1, 6).

Accordingly, a professional golf player traveling from his home to other places for the purpose of giving for compensation exhibitions of golf playing or of competing in professional golf tournaments for prizes or other consideration, is entitled to deduct his ordinary and necessary traveling expenses paid or incurred while away from home in pursuit of such business. It follows that the entire amount expended for railroad fare and for meals and lodging while away from home, in order to perform services for which compensation is received, may be deducted by a professional golf player in computing his net income.

Inasmuch as articles of wearing apparel worn by golf players take the place of regular clothing otherwise worn, no part of the cost thereof constitutes a business expense. (See I. T. 1488, C. B. I-2, 145.) Amounts paid for laundry are likewise personal expenses and are not deductible.

The cost of golf clubs, balls, tees, and other playing equipment other than that constituting a part of the participant's wearing apparel, if purchased for use solely in the tournaments, is an allowable deduction. It is also the opinion of this office that the cost of caddie hire and entry fees incurred in the tournaments is an allowable business expense.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

SECTION 23(c).—DEDUCTIONS FROM GROSS
INCOME: TAXES GENERALLY.

ARTICLE 151: Taxes.

VIII-29-4275

I. T. 2479

REVENUE ACT OF 1928.

The 4 cents per gallon motor fuel tax imposed by the State of North Carolina is deductible in the income tax return of the consumer who pays the tax and to whom it is not refunded. If the tax is made a part of the business expense of such consumer, it can not be deducted separately as a tax.

A ruling is requested as to whether the motor fuel tax imposed by the State of North Carolina is deductible in the returns of the consumers who purchase from the distributors.

It appears that the tax in question is levied in accordance with the provisions of the law of the State of North Carolina which was ratified March 4, 1927, and is headed "An act to amend chapter 55, article 3 (A) of volume 3 of Consolidated Statutes relating to tax on gasoline." Section 1(c) of that act reads as follows:

"Distributor" is any person, firm, association, or corporation that has on hand or in his or its possession, in this State, motor fuels being held for the purpose of sale, distribution or use, within the State, or that produces, refines, manufactures, or compounds such motor fuels in this State for sale, distribution, or use herein.

Sections 2 and 2½ of the act contain the following provisions:

The purpose of this act is to provide for the payment and collection of a tax on the first sale of motor fuels when sold, or the use, when used, in this State; double taxation is not intended. Motor fuel manufactured, produced, or compounded, in or imported into this State and subsequently sold for exportation, and exported are not taxable and should not be included in the reports hereinafter required to be made by distributors.

In the administration of this act the first sale shall not be construed to embrace the sale in tank car shipments from port terminals to licensed distributors within the State, but the tax hereinafter levied on such motor fuel shall be levied against and paid by such licensed distributor.

Section 4 of the act imposes a tax of 4 cents per gallon on all motor fuels sold, distributed, or used in the State, and provides that the tax "*shall be collected* and paid by the distributor." [Italics supplied.] Section 9 provides that purchasers who buy motor fuels in quantities of 10 gallons or more at any one time, for use in any manner except in motor vehicles operated upon the highways, on which motor fuels the tax or taxes have been paid, "shall be reimbursed and repaid the amount of such tax or taxes paid" upon furnishing certain evidence of such purchases.

Section 23(c) of the Revenue Act of 1928 provides that in computing net income there shall be allowed as deductions taxes paid or accrued within the taxable year, with certain exceptions not here material. Article 151 of Regulations 74, promulgated under the Revenue Act of 1928, provides that in general taxes are deductible only by the person upon whom they are imposed.

It is the opinion of this office that the motor fuel tax imposed by the State of North Carolina under the act hereinabove referred to is imposed upon the consumers who purchase from the distributors, and therefore it is held that in accordance with section 23(c) of the Revenue Act of 1928 and article 151 of Regulations 74 the tax is

deductible in the income tax returns of the consumers who pay the tax and to whom it is not refunded. If the tax is made a part of the business expense of such consumers, it can not be deducted separately as a tax.

ARTICLE 151: Taxes.

VIII-30-4282

I. T. 2482

REVENUE ACT OF 1928.

The gasoline tax imposed by the State of Kentucky is a tax upon consumption or upon the privilege of using and is deductible by the consumer who pays it. If the tax is added to or made a part of the business expense of the consumer, it can not be deducted separately as a tax.

Advice is requested whether the gasoline tax levied by the State of Kentucky is deductible by the consumer.

It appears that the tax in question is levied in accordance with the provisions of the State statute, approved March 19, 1928, imposing a tax on gasoline. Sections 1 and 2 of that statute read as follows:

1. That the word "gasoline" as used in this act, shall include all liquid fuels, including liquids ordinarily, practically and commercially usable in internal combustion engines for the generation of power, and all distillates of, and condensates from petroleum, natural gas, coal, coal tar, vegetable ferments, and all other products, so usable and sold in this Commonwealth at wholesale, as the words, "at wholesale" are defined herein, except kerosene, fuel oil and crude oil as such. A State tax of five (5) cents per gallon is hereby imposed on all gasoline, as defined herein, sold in this Commonwealth at wholesale, as the words "at wholesale" are hereinafter defined. No other excise or license tax shall be levied or assessed on gasoline by the State or any county, city, town or other district. The tax hereby provided for shall be paid by the person, firm, association or corporation so selling gasoline, and shall be paid by said person, firm, association or corporation into the general fund of the State treasury in the manner and within the time hereinafter specified. The words "at wholesale" as used in this act, shall be held and construed to mean and include any and all sales made for the purpose of resale or distribution, or for use, and, as well, the gasoline furnished or supplied for distribution within this State, whether the distributor be the same person who so furnished the same, his agent or employee, or another person; and also to mean and include any person who shall purchase or obtain gasoline without the State and sell or distribute or use the same within the State. Provided, that nothing herein contained shall be construed as authorizing or requiring the collection of such tax upon any gasoline after the same shall have been already once taxed under the provisions of this act.

2. All taxes collected under the provisions of this act shall be paid into the State treasury, and shall be used only for the purpose of the construction, reconstruction, maintenance and repair of roads, highways and bridges.

Section 23(c) of the Revenue Act of 1928 provides that in computing net income there shall be allowed as deductions taxes paid or accrued within the taxable year, with certain exceptions not here material. Article 151 of Regulations 74, promulgated under the Revenue Act of 1928, provides that in general taxes are deductible only by the person upon whom they are imposed.

Upon consideration of the provisions of the State statute and the decision of the Court of Appeals of Kentucky in the case of *Shanks, Auditor, v. Kentucky Independent Oil Co.* (225 Ky., 303, 8 S. W. (2d), 383), which decision related to a prior gasoline tax act (Acts 1924, ch. 120), the provisions of which were substantially the same as those of the statute under consideration except as to the rate of

tax, it is concluded that the gasoline tax imposed by the provisions of the State statute above quoted is a tax upon consumption or upon the privilege of using and is not a tax upon the privilege of selling.

In view of the foregoing, it is held that the gasoline tax imposed by the State of Kentucky is deductible in the income tax return of the consumer who pays it. If, however, the tax in question is added to or made a part of the business expense of such consumer, it can not be deducted separately as a tax.

ARTICLE 151: Taxes.

VIII-31-4291

I. T. 2483

REVENUE ACT OF 1928.

The motor fuel tax imposed by the State of New York is deductible in the income tax return of the consumer who pays it and to whom it is not refunded. If the tax is added to or made a part of the business expense of such consumer, it can not be deducted separately as a tax.

A ruling is requested as to whether the gasoline and other motor fuel tax imposed by the State of New York is deductible in the income tax return of the consumer.

The tax in question is levied in accordance with the provisions of an act which became a law of the State of New York on April 8, 1929, headed "An act to amend the tax law, in relation to imposing and providing for the distribution of a tax on gasoline and other motor fuel."

Section 284 of the act reads in part as follows:

1. There is hereby levied and imposed an excise tax of 2-cents per gallon upon motor fuel sold within the State by a distributor, except when sold under circumstances which preclude the collection of such tax by reason of the United States Constitution and of laws of the United States enacted pursuant thereto.

Section 287 of the act contains the following provisions:

Every distributor shall, in each month, file with the department of taxation and finance a return under oath, on forms to be prescribed by the tax commission and furnished by such department, stating the number of gallons of motor fuel sold by such distributor in the State during the preceding calendar month. Such return shall contain such further information as the tax commission shall require. Each such distributor shall pay to the department with the filing of such return, the tax imposed by this article on each gallon of motor fuel sold by such distributor in the State, as so reported, during the calendar month covered by such return, after deducting therefrom an amount equivalent to 1 per centum of the amount due, which is hereby allowed the distributor on account of services and expenses in complying with the provisions of this article.

Section 289-c of the act reads in part as follows:

1. The tax imposed by this article though payable by the distributor, shall be borne by the purchaser and when paid by the distributor shall be deemed to have been so paid for the account of the purchaser. No person shall sell, advertise, or offer for sale motor fuel, separate from the tax herein imposed; and the price paid by the purchaser for motor fuel on which the tax has been paid, if such price be not less than the amount of the tax thereon, shall be presumed for the purpose of this section to have included the tax.

2. However, the intention of this article is to place the ultimate burden resulting from such tax, so far as possible, on persons who use the public highways of the State for operating motor vehicles thereon, and the following refunds are provided to that end, subject to the provisions of subdivision 5 of this section.

3. Any person who shall buy any motor fuel, on which the tax imposed by this article shall have been paid, and shall consume the same in any manner

except in the operation of a motor vehicle upon or over the highways of this State, shall be reimbursed, by the amount of such tax in the manner and subject to the conditions herein provided. All claims for reimbursements shall be made by affidavit in such form and containing such information, and be presented within such time, as the State tax commission, by rules and regulations, shall prescribe, and the claimant shall satisfy the department of taxation and finance that he has borne the tax and that the motor fuel has been consumed by him in a manner other than the operation of a motor vehicle upon or over the highways of this State. * * *

Section 23(c) of the Revenue Act of 1928 provides that in computing net income there shall be allowed as deductions taxes paid or accrued within the taxable year, with certain exceptions not here material. Article 151 of Regulations 74, promulgated under the Revenue Act of 1928, provides that in general taxes are deductible only by the person upon whom they are imposed.

From the foregoing quoted sections of the New York statute imposing a tax on gasoline and other motor fuel, it appears that the tax was intended to be imposed upon those purchasers of gasoline in the State of New York who use the gasoline as a propelling power for motor vehicles upon the public highways, etc., of the State. It is held, therefore, in accordance with the provisions of section 23(c) of the Revenue Act of 1928 and article 151 of Regulations 74, that the motor fuel tax imposed by the State of New York is deductible in the income tax return of the consumer who pays it and to whom it is not refunded. If, however, the tax in question is added to or made a part of the business expense of such consumer, it can not be deducted by him separately as a tax.

ARTICLE 151: Taxes.

VIII-32-4300

I. T. 2486

REVENUE ACT OF 1928.

The motor vehicle fuel tax imposed by the State of Delaware is a license tax for the use of the public highways of the State, and the tax is imposed upon the consumers of the motor fuel who purchase it from the dealers. Accordingly, it is held that the tax is deductible in the income tax returns of the consumers of motor fuel who pay the tax and to whom it is not refunded. However, if the tax is added to or made a part of the business expenses of such consumers, it can not be deducted separately as a tax.

The question is raised whether the motor vehicle fuel tax levied by the State of Delaware is deductible in the income tax returns of the consumers who purchase from the dealers.

The preamble of the statute imposing the tax (chapter 14, Laws of Delaware, 1923) reads in part as follows:

Whereas, it is found that the practicable effect of the levying of a tax on motor vehicle fuels sold by the dealers is that the tax is in fact collected from the consumer, by being added to the price of such fuel, and the burden of the tax paid by the dealer is passed on to and paid and borne by such ultimate consumer, and, accordingly, that the consumer who uses such motor vehicle fuel in motor vehicles and for the operation thereof is in practical effect paying a license fee and tax upon the motor vehicle itself; and

Whereas, it is deemed equitable and proper that persons purchasing motor fuels for purposes other than consumption and use in furnishing the propelling power for motor vehicles used or intended to be used in whole or in part upon the highways of this State should have refunded to them any money which they may be required to pay by reason of the tax provided for by this act; and

Whereas, the successful operation of such motor vehicles over the public roads and highways of the State depends in large measure upon the proper

construction, reconstruction and maintenance of such roads and highways; now therefore

*Be it enacted by the Senate and House of Representatives of the State of Delaware, in General Assembly met: * * **

Section 2 of chapter 14, Laws of Delaware, 1923, as amended by chapter 10, Laws of Delaware, 1927, provides:

SEC. 2. That each and every dealer as defined herein who is now engaged or who may hereafter engage in his own name, or in the name of others, or in the name of his representatives or agents in this State, in the sale or use of motor vehicle fuel as herein defined shall, not later than the last day of each calendar month, render to the State treasurer a statement of all motor vehicle fuel sold or used by him or them in this State during the preceding calendar month, and pay a license tax of three cents (3¢) per gallon on all motor vehicle fuel as shown by such statement in the manner and within the time hereinafter stipulated.

Section 9 of chapter 14, Laws of Delaware, 1923, reads:

SEC. 9. That any person, firm, or corporation who shall buy or use any motor vehicle fuel as defined in this act for the purpose of operating or propelling stationary gas engines, tractors used for agricultural purposes, motor boats, airplanes or aircraft, or who shall purchase or use any of such fuels for cleaning or dyeing or other commercial use except in motor vehicles operated or intended to be operated in whole or in part upon any of the public highways of this State, on which motor fuel the tax imposed by this act shall have been paid, *shall be reimbursed and paid the amount of such tax paid by him* upon presenting to the State treasurer a statement accompanied by the original invoices showing such purchases, which statement shall set forth the total amount of such fuel so purchased and used by such consumer other than in motor vehicles operated or intended to be operated upon any of the public highways of this State, and the said State treasurer, upon the presentation of such statement and vouchers, shall cause to be repaid to such consumer, from the taxes collected on motor vehicle fuels, the said taxes paid on fuels purchased or used other than for motor vehicles, as aforesaid; provided that applications for refunds as provided herein must be filed with the State treasurer within 90 days from the date of purchase or invoice. [Italics supplied.]

From the foregoing, it appears that the purpose of the law is to levy a license tax for the use of the public highways of the State, and that the tax is imposed upon the consumers of the motor fuel who purchase it from the dealers. Accordingly, it is held that the tax is deductible in the income tax returns of the consumers of motor fuel who pay the tax and to whom it is not refunded. However, if the tax is added to or made a part of the business expenses of such consumers, it can not be deducted separately as a tax.

ARTICLE 151: Taxes.

VIII-34-4315

I. T. 2487

REVENUE ACT OF 1928.

The motor vehicle fuel tax imposed by the State of Missouri is deductible in the income tax returns of the consumer of motor vehicle fuel who pays the tax and to whom it is not refunded. If the tax is added to and made a part of the business expense of such consumer, it can not be deducted separately as a tax.

The motor vehicle fuel tax imposed by the city of Kansas City, Mo., is deductible only in the income tax return of the dealer by whom it is paid and to whom it is not refunded. If the tax is deducted as a part of the business expense of such dealer or is added to or made a part of the cost of the motor vehicle fuel, it can not be deducted by him separately as a tax.

A ruling is requested as to whether the motor vehicle fuel taxes imposed by the State of Missouri and the city of Kansas City, Mo., are deductible in the income tax returns of the individual purchasers.

The motor vehicle fuel tax of the State of Missouri is levied in accordance with the provisions of the State Laws of Missouri, 1925, page 282, as amended, entitled "An act to provide funds for the completion of the construction of, and for the maintenance of the State highway system as designated by law, by a license tax equal to 2 cents per gallon of motor vehicle fuels used in motor vehicles on the public highways of this State, by increasing the fees for State registration of motor vehicles and by authorizing the board of fund commissioners to issue bonds authorized by the constitution and statutes for State highway construction not to exceed \$15,000,000 per year; providing for the distribution of the funds authorized by this act and providing penalties for the violation of the act."

The act defines "motor vehicle fuels" to include gasoline and such other volatile and inflammable liquids produced or compounded for the purpose of propelling motor vehicles over the highways of the State. Section 2 of the act reads as follows:

For the purpose of providing funds to complete the construction of and for the maintenance of the State highway system of this State as designated by law there is hereby provided a license tax equal to 2 cents per gallon of motor vehicle fuels as defined in this act used in motor vehicles on the public highways of the State, which license tax shall apply and become effective January 1, 1925.

Section 3 of the act provides that every distributor shall for the year 1925 and subsequent years pay to the State treasurer an amount equal to 2 cents for each gallon of motor vehicle fuels refined, manufactured, produced, or compounded by such distributor and sold by him in the State, or shipped, transported, or imported by such distributor into and distributed by him or sold by him within the State during such year.

Section 12 of the act reads in part as follows:

All motor vehicle fuels, as herein defined, distributed or sold in the State of Missouri by any distributor or dealer, shall be deemed to have been sold for use in operating motor vehicles upon the public highways of this State; provided, however, that any person who shall buy and use any motor vehicle fuels, as defined in this act, for the purpose of operating or propelling stationary gas engines, farm tractors or motor boats, or who shall purchase or use any of such fuels for cleaning, dyeing, or other commercial use of the same, or who shall buy and use such motor vehicle fuels for any purpose whatever, except in motor vehicles operated, or intended to be operated, upon any of the public highways of the State of Missouri, * * * and who shall have paid any license tax required by this act to be paid, either directly or indirectly through the amount of such tax being included in the price of such fuel, shall be reimbursed and repaid the amount of such tax directly or indirectly paid by him, upon presenting to the inspector an affidavit accompanied by the original invoice showing such purchase, which affidavit shall state the total amount of such fuels so purchased and used by such consumer, other than in motor vehicles operated or intended to be operated upon any of the public highways of the State of Missouri, as hereinbefore defined, and shall state for what purpose used. * * *

Section 23(c) of the Revenue Act of 1928 provides that in computing net income there shall be allowed as deductions taxes paid or accrued within the taxable year with certain exceptions not material to the question under consideration. Article 151 of Regu-

lations 74 provides that in general taxes are deductible only by the person upon whom they are imposed.

From the foregoing quotations from the Missouri State law imposing the motor vehicle fuel tax and pertaining to refunds thereof it appears that the purpose of the law is to impose a tax upon the purchaser of motor vehicle fuels used as a propelling power for motor vehicles upon the public highways, etc., of the State. It is held, therefore, in accordance with the provisions of section 23(c) of the Revenue Act of 1928 and article 151 of Regulations 74, that (1) the motor vehicle fuel tax imposed by the State of Missouri is deductible in the income tax returns of the consumer of motor vehicle fuel who pays the tax and to whom it is not refunded and (2) if the tax is added to and made a part of the business expense of such consumer it can not be deducted separately as a tax.

The motor vehicle fuel tax imposed by the city of Kansas City, Mo., is provided for in ordinance No. 54814. Section 3 B of that ordinance provides:

Every person, firm or corporation engaged in the business described in the foregoing section shall, at the time such license is issued, pay to the commissioner of licenses the sum of \$1, and shall thereafter, on or before the 16th day of January, April, July, and October of each year, pay to the commissioner of licenses a sum equal to 1 cent for each gallon of gasoline, benzine, or naphtha so sold, transported or stored by such person, firm or corporation during the preceding three months period, ending on the last day of the preceding December, March, June, and September, respectively. * * *

Section 3 E of the ordinance provides that the tax imposed by section 3 B shall not apply to the "sale, transportation or storage of gasoline, benzine, or naphtha used upon the premises of a manufacturer, cleaner or renovator in a manufacturing, cleaning or renovating process for which a license tax is, in this ordinance, elsewhere provided."

From the foregoing quoted provisions of ordinance 54814, imposing a tax on motor vehicle fuel, it is apparent that the tax in question is imposed upon the dealer who sells, stores, or transports motor vehicle fuel, etc., and not upon the consumer. It is held, therefore, that the motor vehicle fuel tax imposed by the city of Kansas City, Mo., is deductible only in the income tax returns of the dealer by whom it is paid and to whom it is not refunded. However, if the tax is deducted as a part of the business expense of such dealer or is added to or made a part of the cost of the motor vehicle fuel, it can not be deducted by him separately as a tax.

ARTICLE 151: Taxes.
(Also Section 41, Article 322.)

VIII-35-4324
G. C. M. 6667

REVENUE ACT OF 1928.

The ownership of property in the State of Washington on March 1 is the "event" which determines the liability for both real estate and personal property taxes and fixes the amount, although not ascertainable on that date. (Recommended that I. T. 2377 (C. B. VI-2, 59) be revoked.)

An opinion is requested relative to the accrual date of property taxes in the State of Washington.

In General Counsel's Memorandum 6273 (C. B. VIII-1, 168), involving the accrual date of property taxes in the State of Illinois, it was held that under the laws of Illinois the ownership of property on April 1 is the "event" which determines the liability for property taxes and fixes the amount, although not ascertainable on that date. (See also G. C. M. 6272, C. B. VIII-1, 170, involving the accrual date of property taxes in the State of Texas.)

An analysis of the statutes of the State of Washington and certain court decisions thereunder leads to the conclusion that both real and personal property taxes accrue on March 1. Section 11097 of Remington's Compiled Statutes of Washington, 1922, provides that all real and personal property shall be subject to assessment and taxation upon equalized valuations thereof, fixed with reference thereto on the 1st day of March at 12 o'clock meridian, in each and every year in which the same shall be listed.

Section 11109 provides that all real property shall be listed and assessed biennially in every even-numbered year with reference to its value on the 1st day of March preceding the assessment, and that personal property shall be listed and assessed every year with reference to its value on the 1st day of March preceding the assessment; provided, further, that all real estate subject to taxation shall be listed by the assessor every year in the detailed and assessment list, and in each odd-numbered year the valuation of each tract for taxation shall be the same as the valuation as equalized by the county board of equalization in the preceding year.

Section 11110 provides that the assessor shall complete the listing and placing of values on all real property by May 31 of each even-numbered year and on personal property annually.

Section 11127 provides that the owner of personal property moving from one county to another between the 1st day of March and the 1st day of July shall be assessed in either in which he is first called upon by the assessor. The owner of personal property moving into the State from another State between the 1st day of March and the 1st day of July shall list the property owned by him on the 1st day of March of such year in the county in which he resides.

Section 11137 requires owners or agents to file with the assessor a list of all personal property owned on March 1, 12 o'clock m.

Provision is made for a board of equalization for the correction of errors, for the actual levy of the tax and its collection, the latter generally beginning in January of each year.

Section 11272 provides that the taxes assessed upon real property shall be a lien thereon from and including the 1st day of March in the year in which they are levied until the same are paid. The taxes assessed upon personal property shall be a lien upon all the real and personal property of the person assessed from and after the date upon which such assessment is made.

In *Klickitat Warehouse Co. v. Klickitat County* (42 Wash., 299, 84 Pac., 860) the Supreme Court of Washington held that the lien for taxes on personal property attaches to the personal property and real estate of the person assessed immediately when such property is listed with the county assessor, and he has placed his value thereon. This case was followed in *city of Puyallup v. Lakin* (45 Wash., 368, 88 Pac., 578), in which it was said that the word "assessment" as

used in the law meant the valuation of property for taxation by the assessor and not the levy of taxes by the commissioners. It should be noted that these decisions did not mean that there was no liability for the taxes prior to the date the lien attached, as is clearly indicated by the decision of the same court in *Sloan Shipyards Corporation v. Thurston* (111 Wash., 361, 190 Pac., 1015). In this case the plaintiff alleged that the property assessed to it was not its property, and that it did not own the property on the 1st day of March, 1918, the date fixed by law as of which the property was required to be assessed. It appears that the plaintiff had filed with the assessor a list of personal property on March 11, 1918, and later contended that two of the four items listed were not owned by it on March 1, 1918; consequently, that it was not liable for the tax on those items. In denying the plaintiff's contention the court said:

The rule in regard to the ownership of property for the purpose of taxation is stated in 37 Cyc., at page 788, as follows:

"Ordinarily, and in the absence of statute to the contrary, property is taxable only to the person who is the owner thereof at the date for its listing or assessment, or the date fixed by statute as of which its ownership for purposes of taxation is to be determined; and taxes are not a lawful charge on property unless assessed in the name of its owner, and any attempt to enforce the payment of taxes assessed and charged to the wrong person will be ineffective. * * *"

* * * * *

* * * We are satisfied, therefore, that the trial court properly found that the appellant for the purpose of assessment was the owner of the property on the 1st day of March, 1918, and is therefore liable for the whole tax.

In view of the Washington statutes and decisions cited, this office is of the opinion that the ownership of property in Washington on March 1 is the "event" which determines the liability for both real estate and personal property taxes and fixes the amount, although not ascertainable on that date. (G. C. M. 6273, G. C. M. 6272, supra.) It is recommended that I. T. 2377 (C. B. VI-2, 59), holding that property taxes accrue upon delivery of the tax rolls or lists to the treasurer or collector of taxes, be revoked.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

ARTICLE 151: Taxes.

VIII-36-4334

I. T. 2491

REVENUE ACT OF 1928.

The motor vehicle fuel tax imposed by the State of South Dakota is deductible in the income tax return of the consumer who pays the tax and to whom it is not refunded. If the tax is added to or made a part of the business expenses of such consumer, it can not be deducted separately as a tax.

A ruling is requested as to whether the motor vehicle fuel tax imposed by the State of South Dakota is deductible in the income tax return of the individual purchaser.

Chapter 168 of the South Dakota Session Laws of 1927 imposes a tax of 3 cents per gallon, and chapter 169 imposes an additional tax of 1 cent per gallon, on the sale of motor vehicle fuel used in the State.

Section 1 of chapter 168, being an act approved March 11, 1927, entitled "An act imposing a tax on the sale or use of motor-vehicle fuels, prescribing exemptions from the same and providing for the payment, collection and disposition of the revenue derived from said tax, and providing penalties for the violation thereof * * *," defines "motor-vehicle fuel" to mean and include gasoline, benzine, naphtha, benzol, and all other volatile and inflammable liquids, not including kerosene oil, sold or used for the purpose of operating or propelling motor vehicles. That section defines "motor vehicle" to mean and include all vehicles, engines, or machines used on the public roads and highways within the State and which are operated or propelled in whole or in part by the combustion of any one or more of the motor vehicle fuels as defined in the act.

Section 2 of the act provides:

That a tax of 3 cents per gallon, or fraction thereof, is hereby imposed on the sale of all motor-vehicle fuel used in this State for any purpose whatsoever, provided said tax shall be paid but once. Said tax shall be computed upon all motor-vehicle fuel received by each dealer in this State and paid in a manner hereinafter provided: * * *.

Section 3 of the act provides that every dealer paying the tax imposed by the act, or being liable for the payment thereof, shall be entitled to charge and collect the sum of 3 cents per gallon on such motor vehicle fuel sold by him or them, for any purpose whatsoever, as a part of the selling price thereof.

Section 5 of the act provides that the amount of the tax shown by the dealer's report made to the State auditor and State treasurer as prescribed by the act shall on or before 30 days from the date of the filing of said report be paid by the dealer to the State treasurer. The State treasurer shall promptly credit the amounts so received by him to a fund to be known as the gasoline tax fund and shall distribute and apply such fund as provided in the act.

Section 9 of the act provides that any person, firm, or corporation, who shall purchase or receive any motor vehicle fuel from any dealer in the State in the original package in which the same shall have been imported, upon which fuel the said dealer shall not have assumed to pay the tax as provided in the act, shall, on the 25th day of each month, render to the State treasurer the same statement required of the dealer specified in the act, and he shall remit and pay to the State treasurer a tax of 3 cents per gallon on such motor vehicle fuel upon which the dealer has not assumed the tax as provided in section 5 of the act.

Section 10 provides that any person or persons, firm, or corporation, who shall buy or use any motor vehicle fuel as defined in the act for the purpose of operating or propelling stationary gas engines, tractors used for agricultural purposes, etc., or for any commercial use except motor vehicles operated or intended to be operated in whole or in part upon any of the public highways of the State of South Dakota, on which motor fuel the tax imposed by the act in question has been paid, shall be reimbursed and repaid the amount of such tax paid by him upon presentation to the State highway commission, on a form prescribed by the director of audits and accounts, of a sworn statement setting forth the information outlined in the act. Upon the presentation of such sworn statement the State highway commission shall cause to be repaid to such con-

sumer, from the taxes collected on motor vehicle fuels, the taxes on fuels purchased or used for purposes other than for motor vehicles operated upon any of the public highways of the State.

Section 23(c) of the Revenue Act of 1928 provides that in computing net income there shall be allowed as a deduction taxes paid or accrued within the taxable year, with certain exceptions not here material. Article 151 of Regulations 74, promulgated under the Revenue Act of 1928, provides that in general taxes are deductible only by the person upon whom they are imposed.

It appears from the foregoing that the purpose of chapter 168 of the South Dakota Session Laws of 1927 was to impose the tax upon the consumers of the motor vehicle fuel. Chapter 169, imposing an additional tax of 1 cent per gallon, is similar, and the same purpose is manifest. Accordingly, it is held (1) that the motor vehicle fuel tax imposed by the State of South Dakota is deductible in the income tax returns of the consumer who pays the tax and to whom it is not refunded, and (2) that if the tax is added to or made a part of the business expenses of such consumer it can not be deducted separately as a tax.

ARTICLE 151: Taxes.
(Also Section 41, Article 322.)

VIII-39-4365
I. T. 2495

REVENUE ACT OF 1928.

Personal property taxes imposed by the State of Kansas may be accrued as of March 1 and real property taxes as of November 1 by taxpayers whose books of account are kept on the accrual basis. The adoption of a monthly accrual basis in respect of such taxes is not permissible.

A ruling is requested in regard to the proper date of accrual for income tax purposes of property taxes imposed by the State of Kansas.

In this connection the taxpayer refers to the appeal of Russell Milling Co. (1 B. T. A., 194, C. B. IV-1, 3), wherein the Board of Tax Appeals held that property taxes imposed by the State of Kansas can be accrued only when they become due, and that no part thereof can be accrued and deducted in ascertaining net income when the due date is not within the taxpayer's fiscal year. The taxpayer also refers to recent memoranda of the Bureau in regard to the accrual date of property taxes imposed by the States of Illinois and Texas (G. C. M. 6273, C. B. VIII-1, 168, and G. C. M. 6272, C. B. VIII-1, 170), which memoranda revoked certain previously published memoranda on the subject.

In the case of *H. H. Brown Co. v. Commissioner* (8 B. T. A., 112, C. B. VII-1, 5) the Board stated that under the accrual system the word "accrued" does not signify that the item is due in the sense of being then payable, but that on the contrary the accrual system wholly disregards due dates. The Board further stated that it was not necessary that the amount of an incurred liability be accurately ascertained in order to accrue it.

The United States Supreme Court in *United States v. Anderson* (269 U. S., 422, T. D. 3839, C. B. V-1, 179) stated as follows:

In a technical legal sense it may be argued that a tax does not accrue until it has been assessed and becomes due; but it is also true that in advance of the assessment of a tax, all the events may occur which fix the amount of the tax and determine the liability of the taxpayer to pay it.

The position taken by the Bureau with respect to Illinois (G. C. M. 6273) and with respect to Texas (G. C. M. 6272) is that under the laws of those States the ownership of the property on the date as of which the property is assessed is the "event" which determines the liability for property taxes and fixes the amount thereof, although not ascertainable on that date, in accordance with the rule laid down in *United States v. Anderson*, supra.

With respect to the law of Kansas, section 79-309 of the Revised Statutes of Kansas of 1923 provides that all property shall be listed and valued as of the 1st day of March in the year in which the same is assessed, and the transfer or sale of any taxable personal property subsequent to the 1st day of March shall not authorize any person to omit the same from his list, although such list be not made until after the sale or transfer of such property; but all such property shall be listed for taxation in the same manner as if no sale or transfer thereof had been made. The section also contained a provision with regard to the taxation of bonds issued by the United States which was held unconstitutional. (*Lantz v. Hanna*, 111 Kan., 461, 207 Pac., 767; *Western Automobile Insurance Co. v. Lyons*, 112 Kan., 384, 210 Pac., 1117.) The law was, therefore, amended on March 14, 1925 (Laws of Kansas, 1925, page 359), in regard to the taxation of United States bonds, but the provision relating to the listing and valuation of the property as of the 1st day of March remained substantially the same.

In applying that section of law the Supreme Court of Kansas held in *Howell v. Scott* (44 Kan., 247, 24 Pac., 481) that the person who owned certain personal property on the 1st day of March was under a legal obligation to list such property for taxation for the year when called upon by the assessor to do so, and to pay the taxes thereon, notwithstanding he sold and transferred the same on the 8th day of March. In that case a stock of merchandise which had been in the county during the entire preceding year was sold and transferred on the 8th day of March. Thereafter the purchaser was assessed, and a tax warrant issued, under which the sheriff threatened to levy on the property. The court held that the purchaser was not liable to pay the taxes levied on such property, it being the duty of the vendor who owned the property on the 1st day of March to list the same for taxation; and that the purchaser was entitled to an injunction restraining the levy of the tax warrant.

With respect to the accrual of taxes imposed by the State of Kansas on real property the situation is different. Section 79-402 of the Revised Statutes of Kansas of 1923 provides that all real property in the State liable to assessment and taxation shall be assessed in the years 1916 and 1918, and in every fourth year after 1918. Section 79-1805 of the Revised Statutes of Kansas of 1923 provides that as between grantor and grantee of any land, where there is no express agreement as to which shall pay the taxes that may be assessed thereon, if such land is conveyed on or after the 1st day of March and before the 1st day of November, then the grantee shall pay the same; if conveyed on or after the 1st day of November and before

the 1st day of the next ensuing March, then the grantor shall pay them.

In the case of *Trinity Evangelical Lutheran Church of Kansas City v. Board of Commissioners of Wyandotte County et al.* (118 Kans., 742, 236 Pac., 809) the Supreme Court of Kansas considered the question as to the liability for taxes levied upon real property which had been conveyed to an exempt organization. In that case the court held that real estate conveyed to a church organization and occupied by its pastor as a parsonage on March 10, long before the preliminary steps taken had progressed to a charge on the parsonage, was exempt from taxes for that year which would have been due and payable the following 1st day of November. The court, in referring to section 79-309 of the Revised Statutes of Kansas, which provides that all property shall be listed and valued as of the 1st day of March in the year in which the same is assessed, stated as follows:

This provision is in a separate article which prescribes rules relating to the taxation of personal property alone. In a separate article a specific provision is found providing for the manner of assessing real estate. In it no definite tax day is prescribed, nor is any time fixed when a tax shall attach to or be deemed to become a charge on real estate. * * * No time being definitely fixed, we may look to the general scheme of taxation and search for the legislative intention as to the time the tax does attach.

* * * * *

Since neither the status of real estate for taxation nor a definite tax day was fixed by the legislature, we conclude that an assessment, if made on the parsonage, had not ripened into a charge upon the property and, therefore, that it was exempt from the taxes of the year. [Italics supplied.]

In view of the foregoing case decided by the Supreme Court of Kansas, it appears that the test of liability for taxes on real property is not the ownership thereof on March 1. It was held in *Gault v. Hurd* (103 Kan., 51, 172 Pac., 1011) that where a deed was delivered on September 23, the grantee was liable for the taxes which were due on the following 1st day of November. (See also *Armstrong v. Banking Trust Co.*, 96 Kan., 722, 153 Pac., 507.) These cases indicate that liability for real property taxes is determined as of November 1, and it follows that the owner on that date is the one who is entitled to claim a deduction for accrued property taxes in his return of net income.

This office is, therefore, of the opinion that under the law of Kansas ownership of personal property on March 1 and ownership of real property on November 1 are the "events" which, in accordance with *United States v. Anderson*, supra, determine the liability for such taxes and fix the amounts thereof. Personal property taxes in Kansas may accordingly be accrued as of March 1 and real property taxes as of November 1 by taxpayers whose books of account are kept on the accrual basis.

As to the suggestion that property taxes should be accrued monthly, so as to provide a reserve sufficient to meet the requirements at the time of payment or due date, it is the opinion of this office that such a theory of accrual is not in accord with the principle, recognized in *United States v. Anderson*, supra, that the liability should be accrued when it becomes fixed. Such principle, when applied in the light of the decisions of the Supreme Court of Kansas, above referred to, does not permit the adoption of a monthly accrual basis.

This ruling is based on the laws in effect prior to the amendment to section 79-402 of the Revised Statutes of Kansas of 1923, approved February 25, 1927 (Laws of Kansas, 1927, page 526), relating to real property taxes to be imposed for the year 1930 and subsequent years.

ARTICLE 151: Taxes.

VIII-40-4374

I. T. 2497

REVENUE ACT OF 1928.

The motor vehicle fuel tax imposed by the State of Illinois is deductible in the income tax return of the consumer of motor vehicle fuel who pays the tax and to whom it is not refunded. If the tax is added to and made a part of the business expense of such consumer, it can not be deducted separately as a tax.

A ruling is requested as to whether the motor vehicle fuel tax imposed by the State of Illinois is deductible in the Federal income tax return of the consumer.

The motor vehicle fuel tax in question is levied in accordance with the provisions of the law of the State of Illinois, approved March 25, 1929, and effective August 1, 1929, which is headed:

An act in relation to a tax upon the privilege of operating motor vehicles upon the public highways, based upon the consumption of motor fuel therein, and making certain appropriations in connection therewith.

Sections 2, 6, and 13 of the act referred to above read as follows:

SEC. 2. A tax is hereby imposed on the privilege of operating motor vehicles upon the public highways of this State after July 31, 1929, at the rate of 3 cents per gallon of all motor fuel used in such motor vehicles upon such public highways.

SEC. 6. Each distributor who sells any motor fuel for any purpose after July 31, 1929, shall collect from the purchaser at the time of such sale, 3 cents per gallon on all motor fuel sold, and at the time of making the monthly return, the distributor shall pay to the department of finance, the amount so collected " (less the deduction hereinafter provided)," and shall also pay to the department 3 cents per gallon on all motor fuel used by him during the period covered by the return. Each distributor shall determine the actual cost of making the collection and payment above provided on sales of motor fuel, subject to the approval of the department of finance, and such actual cost not to exceed 2 per cent of the amount so collected, shall be deducted from the amount to be paid by the distributor to the department. In each subsequent sale of motor fuel on which the 3 cents per gallon has been collected as herein provided, the amount so collected shall be added to the selling price, so that said amount is paid ultimately by the user of said motor fuel. However, no collection or payment shall be made in the case of the sale or use of any motor fuel which may not, under the Constitution and statutes of the United States, be made the subject of taxation by this State.

SEC. 13. Any person who loses motor fuel through any cause or uses motor fuel (upon which he has paid the amount required to be collected under this act) for any purpose other than operating a motor vehicle upon the public highways of this State, shall be reimbursed and repaid the amount so paid.

* * *

In section 17 of the act it is stated that it is the purpose of the act to impose a tax upon the privilege of operating each motor vehicle upon the public highways of the State of Illinois, such tax to be based upon the consumption of motor vehicle fuel in such motor vehicle, so far as the same may be done, under the Constitution and statutes of the United States and the constitution of the State of Illinois.

Section 23(c) of the Revenue Act of 1928 provides that in computing net income there shall be allowed as a deduction taxes paid or accrued within the taxable year, with certain exceptions not here material. Article 151 of Regulations 74, promulgated under the Revenue Act of 1928, provides that in general taxes are deductible only by the person upon whom they are imposed.

From the foregoing quoted sections of the law of the State of Illinois imposing a tax on motor vehicle fuels, it appears that the tax was intended to be imposed upon the consumer of motor vehicle fuels for the privilege of operating motor vehicles upon the public highways. It is held, therefore, in accordance with the provisions of section 23(c) of the Revenue Act of 1928 and article 151 of Regulations 74, that the tax in question is deductible in the income tax return of the consumer who pays it and to whom it is not refunded. If, however, the tax is added to or made a part of the business expenses of such consumer, it can not be deducted by him separately as a tax.

ARTICLE 151: Taxes.

VIII-40-4375

I. T. 2498

REVENUE ACT OF 1928.

The motor vehicle fuel tax imposed by the State of New Hampshire is deductible in the income tax return of the consumer who pays it and to whom it is not refunded. If, however, the tax in question is added to or made a part of the business expense of such consumer, it can not be deducted by him separately as a tax.

A ruling is requested as to whether the motor vehicle fuel tax imposed by the State of New Hampshire is deductible in the income tax return of the consumer.

Section 1 of chapter 75, Laws of the State of New Hampshire, 1923, provides that the fuels to which the tax in question applies shall include gasoline, benzol, or other products used in internal combustion engines in the propulsion of motor vehicles on the highways of the State.

Section 3 of chapter 104, Public Laws of the State of New Hampshire, 1926, as amended by chapter 123, Laws of the State of New Hampshire, 1927, reads as follows:

3. *Reports.*—Every distributor shall, on or before the 15th day of each month, render a report to the commissioner on forms to be furnished by him, stating the number of gallons of such fuels used or sold in the State during the preceding calendar month and such other information as the commissioner shall prescribe.

Section 4 of chapter 104, Public Laws of the State of New Hampshire, 1926, as amended by chapter 75 (effective May 1, 1927), Laws of the State of New Hampshire, 1927, reads:

14. *Payment.*—On or before the 1st day of the calendar month succeeding the filing of said report, the distributor shall pay to the State treasurer a road toll of 3 cents per gallon, upon each gallon so reported, the same being collected by the distributor from the dealer, and by the dealer from the consumer.

Section 7 of chapter 104, Public Laws of the State of New Hampshire, 1926, reads as follows:

7. *Fuels for other uses.*—Whenever any person shall purchase any such fuels for any purpose other than for the propulsion of motor vehicles upon highways he may, within six months after the date of said purchase, present to the State

treasurer, on blanks furnished by him, a statement under oath as to the number of gallons used for such other purposes and the name of the person from whom purchased. The State treasurer, upon satisfying himself that said fuel was actually used for such other purposes, shall refund the road toll to said purchaser.

Section 6 of chapter 1 (approved November 29, 1927) of the laws of the State passed by the State legislature at the special session of 1927 (New Hampshire Public Acts and Joint Resolutions of the Legislature of 1929 and Special Session of 1927) provided for the collection, beginning January 1, 1928, of "a further motor vehicle road toll of 1 cent per gallon in addition to the motor vehicle road toll now provided by law," such additional toll to be "collected in accordance with chapter 104 of the public laws as amended by chapter 75 of the acts of 1927." Section 8 of chapter 41 (approved March 6, 1929), of the acts of 1929, just cited, changes the period during which this additional 1 cent toll is to be in force but makes no change in the manner of collection.

Section 23(c) of the Revenue Act of 1928 provides that in computing net income there shall be allowed as a deduction taxes paid or accrued within the taxable year, with certain exceptions not here material. Article 151 of Regulations 74, promulgated under the Revenue Act of 1928, provides that in general taxes are deductible only by the person upon whom they are imposed.

From the provisions of the sections of the State law quoted above, it appears that the motor vehicle fuel tax imposed by the law of the State of New Hampshire is imposed upon the consumer who purchases motor vehicle fuel for the purpose of propelling motor vehicles upon the highways of the State. It is held, therefore, in accordance with the provisions of section 23(c) of the Revenue Act of 1928 and article 151 of Regulations 74, that the motor vehicle fuel tax imposed by the State of New Hampshire is deductible in the income tax return of the consumer who pays it and to whom it is not refunded. If, however, the tax in question is added to or made a part of the business expense of such consumer, it can not be deducted by him separately as a tax.

ARTICLE 151: Taxes.

VIII-41-4381

I. T. 2500

REVENUE ACT OF 1928.

The deduction of additional South Carolina State income taxes by a taxpayer on the accrual basis is allowable for Federal income tax purposes only for the year in which the income upon which they are based is earned.

A ruling is requested as to whether additional South Carolina State income taxes paid in later years should be considered to accrue in the year in which the income upon which they are based is earned or whether they may be said to accrue in the year in which the additional tax is determined and paid.

It has been the consistent position of the Bureau that income taxes, whether original or additional, accrue in the year in which the income upon which they are based is earned. If the tax shown by a taxpayer to be due in an original return is subsequently found to be

incorrect, the tax which was properly accruable has always been regarded as the amount which should have been shown to be due with all the proper corrections made in the taxpayer's return. It is by virtue of the taxing statute as it exists at the end of the taxable year that a tax accrues, and the fact that the tax is not definitely ascertained at the end of such year is immaterial. See *United States v. Anderson et al.* and *United States v. Yale & Towne Manufacturing Co.* (269 U. S., 422, T. D. 3839, C. B. V-1, 179) and the comment made thereon in the following extract from the opinion of the Board of Tax Appeals in the case of *Ernest M. Bull, Executor, v. Commissioner* (7 B. T. A., 993, C. B. VII-1, 5) :

The suggestion arises that it is difficult to determine the amount of the estate tax within the period when the first income tax of the estate must be computed and the return audited. This might well give pause. But it is usually no more difficult than the computation of the munitions tax involved in the Yale & Towne case or that required by section 1207 of the Revenue Act of 1926 and the earlier regulations, and such difficulty as there may be is not sufficient to counterbalance the considerations already set forth.

We hold that for the purpose of the deduction allowed in section 214(a)3 of the Revenue Act of 1918, the estate tax of Title IV accrued at the date of the death of testator and may be deducted by the estate in the taxable period of the death, if this is in accordance with its method of accounting, so as clearly to reflect its income. In view of the agreement of the parties as to the method of accounting, we reverse the holding of the respondent on this issue.

There is no provision in the Federal Revenue Acts which would permit additional State income taxes determined and paid in later years to be regarded as an accrual for any other year than that in which the income upon which they are based is earned.

It is therefore held that the deduction of additional South Carolina State income taxes by a taxpayer on an accrual basis is allowable for Federal income tax purposes only for the year in which the income upon which they are based is earned.

ARTICLE 151: Taxes.

VIII-45-4420

I. T. 2505

REVENUE ACT OF 1928.

The tax imposed by the State of Pennsylvania on liquid fuels is deductible in the income tax return of the consumer who pays the tax. If the tax is added to or made a part of the business expenses of such consumer, it can not be deducted separately as a tax.

A ruling is requested as to whether the tax on liquid fuels imposed by the State of Pennsylvania by the act of May 1, 1929, as amended, is deductible in the Federal income tax return of the individual consumer. The act is entitled:

An act imposing a State tax on liquid fuels, including all liquids ordinarily, practically, and commercially usable in internal combustion engines for the generation of power, including all distillates of and condensates from petroleum, natural gas, coal, coal tar, and vegetable ferments so usable and sold by dealers in this Commonwealth, except for the purpose of resale, or used by consumers, when no tax thereon has been collected by dealers; providing for the collection of such tax, and the creation of liens; and for the distribution and use of the revenues derived from such tax; requiring bonds from dealers; and providing for the compensation of dealers; providing for the filing of certificates and reports of the sale of such liquid fuels to dealers and consumers as defined in this act; providing for the issuing, revoking, and use of permits; and fixing penalties.

Section 3 of the act reads as follows:

Until the 1st day of July, 1930, a State tax of 4 cents a gallon, or fraction thereof, and thereafter a State tax of 3 cents a gallon, or fraction thereof, is hereby imposed and assessed upon all liquid fuels sold by dealers in this Commonwealth, except for the purpose of resale, and upon all liquid fuels used within this Commonwealth by consumers when no such tax has been collected thereon by a dealer, except liquid fuels purchased, received or consumed by the United States, or any department, board, commission, or other agency or instrumentality thereof. Duplicate taxation is not intended, but the tax hereby imposed shall apply to all liquid fuels sold or used within this Commonwealth, excepting such transactions in interstate or foreign commerce as are not within the taxing power of the State. The taxes on sales hereby provided for shall be collected by the dealers selling liquid fuels to purchasers who purchase for purposes other than resale; and the taxes on use shall be paid by the consumers who use liquid fuels upon which the tax has not been paid; and said taxes shall be paid by such dealers and consumers into the State treasury through the department in the manner and within the times herein specified. For and in consideration of the filing of the certificate and bond, as provided for in this act, and for and in consideration of the collection of the aforesaid tax, the dealer shall be allowed a commission of 1 per centum on the first \$2,000, or any part thereof, of tax paid by him to the department of revenue; and one-half of 1 per centum on all sums in excess thereof. The commission may be deducted by the dealer in making his payments. The commission shall be allowed only on the aggregate of the tax paid by a dealer for any period, whether his report of sales and use of liquid fuels are combined in one report or made in separate reports.

In accordance with the provisions of section 4 of the act, for the purpose of ascertaining the amount of taxes, it shall be the duty of every dealer and consumer to transmit to the department of revenue of the State of Pennsylvania, hereinafter referred to as the department, a statement, under oath, upon a prescribed form, showing the number of gallons of liquid fuels purchased, sold, or used by such dealer or consumer during the preceding month from the respective places of business of such dealer or consumer. Upon such statement or return the department shall make a determination of the taxes owing to the State. Section 5 of the act provides that every dealer and consumer, at the time of making the statement required by section 4, shall pay to the State treasurer, through the department, the amount of the tax due for the month covered by such statement.

Section 9 of the act reads in part as follows:

The tax imposed by this act shall be paid by the person, firm, copartnership, association, or corporation, purchasing liquid fuels from dealers for his own use and not for the purpose of resale, or by the person, firm, copartnership, association, or corporation, using liquid fuels, upon which no tax has been collected by a dealer; and every person, firm, copartnership, association, or corporation, required by this act to collect the tax herein specified, shall state the amount of such tax, separately from the price of the said liquid fuels, on all liquid fuel price display signs, sales or delivery slips, bills, statements, etc. * * *

Section 23(c) of the Revenue Act of 1928 provides that in computing net income there shall be allowed as deductions taxes paid or accrued within the taxable year, with certain exceptions not here material. Article 151 of Regulations 74, promulgated under the Revenue Act of 1928, provides that in general taxes are deductible only by the person upon whom they are imposed.

From the foregoing quoted sections of the law of the State of Pennsylvania imposing a tax on liquid fuels, it appears that the tax was intended to be imposed upon the consumer of liquid fuels,

and not upon the dealer. In accordance with the provisions of section 23(c) of the Revenue Act of 1928 and article 151 of Regulations 74, it is held that the tax in question is deductible in the income tax return of the consumer who pays it. If, however, such tax is added to or made a part of the business expenses of such consumer, it can not be deducted by him separately as a tax.

ARTICLE 151: Taxes.

VIII-46-4426
G. C. M. 7071

REVENUE ACT OF 1928.

The tax imposed by the State of Washington on liquid fuel is deductible in the income tax return of the consumer who pays it and to whom it is not refunded. If, however, the tax in question is added to or made a part of the business expense of such consumer, it can not be deducted by him separately as a tax.

An opinion is requested as to whether the tax on liquid fuel imposed by the State of Washington is deductible in the Federal income tax return of the consumer.

Chapter 173 of the Session Laws of the State of Washington, 1921, imposes an excise tax of 1 cent per gallon on all liquid fuel sold by distributors and requires that the tax be paid by the distributors. The terms "liquid fuel," "liquid fuels," "fuel," and "fuels," as used in the act, are defined to mean and include gasoline and all volatile and inflammable liquid fuels produced or compounded for the purpose of operating or propelling internal combustion engines, but kerosene is not to be considered a liquid fuel within the meaning of the act.

Chapter 81 of the Session Laws of the State of Washington, 1923, effective from and after January 1, 1924, amended sections 8328 and 8331 of Remington's Compiled Statutes of Washington, 1922, and added two new sections, known as sections 8328-1 and 8331-1.

Section 8328-1 reads as follows:

Every person, firm, or corporation, including distributors, who shall use liquid fuel for the purpose of operating motor vehicles, including motor trucks, upon the highways of the State, or the political subdivisions thereof, upon the sale or use of which liquid fuel the excise tax imposed by this chapter has not been theretofore paid, shall pay an excise tax of 2 cents per gallon upon all such liquid fuel so used, and, in so far as such liquid fuel is concerned, shall make the same reports and pay the same taxes as and be subject to all the other provisions of this chapter relating to distributors of liquid fuel: *Provided*, That any tourist or traveler coming into the State in a motor vehicle may transport, for his own use only, not more than 20 gallons of liquid fuel at one time and use the same for the purpose of operating such motor vehicle without the payment of said tax.

Section 8331-1 provides in part as follows:

Any person, firm or corporation who shall buy and use any liquid fuel as defined in this chapter for the purpose of operating or propelling stationary gas engines, farm tractors or motor boats, or who shall purchase and use any such fuel for cleaning or dyeing or other commercial use of the same, except in motor vehicles operated or intended to be operated upon any of the public highways of the State, and who shall have paid any tax on such liquid fuel, levied or directed to be paid as provided by this act, either directly by the collection of such tax by the vendor from such consumer, or indirectly by adding the amount of such tax to the price of such liquid fuel and paid by such consumer, shall be reimbursed and repaid the amount of such tax paid by him upon presenting to the State treasurer an affidavit accompanied by the original invoice showing such purchase, which affidavit shall be verified by the oath of the con-

sumer, and shall state the total amount of such liquid fuel so purchased and used by such consumer, other than in motor vehicles operated or intended to be operated upon any of the highways of the State * * *.

Section 3 of chapter 88 of the Session Laws of the State of Washington, 1929, effective July 1, 1929, contains the following provision:

That in addition to the excise tax required to be paid by each distributor of liquid fuel under the provisions of chapter 173 of the Laws of 1921, as amended by chapter 81 of the Laws of 1923, or heretofore, or hereafter, otherwise amended, there shall be paid to the State treasurer by every such distributor, in the manner and at the times of paying the excise taxes provided for by said acts, an excise tax of 1 cent per gallon on all liquid fuel sold by him.

Section 4 of the 1929 act, referred to above, reads as follows:

Every person, firm, or corporation, including distributors, who shall use liquid fuel for the purpose of operating motor vehicles, including motor trucks, upon the public highways of the State, or the political subdivisions thereof, upon the sale or use of which liquid fuel the additional 1 cent excise tax imposed by this act has not been theretofore paid, shall pay a tax of 1 cent per gallon in addition to the tax imposed by section 2 of chapter 81 of the Laws of 1923, or any amendments heretofore or hereafter made to said chapter, upon all such liquid fuel so used, and, in so far as such liquid fuel is concerned, shall make the same reports and pay the same taxes and be subject to all the other provisions of this act relating to distributors of liquid fuel: *Provided*, That any tourist or traveler coming into the State in a motor vehicle may transport, for his own use only, not more than 20 gallons of liquid fuel at one time and use the same for the purpose of operating such motor vehicle without the payment of said tax.

A provision similar to that just quoted, requiring that the tax unless already paid be paid by the user, is contained in the 1923 act.

Section 23(c) of the Revenue Act of 1928 provides that in computing net income there shall be allowed as deductions taxes paid or accrued within the taxable year, with certain exceptions not here material. Article 151 of Regulations 74, promulgated under the Revenue Act of 1928, provides that in general taxes are deductible only by the person upon whom they are imposed.

Upon consideration of the provisions of law which are quoted or to which reference is made above, it appears that the purpose of the law was to impose a tax upon the consumer of liquid fuel. Therefore, it is held that the tax imposed by the State of Washington on liquid fuel is deductible in the income tax return of the consumer who pays it and to whom it is not refunded. If, however, the tax in question is added to or made a part of the business expense of such consumer, it can not be deducted by him separately as a tax.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

ARTICLE 151: Taxes.

VIII-47-4432
G. C. M. 7098

REVENUE ACT OF 1928.

The motor-fuel and kerosene tax imposed by the State of Georgia is an occupation tax imposed upon distributors of such motor fuel and kerosene, and is deductible by the distributor who pays it and not by the purchaser. If, however, the tax is added to or made a part of the business expenses of such distributor, it can not be deducted separately as a tax.

An opinion is requested as to whether the motor-fuel and kerosene tax imposed by the State of Georgia is deductible in the income tax return of the purchaser.

The act of the General Assembly of the State of Georgia approved August 24, 1927, effective September 1, 1927 (Acts and Resolutions of the General Assembly of the State of Georgia, 1927, page 104), provides for an "occupation tax" upon all distributors of motor fuels and kerosene engaged in business in the State. The act defines the word "distributor" to include any person, association of persons, firm, corporation, and political subdivision of the State, (a) that imports or causes to be imported, and sells at wholesale or retail or otherwise within the State, any of the fuels or kerosene as specified therein; or (b) that imports or causes to be imported, and withdraws for use within the State by himself or others, any of such fuels or kerosene from the tank-car or other original container or package in which imported into the State; or (c) that manufactures, refines, produces, or compounds any of such fuels or kerosene within the State, and sells the same at wholesale or retail or otherwise within the State for use or consumption within the State. It excludes "any retail dealer in such fuels or kerosene, or operator or proprietor of a gasoline filling station or public garage or other place at which such fuels are sold, where such dealer or other person procures his entire supply thereof from a 'distributor' as above defined * * *."

Section 2 of the act provides as follows:

Be it further enacted by the authority aforesaid, that each distributor of fuels who engages in such business in this State shall pay an occupation tax of 4 cents per gallon, for each and every gallon of such fuels (1) imported and sold within this State, or (2) imported and withdrawn for use within this State, or (3) manufactured, refined, produced, or compounded within this State and sold for use or consumption within this State, or used and consumed within this State by the manufacturer, refiner, producer, or compounder. Nothing in this act contained shall be so construed as to cause double taxation on any of the products specified herein. Where kerosene or fuels are manufactured or refined in this State and shipped out of this State, and are brought back into this State and used or consumed, the respective taxes herein fixed shall be paid on such kerosene and fuels. Any manufacturer or refiner in this State may sell to any duly licensed distributor under the terms of this act, and require the purchasing distributor to pay the tax herein imposed; provided, such manufacturer or refiner shall report all such sales to the comptroller-general not later than the next business day after the shipment was made, giving full details of the sale, including quantity, the car initials and number if a carload shipment, date of shipment, and name and address of consignee. * * *

Section 6 provides as follows:

Be it further enacted by the authority aforesaid, that each distributor of fuels and kerosene engaged in such business in this State shall pay the occupation tax of 4 cents per gallon on fuels and 1 cent per gallon on kerosene, as herein provided, to the comptroller-general of this State. * * *

The act of the General Assembly of the State of Georgia approved August 19, 1929, amending the act of August 24, 1927, increases the amount of the tax to be paid by distributors of fuels to 6 cents a gallon.

Section 23(c) of the Revenue Act of 1928 provides in part that in computing net income there shall be allowed as deductions taxes paid or accrued within the taxable year, with certain exceptions not here material.

Article 151 of Regulations 74, promulgated under the Revenue Act of 1928, provides that in general taxes are deductible only by the person upon whom they are imposed.

There is nothing in the Georgia statutes, above referred to, either by provision for a refund of the tax or otherwise, to indicate an intention or purpose to impose a tax upon the purchaser of motor fuels or kerosene. The statutes by their express terms, however, do evidence a clear purpose to impose "an occupation tax upon all distributors of motor-fuels and kerosene" doing business in the State. It is, therefore, the opinion of this office that the motor-fuel and kerosene tax imposed by the State of Georgia is an occupation tax imposed upon distributors of such motor fuels and kerosene, and is deductible under the provisions of section 23(c) of the Revenue Act of 1928 and article 151 of Regulations 74 by the distributor who pays it and not by the purchaser. If, however, the tax in question is added to or made a part of the business expense of such distributor, it can not be deducted separately as a tax.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

ARTICLE 151: Taxes.

VIII-48-4440
I. T. 2510

REVENUE ACT OF 1928.

The tax imposed by the State of Rhode Island on gasoline and other products used in the propelling of motor vehicles is deductible in the income tax return of the consumer who pays it and to whom it is not refunded. If, however, the tax is added to or made a part of the business expense of such consumer, it can not be deducted by him separately as a tax.

A ruling is requested as to whether the tax imposed by the laws of the State of Rhode Island on gasoline and other products used in the propelling of motor vehicles is deductible for Federal income tax purposes in the income tax return of the individual consumer.

The tax in question is levied in accordance with the provisions of chapter 679 of the Public Laws of Rhode Island, 1925, as amended by chapter 1033 of the Public Laws of Rhode Island, 1927, and chapter 1405 of the Public Laws of Rhode Island, 1929, entitled "An act providing for a tax upon gasoline and other products used in the propelling of motor vehicles."

Section 4 of the act contains the following provisions:

Every distributor shall, on or before the 15th day of each month, render a report under oath to the board, upon forms to be obtained from the board, of the amount (number of gallons) of fuels purchased, sold or used by him or it within this State and the amount of fuels sold by him or it without this State from fuels within this State during the preceding calendar month and, if required by the board, as to purchases, the name or names of the person or persons from whom purchased and the date and amount of each purchase, and as to sales, the name or names of the person or persons to whom sold and the amount and date of each sale. The board shall assess a tax of 2 cents per gallon on all fuels sold or used by such distributor within this State, and on or before the 1st day of the calendar month next succeeding the filing of such report said board shall certify to the general treasurer the amount of the tax due from each distributor, and on or before the 10th day of such calendar month each distributor shall pay to the general treasurer the tax so certified.

Section 5 of the act reads in part as follows:

Any person who shall purchase fuels on which the tax provided in this chapter shall have been paid and shall use the same in any manner other than for operating or propelling motor vehicles shall be reimbursed the amount of such tax in the manner and subject to the conditions herein provided. * * *

Section 23(c) of the Revenue Act of 1928 provides that in computing net income there shall be allowed as a deduction taxes paid or accrued within the taxable year, with certain exceptions not here material. Article 151 of Regulations 74, promulgated under the Revenue Act of 1928, provides that in general taxes are deductible only by the person upon whom they are imposed.

From the provisions of the sections of the public laws of Rhode Island, quoted above, it appears that the tax on gasoline and other motor fuel is imposed upon the consumer who purchases it for use in operating or propelling motor vehicles. It is held, therefore, in accordance with the provisions of section 23(c) of the Revenue Act of 1928 and article 151 of Regulations 74, that the tax imposed by the State of Rhode Island on gasoline and other products used in the propelling of motor vehicles is deductible in the income tax return of the consumer who pays it and to whom it is not refunded. If, however, the tax in question is added to or made a part of the business expense of such consumer, it can not be deducted by him separately as a tax.

ARTICLE 151: Taxes.

VIII-49-4449
G. C. M. 7167

REVENUE ACTS OF 1924 AND 1928.

The motor vehicle fuel tax imposed by the State of Maryland is a tax imposed upon the consumer and not upon the dealer and is deductible, for Federal income tax purposes, by the consumer who pays it and to whom it is not refunded. If, however, such tax is added to or made a part of the business expense of such consumer, it can not be deducted separately as a tax.

Recommended that I. T. 2157 (C. B. IV-1, 35) be revoked in so far as it holds that the motor vehicle fuel tax imposed by the State of Maryland is deductible only by the dealers.

An opinion is requested as to whether the motor vehicle fuel tax imposed by the State of Maryland is deductible, for Federal income tax purposes, by the consumer.

Section 211 of article 56 of the Annotated Code of Maryland, 1924, defines "motor vehicle fuels" to be such fuels as gasoline and such other volatile and inflammable liquids produced or compounded for the purpose of operating or propelling motor vehicles, except the product commonly known as kerosene oil.

Section 212 of article 56 of the Annotated Code of Maryland, 1924, provides:

On and after January 1, 1924, each and every dealer as defined in this subtitle who is now engaged or who may hereafter engage in his own name or in the name of others, or in the name of his representatives or agents in this State, in the sale or use of motor vehicle fuel as herein defined shall not later than the last day of each calendar month render to the comptroller a statement of all motor vehicle fuel sold or used by him or them in the State of Maryland during the preceding calendar month, and pay a license tax of two (2) cents per gallon on all motor vehicle fuel as shown by such statement in the manner and within the time hereinafter stipulated (provided, however, that the tax imposed upon motor vehicle fuel sold to compounders shall be returned and paid as herein provided by such compounders upon all motor vehicle fuel purchased by them and sold or used in the State of Maryland in the form of a compound or otherwise).

Section 219 of article 56, referred to above, provides:

Any person, firm or corporation who shall buy or use any motor vehicle fuel as defined in this subtitle for the purpose of operating or propelling stationary gas engines, tractors used for agricultural purposes, motor boats, airplanes, or aircraft, or who shall purchase or use any of such fuel for cleaning or dyeing or other commercial use of the same, except in motor vehicles operated or intended to be operated in whole or in part upon any of the public highways of the State of Maryland, on which motor fuel the tax imposed by this subtitle shall have been paid, shall be reimbursed and repaid the amount of such tax paid by him upon presenting to the comptroller a statement accompanied by the original invoices showing such purchase, which statement shall set forth the total amount of such fuel so purchased and used by such consumer, other than in motor vehicles operated or intended to be operated upon any of the public highways of the State of Maryland * * *.

Section 212-A of article 56 of the Annotated Code of Maryland, 1924, as added by chapter 327 of the Laws of Maryland, 1927, was repealed and reenacted by chapter 96, Laws of Maryland, 1929, to read as follows:

On and after the 1st day of April, 1927, the license tax in respect of motor vehicle fuels, prescribed by this subtitle, shall be increased one-half cent per gallon. The State treasurer shall create a special fund of the receipts from the said additional tax of one-half cent per gallon, and shall disburse the same monthly (less such sum to be retained by the comptroller as, in the judgment of the comptroller, shall be sufficient to enable him to pay promptly all claims for refunds), as follows: One-fifth thereof to the mayor and city council of Baltimore, to be used for the elimination of railroad grade crossings within the limits of said city, and the balance to be credited to the account of the State Roads Commission of Maryland, to be paid out of the treasury of the State, only upon the warrant of the comptroller, and to be used for the elimination of railroad grade crossings, as provided by sections 38A to 38J, both inclusive, of article 91 of the code of 1924, as enacted by chapter 327 of the Acts of 1927.

Chapter 118 of the Laws of Maryland, 1927, added sections 212-B and 212-C to article 56 of the Annotated Code of Maryland, 1924.

Section 212-B provides that on and after the 1st day of April, 1927, "the license tax in respect of motor vehicle fuels, prescribed by this subtitle, shall be increased 1½ cents per gallon."

Section 212-C provides:

Any person, firm or corporation, who shall purchase and use any motor vehicle fuel, in respect of which the tax imposed by section 212-B has been paid, for the purpose of propelling any motor vehicle, equipped with a commercial body, or any motor vehicle used and registered pursuant to law for use in the transportation of persons for hire, shall be reimbursed and repaid out of the "lateral road gasoline tax fund" 1 cent per gallon for each gallon of motor vehicle fuel used in such motor vehicle; provided such motor vehicle is regularly operated as a part of the principal business of the person, firm or corporation by whom the claim for refund is made; and provided further, that such motor vehicle while specially licensed as provided in this act is operated exclusively within the corporate limits of Baltimore City or of any other incorporated city or town in Maryland * * *.

Section 23(c) of the Revenue Act of 1928 provides that in computing net income there shall be allowed as deductions taxes paid or accrued within the taxable year, with certain exceptions not here material. Article 151 of Regulations 74, promulgated under the Revenue Act of 1928, provides that in general taxes are deductible only by the person upon whom they are imposed.

It appears from the above-quoted provisions of the laws of the State of Maryland that the motor vehicle fuel tax here in question is imposed upon the consumer and not upon the dealer. It is held, therefore, in accordance with section 23(c) of the Revenue Act of

1928 and article 151 of Regulations 74, that such tax is deductible, for Federal income tax purposes, by the consumer who pays it and to whom it is not refunded. If, however, such tax is added to or made a part of the business expense of such consumer, it can not be deducted by him separately as a tax. It is recommended that I. T. 2157 be revoked in so far as it holds that the motor vehicle fuel tax imposed by the State of Maryland is deductible only by the dealers.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

ARTICLE 151: Taxes.

VIII-50-4462

I. T. 2512

REVENUE ACT OF 1928.

The tax imposed by the State of Massachusetts on gasoline is deductible in the income tax return of the consumer who pays it and to whom it is not refunded. If, however, the tax is added to or made a part of the business expense of such consumer, it can not be deducted by him separately as a tax.

A ruling is requested as to whether the gasoline tax imposed by the State of Massachusetts is deductible in the Federal income tax return of the individual consumer.

The gasoline tax in question is levied in accordance with chapter 316, Acts and Resolves of Massachusetts, 1928, which is headed:

An act changing the method of raising funds toward the cost of construction and maintenance of highways and bridges by providing that the excise tax on the privilege of registering motor vehicles as fit for operation on the highways in so far as it relates to such operation by means of gasoline or other petroleum products be measured in part on the amount thereof so consumed instead of wholly upon the horsepower or weight and carrying capacity.

Sections 4, 7, and 9 of the law referred to above read as follows:

SEC. 4. Every distributor shall, on or before the 15th day of each month, file with the commissioner a return under oath, on forms to be furnished by the commissioner, stating the number of gallons of fuel sold by him in the Commonwealth during the preceding calendar month, and said returns shall contain or be accompanied by such further information as the commissioner shall require. On or before the 15th day of each month next succeeding the filing with the commissioner of said return, each distributor shall pay to the commissioner for the account of the purchaser an excise of 2 cents on each gallon of fuel sold by him in the Commonwealth during the calendar month covered by the return.

* * * * *

SEC. 7. Unless otherwise provided by the rules or regulations of the commissioner made under authority of this section, any person who shall buy any fuel, on which an excise has been paid or is chargeable under this chapter, and shall consume the same in any manner except in the operation of motor vehicles upon or over the highways of the Commonwealth, shall be reimbursed the amount of said excise in the manner and subject to the conditions herein provided. All claims for reimbursement shall be made by affidavit in such form and containing such information as the commissioner shall prescribe, and shall be accompanied by original invoices or sales receipts, and shall be filed with the commissioner within 90 days from the date of purchase or invoice. The commissioner may require such further information as he shall deem necessary for the determination of such claims, and shall within 30 days after receipt transmit all claims approved by him to the comptroller for certification;

and the amount approved by the commissioner and certified as aforesaid shall be paid forthwith from the proceeds of the excise tax levied under this chapter, without specific appropriation. The commissioner shall provide by reasonable rules or regulations for the sale of fuel, free of the excise imposed by this chapter, by any person, to the ultimate purchaser upon the receipt of a written statement, signed by such ultimate purchaser, that such fuel is intended to be consumed in some manner other than in the operation of motor vehicles upon or over the highways of the Commonwealth, and if such excise has already been paid or is chargeable, for the reimbursement, out of the proceeds of the excise levied under this chapter, of the person so selling such fuel, to the amount of such excise.

* * * * *

SEC. 9. Except as otherwise provided in section 7, the tax in every instance shall be borne by the purchaser, and no person offering fuel for sale shall sell, advertise or offer for sale said fuel separately from the tax imposed by this chapter. For any violation of this section, the permit to keep and sell crude petroleum or any of its products, issued by the State fire marshal or his agent, shall be suspended by the said marshal on request of the commissioner for such time as said commissioner deems proper.

Section 23(c) of the Revenue Act of 1928 provides that in computing net income there shall be allowed as deductions taxes paid or accrued within the taxable year, with certain exceptions not here material. Article 151 of Regulations 74, promulgated under the Revenue Act of 1928, provides that in general taxes are deductible only by the person upon whom they are imposed.

From the foregoing quoted sections of the Massachusetts law, it is evident that the tax therein provided is imposed upon the consumer. It is held, therefore, in accordance with the provisions of section 23(c) of the Revenue Act of 1928 and article 151 of Regulations 74, that the gasoline tax imposed by the State of Massachusetts is deductible in the income tax return of the consumer who pays it and to whom it is not refunded. If, however, the tax is added to or made a part of the business expense of such consumer, it can not be deducted by him separately as a tax.

ARTICLE 151: Taxes.
(Also Section 41, Article 322.)

VIII-50-4463
G. C. M. 7190

REVENUE ACT OF 1928.

In the State of Indiana, the liability for real and personal property taxes is incurred on March 1 of each year, and accordingly such taxes accrue on that date for income tax purposes.

An opinion has been requested as to the proper accrual date of property taxes under the laws of the State of Indiana.

Under the provisions of section 14034, chapter 102 of the Indiana Statutes (Burns Annotated Indiana Statutes, 1926), all property within the jurisdiction of the State, not expressly exempted, is subject to taxation. It is further provided in that section that all property of every kind and nature, both real and personal, and wherever situated, owned or possessed, and subject to taxation within the State of Indiana, shall be assessed and valued for taxation purposes, at the true cash value thereof, on the 1st day of March in each year in which it is subject to assessment and valuation for taxing purposes.

Section 14047 provides that personal property shall be listed for taxation between the 1st day of March and the 15th day of May, each year, with reference to the quantity and quality held or owned on the 1st day of March in the year for which the property is required to be listed.

Section 14048 provides that the person purchasing or acquiring property, whether real or personal, on the 1st day of March in any year shall be considered as the owner on that day, and shall be assessed and liable for the taxes of that year.

Section 14288 provides that all the property, both real and personal, situated in any county, shall be liable for the payment of all taxes, penalties, interest, and costs charged to the owner thereof in such county, and no partial payment of such taxes, penalties, interest, or costs shall discharge or release any part or portion of such property until the whole is paid; which lien shall in nowise be affected or destroyed by any sale or transfer of any such personal property, and shall attach on the 1st day of March, annually, for the taxes of such year.

Section 14383 provides that the lien of the State for all taxes for State, county, school, road, township, and all other purposes, and all taxes for city, town, or municipal purposes, shall attach on all real estate on the 1st day of March, annually.

In the case of *Prudential Casualty Co. v. State et al.* (194 Ind., 542, 143 N. E., 631), the Supreme Court of Indiana held that it should be regarded as settled in that State that general taxes constitute a personal liability against the owner of the property upon which the assessment is based. With respect to the date as of which the liability for property taxes accrues, the Appellate Court of Indiana in *Barnum v. Rallihan* (63 Ind. App., 349, 112 N. E., 561) stated as follows:

By the statute the taxes for each year attach and become a lien upon both real and personal property on the 1st day of March annually, though the same are not due and payable until the following year, and will not become delinquent until after the first Monday in May. While not expressly so stated, our decisions seem to treat all taxes as accruing on the 1st day of March when the lien thereof attaches to the property assessed.

The United States Supreme Court in *United States v. Anderson* (269 U. S., 422, T. D. 3839, C. B. V-1, 179), in consideration of the question as to when taxes accrue for income tax purposes, used the following language:

In a technical legal sense it may be argued that a tax does not accrue until it has been assessed and becomes due; but it is also true that in advance of the assessment of a tax all the events may occur which fix the amount of the tax and determine the liability of the taxpayer to pay it.

In view of the express statutory provisions referred to above and the interpretation placed thereon by the State courts, this office is of the opinion that under the law of Indiana ownership of property on March 1 of each year is the "event" which, in accordance with *United States v. Anderson*, supra, determines the liability for property taxes and fixes the amounts thereof. Personal property and real property taxes in Indiana may accordingly be accrued as of March 1 of each year, for income tax purposes, by taxpayers whose books of account are kept on the accrual basis. (See also *H. H. Brown Co. v. Commissioner*, 8 B. T. A., 112, C. B. VII-1, 5, with

respect to the accrual date of property taxes in Massachusetts, and G. C. M. 6273, C. B. VIII-1, 168, with respect to the accrual date of property taxes in Illinois.)

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

SECTION 23(i).—DEDUCTIONS FROM GROSS INCOME: NET LOSSES.

ARTICLE 171: Losses.

VIII-27-4260

G. C. M. 6122

REVENUE ACT OF 1928.

Where a building on which there was no storm insurance was extensively damaged by a hurricane, but not entirely destroyed, and was later restored to its former condition, the deductible loss is the same percentage of the depreciated cost or March 1, 1913, value, as the case may be, which the destroyed portion is of the entire property. Such loss is deductible in its entirety in the year of the storm, even though the amount expended in that year toward restoring it to its former condition was a small amount as compared to the amount expended in the succeeding year for that purpose.

An opinion is requested as to the deduction allowable for income tax purposes under the following statement of facts:

It appears that the taxpayer has a part interest in a business building which was extensively damaged by a hurricane in September, 1928. Some repairs were made in 1928, but the making of other repairs during the year 1929 is contemplated.

It is contended that, since the building was only damaged or partially destroyed, the amount deductible should be the cost of the repairs which are required to restore the building to its condition prior to the storm.

Reference is made to the case of *Tampa Electric Co. v. Commissioner* (12 B. T. A., 1002, C. B. VII-2, 39). That case involved an item of \$13,904.96. The Board stated, page 1008:

* * * The work classified as repairs consisted of rewinding armatures damaged by salt water; dredging a fill washed into the bay; and repairs of a miscellaneous character to a steam plant, lighting lines, machinery, a building, and passenger cars. We are convinced from a careful consideration of all the evidence that the work performed may be properly characterized as repairs and as such constitute an allowable deduction in 1922. (See *Illinois Merchants Trust Co., Executor*, 4 B. T. A., 103, and *Yakima Hop Co.*, 8 B. T. A., 441.)

Evidently the Board uses the word "repairs" in a technical and restricted sense, as covering minor expenditures only. This view of the meaning of the word is also indicated by the case of *Joseph E. Hubinger v. Commissioner* (13 B. T. A., 960). In that case the taxpayer claimed a deduction on account of expenditures for repairing extensive damage to a building by fire. The deduction was disallowed. The Board said, page 964:

* * * The difficulties that lie in the way of adopting any general rule and attempting to fit all cases to it are obvious. An item, in relation to income, may in one case be so insignificant that it would be absurd to require its capitalization even though under a technical definition it might be an improvement, while in another case the cost of a similar item might be sufficient to absorb all the income for the year. *We can not believe that Congress intended to allow as charges against the revenues of a day or year the cost of restoring*

major parts of income-producing property where the restoration is of such character as to be useful over a long period of years.

The distinction between maintaining property through repairs necessitated as the result of a casualty, such as in Illinois Merchants Trust Co. (4 B. T. A., 103), and the restoration of a major part of the property itself, is readily apparent. [Italics supplied.]

In the case of *Ben Baer v. Commissioner* (12 B. T. A., 1060) the question involved was the deductibility of an amount spent for restoring a building which had been 50 per cent destroyed by fire the previous year. It was held that the loss suffered was deductible for the year in which the fire occurred, and that the amount spent for restoration over and above the insurance recovered was a capital expenditure and not a deductible expense item.

The import of the Board's decisions is that the decisive factor is not the length of time required to do the work but the relative importance thereof. In the instant case it appears that, while the building was not totally destroyed by the hurricane, the damage was quite extensive. In such situation the proper treatment is by a deduction for loss for 1928 and not by deductions for repairs for 1928 and 1929.

It is contended that the amount of the loss is the difference between the depreciated cost or March 1, 1913, value of the building, as the case may be, and the salvage value of the property after the storm. This is the proper rule only when damaged property is to be discarded or junked. Otherwise, the rule is that the deductible loss is the same percentage of the depreciated cost or March 1, 1913, value, as the case may be, which the destroyed portion is of the entire property. If any portion of the building is continued in use, though damaged, a proportionate deduction may be taken. (A. R. R. 4725, C. B. III-1, 143.)

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

ARTICLE 172: Voluntary removal of buildings.

VIII-41-4382
I. T. 2501

REVENUE ACT OF 1928.

The taxpayer purchased a lot and building known as the R Building and an adjoining lot and building known as the S Building. It was the purpose and intention of the taxpayer to raze the buildings on the two lots and erect a new business building. However, due to a long-term lease on the S Building, which the lessee would not sell or otherwise terminate, the taxpayer's plans had to be abandoned. The properties were thereupon set up on the taxpayer's books as rental properties and were thus carried for a period of three years. In 1929, however, the taxpayer, having made new plans, demolished the R Building and erected an office building.

Held, that no deductible loss was sustained by the taxpayer by reason of the demolition of the R Building.

A ruling is requested as to whether the M Company is entitled to a loss for 1929 by reason of the demolition of a building.

It appears that on January —, 1926, the M Company purchased a lot and building known as the R Building, and on January —, 1926, it purchased an adjoining lot and building known as the S Building. It was the purpose and intention of the M Company to raze the build-

ings on these two lots and to erect a new business building. It developed, however, that due to a long-term lease on the S Building, which the lessee would not sell or otherwise terminate, the taxpayer's plans had to be abandoned. The properties were thereupon set up on the taxpayer's books as rental properties and were thus carried for a period of three years. In 1929, however, the taxpayer, having made new plans, demolished the R Building and erected an office building.

The taxpayer contends that it is entitled to claim as a loss the cost of the R Building, less depreciation for the three years it was held as rental property. The taxpayer as a basis for its contention cites Solicitor's Recommendation 17 (C. B. III-2, 112) and the three decisions of the Board of Tax Appeals referred to below.

Article 172 of Regulations 74 and the corresponding article of prior regulations read as follows:

ART. 172. Voluntary removal of buildings.—Loss due to the voluntary removal or demolition of old buildings, the scrapping of old machinery, equipment, etc., incident to renewals and replacements will be deductible from gross income. When a taxpayer buys real estate upon which is located a building, which he proceeds to raze with a view to erecting thereon another building, it will be considered that the taxpayer has sustained no deductible loss by reason of the demolition of the old building, and no deductible expense on account of the cost of such removal, the value of the real estate, exclusive of old improvements, being presumably equal to the purchase price of the land and building plus the cost of removing the useless building.

In Solicitor's Recommendation 17 the taxpayer in 1916 and 1917 purchased near its place of business two lots with frame buildings thereon. The buildings were leased from date of purchase until 1919, when they were razed in order that the taxpayer might erect a brick building to be used in connection with its business. The taxpayer was permitted to claim as a loss the difference between the original cost of the property and the depreciation thereon, less salvage value. That case is distinguished from the instant one in that it was not the taxpayer's purpose and intention at the time of the purchase of the property to raze the buildings thereon.

The facts in the other three cases cited by the taxpayer are, briefly, as follows:

In the case of the First National Bank of Evanston, Wyo. (1 B. T. A., 9, C. B. IV-1, 2), the taxpayer made alterations to its building whereby a wall was torn out, floors discarded, window openings dropped, new windows installed, doors discarded, ceiling and roof changed, and the old entrance taken out.

In the case of the First National Bank of Goodland, Kans. (5 B. T. A., 1174, C. B. VI-2, 2), the taxpayer in 1901 purchased a bank building, which it used constantly as its place of business until some time in 1921. In the latter year the taxpayer remodeled and reconstructed the building, as a result of which the roof was taken off and practically all of three walls were torn down. Only an inside or party wall was left standing. The building was changed from a two-story to a one-story structure.

In the case of the Steinbach Co. (3 B. T. A., 348, C. B. VI-1, 6), due to the expansion of the taxpayer's business, the building which it occupied was enlarged from time to time. At the beginning of 1921 only a portion of such building was five stories in height. More floor space having become necessary, the taxpayer voluntarily demol-

ished the entire fractional fifth floor for the purpose of bringing the entire building to a height of five stories.

In all three of the above-mentioned cases the taxpayers were allowed a deductible loss on the unextinguished cost of the parts of the buildings demolished. All three cases fall within the provisions of article 172 of Regulations 74 and the corresponding article of prior regulations, wherein it is held that loss due to the voluntary removal or demolition of old buildings, the scrapping of old machinery, equipment, etc., incident to renewals and replacements will be deductible from gross income. The instant case is not analogous to any of the above-mentioned cases, since in none of those cases were the properties purchased with the purpose and intention of razing the buildings thereon or any portions thereof.

Inasmuch as it was the purpose and intention of the taxpayer in the instant case to raze the building in question at the time the property was purchased, it is held that the case comes squarely within the provisions of the last part of article 172 of Regulations 74. No deductible loss was, therefore, sustained by the taxpayer by reason of the demolition of the building, it being presumed that the value of the real estate, exclusive of the building, was equal to the purchase price of both the land and building plus the cost of the removal of the old building. It is immaterial that the taxpayer had to make some change in its original plans regarding the demolition of the building. (See *Liberty Baking Co. v. D. B. Heiner*, United States District Court, Western District of Pennsylvania.)

SECTION 23(1).—DEDUCTIONS FROM GROSS INCOME: DEPLETION.

ARTICLE 251: Charges to capital and to expenses in the case of timber.

VIII-30-4283
G. C. M. 6544

REVENUE ACT OF 1928.

The fact that the election permitted by article 251, Regulations 74, extends only to "expenditures for administration, protection, and other carrying charges" implies that as to expenditures not included in that category, for example, the cost of planting trees, there is no such right of election, and that such costs are to be treated, in accordance with their inherent nature, as capital expenditures.

An opinion is requested as to the proper treatment for income tax purposes of expenditures made by the M Company representing the cost of planting trees in connection with an extensive reforestation program upon which the company has recently entered. The taxpayer states that the "reforesting of this land will be of no benefit to the present generation, as it will take from 40 to 50 years before the timber is cut."

Article 251 of Regulations 74, entitled "Charges to capital and to expenses in the case of timber," provides:

In the case of a timber property held for future operation by an owner having no substantial income from the property or from other sources, all expenditures for administration, protection, and other carrying charges prior to production

on a normal basis shall be charged to capital account; after such a property is on a normal production basis such expenditures shall be treated as current operating expenses. In case a taxpayer, who has a substantial income from other sources, owns a timber property which is not yet on a normal production basis he may charge such expenditures with respect to such timber property to capital or treat them as current operating expenses, but whichever system is adopted must be followed until permission to change to the other system is secured from the Commissioner. In the case of timber operations all expenditures for plants, improvements, and equipment shall be charged to capital account for purposes of depreciation.

The fact that the election permitted by article 251 extends only to "expenditures for administration, protection, and other carrying charges" implies that as to expenditures not included in that category, for example, the cost of planting trees, there is no such right of election, and that such costs are to be treated, in accordance with their inherent nature, as capital expenditures.

A case in point is the appeal of J. H. Sanford (2 B. T. A., 181), in which the Board said:

The taxpayer has included in his deductions items which are capital expenditures, as, for example, amounts expended in removing trees and brush from land which was not seeded to a marketable crop in the same year in which it was cleared. Such expenditures are comparable to the *expenditures incident to the planting of an orchard which will not come into bearing for six years. These expenses are preparatory for the actual operations for profit and are not at all the same as the current annual operating expenses.* [Italics supplied.]

In the opinion of this office the expenditures made by the M Company representing the cost of planting trees in connection with its reforestation program should be capitalized and can not be deducted as current operating expenses.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

SECTION 23(m).—DEDUCTIONS FROM GROSS INCOME: BASIS FOR DEPRECIATION AND DEPLETION.

ARTICLE 222: Amount returnable through depletion and depreciation deductions in the case of an operating owner.

VIII-35-4325
G. C. M. 6746

REVENUE ACT OF 1928 AND PRIOR REVENUE ACTS.

The decision of the Supreme Court in *United States v. Ludey* (274 U. S., 295, T. D. 4046, C. B. VI-2, 157) does not apply to the basis for depletion and depreciation as well as for the computation of gain or loss on sale of property.

In computing depletion and depreciation, the basis is the cost (or other basis) minus the depletion and depreciation sustained, whether legally allowable or not.

An opinion is requested upon the following question:

Shall the opinion of the Supreme Court (in the case of *United States v. Ludey*) be construed to apply to the basis for depletion and depreciation as well as for the computation of profit or loss on the sale of property?

In the computation of profit or loss on a sale, the Supreme Court held that the cost or March 1, 1913, value should be reduced by the

amount of depletion or depreciation allowable instead of by the amount of depletion or depreciation sustained or claimed.

In the computation of depletion and depreciation, however, the basis is the cost (or other basis) minus the depletion and depreciation sustained, whether legally allowable or not. (Articles 202, 203, and 204 of Regulations 45, 62, 65, 69, and articles 222, 223, and 224 of Regulations 74.) (See *Thompson Oil & Gas Co. v. Commissioner*, 15 B. T. A., 993, distinguishing *United States v. Ludey*, supra.)

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

PART IV.—ACCOUNTING PERIODS AND METHODS OF ACCOUNTING.

SECTION 41.—GENERAL RULE.

ARTICLE 322: Bases of computation.

REVENUE ACT OF 1928.

Accrual of property taxes in the State of Washington. (See G. C. M. 6667, page 94.)

ARTICLE 322: Bases of computation.

REVENUE ACT OF 1928.

Accrual of Kansas property taxes. (See I. T. 2495, page 98.)

ARTICLE 322: Bases of computation.

REVENUE ACT OF 1928.

Accrual of real and personal property taxes in Indiana. (See G. C. M. 7190, page 113.)

SECTION 44.—INSTALLMENT BASIS.

ARTICLE 352: Sale of real property involving deferred payments.

VIII-36-4335
I. T. 2492

REVENUE ACT OF 1928.

The "taxable period" in which the initial payments as defined in section 44(b) of the Revenue Act of 1928 may be received means the "taxable year" defined by section 48(a) of that Act.

The M Company was organized in 1925 for the purpose of purchasing, developing, and subdividing real estate, and a fiscal-year accounting period ending May 31 was used. The subdivision lots were first placed on sale in August and September, 1927. The ma-

majority of the lots were sold at that time for $6x$ dollars each, of which amount x dollars was payable in cash at the date of sale, the balance of the purchase price being represented by four notes of $1.25x$ dollars each, maturing in 6, 12, 18, and 24 months, respectively, from the date of sale.

The question presented is whether the income from the sale of the lot as outlined above should be computed under the Revenue Act of 1926 or 1928, or, in other words, is the transaction an installment sale or a completed sale.

Section 44(b) of the Revenue Act of 1928 defines initial payments as follows:

* * * As used in this section the term "initial payments" means the payments received in cash or property other than evidences of indebtedness of the purchaser during the taxable period in which the sale or other disposition is made.

Section 48(a) of the Revenue Act of 1928 defines taxable year in the following language:

"Taxable year" means the calendar year, or the fiscal year ending during such calendar year, upon the basis of which the net income is computed under this part. * * * The first taxable year, to be called the taxable year 1928, shall be the calendar year 1928 or any fiscal year ending during the calendar year 1928.

Article 352 of Regulations 74 states, in part:

Sale of real property involving deferred payments.—Under section 44 deferred-payment sales of real property fall into two classes when considered with respect to the terms of sale, as follows:

(1) Sales of property on the installment plan, that is, sales in which the payments received in cash or property other than evidences of indebtedness of the purchaser during the taxable year in which the sale is made do not exceed 40 per cent of the selling price.

The above-quoted article makes it clear that the "taxable period" in which the initial payments as defined in section 44(b) of the Revenue Act of 1928 may be received means the "taxable year" defined by section 48(a) of that Act. It is held, therefore, that the installment provisions of the Revenue Act of 1928 apply in reporting income from all sales of real estate made by the taxpayer during its fiscal year ended May 31, 1928. (*Cf. Kentucky Jockey Club v. Lucas*, 14 Fed. (2d), 539, T. D. 3915, C. B. V-2, 191.)

ARTICLE 352: Sale of real property involving deferred payments.

VIII-51-4469
I. T. 2513

REVENUE ACTS OF 1926 AND 1928.

Where a sale of real estate is made in a taxable period beginning in 1927 and ending in 1928, and the initial payments thereon aggregate more than 25 per cent but not more than 40 per cent of the selling price, installment classification of such sale may be made only in determining the tax attributable to that part of the taxpayer's fiscal year falling in 1928, in applying the provisions of section 105 of the Revenue Act of 1928.

I. T. 2492 (see on page 120) modified.

In I. T. 2492 it is held that the installment provisions of the Revenue Act of 1928 are applicable in reporting income from sales

of real estate made by the taxpayer, the M Company, during its fiscal year ended May 31, 1928. The facts in that case are stated as follows:

The M Company was organized in 1925 for the purpose of purchasing, developing, and subdividing real estate, and a fiscal-year accounting period ending May 31 was used. The subdivision lots were first placed on sale in August and September, 1927. The majority of the lots were sold at that time for 6 $\times$ dollars each, of which amount $\times$ dollars was payable in cash at the date of sale, the balance of the purchase price being represented by four notes of 1.25 $\times$ dollars each, maturing in 6, 12, 18, and 24 months, respectively, from the date of sale.

The ruling in I. T. 2492 should not be taken as contemplating a computation of tax other than in accordance with the provisions of section 105 of the Revenue Act of 1928 and article 551 of Regulations 74.

Article 551, Regulations 74, provides that the tax for a period beginning in 1927 and ending in 1928 is the sum of the following: (a) The tax attributable to the calendar year 1927, found by computing the tax upon the income of the taxpayer for the fiscal year under the provisions of the Revenue Act of 1926, and by taking the proportion of such tax which the portion of the period falling within the calendar year 1927 is of the entire period, and (b) the tax attributable to the calendar year 1928, found by computing the tax upon the income of the taxpayer for the fiscal year under the provisions of the Revenue Act of 1928, and by taking the proportion of such tax which the portion of the period falling within the calendar year 1928 is of the entire period.

In accordance with the provisions of section 105 of the Revenue Act of 1928 and article 551 of Regulations 74, it is necessary to treat the sales of real estate under consideration as closed transactions in ascertaining net income under the provisions of the Revenue Act of 1926 for the purpose of computing the tax attributable to that part of the taxpayer's fiscal year falling in the calendar year 1927. This is true because of the fact that the initial payments received on the sales exceeded 25 per cent of the selling price of the respective lots. In ascertaining net income under the provisions of the Revenue Act of 1928 for the purpose of computing the tax attributable to that part of the taxpayer's fiscal year falling within the calendar year 1928, the sales may, if the taxpayer so desires, be treated as installment transactions, since the initial payments received on the sales did not exceed 40 per cent of the selling price of the respective lots sold. (*Appeal of Arthur P. Pearce et al. v. Commissioner*, 13 B. T. A., 150, C. B. VII-2, 31.) In case the taxpayer treats the sales as installment transactions in computing the tax attributable to the calendar year 1928, no payments received thereon in subsequent taxable years shall be excluded in computing the amount of income to be returned on the ground that they were received under a sale from which the total profit was returned as income in computing the tax attributable to the calendar year 1927.

I. T. 2492 is modified to conform to the position herein taken.

SECTION 53.—TIME AND PLACE FOR FILING RETURNS.

ARTICLE 402: Extensions of time for filing
returns.

VIII-42-4388
Mim. 3759

Instructions to collectors relative to extensions of time for filing
income tax returns.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, D. C., October 9, 1929.

*Collectors of Internal Revenue, Internal Revenue Agents in Charge,
and Others Concerned:*

Reference is made to Mimeograph 3361, dated November 20, 1925 [C. B. IV-2, 69], under which collectors were given authority to grant extensions of time for filing income tax returns. Such extensions were to be allowed in accordance with the rules set forth therein, upon the condition, however, that an explanation satisfactory to the collector would be given. The mimeograph was given due publicity in order to acquaint taxpayers with the privilege thus afforded for securing extensions of time and they in turn have generally availed themselves of this privilege.

It has come to the attention of this office that in numerous instances taxpayers, evidently relying upon the privilege of securing an extension of time, have failed to make every reasonable effort to file returns on or before the regular due date. For example, in many cases taxpayers or attorneys on their behalf have habitually requested extensions of time for filing returns year after year, so that in these cases the filing of delayed returns has been the rule rather than the exception. It is believed in these as well as in many other cases the delay in filing the returns was occasioned primarily by an undue exercise of the privilege afforded taxpayers to secure extensions of time rather than by meritorious causes. In short, the privilege so given to taxpayers has been subjected to abuse.

Inasmuch as it is essential to the proper administration of the internal revenue laws that returns be filed on or before the regular due date whenever possible, and inasmuch as extensions of time were intended to be granted only in those cases in which by reason of the circumstances involved the taxpayers could not have filed a timely return through the exercise of ordinary diligence, collectors are hereby instructed to grant extensions of time only upon the showing of a good and sufficient cause for the delay in filing the return. It is deemed inadvisable to define what will constitute a good and sufficient cause for this purpose other than as indicated in Mimeograph 3361, and the determination, therefore, of whether an extension of time should be granted in a particular case is left to the discretion of the collector.

Collectors are cautioned that the purpose of this mimeograph is to prevent the allowance of unnecessary extensions of time in those cases in which, as already stated, the need therefor reasonably could have been avoided, but it is not intended that in this matter the Bureau should go to one extreme or the other. In other words, in

the administration of the authority conferred upon them to grant extensions of time collectors should endeavor to prevent as much as possible the abuse by taxpayers of the privilege and at the same time continue to grant extensions of time in every case in which the circumstances warrant such action.

Queries regarding this mimeograph will refer to the number of the mimeograph and the symbols IT: E: RR.

This mimeograph should be given proper publicity in order that taxpayers may be duly informed as to the policy thereby established.

ROBT. H. LUCAS, *Commissioner.*

ARTICLE 402: Extensions of time for filing
returns.

VIII-51-4470
Min. 3706

Computation of interest where returns filed and taxes paid prior
to expiration of period of extension for filing return.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, D. C., February 15, 1929.

*Collectors of Internal Revenue, Internal Revenue Agents in Charge,
and Other Officers and Employees Concerned:*

Reference is made to I. T. 2173 (C. B. IV-1, 68) and to paragraph 10 of Mimeograph 3361, dated November 20, 1925 [C. B. IV-2, 69], which provide that where an extension of time within which to file a return is granted, interest at the rate of 6 per cent per annum is collectible on the difference between the amount paid and the amount due, for the full period of the extension of time granted, even though the return is filed and the tax paid prior to the expiration of the extension period.

For the purpose of the computation of interest in cases of this character, extensions of time to file returns will hereafter be deemed to have been granted for such period as may have been necessary, not exceeding the number of days mentioned in the grant, and interest on the difference between the amount due and the amount already paid will be computed from the original due date to the date of payment thereof, instead of to the final date upon which the return could have been filed under the extension granted.

Queries regarding this mimeograph or procedure in connection therewith should refer to the number of the mimeograph and the symbols IT: E: RR.

H. F. MIREs,
Acting Commissioner.

PART V.—RETURNS AND PAYMENT OF TAX.

SECTION 55.—PUBLICITY OF RETURNS.

ARTICLE 421: Inspection of returns.

VIII-39-4366

T. D. 4271

Income tax—Inspection of returns—Article 421 of Regulations 74 amended.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, D. C.

To Collectors of Internal Revenue and Others Concerned:

Article 421 of Regulations 74 is hereby amended by adding at the end thereof the following:

Under date of March 14, 1929, the foregoing regulations were amended with the approval of the President by the addition thereto of the following paragraph:

"20. The Commissioner of Internal Revenue shall cause to be prepared a written decision in every case in which an overassessment (whether resulting in a refund, credit, or abatement) of an income, war-profits, excess-profits, estate, or gift tax is allowed, in excess of \$20,000, and such decision shall be considered a public record and shall be open to inspection, during regular hours of business, in the office of the Commissioner of Internal Revenue or such office as he may designate. Such decision shall give the amount of the overassessment and shall be accompanied by a brief summary of the relevant facts and a citation of the authorities applicable thereto, or, in a case in which a decision of a court or of the Board of Tax Appeals has become final, by a citation of the court or Board decision. Under no circumstances shall the provisions of this paragraph be construed as making any return, or any part thereof, open to inspection, or as authorizing the source of any income, gains, or profits, or the specific transactions resulting in losses or expenditures, to be made public; nor shall any of the information contained in any return or relating thereto be made public except in accordance with, and to the extent necessary in carrying out, these regulations."

ROBT. H. LUCAS,
Commissioner of Internal Revenue.

Approved September 20, 1929.

OGDEN L. MILLS,
Acting Secretary of the Treasury.

SECTION 56.—PAYMENT OF TAX.

ARTICLE 432: Extension of time for payment
of the tax or installment thereof.

VIII-51-4471

G. C. M. 6801

REVENUE ACTS OF 1926 AND 1928.

A parent corporation may enter into a contract of suretyship to guarantee the tax liability of its subsidiary.

An opinion is requested relative to the rights of the United States under a bond given by the M Company, as principal, and the O Company, as surety, covering an assessment of taxes for the year 1926.

The M Company is a voluntary association, the shares of which are owned by the O Company. Its profits are principally of a non-recurrent character, and under its constitution may be distributed only to the O Company. On June —, 1927, the M Company filed a separate return, showing an income tax liability of 55*x* dollars. Of this amount, 26*x* dollars has been paid, leaving a balance due of 29*x* dollars. An extension of time was given to pay the balance of 29*x* dollars in installments of 14½*x* dollars on March 15, 1928, and June 15, 1928. As a condition of the extension of time a bond, running to the United States and conditioned upon the payment of the amount of 29*x* dollars, was given. Inquiry is made as to whether the Government is protected by the bond; and if so, for what period of time.

The issues involved are (1) the authority of the surety to act as such; and (2) the limitation period on collection under the bond, if any.

The bond is binding upon the principal as well as the surety. Therefore, if the debt is readily collectible from the principal, no recourse to the surety need be had. If recourse to the surety should become necessary, it seems clear that the bond is legally binding on that corporation. The surety is a stock corporation organized under the laws of the State of New York, and is subject to the provisions of the stock corporation law of that State, section 18 of which authorizes the holding by one corporation of the stock of another. Section 19 of the same statute provides that a corporation having the stock of another may guarantee its bonds. No express authorization to act as surety for a voluntary association has been noted, but it seems certain that, under the circumstances of the instant case, such authority exists by virtue of general law. See *Corpus Juris*, volume 14A, page 742, wherein it is stated:

* * * a corporation may enter into a contract of guaranty or suretyship when reasonably incidental to the conduct of its authorized business, * * *. On similar grounds it has been held that a corporation may guarantee the principal and interest of indebtedness incurred by its subsidiaries. And so a corporation has implied power to guarantee bonds issued by a subsidiary company, * * *. And, where a corporation organized another corporation to acquire the business of a competitor and the stock of the nominal purchasing corporation is owned by stockholders of the principal company, the principal company may guarantee the obligations of the nominal purchasing company.

It is now well settled that the limitation periods prescribed for collection of taxes as such are not applicable to suits for recovery under bonds. (*United States v. Barth*, 279 U. S., 370, 49 Sup. Ct., 366, Ct. D. 65, C. B. VIII-1, 189.) The bond given in this case runs expressly to the United States. The general rule is that the United States is not bound by any statute of limitations unless expressly named therein. (*Dollar Savings Bank v. United States*, 19 Wall., 227, 239; *United States v. Railway*, 118 U. S., 120, 125; *Stanley v. Schwalley*, 147 U. S., 508, 515; *United States v. American Bell Telephone Co.*, 159 U. S., 548, 554.) Since there is no statutory limitation provision naming the United States which would apply to the bond in the instant case, it follows that the bond is effective for an unlimited time.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

SUBTITLE C.—SUPPLEMENTAL PROVISIONS.

SUPPLEMENT A.—RATES OF TAX.

SECTION 101.—CAPITAL NET GAINS AND LOSSES.

ARTICLE 501: Definition and illustration of
capital net gain.

VIII-34-4316

I. T. 2488

REVENUE ACTS OF 1921, 1924, 1926, AND 1928.

The net gain from bonds held for more than two years, whether received as the result of the maturity of the bonds or as the result of their redemption before maturity, may, at the option of a taxpayer other than a corporation, be taxed as a capital net gain under the provisions of section 206 of the Revenue Act of 1921. I. T. 1637 (C. B. II-1, 36) revoked.

Likewise, any individual who has held stock in a corporation for more than two years and who derives a gain when the stock is "called in" may elect to have such gain taxed as a capital net gain in the manner and subject to the conditions prescribed in section 206 of the Revenue Act of 1921.

The foregoing ruling is also applicable under the Revenue Acts of 1924, 1926, and 1928.

A ruling is requested as to the manner in which the gain from bonds or stock held for more than two years should be treated where the bonds are redeemed before their maturity date or the stock is "called in."

Under the provisions of section 206 of the Revenue Act of 1921, any taxpayer (other than a corporation) who for any taxable year derives a capital net gain may elect to be taxed on such capital net gain at the rate of 12½ per cent in lieu of the tax he would otherwise pay on such income under sections 210 and 211. Section 206 of the Revenue Act of 1921 reads in part as follows:

(a) That for the purpose of this title:

(1) The term "capital gain" means taxable gain from the sale or exchange of capital assets consummated after December 31, 1921.

In I. T. 1637 it was held that when an obligation matures it is neither sold nor exchanged. It was further held that any taxable profit derived upon maturity of an obligation is therefore not "capital gain" derived from the sale or exchange of capital assets and section 206 does not apply.

Under date of February 19, 1929, the United States Board of Tax Appeals decided, in the case of Henry P. Werner (15 B. T. A., 482, see on page 56), that the redemption of bonds at a "called" date for an amount in excess of the cost of the bonds to the bondholder results in a gain from the sale or exchange of capital assets within the meaning of section 206 of the Revenue Act of 1921. In the decision the legislative history of section 206 of the Revenue Act of 1921 was reviewed. It was stated that the Ways and Means Committee of the House and the Finance Committee of the Senate declared that the provision was intended to be applicable to the "sale or other disposition of capital assets."

The ruling contained in I. T. 1637 is hereby revoked. The net gain from bonds held for more than two years, whether received as

the result of the maturity of the bonds or as the result of their redemption before maturity, may, at the option of a taxpayer other than a corporation, be taxed under the provisions of section 206 of the Revenue Act of 1921.

Likewise, any individual who has held stock in a corporation for more than two years and who derived a gain when the stock is "called in" may elect to have such gain taxed as a capital net gain in the manner and subject to the conditions prescribed in section 206 of the Revenue Act of 1921.

As the provisions of the Revenue Acts of 1924, 1926, and 1928 relating to capital net gains are similar to the provisions of section 206(a)1 of the Revenue Act of 1921, the foregoing ruling is also applicable under those Acts.

ARTICLE 501: Definition and illustration of
capital net gain.

VIII-42-4389
I. T. 2502

REVENUE ACT OF 1928.

The gain resulting from the sale of shares of stock held for more than two years by a dealer in securities may be treated as capital net gain subject to tax under section 101 of the Revenue Act of 1928, provided the stock was held by such dealer primarily for investment and was not a part of the securities traded in.

Inquiry is made as to whether the gain resulting to the taxpayer, A, from the sale of 10 shares of stock of the M Company may be treated as capital net gain subject to tax under section 101 of the Revenue Act of 1928.

The 10 shares of stock were acquired by the taxpayer for a consideration of x dollars upon the formation of the corporation in 1925, and were sold in 1928 at the price of $2x$ dollars. The taxpayer is a "dealer in securities," and the benefits of section 101 of the Revenue Act of 1928 are not available to him with respect to gains realized from the sale of securities regularly traded in. Although it is stated in article 501 of Regulations 74 that "a dealer in securities is not entitled to the benefits of section 101" of the Revenue Act of 1928 with reference to gain from the sale of securities, it seems clear that the securities there referred to are such securities as are regularly traded in and may properly be included in the inventory of the taxpayer under article 105 of Regulations 74.

In I. T. 2297 (C. B. V-2, 109) it was held *inter alia* that if a dealer in real estate could establish that any of the real property sold by him was held primarily for investment, the provisions of section 206(b) of the Revenue Act of 1921 and section 208(b) of the Revenue Act of 1924 would apply to the taxation of the profits realized from the sale thereof. The principle applied in that ruling in the case of a dealer in real estate appears to be equally applicable in the instant case.

It is held, therefore, that the gain resulting from the sale of shares of stock held for more than two years by a dealer in securities may be treated as capital net gain subject to tax under section 101 of the Revenue Act of 1928, provided the stock was held by such dealer primarily for investment and was not a part of the securities traded in. A's case should be disposed of accordingly.

ARTICLE 501: Definition and illustration of
capital net gain.
(Also Section 162, Article 862.)

VIII-45-4421
I. T. 2506

REVENUE ACT OF 1928.

Where a widow accepts the provisions of her husband's will and is paid annually the income from a residuary trust in lieu of her statutory share of the corpus of the estate, amounts paid by the trust after the value of her statutory interest in the estate as of the date of the testator's death has been fully received are not considered capital gain but are treated as ordinary income distributions under the terms of the will or trust.

Payments made by the trust prior to the time the value of taxpayer's statutory interest has been recovered may not be deducted in computing the net income of the trust.

Advice is requested as to how A, the taxpayer, should report for income tax purposes the income received by her from a trust created under the will of B, her deceased husband.

The will in question was executed February —, 191—, and the testator, B, died —, 1919. The provisions of the will, pertinent to the questions here involved, read as follows:

* * * * *
Second: All the residue of my estate, both real and personal and wherever situated, I give, devise and bequeath to the trustees hereinafter named, but in trust nevertheless for the following purposes:

To hold, manage and at their discretion to sell the same or any part thereof, and to invest and reinvest the proceeds and to pay the net income to my wife, A, in case she survives me, until her death, unless she should remarry, in which case in view of the fact that she has property of her own I direct that the payment of income to her shall cease.

* * * * *
Thirteenth: I direct that all legacy and inheritance taxes shall be paid out of the residue of my estate.

Fourteenth: I appoint C, my wife, A, and D to be executors of and trustees under this will.

* * * * *
Eighteenth: The provisions herein contained for the benefit of my wife are in lieu of dower and all other claims of hers to my estate, real and personal.

* * * * *
The value of the testator's estate as of the date of his death has been determined to be 5x dollars. The interest of A in the estate under the laws of the State of R, in the event she had elected to take under the statute and not under the will, would have been \$— in cash and the income for life on 2x dollars. The value of such statutory interest as of the date of the death of the testator has been determined to be x dollars.

The amount which the taxpayer received from the trust prior to January 1, 1928, was in excess of the value of her statutory interest in the estate at the date of the death of the testator. A portion of the income of the trust is derived from dividends of corporations, interest on State obligations, and interest on nontax-exempt bonds. The question presented is whether the taxpayer should report the income received from the trust for the years 1928 and 1929 according to the actual sources of such income, or whether she should report such income as a gain over and above the value of her dower interest, and, if the latter, whether she should report the amount received as capi-

tal net gain taxable at 12½ per cent. Request is also made as to how the trustees should report the income of the trust.

While payments to the taxpayer by the trust are considered a return of capital until such time as the value of her statutory interest in her husband's estate as of the date of his death has been fully received, the amounts thereafter paid to her are not considered capital gain to her but are treated as ordinary income distributions under the terms of the will or trust. The income of the trust paid or made available to her during the years 1928 and 1929 should be reported in her 1928 and 1929 income tax returns, respectively. Any part of the trust income derived from State obligations and paid to her may be excluded from her gross income. Also the amounts received by her from the trust representing dividends specified in section 25(a) of the Revenue Act of 1928 may be taken by her as a credit for the purpose of computing the normal tax but not the surtax. (Section 163(b) of the Revenue Act of 1928.)

The payments made by the trust to the taxpayer prior to the time the value of her dower or statutory interest in the estate as of the date of the death of her husband was recovered by her are treated as payments on the purchase price of her dower or statutory interest. Prior to that time, the payments so made by the trust may not be deducted in computing the net income of the trust, as only those distributions of income by an estate or trust which under the taxing statutes "shall be included in computing the net income of the beneficiaries" are allowable as deductions in computing the net income of the estate or trust. Thereafter the payments are treated as ordinary income distributions under the terms of the will or trust, and may be taken as deductions in computing the net income of the trust or estate.

Due to the fact that if the taxpayer had elected to take under the statute instead of under the will she would have been entitled to receive the income for life on approximately one-third of the value of the estate, the question is raised as to whether she should report now on only two-thirds of the income received from the trust. The value of her right to receive income for life on approximately one-third of the testator's estate was a factor necessary in determining the value of her statutory interest in the estate as of the date of the death of the testator. This value now having been returned to her, the income of the trust distributed or credited to her in any taxable year, with the exception of any income from State obligations, constitutes taxable income to her in its entirety and should be so reported in her income tax return.

SECTION 105.—TAXABLE PERIOD EMBRACING YEARS WITH DIFFERENT LAWS:

ARTICLE 551: Fiscal years ending in 1928.

VIII-26-4250
I. T. 2476

REVENUE ACT OF 1928.

In the case of the first return of the M Company, which was incorporated October 24, 1927, and established the last day of February as the close of its fiscal year, the tax should first be computed under the Revenue Act of 1926 as if the entire income was received during the calendar year 1927, and the tax attributable to

the year 1927 is 10/12 of that amount; the tax should then be computed under the Revenue Act of 1928 as if the entire income were received during the year 1928, and the tax attributable to 1928 is 2/12 of that amount; the amounts of tax attributable to each year, as so computed, should be added together, and the total is the amount of tax due.

A ruling is requested relative to the method of computing the tax under the rates applicable to the years 1927 and 1928, in the case of the first return filed by the M Company, which was incorporated October 24, 1927, and established the last day of February as the close of its fiscal year. Should the tax in such case be prorated on the basis of a period of 4 months and 8 days or on the basis of a period of 12 months?

The position of the Bureau is that the return of a corporation of the income received or accrued from the date of its incorporation to the end of its first accounting period, even though such period is less than 12 months, is a return for a period of 12 months and not a return for a fractional part of a year. (See G. C. M. 5695, C. B. VIII-1, 285, and the authorities referred to therein.) Accordingly, the return in the instant case was a return for a full taxable year of 12 months; and the tax should be computed on that basis the same as if the corporation had been in existence during the entire 12-month period.

Applying the foregoing principle and the provisions of section 105 of the Revenue Act of 1928, the tax of the M Company for the fiscal year ended February 29, 1929, should first be computed under the Revenue Act of 1926 as if the entire income was received during the calendar year 1927, and the tax attributable to the year 1927 is 10/12 of that amount; the tax should then be computed under the Revenue Act of 1928 as if the entire income were received during the year 1928, and the tax attributable to 1928 is 2/12 of that amount; the amounts of tax attributable to each year, as so computed, should be added together, and the total is the amount of tax due.

SUPPLEMENT B.—COMPUTATION OF NET INCOME.

SECTION 113.—BASIS FOR DETERMINING GAIN OR LOSS.

ARTICLE 591: Basis for determining gain or loss
from sale.

REVENUE ACT OF 1928.

Dower or statutory interest, value not having been returned to widow before her death. (See I. T. 2480, page 141.)

ARTICLE 591: Basis for determining gain or loss
from sale.

REVENUE ACT OF 1928.

Warrants distributed by an investment company to stockholders of another company giving them preferential right to subscribe to stock in the investment company. (See G. C. M. 7246, page 80.)

ARTICLE 600: Stock or securities distributed in re-organization.

REVENUE ACT OF 1928.

Amendment of article 600, Regulations 74. (See T. D. 4274, page 240.)

SECTION 115.—DISTRIBUTIONS BY CORPORATIONS.

ARTICLE 628: Stock dividends.

VIII-39-4367
G. C. M. 6709

REVENUE ACT OF 1928.

By the terms of the charter of the M Company the dividend on the "Convertible class A stock, optional dividend series," is payable (1) in class B stock at a given rate or (2), at the option of the stockholders, in cash at a certain rate per annum.

The charter of the O Company contains similar provisions, varying only as to the amount of dividend payable in stock.

Held, that a stockholder who does not exercise his option to take cash receives a true stock dividend, and such dividend does not constitute taxable income.

An opinion is requested relative to the taxable status of the dividends paid to the stockholders of the M Company and the O Company in accordance with the declarations by the respective boards of directors on —, 1929.

Under the terms of its charter the M Company has issued stock known as "Convertible class A stock, optional dividend series." By the terms of the charter the dividend on the convertible stock is payable (1) in class B stock of the corporation at a given rate or (2), at the option of the stockholders, in cash at a certain rate per annum. If, prior to the expiration of the tenth day following the record date, the corporation receives from a holder of record of the convertible stock a notice of his election to receive cash in lieu of class B stock, then the dividend is to be paid to said stockholder in cash. If no such notice is received, the dividend is paid in stock.

The charter of the O Company contains similar provisions, varying only as to the amount of dividend payable in stock.

The question submitted is whether under the circumstances stated above the dividends received by a stockholder who does not exercise his option to take cash are to be treated for income tax purposes as stock dividends or cash dividends.

It is apparent that the dividends in the case of each of the corporations are by the terms of the corporation's charter primarily stock dividends, and become cash dividends only if a stockholder elects to receive cash in lieu of stock and, within a given time, notifies the corporation of such election. Many cases have been decided where the dividend is available in cash but the cash may be used to purchase stock (see O. D. 565, C. B. 3, 22; T. B. R. 63, C. B. 1, 24; A. R. R. 1127, C. B. 1-2, 8; W. J. Hunt, *supra*; W. H. Davidow Sons Co., 1 B. T. A., 1215), but that is not the situation in the instant case.

The dividends under consideration are not available to a stockholder as cash dividends unless and until the stockholder notifies the

corporation of his desire to receive cash. Then, and not before, does the relationship of debtor and creditor arise as between the corporation and the stockholder who elects to receive cash. The contingency might well arise whereby none of the stockholders would notify the corporation. In that event a true stock dividend would be distributed, and the stockholders would not receive "income" within the meaning of the word as used in the sixteenth amendment and as interpreted by the Supreme Court in the case of *Eisner v. Macomber* (252 U. S., 189, T. D. 3010 (C. B. 3, 25)). (See also section 115(f) of the Revenue Act of 1928.)

In case there is no election to receive cash in lieu of stock of the corporation, the shareholder does not receive a distribution from the surplus of the corporation. The stockholder receives nothing out of the corporation's assets for his individual use, and those assets still remain the property of the corporation, subject to all the hazards of the business. He does not receive "income"; the corporation is none the poorer, and the stockholder is none the richer. There is merely a transfer of surplus to capital account, although the number of shares issued and outstanding is increased. Such dividends would not, under *Eisner v. Macomber*, supra, be taxable.

When a corporation declares a dividend payable partly in cash and partly in stock, the portion of the dividend paid in stock is not subject to taxation. (In this connection compare O. D. 587, C. B. 3, 23; and see T. D. 3052, paragraph 4, C. B. 3, 38.)

In view of the foregoing, this office is of the opinion, under the facts hereinbefore stated, that a stockholder who does not exercise his option to take cash receives a true stock dividend, and such dividend does not constitute taxable income.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

ARTICLE 629: Distribution in redemption or cancellation of stock taxable as dividend.

VIII-36-4336
I. T. 2493

REVENUE ACT OF 1928.

To holders of record of common stock of the M Company as of January —, 1929, one share of class "A" stock was distributed for each share of common stock then held. The class "A" stock was issued with the further provision that 20 per cent of the amount thereof would be purchased or redeemed by the company, at the option of the holder, on or before March —, 1929, at 10x dollars per share. The taxpayer received 5y shares of the class "A" stock and in accordance with the terms of the issue surrendered y shares to the company on March —, 1929.

The entire amount realized by the taxpayer from the surrender of the y shares should be reported as a taxable dividend. With respect to the remaining shares of the class "A" stock which were not redeemed, the transaction constituted a true stock dividend.

Advice is requested relative to the determination of the taxable gain resulting from the disposition to the M Company by A on March —, 1929, of y shares of class "A" stock of the M Company following a distribution of class "A" stock as a stock dividend to the holders of record of the common stock as of January —, 1929.

The class "A" stock is preferred as to dividends over the common stock at the annual rate of — per cent a share, such dividends being cumulative. One share of class "A" stock was distributed for each share of common stock then held. The class "A" stock was issued with the further provision, however, that 20 per cent of the amount thereof would be purchased or redeemed by the company at 10 x dollars a share upon presentation of the certificate properly indorsed along with payment of the transfer tax.

From 1921 to 1927 A purchased, apparently in various lots, 2.5 y shares of the common stock, which, as a result of a 100 per cent stock dividend, were increased to 5 y shares. A accordingly received 5 y shares of the class "A" stock, and in accordance with the terms of the issue surrendered y shares to the company on March —, 1929, and received as consideration therefor 20 z dollars, less transfer tax.

With reference to the question presented, attention is directed to section 115(g) of the Revenue Act of 1928, which is as follows:

Redemption of stock.—If a corporation cancels or redeems its stock (whether or not such stock was issued as a stock dividend) at such time and in such manner as to make the distribution and cancellation or redemption in whole or in part essentially equivalent to the distribution of a taxable dividend, the amount so distributed in redemption or cancellation of the stock, to the extent that it represents a distribution of earnings or profits accumulated after February 28, 1913, shall be treated as a taxable dividend. In the case of the cancellation or redemption of stock not issued as a stock dividend this subsection shall apply only if the cancellation or redemption is made after January 1, 1926.

To the extent of 20 per cent thereof, the class "A" stock was subject to redemption at the option of the holder by presentation of the certificate at any time from the date of issue to the close of business on March —, 1929, and the consideration therefor in the amount of 10 x dollars a share less transfer tax was available to the holder in cash during such time. Such redemption of stock clearly comes within the above-quoted provisions of the statute and the transaction is held to be equivalent to the distribution of a taxable dividend, assuming the company to have had on hand earnings or profits accumulated after February 28, 1913, equal to or in excess of the amount paid to the shareholders.

The entire amount realized by A from the surrender of the y shares of such stock on March —, 1929, should accordingly be reported as a taxable dividend subject to the surtax only. On the understanding that the remaining shares of the class "A" stock received by A were not redeemed, the transaction resulted in a true stock dividend as to such shares which did not give rise to taxable income but which called for the allocation or apportionment of the costs of the various lots of his common stock then held between such common stock and the class "A" stock received as a stock dividend.

As will be seen from the foregoing, $4/5$ of a share of the class "A" stock was received as a stock dividend for each share of the common stock then held. The value of the class "A" stock at the time is shown to have been 10 x dollars a share. The value of the $4/5$ of a share received with each share of the common stock was therefore 8 x dollars and the value of the common share is shown to have been 25 x dollars, the total of such two values being 33 x dollars. The cost of the various lots of the common stock then held as previously increased by the 100 per cent stock dividend should accordingly be

apportioned between the common shares and the class "A" shares distributed as a stock dividend in the ratio or proportion of the respective values as indicated above.

SECTION 141.—CONSOLIDATED RETURNS OF CORPORATIONS—1929 AND SUBSEQUENT TAXABLE YEARS.

ARTICLE 712: Formation of and changes in affiliated group.

VIII-52-4480
G. C. M. 7331

REVENUE ACT OF 1928.

Where a parent corporation, for a legal intra vires purpose, has placed the record ownership of a share of stock of a subsidiary in a nominee, such nominee being at all times legally obligated to hold and deal with such share according to such orders and direction as the parent corporation may, from time to time, give him, the ownership of the parent corporation is "direct" within the meaning of section 141(d) of the Revenue Act of 1928.

The opinion of this office has been requested as to whether a parent corporation *owns directly* a share of stock of a subsidiary, within the meaning of section 141(d) of the Revenue Act of 1928, in a case where the parent corporation, for a legal intra vires purpose, has caused the name of another (commonly called a nominee) to appear upon the stock book and records of the subsidiary as the owner of such share, the nominee being at all times legally obligated to hold and deal with such share according to such orders and direction as the parent corporation may, from time to time, give him. Characteristically, the certificate representing the share is indorsed to the nominee; transfer is thereupon made upon the stock book of the subsidiary, the nominee's name is entered upon the stock book as the owner of the share, and the nominee then indorses the new certificate in blank or to the parent corporation and delivers it to the parent corporation, which retains the certificate in its possession. Placing the record ownership of the share in a nominee serves a variety of purposes, among them being the qualification of the nominee as a director of the subsidiary, the convenient conduct of corporate meetings of the subsidiary, and the convenient transfer of shares of the subsidiary.

The legal relationship between the parent corporation and the nominee, as respects the share, is clear. The entire beneficial, or equitable, ownership (often spoken of as the "real" ownership) is in the parent corporation, but the legal title to the share is in the nominee. (Clark and Marshall Corporations, section 661; *People ex rel. Matthiessen et al. v. Lihme*, 269 Ill., 351, 109 N. E., 1051.) But, while the nominee is a technical trustee of the legal title, his relationship to the parent corporation is essentially that of an agent to his principal. (Cox's Case, 4 De Gex, J & S., 53; Pugh and Sharman's Case, L. R. 13 Eq., 566; "Trusteeship and Agency," 8 Law Qu. Rev., 220.) The rights, duties, powers, liabilities, and immunities existing between the parent corporation and the nominee are, in all essential respects, those existing between principal and agent. (*Stover v. Flock* (1864), 30 N. Y., 64; *Morse v. Pacific R. Co.*

(1900), 93 Ill. App., 33; see Note 3, B. R. C., 365.) It is true that the nominee, as holder of the legal title to the share, may, in violation of the instructions of the parent corporation, or in fraud of it, transfer the share to a bona fide purchaser, for value and without notice, and thus vest in such a purchaser a title, absolute in its nature, good against the world. (*Dueber, etc., Co. v. Daugherty*, 62 Ohio St., 589.) But so may any other agent, where the parent has given to the agent the indicia of ownership. (*Smith v. Clews*, 105 N. Y., 283; *Wilson v. Loeb*, 69 Ill. App., 445; *Ferquharson v. King* (1901), 2 K. B., 697; *Heath v. Stoddard*, 91 Me., 499.) It is also true that, upon demand made of the nominee by the parent corporation for a transfer to it of the nominee's legal title (and/or the transfer of the share certificate), the legal title vests forthwith in the parent corporation and, upon refusal, the nominee becomes a converter. (*Guaranty Loan Co. v. Treadwell*, 53 Cal. App., 538, 200 Pac., 653.)

The almost universal rule that the nominee is entitled to vote as a shareholder, and qualified to act as a director (where shareholding is a prerequisite to qualifying as a director) (*People ex rel. Matthiessen et al. v. Lihme*, supra; *Re Leslie*, 58 N. J. L., 609; *In re Argus Printing Co.*, 1 N. D., 434, 12 L. R. A., 781; 48 N. W., 347; *State v. Leele*, 16 Nev., 242; *Toronto Brewing Co. v. Blake*, 2 Ont. (Can.), 175; *Pulbrook v. Richmond, etc., Co.*, L. R., 9 Ch. D., 610; *Bainbridge v. Smith*, 41 Ch. D., 462; *Citizens National Bank v. Sturgis National Bank*, 81 S. W., 550) is not premised upon the ground that the nominee is the equitable, beneficial, or real owner, but upon a quite different ground, adequately expressed by the Supreme Court of Wisconsin in *Casper v. Kalt-Zimmers Manufacturing Co.* (159 Wis., 517, 149 N. W., 754):

The reason given for a * * * rule requiring that the equitable or beneficial interest in the stock should be in a person in order to render him eligible as an officer * * * is that officers of a corporation should be personally interested in its welfare, and that can be the case only when the legal and beneficial interest unite [sic] in the same person. We do not so consider it. Trust duties are some of the most sacred duties there are, and the confidence reposed through them is seldom abused. Even where stock is transferred for the express purpose of qualifying one to hold a corporate office, the person so transferring it is personally interested in the sound management of the corporation and would be unlikely to jeopardize his interest by placing the stock in incompetent hands. The rule that merely a legal title qualifies is more in consonance with present business requirements and is fraught with no undue hazard to stockholders.

And the contrary rule, prevailing at one time in New York, rested squarely upon the ground that, the New York statute requiring a director to be an "owner" of at least one share of stock, the nominee was not the "owner" while his principal was the "owner." (*Chemical National Bank of New York v. Colwell*, 132 N. Y., 250, 30 N. E., 644; *In re Elias*, 17 N. Y. Misc., 718, 40 N. Y. Supp., 910; *In re George Ringler & Co.*, 204 N. Y., 30, 97 N. E., 593, reviewing 145 N. Y. App. Div., 361, 130 N. Y. Supp., 62, affirming 70 N. Y. Misc., 581, 127 N. Y. Supp., 938.)

The essential character of the relationship between the parent corporation and the nominee as an agency finds uniform application under the various Revenue Acts. Under them, it has uniformly been recognized that the principal, the parent corporation, is the

owner of the share, is in receipt of income when dividends are declared upon the share, and realizes gain or loss from the sale or disposition of the share. (Cf. Appeal of Henry Grimmer, 3 B. T. A., 313, C. B. V-1, 3; appeal of Kathryn M. Haskell, Exr., 2 B. T. A., 1300, C. B. IV-2, 3; *P. J. Clancy & Co., Inc., v. Commissioner*, 12 B. T. A., 855; *A. W. E. Capel v. Commissioner*, 7 B. T. A., 1076, C. B. VII-1, 6; *Elizabeth Berthold et al. v. Commissioner*, 12 B. T. A., 1306.) The combination in the parent corporation of complete beneficial ownership of, and complete dominion over, the shares is such that it has not been suggested that the nominee is subject to the provisions of sections 161 and 143 of the Revenue Act of 1928 and the corresponding provisions of earlier Acts, relating to trusts and fiduciary returns. (Cf. *G. C. M. 2185*, C. B. VI-2, 75; *G. C. M. 4120*, C. B. VII-2, 108; and *United States v. Robbins et al.*, 269 U. S., 315 (T. D. 3817, C. B. V-1, 188).)

Does the parent corporation having the whole beneficial ownership of, and complete legal dominion over, the share own directly such share, within the meaning of section 141(d) of the Revenue Act of 1928? That subsection reads:

SEC. 141. (d) *Definition of "affiliated group."*—As used in this section an "affiliated group" means one or more chains of corporations connected through stock ownership with a common parent corporation if—

(1) At least 95 per centum of the stock of each of the corporations (except the common parent corporation) is owned directly by one or more of the other corporations; and

(2) The common parent corporation owns directly at least 95 per centum of the stock of at least one of the other corporations. As used in this subsection the term "stock" does not include nonvoting stock which is limited and preferred as to dividends."

Only one thing is lacking to the parent corporation's complete and absolute ownership, namely, the legal title, and even this the parent corporation may at any time obtain by a demand made upon the nominee. As has been pointed out, actual beneficial ownership, when complete and entire, is decisive generally for the purposes of the Revenue Acts. And the parent corporation assuredly in every substantial sense of the term owns the share. The only relevant question is whether it owns the share "directly."

The literal meaning of the term "directly" would seem to contemplate the ownership existing in the case under consideration. The parent corporation, being possessed of the entire beneficial ownership of the share and thus owning it, owns it "directly," because of direct power over the share possessed by the parent corporation—a power exercisable and legally enforceable at all times and as complete as the dominion exercisable by one having both beneficial and legal ownership. The ownership of the parent corporation, being sufficiently complete for all other purposes of the Revenue Act of 1928, is, therefore, "direct" within the meaning of section 141(d) of the Revenue Act of 1928. Cf. General Counsel's Memorandum 2780 (C. B. VII-1, 175), in which it is stated:

This office is unable to find any authority for considering the so-called "indirect" ownership of stock under the consolidated returns provisions of the 1924 Act. Possibly that theory may have had some value in applying such terms as "controls through closely affiliated interests" in the former Acts. No doubt where one owns stock in a corporation which in turn owns stock in a second corporation, he may be said to have an *interest* in such stock of the second, for,

as was said in the case of *Elsner v. Macomber* (252 U. S., 189 [T. D. 3010, C. B. 3, 25]), the "interest" of a stockholder "pertains, not to any part divisible or indivisible, but to the entire *assets*, business and affairs of the company." But, as the court further observes, this "interest" is not that "of *owner* in the assets themselves since the corporation has *full title*, legal and equitable, to the *whole*." [*Italics supplied.*]

Cases where a corporation for illegal or ultra vires purposes vests in a nominee the bare legal title to a share, and cases where a corporation for legal or intra vires purposes vests in a nominee legal title to a share but does not retain a complete dominion over the share exercisable and enforceable at all times by legal remedies, rest upon considerations fundamentally different from those in the case here under consideration. Hence, this office expresses no opinion with respect to the applicability of section 141(d) of the Revenue Act of 1928 to such cases.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

SECTION 148.—INFORMATION AT SOURCE.

ARTICLE 811: Return of information as to pay- VIII-48-4445
ments of \$1,500. T. D. 4278
(Also Articles 812 and 817.)

INCOME TAX.

Articles 811, 812, and 817 of Regulations 74 amended.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, D. C.

To Collectors of Internal Revenue and Others Concerned:

The first sentence of article 811, Regulations 74, is amended to read as follows:

All persons making payment to another person of fixed or determinable income of \$1,500 or more in any calendar year must render a return thereof for such year on or before February 15 of the following year to the collector of internal revenue for the payor's district, except as specified in articles 813-815.

The second sentence of article 812 of Regulations 74 is amended to read as follows:

Heads of branch offices and subcontractors employing labor, who keep the only complete record of payments therefor, should file returns of information in regard to such payments directly with the collector of internal revenue for the payor's district.

The last sentence of article 817, Regulations 74, is amended to read as follows:

Such forms accompanied by Form 1096 should be forwarded to the collector of internal revenue for the payor's district on or before February 15 of each year.

In any case where it is shown that it is impossible to file the return within the time herein prescribed, a reasonable extension of time may be obtained for filing the return. The request for the extension of

time must be forwarded to the collector for the payor's district on or before the date prescribed for filing the return.

ROBT. H. LUCAS,
Commissioner of Internal Revenue.

Approved November 23, 1929.

A. W. MELLON,
Secretary of the Treasury.

ARTICLE 811: Return of information as to payments of \$1,500.

VIII-51-4472
Mim. 3772

Preparation of information Forms 1096 and 1099 by oil producers and lessees of prospective oil-producing property.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, D. C., December 2, 1929.

Collectors of Internal Revenue, Internal Revenue Agents in Charge, and Others Concerned:

It has come to the attention of the Bureau that in many instances individuals, partnerships, and corporations engaged in the prospecting and development of oil-producing properties have not complied with the provisions contained in section 148 of the Revenue Act of 1928 and the corresponding sections of the prior Revenue Acts relating to information at the source. Under these provisions of law the Bureau requires all persons, in whatever capacity acting, including lessees of real property, making payment to another person of fixed or determinable gains, profits, and income, to render an information return on Forms 1096 and 1099 in respect of such payments.

Royalties, rentals, bonuses, and similar payments designated by any other classification paid to owners of the fee to land which has been or will be exploited for natural resources are types of income included under the provisions of the statute. Rentals, royalties, or bonuses paid in advance upon the acquisition of a lease and commissions paid to lease brokers and others interested in leases, although not owners of the fee, are also included.

Income of this nature must be reported on Form 1099 when paid to individuals, if the payments made during the calendar year equal \$3,500 or more in the case of a married person, or \$1,500 or more in the case of a single person.

Banks, trust companies, abstract companies, and others receiving such income as described above in the capacity of collection agents for the fee owners are the source of the information and must prepare Form 1099 for each individual to whom amounts equal to those referred to above are paid or credited. Care should be used by all payors to include on Forms 1099 only those amounts paid during the calendar year for which the report is made. For the purposes of section 148, an amount is deemed to have been paid when it is credited or set apart to the taxpayer without any substantial limitation or restriction as to the time or manner of payment or condition upon which payment is to be made, and which is made available to

him so that it may be drawn at any time, and its receipt brought within his own control and disposition.

Forms 1096 and 1099 covering such payments are required to be filed with the collector of internal revenue for the payor's district on or before February 15 of the following year.

Queries regarding this mimeograph or procedure in connection therewith should refer to the number of the mimeograph and the symbols IT:R:S.

ROBT. H. LUCAS, *Commissioner*.

ARTICLE 812: Return of information as to payments to employees.

REVENUE ACT OF 1928.

Amendment of article 812, Regulations 74. (See T. D. 4278, page 138.)

ARTICLE 817: Return of information as to foreign items.

REVENUE ACT OF 1928.

Amendment of article 817, Regulations 74. (See T. D. 4278, page 138.)

SECTION 149.—INFORMATION BY CORPORATIONS.

ARTICLE 831: Return of information as to payments of dividends.

VIII-48-4444
T. D. 4277

INCOME TAX.

Returns of information as to payments of dividends to be filed not later than February 15 of the following year.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, D. C.

To Collectors of Internal Revenue and Others Concerned:

Section 149 of the Revenue Act of 1928 provides that every corporation subject to income tax shall, when required by the Commissioner, render a correct return, duly verified under oath, of its payments of dividends, stating the name and address of each shareholder, the number of shares owned by him, and the amount of dividends paid to him. In accordance with this section of the Act, returns of information in respect of dividend payments shall be rendered for the calendar year 1929 and each calendar year thereafter as follows:

(a) Except as provided in paragraph (b) below, every domestic or resident foreign corporation and every nonresident foreign corporation having a fiscal or paying agent in the United States, not specifically exempt from taxation, making payments of dividends and distributions out of its earnings or profits accumulated since February 28, 1913 (other than stock dividends or distributions in

liquidation), to any shareholder who is an individual (citizen, resident, or nonresident alien), a fiduciary, or a partnership, amounting to \$500 or more during the calendar year, shall render an information return on Forms 1096 and 1099 for the calendar year 1929 and each calendar year thereafter. A separate Form 1099 must be prepared for each shareholder, upon which will be shown the name and address of the shareholder to whom such payment was made, and the amount paid. These forms, accompanied by letter of transmittal on Form 1096 showing the number of Forms 1099 filed therewith, shall be forwarded to the collector of internal revenue for the district in which the corporation has its principal office or place of business on or before February 15 of the following year.

(b) In cases where distributions are made from a depletion or depreciation reserve, or which for any other reason are deemed by the corporation to be nontaxable or partly nontaxable to its shareholders, the corporation will first fill in the information on the reverse side of Form 1096 and forward this form to the Commissioner of Internal Revenue, Sorting Section, Washington, D. C., not later than February 1 of the following year. Upon receipt of this information the Commissioner will determine and advise the corporation by letter whether any portion of such distribution is subject to tax. The corporation after receiving this letter will then properly prepare for each shareholder a Form 1099, which shall be forwarded with Form 1096 to the Commissioner of Internal Revenue, Sorting Section, Washington, D. C., not later than 30 days after such letter is received.

In any case where it is impossible to file the return within the time herein prescribed, the corporation may, upon a showing of such fact, obtain a reasonable extension of time for filing the return. The request for the extension of time must be forwarded to the collector on or before the date prescribed for filing the return.

Treasury Decision 4236 (C. B. VII-2, p. 71), in so far as it is inconsistent with the provisions of this Treasury decision, is hereby revoked.

ROBT. H. LUCAS,

Commissioner of Internal Revenue.

Approved November 23, 1929.

A. W. MELLON,

Secretary of the Treasury.

SUPPLEMENT E.—ESTATES AND TRUSTS.

SECTION 162.—NET INCOME.

ARTICLE 861: Estates and trusts.
(Also Section 113, Article 591.)

VIII-29-4276
I. T. 2480

REVENUE ACT OF 1928 AND PRIOR REVENUE ACTS.

The income from property held by an estate or trust to satisfy annual payments to a widow in lieu of her dower or statutory interest is not an allowable deduction in the return of the estate or trust prior to the time such payments equal the value of her dower

or statutory interest in her deceased husband's estate. After that time, she is treated as any other income beneficiary under the will, and the executors or trustees are permitted to deduct the amount of the annual payments in computing the net income of the estate or trust. The basis of the property representing the widow's dower or statutory interest in the hands of the estate or trust can not exceed the value thereof on the date of the testator's death. If the widow dies before the value of her dower or statutory interest has been returned to her and a sale or other disposition is made by the estate or trust, the basis for determining gain or loss is the actual cost measured by the annual payments actually made.

A ruling is requested in connection with the proper application of the decisions of the circuit courts of appeals in the cases of *Warner v. Walsh* (15 Fed. (2d), 367, T. D. 4257, C. B. VIII-1, 245), *United States v. Bolster* (26 Fed. (2d), 760, T. D. 4258, C. B. VIII-1, 247), and *Allen v. Brandeis* (29 Fed. (2d), 363, T. D. 4256, C. B. VIII-1, 243).

In the case of *Warner v. Walsh* the facts stated by the court are as follows:

Under the will of plaintiff's deceased husband, a large and ample trust fund was created, out of the income, and, if necessary, out of the principal, of which plaintiff was to receive \$50,000 a year for life. This provision was expressly made in lieu of her statutory rights in the estate under the laws of Connecticut and was so accepted by her. She personally was compelled to pay Federal income tax on the \$50,000 for each of the years 1917 and 1918.

In considering the question of whether the claimant (the widow) should pay income tax on the annual payments received by her, the court held that the widow should be treated as the purchaser of the annuities by the relinquishment of her statutory rights in her husband's estate, and that no tax could be collected from her until the purchase price was returned to her.

In *United States v. Bolster*, the material facts are as follows:

Sarah A. Davenport, of Boston, was the beneficiary under the will of her husband, Orlando H. Davenport, who died on the 11th day of January, 1925. The will provided that the residue of the decedent's estate should be held in trust, and, after payment of expenses of administering the trust, the income was to be paid over to Sarah A. Davenport, for and during her life; and that the provision made for her should be "in lieu of dower and all claims she might or could have by any possibility upon the estate."

The wife accepted the provisions made for her in the will, and received the net income of the trust during the years 1919 to 1923, inclusive, namely, \$113,811.82. This sum Sarah A. Davenport included in her income tax returns for the above years as a part of her gross income.

In that case the court recognized that the annual payments were not strictly annuities, but it applied the rule laid down in *Warner v. Walsh* and held that the widow was the purchaser of the annual payments to the extent of the value of her statutory interest in her husband's estate as of the date of his death. The court also stated that the income from the property would have been taxable to the trust if it were not for the fact that the entire residue of the decedent's estate was under the will "permanently set aside for the benefit of charitable institutions."

In *Allen v. Brandeis* the facts are that on June 10, 1916, Arthur D. Brandeis died, leaving a will which provided, in the tenth paragraph thereof, for a payment of \$50,000 per year to his wife for life in lieu of her statutory interest in his estate. The will further provided:

* * * only the net income and profits from my property shall be available to pay the bequests mentioned in the seventh, tenth, eleventh, and twelfth paragraphs hereof. Should such income and profits be insufficient at any time to pay the bequests mentioned in said paragraph in full, each of said bequests shall bear a proportionate part of such deficiency. A deficiency arising during any year may be made up out of the income and profits for any succeeding year or years.

The widow elected to take under the terms of the will. The value of her statutory interest in her husband's estate was determined to be \$483,737.79. The court in following *Warner v. Walsh*, supra, and *United States v. Bolster*, supra, held that the widow purchased the annual payments "from those representing her husband's estate" by the relinquishment of her statutory interest in her husband's estate, and that she should not be required to pay income tax on the annual payments received until the capital invested in the annuities had been returned to her. After that time, the court conceded she should pay tax.

The question arises whether the income from the property, held by the estate or trust, which is used to satisfy the annual payments to the widow, should be taxed to the estate or trust.

It is apparent from the decisions mentioned that the courts regarded the annual payments to the widow as constituting a return of capital to her until such time as the value of her dower or statutory interest in her husband's estate as of the date of his death was fully recovered by her. Under these decisions, the annual payments made prior to the time when they equal the value of the widow's interest in her husband's estate are not treated as gifts or bequests, but are treated as payments made on the purchase price of the widow's dower or statutory interests. It is also apparent from these decisions that the courts regarded the estate or trust as liable for a tax upon the income paid over to the widow. In *United States v. Bolster*, supra, the court said:

By the later Acts Congress provided that the tax should apply to "income of estates and trusts" and "should be paid by the trustee" in certain cases where the trustee could not be reached by the earlier Act. In the instant case we do not have to consider the possibility of the Government losing its rightful tax upon income which Congress intended should be taxed. It is not a question of a statute "failing to hit" something which ought to be taxed. Under the statute with which we are dealing a trust is the subject of taxation just as an individual. *We think the Government must look to the trustee for its tax*; and that the trust would clearly be taxable upon this income if it were not expressly exempted because of its charitable character.

In *Heiner v. Beatty* (17 Fed. (2d), 743) it was contended that income received by the taxpayer under the will of the decedent was exempt from taxation because that income constituted a "bequest." In the instant case the ground of the exemption is not that the income received is a bequest but that such income is exempt because it represents "purchase money" or a return of capital. [Italics supplied.]

To the same general effect see *Codman v. Miles* (28 Fed. (2d), 823 [Ct. D. 46, C. B. VIII-1, 240]), where the court said:

If by special provision the plaintiff had been entitled to receive the specific amounts equaling each year's income as bequests or gifts and not income *eo nomine*, appellant's contention might have been well taken, *but in such instance the estate itself* would have been subject to the tax. [Italics supplied.]

Since the payments to the widow are made in satisfaction of a capital obligation of the estate or trust, it follows that in computing the net income of the estate or trust the payments so made prior to

the time that the value of the widow's dower or statutory interest is returned to her can not be deducted as ordinary distributions of income to beneficiaries. It is only those distributions of income by an estate or trust which under the taxing statute "shall be included in computing the net income of the beneficiaries" that are allowable as deductions in computing the net income of the estate or trust. Such distributions do not include payments made to a widow prior to the time they equal the value of her dower or statutory interest in her deceased husband's estate. After that time, however, the annual payments should be treated as ordinary income distributions under the terms of the will or trust, and may be taken as deductions in computing the net income of the estate or trust. In other words, the excess of the annual payments over the value of the widow's statutory or dower interest is not to be regarded as being received for a consideration. In this connection see *Robertson v. Commissioner* (5 B. T. A., 748; C. B. VI-1, 5; O. D. 847, C. B. 4, 45). See also the decision of the United States Circuit Court of Appeals for the Seventh Circuit in the case of *John W. Scott v. Commissioner* (29 Fed. (2d), 472). The facts in that case were that the father conveyed a partnership interest to his three sons in consideration for the payment by them of certain annuities to the father and on his death to their mother. The value of the partnership interest conveyed was greatly in excess of the value of the annuity to the father and mother. The court held that the annual payments could not be deducted by the sons in computing their net income. In the course of its opinion the court said:

While unquestionably the actual value of the interest was many times more than the value of the stipulated annuity to father and mother, *and to the extent of the excess might be considered a gift in the usual purport of that term*, nevertheless the annuity can not be regarded as being merely nominal, and warranting the conclusion that the entire transaction manifests a gift. It is surely not so nominal but that the petitioner is predicated this claim upon the right to deduct one-third of it from his income. [Italics supplied.]

Attention is called to certain problems arising from the disposition of the property held subject to the widow's annuity by the estate or trust, and an opinion is requested as to the proper basis for determining gain or loss from the sale or other disposition by the estate or trust. As pointed out above, the courts have treated the widow as the purchaser of the annual payments only until the sum of the annual payments equals the value of her interest in her husband's estate. After that time she is treated as any other income beneficiary under the will, and the executors or trustees are permitted to deduct the amount of the annual payments in computing the net income of the estate or trust.

Since the annual payments made to the widow, after the value of her dower or statutory interest has been returned to her, are taxable to her and may be taken as deductions by the estate or trust, it is evident that the basis of the property representing the widow's dower or statutory interest in the hands of the estate or trust can not exceed the value thereof on the date of the testator's death. If the widow dies before the value of her dower or statutory interest has been returned to her and a sale or other disposition is made by the estate or trust, the basis for determining gain or loss is the actual cost measured by the annual payments actually made.

ARTICLE 862: Method of computation of net income and tax.

REVENUE ACT OF 1928.

Payments to widow of income from a residuary trust prior to the time the value of her statutory interest in her husband's estate as of the date of his death has been fully received. (See I. T. 2506, page 129.)

SECTION 189.—PARTNERSHIP RETURNS.

ARTICLE 942: Contents of partnership return.

VIII-42-4390

I. T. 2503

REVENUE ACT OF 1928.

The capital contribution of a special partner is at the risk of the business the same as the contributions of the general partners. The money distributable to him, even though termed interest, represents a division of partnership profits, and is not deductible by the partnership as a business expense.

Advice is requested in regard to the treatment, by a partnership, of an amount paid to a special partner which is termed interest on his investment in the partnership.

In accordance with articles of agreement, a partnership was formed between A as special partner and other individuals as general partners. The agreement stated that A should be the special partner and should contribute to the capital of the firm the sum of x dollars in cash, upon which the firm was to pay him so-called interest at the rate of y per cent per annum, payable semiannually. The agreement specified that A should not receive a share in the profits of the firm or pay or be responsible for any portion of its losses or expenses, but the said payment of interest should be net to him. It was provided that upon liquidation of the firm, the said x dollars should be paid to A or his representative before payment was made to any of the other partners, but the said x dollars and any interest thereon should be liable for the debts of the firm to third parties. It was further provided that each of the general partners should receive so-called interest at the rate of z per cent per annum upon the amount of his investment in the partnership, and should, in addition, share in the net gains and profits of the firm in the proportion specified in the partnership agreement.

Inquiry is made whether the so-called interest paid to A as special partner is deductible as a business expense by the partnership in computing its net income, or whether the so-called interest received by A represents his distributive share of the net income of the partnership, to be ratably allocated to him in the same way as are the distributive shares of the general partners.

An examination of the partnership agreement discloses that the capital contribution of A to the firm is at the risk of the business, the same as the contributions of the general partners. It is held, therefore, that the money distributable to him as a special partner, but which is termed interest, represents a division of the profits earned during the year from the conduct of the partnership business, and is not deductible by the partnership as an item of business expense.

SUPPLEMENT H.—NONRESIDENT ALIEN INDIVIDUALS.

SECTION 212(b).—GROSS INCOME.

ARTICLE 1042: Exclusion of earnings of foreign ships from gross income.

VIII-27-4261
T. D. 4269

INCOME TAX.

Exemption from taxation of earnings of ships documented under the laws of Greece.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, D. C.

To Collectors of Internal Revenue and Others Concerned:

Section 213(b)8 of the Revenue Acts of 1921, 1924, and 1926, and sections 212(b) and 231(b) of the Revenue Act of 1928, provide that there shall be exempt from taxation the income of a nonresident alien or foreign corporation which consists exclusively of earnings derived from the operation of a ship or ships documented under the laws of a foreign country which grants an equivalent exemption to citizens of the United States and to corporations organized in the United States.

Greece grants an equivalent exemption to citizens of the United States and to corporations organized in the United States, from January 1, 1921. Accordingly, article 89 of Regulations 62, as amended by Treasury Decisions 3488 (C. B. II-1, p. 80), 3813 (C. B. V-1, p. 225), 4013 (C. B. VI-1, p. 59), 4098 (C. B. VI-2, p. 58), and 4227 (Bulletin VII-42, p. 4 [C. B. VII-2, 125]); article 89 of Regulations 65, as amended by Treasury Decisions 3812 (C. B. V-1, p. 47), 4013 (C. B. VI-1, p. 59), 4098 (C. B. VI-2, p. 58), and 4227 (Bulletin VII-42, p. 4 [C. B. VII-2, 125]); article 89 of Regulations 69, as amended by Treasury Decisions 4013 (C. B. VI-1, p. 59), 4098 (C. B. VI-2, p. 58), and 4227 (Bulletin VII-42, p. 4 [C. B. VII-2, 125]); and article 1042 of Regulations 74 are hereby amended so as to include Greece in the list of countries which exempt from tax so much of the income of citizens of the United States nonresident in such foreign countries and of corporations organized in the United States as consists of earnings derived from the operation of a ship or ships documented under the laws of the United States, and to exclude Greece from the list of countries which do not grant such exemption.

ROBT. H. LUCAS,
Commissioner of Internal Revenue.

Approved June 29, 1929.

A. W. MELLON,
Secretary of the Treasury.

SUPPLEMENT L.—ASSESSMENT AND COLLECTION OF DEFICIENCIES.

SECTION 272.—PROCEDURE IN GENERAL.

ARTICLE 1172: Collection of a deficiency.

VIII-31-4292

I. T. 2484

REVENUE ACT OF 1928.

The surety on the bond of the taxpayer, conditioned upon payment by the principal, on notice and demand, of such tax as was found to be due, is not entitled to have the bond released because of the mere filing by the collector of internal revenue of a notice of lien. Since the tax found to be due has not been paid, there has not been a compliance with the conditions of the bond.

It appears that additional tax for the year 1921 was assessed against A in March, 1926, in the sum of 6*x* dollars. From this assessment the taxpayer appealed to the Board of Tax Appeals, giving a bond to the collector of internal revenue, district of —, for the purpose of staying collection of the tax pending the outcome of the appeal. It also appears that a determination was made as to the amount due the Government; that on October —, 1928, a warrant of distraint was issued for what was then due; and that on January —, 1929, notice of lien was filed by the collector. The balance of the tax remaining unpaid now amounts to the sum of *x* dollars with interest.

Because of the fact that notice of lien was filed, inquiry is made on behalf of the M Company, surety on the bond, whether the bond may be withdrawn.

The bond given by the taxpayer is conditioned upon payment by the principal, on notice and demand, of such tax as was found to be due, plus any penalties and interest. It is clear that the taxpayer's indebtedness to the Government is not satisfied or paid by the mere filing of a notice of lien. Therefore, although notice of lien was filed, since the tax found due has not been paid, there has not been a compliance with the conditions of the bond. Accordingly, the obligations under the bond remain in force so that the surety thereunder is not now entitled to have the bond released.

SECTION 275.—PERIOD OF LIMITATION UPON ASSESSMENT AND COLLECTION.

ARTICLE 1202: Period of limitation upon collection of tax.

VIII-28-4271

Ct. D. 78

INCOME AND PROFITS TAXES—CANCELLATION OF WAIVER—DECISION OF COURT.

SUIT—WAIVER—CANCELLATION—UNITED STATES AS PARTY.

The United States is a necessary party to a suit in equity by a taxpayer to cancel and annul a consent in writing which purports to extend the period of limitations for the collection of income taxes.

UNITED STATES CIRCUIT COURT OF APPEALS, NINTH CIRCUIT.

Electric Steel Foundry, a Corporation, appellant, v. Clyde G. Huntley, as Collector of United States Internal Revenue, Oregon, and W. S. Shanks, as Deputy Collector, etc., appellees.

[May 27, 1929.]

OPINION.

RUDKIN, Circuit Judge: This was a suit by a corporation taxpayer against the United States collector of internal revenue and his deputy to cancel and annul an income and profits tax waiver executed by the secretary of the corporation, on the ground that the waiver was procured by duress and on the further ground that the secretary was without authority to bind the corporation. The bill of complaint was dismissed on motion in the court below for the reason that the United States was a necessary party, and the plaintiff has appealed.

The purpose of the waiver was to extend the period of the statute of limitations for the collection of a tax by distraint or by suit, and if the instrument has any virtue at all it is as a contract between the taxpayer and the United States. That such a contract can not be annulled or canceled in a suit against officers of the United States to which the United States is not a party would seem too plain to admit of discussion. No doubt, the Government is not a necessary party to a suit against an officer to compel him to perform ministerial duties enjoined by law, to restrain him from acting illegally or without authority of law, or in an action of trespass or for a tort. But this is not such a case. In the cases to which we have referred the judgment in nowise impairs the rights of the United States and does not affect it in its property or property rights, while here the decree will have the contrary effect if it be given any effect at all.

The distinction between the two classes of cases is clearly pointed out in *Sanders v. Saxton* (75 N. E., 529). There a landowner brought an action against the commissioners of the land office of the State of New York and the comptroller of the State to have certain deeds executed by the comptroller to the people of the State for unpaid taxes adjudged illegal and void. In reversing a decree in favor of the landowner, the court of appeals said:

"The action is both in effect and in form to cancel and remove the deeds to the people of the State of New York as clouds upon the plaintiff's title. The grantee in such a deed is plainly a necessary party to such an action, as it is the title of that grantee that is to be passed upon, and it can not be adjudged void unless he is brought in court. No one would ordinarily think of disputing this proposition. The only reason for omitting to make the State a party in this case is that it can not be made a party, and for that reason it is sought to avoid the immunity that the State possesses by making its officers parties in its stead. But it is also settled by the decisions of the Supreme Court that 'the United States are not bound by a judgment to which they are not parties, and that no officer of the Government can, by defending a suit against private persons, conclude the United States by the judgment.' (*Carr v. United States*, 98 U. S., 433; *United States v. Lee*, supra.) Now, as the only object and purpose of a suit in equity to remove a cloud on the title to property is to have any adverse title that may be asserted under such cloud passed on and adjudged void, so that the plaintiff in possession may be forever afterwards free from any danger of the hostile claim, it would seem plain that, where the judgment in an action can not conclude or bind a party claiming under the adverse title, the action must fail."

To the same effect see *Oregon v. Hitchcock* (202 U. S., 60), *Louisiana v. Garfield* (211 U. S., 70), *Goldberg v. Daniels* (231 U. S., 218), *Wells v. Roper* (246 U. S., 335).

So here, the only object and purpose of the suit was to destroy the waiver so that it could not be set up by the United States in opposition to a claim by the taxpayer that the right to collect the tax was barred by the statute of limitations. But a decree of the court in a suit against officers of the United States would not and could not deprive the Government of the right to plead the waiver or destroy its legal effect; and this much was conceded by the appellant on the argument before this court. Such being the case, a court of equity will not enter a decree that binds no one and determines nothing.

The decree of dismissal is affirmed.

TITLE IV.—ADMINISTRATIVE PROVISIONS.

SECTION 606.—CLOSING AGREEMENTS.

ARTICLE 1301: Closing agreements relating to tax liability in respect of internal-revenue taxes. VIII-28-4267
G. C. M. 6423

REVENUE ACT OF 1928.

The filing of a claim for refund may not be considered as a withdrawal of an offer to enter into a closing agreement under section 606 of the Revenue Act of 1928.

An opinion is requested as to whether the filing of a claim for refund may be considered as a withdrawal of an offer to enter into a closing agreement under section 606 of the Revenue Act of 1928.

An agreement form as to the final determination of tax liability, Form 866, was signed by the taxpayer on December 19, 1928, whereby it was proposed to agree that the tax liability for the year 1927 should be 5*x* dollars. In the last paragraph of the form it was stated that "the said taxpayer and said Commissioner of Internal Revenue hereby mutually agree that the principal amount of such liability so determined shall be final and conclusive if and when this agreement is approved by the Secretary of the Treasury or the Undersecretary." There was no time limit specified in the proposed agreement as to when the offer submitted by the taxpayer should be accepted. This agreement form was signed by the Commissioner on March 6, 1929, and approved by the Secretary of the Treasury on March 14, 1929.

The taxpayer under date of March 2, 1929, filed a claim for refund with the collector of internal revenue, stating that for the year 1927 there had been an overpayment of tax amounting to *x* dollars. This claim was received by the claims control section of the Bureau of Internal Revenue, at Washington, D. C., on March 5, 1929. The claim was based on the alleged nontaxability of certain dividends received during 1927 from the M Company. There was no letter of transmittal or statement in the claim requesting that the offer of the taxpayer to enter into a closing agreement be considered as withdrawn or canceled.

Section 606 of the Revenue Act of 1928 provides in part as follows:

(a) *Authorization*.—The Commissioner (or any officer or employee of the Bureau of Internal Revenue, including the field service, authorized in writing by the Commissioner) is authorized to enter into an agreement in writing with any person relating to the liability of such person (or of the person or estate for whom he acts) in respect of any internal-revenue tax for any taxable period ending prior to the date of the agreement.

(b) *Finality of agreements*.—If such agreement is approved by the Secretary, or the Undersecretary, within such time as may be stated in such agreement, or later agreed to, such agreement shall be final and conclusive, and, except upon a showing of fraud or malfeasance, or misrepresentation of a material fact—

(1) the case shall not be reopened as to the matters agreed upon or the agreement modified, by any officer, employee, or agent of the United States, and

(2) in any suit, action, or proceeding, such agreement, or any determination, assessment, collection, payment, abatement, refund, or credit made in accordance therewith, shall not be annulled, modified, set aside, or disregarded.

The agreement referred to in section 606 is in effect a contract entered into by the taxpayer and the Commissioner of Internal Revenue which is complete and binding on both when it is approved by the Secretary or the Undersecretary. The taxpayer did not in his claim for refund withdraw his offer to enter into a closing agreement, nor did he by letter or otherwise expressly withdraw his offer.

A claim for refund is a demand of money from the United States. (*Hobbs v. McLean*, 117 U. S., 567.) It is a formal document which has the effect of tolling the statute of limitations against refund and is recognized as such in the Revenue Act of 1928 and prior Revenue Acts. Its filing can not, however, even inferentially be considered as a withdrawal of an offer to enter into a closing agreement submitted for the signature of the Commissioner and the approval of the Secretary. Filing a claim for refund is an act not necessarily inconsistent with a pending offer to enter into a closing agreement. It is therefore the opinion of this office that the taxpayer, having submitted an offer to enter into a closing agreement which was accepted and approved within a reasonable time, can not now successfully contend that the filing of a claim for refund effected a withdrawal of the offer before its acceptance. In view of the provisions of section 606 of the Revenue Act of 1928, the determination of the taxpayer's liability for the year 1927 as set forth in the agreement must be considered final.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

SECTION 607.—EFFECT OF EXPIRATION OF PERIOD OF LIMITATION AGAINST UNITED STATES.

SECTION 607.

VIII-40-4376
G. C. M. 6898

REVENUE ACT OF 1928.

The 1917 return of the taxpayer was filed on April 11, 1918, the 5-year period provided by section 250(d) of Revenue Act of 1921 expiring on April 11, 1923. In November, 1922, the taxpayer filed a waiver for 1917, which by its terms waived "for a period of two years ending March 31, 1925, any and all statutory limitations as to the time within which assessments based upon such liability may be entered." The tax was assessed in December, 1923, and collected in January, 1924.

Held, collection of the deficiency tax within the extended period was authorized by the consent in writing and there has been no overpayment within the meaning of section 607 of the Revenue Act of 1928.

An opinion is requested as to whether there has been an overpayment of tax within the meaning of section 607 of the Revenue Act of 1928 under the following circumstances:

The 1917 return of the M Company (Forms 1031 and 1103) was filed on April 11, 1918, the 5-year period as provided by section 250(d) of the Revenue Act of 1921 expiring on April 11, 1923. On November 10, 1922, the taxpayer filed a waiver for the year 1917, which by its terms waived "for a period of two years ending March 31, 1925, any and all statutory limitations as to the time within which

assessments based upon such liability may be entered." On January 31, 1923, the taxpayer filed a waiver embodying the same terms as were embodied in the waiver filed on November 10, 1922. The tax was assessed in December, 1923, and collected in January, 1924.

It will be noted that the tax in question was assessed after the *assessment* waivers were filed and was collected in January, 1924, which was within the statutory period of limitation as extended by those waivers.

The question involved is whether the collection of the deficiency tax within the statutory period of limitation as extended by the assessment waivers filed while the Revenue Act of 1921 was in force was authorized by such waivers.

The waivers in this case were filed, and both the assessment and collection of the deficiency tax were made, while the Revenue Act of 1921 was in force. Section 250(d) of the Revenue Act of 1921 provides that taxes for the year 1917 "shall be determined and assessed within five years after the return was filed, unless both the Commissioner and the taxpayer *consent in writing to a later determination, assessment, and collection of the tax * * *.*" [Italics added.]

A consent filed pursuant to this provision of the law would, under a reasonable construction, necessarily carry with it the right to collect, within the consent period, deficiency taxes assessed within such period. The presumption would be that the parties to the consent were aware of the provisions of the statute authorizing the consent, and that if deficiency taxes were determined and assessed within the time as extended by the consent in writing, the natural and logical result, namely, collection, provided for and an integral part of the law relating thereto, was also authorized by the consent. Any other construction would render such a consent a nullity, for an assessment of deficiency tax without the right to collect is certainly a useless act.

The point seems to be well settled that in the construction of written instruments the courts will adopt that construction which will give to them effect rather than the construction which will invalidate them, and in this case this office is of the opinion that the construction should be adopted which gives effect to the waiver in question by holding that collection of the deficiency tax within the extended period was authorized by the consent in writing.

The conclusion of this office is that there has been no overpayment of the deficiency tax in this case within the meaning of section 607 of the Revenue Act of 1928.

C. M. CHAREST,

General Counsel, Bureau of Internal Revenue.

SECTION 608.—EFFECT OF EXPIRATION OF PERIOD OF LIMITATION AGAINST TAXPAYER.

SECTION 608.

VIII-34-4317

I. T. 2489

REVENUE ACT OF 1928.

Section 608(b)2 of the Revenue Act of 1928 applies to claims rejected after the enactment of the Revenue Act of 1928 only. Inas-

much as the statutory period of limitation for commencing suit in any such case will not expire before May 29, 1930, two years after the enactment of the Revenue Act of 1928, agreements to suspend the running of the statute of limitations will not be entered into by the Bureau at this time, regardless of what section of the law is involved. Applications on Form 907 should not be submitted to the Bureau until approximately six months before the expiration of the statutory period of limitation for commencing suit.

SECTION 611.—COLLECTIONS STAYED BY CLAIM IN ABATEMENT.

SECTION 611.

VIII-35-4326

G. C. M. 6296

REVENUE ACT OF 1928.

Section 611 of the Revenue Act of 1928 is not applicable to the case where a claim for credit of an overpayment has operated to stay the collection of an outstanding assessment.

An opinion is requested as to whether a portion of an overpayment of tax made by the taxpayer, the M Company, for the year 1918 which was applied against an outstanding additional tax for 1917 should be refunded to the taxpayer in accordance with the provisions of section 607 of the Revenue Act of 1928.

On August 8, 1923, within the statutory period of limitation as extended by a waiver executed by the taxpayer with respect to the collection of 1917 taxes, the taxpayer filed a claim for credit, requesting that an overpayment of tax for the year 1918 be applied against the additional tax due by the taxpayer for the year 1917. It is stated by the Income Tax Unit that under the procedure in effect at that time the filing of a claim for credit operated to stay the collection of the outstanding tax against which the alleged credit was requested to be applied in the same manner that a claim for abatement operated to stay collection. The opinion of this office is requested as to whether the taxpayer's claim for refund may be rejected, under the provisions of section 611 of the Revenue Act of 1928, by reason of the filing of the claim for credit by the taxpayer under the circumstances set forth above.

Section 611 of the Revenue Act of 1928 provides as follows:

SEC. 611. COLLECTIONS STAYED BY CLAIM IN ABATEMENT.

In any internal-revenue tax (or any interest, penalty, additional amount, or addition to such tax) was, within the period of limitation properly applicable thereto, assessed prior to June 2, 1924, and if a claim in abatement was filed, with or without bond, and if the collection of any part thereof was stayed, then the payment of such part (made before or within one year after the enactment of this Act) shall not be considered as an overpayment under the provisions of section 607, relating to payments made after the expiration of the period of limitation on assessment and collection.

In many cases in which taxes were duly assessed prior to the enactment of the Revenue Act of 1924 claims in abatement were filed by taxpayers in which it was alleged that the outstanding taxes sought to be abated had been erroneously and illegally assessed, and collection of these taxes was frequently delayed, in order that these abate-

ment claims might be considered, until after the running of the statute of limitations. Section 611 of the Revenue Act of 1928, being an exception to the general rule set out in section 607 with respect to payments made after the expiration of the period of limitation against the United States, was intended to cover those cases in which collection of taxes was stayed by reason of the filing of such claims in abatement. It may be conceded that at one time the filing of claims for credit by taxpayers likewise had the effect of staying the collection of outstanding taxes. It is to be noted, however, that it is expressly provided in section 611 that before a tax paid after the running of the statute of limitations may be considered not to constitute an overpayment which must be refunded, it must appear that a claim in abatement was filed and that collection of the tax was stayed. No mention is made in section 611 of the filing of a claim for credit by the taxpayer. A claim for credit is not a claim that the taxpayer owes no tax. In requesting that an overpayment for another period be applied against a certain outstanding tax the taxpayer in effect admits the correctness of the outstanding assessment. Consequently, section 611 of the Revenue Act of 1928 is not applicable to the case where a claim for credit of an overpayment has operated to stay the collection of an outstanding assessment.

It not appearing that any claim in abatement was filed by the taxpayer in this case, this office is of the opinion that section 611 of the Revenue Act of 1928 may not be relied upon as a basis for rejecting the taxpayer's claim for refund.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

SECTION 611.

VIII-37-4354
Ct. D. 106

FEDERAL TAXES—REVENUE ACT OF 1928—DECISION OF COURT.

SUIT—COLLECTION—LIMITATION—CLAIM FOR ABATEMENT—CONSTITUTIONALITY.

Section 611 of the Revenue Act of 1928 withdraws the statute of limitation upon collection as a ground for the recovery back of a tax paid under the conditions therein stated even though suit was commenced before that Act was passed. As so construed the section is constitutional.

DISTRICT COURT OF THE UNITED STATES FOR THE WESTERN DISTRICT OF KENTUCKY,
AT LOUISVILLE.

Wright & Taylor, Inc., plaintiff, v. Robert H. Lucas, Collector of Internal Revenue for the Collection District of Kentucky, defendant.

[July 26, 1929.]

OPINION.

DAWSON, Judge: This is a suit to recover income and profits taxes for the fiscal year ended June 30, 1918, collected by duress from the plaintiff after the period of limitation for collection had expired. The facts are stipulated and the case has been submitted to the court for determination without the intervention of a jury. Briefly stated, the facts are these:

The plaintiff, a corporation, made its income tax returns on a fiscal-year basis, its fiscal year ending on June 30. In August, 1918, it made its income and

profits tax return for the fiscal year ended June 30, 1918, and the amount shown to be due by that return, after the allowance by the Commissioner of certain abatements and after the crediting of certain overpayments on previous years, was paid and is not here in controversy.

Pursuant to the provisions of the Revenue Act of 1918, approved February 24, 1919, the plaintiff, on March 15, 1919, filed a tentative supplemental return for the fiscal year ended June 30, 1918, and on June 17, 1919, filed a complete supplemental return for the fiscal year ended June 30, 1918, showing an additional tax of \$85,186.71 due for said fiscal year, and this amount was assessed by the Commissioner of Internal Revenue on September 12, 1919. On the August, 1919, assessment list the Commissioner of Internal Revenue assessed a further tax of \$26,376.29 against the plaintiff for the same fiscal year. At the time the two supplemental returns were made the plaintiff paid in the aggregate, on account of additional tax shown to be due thereon, the sum of \$49,344.88. On September 15, 1919, abatement claims in the respective amounts of \$53,824.85 and \$26,276.29 were filed. On December 13, 1923, plaintiff signed and delivered to the Commissioner of Internal Revenue a waiver, consenting to an extension of time for the assessment and collection of any additional income and profits taxes which might be due for the fiscal year ended June 30, 1918, for a period of one year from the date said waiver was signed.

No further steps were taken for the collection of the unpaid balance due on the assessment of September 12, 1919, or for the collection of the August, 1919, assessment until September 8, 1925, when the defendant collected from the plaintiff, under threat of distraint, the sum of \$84,809.47. This sum represented the balance due on the two assessments of September 12, 1919, and August, 1919, and interest. No suit or proceeding of any character had been begun prior to September 8, 1925, for the collection of said tax and interest, or any part thereof.

On September 30, 1925, plaintiff filed a claim for the refund of said sum of \$84,809.47, and the Commissioner of Internal Revenue having failed to act on this claim within six months from the date of its filing, this suit was filed on April 14, 1927.

From the foregoing statement it is apparent that under the applicable limitation statutes, and giving full effect to the year's extension granted by the waiver signed December 13, 1923, the collection of this \$84,809.47 became barred on December 13, 1924, and that on September 8, 1925, when same was collected, the defendant was without authority to enforce collection, either by distraint or suit. (*Bowers v. New York & Albany Lighterage Co.*, 273 U. S., 346 [T. D. 4009, C. B. IV-1, 268]; *Russell v. United States*, 278 U. S., 181 [T. D. 4260, C. B. VIII-1, 206].) This is admitted by the defendant, and, unless section 611 of the Revenue Act of 1928 applies to the situation here, the plaintiff is entitled to recover. Section 611 of that Act is as follows:

"If any internal revenue tax (or any interest, penalty, additional amount, or addition to such tax) was, within the period of limitation properly applicable thereto, assessed prior to June 2, 1924, and if a claim in abatement was filed, with or without bond, and if the collection of any part thereof was stayed, then the payment of such part (made before or within one year after the enactment of this Act) shall not be considered as an overpayment under the provisions of section 607, relating to payments made after the expiration of the period of limitation on assessment and collection."

Section 607 of the Act of 1928 provides:

"Any tax (or any interest, penalty, additional amount, or addition to such tax) assessed or paid (whether before or after the enactment of this Act) after the expiration of the period of limitation properly applicable thereto, shall be considered an overpayment and shall be credited or refunded to the taxpayer if claim therefor is filed within the period of limitation for filing such claim."

It is admitted in this case that the assessment was made prior to June 2, 1924, that a claim in abatement was filed, and that pending decision on the claim in abatement the collector made no attempt whatever to collect the tax assessed. The plaintiff contends, however, that the mere voluntary postponement by the collector of the collection of the tax assessed, pending decision on the claim in abatement, is not a stay of collection within the meaning of section 611. It is insisted that the stay contemplated in that section is a compulsory stay, such as was provided by section 279 of the Revenue Act of 1924, which provided that a claim in abatement "shall be accompanied by a

bond, in such amount, not exceeding double the amount of the claim, and with such sureties, as the collector deems necessary, conditioned upon the payment of so much of the amount of the claim as is not abated, together with interest thereon as provided in subdivision (c) of this section. Upon the filing of such claim and bond, the collection of so much of the amount assessed as is covered by such claim and bond shall be stayed pending the final disposition of the claim."

Section 611, by its express terms, deals with taxes assessed under Revenue Acts in force prior to the effective date of the Revenue Act of 1924. Therefore, it seems to me that a review of the history of the use of claims in abatement under the Acts of 1916, 1917, 1918, and 1921, and the provisions of those Acts in relation to such claims, and the regulations of the Treasury Department under which those Acts were administered, will be helpful in arriving at the true meaning of section 611.

The Acts of 1916, 1917, and 1921 contain no provision whatever for the filing of claims in abatement, or for staying collection of the tax pending decision on claims in abatement, and the only provision with reference to claims in abatement contained in the 1918 Act is paragraph 14 of section 234, which authorized a taxpayer, at the time of filing his return for the taxable year 1918, to file a claim in abatement, based on the fact that he had sustained a substantial loss arising from shrinkage in inventory value, etc., during such taxable year. This section further provides:

" * * * In such case payment of the amount of the tax covered by such claim shall not be required until the claim is decided, but the taxpayer shall accompany his claim with a bond in double the amount of the tax covered by the claim, with sureties satisfactory to the Commissioner, conditioned for the payment of any part of such tax found to be due, with interest. * * *"

Thus it will be observed that when the Act of 1928 was enacted the only statutory provision in any of the Revenue Acts affected by the provisions of section 611 was the one contained in the Act of 1918, which specifically provided for the execution of a bond as a condition precedent for staying collection pending decision on a claim in abatement. It is apparent, however, that section 611 is not restricted in its operation to the special claim in abatement and the stay of collection thereunder provided for in the Act of 1918, because section 611, by its express terms, operates in those cases where the stay was granted without bond as well as in those cases where it was granted with bond. While neither the Acts of 1916, 1917, 1921, nor the Act of 1918 except as hereinbefore pointed out, made any provision for the filing of claims in abatement, yet section 3220 of the Revised Statutes, as amended and reenacted by those Acts, gave to the Commissioner ample authority to abate taxes illegally or erroneously assessed. Each of those Acts gave to the Commissioner of Internal Revenue the authority, with the approval of the Secretary of the Treasury, to make rules and regulations for the enforcement of its provisions, and it is well settled that these rules and regulations, if not in conflict with the law, have the force and effect of law. By virtue of this authority, Regulations 33 were promulgated for the administration of the Revenue Acts of 1916 and 1917, Regulations 45 for the administration of the Revenue Act of 1918, and Regulations 62 for the Act of 1921. Each of these regulations made specific provision for the filing of claims in abatement. In none of these regulations, however, was any provision made for the execution of bond, nor was there any mandatory provision that collection must be or must not be stayed pending decision on a claim in abatement. Each of these regulations, however, contain a provision similar to that found in article 1032 of Regulations 45, which declares:

" * * * The filing of a claim in abatement does not necessarily operate as a suspension of the collection of the tax or make it any less the duty of the collector to exercise due diligence to prevent the collection of the tax being jeopardized. He should, if he considers it necessary, collect the tax and leave the taxpayer to his remedy by a claim for refund. * * *"

See article 261, Regulations 33; article 1032, Regulations 45; article 1032, Regulations 62.

It is thus clear that, inferentially, the regulations authorized the collectors to postpone the collection of the tax pending decision on the claim in abatement, unless such postponement, in the judgment of the collector, would jeopardize the collection of the amount finally determined to be due, and it is common knowledge that such was the usual practice. Sometimes a collector would demand a bond as a consideration for postponement of collection; sometimes,

when he had reason to doubt the solvency of a taxpayer, collection was immediately enforced; but, as a usual thing, if the collector had no doubt of the solvency of the taxpayer, collection was withheld until final action on the claim.

It thus happened that in many cases arising under the Revenue Acts of 1916, 1917, 1918, and 1921 limitation had run against collection of the tax by the time the claim in abatement had been disposed of, and in those cases where bonds had not been exacted the taxpayer was resisting collection or paying under protest, on the claim that the tax was barred by limitation. Prior to the decision of the case of *Bowers v. New York & Albany Lighterage Co.*, supra, those charged with the collection of income and profits taxes went on the assumption that the limitation provision of the respective Acts did not apply to distraints. See I. T. 1446, page 218, Internal Revenue Cumulative Bulletin I-2. This, no doubt, made the collectors generally more willing to postpone collection of an assessment pending decision on a claim in abatement than they otherwise would have been.

Following the decision of the Supreme Court in the case of *Bowers v. New York & Albany Lighterage Co.*, a great many taxpayers who had failed to get relief on their claims in abatement, and who had paid their taxes under threat of distraint after limitation had run, were seeking to secure refunds, on the ground that the collection had been forced from them illegally. This situation was at its height when Congress came to consider the enactment of the Revenue Act of 1928, and it was to prevent taxpayers taking advantage of the delay occasioned by their having filed claims in abatement that section 611 was enacted. The purpose of section 611 is very clearly portrayed in the explanation of that section contained in the report of the Ways and Means Committee made when that committee reported the bill to the House of Representatives. This report stated:

"Prior to the enactment of the Revenue Act of 1924 it was the administrative practice to assess immediately additional taxes determined to be due. Upon the assessment, taxpayers were frequently permitted to file claims in abatement with the collector and thus delay the collection until the claim in abatement could be acted upon. If this practice had not been followed, undue hardship undoubtedly would have been imposed upon the taxpayer. It was supposed that there was no limitation upon the collection by distraint of the amount ultimately determined to be due. However, the Supreme Court has recently held in a case in which the period for assessment expired prior to the enactment of the 1924 Act that the period for collection was limited to five years from the date on which the return was filed. Decisions upon claims in abatement are being made every day. Amounts have been paid, are being paid, by the taxpayer, even though the statute of limitations may have run. Exceptionally large amounts are involved. Accordingly, it is of utmost importance to provide that the payments already made should not be refunded. In order to prevent inequality, it is also provided that the amounts not yet paid may be collected within a year after the enactment of the new Act.

"Your committee appreciates the fact that this provision will probably be subjected to severe criticism by some of the taxpayers affected. However, it must be borne in mind that the provision authorizes the retention and collection only of amounts properly due, and merely withdraws the defense of the statute of limitations. If it is determined that the amount paid is in excess of the proper tax liability, computed without regard to the statute of limitations, such excess will constitute an overpayment which may be refunded or credited as in the case of any other overpayment." (Report No. 2, Seventieth Congress, first session, page 34.)

Considering the language of section 611 in connection with the provision of the Revenue Acts under which the assessments affected by that section were made, the regulation and practice of the Treasury Department with reference to claims in abatement under those Acts, and the purpose sought to be accomplished, as shown by the committee report, supra, there can not be any doubt that it was the purpose of Congress through this section to prohibit refunds being made from the Treasury in cases similar to the one at bar. There is no merit in the plaintiff's suggestion that section 611 is only an inhibition against the Commissioner of Internal Revenue making refunds in such cases, but that it has no application in a suit against a collector such as the one here. Such a construction of this section would lead to an unconscionable result. When he collected the tax, the collector was required by law to immediately pay same into the Treasury. He had no right to retain the money pending the outcome of

threatened litigation over the collection. The Government has had the benefit of the collection. Yet, if the plaintiff's theory is correct, Congress intentionally left collectors open to suit and judgment in such cases as the one at bar, but denied them the right of reimbursement for any judgments thus obtained. It seems to me that the mere suggestion of the result of such construction forces us to reject it.

I must therefore conclude that section 611 was intended by Congress to take away from those taxpayers who had filed claims in abatement of assessments made prior to June 2, 1924, and who had, as the result of filing such claims, secured a postponement of payment pending decision on the claims, and who had been forced after the running of limitation to pay the tax thus assessed, the right to rely upon the fact that collection had been forced after the running of limitation as a basis for recovering a refund, whether the suit for such recovery is against the collector who made same or directly against the United States. Having reached this conclusion, it remains to be determined if the statute so construed deprives plaintiff of its property rights, in violation of the fifth amendment to the Federal Constitution, as contended by the plaintiff.

It is well settled that no one has a vested right to rely upon a statute of limitation to defeat a debt or other personal obligation. The legislature which gave the right may take it away, even after the bar has become complete. (*Campbell v. Holt*, 115 U. S., 620.) If this suit were turned around and were one by the United States against the plaintiff, to collect the tax involved here, the plaintiff certainly could not be heard to plead a statute of limitation formerly in force but which had been repealed before the bringing of the suit, even though the bar under the former statute was complete prior to its repeal and prior to filing the suit. If a taxpayer has no vested interest in the defense of the statute of limitation, it is difficult to understand how he can have any vested interest in the right to recover taxes from the collector, on the sole ground that payment was coerced after limitation had run. It seems to me that if his right to rely upon the statute as a defense may be destroyed by repeal or modification, his right to rely upon the statute as a basis for recovery may likewise be destroyed by repeal or modification. There can be no doubt that Congress had full power, immediately before the taxes were collected in this case, to have passed a law denying to taxpayers situated as the plaintiff was the right to rely upon the statute of limitation, although the statute had run at the time of the passage of such law. Neither can there be any doubt of the soundness of the proposition that the collector, in collecting taxes, acts as an agent of the United States. Furthermore, it is well settled that where an agent, without precedent authority, has exercised, in the name of a principal, a power which the principal had the capacity to bestow, the principal may ratify and affirm the unauthorized act and thus retroactively give it validity, when rights of third persons have not intervened. (*United States v. Heinszen & Co.*, 206 U. S., 370; *Rafferty v. Smith-Bell Co.*, 257 U. S., 226.)

In this case we have the defendant, as collector, acting as the agent of the United States. At a time when he was not authorized so to do, but at a time when the Congress of the United States had full authority to authorize him so to do, he collected, after limitation had run, the taxes involved in this case, and Congress had the power then and has had that power at all times since then to ratify the unauthorized collection, and that is what it did do, in effect, by the enactment of section 611. It is true, when the plaintiff paid the taxes under duress, after the running of limitation, a right accrued to it to recover the taxes so paid, but that right was necessarily limited by the superior right of Congress to ratify the unauthorized collection.

As pointed out in the case of *United States v. Heinszen*, supra:

"To hold to the contrary would be to say that whilst the unauthorized act of an officer done on behalf of the United States was subject to ratification by the United States, yet if the officer acted without authority, the act when performed annihilated the power to ratify; that is, that the very condition which engendered the power destroyed it."

The fact that plaintiff had brought suit on its claim prior to the enactment of section 611 did not change the nature of plaintiff's right nor impair the paramount right of Congress to ratify.

In discussing how far the bringing of actions would operate to deprive the Government of the power to enact ratifying statutes which, if the action had

not been brought, would have been valid, Cooley in his *Constitutional Limitations* (7th Ed., p. 543) says:

"Nor is it important in any of the cases to which we have referred that the legislative act which cures the irregularity, defect or want of original authority was passed after suit brought, in which such irregularity or defect became matter of importance. The bringing of suit vests in a party no right to a particular decision."

This quotation was cited with approval in the *Heinszen* case, *supra*.

For the reasons stated, I am convinced that section 611 controls the case at bar, and therefore plaintiff's petition will be dismissed and costs awarded to the defendant. A judgment conforming to the views herein expressed may be prepared by counsel and presented for entry.

SECTION 611.

VIII-37-4358
Ct. D. 110

FEDERAL TAXES—REVENUE ACT OF 1928—DECISION OF COURT.

SUIT—COLLECTION—LIMITATION—CLAIM FOR ABATEMENT—CONSTITUTIONALITY.

Section 611 of the Revenue Act of 1928 withdraws the statute of limitation upon collection as a ground for the recovery back of a tax paid under the conditions therein stated and as so construed the section is constitutional.

UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT.

Clyde G. Huntley, Collector of Internal Revenue of the United States for the District of Oregon, appellant, v. H. S. Gile and W. T. Jenks, Copartners, Doing Business Under the Firm Name and Style of H. S. Gile & Co., appellees.

Upon appeal from the District Court of the United States for the District of Oregon.

[May 27, 1929.]

OPINION.

DIETRICH, Circuit Judge: The appellees, plaintiffs below, brought this suit to recover \$18,696.97 which they allege the appellant, collector, illegally compelled them to pay on account of income and excess-profits tax for the fiscal year ending August 31, 1917. Their return was filed March 30, 1918, and the additional tax here in question was assessed in December, 1922. On March 23, 1923, they filed with the defendant a claim for the abatement of the assessment, which was disallowed by the Commissioner of Internal Revenue on May 23, 1924, and on September 11, 1924, they paid the assessment under compulsion of a warrant of distraint issued September 6, 1924. On January 30, 1925, they filed their claim for a refund of the amount so paid, which was disallowed on May 19 of the same year, and on March 17, 1926, they commenced this action. They set up (1) that in point of fact and law there was no basis for the assessment, and (2) that when the distraint proceedings were instituted the statute of limitations had run. Without considering the first contention the court below sustained the second and accordingly gave them judgment as prayed.

Appellant concedes that under the rule of *Bowers v. New York & A. L. Co.* (273 U. S., 346 [T. D. 4009, C. B. VI-1, 268]), the 5-year period of limitation prescribed by section 250(d) of the Act of 1921 constituted a bar at the time the collection was made, and further, that the bar being complete at the time the 1924 Act was passed (June 2, 1924), the collection was not authorized under section 278(e) of that Act. In short, it is conceded that as the statutes stood at the time of the collection the distraint proceedings were unlawful, and plaintiffs would be entitled to recover but for the provisions of sections 607 and 611 of the Revenue Act of 1928, which appellant contends operated to disable plaintiffs to recover unless they show that upon the merits the assessment was invalid. By this section 607 it is declared that any tax assessed or paid after the expiration of the period of limitation properly applicable thereto "shall be considered an overpayment and shall be credited or refunded to the taxpayer if claim therefor" is seasonably filed; and section 611 is as follows:

"If any internal-revenue tax (or any interest, penalty, additional amount, or addition to such tax) was, within the period of limitations properly applicable thereto, assessed prior to June 2, 1924, and if a claim in abatement was filed, with or without bond, and if the collection of any part thereof was stayed, then the payment of such part (made before or within one year after the enactment of this Act) shall not be considered as an overpayment under the provisions of section 607, relating to payments made after the expiration of the period of limitation on assessment and collection."

By appellees it is conceded that the payment here in question falls within all the descriptive requirements of this latter section save possibly the qualifying condition, "if the collection of any part thereof was stayed"; but upon that point it is to be noted that in the course of the trial the following colloquy took place in open court between Mr. Littlefield, attorney for appellant, and Mr. McCulloch, attorney for appellees:

"Mr. LITTLEFIELD. I think it is admitted, isn't it, Mr. McCulloch, that in that stipulation that you filed a claim of abatement?"

"Mr. MCCULLOCH. Yes, your honor, if there is any virtue in the section of the 1928 Act with respect to filing a claim of abatement, the stipulation admits that we did file a claim in abatement and that collection was stayed."

It is true that appellees did thus in terms admit that the stay was effected by or ensued because of the pendency of the claim in abatement, but we are unable to escape the view that both sides intended to be understood as agreeing that the facts were such as to bring the case within the statutory condition and that because of such understanding counsel for appellant refrained from offering evidence upon the point.

While textually section 611 is open to construction, upon the whole we are left in no doubt that by it Congress intended to withhold from the taxpayer the right to have refunded money paid by him in the discharge of a valid tax, under the conditions therein stated, where the only objection which could be made to its collection was the expiration of the applicable period of limitation. Otherwise the section is without apparent meaning. To appellees' contention that effect may be given to it by holding that it was intended to apply only to cases of voluntary payment, the answer is that not only does the language fail to intimate such a limitation but, to the contrary, the entire section relates to assessments which the taxpayers by claims for abatement sought to escape and which therefore presumably they unwillingly paid. And in reporting the bill which afterwards became the Revenue Act of 1928 the Ways and Means Committee made a statement explanatory of the conditions the proposed section 611 was designed to meet which puts beyond all possibility of doubt the committee's conception of its purpose and intent. It was said:

"Prior to the enactment of the Revenue Act of 1924 it was the administrative practice to assess immediately additional taxes determined to be due. Upon the assessment, taxpayers were frequently permitted to file claims in abatement with the collector and thus delay the collection until the claim in abatement could be acted upon. If this practice had not been followed, undue hardship undoubtedly would have been imposed upon the taxpayer. It was supposed that there was no limitation upon the collection by distraint of the amount ultimately determined to be due. However, the Supreme Court has recently held in a case in which the period for assessment expired prior to the enactment of the 1924 Act that the period for collection was limited to five years from the date on which the return was filed. Decisions upon claims in abatement are being made every day. Amounts have been paid, are being paid, by the taxpayer, even though the statute of limitations may have run. Exceptionally large amounts are involved. Accordingly, it is of utmost importance to provide that the payments already made should not be refunded. In order to prevent inequality, it is also provided that the amounts not yet paid may be collected within a year after the enactment of the new Act.

"Your committee appreciates the fact that this provision will probably be subjected to severe criticism by some of the taxpayers affected. However, it must be borne in mind that the provision authorizes the retention and collection only of amounts properly due, and merely withdraws the defense of the statute of limitations. If it is determined that the amount paid is in excess of the proper tax liability, computed without regard to the statute of limitations, such excess will constitute an overpayment which may be refunded or credited as in the case of any other overpayment." (Report No. 2, Seventieth Congress, first session, page 34.)

Under a fair construction we are of the opinion that the section as enacted into law expresses this intent and accordingly that under the admitted facts plaintiffs are entitled to a refund only in case they show that the assessment is invalid upon the merits.

The further contention made is that so construed the statute is invalid because it purports to deprive plaintiffs of a vested right. But no vested right accrues to the taxpayer out of the running of the period of limitation for the collection of a valid tax. (*Rafferty v. Smith, Bell & Co.*, 257 U. S., 226; *United States v. Heinszen & Co.*, 206 U. S., 370; *Collector v. Hubbard*, 79 U. S., 1; *Haight v. United States*, 22 Fed. (2d), 367 [T. D. 4113, C. B. VII-1, 148]; *Campbell v. Holt*, 115 U. S., 620; *Railroad Co. v. Alabama*, 101 U. S., 832; *Beers v. Arkansas*, 61 U. S., 527; *West Side Belt Co. v. Pittsburgh Construction Co.*, 219 U. S., 92; *Brushaber v. U. P. R. R. Co.*, 240 U. S., 1; *Lynch v. Hornby*, 247 U. S., 339, 343.)

Inasmuch as pursuant to stipulation the cause was tried by the court without a jury and there was no determination of the question of the validity of the assessment and no findings were made in respect thereof, the judgment will be reversed, with leave to both parties to introduce further evidence upon the question, if so advised, and with directions to the court to take further proceedings not inconsistent herewith, including the determination of such issue. Should an appeal be taken by either party from the judgment that shall be entered, it will be unnecessary for the appellant to reprint or otherwise bring up such parts of the record as are embraced in the printed transcript now on file in this court.

Reversed.

SECTION 611.

VIII-49-4450
Ct. D. 132

INTERNAL REVENUE TAXES—REVENUE ACT OF 1928—DECISION OF COURT.

SUIT—OVERPAYMENT—STAY OF COLLECTION—MEANING OF STAY.

Collection of an internal revenue tax has been stayed within the meaning of section 611 of the Revenue Act of 1928 where actual delay has resulted from the filing of a claim for abatement.

UNITED STATES CIRCUIT COURT OF APPEALS, NINTH CIRCUIT.

Rea B. Goodcell, Former Collector of Internal Revenue of the United States of America in and for the Sixth Collection District, State of California, appellant, v. R. E. Graham and E. E. Foster, Copartners, Doing Business Under the Firm Name of Millie Francis Oil Co., a Copartnership, appellees.

[November 4, 1929.]

OPINION.

WILBUR, Circuit Judge: The question involved in this case is the proper interpretation of the word "stay" used in section 611 of the Revenue Act adopted by Congress in 1928 (45 Stat., 875; 26 U. S. C. A., section 2611). The appellees brought an action to recover \$9,039.40 taxes they paid under duress to the appellant as internal revenue collector on December 3, 1924, for the year 1917, after the 5-year period of limitation had run. (26 U. S. C. A., 2607; 45 Stat., 874.) The appellees predicated their right to recover upon sections 3220 and 3226 of the Revised Statutes and section 250(d) of the Revenue Act of 1921 (42 Stat. L., 265), as construed in *Bowers v. New York & Albany Lighterage Co.* (47 Sup. Ct., 389, 273 U. S., 346 [T. D. 4009, C. B. VI-1, 268]) and *Russell et al. v. United States* (278 U. S., 181 [T. D. 4260, C. B. VIII-1, 206]). While the action was pending Congress enacted sections 607 and 611, supra, which prohibited a recovery where a claim in abatement had been filed and there had been a stay thereunder. The appellees filed a claim for abatement on February 11, 1920, which was rejected December 27, 1922. Most of the questions involved here were decided by this court in *Huntley v. Gile* (32 F. (2d), 857 [see Ct. D. 110, on page 158]), but in that case it was stipulated that there had been a "stay." Here it is contended that the voluntary act of the collector in suspending or delaying the collection after appellee

filed its claim for abatement was not a "stay" within the meaning of the statute. The view advanced is that to be a "stay" within the meaning of this statute there must have been a legal inhibition against the collection of the tax, or, as it is said, a "legal" stay.

The word "stay," in its varying forms, has numerous definitions, and is applied to somewhat widely differing acts and things, with, however, the general underlying idea of the stoppage or suspension of movement. The following definitions seem pertinent:

Stay (used as a transitive verb, with the preterite and past participle stayed) is in Webster's New International Dictionary (1913) among other things defined as—

"4. To hold from proceeding; to stop; check; restrain; also, to hinder; delay; detain; postpone; keep back; specif., to stop, or more usually suspend, the progress of by judicial proceedings or executive mandate."

Stay (used as an intransitive verb, in same dictionary):

"(From stay to hold up; from the idea of standing firm.)

"1. To rest; depend; rely; stand * * *

"2. To cease from any motion or course of action; specif.: a. To come to an end; to cease; stop; as, that day the storm stayed. *Archaic.* b. To delay; wait; tarry; linger; as, stay and hear me. * * * d. to stand still; not to retreat; to remain at a certain point or in a certain state."

In the Standard Dictionary (1913), stay, used as a verb, is defined as follows:

"1. To stop the progress of; check; hold back; prevent; not now usually of physical motion; as to stay the ravages of a pestilence or pangs of hunger. * * *

"3. To put off until a future time; postpone; hinder; suspend; as, to stay judgment."

The appellee is unable to point out any provision of law which would operate as a compulsory stay in a case where no bond is filed with the claim for abatement, and section 611, *supra*, expressly applies to a "stay" without bond. It is not claimed that any court, State or Federal, is authorized to "stay" the collection of the tax. (R. S., 3224, 26 U. S. C. A., 154.) Even if we were empowered to insert in the statute (section 2611, *supra*) the word "legal" before the word stay, which we are not authorized to do by construction or otherwise, it would apparently cover a situation that can not exist, and, therefore, be a useless addition. We see no reason why the word "stay" should not be given its usual significance, which in this case would be delay of executive action. The title of the section under consideration (section 2611) can be referred to for the purpose of determining the proper interpretation of the section. (*Church of the Holy Trinity v. U. S.*, 143 U. S., 457, 462.) The title of this section is "Collection stayed by claim in abatement." Congress evidently intended to cover cases where actual delay had resulted from the filing of a claim in abatement. The idea of a legal or compulsory or involuntary stay is neither expressed nor implied. The language of the Act is as apt to describe a voluntary delay by the collector to enable the claimant in good faith to secure a decision on his claim for abatement before the tax is collected as it is to describe an involuntary delay. The report of the committee of Congress on the bill states this definitely to be the purpose of the proposed enactment. That report is set forth in the opinion in *Huntley v. Gile*, *supra*, and need not be repeated here. Our attention has been called to the decision of the Circuit Court of Appeals of the Fifth Circuit in a similar case, *United States v. Burden, Smith & Co.* (33 F. (2d), 229). For the reason we have stated we can not follow that decision.

It is urged by the appellees that the case was not tried below upon the theory that section 2611, *supra*, was involved and that the appellant did not call the attention of the trial court to this section. It is true that the parties can not change their theory of a case on appeal, but appellant's theory in the court below was that the stipulated facts were legally insufficient to justify a recovery and that is the point presented here. The point was presented in the court below by motion for a judgment on the admitted facts. The circumstance that the district court was not called upon to construe section 2611, *supra*, does not prevent a consideration on appeal of the objections and motions made and ruled upon in the trial court.

Judgment reversed.

SECTION 611.

VIII-49-4451
Ct. D. 133

INTERNAL REVENUE TAXES—REVENUE ACT OF 1928—DECISION OF COURT.

SUIT—COLLECTION—LIMITATION—CLAIM FOR ABATEMENT—STAY OF
COLLECTION—CONSTITUTIONALITY.

Section 611 of the Revenue Act of 1928 withdraws the statute of limitations upon collection as a ground for the recovery back of an internal revenue tax, duly assessed prior to June 2, 1924, and paid within the period therein stated, where the claim for abatement filed had in fact resulted in an administrative delay in collecting the tax. As so construed the section is constitutional.

UNITED STATES DISTRICT COURT, SOUTHERN DISTRICT OF NEW YORK.

Regla Coal Co., plaintiffs, v. Frank K. Bowers, defendant.

Philip S. Authur, plaintiff, v. Frank K. Bowers, defendant.

Homer Brooke Glass Co., plaintiffs, v. Frank K. Bowers, defendant.

Daniel Reeves, Inc., plaintiff, v. Chas. W. Anderson, defendant.

Robin Conveying Belt Co., plaintiffs, v. Frank K. Bowers, defendant.

[November 13, 1929.]

OPINION.

MACK, C. J.: Motions for judgment on the pleadings in five cases. The facts as alleged in the complaint and admitted in the answer in the Regla Co. case raise the identical legal questions involved in each of the other cases.¹

In the Regla case, plaintiff, on May 1, 1918, filed its income and excess profits tax return for the fiscal year ending June 30, 1917, and was duly assessed and paid the sum of \$6,867.94 as taxes for that year. On April 18, 1923, it received a bill for an additional assessment of \$16,679.80; it appealed to the special assessment section of the Income Tax Unit at Washington, and as part of the appeal, on April 26, 1923, filed a claim for the abatement of these taxes. No further proceedings to collect the taxes were taken until May 28, 1924, when defendant collected \$7,194.44 additional taxes. Three years later, on April 27, 1927, plaintiff's application for a refund was refused (except as to a sum of \$220.40 refunded as an overassessment). As defendant took no further action within the statutory period of six months (26 U. S. C., sec. 156), plaintiff brought the present suit on January 17, 1928, to recover the balance of \$6,974.04. * * *

Plaintiff contends that: (1) The collection of May 28, 1924, was wholly illegal under the statutes then in force because made more than five years after the date of the original return; (2) they have a common-law right to recover the money thus collected; (3) recovery is not barred because of sections 607 and 611 of the Revenue Act of 1928, since that Act is inapplicable because (a) a formal stay of collection is necessary under section 611, and (b) the Act created merely a new status of overpayer and was not intended to destroy the right to recover taxes illegally collected; (4) if sections 607 and 611 of the Act of 1928 are to be construed as destroying this right, they are unconstitutional as constituting a deprivation of property without due process of law and as an improper delegation of the Federal taxing power to the collector.

¹ There are certain minor, immaterial differences: (a) In the Authur, Daniel Reeves, Inc., and Robin Conveying Co. cases, plaintiffs received letters from the Commissioner stating that an immediate assessment would be made but that the Income Tax Bureau would entertain a claim in abatement if filed within a specified time; (b) in the Authur case, a part of the claim for abatement was allowed; (c) in the Brooke Glass Co. and Daniel Reeves, Inc., cases, the Commissioner definitely refused the application for a refund instead of merely taking no action thereon within the statutory six months prior to suit. (26 U. S. C., sec. 156.)

Defendant contends that (1) as a measure of curative expediency, Congress has the constitutional power, without depriving a taxpayer of his property without due process of law, to remove the bar of a statute of limitation on tax collection, which, as an act of grace, it had previously enacted for the repose of the taxpayer; (2) the intent of Congress in passing sections 607 and 611 was to remove the bar of the existent statute of limitations as a defense or as a cause of action, and to legalize collections made more than five years after the filing of returns in all cases where consideration of claims for abatement of duly assessed taxes delayed collection until after the 5-year period of limitation on collection had expired.

(1) Under section 250(d) of the Revenue Act of 1921, it is clear that the collection of the \$16,679.80 was barred on May 1, 1923, five years after the date of the original return, and that on May 28, 1924, when this sum was actually collected from plaintiff, defendant was without authority to enforce collection either by distraint or suit. (*Bowers v. New York & Albany Lighterage Co.*, 273 U. S., 346 [T. D. 4009, C. B. VI-1, 268].) Accordingly, plaintiff is entitled to judgment unless sections 607 and 611 of the Revenue Act of 1928 may be construed as barring such collection, and, further, unless those sections, so construed, are constitutional.

(2) In my judgment, section 611 of the Act of 1928 is applicable to the cases at bar. In all of them the assessments in question were made prior to June 2, 1924; claims for abatement were filed by the taxpayer (in three of them at the invitation of the Commissioner); and pending decisions on such claims, the collector made no attempt whatever to collect the taxes within the time remaining before the statutory bar would fall. But plaintiff, in reliance on the case of *United States v. Burden, Smith & Co.* (83 F. (2d), 229 (C. C. A., 5th)), followed in *Cutcheon v. Rafferty* (E. D. N. Y., decided July 15, 1929) and *Pepsin Syrup Co. v. Schwaner* (S. D. Ill., decided July 20, 1929), contends that the words "and if the collection * * * was stayed," in section 611, require some form of compulsory stay binding upon the collector. In the *Burden, Smith & Co.* case the court decided that "stayed," in a legal sense, is not interchangeable with "delayed," and necessarily connotes "some act on the part of the taxpayer which would morally or legally tie the hands of the Commissioner and prevent collection of the tax"; and since article 1032 of Regulations 62 of the Income Tax Bureau specifically provides that the filing of a claim for abatement did not of itself operate as a suspension of collection, the court held that some kind of formal stay is necessary within section 611 of the Act of 1928.

With all due respect, I have been unable to concur in this conclusion, and, in this district, am not bound to accept it. While taxing statutes are to be interpreted liberally in favor of the taxpayer, particular Revenue Acts which complement existing statutes must be interpreted with reference to such earlier Acts and in the light of conditions resulting from their interpretation and administration. Section 611 of the Act of 1928 can not be construed to contemplate a judicial stay of collection, for it has long been settled that such an injunction will not issue (R. S., section 3224, 26 U. S. C., section 154) even against collections after the statutory period. (*Ellay Co. v. Bowers*, 25 F. (2d), 637 (C. C. A. 2d).) Plaintiff contends, however, that a compulsory stay binding on the Bureau and the collector, similar to that formerly provided in section 279 of the Revenue Act of 1924 (43 Stat., 300, see 26 U. S. C. A., section 1063, Historical Note), must have been intended. But as pointed out by Judge Dawson in *Wright & Taylor, Inc., v. Lucas* (W. D. Ky., decided July 26, 1929, [see Ct. D. 106, on page 153]), section 611, by its express terms, deals with taxes assessed prior to June 2, 1924, which was the effective date of the Revenue Act of 1924. Accordingly, it seems necessary to examine the provisions of statutes enacted prior to that date relating to claims for the abatement of taxes. The only Act making provisions for such claims is that of 1918, in which paragraph 14 of section 234 (40 Stat., 1079) authorizes a taxpayer at the time of filing his return to file a claim in abatement, provides that payment should not be required until such claim is passed upon; but the taxpayer must file a proper bond. This section was thus the only provision in any of the prior Revenue Acts which fell within the specific terms of section 611 in the Act of 1928.

The 1918 Act, however, required that a claim for abatement be accompanied by a bond. Section 611 of the Act of 1928, by its express terms, is applicable irrespective of whether or not a bond accompanied the claim. Moreover, while the Act of 1918 was the only statute prior to 1924 which made provision

for a claim and formal stay, the Commissioner of Internal Revenue has had authority to abate or refund taxes illegally assessed throughout the period under review. See 26 U. S. C. A., section 149, Historical Note. And pursuant to statutory authority, the Commissioner, with the approval of the Secretary of the Treasury, promulgated regulations which included provisions for the filing of claims in abatement. In none of them, however, was the execution of a bond required or was there a mandatory provision that collection must be stayed pending decision on the claim in abatement. On the contrary, it was provided that the filing of a claim in abatement did not necessarily operate as a suspension of the collection of the tax or make it any less the duty of the collector to exercise due diligence to prevent the collection of the tax being jeopardized by the running of the statute or otherwise. (See art. 261, Reg. 33; art. 1032, Reg. 45; art. 1032, Reg. 62; cf. *United States v. Burden, Smith & Co.*, 33 F. (2d), 229, 230.) Under these regulations, the collector had authority to postpone the collection of the tax pending the determination of the claim for abatement unless, in his judgment, such action would jeopardize the ultimate collection of the tax. Postponement was the common practice where there was no doubt as to the solvency of the taxpayer; in many cases the period of the statutory bar on collection expired before the decision on the claim in abatement had been rendered. (See H. R. Rep. No. 2, 70th Cong., 1st sess., p. 34; H. R. Doc. No. 578, 69th Cong., 2d sess., p. 3 et seq.) This was because prior to *Bowers v. New York & Albany Lighterage Co.* (273 U. S., 346) the Bureau believed that the limitation provisions did not apply to distraints and that therefore the collection was not in fact jeopardized.

Following the decision in the Albany Lighterage case, a large number of taxpayers in the situation of the present plaintiffs, who had failed to have their assessments abated and who had been forced to pay under threat of distraint, sought to secure refunds on the ground that the taxes had been illegally collected. It was to meet this situation that the present section 611 was drafted; its purpose is clearly set forth in the report of the Ways and Means Committee in presenting the bill to the House:

"Prior to the enactment of the Revenue Act of 1924 it was the administrative practice to assess immediately additional taxes determined to be due. Upon the assessment, taxpayers were frequently permitted to file claims in abatement with the collector and thus delay the collection until the claim in abatement could be acted upon. If this practice had not been followed, undue hardship undoubtedly would have been imposed upon the taxpayer. It was supposed that there was no limitation upon the collection by distraint of the amount ultimately determined to be due. However, the Supreme Court has recently held, in a case in which the period for assessment expired prior to the enactment of the 1924 Act, that the period of collection was limited to five years from the date on which the return was filed. Decisions upon claims in abatement are being made every day. Amounts have been paid, are being paid, by the taxpayer, even though the statute of limitations may have run. Exceptionally large amounts are involved. Accordingly, it is of utmost importance to provide that the payments already made should not be refunded. In order to prevent inequality, it is also provided that the amounts not yet paid may be collected within a year after the enactment of the new Act.

"Your committee appreciates the fact that this provision will probably be subjected to severe criticism by some of the taxpayers affected. However, it must be borne in mind that the provision authorizes the retention and collection only of amounts properly due, and merely withdraws the defense of the statute of limitations. If it is determined that the amount paid is in excess of the proper tax liability, computed without regard to the statute of limitations, such excess will constitute an overpayment which may be refunded or credited as in the case of any other overpayment." (H. R. Rept. No. 2, 70th Cong., 1st sess., p. 34; see also Sen. Rept. No. 960, 70th Cong., 1st sess., p. 42.)

That section 611 was intended to include more than those cases in which a formal claim in abatement and bond had been filed is further indicated in the light of the inapplicability of the time limitation to the liability on the bond. (See *United States v. The John Barth Co.*, 279 U. S., 370, 376 [Ct. D. 65, C. B. VIII-1, 189].)

In view of the prior legislation, the departmental regulations and practice thereunder, and the statements in the committee reports, I am entirely

clear that section 611 should be construed as applicable to those cases in which the filing of a claim in abatement had *in fact* resulted in an administrative delay in collecting duly assessed taxes even though no formal "stay" had been granted.

(3) I come then to a consideration of the constitutionality of section 611 as applied to the cases at bar. It is well settled that Congress has the power to ratify by subsequent legislation an unauthorized and illegal tax collection so as to give it retroactive validity. (*United States v. Heinssen & Co.*, 206 U. S., 370; *Rafferty v. Smith, Bell & Co.*, 257 U. S., 226.) But plaintiff insists that this power is conditioned both upon the power of Congress at the time of the unauthorized collection to lay the tax and upon an unequivocal manifestation of the legislative intent to ratify the unauthorized collection. It is urged that section 611 evidences no such intent, that in any event, after the statutory bar has fallen, the taxpayer has a vested right to recover the taxes, and that to deprive him of this right constitutes a taking of property without due process of law.

In my judgment, an examination of the three pertinent sections of the Act of 1928 sufficiently indicates the intent to ratify the illegal collection and to prevent the return of taxes properly assessed and, but for the limitation Act, otherwise valid and due. Section 612 repeals as of its original date of enactment section 1106(a) of the Revenue Act of 1926, which specifically provided that the running of the statute should extinguish the right as well as bar the remedy. Section 607 provides that in the ordinary case of payment after the statute has run, such payment shall be considered an overpayment and refunded or credited as such. Section 611 exempts from the operation of section 607 cases, such as those at bar, in which a claim in abatement had been filed and collection delayed. While no express mention is made of ratification, a reading of these three sections in the light of their purpose, as above stated, makes it abundantly clear that Congress intended to give to the collections already made (or to be made within a year) whatever validity it was empowered to give.

Contrary to *Clinton Iron & Steel Co. v. Heiner* (30 F. (2d), 542), relied on by plaintiff, I agree with the views expressed by Judge Dawson in *Wright & Taylor, Inc. v. Lucas*, supra, as follows: "There is no merit in the plaintiff's suggestion that section 611 is only an inhibition against the Commissioner of Internal Revenue making refunds in such cases, but that it has no application in a suit against a collector such as the one here. Such a construction of this section will lead to an unconscionable result. When he collected the tax, the collector was required by law to immediately pay same into the Treasury. He had no right to retain the money pending the outcome of threatened litigation over the collection. The Government has had the benefit of the collection. Yet, if the plaintiff's theory is correct, Congress intentionally left collectors open to suit and judgment in such cases as the one at bar * * *. It seems to me that the mere suggestion of the result of such construction forces us to reject it." To hold that the Commissioner is prohibited from making refunds but that the collector nevertheless be sued would produce an anomalous situation in view of the decisions that though in form such suit is against the collector, in substance it is an action against the United States within the Tucker Act. (*United States v. Emery*, 237 U. S., 28, 32.)

Plaintiff's final contention that inasmuch as the statute had run at the time of the collection, Congress was then and is still without the constitutional power to remove the bar, can not be sustained. It is well settled that there is no vested right to rely upon a statute of limitation to defeat a debt or other personal obligation; the legislature which imposed the bar may remove it. (*Campbell v. Holt*, 115 U. S., 620; cf. *Decker v. Pourallsmith Corp.*, N. Y. Ct. App., decided Oct. 15, 1929, reported in N. Y. L. J., Nov. 7, 1929, at p. 1.) That because of sovereign grace the expiration of the statutory period not only gave the taxpayer a defense but also a right to recover taxes paid thereafter does not, in my judgment, change the result. Nor is this a case like *Davis v. Mills* (194 U. S., 451) or *Danzer v. Gulf & S. I. R. R. Co.* (268 U. S., 633), in which the grant of a right is conditioned upon its being exercised within a prescribed period; for the right of the United States to these taxes existed prior to and independent of the grant of a limitation statute for the repose of the taxpayer. This result is identical with that reached by the Circuit Court of Appeals for the Ninth Circuit in *Huntley v. Gile* (32 F. (2d), 857 [see Ct. D. 110, on page 158]), and by Judge Dawson in *Wright & Taylor, Inc. v. Lucas*, supra, in both of which cases the constitutionality of section 611 was sustained.

No injustice to the taxpayer results from such construction. The purpose of the limitation statute was to protect the taxpayer against the assertion of stale governmental tax claims at a time when most of the evidence bearing on the correctness of the assessment would have been lost. This purpose is certainly satisfied where, as here, the evidence relating to the assessment has been preserved in the claim for abatement.

(4) The objection that section 611 is unconstitutional because it leaves to the collector the arbitrary power to determine whether or not to collect the tax and thereby prevent the taxpayer from recovering it can not be sustained. The section specifically covers payments (which includes collections) made within one year after its enactment. As held in *Ellay v. Bowers*, supra, such collection can not be enjoined, and by virtue of section 611, once the money has been collected, it may not be recovered solely because it was collected after the statutory period. That some taxpayers may escape because the collector does not act within the one-year period is beside the point; it must be assumed that the executive department of the Government will act with due diligence.

Since the hearing on these motions for judgment on the pleadings, the precise question involved has been passed upon in this court in *Laura H. Jennings v. Anderson*, decided October 11, 1929. In that case Judge Grubb directed a verdict in favor of the plaintiff taxpayer but filed no opinion. While ordinarily the rule of comity would require me to follow Judge Grubb's decision, in view of the fact that he rendered no opinion in the case and that he may perhaps have felt to some extent bound by the views of the circuit court of appeals of his home circuit (*United States v. Burden, Smith & Co.*, supra), and in consideration, too, of the importance of the question presented, I have deemed it my duty, sitting in this court, briefly to state my own views and conclusions.

Since the foregoing opinion was dictated, the opinion of the Ninth Circuit Court of Appeals, in *Goodcell v. Millie Francis Oil Co.*, filed November 4, 1929, and published in the *United States Daily* November 13, 1929, at page 2324 [see Ct. D. 132, on page 160], has come to my attention. The foregoing opinion is entirely in accord with that opinion in the interpretation of the word "stay" and in declining to follow *United States v. Burden, Smith & Co.*, supra.

SECTION 613.—LIEN FOR TAXES.

SECTION 613.

VIII-28-4268

I. T. 2478

REVENUE ACT OF 1928.

Paragraph 855 of the Revised Statutes of Arizona, 1928, is accepted by the Bureau of Internal Revenue as coming within the purview of subsection (b)1 of section 3186, Revised Statutes, as amended, as further amended by section 613 of the Revenue Act of 1928, relative to the filing of notices of Federal tax liens with local or State officials.

I. T. 2180 (C. B. IV-2, 93) amended.

SECTION 613.

VIII-46-4427

I. T. 2507

REVENUE ACT OF 1928.

The act of May 1, 1929, passed by the Legislature of Pennsylvania, effective from the date of its enactment, is accepted by the Bureau of Internal Revenue as coming within the purview of subsection (b)

(1) of section 3186, Revised Statutes, as amended, as further amended by section 613 of the Revenue Act of 1928, relative to the filing of notices of Federal tax liens with local or State officials.

SECTION 613.

VIII-47-4435
T. D. 4275

REGULATIONS GOVERNING THE RELEASE OF FEDERAL TAX LIENS.

Section 3186 of the Revised Statutes further amended by section 613 of the Revenue Act of 1928.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, D. C.

To Collectors of Internal Revenue and Others Concerned:

Section 3186 of the Revised Statutes, as amended, is further amended by section 613 (entitled "Lien for taxes") of the Revenue Act of 1928 to read as follows:

SEC. 3186. (a) If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, penalty, additional amount, or addition to such tax, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person. Unless another date is specifically fixed by law, the lien shall arise at the time the assessment list was received by the collector and shall continue until the liability for such amount is satisfied or becomes unenforceable by reason of lapse of time.

(b) Such lien shall not be valid as against any mortgagee, purchaser, or judgment creditor until notice thereof has been filed by the collector—

(1) In accordance with the law of the State or Territory in which the property subject to the lien is situated, whenever the State or Territory has by law provided for the filing of such notice; or

(2) In the office of the clerk of the United States district court for the judicial district in which the property subject to the lien is situated, whenever the State or Territory has not by law provided for the filing of such notice; or

(3) In the office of the clerk of the Supreme Court of the District of Columbia, if the property subject to the lien is situated in the District of Columbia.

(c) Subject to such regulations as the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, may prescribe, the collector of internal revenue charged with an assessment in respect of any tax—

(1) May issue a certificate of release of the lien if the collector finds that the liability for the amount assessed, together with all interest in respect thereof, has been satisfied or has become unenforceable;

(2) May issue a certificate of release of the lien if there is furnished to the collector and accepted by him a bond that is conditioned upon the payment of the amount assessed, together with all interest in respect thereof, within the time prescribed by law (including any extension of such time), and that is in accordance with such requirements relating to terms, conditions, and form of the bond and sureties thereon, as may be specified in the regulations;

(3) May issue a certificate of partial discharge of any part of the property subject to the lien if the collector finds that the fair market value of that part of such property remaining subject to the lien is at least double the amount of the liability remaining unsatisfied in respect of such tax and the amount of all prior liens upon such property.

(d) A certificate of release or of partial discharge issued under this section shall be held conclusive that the lien upon the property covered by the certificate is extinguished.

(e) The Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, may by regulation provide for the acceptance of a single bond complying both with the requirements of section 272(j) of the Revenue Act of 1928 (relating to the extension of time for the payment of a deficiency), or of any similar provisions of any prior law, and the requirements of subsection (c) of this section.

(f) Subsections (c), (d), and (e) of this section shall apply to a lien in respect of any internal-revenue tax, whether or not the lien is imposed by this section.

In accordance with the provisions of subsections (c) and (e), supra, the following regulations are hereby prescribed:

The collector of internal revenue to whom is charged an assessment in respect of any internal-revenue tax shall issue a certificate of release of the tax lien whenever he finds that the liability for the amount assessed (together with all interest in respect thereof) has been satisfied or has become unenforceable. The word "unenforceable" as here used means unenforceable as a matter of law, and not merely uncollectible or unenforceable as a matter of fact. Tax liabilities frequently are unenforceable in fact for the time being, due to the temporary nonpossession by the taxpayer of discoverable property or property rights. In all cases the liability for the payment of the tax continues until satisfaction of the tax in full or until the expiration of the statutory period for collection, including such period as the taxpayer by consent in writing may agree with the Commissioner shall constitute the time within which the tax assessed may lawfully be collected. Collectors should continue to investigate carefully all cases of delinquent taxpayers where notice of lien has been filed, with a view of obtaining, before the expiration of the collection period, such written consent for the extension of the collection period, whenever it is reasonably possible that the taxpayer may, in the future, acquire property or property rights from which the tax liability may be satisfied.

The collector may in his discretion issue a certificate of release of the tax lien if he is furnished and accepts a bond that is conditioned upon the payment of the amount assessed (together with all interest in respect thereof) within the time agreed upon in the bond, but not later than six months prior to the expiration of the statutory period for collection, including any period for collection agreed upon in writing by the Commissioner and the taxpayer. The form of any bond so furnished shall be the standard form (Form 1131), entitled "Bond for release of Federal tax lien," and shall be executed by a surety company holding a certificate of authority from the Secretary of the Treasury as an acceptable surety on Federal bonds.

The collector may also in his discretion issue a certificate of discharge of any part of the property subject to the tax lien if he finds that the fair market value of the part of the property not released from such lien is at least double the amount of the existing liability in respect of such tax plus double the amount of all liens prior to that of the tax lien. In general, fair market value is that amount which one ready and willing but not compelled to buy would pay to another ready and willing but not compelled to sell the property. Collectors must be conservative in determining property values and should make careful inquiry with respect thereto.

In cases where the collector issues a certificate of release of tax lien and at the same time an extension of time is granted for the payment of the deficiency in tax pursuant to the provisions of section 272(j) of the Revenue Act of 1928 or section 274(k) or 308(i) of the Revenue Act of 1926, a single bond may be accepted by the collector conditioned upon the payment of the amount assessed (together with all interest in respect thereof) in accordance with the terms of the extension and not later than six months prior to the expiration of the statutory period for collection, including any period for collection agreed upon in writing by the Commissioner and the taxpayer. Form 1131, hereinbefore mentioned, shall be used in these cases and shall be modified to meet the circumstances. Where a certificate of release of the tax lien has been issued by the collector, and the bond furnished to and accepted by the collector fully protects the interests of the United States with respect to the tax assessed, no additional bond will be required by the Commissioner as a condition to the granting of an extension of time for the payment of the deficiency in tax under the provisions of section 272(j) of the Revenue Act of 1928 or section 274(k) or 308(i) of the Revenue Act of 1926.

ROBT. H. LUCAS,
Commissioner of Internal Revenue.

Approved November 13, 1929.

A. W. MELLON,
Secretary of the Treasury.

INCOME TAX RULINGS.—PART II.**REVENUE ACT OF 1926.****TITLE II.—INCOME TAX.****PART I.—GENERAL PROVISIONS.****SECTION 201.—DISTRIBUTIONS BY CORPORATIONS.****ARTICLE 1545:** Distributions in liquidation.VIII-37-4349
G. C. M. 6590**REVENUE ACT OF 1926.**

The M Company was a corporation organized in the year 1908 for the purpose of engaging in the real estate subdivision business. Its sole activity has been the development of a high-class residential neighborhood. Early in 1925 it was informally agreed by the stockholders to liquidate the company as soon as possible. In March, 1925, and June, 1926, resolutions were passed to decrease the capital stock of the company by retiring and liquidating 12½ shares, and dividends were paid in those years to retire same. No land has been purchased by the company since the passage of the first resolution, but it is expected that it will be two or three years before the remaining land will be entirely sold.

Held, that the transaction constituted a bona fide distribution in liquidation, and that the amounts received by the stockholders should be considered for income tax purposes as payments in exchange for stock and not as ordinary dividends.

An opinion is requested as to whether certain dividends received by a taxpayer from the M Company during the years 1925 and 1926 are taxable as ordinary dividends or should be considered as dividends in liquidation.

The facts are as follows: The M Company was a corporation organized in the year 1908 for the purpose of engaging in the real estate subdivision business. Its sole activity has been the development of a high-class residential neighborhood at the city of R. The stock of the corporation has always been closely held, there having been but three stockholders originally and the number never having been increased to more than five or six. The original three, A, B, and C, however, have retained control of its affairs. As early as 1917 or 1918 the question of the future of the corporation was discussed by these three stockholders, and it was agreed that no new purchases of land would be made. Early in the year 1925 it was informally agreed by these stockholders to liquidate the company as soon as possible. At that time three-fourths of its holdings had been sold, and all major improvements had been made.

As stated above, the project was one calling for high-class residences. To establish and preserve this sort of a neighborhood, restrictive covenants limiting the kind and cost of the homes to be

built were inserted in the deeds, and the company required that all plans for homes be first submitted to it for approval. Incidentally it had to pass upon the financial ability of prospective purchasers to build houses of the required character. In general, the planting of shrubbery and trees, the landscape gardening, and the architecture of the homes were under the control of the company, in order that the subdivision might be kept harmonious as a whole. These facts are mentioned for the purpose of showing that no wholesale liquidation was possible, and that it would have to be a gradual process.

It was early in the year 1925 that the stockholders informally agreed that the company's affairs should be liquidated. Thereafter, on March —, 1925, a resolution was passed to decrease the capital stock from 28 $\times$ dollars to 21 $\times$ dollars by retiring and liquidating 7 y shares. The preamble to this resolution reads as follows:

WHEREAS, The M Company has sold and otherwise disposed of the major portion of its land, and whereas the operations in the future will be restricted to the sale of the remaining land and no further development of the company will be carried on, and whereas it is the desire of the stockholders to liquidate the company as rapidly as possible consistent with the protection of the value of its assets, be it * * *.

Again, on June —, 1926, a resolution was passed further to decrease the capital stock to 15 $\times$ dollars by retiring and liquidating 5 y shares. The preamble to this resolution reads:

WHEREAS, The stockholders of the M Company at a meeting held March —, 1925, announced their desire to liquidate the stock of this corporation as rapidly as possible, and in furtherance of this intention, be it * * *.

The dividends paid upon the occasion of these two retirements of stock are the dividends under consideration.

No land has been purchased by the company since the passage of the first resolution, but it is expected that it will be two or three years before the remaining land will be entirely sold. The taxpayer contends that the dividends paid in 1925 and 1926 upon the partial retirement of stock are liquidating dividends, to be applied against the cost of the stock retired, and, since not in excess of the same, are not subject to any tax.

Section 201(c) of the Revenue Act of 1926 provides in part:

Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock.

Section 201(g) provides:

If a corporation cancels or redeems its stock (whether or not such stock was issued as a stock dividend) at such time and in such manner as to make the distribution and cancellation or redemption in whole or in part essentially equivalent to the distribution of a taxable dividend, the amount so distributed in redemption or cancellation of the stock, to the extent that it represents a distribution of earnings or profits accumulated after February 28, 1913, shall be treated as a taxable dividend. In the case of the cancellation or redemption of stock not issued as a stock dividend this subdivision shall apply only if the cancellation or redemption is made after January 1, 1926.

Article 1549, Regulations 69, provides in part as follows:

The question whether a distribution in connection with a cancellation or redemption of stock is essentially equivalent to the distribution of a taxable dividend depends upon the circumstances of each case. A bona fide distribution, however, in complete cancellation or redemption of all the stock of a

corporation, or one of a series of bona fide distributions in complete cancellation or redemption of all of the stock of a corporation, is not essentially equivalent to the distribution of a taxable dividend. Where a distribution is made pursuant to a corporate resolution reciting that the distribution is made in liquidation of the corporation, and the corporation is completely liquidated and dissolved within one year after the distribution, the distribution will not be considered essentially equivalent to the distribution of a taxable dividend; in all other cases the facts and circumstances should be reported to the Commissioner for his determination whether or not the distribution, or any part thereof, is essentially equivalent to the distribution of a taxable dividend.

In view of the informal agreement made by the stockholders to liquidate the corporation and not to acquire any more land, which agreement was in substance reiterated in the resolutions of March —, 1925, and June —, 1926, in connection with the reductions of the capital stock and the declaration of the dividends in question, there can be no doubt that the dividends declared were intended as liquidating and not as ordinary dividends. There was something more than simply a reduction of capital stock and a distribution pro rata among all the stockholders, for the dividends were but steps in a plan of complete liquidation.

The fact that the winding up will take some time does not make it any less a liquidation. It is recognized in the regulations that there may be a liquidation taking some years, for article 1549, Regulations 69, provides, in substance, that when liquidation takes longer than one year, the circumstances shall be submitted to the Commissioner for his determination as to whether or not the distribution is essentially equivalent to a taxable dividend. In the instant case the company could not wisely have sold the remaining land at wholesale. It was bound to keep up the character of the homes to be built by approving the plans for the same as well as the purchasers. Likewise, it was bound to see that the proper restrictive covenants were inserted in the purchasers' deeds and enforced, that the trees, shrubbery, and landscape gardening were kept in harmony with that already put in, and that the plans for houses to be erected were in accord with the general scheme of architecture. For like reasons it could not split up the lots and sell them as sites for cheaper homes. Good faith to its former purchasers as well as good business required that it continue to make the sales as it had before. That some other means might have been devised to liquidate more rapidly makes this none the less a liquidation. It can not be said that a taxpayer must choose the quickest way at its peril. It is enough if it can be said that the corporation is honestly engaged in reducing its assets to cash and is not engaging in any new business. In this connection it is well to note that article 1549 of Regulations 69 speaks of and is apparently mainly concerned with "bona fide distributions in complete cancellation."

This office is of the opinion that under all the circumstances of the instant case the transaction constituted a bona fide distribution in liquidation, and that the amounts received by the stockholders should be considered for income tax purposes as payments in exchange for stock and not as ordinary dividends.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

SECTION 204.—BASIS FOR DETERMINING GAIN OR LOSS, DEPLETION, AND DEPRECIATION.

ARTICLE 1591: Basis for determining gain or loss from sale.

VIII-33-4310
G. C. M. 6677

REVENUE ACT OF 1926.

The basis to be used in the case of a sale by the surviving spouse of property situated in Illinois and held by the husband and wife as joint tenants is the cost thereof to the husband and wife.

An opinion is requested as to the proper basis to be used in computing profit from the sale by a surviving joint tenant of real property located in Illinois.

On May —, 1920, the taxpayer and her husband purchased real estate for x dollars. Each contributed 50 per cent of the purchase price, and the property was conveyed to them by a deed providing that they should take the title as joint tenants and not as tenants in common. On April —, 1923, the taxpayer's husband died. In 1926 the taxpayer sold the property, and used as a basis, in determining the taxable profit, 50 per cent of the original cost of the real estate plus 50 per cent of the fair market value at the date of her husband's death.

It is contended on the one hand that the basis is the total original cost of the property, reliance being placed on I. T. 1635 (C. B. II-1, 19), which reads as follows:

The basis to be used in the case of a sale by the surviving spouse of property held by the husband and wife as tenants by the entirety is the same as if the surviving spouse had alone owned the property from the date of its acquisition by the husband and wife.

On the other hand, it is contended that this ruling is wrong on principle; and that, even if it is right, it has no application to the instant case, because tenancy by the entirety is not recognized in Illinois, where the real estate is located.

It is true that tenancy by the entirety has not been recognized in Illinois since the enactment, in 1861, of the married woman's act. A conveyance to husband and wife as joint tenants, and not as tenants in common, creates a common law joint tenancy, which, unlike a tenancy by the entirety, can be severed during the joint lives by the conveyance of an undivided interest in the property by one tenant to a stranger. (*Lawler v. Byrne*, 252 Ill., 194, 96 N. E., 892; *Liese v. Hentze*, 326 Ill., 633, 158 N. E., 428.) In the opinion of this office, however, the principle of I. T. 1635 is not only correct with respect to tenancies by the entirety, but also applies with equal force to joint tenancies, provided, of course, that the tenancy has not been severed during the joint lives of the tenants.

The basis for determining the gain or loss from the sale or other disposition of property depends entirely, under the Revenue Acts, upon the method by which the property was acquired by the taxpayer. If a surviving tenant by the entirety acquires an undivided one half of the property when it is originally conveyed to husband and wife and acquires the other half, upon the death of the spouse, by bequest, devise, or inheritance, then the basis, on a sale by the survivor, is one-half the cost price plus one-half the value at decedent's death; while if, on the original conveyance to husband and wife, each is regarded

under the law as receiving the *entire* estate at that time, and the subsequent death of one spouse is looked upon, not as a transfer of his or her interest to the survivor, but merely as a cessation of the decedent's interest, leaving the survivor with the entire estate that he or she already had under the original conveyance, then the basis on a sale by the survivor is the original cost of the property, because he or she acquired the whole estate when that purchase price was paid.

It is the latter view which prevails in the case of tenancies by the entirety, and the same reasoning applies to a sale by the surviving joint tenant. The common law view, and the view still obtaining in the great majority of States which recognize the common law joint tenancy, is that a conveyance to two persons as joint tenants gives to each tenant the *entire* estate, so that, on the death of one tenant, nothing passes from the decedent to the survivor, but the interest of the decedent merely ceases, and the survivor has the entire estate that he already had from the beginning. In other words, the power of a joint tenant to sever the estate during their joint lives is not regarded, so long as it is not exercised, as affecting the theory that each holds the entire estate, and that the survivor gets nothing new or additional when the first tenant dies. Thus, in 1 Washburn on Real Property, star pages 404, 410, 412, it is stated:

A joint-tenancy is defined to be "when several persons have any subject of property jointly between them in equal shares by purchase." "Each has the whole and every part with the benefit of survivorship, *unless the tenancy be severed.*" In the quaint language of the law they hold, each "per my et per tout," the effect of which, technically considered, is, that for purposes of *tenure* and *survivorship*, each is the holder of the whole. But for purposes of *alienation*, each has only his own share.

* * * * *

The interest which a joint-tenant has as survivor, is not a new one acquired by him from his cotenant, upon the latter's death, *for his own interest is not changed in amount*, but only his cotenant's is extinguished.

No charge, therefore, like a rent, or a right of way, or a judgment, created by one cotenant, can bind the estate in the hands of the survivor, unless the charge be created by the one who becomes such survivor, or the creator of the charge releases his estate to a cotenant, who, as releasee, accepts, with that part of the estate, the charge inhering therein by his own act.

* * * * *

In conveying his interest to a stranger, a joint-tenant like a tenant in common, must do so by deed of grant with words of inheritance if it is intended to pass an estate in fee. Whereas, in conveying to his cotenant, a release is not only sufficient, but is the *proper* form of making such conveyance, *nor need there be any words of inheritance in the same*, since the one to whom the conveyance is made, *is already seized of the estate as a whole*, and it is only necessary to extinguish the right of his cotenant in order to invest him with the exclusive ownership of the entire estate. [Italics supplied.]

And in 2 Tiffany, Real Property, second edition, pages 625, 628, 629, it is stated:

In the case of a joint tenancy all the tenants have together, in the theory of the law, but *one* estate in the land and this estate each tenant owns conjointly with the other cotenants. All the joint tenants * * * constitute for some purposes but one tenant, or, as it has been more specifically stated, each joint tenant is regarded as tenant of the *whole* for purposes of *tenure* and *survivorship*, while for purposes of alienation and forfeiture each has an undivided share only. [The author then states in a note that "this is apparently the meaning of the statement in the books that each tenant holds 'per my et per

tout,' whether 'my' means 'half,' or whether it means 'nothing'—a matter on which there has been a conflict of opinion.”]

* * * This doctrine of survivorship appears to be the result of, or at least associated with, the theory that the joint tenants together own but one estate, a theory which, rigidly applied, would recognize no distinct interest in one to pass on his death to his heirs or devisees, his claim being, as against the others, merely *extinguished* in that case.

* * * Somewhat analogous to the doctrine of survivorship, and like it based on the theoretical nature of a joint tenancy, is the rule that in the case of a devise to two or more persons, in such form or under such circumstances as otherwise to make them joint tenants, if it is ineffective as to one * * * the devise is effective in favor of the other person or persons * * * they taking the *whole*. And the same rule applies in the case of a conveyance *inter vivos* to two or more persons as joint tenants, which is for any reason not effective in favor of one of such persons. [Italics supplied.]

In *Smith v. Douglas County* (254 Fed., 244), writ of error dismissed for want of jurisdiction (253 U. S., 474), it was held that a surviving joint tenant takes the property, not by gift, bequest, devise, or inheritance, but under the original grant; and that, consequently, a Nebraska statute imposing a tax on legacies, inheritances, and gifts made in contemplation of death does not cover the interest of a deceased joint tenant. In *Fleming v. Fleming* (194 Iowa, 71, 174 N. W., 946), the court said:

The joint tenancy, when created, vests in each of the tenants a common right in the property which does not survive his death, unless he becomes the last survivor of all the tenants. * * * In a legal sense, his death does not transfer the rights that he possessed in the property to the surviving tenants. Death does not enlarge or change the estate. Death terminates his interest in the estate. It is rather a falling away of the tenant from the estate than the passing of the estate to others.

Accordingly, it was held, in *Wood v. Logue* (167 Iowa, 436, 149 N. W., 613), that on the death of a joint tenant his creditors have no rights in the property as against the survivors, because the survivors take, not from the decedent, but directly from the grantor in the deed creating the tenancy. In *Attorney General v. Clark* (222 Mass., 291, 110 N. E., 299), it was held that upon the death of one joint tenant, the other takes the whole estate, not by descent as the heir at law of the other, but as the sole surviving tenant, and that consequently decedent's interest was not subject to the State inheritance tax. In *Chippendale v. North Adams Savings Bank* (222 Mass., 499, 111 N. E., 371), it was held that where a man deposited money in a savings bank to the account of himself and his sister as joint tenants, and his sister survived him, she took the deposit under the original contract with the bank, and not by gift to take effect on her brother's death, and, consequently, compliance with the statute of wills was not necessary. In the case of *In re Gurnsey's Estate* (177 Cal., 211, 170 Pac., 402), it was held that a transfer to joint tenants gives each of the tenants immediately the title and right of possession and enjoyment of the whole property, and the survivor succeeds to no new title or right on the death of his cotenant.

The same conclusion was reached as to the California and common law in *Carter v. English* (C. C. A., Ninth Circuit, 15 Fed. (2d), 6), where it was held that no part of the property held in joint tenancy in that case was subject to Federal estate tax. The court said:

It has been held that under the civil code of the State, as at common law, in joint tenancy the title to the joint property does not pass to and vest in the survivor upon the death of his cotenant, but each tenant is seized of the whole estate from the first; that no change occurs in his title on the death of his cotenant; that it simply "remains to him" and comes wholly from the original grant, so that, after the death of one, the other, in pleading his title, can allege conveyance by the original grantor to himself without mentioning his cotenant. (*Estate of Gurnsey*, 177 Cal., 211, 170 Pac., 402.) That being the law, title to the property of Charles L. Ames did not vest in the survivor (Edith) upon the death of her cotenant (Annie); nor did it descend to her from her cotenant, for it had already vested in her by and at the time of the death of Charles L. Ames. [The latter having devised the property to Edith and Annie as joint tenants.]

In the case of *In re Leach's Estate* (282 Pa., 545, 128 A., 497), in determining whether the State inheritance tax on transfers of property applied to a joint tenancy between brother and sister, the court said:

The court below has found a joint tenancy was created here when the library and its additions were secured, with the understanding that all the property acquired should belong exclusively to the survivor. This arrangement was put into effect more than 20 years before the brother's death. * * * The sister's rights then accrued, and the one-half did not pass to her by succession from him, but by reason of her contract of purchase. Under the circumstances, no collateral inheritance tax was chargeable * * *.

The theory of joint tenancies outlined above obtains in Illinois, where the real estate in the instant case was located. In *Erwin v. Felter* (283 Ill., 36, 119 N. E., 926), a mother deposited money in a bank to be payable either to herself or to the daughter or to the survivor of either. The court said:

The form of the certificates indicates an intention to create a joint tenancy in the money. A joint tenancy is not confined to real estate, but may exist in personal property * * *. The mother and daughter were equally entitled to withdraw the entire deposit. Each held during their joint lives subject to this right in the other, and upon the death of either the other held by the *same title* under the instrument creating the joint tenancy. The right of each party to receive from the bank payment of the money was the same and vested at the time the bank issued the certificates. *No greater right accrued by the death of either party, but the right already existing in the survivor continued while that which had existed in the deceased ceased.* There was therefore nothing in the nature of a testamentary disposition of the property; no gift to take effect at the donor's death. Whatever right Mrs. Erwin [the daughter] had in the money was acquired from the certificates. [Italics supplied.]

It is true that under the Illinois inheritance tax statute, which imposes a tax upon the *transfer* of property, it is specifically provided that the right of the surviving joint tenant to the whole property shall be "deemed" a taxable "transfer"; but the statute, itself, as well as Illinois cases decided since this inheritance tax provision was enacted (1919), show that that provision does not purport to change the nature of the tenancy itself, or state that there actually is a transfer from the decedent joint tenant to the survivor, but merely provides that the situation shall be treated as *though* there were a tenancy in common, and as *though* the deceased tenant had transferred his interest to the survivor by will. The provision reads as follows (Smith-Hurd Illinois Revised Statutes, 1925, ch. 120, par. 375, subsection 5):

Whenever property, real or personal, is held in the joint names of two or more persons, or is deposited in banks or other institutions * * * in the joint names of two or more persons and payable to either or the survivor, upon the death of one of such persons the right of the surviving joint tenant or joint

tenants, person or persons, to the immediate ownership or possession and enjoyment of such property shall be deemed a transfer taxable under the provisions of this act in the same manner as though the whole property to which such transfer relates was owned by said parties as tenants in common and had been bequeathed to the surviving joint tenant or joint tenants, person or persons, by such deceased joint tenant or joint depositor by will.

In other words, instead of providing that joint tenancies shall henceforth, for all purposes, be tenancies in common, the statute impliedly recognizes that joint tenancies shall continue as theretofore, but provides that they shall be treated, for inheritance tax purposes *only*, as though the parties *had* been tenants in common, and as though a transfer *had* been made by one to the other. That the parties are not actually tenants in common for other purposes was expressly recognized as recently as 1926 by the Illinois Supreme Court in *Engelbrecht v. Engelbrecht* (323 Ill., 308, 153 N. E., 827), when it stated:

If the estate is held by several persons as joint tenants, it is not and can not be held by them at the same time as tenants in common. It follows that to say of an estate that it is held by several persons as joint tenants is to say, in effect, that it is not held by them as tenants in common.

In *Deslauriers v. Senesac* (1928) (331 Ill., 437, 163 N. E., 327), the Supreme Court of Illinois again recognized that joint tenancy in the common law sense still existed in that State. In *Partridge v. Berliner* (1927) (325 Ill., 253, 156 N. E., 352) the court said:

A joint tenancy is a present estate in all the joint tenants, each being seized of the whole * * *. [Italics supplied.]

In *Liese v. Hentze* (326 Ill., 633, 158 N. E., 428), it is stated:

Joint tenancy is defined as "where two or more have any subject of property jointly, in which there is unity of interest, unity of title, unity of time, and unity of possession." (2 Blackstone's Com., 180; *Gaunt v. Stevens*, 241 Ill., 542, 89 N. E., 812.)

Since the statute does not change the general nature of joint tenancy in Illinois, it is obvious that it can have no effect for Federal tax purposes. As stated by the court in *Allen v. Henggeler* (32 Fed. (2d), 69 C. C. A., Eighth Circuit, March 25, 1929 [see Ct. D. 92, on page 387]) with respect to the Federal estate tax law:

* * * the State statutes and State decisions are looked to for the purpose of determining the quantity and quality of the decedent's interest in property * * *.

* * * But when that quantity and quality is found, then the Federal courts must determine whether such interest is taxable under the Federal estate tax law. [Without regard, that is, to the local inheritance tax law.]

As demonstrated above, the "quantity and quality" of a joint tenant's interest in property in Illinois is that each tenant owns the whole, and that the death of the first tenant constitutes a mere falling away of his interest, thereby giving the survivor nothing additional, but leaving him with what he had had from the beginning of the tenancy. It follows that the inheritance tax provision that for inheritance tax purposes, only, a joint tenancy shall be treated as though it were something different from what it is, and as though the decedent had done something he did not do (i. e., had devised or bequeathed an interest in the property to the survivor), can not affect Federal tax laws.

There are occasional court decisions in which the view appears to be taken that because of the right of a joint tenant to sever the

tenancy and convey, inter vivos, an undivided interest to a stranger, the tenants hold "by the half," not only for purposes of alienation and forfeiture, but for purposes of tenure as well. It is not denied that, in the absence of such a severance, the survivor takes the whole, but the death of the decedent appears to be regarded as constituting, not a mere falling away of his interest, but as a transfer of his interest to the survivor. This theory was recently adopted by the Board of Tax Appeals with respect to the law of Michigan in the case of *Sophia Weil* (15 B. T. A., 965, nonacquiescence, see on page 73), and was believed by the Board to represent the general view. With respect to the law generally, the Board relied on the case of *United States v. Robertson* (1910) (183 Fed., 711, certiorari denied, 220 U. S., 616). In that case the War Revenue Act of June 13, 1898 (ch. 448, 30 Stat., 464), provided that a tax should be imposed upon "* * * any personal property or interest therein transferred by deed, grant, bargain, sale, or gift, made or intended to take effect in possession or enjoyment after the death of the grantor * * * to any person * * *."

The Circuit Court of Appeals, Seventh Circuit, reversed the United States District Court for the Eastern Division of the Northern District of Illinois, and held that under a written instrument creating a joint tenancy in personal property, each held title to his own proportionate share until his death, and, on the death of one tenant, the title to his share then vested for the first time in the surviving tenants, and was subject to tax under the section of the War Revenue Act above quoted. There were no cases cited from Illinois or from any other jurisdiction to support the theory of joint tenancy there laid down, and Illinois cases taking the other view have been cited above, which were decided after the decision in *United States v. Robertson* was published.

Under any theory it seems perfectly clear that the survivor gets nothing by *bequest, devise, or inheritance*. Nothing passes by bequest or devise, because the law is well settled that, although a joint tenant may convey an undivided interest *inter vivos*, he can not pass such interest by will unless a statute expressly permits it, or unless, possibly, the devise is made in pursuance of a prior agreement between the joint tenants. (33 C. J., 908; 1 Tiffany, Real Property, page 628; 1 Washburn, Real Property, star page 412.) Furthermore, there was not in the instant case, nor is there in the ordinary case, any *attempt* to devise or bequeath the interest.

It is equally clear that the interest can not pass by inheritance, because, if it did, the share of a joint tenant would go to his heirs or representatives, whereas, in fact, the entire property is in the surviving tenant, although he may be no relation whatever to the deceased. (1 Washburn, Real Property, star page 407.)

Indeed, the court, in *United States v. Robertson*, did not hold that the share passed by bequest, devise, or inheritance, but that it was (to quote the statute) "transferred by deed, grant, bargain, sale or gift, made or intended to take effect in possession or enjoyment after the death of the grantor or bargainor."

In other words, the court may have considered a joint tenancy as being substantially a tenancy in common (with each owning an undivided one-half interest in the property) plus mutual promises, con-

stituting a contract, that whoever dies first shall have the other's property, which contract the law carries out, without requiring deeds, by a kind of legal "specific performance," whereby the decedent's title to his one-half share is carried automatically to the survivor. But the fallacy in this theory lies in the fact, first, that there are actually no such mutual promises in the ordinary case, and, second, that, if there were such promises, neither party would be free to convey an undivided interest, *inter vivos*, to a stranger, whereas in truth, in the ordinary joint tenancy, either tenant *is* free to convey such an interest. As a matter of fact, there happened to be, in *United States v. Robertson*, express promises by the tenants that the property should go to the survivor, and it is possible that this fact influenced the court in regarding the transaction as one where each tenant in effect conveyed an interest in the property to the others to take effect on his prior decease.

In any event, it is clear that the Federal courts can not establish local rules of property for Illinois or for any other State, and the nature of a joint tenancy appears to be a rule of property as to which the State laws must, in general, govern, although the effect of such local rules, for Federal tax purposes, is, of course, a Federal question. (*Allen v. Henggeler*, *supra*; *Carter v. English*, *supra*.)

In spite of *United States v. Robertson*, therefore, it appears that in Illinois, as in most States recognizing common law joint tenancies, the substance of the tenancy is that each tenant holds the entire estate, subject to a condition subsequent that the whole of it will terminate on the occurrence of his decease prior to the decease of the other tenant, and subject to the further condition subsequent that a portion of it will be divested by the execution of a conveyance, *inter vivos*, to a stranger of an undivided interest in the estate by the other tenant. A joint tenant differs principally from a tenant by the entirety in that the latter's estate is subject only to the first condition subsequent, while the former's estate is subject to both conditions subsequent. In either case, however, the tenant is looked upon as having the entire estate so long as a condition subsequent does not occur.

With respect to tenancies by the entirety, there is no inconsistency involved in including the entire value of property jointly held in the gross estate of the decedent, for estate tax purposes, and at the same time requiring that the basis in the hands of the survivor, for income tax purposes, shall be the original cost. The Federal estate tax law taxes "not the interest to which some person succeeds on a death, but the interest which ceased by reason of the death." (*Young Men's Christian Association v. Davis*, 264 U. S., 47; *Edwards v. Stocum*, 264 U. S., 61.) Since, during the joint lives, each joint tenant, in legal theory, has the entire estate, it follows that the interest which ceases on the death of the first joint tenant is the entire interest, and therefore the entire value of the property may properly be included in decedent's estate for estate tax purposes. The same theory requires holding that the survivor acquires the entire estate, not when decedent dies, but on the original conveyance to the joint tenants, and that the basis in the survivor's hands is, therefore, the cost at that time. The Government, therefore, is not applying one theory of joint tenancy to the estate tax and another theory to the income tax, but is using the same conception of joint tenancy for both taxes. Moreover, the Reve-

nue Act contains specific instances of the overlapping of estate and income taxes, so that Congress can not be said to have had any consistent intention that there should be no impinging of the two. The estate tax law does, however, make special provision for the situation where, as in the instant case, the wife contributes a part of the cost of the property. In that event the entire value of the property is not included in the gross estate of the decedent, whether the estate is a joint tenancy or a tenancy by the entirety. (See section 402(d), Revenue Act of 1921.) (As the husband's estate was less than the exemption, no Federal estate tax was paid at all in the instant case.) But there is no corresponding authority in the income tax provisions of the Revenue Acts, which define the basis of property for gain and loss purposes, for such a recognition of economic as opposed to legal interests; nor has this office recognized such interests in determining the basis of property in the case of estates by the entirety. (I. T. 1635, *supra*.)

It is the opinion of this office that in the instant case the basis of the property in the taxpayer's hands after her husband's death is the cost thereof (that is, the total sum paid for the property by the taxpayer and her husband), rather than one-half the cost plus one-half the fair market value at her husband's death.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

ARTICLE 1591: Basis for determining gain or loss from sale.

REVENUE ACT OF 1926.

Dower or statutory interest, value not having been returned to widow before her death. (See I. T. 2480, page 141.)

ARTICLE 1599: Stock or securities distributed in re-organization.

REVENUE ACT OF 1926.

Amendment of article 1599, Regulations 69. (See T. D. 4274, page 240.)

SECTION 206.—NET LOSSES.

ARTICLE 1625: Net losses of partnerships, estates and trusts, and insurance companies.
(Also Section 208, Article 1653.)

VIII-33-4311
G. C. M. 6630

REVENUE ACTS OF 1921, 1924, AND 1926.

Whenever the operations of a trust which comes within the provisions of section 704(b) of the Revenue Act of 1928 result in a loss for a given year, and the application of a proportionate part of that loss against the income of a particular beneficiary discloses a net loss for the beneficiary, such net loss may be claimed by him, under the Revenue Acts of 1924 and 1926, as a deduction

in his return for the following year. The beneficiary of a trust similar to the one considered in General Counsel's Memorandum 4120 (C. B. VII-2, 108) may likewise claim the benefit of the net loss provisions of these Revenue Acts.

The capital gain provisions of the Revenue Acts of 1921, 1924, and 1926 are not applicable with respect to profit derived from the sale of land covered by such trusts.

An opinion is requested as to whether the net loss provisions of the Revenue Acts of 1924 and 1926 and the capital gain provisions of the Revenue Acts of 1921 to 1926, inclusive, are applicable:

(1) To the beneficiaries of California real estate trusts which, except for section 704(b) of the Revenue Act of 1928, would be taxable as associations, but which are entitled to, and do, take advantage of that subsection; and

(2) To trusts similar to the one considered in General Counsel's Memorandum 4120, with a single beneficiary who, himself, manages and carries on the subdivision project as his individual business, the trust being merely an incidental security device in the nature of a mortgage, constituting, for income tax purposes, neither an association nor a strict trust, the income being taxable directly to the beneficiary as though the trust did not exist.

Considering first the trusts under section 704(b) of the 1928 Act, it appears that in General Counsel's Memorandum 4842 (C. B. VII-2, 103) it was stated:

This language of section 704(b), Revenue Act of 1928, is unambiguous, and, under it, it is entirely clear that all the income of a trust coming within that section is taxable, at the option of the trustee, to the beneficiaries, whether distributed or not, and without regard to the fact that under the terms of a particular trust instrument no part of the income of the trust is distributed or made available, or may be distributed or made available, to the beneficiaries until all of the capital costs of the trust have been fully paid and all obligations, whether or not secured by lien upon the trust property, have been discharged.

In General Counsel's Memorandum 5426 (C. B. VIII-1, 148) it was said:

Once an election is made under section 704(b) to have the concern taxed as a trust, it is treated, under that section, more like a partnership than like a strict trust, * * *. The income is taxable to the beneficiaries whether distributed or distributable, whereas, in the case of a strict trust, income which is not distributed or distributable is taxed to the trust as an entity. Consistency seems to require, therefore, that the beneficiaries should be allowed to deduct their proportionate shares of the [operating] losses of the trust * * *.

In view of these rulings and of the language of section 704(b), on which the rulings are based, it is evident that a subdivision trust, which is entitled to, and does, take advantage of that subsection, is not a taxable entity. The Revenue Acts define a "taxpayer" as including "any person, trust or estate subject to a tax imposed by this Act." Since trusts, as entities, are not "subject to tax" under section 704(b), they are not taxpayers. The only persons "subject to tax" with respect to such trusts, and, therefore, the only "taxpayers," are the beneficiaries. The trusts, like partnerships, are entities only for purposes of accounting. It follows that, as in the case of partnerships, the business of such trusts must be regarded as belonging to, and as being carried on by, the beneficiaries.

Although the Revenue Acts provide that the net-loss provisions apply only to net losses from the operation of any trade or business "regularly" carried on by the taxpayer, it has been held that a tax-

payer may "regularly" carry on more than one business and that a net loss sustained in any such business is deductible even though it is not the taxpayer's principal business. (Oscar K. Eysenbach, 10 B. T. A., 716, C. B. VII-2, 12.) This office has held, further, that, since some degree of regularity is essential in order to distinguish isolated or sporadic transactions from a "business," any course of action, which is sufficiently regular to constitute a business at all, is also a business "regularly carried on." As the Department has long maintained that the typical subdivision project, requiring consistent effort and attention over a considerable period of time, is clearly a business enterprise, it follows that it is a business "regularly carried on" within the meaning of the net loss provisions.

It is also evident, from what has been said, that the business must be regarded as having been regularly carried on by the beneficiaries, that is, by the "taxpayers." While many of them may not have taken active part in the business, it was carried on in their behalf and their lack of activity may be ignored, as in the case of silent partners, or as in the case of some of the stockholders of a personal service corporation when the stockholders of such a corporation were taxed in the same manner as members of a partnership. (See I. T. 1655, C. B. II-1, 128.)

Whenever, therefore, the operations of a trust which comes within the provisions of section 704(b) result in a loss for a given year and the application of a proportionate part of that loss against the income of a particular beneficiary discloses a net loss for the beneficiary, such net loss may be claimed by him, under the Revenue Acts of 1924 and 1926, as a deduction in his return for the following year.

A fortiori the beneficiary of a trust similar to the one considered in General Counsel's Memorandum 4120, *supra*, may claim the benefit of the net loss provisions because, even apart from section 704(b) of the 1928 Act, the business of such a trust is the individual business of the beneficiary, the trust, as a separate entity, being ignored for income tax purposes.

On the other hand, the capital gain provisions of the Revenue Acts of 1921 to 1926, inclusive, are not applicable to the income of trusts which come within the provisions of section 704(b) of the Revenue Act of 1928 nor to the type of trust referred to in General Counsel's Memorandum 4120, *supra*. In both cases, the subdivision project is a business enterprise and the land is its "stock in trade." In both cases, the trust, as a separate entity, is ignored for tax purposes, so that both land and business must be considered as though they belonged directly to the beneficiaries or beneficiary. It follows that the land is, in each case, the "stock in trade of the taxpayer," that is, of the beneficiaries or beneficiary, and, under the 1924 and 1926 Acts, the land also constitutes "property held by the taxpayer primarily for sale in the course of his trade or business." The result is, of course, that the land does not come within the meaning of the term "capital assets," as defined in the Revenue Acts, and the capital gain provisions are not applicable with respect to profit derived from the sale of the land.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

SECTION 208.—CAPITAL GAINS AND LOSSES.

ARTICLE 1651: Definition and illustration of capital net gain.

REVENUE ACT OF 1926.

Stock called in or bond redeemed before maturity date. (See I. T. 2488, page 127.)

ARTICLE 1653: Partnerships, estates, and trusts.

REVENUE ACTS OF 1921, 1924, AND 1926.

Profit derived from sale of land covered by a trust governed by section 704(b), Revenue Act of 1928, or a trust similar to one considered in General Counsel's Memorandum 4120 (C. B. VII-2, 108). (See G. C. M. 6630, page 179.)

SECTION 209.—EARNED INCOME.

ARTICLE 1661: Earned income.

VIII-43-4403
G. C. M. 6645

REVENUE ACT OF 1926.

(1) Dividends received by a partnership form a part of each partner's share of the partnership profits, and should be so included in applying the 20 per cent limitation provided for in section 209(a)1 of the Revenue Act of 1926 for the purpose of determining the amount of the partner's share which represents compensation for his services.

(2) That portion of dividends which is community income received by one spouse but properly reported in the separate return of the other spouse does not lose its character as dividends.

(3) The spouse who actually rendered the services may treat an amount not in excess of 20 per cent of the half of his profits reported by him as earned income for the purpose of computing his earned income credit.

An opinion is requested relative to the questions hereinafter stated arising out of the division of the profits from the M partnership between A and B, husband and wife, domiciled in the State of R, a community property State.

It appears that A and B are both members of the partnership; that B's interest is $21\frac{1}{2}$ per cent, and is her separate property; and that A's interest is $68\frac{1}{2}$ per cent, and is community property. The other 10 per cent is owned by a third party. The business of the partnership is such that both capital and labor are material income-producing factors. The husband received a salary from the partnership of 26.30x dollars. In addition to this, the husband received as his share of the partnership profits 115.70x dollars, of which 1.33x dollars represented his share of dividends received by the partnership. The husband's total partnership profits, therefore, were 142x dollars. The wife received 36x dollars as her share of the partnership profits, of which .40x dollars represented her share of the dividends. The wife rendered no services to the partnership.

This case does not involve the question of whether a husband and wife can be members of the same partnership. If the wife invests her separate property in a partnership she is entitled to share in the gains and profits of the enterprise. (Appeal of Elmer Klise, 10 B. T. A., 1234, C. B. VII-2, 22.) If husband and wife reside in a community property State, the income of each which is community income may be divided pending final adjudication of the question as to the right of the Government to tax the entire community income to the husband. (See Mim. 3723, C. B. VIII-1, 89.) In the instant case the income of both husband and wife is community income. Therefore, each may report one-half of the profits received by the other.

As a part of the partnership profits of each was dividends and as only the husband rendered services to the partnership, a question arises as to how dividends should be treated in the separate returns of husband and wife and how the earned income of the husband should be determined for the purpose of computing his earned income credit.

The examining officer excluded the husband's share of dividends, namely, 1.33*x* dollars, from his share of the profits and treated 20 per cent of the balance, 140.67*x* dollars, as earned income of the husband. This gave the husband earned income of 28.13*x* dollars on which his credit was computed. The wife's earned income credit was computed on \$5,000, the minimum allowance. The dividends received by the husband were allowed as a credit against his net income and the dividends received by the wife were allowed as a credit against her net income.

Another position taken in the same case is that as the amount distributed to A and B was 178*x* dollars, and as the returns were filed on a community property basis, one-half of 178*x* dollars, or 89*x* dollars, was the amount to be reported by the husband, and that his earned income credit was, therefore, 20 per cent of 89*x* dollars, or 17.80*x* dollars, instead of the amount shown in the report.

Still another view is that only 20 per cent of one-half of 140.67*x* dollars (the husband's share of the profits less his share of the dividends), or 14.06*x* dollars, was earned income of the husband.

These conflicting views raise three specific questions:

(1) In determining the portion of partnership profits which may be treated as earned income in cases where the partnership is engaged in a business in which both capital and labor are material income-producing factors, should the 20 per cent be computed on the total share of the profits of the partnership or on the total share less dividends?

(2) Is the wife in a community property State entitled to treat the half of her husband's partnership profits reported in her return as including one-half of the dividends received by the husband? The same question also applies to the husband in case the wife is a member of a partnership and receives dividends from the partnership.

(3) Is the husband's earned income for the purpose of computing the credit limited to 20 per cent of his share of the profits, 20 per cent of the half of his share reported by him, or 20 per cent of the sum of half of his share and half of his wife's share?

Section 209 of the Revenue Act of 1926 contains the following provisions:

(a) For the purposes of this section—

(1) * * * In the case of a taxpayer engaged in a trade or business in which both personal services and capital are material income producing factors, a reasonable allowance as compensation for the personal services actually rendered by the taxpayer, not in excess of 20 per centum of his share of the net profits of such trade or business, shall be considered as earned income.

(c) In the case of the members of a partnership the proper part of each share of the net income which consists of earned income shall be determined under rules and regulations to be prescribed by the Commissioner with the approval of the Secretary and shall be separately shown in the return of the partnership and shall be taxed to the members as provided in section 218.

Article 1661 of Regulations 69 provides in part as follows:

* * * The earned income credit will be allowed to the members of a partnership with respect to the share of the net income belonging to each which consists of earned income. There must be included in the return of the partnership a statement showing—

(1) The amount of earned income as defined in section 209(a) and article 1662, and

(2) The names of the members and the amounts of their respective shares of earned income. (See article 412.)

Article 412 of Regulations 69 provides in part as follows:

The return of a partnership shall state specifically—

(e) The names and addresses of the individuals who would be entitled to share in the net income of the partnership if distributed;

(f) The amount of the distributive share of such net income of each such individual;

(g) The part of such share of the net income which consists of earned income; and

(h) Such other facts as are required by Form 1065.

Instruction 13 on Form 1065, "Partnership return of income," provides in part:

Earned income.—Each member of a partnership engaged in a trade or business in which both personal services and capital are material income-producing factors may claim a reasonable amount as compensation for personal services actually rendered, not in excess of 20 per cent of his share of the net profits, which amount shall be considered as earned income and shall be separately shown in column 4, for the purpose of claiming on the individual return the credit of 25 per cent of the tax on earned net income.

Under the regulations referred to above and the instructions contained on Form 1065, an amount not in excess of 20 per cent of the share of a partner who actually rendered personal services may be treated as earned income. Dividends received by a partnership are part of the partnership profits which are distributed to the members and form a part of each partner's share. Such dividends should therefore be included in the share of the profits in determining the amount of the partner's share which represents compensation for his services. In this connection see I. T. 2328 (C. B. VI-1, 21).

The second question is whether that portion of dividends which is community income received by one spouse but properly reported in the separate return of the other spouse loses its character as dividends. The conclusion of this office is that it does not. Accordingly, if dividends are received by the husband and are community income,

the half of such community income reported by the wife retains its character as dividends, and the wife may credit the amount of the dividends reported by her against net income for normal tax purposes. The husband's credit for the same purpose is limited to the amount of dividends reported in his return.

In connection with the third question, reference is made to Mimeograph 3283 (C. B. IV-1, 14), issued under the Revenue Act of 1924, relative to the computation of the earned income credit. It was held in part (2) (c) of this mimeograph with respect to the earned income of a partnership:

(c) In the case of a partnership which is engaged in a trade or business in which both capital and labor are material income-producing factors, each partner who renders services may consider as reasonable compensation for such services an amount not in excess of 20 per cent of his share of the net profits of the partnership. A member of the partnership who does not render services to the partnership may not consider any part of his share of the profits as earned income.

With respect to the credit allowable when husband and wife file separate returns in States having community property laws it was held in part 7(b)1:

(1) Since "earned income" is the amount received as compensation for the personal services *actually rendered by the taxpayer*, the spouse in a community property State who reports half of the earned income received by the other spouse may not treat that portion of such income in excess of \$5,000 as earned income for the purpose of computing the credit; \$5,000 of such income may be treated as earned net income by reason of the fact that every individual taxpayer is entitled to consider the first \$5,000 as earned net income. The spouse who actually performed the services for which the income was received may compute his or her credit on the actual amount of the earned income reported in his or her return up to \$10,000. If the husband is engaged in a trade or business in which both capital and labor are material income-producing factors, his earned income from the business, for the purpose of computing the credit, is 20 per cent of the half of the profits reported by him.

In other words, the earned income credit, in all cases where the amount of earned net income is more than \$5,000, inures to the benefit of the *person who performed* the services, to the extent that he is required to report the compensation for such services in his gross income, and is not a benefit which inheres in the income itself.

It is the opinion of this office that the same principle applies in computing the earned income of a partner in cases where the spouses report such income in separate returns as was applied to earned income from a business in Mimeograph 3283, quoted above. The spouse who actually rendered the services may treat an amount not in excess of 20 per cent of the half of his profits reported by him as earned income for the purpose of computing his earned income credit.

In the instant case the partnership profits of the husband and wife are as follows, and should have been so shown on the partnership return:

	Husband's share.	Wife's share.
	Dollars.	Dollars.
Dividends.....	1. 33x	. 40x
Earned income.....	28. 40x	
Balance of profits.....	112. 27x	35. 60x
Total.....	142x	36x

The amount shown above as earned income, namely, 28.40x dollars, represents 20 per cent of 142x dollars, the husband's share of the partnership profits, including the salary paid to him. One-half of the husband's share of the profits is 71x dollars, and 20 per cent of this amount is 14.20x dollars.

There should be reported in the husband's separate return, one-half of each item of his share and one-half of each item of his wife's share. This would result in the husband reporting—

Dividends.....	.67x dollars +	.20x dollars =	.87x dollars
Earned income.....	14.20x dollars		= 14.20x dollars
Balance partnership profits.....	56.13x dollars +	17.80x dollars =	73.93x dollars
Total.....	71x dollars +	18x dollars =	89x dollars

The husband's earned income credit should be computed on 14.20x dollars. The wife's earned income credit should be computed on \$5,000, the minimum allowance.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

ARTICLE 1662: Definitions and limitations.

VIII-32-4301
G. C. M. 6563

REVENUE ACT OF 1926.

A loss in one business in which both personal services and capital are material income-producing factors is not a deduction in computing the net profit from another business in which both personal services and capital are material income-producing factors; neither is the loss a deduction which is properly allocable to or chargeable against earned income. Such a loss is not allocable to or chargeable against any particular item of income.

While the loss in one business will operate to reduce total net income and thereby reduce the tax payable, it will not reduce the amount of the earned income.

An opinion is requested as to whether in case a taxpayer has more than one business in which both personal services and capital are material income-producing factors, and sustains a loss in one and derives a profit from the other, the loss should be applied against the profit and 20 per cent of the remainder taken to determine the taxpayer's earned net income from such business.

The statute involved is section 209(a)1 of the Revenue Act of 1926, which provides as follows:

SEC. 209. (a) For the purposes of this section—

(1) The term "earned income" means wages, salaries, professional fees, and other amounts received as compensation for personal services actually rendered, but does not include that part of the compensation derived by the taxpayer for personal services rendered by him to a corporation which represents a distribution of earnings or profits rather than a reasonable allowance as compensation for the personal services actually rendered. In the case of a taxpayer engaged in a trade or business in which both personal services and capital are material income producing factors, a reasonable allowance as compensation for the personal services actually rendered by the taxpayer, not in excess of 20 per centum of his share of the net profits of such trade or business, shall be considered as earned income.

The question presented arises in the case of A, who in 1926 received partnership income of 8x dollars and sustained a loss from

another business carried on by him of x dollars. Personal services and capital were material income-producing factors in both businesses.

The contention is made that where a taxpayer has more than one business in which both his personal services and capital are material income-producing factors and he sustains a loss in one and derives a profit from the other, the profit from the one should be reduced by the loss sustained in the other in order to determine the net amount of profit attributable to his businesses in which both his personal services and capital are material income-producing factors. It is not believed that this contention is sound.

An individual may engage in one business with separate departments or in several different businesses which are in no way related except by a common ownership. If each separate business in which a taxpayer is engaged is one in which both personal services and capital are material income-producing factors and the taxpayer actually renders substantial personal services in the conduct of each business, 20 per cent of the taxpayer's net profit from each business shall be treated as compensation for the personal services actually rendered by the taxpayer under the provisions of section 209(a)1. A loss in one business in which both personal services and capital are material income-producing factors is not a deduction in computing the net profit from another business in which both personal services and capital are material income-producing factors; neither is the loss a deduction which is properly allocable to or chargeable against earned income. Such a loss is not allocable to or chargeable against any particular item of income any more than a loss by fire of the residence of a taxpayer and a charitable contribution are deductions properly allocable to or chargeable against a particular item of income. Such items of deductions are chargeable against total income.

The fact that a taxpayer gets nothing for his services in a business which results in a loss should not operate to reduce the amount of the compensation for his services rendered to the business which results in a net profit. While the loss in one business will operate to reduce the taxpayer's total net income, and thereby reduce the tax payable, it will not reduce the amount of his earned income.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

PART II.—INDIVIDUALS.

SECTION 212.—NET INCOME OF INDIVIDUALS DEFINED.

ARTICLE 23: Bases of computation.

REVENUE ACT OF 1926.

Revocation of I. T. 2377 (C. B. VI-2, 59) in so far as inconsistent with General Counsel's Memorandum 6667 (page 94). (See I. T. 2490, page 195.)

ARTICLE 23: Bases of computation.

REVENUE ACT OF 1926.

Accrual of real and personal property taxes in Minnesota. (See G. C. M. 7235, page 197.)

SECTION 213(a).—GROSS INCOME DEFINED:
INCLUSIONS.

ARTICLE 31: What included in gross income.

VIII-26-4251
G. C. M. 6351

REVENUE ACT OF 1926.

Cash bonuses paid to a wife living with her husband and domiciled in the State of Texas, in consideration of her execution of oil leases on real estate inherited and owned by her in fee simple prior to her marriage, constitute the separate income of the wife and should be included in her separate return.

An opinion is requested as to whether cash bonuses received by a married woman in Texas under the facts hereinafter stated are separate or community income.

It appears that A, prior to her marriage, inherited certain lands located in R County, Tex. In the year 1925, subsequent to her marriage, A executed certain oil and gas leases, in which her husband joined, to the M Company and various other lessees, in consideration of the execution of which each lessee paid to A certain cash bonuses and further agreed to deliver to the credit of A free of cost in the pipe line one-eighth part of all oil produced and saved from the leased premises. The cash bonuses paid to A in 1925 amounted to 42.8x dollars. In their separate returns for 1925 A and B, her husband, treated the bonuses as community income, and each spouse reported one-half thereof.

An audit in the office of the collector of internal revenue was thereafter made, as a result of which the entire amount of the bonuses was treated as the separate income of A. An additional assessment against A was made in the amount of 2.4x dollars, which amount A paid on January —, 1928. On January —, 1928, B filed a claim for refund of x dollars, alleging that he had overpaid his tax for the year 1925 in such amount because he had erroneously included in his 1925 return one-half the bonuses received by his wife in that year.

It is contended, on the one hand, that the claim for refund of the husband should be rejected and that the additional tax paid by the wife should be refunded upon the theory that the bonuses constituted community income and therefore were properly reported in the first instance by both A and B. On the other hand, it is urged that under the law of Texas the bonuses are the exclusive and separate property of the wife and therefore are to be reported by her alone. Thus the issue is presented whether cash bonuses paid to a wife, living with her husband and domiciled in the State of Texas, in consideration of her execution of oil leases on real estate inherited and owned by her in fee simple prior to her marriage, constitute community income or the separate income of the wife.

It is now well established that bonuses and royalties derived from mineral leases (including oil leases) constitute ordinary income subject both to normal tax and surtax. (*Rosenberger v. McCaughn*,

C. C. A., 25 Fed. (2d), 699, cert. denied 278 U. S., 604; *John Hirschi v. United States*, Court of Claims, May 6, 1929; appeal of Nelson Land & Oil Co., 3 B. T. A., 315; *Henry L. Berg et al. v. Commissioner*, 6 B. T. A., 1287; *R. H. Hazlett v. Commissioner*, 10 B. T. A., 332; *James R. Parkey et al. v. Commissioner*, 16 B. T. A., 441; G. C. M. 4299, C. B. VII-2, 116.) Hence it remains necessary in this case only to determine to whom the bonuses should be taxed.

For the purpose of determining the respective rights of A and B in and to the fund which the bonuses constituted, the law of Texas must be considered, for it is settled that the Federal courts follow the State courts where they have spoken in regard to the property rights of their citizens. (*DeVaughn v. Hutchinson*, 165 U. S., 566; *Erie Railroad Co. v. Hilt*, 247 U. S., 97.) In this manner the Federal courts apply the State law in determining the owner of the fund regarded as income, and so ascertain the person to whom that income is to be taxed. (*Etta Radin, Administratrix, v. Commissioner*, C. C. A. 3d Circuit, April 9, 1929; G. C. M. 4596, C. B. VII-2, 133; I. T. 1267, C. B. I-1, 212; I. T. 2349, C. B. VI-1, 78; T. D. 2987, C. B. 2, 180.)

In *Stephens v. Stephens* (Tex. Civ. App., 292 S. W., 290), the husband sued his wife for a divorce and for a decree that the entire amount of royalties derived from the leasing of his separately-owned real estate acquired before marriage constituted his separate property. From a decree in favor of the husband the wife appealed, and the Court of Civil Appeals of Texas affirmed the judgment. Rehearing was denied, and, as an application for writ of error was denied for want of jurisdiction by the Supreme Court of Texas, the case is authority in that State. In the course of its opinion the Court of Civil Appeals stated:

It has always been held in this State that the consideration received for the separate estate of the husband or wife, whether money or property, continues to be separate property (*Chappell v. McIntyre*, 9 Tex., 161; *Oliver v. Robertson*, 41 Tex., 422), and that the separate estate may undergo mutations and changes and still remain separate property so long as it can be clearly traced and identified. (*Arnold v. Leonard*, 114 Tex., 535, 273 S. W., 802; *Rose v. Houston*, 11 Tex., 324, 62 Am. Dec., 478; *Schmidt v. Huppmann*, 73 Tex., 112, 11 S. W., 175.)

The land is separate property. The oil in place is realty capable of distinct ownership, severance, and sale. It is a part of the corpus of appellee's sole estate. He conveyed his oil and received as the principal consideration therefor one-eighth of the production. No skill, labor, or supervision of either of the spouses, and no community property was expended in the sale or production. The oil and the proceeds thereof received by appellee were neither rent nor profits, within the meaning of the law making such common property, but the consideration for separate realty. Extracting the oil from beneath the surface depletes and exhausts forever the corpus of his separate property; removing it to the top of the ground changes it from real to personal property; but such change or mutation, and the money received, are definitely traced, and, in our opinion, the fund in controversy belonged to appellee in his sole and separate right.

(See also *James R. Parkey et al. v. Commissioner*, supra.)

In view of the foregoing, it is the opinion of this office that the bonuses were the separate property of A and must be taxed as her separate income. It follows that no part of the bonuses should be included in B's separate return, and that any refund due B by reason of such fact should be allowed.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

ARTICLE 39: Sale of stock and rights.

REVENUE ACT OF 1926.

Rights to subscribe to bonds. (See I. T. 2494, page 76.)

ARTICLE 44: Sale of real property involving deferred payments.

REVENUE ACT OF 1926.

Sales during fiscal year ended in 1928 and computation of tax attributable to that part of the fiscal year falling in the calendar year 1927. (See I. T. 2513, page 121.)

ARTICLE 48: Improvements by lessees.

REVENUE ACT OF 1926.

Amendment of article 48, Regulations 69. (See T. D. 4281, page 244.)

ARTICLE 50: When included in gross income.

VIII-44-4411
G. C. M. 6982

REVENUE ACT OF 1926.

Under the provisions of a lease between the taxpayer and the M Company, title to a building and other improvements erected by the M Company (lessee) on land of the taxpayer (lessor), situated in the State of New York, is expressly provided to be and remain in the lessee, its successors or assigns, until the termination of the lease and/or until the termination of the last term of the three renewals provided for in the lease, and such building and improvements do not become the taxpayer's property until such termination.

Held, that the taxpayer derived no taxable income upon the completion of the building and other improvements erected by the lessee on the land owned by the taxpayer.

An opinion is requested as to whether the O Company, the taxpayer, derived taxable income upon the completion of a building and other improvements erected by the M Company, a lessee, upon land owned by the taxpayer.

The O Company is the fee simple owner of certain real property situated in the State of New York. On April —, 1925, the O Company entered into an agreement with the M Company, in which it had no financial interest, whereby the O Company agreed to lease the property to the M Company for a period of 21 years from April —, 1925. The agreement also granted to the lessee three options to renew the lease for a further period of 21 years under each option. The lessee agreed to improve the premises by erecting thereon a new building to cover substantially the whole of the premises which should cost the lessee not less than x dollars and which should be completed by September —, 1926.

Article — of the lease in question reads as follows:

—. That the title to all buildings, all alterations and all other improvements and fixtures and to all boilers, machinery, elevators, apparatus, electric and

gas fixtures, equipment, decoration, furnishings and all personal property used by the tenant, its successors or assigns, in the maintenance and operation of the said demised premises and all replacements and betterments that shall be erected, made or placed on the demised premises by the tenant, its successors or assigns, shall be the property of the tenant, its successors or assigns, but at the expiration of the demised term or other sooner termination thereof, or, if this lease shall be renewed as hereinafter provided, at the expiration of the last term for which the same shall be renewed or other sooner termination thereof, shall vest in the landlord, its successors and assigns, forever and become at that time their property free from any and all right, title or interest of the tenant, its successors or assigns therein.

Furthermore, article — of the lease in question makes it obligatory upon the lessor to renew the lease upon the expiration thereof, and so on for two additional renewals, thus in effect providing for four leases of 21 years each. This article also provides that upon each renewal of the lease the rental shall be calculated as "a net annual rental of 6 per cent of the full value of the land at the expiration of this lease, to be determined by appraisal as herein provided." Provision is thereupon made that the appraisers shall "determine the value of the land demised at the time of such valuation * * * considering it as a vacant piece or parcel of land at its full and fair value at private sale."

It is thus clearly apparent that the parties to this lease intended that the title to the building and other improvements should remain in the lessee, its successors and assigns, until the expiration of the last lease, unless otherwise sooner terminated, and that the title to the building and other improvements should not vest in the lessor until such termination.

It is the law in New York State that title to buildings or permanent improvements erected by a lessee vests in the lessor, but by agreement the lessee may reserve his title thereto, in which case the improvements belong to the lessee and not to the lessor. (See *Smith & Britton v. Benson & Peck*, 1 Hill (N. Y.), 176; *People v. Board of Tax Assessors*, 93 N. Y., 308; *People v. Commissioners*, 80 N. Y., 573; *Precht v. Howard*, 187 N. Y., 136, 79 N. E., 847; *People v. Barker*, 153 N. Y., 98, 47 N. E., 46.)

It is evident that the provisions of the lease here under consideration differ materially from the provisions contained in the ordinary lease. Article 48 of Regulations 69, *Miller v. Gearin* (258 Fed., 225, certiorari denied 250 U. S., 667), and *Cryan v. Wardell* (263 Fed., 248) deal with cases where title to improvements erected by a lessee vests upon completion in the lessor, and have no application to the situation here presented.

In view of the foregoing, it is the opinion of this office that the O Company, the taxpayer, derived no taxable income upon the completion of the building and other improvements erected by the lessee on the land owned by the taxpayer.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

SECTION 213(b).—GROSS INCOME DEFINED:
EXCLUSIONS.

ARTICLE 89: Additional exclusions from gross income.

REVENUE ACT OF 1926.

Amendment of article 89, Regulations 69, to include Greece in the list of countries which satisfy the equivalent exemption requirement of section 213(b)8 of the Revenue Act of 1926. (See T. D. 4269, page 146.)

SECTION 214(a)1.—DEDUCTIONS ALLOWED INDIVIDUALS: BUSINESS EXPENSES.

ARTICLE 107: Treatment of excessive compensation.

VIII-44-4412
G. C. M. 6952

REVENUE ACT OF 1926.

A corporation took a deduction in its income tax returns for 1925 and 1926 on account of salaries paid to certain officers who were stockholders. A portion of the salaries paid was disallowed on the ground that, to the extent of the amount disallowed, the salaries were excessive and unreasonable. The excessive amounts paid did not bear a close relationship to the stock holdings of the respective officers.

Held, that the officers can not recover the tax paid on the excessive amounts received as salaries but disallowed as a deduction to the corporation.

An opinion is requested as to the taxable status of amounts received in 1925 and 1926 by C, the taxpayer, as part of his salary from the M Company, but disallowed as a deduction to the corporation because excessive and unreasonable.

The M Company was incorporated in the spring of 1925 with a paid-in capital of 30x dollars. The original issue of stock was subscribed and paid for in cash as follows:

	Dollars.
A-----	7.5x
B-----	7.5x
C-----	15x
Total-----	30x

The stock of B was canceled and then reissued on April —, 1925, to D, a child of A, and was paid for by him. No other change in stock ownership occurred during the years in question—that is, 1925 and 1926. It therefore appears that D and A each owned one-fourth of the stock, while the taxpayer owned one-half.

The M Company, on its return for 1925, took a deduction for officers' salaries of 5.58x dollars, of which 2.79x dollars, or one-half, was paid to A and a like amount to the taxpayer. Again, in 1926 it took a deduction of 6.02x dollars for officers' salaries, of which one-half, or 3.01x dollars, was paid to A and a like amount to the taxpayer. The latter reported the amount thus paid him as salary in his individual returns for 1925 and 1926, and paid the tax upon the same. Upon examination of the corporation's returns, the revenue agent disallowed 2.4x dollars of the amount paid as officers'

salaries for each year, upon the ground that to that extent the salaries were excessive and unreasonable. He judged the salaries excessive by comparison with the salaries of officers of corporations engaged in the same line of business and also by comparison with gross sales of the corporation. He further took the position that to the extent of the excess the payments were dividends or a return of capital to the stockholders. The taxpayer now contends that inasmuch as the corporation did not have any surplus in 1925 or 1926, out of which dividends could have been paid, the excessive payments (that is, the excess of the payments over a reasonable salary), not being in excess of the cost of his stock, should be held to be a return of capital and not taxable income. He therefore seeks to recover the normal tax and surtax which he paid on account of the inclusion of 1.2x dollars in his return for each of the years in question, relying on article 1544 of Regulations 69, which provides in part that:

Any distribution (not in partial or complete liquidation) made by a corporation to its shareholders otherwise than out of increase in value of property accrued prior to March 1, 1913, or earnings or profits, shall be taxable to the recipient only if and to the extent that such distribution exceeds the basis of his stock * * *.

As the Revenue Act of 1926 permits only a reasonable allowance for salaries to be taken as a deduction from gross income (see section 234(a)1 of the Revenue Act of 1926 and article 106, Regulations 69), it will often happen that a corporation which has paid excessive amounts as salaries can not deduct the same to the extent of the excess (see *J. Livingston & Co. v. United States*, Court of Claims, decided May 6, 1929) and, at the same time, the recipient will be obliged to pay both normal tax and surtax on the same (*United States v. Snook*, 24 Fed. (2d), 844). As was said in the Snook case, "The fact that an unreasonable salary paid can not be fully availed of by the corporation as a deduction in fixing its taxes under the tax law has no bearing on the recipient and his tax liability. This is quite evident in case the officer does not happen to be also a stockholder." The disallowance of the deduction to the corporation in the instant case therefore does not of itself entitle the officer, who has received the amount disallowed the corporation as a deduction, to escape tax thereon.

It is unnecessary to decide what the result would be if the excessive payments bore a close relationship to stock holdings, there being no surplus to distribute. Perhaps, in such a case, on the portion disallowed as a deduction, the officer should pay no tax, on the theory of article 1544 that there has simply been a return of capital with respect to the stock. (Cf. *Daniel Winant et al., Executors, v. Gardner*, Circuit Court of Appeals, Second Circuit, 29 Fed. (2d), 836.) Article 107 of Regulations 69 provides in part that—

* * * in the case of excessive payments by corporations, if such payments correspond or bear a close relationship to stock holdings, and are found to be a distribution of earnings or profits, the excessive payments will be treated as a dividend, and will thus be exempt from the normal tax in the hands of the recipient.

In cases where the recipient of excessive payments, which have been paid out of surplus, has sought to escape the normal tax on the amount disallowed the corporation as a deduction, it has been consistently held that, unless the excessive payments bore a close rela-

tionship to stock holdings, they would not be regarded as dividends in the hands of the recipient. (*Johnston Livingston v. United States*, Court of Claims, decided May 6, 1929; *Mary B. Brauer et al., Executors, v. Commissioner*, 6 B. T. A., 579, C. B. VII-1, 4.)

A dividend, or, in fact, any distribution of corporate assets among stockholders, must be made in proportion to the respective stock holdings. "It is an undoubted general rule that, in the absence of agreement to the contrary, all persons who own shares of stock in a corporation at the time a dividend is declared are entitled, as a matter of absolute right, to share ratably in the dividend in proportion to their respective shares, without discrimination and regardless of the time when their shares were acquired." (Fletcher *Cyclopedia of Corporations*, section 3699.) "Dividends among stockholders of the same class must always be pro rata, equal, and without discrimination or preference. * * * The directors have no authority to declare a dividend on any other principle. They can not exclude any portion of the stockholders from an equal participation in the profits of the company." (Fletcher, *supra*, section 3674.) There can be no doubt that the same rule applies to dividends illegally paid out, because they impair capital, and which are in effect distributions of capital. In any event, all stockholders in the same class are to be treated alike. In the instant case, the excessive payments do not bear a close relationship to stock holdings. The rule contended for by the taxpayer does not, therefore, apply, and the sum paid him as salary is taxable as such.

The fact that the revenue agent termed the excessive payments dividends or a return of capital is of no consequence. In *Johnston Livingston v. United States*, *supra*, the Court of Claims dispelled any doubts on this score in the following language:

* * * Whatever else may be said, it is indisputable that the sums paid the plaintiff were, in fact, paid to him as salary, and in no way predicated upon his stock holdings in the corporation. It is true that the Commissioner justified the disallowance of the sums here involved, as deductions from the gross income of the corporation, upon the basis of a distribution of earnings, and if in fact and in law the sums paid were dividend distributions, they were, under the quoted statutes, payable, so far as the normal tax is concerned, at the source. However, it is at once apparent that the sums received by the plaintiff were not received as dividends, and under the record herein may not be held to be such. It was a voluntary distribution to the plaintiff of a fixed sum as compensation for services rendered, irrespective of ownership of stock, and in nowise calculated upon the basis of a distribution of earnings as a dividend. The Commissioner in auditing the tax return of the Livingston corporation was under the law empowered to disallow unreasonable salaries paid to officials of a corporation as deductions from gross to ascertain net income. By so doing he did not convert an actuality into what he may have termed in his rulings as something else.

This office therefore concludes that the entire sum received by the taxpayer as salary from the M Company is taxable as such and, consequently, he is not entitled to recover the tax paid on the excessive salary payments.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

SECTION 214(a)3.—DEDUCTIONS ALLOWED INDIVIDUALS: TAXES.

ARTICLE 131: Taxes.
(Also Section 212, Article 23.)

VIII-35-4327
I. T. 2490

REVENUE ACT OF 1926.

I. T. 2377 (C. B. VI-2, 59), holding that taxpayers in the States of Washington and Oregon who maintain books of account on the accrual basis may, in the computation of net income, take a deduction because of accrued property taxes only for the year within which such taxes become a fixed liability, which is the date when the tax rolls or lists are delivered to the treasurer or collector of taxes, is revoked in so far as inconsistent with General Counsel's Memorandum 6667 (see on page 94).

ARTICLE 131: Taxes.

VIII-38-4361
G. C. M. 6770

REVENUE ACT OF 1926.

The Wisconsin motor vehicle fuel tax is imposed upon the purchaser of the motor fuel, whether purchased in bulk or in the original package, and the amount of any tax so paid by the purchaser and not refunded to him is deductible by the purchaser under section 214(a)3 of the Revenue Act of 1926, in computing his net income, subject, however, to the provision that if the tax is added to or made a part of the business expense of such purchaser it can not be deducted separately as a tax.

Solicitor's Memorandum 3714 (C. B. IV-2, 50) revoked.

An opinion is requested relative to the deductibility, for Federal income tax purposes, of the motor vehicle fuel tax imposed by the State of Wisconsin.

The pertinent provisions of the Wisconsin motor vehicle fuel tax law of 1925 (Wisconsin Statutes, 1925), as amended (Laws of Wisconsin, 1927), are as follows:

78.01. *Purpose of chapter.*—It is the intent of this chapter to impose a tax upon the owners and operators of motor vehicles propelled by an engine or engines driven directly or indirectly by the combustion of motor vehicle fuel, over and upon the public streets, roads and highways, by requiring them to pay for the privilege thereof, in addition to the registration fee, at the rate of 2 cents per gallon for all motor vehicle fuel so used, which tax is to be collected as hereinafter provided. * * *

78.05. *Tax, when collected, original packages.*—Every dealer shall collect from the purchaser, in the first sale in commerce wholly within the State, and pay to the State treasurer, a license tax of 2 cents per gallon on all motor vehicle fuel sold, used or distributed by him in this State, other than such fuel sold by him in the original packages as above specified, unless the tax has already been paid, and shall have the option of paying said tax of 2 cents per gallon on all motor vehicle fuel sold by him in the State in the original packages in which the same was imported. Whenever any sale is made by a dealer in the original packages in which the same was imported, such dealer shall deliver to the purchaser thereof an invoice of such motor vehicle fuel, stating the name and address of the purchaser, the quantity and kind of fuel sold, and whether or not said dealer assumes and agrees to pay the license tax on the said fuel, and such dealer shall transmit to the State treasurer at the same time he shall render the statement required in section 78.04 duplicate copies of all such invoices delivered by him during the period covered by such statement.

78.06. *Tax, when paid; dealer's option; double tax.*—The license tax upon motor vehicle fuel sold or used in any calendar month shall be paid at the same time the statement required by section 78.04 is rendered to the State treasurer, who shall receipt the dealer therefor. If such tax is not paid at the time specified by law, interest shall be charged and collected thereon at the rate of 10 per cent per annum from the time the tax accrued. Every dealer paying such tax or being liable for the payment thereof shall be entitled to charge and collect the sum of 2 cents per gallon on such motor vehicle fuel sold by him, as part of the selling price thereof, * * *

78.07. *Invoice with original package; buyer's report and tax.*—* * * Any person, firm or corporation who shall purchase or receive any motor vehicle fuel from any dealer in this State in the original packages in which the same shall have been imported, and upon which fuel the said dealer shall not have assumed to pay the tax as required by this chapter, shall on the 15th day of each month render to the State treasurer the same statement required of the dealer by section 78.04, and at the same time shall remit and pay to the State treasurer a license tax of 2 cents per gallon on such motor vehicle fuel upon which the dealer has not assumed to pay the tax.

Section 214(a)3 of the Revenue Act of 1926 provides, in part, as follows:

(a) In computing net income there shall be allowed as deductions:

* * * * *

(3) Taxes paid or accrued within the taxable year * * *.

Article 131 of Regulations 65 provides that taxes are deductible as such only by the person upon whom they are imposed.

The sole question in this case is whether the tax imposed by the Wisconsin statute, *supra*, is imposed upon the purchaser of motor vehicle fuel or upon the dealer.

In the opinion of this office the words "pay" and "paid" appearing in the above-quoted sections of the statute do not refer to the payment of the tax in the first instance, but refer to the remittance to the State treasurer of the tax collected by the dealer from the purchaser. It follows that where the statute provides that the dealer may, at his option, pay the tax on fuel sold in the original package, it in reality means that the dealer may, at his option, collect and remit to the State treasurer the tax upon such sales, but that he is not required to do so. In this connection the statute requires the dealer to transmit to the State treasurer invoices of all sales in the original packages, apparently in order that the State treasurer may know whom to hold responsible for the remittance of the tax. This construction is supported by section 78.01, *supra*, wherein it is stated that the intention of the legislature is to impose a tax upon the owners and operators of motor vehicles, etc. The legislative purpose so expressed applies with equal force to both sales of motor fuel in the original package and sales in bulk.

It is, therefore, the opinion of this office that the Wisconsin motor vehicle fuel tax is imposed upon the purchaser of the motor fuel, whether purchased in bulk or in the original package, and that the amount of any tax so paid by the purchaser and not refunded to him is deductible by the purchaser under section 214(a)3, *supra*, in computing his net income, subject, however, to the provision that if the tax is added to or made a part of the business expense of such purchaser it can not be deducted separately as a tax.

Solicitor's Memorandum 3714 is hereby revoked.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

ARTICLE 131: Taxes.
(Also Section 212, Article 23.)

VIII-52-4481
G. C. M. 7235

REVENUE ACT OF 1926.

In the State of Minnesota the liability for real and personal property taxes is incurred on May 1 of each year, and accordingly such taxes accrue on that date for income tax purposes. General Counsel's Memorandum 1236 (C. B. VI-1, 63) is revoked.

A taxpayer on the accrual basis who purchased real property in Minnesota on August 1, 1927, may not set up as of December 31, 1927, an accrued liability for 1927 property taxes thereon and deduct the amount thereof in his 1927 income tax return.

An opinion is requested as to the time of accrual of property taxes in the State of Minnesota.

Reference is made to General Counsel's Memorandum 1236, in which it is held that the real estate taxes imposed by the laws of Minnesota constitute an accrual on the date of the delivery of the tax lists by the county auditor to the county treasurer, as provided in section 2074 of the General Statutes of Minnesota, 1923, and to General Counsel's Memorandum 6273 (C. B. VIII-1, 168), in which it is held that the ownership of property on April 1 of each year is the "event" which determines the liability for property taxes in the State of Illinois, and which fixes the amount thereof, although not ascertainable on that date, and that such taxes accrue on April 1 of each year for income tax purposes.

The pertinent provisions of the General Statutes of Minnesota, 1923, are as follows:

SEC. 1984. All real property subject to taxation shall be listed and assessed every even-numbered year with reference to its value on May 1 preceding the assessment, and all real property becoming taxable any intervening year shall be listed and assessed with reference to its value on May 1 of that year. Personal property shall be listed and assessed annually with reference to its value on May 1, and, if acquired on that day, shall be listed by or for the person acquiring it.

SEC. 2191. The taxes assessed upon real property shall be a perpetual lien thereon, and on all structures and standing timber thereon and on all minerals therein, from and including May 1 in the year in which they are levied, until they are paid; but, as between grantor and grantee, such lien shall not attach until the first Monday of January of the year next thereafter.

There is nothing in the sections quoted to warrant the adoption of a different principle in determining the time of accrual of Minnesota property taxes from that followed in General Counsel's Memorandum 6273. In the opinion of this office, ownership of property on May 1 of each year is the "event" which determines the liability for both real and personal property taxes in Minnesota, and which fixes the amount thereof, although not ascertainable on that date. Accordingly, such taxes accrue on that date for income tax purposes.

The question has been submitted whether a taxpayer on the accrual basis who purchased real property in Minnesota on August 1, 1927, may set up as of December 31, 1927, an accrued liability for 1927 property taxes and deduct the amount thereof in his 1927 income tax return. Since the taxpayer was not the owner of the property on May 1 of that year, when the taxes accrued, and since the ownership of the property on that date was the event which determined the liability for the taxes, the answer must be in the negative. If under the terms of sale the taxpayer assumed the payment of the 1927

property taxes for the period from August 1, 1927, to December 31, 1927, such payment must be treated, for income tax purposes, as a capital expenditure constituting part of the purchase price of the property.

General Counsel's Memorandum 1236, being inconsistent with the position herein taken, is revoked.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

SECTION 214(a)9.—DEDUCTIONS ALLOWED INDIVIDUALS: DEPLETION.

ARTICLE 202: Amount returnable through depletion and depreciation deductions in the case of an operating owner.

REVENUE ACT OF 1926.

Computation basis. (See G. C. M. 6746, page 119.)

SECTION 217.—NET INCOME OF NONRESIDENT ALIEN INDIVIDUALS.

ARTICLE 326: Apportionment of deductions.

VIII-44-4413
G. C. M. 6953

REVENUE ACT OF 1926.

Amendment of General Counsel's Memorandum 3179 (C. B. VII-1, 240).

In view of the conclusion reached in General Counsel's Memorandum 5971 (C. B. VIII-1, 182), General Counsel's Memorandum 3179 (C. B. VII-1, 240) is amended by deleting therefrom the paragraph beginning at the bottom of page 243 and ending on page 244, which reads:

It is the sum of the income assessed under the various heads which forms the statutory income assessable under Schedule D, but the tax charged on such income is charged and paid in respect to the actual income of the year of assessment. Prior to the Finance Act of 1926 no income tax was imposed in respect of any source of income unless the person assessed possessed that source of income during the year of assessment (*National Provident Institution v. Brown*, 8 T. C., 57) or had received income from that source during the year of assessment (*Whalen v. Henning*, 10 T. C., 263). Consequently, the income tax paid for the year of assessment on the statutory income from a particular source was the income tax paid with respect to the actual income from that source arising in the year of assessment.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

SECTION 218.—PARTNERSHIPS.

ARTICLE 335: Partnerships.
(Also Section 223, Article 401.)

VIII-27-4262
I. T. 2477

REVENUE ACT OF 1926.

While the Supreme Court of Michigan has decided that a wife can not enter into a partnership relation with her husband, there

Is ample authority for the proposition that she does not forfeit her capital investment, or her rights to the gains and profits therefrom, by attempting to become a member of a partnership of which her husband is a member. In such a case the wife is entitled to report in her separate income tax returns the gains or profits derived from the use of her separate property in the partnership business or from the sale or other disposition thereof.

Solicitor's Recommendation 7199 (C. B. V-1, 269) revoked in so far as inconsistent herewith.

A ruling is requested relative to the treatment of income received by A and his wife, of ———, Mich., from a business in which they claim they were partners.

A and his wife started the business in 1906 with money given them by the wife's parents. They sold the business in 1927 for x dollars. Each reported one-half of the profits realized from the business as well as from the sale thereof in a separate income tax return.

In Solicitor's Recommendation 7199 it was held that although the wife contributed her separate property to the partnership enterprise, she was not considered a partner with her husband in that business, for the reason that under the law and court decisions of the State of Michigan a wife may not become a member of a partnership with her husband. The income from the partnership enterprise which was credited to the wife's account was, therefore, held to be taxable to the husband.

In the case of *Crossman v. Commissioner* (10 B. T. A., 248, C. B. VII-2, 10), it was held that the income which was credited to Mrs. Crossman on the books of the Crossman Lumber Co. did not represent taxable income to Mr. Crossman. The Board pointed out that, as stated in *Gillespie v. Beecher* (94 Mich., 374), the married woman's act of the State of Michigan was passed for the protection of married women. Its purpose was to enlarge her rights, not to contract them, and it certainly was not meant to deprive her of the right, either acting alone or jointly with others, of protecting her rights in property.

While the Supreme Court of Michigan has decided that a wife can not enter into a partnership relation with her husband, there is ample authority for the proposition that she does not forfeit her capital investment, or her rights to the gains and profits therefrom, by attempting to become a member of a partnership of which her husband is a member. Since, therefore, a part of the money or other property invested in the business carried on by A and his wife was the separate property of the wife, she is entitled to report in her Federal income tax returns the gains or profits derived from the use of her separate property in such business, or from the sale or other disposition thereof, regardless of the fact that under the laws of the State of Michigan she may not enter into a partnership relationship with her husband.

Solicitor's Recommendation 7199 is revoked in so far as it is inconsistent herewith.

ARTICLE 336: Distributive shares of partners.

VIII-36-4387
G. C. M. 6582

REVENUE ACT OF 1926.

For income tax purposes so-called salaries of partners can not be recognized and are not permitted as deductible operating expenses of a partnership. Whatever is received by a partner in the form of salary constitutes a withdrawal from partnership profits or from capital.

Method outlined of determining taxpayer's distributive share of partnership income for 1927 where withdrawals exceeded profits.

An opinion is requested as to the method of determining the distributive share of partnership income for 1927 of A from the M Company.

It is stated that B acquired a 68/100 per cent interest by purchase in the partnership, which interest represented a capital investment 2,050*x* dollars. A owns the remainder, representing an investment of 300,000*x* dollars. In view of the small amount of interest held by B, it was agreed as between the partners that he should receive a salary of 5,000*x* dollars per annum.

It appears that in computing the partnership net income a salary deduction of 12,000*x* dollars paid to A and 5,000*x* dollars paid to B has been claimed, which results in a net operating loss to the partnership of 16,608.03*x* dollars. The partnership return allocates 16,495.10*x* dollars of this loss to A and 112.93*x* dollars to B. A reported in his individual return 12,000*x* dollars as salary and claimed a loss of 16,495.10*x* dollars from the partnership.

The withdrawals of members of a partnership are not allowable deductions as salaries of such members in computing net income of the partnership for income tax purposes. While it is permissible for the partners as between themselves to agree upon salaries, so called, which each partner may be entitled to receive, and while such agreements are not generally open to question by parties not members of the partnership, the fact remains that for income tax purposes so-called salaries of partners can not be recognized and are not permitted as deductible operating expenses of a partnership, for the reason that partners receiving from partnership funds any sums of money necessarily receive such sums either out of the profits made by the partnership or, if there be no sufficient profit made, then out of the capital investment. Partners are working for themselves, and, in contemplation of law, a man may not constitute himself his own employee. (*Estate of S. U. Tilton et al. v. Commissioner*, 8 B. T. A., 914 (C. B. VII-1, 31); appeal of Harriet Taylor, 2 B. T. A., 1159 (C. B. VII-1, 31).) Therefore, whatever is received by a partner in the form of or under the name of salary constitutes nothing more or less than a withdrawal from the partnership of anticipated profits, and if, at the end of the taxable period of the partnership, it is discovered that the total of the amounts so withdrawn by the partners exceeds the apparent profits, it is evident that the true net profit realized is ascertained only by eliminating from the calculation the total amount withdrawn as salary. In the instant case, it appears that the withdrawals totaled 17,000*x* dollars, which, when deducted in the partnership return, produced an apparent net operating loss of 16,608.03*x* dollars. Eliminating the withdrawals as not deductible, an actual net profit from partnership operations in the amount of

391.97*x* dollars is found to have been realized for the taxable period, and, since this amount only is distributable as profit to the partners, any sums in excess thereof withdrawn by them must be considered as withdrawals from capital investment, as there is no other source from which the withdrawals could be derived. The proper method of accounting in this case, for income tax purposes, is that followed by the United States Board of Tax Appeals in the recently reported case of *Augustine M. Lloyd et al. v. Commissioner* (15 B. T. A., 82, C. B. VIII-1, 27), where the controlling facts closely approximated those of the partnership under discussion.

Following the principles there adopted, it results that the taxable net income received by B and A from partnership operations for the taxable period involved is to be ascertained by first allocating the actual net profit of 391.97*x* dollars to the partners in the proportion of their partnership interests, as follows:

	Partnership interests.	Share of profits.
	<i>Per cent.</i>	<i>Dollars.</i>
A.....	99.32	389.30 <i>x</i>
B.....	.68	2.67 <i>x</i>

Deducting these distributable shares from the amounts actually withdrawn by the partners, it is seen that A withdrew 11,610.70*x* dollars and B 4,997.33*x* dollars in excess thereof, which total excess is derived from capital. To the extent that the excess amount withdrawn by a partner represents his personal capital investment it is capital investment of the partner and not taxable income, but to the extent that the excess amount withdrawn is chargeable to the other partner's capital account it is taxable income to the partner receiving it, although deductible by the partner from whose capital investment it is taken. The calculation may be expressed thus:

	Excess withdrawn.	Partnership interest.	Chargeable to own account.	Chargeable to other partner's account.
	<i>Dollars.</i>	<i>Per cent.</i>	<i>Dollars.</i>	<i>Dollars.</i>
A.....	11,610.70 <i>x</i>	99.32	11,531.75 <i>x</i>	78.95 <i>x</i>
B.....	4,997.33 <i>x</i>	.68	33.98 <i>x</i>	4,963.35 <i>x</i>

This latter ascertained balance is derived by each partner from the capital of the other partner. The capital depletion of each partner thus sustained constitutes an allowable deduction to be taken by each partner as an ordinary and necessary expense in carrying on the business. A, then, is entitled to take a deduction of 4,963.35*x* dollars and B a deduction of 78.95*x* dollars.

The net taxable income, then, of B is found by adding his distributive share of the net partnership profits, 2.67*x* dollars, to the amount of the salary paid him out of the capital of A, 4,963.35*x* dollars, making 4,966.02*x* dollars, and from this sum deducting 78.95*x* dollars, which entered into A's salary from B's investment. The net income of B is thus ascertained to be 4,887.07*x* dollars. Calculated

in the same manner, A's taxable income from partnership operations is his distributable share of the net profits, or 389.30*x* dollars, plus 78.95*x* dollars which moves to him from B's capital investment, making a total of 468.25*x* dollars; but, since the sum of 4,963.35*x* dollars has been found to move from A's capital to make up the salary paid B, A had sustained a loss of the difference between these two amounts, or 4,495.10*x* dollars.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

SECTION 219.—ESTATES AND TRUSTS.

ARTICLE 341: Estates and trusts.

REVENUE ACT OF 1926.

Annuity payments to widow in lieu of her dower or statutory interest. (See I. T. 2480, page 141.)

ARTICLE 342: Method of computation of net income and tax.

VIII-47-4433
G. C. M. 7101

REVENUE ACT OF 1926.

In April, 1925, the two children and four grandchildren of C, owners as tenants in common of certain property, entered into a voluntary trust agreement whereby they transferred the property to trustees for the purpose of providing for the widow of C, during her lifetime, one-third of the net income of the property. Upon her death the corpus of the trust was to vest in the children and grandchildren of C in proportions different from their interests in the income during the existence of the trust.

Held, the beneficiaries under the trust are not entitled to deduct from their distributive shares of income for 1925 from the trust a proportionate amount of the depletion sustained by the trust.

An opinion is requested as to whether A and B are entitled to deduct from their distributive shares of income received from the M Trust a proportionate amount of the depletion sustained by the trust for the period April 29 to December 31, 1925.

A and B, the taxpayers, were the daughters of C, who died on December —, 1915, and D, E, F, and G were the grandchildren of C. In 1913 C deeded certain lands to H and K, his sons, as trustees, the deed of trust providing for the distribution of the income from the lands, and also providing that upon the death of both trustees the trust was to terminate and the property covered thereby was to vest, share and share alike, in the children of C or in the issue of any said child who may have died prior to the termination of the trust. The last surviving trustee died on April 15, 1925, and the property then vested one-fourth in B, one-fourth in A, and one-eighth in each of the above-named grandchildren of C.

On April 29, 1925, A, B, and the four grandchildren of C, the owners as tenants in common of the property, entered into a voluntary trust agreement whereby they transferred the property in question to L and D, as trustees, for the purpose of providing for

N, widow of C, during her lifetime, one-third of the net income of the property. The trustees were directed to pay the annual income from the property quarterly as follows: One-third to N, one-sixth to A, one-sixth to B, one-twelfth to D, one-twelfth to E, one-twelfth to F, and one-twelfth to G.

The trust was to terminate upon the death of N, or could be terminated by the trustees, provided, however, that an annuity be purchased in behalf of N based upon a 5 per cent return on one-third of the then fair market value of the trust estate. Certain other provisions, not pertinent here, relative to alternative methods of providing for N during her lifetime were also contained in the trust agreement. Upon termination of the trust, the corpus thereof was to vest immediately as follows: One-fourth in A, one-fourth in B, one-eighth in D, one-eighth in E, one-eighth in F, and one-eighth in G. These interests are in the same proportion as were the interests owned prior to the creation of the voluntary trust on April 29, 1925.

The taxpayers contend that they are entitled to a deduction on account of depletion sustained in 1925 by the trust upon the ground that they were the real owners as tenants in common of the lands which comprised the trust, and that the trust agreement dated April 29, 1925, was in fact in the nature of an agency with the object of securing a satisfactory income to N during her lifetime. The taxpayers have cited the cases of *Julia N. De Forest* (4 B. T. A., 1059, nonacquiescence, C. B. VI-2, 8) and *Trudie T. Munger et al.* (16 B. T. A., 168, see acquiescence, on page 37), in support of their position. The Income Tax Unit contends that the distributive shares of income received by the taxpayers from the M Trust should not be offset by a deduction for the depletion sustained by the trust, and calls attention to the fact that the trust agreement dated April 29, 1925, does not contain any provision authorizing the trustees to withhold from income and add to the corpus of the trust an amount sufficient to provide for depletion sustained.

The Board of Tax Appeals has considered a large number of cases involving a deduction to beneficiaries, or the reduction of their distributive shares of income of a trust, on account of depletion, etc., sustained by the trust, among which are the appeals of *Arthur H. Fleming* (6 B. T. A., 900), *Louise P. V. Whitcomb* (4 B. T. A., 80), *Mary P. Eno Steffanson* (1 B. T. A., 979), *George M. Studebaker* (2 B. T. A., 1020), *Henry Stoddard* (3 B. T. A., 79), *Julia N. De Forest* (4 B. T. A., 1059), and *Trudie T. Munger et al.* (16 B. T. A., 168). The question has also been considered by the courts. (See *Baltzell v. Mitchell*, 3 Fed. (2d), 428, T. D. 3668, C. B. IV-1, 191, and *Mary Roxburghe v. United States*, 64 Ct. Cl., 223, T. D. 4136, C. B. VII-1, 250.) In all of these cases the position of the Bureau was sustained except in the *De Forest* and *Munger* appeals.

The appeal of *Julia N. De Forest*, supra, relied upon by the taxpayers, involved a state of facts materially different from practically all other cases considered by the Board and was decided on the particular facts there under consideration. In that case interests in a certain patent, owned by a number of individuals, were transferred to a trustee in trust for the purpose of enforcing all rights under the patent, collecting the royalties therefrom, paying the necessary

expenses, and turning over the net income to the grantors in proportion to their respective interests during the life of the patent. The beneficial interests in the De Forest case were in no way affected by the so-called trust. The question arose as to whether depreciation on the patent constituted a proper deduction to the individuals. The Board held that inasmuch as the property was only temporarily in the hands of the trustees, and the trust was in the nature of an agency for the benefit of the owners of the property, depreciation should be allowed in determining the net income of the beneficiaries, who were also the remaindermen.

In the appeal of Trudie T. Munger et al., supra, the Board of Tax Appeals held that the beneficiaries were the real owners of the property and as such were entitled to deductions for depreciation and depletion. Although the Commissioner acquiesced in that decision, it may be noted that the Board made the statement that the trust under consideration "was not created for the purpose of preserving or conserving the trust *res*, but for the very opposite purpose of converting the trust *res* into money and the immediate distribution of the cash." The Board pointed out that no beneficial interests were vested or divested by reason of the termination of the trust. It was also stated that the only bars to complete title and ownership were the bare legal title in the trustee and certain powers vested in him which could as well have existed under an irrevocable power of attorney. The beneficial interests in that case appear to have been no different during the period of the trust than after its termination. Such is not true in the instant case, since N had a beneficial interest to the extent of one-third of the income of the trust during her lifetime, and upon her death the trust corpus vested in the children and grandchildren of C in proportions different from their interests in the income during the existence of the trust.

Section 219 of the Revenue Act of 1926, dealing with the taxation of trusts, recognizes that the trust and beneficiary are separate taxable persons. (See also *Merchants' Loan & Trust Co. v. Smietanka*, 255 U. S., 509 (Ct. D. 6), T. D. 3173, C. B. 4, 34.)

In General Counsel's Memorandum 1673 (C. B. VI-1, 252) the following statement was made:

In the instant case the beneficiaries by their own acts created a new taxable entity, namely, the trust estate. Having chosen to take advantage, if any, of the creation of this new taxable entity, they should not be heard to complain because deductions for depletion are allowable to the trust instead of to them.

* * * Where there is income of the trust to distribute and such income is distributed, the beneficiaries, under the law, must pay a tax on the amount actually received. The beneficiaries have no present right in the enjoyment of the corpus of the trust. Their right until the termination of the trust is in the income alone. They are, therefore, interested at this time as beneficiaries in the income, and not in the corpus.

It was also stated in General Counsel's Memorandum 1673, supra, that there is no more reason for ignoring the separate entity doctrine where the beneficiaries and remaindermen are the same than there would be in the case where the beneficiary, the creator, and the remainderman were different individuals. The beneficiaries as beneficiaries are not immediately concerned with the deduction for depletion, inasmuch as depletion is a deduction designed to restore capital and does not affect the distributive share of the beneficiaries.

In I. T. 2218 (C. B. IV-2, 61) the following statement is made:

In no case may beneficiaries, entitled to the income only during the taxable year, take deductions for depreciation of trust property on their individual returns either as a general deduction or as an offset to the full amounts of income distributed or distributable to them.

In the instant case it is clear that N, who was entitled to a share only in the income of the trust during her lifetime and at no time had title to any part of the property placed in trust, could not deduct from her distributive share of the income received from the trust a proportionate amount of the depletion sustained by the trust. The separate trust entity must be recognized in so far as she is concerned, and not to recognize the trust entity in so far as the others are concerned would be inconsistent.

It is the opinion of this office that under the decisions above cited the beneficiaries under the trust here involved are not entitled to deduct from their distributive shares of income for 1925 from the trust a proportionate amount of the depletion sustained by the trust.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

ARTICLE 343: Decedent's estate during administration.

VIII-48-4441
G. C. M. 6906

REVENUE ACTS OF 1924 AND 1926.

Royalties under a coal lease in Pennsylvania, unlimited as to time and giving no right of termination to the lessee, are to be included, after the death of the decedent lessor, in the income of his estate in process of administration.

An opinion is requested on the questions hereinafter set out, arising in connection with the estate of A.

A died in 1920, leaving a will which, after providing for two small bequests, provided in part as follows:

All the rest and remainder and residue of my whole estate, real, personal, and mixed, of whatsoever kind and wheresoever situate, including my coal rents and royalty and interest in coal and coal lands, I give, bequeath, and devise to my son, B.

The questions presented are as follows:

1. Whether the estate of A was in process of administration for the years 1924 to 1926, inclusive, for the purpose of determining income tax liability.
2. Whether the coal royalties passing under the will of A should be taxed to the estate of A, or to B.

The executor contends that the estate of A was in process of administration for the years 1924 to 1926, inclusive, under article 343 of Regulations 65 and 69, Tax Board Recommendation 47 (C. B. 1, 178), Solicitor's Memorandum 1709 (C. B. III-1, 218), and Solicitor's Memorandum 3505 (C. B. IV-1, 183), in view of the following considerations:

1. Complete distribution of the estate was not made during 1926, and the Orphan's Court of ——— County, Pa., as late as May, 1928, deferred the order for final distribution until income tax matters had been finally settled.
2. The overassessment of Federal income tax upon the estate of A for the year 1920 could not be collected by the executor until March, 1926.

3. The income tax liability of the estate for the year 1922 was not finally determined until July, 1927, and subsequent years are still under consideration.

4. Final payment of claims against the Government for overpayments of Federal income tax by A for the years 1916 to 1920, inclusive, was not received until 1927.

5. Collection of the sum of x dollars due the estate from O was not made until the latter part of 1926.

6. The executor collected back interest to March 1, 1926, on certain bonds on which there had been a default in payment of interest and principal.

7. The segregation of the coal properties owned by the M Company, in which company the estate of A was interested as a shareholder, was not finally consummated until 1927.

Article 343 of Regulations 65 and 69 reads in part as follows:

The "period of administration or settlement of the estate" is the period required by the executor or administrator to perform the ordinary duties pertaining to administration, in particular the collection of assets and the payment of debts and legacies. It is the time actually required for this purpose, whether longer or shorter than the period specified in the local statute for the settlement of estates. Where an executor, who is also named as trustee, fails to obtain his discharge as executor, the period of administration continues up to the time when the duties of administration are complete and he actually assumes his duties as trustee, whether pursuant to an order of the court or not.

Solicitor's Memorandum 3505 (C. B. IV-1, 183), in discussing the meaning of this article, states in part as follows:

The administration of the estate of A continued throughout 1920, as a matter of fact. Perhaps it could have been terminated at an earlier date, but this actually was not done. Assets of uncertain and doubtful value had come into the hands of the executors. These were unacceptable to the trustees as a part of the trust estate. Until such assets had been converted into cash or form available for distribution, the executors had not completed their task of collecting the assets of the deceased. The amount of inheritance and income tax liability to the various States and to the Federal Government had not been determined nor the taxes paid. Until this was done the executors had not paid the obligations of the deceased and of his estate. A surplus estate remained in their hands in a form unacceptable to the trustees. Until such surplus was converted in form and transferred to the trust the distribution of assets was not complete.

In the instant case the estate of A was a large and complicated one, and in view of all the facts, the provisions of article 343 of Regulations 65 and 69, and the Bureau rulings cited herein, it is the opinion of this office that the estate of A was in process of administration during the years 1924 to 1926, inclusive.

In connection with the second question, the executor contends that under the law of Pennsylvania the royalties here under consideration are personalty receivable by the executor as proceeds from the sale of coal in place, and are not receivable by the residuary legatee until distributed to him by the executor (citing *Lazarus' Estate*, 145 Pa., 1, 23 Atl., 372; *Robinson v. Pierce*, 278 Pa., 372, 123 Atl., 324; *Birdsall v. Delaware & Hudson Co.*, 244 Fed., 594). The executor further contends that the decisions of the Supreme Court of the United States in *Von Baumbach v. Sargent Land Co.* (242 U. S., 503) and *United States v. Biwabik Mining Co.* (247 U. S., 116) and the decision of the Circuit Court of Appeals in *Rosenberger v. McCaughn* (25 Fed. (2d), 699, T. D. 4171, C. B. VII-2, 253), holding, in substance, that for Federal income tax purposes, mining leases do not constitute a sale of minerals in place, and that the royalties are in-

come to the lessors under the Federal Revenue Acts, can not be considered as overruling the Pennsylvania cases above cited.

The Bureau consistently has taken the position that resort must be had to the State law to determine what must be included in the gross income of an estate for Federal income tax purposes. (S. M. 3256, C. B. IV-1, 186; S. M. 3790, C. B. IV-2, 61; I. T. 2349, C. B. VI-1, 78.) (See also *De Vaughn v. Hutchinson*, 165 U. S., 566.)

The coal leases or agreements from which the royalty income here under consideration was derived are seven in number. Although the instruments differ in detail, they provide in substance for the mining of all the coal (or all the merchantable coal) underlying the tracts of land described in the instruments, they are not limited as to time, and they give no right of termination to the grantees thereunder. The Pennsylvania courts have consistently laid down the principle that leases or demises of this character constitute a sale of the coal in place, and that royalties received thereunder after the death of the grantor are payable as purchase money to his administrators and distributable as personalty to those entitled thereto. This principle has been reviewed at length by the Supreme Court of Pennsylvania in its opinion in the case of *Robinson v. Pierce* (1924), supra, from which the following extract is taken:

In passing upon the conclusion reached, the effect of the agreement made by Robinson in his lifetime must first be considered. Was it a sale of coal in place, or merely a lease providing for the payment of rentals? The former position seems to be conceded as correct by all the parties, and the trial judge, as stated in the oral charge. This construction of the language used was recognized by this court as proper in a prior proceeding involving the same conveyance. (*McKeever v. Westmoreland Coal Co.*, 219 Pa., 234, 68 Atl., 670.) It will be noted that the grant was of all the coal remaining on the land, without fixing the maximum time of taking, though it was provided that a certain amount should be removed, or paid for, each year. Even had a limitation of the term appeared, it would not have been effective to change the character of the transaction, though to be considered in determining the intent of the parties. (Hope's Appeals (Pa.), 3 Atl., 23; *Montooth v. Gamble*, 123 Pa., 240, 16 Atl., 594; *Kingsley v. Hillside Coal & Iron Co.*, 144 Pa., 613, 23 Atl., 250.) The construction applied is not altered by the use of the word "lease" in the agreement (*Dorr v. Reynolds*, 26 Pa. Super. Ct., 139; *Millard v. Delaware, Lackawanna & Western Railroad Co.*, 240 Pa., 234, 87 Atl., 607; *Turner v. Coal Co.*, 34 Pa. Super. Ct., 101); or the limitation of the right to take only "merchantable coal" (*Lillibridge v. Lackawanna Coal Co.*, 143 Pa., 293, 22 Atl., 1035, 13 L. R. A., 627, 24 Am. St. Rep., 544; *Millard v. Delaware, Lackawanna & Western Railroad Co.*, supra); or the designation of the sums to be paid as rentals (*Lazarus' Estate*, supra); nor does the insertion of a forfeiture clause affect the conclusion reached (*Sanderson v. Scranton*, 105 Pa., 469; *Delaware, Lackawanna & Western Railroad Co. v. Sanderson*, 109 Pa., 583, 1 Atl., 394, 58 Am. Rep., 743).

If the transfer by Robinson constituted a sale in place, and we so hold, the payments of royalties or rents are to be treated as purchase money, and for the purpose of distribution considered as personalty. (*Hosack v. Crill*, 18 Pa. Super. Ct., 90, affirmed 204 Pa., 97, 53 Atl., 640; *Dorr v. Reynolds*, supra; Hope's Appeals (Pa.), supra; *Fairchild v. Fairchild* (Pa.), 9 Atl., 255; Murray's Estate, 216 Pa., 270, 65 Atl., 675.) The same rule is invoked as in the case of conveyances of, or agreements to convey, real property, executed during the lifetime of the decedent; the payments stipulated being payable thereafter to the executor or administrator. (13 C. J., 855; 11 R. C. L., 108; *Helsel's Estate*, 255 Pa., 612, 100 Atl., 462; *Bender v. Luckenbach*, 162 Pa., 18, 29 Atl., 295, 296; *Drenkle's Estate*, 3 Pa., 377.)

In the case of *Birdsall v. Delaware & Hudson Co.*, supra, where the question was whether the executors or residuary legatees should receipt for the payment of royalties made by the lessee companies,

the court found that the royalties passed to the executor. The opinion reads in part as follows:

It has been decided that royalties under a coal lease are in the nature of purchase money of real estate, and that the right to collect the same vests in the personal representatives of a deceased lessor, and not in his heirs or devisees of the land. (Lazarus' Estate, 145 Pa., 1, 23 Atl., 372; McFadden's Estate, 224 Pa., 443, 73 Atl., 927.) It is equally well settled that, regarding assets or choses in action not administered by an executor of a decedent, the right to administration upon such remaining assets, upon the death of such executor, remains in the estate, and must be administered by an administrator de bonis non. (Wagner's Estate, 227 Pa., 460, 76 Atl., 215.)

Until it is conclusively determined that all accounts have been settled and claims of creditors discharged, it may be assumed that the estate is in process of settlement, and, until complete settlement has been made, it will not be possible to determine whether the residuary legatees receive any portion of these royalties, or, in fact, any other portion of the estate of their decedent. Therefore, the executors, Robert A. Jadwin, Mary B. Manville, and Lilian Jadwin, and not the residuary legatees, are entitled to receipt for their decedent's interest in the judgment and should be parties to the release on payment of the same by defendant.

The Supreme Court of the United States in *Von Baumbach v. Sargent Land Co.*, supra, and *United States v. Biwabik Mining Co.*, supra, and the Circuit Court of Appeals in *Rosenberger v. McCaughn*, supra, held that the Minnesota and Pennsylvania mining leases in those cases, for Federal income tax purposes, were not to be considered as effecting a sale of ore in place, and that the moneys derived from the leases and paid under the instruments were not converted capital and did not constitute the purchase price of the ore in question, but were royalties or rents and as such were income under the Revenue Acts. The Federal courts in the cases above enumerated decided that mining royalties are income under the Revenue Acts (which is conceded by the taxpayer in the instant case), but did not pass upon the question of whether such income, in a case similar to the instant case, would go to the executor of a decedent, or directly to his devisees or legatees.

In view of the foregoing, it is the opinion of this office that the royalties here under consideration are to be included in gross income under the Revenue Acts, but that the income is income to the estate of A and taxable to it.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

SECTION 223.—INDIVIDUAL RETURNS.

ARTICLE 401: Individual returns.

REVENUE ACT OF 1926.

Profits derived from use of wife's separate property in a Michigan partnership enterprise, or from the sale or other disposition thereof. (See I. T. 2477, page 228.)

PART III.—CORPORATIONS.

SECTION 231.—CONDITIONAL AND OTHER
EXEMPTIONS OF CORPORATIONS.

ARTICLE 522: Farmers' or other mutual hail,
cyclone, casualty, or fire insurance com-
panies or associations.
(Also Section 234, Article 568.)

VIII-37-4350
G. C. M. 6782

REVENUE ACT OF 1926.

Where a State law expressly requires insurance companies writing certain kinds of insurance to have a fully paid up guaranty capital represented by shares, for Federal income tax purposes such companies are not mutual insurance companies within the contemplation of section 231(11) of the Revenue Act of 1926 and are not entitled to the deductions allowed by section 234(a), paragraphs (9) and (11), of that Act.

The M Liability Insurance Co. is a corporation organized under private and general laws of the State of R. The company was incorporated as a mutual insurance company without capital stock, under a private law of the State of R, its charter being subsequently amended under the general laws of that State. The company was originally chartered for the purpose of writing employees' liability insurance, which purpose and authority were later extended to include workmen's compensation insurance and the various kinds of automobile insurance and other insurance authorized by the State's general laws. In order to qualify to write fidelity bonds or insurance under the State's general laws, it was necessary for the company to have a fully paid up guaranty capital of not less than x dollars. To meet this requirement the policyholders of the company on February —, 1926, voted to approve the creation and issuance of such guaranty capital in the amount of x dollars, the statutory minimum. The rights of the holders of the shares of guaranty capital are defined by statute and are, in substance, as follows:

(a) The right to a dividend, limited to — per cent semiannually, if unused premiums left after all expenses, losses and liabilities then incurred are provided for, shall be sufficient to pay the same;

(b) The right to have all other assets of the company, other than uncollected premiums, exhausted before the fund created by the guaranty capital is drawn upon for the payment of losses;

(c) The right to have this fund restored by assessment upon the policyholders whenever the fund may be thus impaired;

(d) The right to vote with the policyholders at all meetings of the company according to the number of shares held;

(e) The right to have one-half of the members of the board of directors selected from their own number by vote of the policyholders and holders of guaranty capital;

(f) The right to return of their investment on dissolution of the company or retirement of the guaranty capital but with no participation in the assets or income of the company beyond the par value of the guaranty capital and such dividend as may be due in accordance with (a) above; and,

(g) Subject to the right of the policyholders, the right to retire the entire guaranty capital under the terms of the general laws of the State.

On these facts the question is presented whether the company is entitled to exemption under section 231(11) of the Revenue Act of 1926, and, if not, whether it is entitled to the deductions allowed mutual insurance companies, other than life, by section 234(a), paragraphs (9) and (11), of the Revenue Act of 1926.

Speaking with respect to the characteristics of mutual insurance companies, the Supreme Court in the case of *Penn Mutual Life Insurance Co. v. Lederer* (252 U. S., 523, T. D. 3046, C. B. 3, 249) said:

* * * In a mutual company, whatever the field of its operation, the premium exacted is necessarily greater than the expected cost of the insurance, as the redundancy in the premium furnishes the guaranty fund out of which extraordinary losses may be met, while in a stock company they may be met from the capital stock subscribed. It is of the essence of mutual insurance that the excess in the premium over the actual cost as later ascertained shall be returned to the policyholder.

* * * Mutual fire, mutual marine, and mutual life insurance companies are analogous in that each performs the service called insuring wholly for the benefit of their policyholders, and not like stock insurance companies in part for the benefit of persons who, as stockholders, have provided working capital on which they expect to receive dividends representing profits from their investment. * * *

This statement of the Supreme Court is peculiarly appropriate, if not conclusive, in the instant case, for the reason that the court was speaking of mutual insurance companies contemplated by Section II G(b) of the Revenue Act of 1913, the provisions of which were in substance reenacted as section 234(a), paragraphs (9) and (11), of the Revenue Act of 1926.

In the case of *Dwinnell et al. v. Minneapolis Fire & Marine Insurance Co. et al.* (87 Minn., 59, 91 N. W., 266, 267), the Supreme Court of Minnesota, speaking with respect to the right of a mutual insurance company to provide a guaranty fund on capital stock, said:

* * * Treating it as a mutual company, the first question with which we are confronted is whether such an insurance company, incident to its general power to do an insurance business, has authority to create and provide a capital stock or guaranty fund for the payment of losses. The feature distinguishing a mutual insurance company from all others is that in the mutual company the policyholders are at once the insurers and the insured; in all others the policyholder is the insured and the company the insurer. * * * the question presented is whether the power to create such a fund is one of the incidental powers of such a corporation. This question came before the Supreme Court of the State of Wisconsin in the case of *Kenman v. Rundie* (81 Wis., 212, 51 N. W., 426), where the court in a very able and clear opinion held that such a corporation had no power to create such a fund; that to permit it to do so would be to change wholly the character of the corporation and destroy the mutuality principle upon which it is founded. It was there said: "It therefore follows that if the money to be paid in for losses and expenses is to be raised through such a guaranty fund, or by other extraneous means, and the members of the company are thereby exempted from assessments and the payment of their pro rata shares of such losses and expenses proportionate to their insurance, the essential feature of the mutuality is entirely destroyed and the company ceases to be a mutual insurance company." The same conclusion was reached in *Insurance Co. v. McKelway* (12 N. J. Eq., 133); and the decision there made was followed and approved in *Barriclo v. Insurance Co.* (13 N. J. Eq., 154), *Trust Co. v. Miller* (33 N. J. Eq., 160), and in *Morris & E. R. Co. v. Sussex R. Co.* (20 N. J. Eq., 564). * * *

It is true that the statutes of the State of R, under which the company in the instant case was organized and is operated, expressly require the creation of a guaranty fund in the case of insurance companies writing certain kinds of insurance and treat such companies as mutual insurance companies notwithstanding. However, this is the result of an express statutory authorization or requirement and involves a departure from the common law concept of a mutual insurance company as announced by the courts as well as the Bureau. In the latter connection, attention is invited to Treasury Decision 4053 (C. B. VI-2, 292) and the ruling of the Bureau in the case of the M Life Insurance Co., in which a life insurance company operated in a manner substantially similar to the instant one was held not to be a mutual insurance company. (I. T. 2423, C. B. VII-2, 320.) The Bureau in these instances deals with life insurance companies. However, there is no fundamental distinction between a mutual life insurance company and mutual insurance companies other than life which would justify a different rule in the case of the latter companies. (*Penn Mutual Life Insurance Co. v. Lederer*, supra.) Furthermore, the Bureau has uniformly refused to accept as conclusive under Federal revenue laws the status accorded insurance companies by a State statute or officer. In this connection see Solicitor's Memorandum 5501 (C. B. V-1, 102) and the opinion of the court in the case of *Louisville Title Co. v. Lucas* (27 Fed. (2d), 413, T. D. 4233, C. B. VII-2, 388); also *Burk-Waggoner Oil Association v. Hopkins* (269 U. S., 110, 114, T. D. 3790, C. B. V-1, 147).

In view of the foregoing, it is concluded that the M Liability Insurance Co. is not a mutual insurance company within the contemplation of section 231(11) of the Revenue Act of 1926, and that it is not entitled to the deductions allowed by section 234(a), paragraphs (9) and (11), in the case of mutual insurance companies taxable under section 230 of that Act, but is subject to the tax imposed "upon the net income of every insurance company (other than a life or mutual insurance company)" by section 246 of the Revenue Act of 1926.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

SECTION 234.—DEDUCTIONS ALLOWED CORPORATIONS.

ARTICLE 568: Deductions allowed mutual insurance companies other than life insurance companies.

REVENUE ACT OF 1926.

Companies required by State law to have a fully paid up guaranty capital represented by shares. (See G. C. M. 6782, page 209.)

SECTION 238.—CREDIT FOR TAXES IN CASE
OF CORPORATIONS.

ARTICLE 611: Credit for foreign taxes.
(Also Section 240, Article 631.)

VIII-30-4284
G. C. M. 6640

REVENUE ACTS OF 1921, 1924, AND 1926.

The credit for foreign taxes allowable in the case of an affiliated group of corporations is required to be computed on a consolidated basis under the express terms of section 240, which requires the total tax to be assessed to be computed in the first instance as a unit.

An opinion is requested whether in cases where consolidated returns are filed the credit for foreign taxes should be computed on a separate or on a consolidated basis under the Revenue Acts of 1921, 1924, and 1926.

Careful consideration has been given to the question involved in the light of the arguments presented as to why the separate basis should be followed and of the exhibits which illustrate both methods of computation.

Section 240 of the Revenue Act of 1921 (so far as any taxable year beginning on or after January 1, 1922, is concerned) and section 240 of the Revenue Acts of 1924 and 1926 provide that corporations which are affiliated may make separate returns or, "under regulations prescribed by the Commissioner with the approval of the Secretary, make a *consolidated return* of net income for the purpose of this title, *in which case the taxes thereunder shall be computed and determined upon the basis of such return,*" and that—

(b) In any case in which *a tax is assessed* upon the basis of a consolidated return, *the total tax* shall be computed in the first instance as a unit and shall *then* be assessed upon the respective affiliated corporations in such proportions as may be agreed upon among them, or, in the absence of any such agreement, then on the basis of the net income properly assignable to each. [Italics supplied.]

Article 631 of Regulations 62, 65, and 69 provides that consolidated returns are based upon the principle of levying the tax according to the true net income of a single enterprise, even though the business is operated through more than one corporation.

One contention made is that the credit allowed in section 238 is allowed to the taxpayer, and that each separate corporation in the group is a taxpayer. In the opinion of this office, the question does not turn on whether the affiliated group is the taxpayer or whether the separate members are the taxpayers. The correct tax to be assessed and paid is required to be determined on the basis of the consolidated return. If it were not for the provision in section 240(b), the tax would be assessed in one amount.

The expressions "the taxes thereunder," "a tax is assessed," and "the total tax" used in section 240 refer to the tax which is to be assessed by the Commissioner and paid by the group. This amount can not be determined until the credit for foreign taxes allowable has been taken against the tax computed on the aggregate net income less the specific exemption allowable, if any. It is plainly the purpose of section 240 of the various Revenue Acts involved to permit an affiliated group of corporations to elect to be treated as a single enterprise, in which case the tax due from such enterprise on its net income

is to be computed in the same manner that it would be computed if the enterprise were one corporation. The law is mandatory in requiring that the total tax in the first instance be computed as a unit. This total tax is then to be assessed upon the respective affiliated corporations in such proportions as may be agreed upon among them or in the absence of any such agreement then on the basis of the net income properly assignable to each.

One of the very important items entering into the amount of tax to be assessed is the credit for taxes paid to foreign countries. The amount of the credit allowable is directly dependent upon the net income from sources without the United States included in total net income on which the tax is computed. Where losses have been brought into a consolidated return by one member it operates to reduce the income of the other members so that net income from foreign sources or net income from domestic sources, perhaps both, will be reduced in the case of the other members. A computation of the credit allowable on a separate basis in such a case would result in allowing as a credit to one member the amount which it would have been entitled to claim if a separate return had been filed, notwithstanding the fact that a part of its net income had been wiped out by losses of other members, but the amount of the credit thus computed would be credited against the tax allocable to such corporation on the basis of the consolidated return. The effect would be to allow the corporation a credit based on foreign income which had been wiped out in whole or in part by losses. Section 238 does not authorize a credit computed in such a manner.

It is the opinion of this office that the credit for foreign taxes allowable in the case of an affiliated group of corporations is required to be computed on a consolidated basis under the express terms of section 240, which requires the total tax to be assessed to be computed in the first instance as a unit.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

SECTION 240.—CONSOLIDATED RETURNS OF CORPORATIONS.

ARTICLE 631: Affiliated corporations.

REVENUE ACT OF 1926.

Computation of credit for foreign taxes. (See G. C. M. 6640, page 212.)

SECTION 246.—TAXES ON INSURANCE COMPANIES.

ARTICLE 691: Tax on insurance companies.

VIII-43-4404
G. C. M. 6988

REVENUE ACT OF 1926.

The income of the M Company is primarily derived from its bond sales service and the incidents thereto. A small part only of its income is received from title insurance business. The company is not an insurance company within the meaning of section 246, Revenue Act of 1926.

An opinion is requested as to whether the M Company is an insurance company within the purview of section 246, Revenue Act of 1926.

The company was incorporated under an act to provide for the regulation and incorporation of insurance companies and to regulate the transaction of the insurance business. Pursuant to this law, it is regularly supervised by the insurance department of the State of R, and files annual statements with the insurance commissioner. The company is authorized to transact the business of making insurance against loss or damage on account of encumbrances upon or defects in titles to real property; to take, buy, sell, and deal in first mortgages on real estate; and to issue bonds, debentures, and certificates against such mortgages. The company lends its funds on real estate the title to which it insures. Against the mortgages which the company acquires it issues bonds, which it sells, guaranteeing the purchaser against any loss which may result from the nonpayment of principal and interest.

The fact that a particular company makes reports to the State insurance department or is under the jurisdiction and control of such department is not conclusive of its status as an insurance company under the Federal Revenue Acts. In the determination of this question the entire business conducted by the company must be considered and the nature of the contracts it issues must be examined with regard to the purpose or object for which they are made. If the contracts issued are contracts of insurance, it follows that any corporation issuing such contracts and not engaging in any other distinctive line of business is an insurance company within the meaning of section 246, Revenue Act of 1926.

It appears from the annual statement filed by the M Company with the State of R department of banking and insurance for the year 1927 that the income of the company from title insurance business amounted to x dollars and that its income from its bond sales service and the incidents thereto amounted to 512 x dollars. It is apparent from the foregoing that the income of the company, other than investment income, is derived primarily from its bond sales service. The guaranty to the purchaser of the bonds against loss resulting from nonpayment of principal and interest is an incident to the bond sales service and is not an insurance contract. (*Louisville Title Co. v. Lucas, Collector*, 27 Fed. (2d), 413, T. D. 4233, C. B. VII-2, 389, 393.) It is clear, therefore, that only a small part of the company's income is derived from the issuance of contracts of insurance or activities incidental thereto.

It is accordingly the opinion of this office that the M Company is not an insurance company within the purview of section 246, Revenue Act of 1926.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

PART IV.—ADMINISTRATIVE PROVISIONS.

SECTION 257.—RETURNS TO BE PUBLIC RECORDS.

ARTICLE 1090: Inspection of returns.

VIII-39-4368

T. D. 4272

Income tax—Inspection of returns—Article 1090 of Regulations 69 amended.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, D. C.

To Collectors of Internal Revenue and Others Concerned:

Article 1090 of Regulations 69 is hereby amended by adding at the end thereof the following:

Under date of July 23, 1928, paragraph numbered 10 of the foregoing regulations was amended with the approval of the President to read as follows:

"10. The return of a corporation shall be open to inspection by the president, vice president, secretary, or treasurer of such corporation, or, if none, by any of its principal officers, upon satisfactory evidence of identity and official position, or by the duly constituted attorney in fact of such officer. The return of a corporation which has since been dissolved shall, in the discretion of the Commissioner of Internal Revenue, be open to inspection to any person who under these regulations might have inspected the return at the date of dissolution."

Under date of March 14, 1929, the foregoing regulations were amended with the approval of the President by the addition thereto of the following paragraph:

"20. The Commissioner of Internal Revenue shall cause to be prepared a written decision in every case in which an overassessment (whether resulting in a refund, credit, or abatement) of an income, war-profits, excess-profits, estate, or gift tax is allowed, in excess of \$20,000, and such decision shall be considered a public record and shall be open to inspection, during regular hours of business, in the office of the Commissioner of Internal Revenue or such office as he may designate. Such decision shall give the amount of the overassessment and shall be accompanied by a brief summary of the relevant facts and a citation of the authorities applicable thereto, or, in a case in which a decision of a court or of the Board of Tax Appeals has become final, by a citation of the court or Board decision. Under no circumstances shall the provisions of this paragraph be construed as making any return, or any part thereof, open to inspection, or as authorizing the source of any income, gains, or profits, or the specific transactions resulting in losses or expenditures, to be made public; nor shall any of the information contained in any return or relating thereto be made public except in accordance with, and to the extent necessary in carrying out, these regulations."

ROBT. H. LUCAS,
Commissioner of Internal Revenue.

Approved September 20, 1929.

OGDEN L. MILLS,
Acting Secretary of the Treasury.

SECTION 270.—DATE ON WHICH TAX SHALL BE PAID.

ARTICLE 1202: Extension of time for payment of the tax or installment thereof.

REVENUE ACT OF 1926.

Contract of suretyship of parent corporation on behalf of subsidiary. (See G. C. M. 6801, page 125.)

SECTIONS 273 AND 274.—DEFICIENCY IN TAX.

ARTICLE 1234: Extension of time for payment
of a deficiency.

VIII-41-4383
G. C. M. 6872

REVENUE ACT OF 1926.

Federal farm loan bonds are not obligations of the United States and may not be accepted as security in connection with a bond filed under the provisions of section 274(k) of the Revenue Act of 1926.

An opinion is requested as to whether Federal farm loan bonds may be accepted as security in connection with bonds filed under the provisions of section 274(k) of the Revenue Act of 1926.

Section 274(k) of the Revenue Act of 1926 reads in part as follows:

Where it is shown to the satisfaction of the Commissioner that the payment of a deficiency upon the date prescribed for the payment thereof will result in undue hardship to the taxpayer the Commissioner, with the approval of the Secretary (except where the deficiency is due to negligence, to intentional disregard of rules and regulations, or to fraud with intent to evade tax), may grant an extension for the payment of such deficiency or any part thereof for a period not in excess of 18 months. If an extension is granted, the Commissioner may require the taxpayer to furnish a bond in such amount, not exceeding double the amount of the deficiency, and with such sureties, as the Commissioner deems necessary, conditioned upon the payment of the deficiency in accordance with the terms of the extension. * * *

To aid in carrying out the provisions of the foregoing section, article 1234 of Regulations 69 provides in part as follows:

Extension of time for payment of a deficiency.—Where it is shown to the satisfaction of the Commissioner that the payment of a deficiency upon the date or dates prescribed for payment thereof will result in undue hardship to the taxpayer, the Commissioner, with the approval of the Secretary, may grant an extension of time for the payment of the deficiency or any part thereof for a period not in excess of 18 months. * * *

* * * * *
As a condition to the granting of such an extension, the Commissioner may require the taxpayer to furnish a bond in an amount not exceeding double the amount of the deficiency. If a bond is required it must be filed with the collector within 10 days after notification by the Commissioner that such bond is required. It shall be conditioned upon the payment of the deficiency, interest, and additional amounts assessed in connection therewith in accordance with the terms of the extension granted, and shall be executed by a surety company holding a certificate of authority from the Secretary of the Treasury as an acceptable surety on Federal bonds, and shall be subject to the approval of the Commissioner. In lieu of such a bond, the taxpayer may file a bond secured by deposit of Liberty bonds or other bonds or notes of the United States equal in their total par value to an amount not exceeding double the amount of the deficiency. * * *

Section 1126 of the Revenue Act of 1926, so far as here pertinent, reads as follows:

Wherever by the laws of the United States or regulations made pursuant thereto, any person is required to furnish any recognizance, stipulation, bond, guaranty, or undertaking, hereinafter called "penal bond," with surety or sureties, such person may, in lieu of such surety or sureties, deposit as security with the official having authority to approve such penal bond, United States Liberty bonds or other bonds or notes of the United States in a sum equal at their par value to the amount of such penal bond required to be furnished, together with an agreement authorizing such official to collect or sell such bonds or notes so deposited in case of any default in the performance of any of the conditions or stipulations of such penal bond. The acceptance of such United States bonds or notes in lieu of surety or sureties required by law shall have the same force and effect as individual or corporate sureties, or certified

checks, bank drafts, post-office money orders, or cash, for the penalty or amount of such penal bond. * * *

It is apparent from the above-quoted provisions of sections 274(k) and 1126 and of article 1234 that if a taxpayer desires an extension of time in which to pay a deficiency in tax, the Commissioner, as a condition to the granting of such extension, may require the taxpayer to furnish a bond with approved sureties, or in lieu thereof, a bond secured by a deposit of "United States Liberty bonds or other bonds or notes of the United States." The question then arises as to whether the bonds issued by Federal land banks are "bonds or notes of the United States."

Under the provisions of the Act of July 17, 1916 (ch. 245, 39 Stat. L., 360), Federal farm loan bonds are bonds issued by Federal land banks with the approval of the Federal Farm Loan Board. These bonds are obligations of the Federal land banks and are secured either by a deposit of United States Government bonds or by mortgages on farm lands, securing loans made by such banks, deposited by the banks with the Federal Farm Loan Board. Section 21 of the Act of July 17, 1916, states that all Federal land banks are liable for the payment of each bond. It is apparent that these bonds are obligations of the Federal land banks, secured either by deposit of farm land mortgages or by deposit of United States Government bonds, and are not obligations of the United States Government. It is true that section 26 of said Act provides that the bonds are to be deemed instrumentalities of the Government, and that all income derived therefrom shall be exempt from Federal, State, municipal, or local taxation, but it is quite obvious that, although these obligations may be instrumentalities of the Government in carrying out its policy of aiding agriculture, such bonds can in no wise be deemed to be obligations of the Government (compare O. D. 1069, C. B. 5, page 278). As these obligations are not obligations of the United States, they are not "bonds or notes of the United States" as that term is used in article 1234 of Regulations 69, or as used in section 1126 of the Revenue Act of 1926, and accordingly they may not be accepted as security in connection with a bond filed under the provisions of section 274(k) of the Revenue Act of 1926.

C. M. CHAREST,

General Counsel, Bureau of Internal Revenue.

ARTICLE 1234: Extension of time for payment
of a deficiency.

VIII-52-4482
I. T. 2514

REVENUE ACT OF 1926.

General Counsel's Memorandum 6872 (see on page 216), holding that although Federal farm loan bonds issued under the Act of July 17, 1916 (39 Stat., 360), are instrumentalities of the Government, such bonds are not obligations of the Government, applies with equal force to joint stock land bank bonds issued under authority of the Federal Farm Loan Act.

A taxpayer makes the following inquiries with respect to General Counsel's Memorandum 6872, in which it is held that Federal farm loan bonds, while instrumentalities of the Government, are not obligations of the United States:

1. Whether Federal farm loan bonds are not in fact obligations of the United States as well as instrumentalities of the Government, and

2. Whether the conclusion reached in General Counsel's Memorandum 6872 applies to joint stock land bank bonds as well as Federal farm loan bonds.

As to the first question, it is held that Federal farm loan bonds are executed by the proper officers of the issuing banks and do not purport to be obligations of the United States. While it is true that the bonds do state, as is provided by the Act of July 17, 1916 (39 Statutes at Large, 360), that Federal farm loan bonds issued under the provisions of this Act shall be deemed and held to be instrumentalities of the Government, and that as such they and the income derived therefrom shall be exempt from Federal, State, municipal, or local taxation, yet, as pointed out in the memorandum of the General Counsel, this does not make such bonds obligations of the United States.

As to the second question, it is held that while the memorandum mentioned was concerned with Federal farm loan bonds only, the conclusions reached therein apply with equal force to joint stock land bank bonds issued under authority of the Federal Farm Loan Act.

SECTIONS 277 AND 278.—PERIOD OF LIMITATION UPON ASSESSMENT AND COLLECTION OF TAX.

ARTICLE 1272: Period of limitation upon collection of tax.

VIII-43-4405
Ct. D. 125

INCOME TAX—REVENUE ACT OF 1926—DECISION OF COURT.

1. COLLECTION—LIMITATION—WAIVER.

Where the right to assess and collect taxes for the year 1920, which would otherwise expire on April 14, 1926, is extended by an agreement in writing to December 31, 1926, an assessment made before the latter date by virtue of the agreement may be collected within six years from the date of such assessment, as provided by section 278(d) of the Revenue Act of 1926.

2. WAIVER—CONSIDERATION—VALIDITY.

An agreement in writing between the Commissioner and a taxpayer that a tax may be assessed or collected after the prescribed statutory period requires only a consent and need not be supported by a consideration in order to be valid.

UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

Loewer Realty Co., plaintiff, v. Charles W. Anderson, Individually and as Collector of Internal Revenue of the United States, defendant.

In error to the District Court of the United States for the Southern District of New York by Loewer Realty Co. against a collector of internal revenue to recover income taxes claimed to have been erroneously assessed and collected; judgment for plaintiff, and defendant brings error. Reversed.

[March 11, 1929.]

OPINION.

AUGUSTUS N. HAND, Circuit Judge: The question before us is whether the taxes were exacted at a time when the right to collect them was barred by the statute of limitations.

When the taxpayer's return was filed on April 14, 1921, the Revenue Act of 1918 was in effect. That Act (section 250(d)) provided that the amount of the tax should be assessed by the Commissioner within five years after the return was made and that no suit or proceeding for collection should be begun after five years after the date when the return was due or was made. The Revenue Act of 1921 (section 250(d)) contained similar provisions relating to the assessment and collection of taxes due under prior income tax Acts, and provided that taxes for prior years should be assessed within five years after the return was filed unless the Commissioner and taxpayer consented to a later assessment, and added that "no suit or proceeding for the collection of any such taxes * * * shall be begun, after the expiration of five years after the date when such return was filed." When the waiver was signed in December, 1925, about four months still remained under both the Act of 1918 and the Act of 1921 within which the collector might assess and collect the additional taxes.

Prior, however, to the time when the waiver was obtained the Revenue Act of 1924 had taken effect. By that Act it was similarly provided in section 277(a)2 that income taxes imposed by prior Acts should be assessed within five years after the return was filed. It also provided in section 278(c) that where the Commissioner and the taxpayer consented in writing to the assessment of the tax after the time prescribed in section 277 for its assessment, the tax may be assessed at any time prior to the expiration of the period agreed upon. In section 278(d) the Act went on to say that where the assessment of the tax was made within the period prescribed in section 277 "or in this section," the tax might be collected by a proceeding begun within six years after the assessment of the tax. It is entirely clear that the words "or in this section" were placed in the statute in order to give the Government six years within which to collect the tax after an assessment made either within five years succeeding the filing of the return or within any extended period agreed to by the Commissioner and the taxpayer. So, when the waiver was signed on December 21, 1925, it had full warrant under section 278(c) of the Act of 1924. By its terms, the Commissioner had until December 31, 1926, to make the assessment for additional taxes, and he made the assessment in July, 1926, and collected the tax in September, 1926, while the time called for by the waiver was still running.

But on February 26, 1926, a new Revenue Act went into effect, known as the "Revenue Act of 1926." That Act provided that assessment of income taxes imposed under prior Acts should be assessed within five years after the return was filed. It went on in section 278 (c), (d), and (e) to say:

"(c) Where both the Commissioner and the taxpayer have consented in writing to the assessment of the tax after the time prescribed in section 277 for its assessment the tax may be assessed at any time prior to the expiration of the period agreed upon.

"(d) Where the assessment of any income, excess-profits, or war-profits tax imposed by this title or by prior Act of Congress has been made (whether before or after the enactment of this Act) within the statutory period of limitation properly applicable thereto, such tax may be collected by distraint or by a proceeding in court (begun before or after the enactment of this Act), but only if begun (1) within six years after the assessment of the tax, or (2) prior to the expiration of any period for collection agreed upon in writing by the Commissioner and the taxpayer.

"(e) This section shall not bar a distraint or proceeding in court begun before the enactment of the Revenue Act of 1924, nor shall it authorize the assessment of a tax or the collection thereof by distraint or by proceeding in court (1) if at the time of the enactment of this Act such assessment, distraint or proceeding was barred by the statutory period of limitation properly applicable thereto, unless prior to the enactment of this Act the Commissioner and the taxpayer agreed in writing thereto, or (2) contrary to the provisions of subdivision (a) of section 274 of this Act."

It is contended by the plaintiff that section 278(d) of the Act of 1926 precluded the collection of any tax that had not been assessed within five years after the filing of the return and this because of the words "within the statutory period of limitation properly applicable thereto." But such an interpretation gives no effect whatever to section 278(c), providing in substance that where a waiver is signed "the tax may be assessed at any time prior to the expiration of the period agree upon." It also involves a complete change

in legislative policy over the Act of 1924, although the language of section 278(c) in the two Acts providing for a consent in writing to the assessment of the tax after the time prescribed in section 277 is identical.

Statutes of limitation barring the collection of taxes must receive a strict construction in favor of the Government. Limitation will not be presumed in the absence of clear congressional action. (*E. I. DuPont de Nemours & Co. v. Davis*, 264 U. S., 462; *Bowers v. N. Y. & Albany Co.*, 273 U. S., 349 [T. D. 4009, C. B. VI-1, 268].) But it is not necessary to invoke such a rule here. The plain purpose of section 278 of the Act of 1926, as that of section 278 of the Act of 1924 and section 250(d) of the Act of 1921, was to give the Commissioner additional time to assess taxes if he could obtain the consent of the taxpayer. Plaintiff's interpretation of the Act of 1926 would render the consent valueless. But it is perfectly consonant with the language of section 278(c) to say that the words "statutory period of limitation applicable thereto" were intended to include both the five years allowed to make the assessment where no extension had been agreed to and the five years, plus the extended period, in case a waiver had been signed. Each period is "statutory," for the statute provides for them both. In our opinion, a fair reading of the Act of 1926 shows that the Commissioner was within his rights in making the assessment within the extended period and that the collector was authorized to require payment of the taxes within six years after such an assessment. (*Florsheim Bros. Dry Goods Co. v. United States*, 29 Fed. (2d), 895 [Ct. D. 35, C. B. VIII-1, 209].) See also *United States v. Crook* (18 Fed. (2d), 449).

It is objected that the waiver was without consideration, but the statute requires nothing but a consent without mentioning consideration, and the taxpayer should not in any event be allowed to repudiate a consent upon which the Commissioner has relied.

The judgment is reversed and the case remanded with directions to grant defendant's motion to dismiss the complaint.

PART V.—PAYMENT, COLLECTION, AND REFUND OF TAX AND PENALTIES.

SECTION 280.—CLAIMS AGAINST TRANSFERRED ASSETS.

ARTICLE 1291: Claims in cases of transferred assets.

VIII-28-4269
G. C. M. 6343

REVENUE ACT OF 1926.

In accordance with section 280 of the Revenue Act of 1926, assessments were made against A and B of the amounts of their liability as transferees of the assets of a dissolved corporation in respect of a deficiency in tax assessed against the corporation for 1918. With the consent of A and B, overpayments of income taxes made by them for the year 1918 were applied against these assessments. Since the effect of the action taken was to allow and pay a refund, and since there were no taxes due against which the overpayments could be credited, A and B are entitled to interest on their overpayments for 1918.

An opinion is requested as to whether A and B are entitled to interest on certain overpayments of their 1918 income taxes, which were applied against assessments made against them, under section 280 of the Revenue Act of 1926, as transferees of the assets of a dissolved corporation.

The following provisions contained in the Revenue Act of 1926 are pertinent:

SEC. 280. (a) The amounts of the following liabilities shall, except as herein-after in this section provided, be assessed, collected, and paid in the same man-

ner and subject to the same provisions and limitations as in the case of a deficiency in a tax imposed by this title (including the provisions in case of delinquency in payment after notice and demand, the provisions authorizing distraint and proceedings in court for collection, and the provisions prohibiting claims and suits for refunds):

(1) The liability, at law or in equity, of a transferee of property of a taxpayer, in respect of the tax (including interest, additional amounts, and additions to the tax provided by law) imposed upon the taxpayer by this title or by any prior income, excess-profits, or war-profits tax Act.

SEC. 1116. (a) Upon the allowance of a credit or refund of any internal-revenue tax erroneously or illegally assessed or collected, or of any penalty collected without authority, or of any sum which was excessive or in any manner wrongfully collected, interest shall be allowed and paid on the amount of such credit or refund at the rate of 6 per centum per annum from the date such tax, penalty, or sum was paid to the date of the allowance of the refund, or in the case of a credit, to the due date of the amount against which the credit is taken, but if the amount against which the credit is taken is an additional assessment made under the Revenue Act of 1921, the Revenue Act of 1924, or this Act, then to the date of the assessment of that amount.

(b) As used in this section—

(1) The term "additional assessment" means a further assessment for a tax of the same character previously paid in part, and includes the assessment of a deficiency under Title II or Title III of the Revenue Act of 1924 or of this Act;

(2) The term "date of the allowance of the refund" means, in the case of any income, war-profits, or excess-profits tax, the first date on which the Commissioner signs the schedule of overassessments in respect thereof.

In accordance with section 280, the Commissioner, on the March, 1927, list, assessed against A and B the amounts of their liability as transferees of the assets of the corporation in respect of a deficiency in tax assessed against the corporation for the year 1918. Against these amounts assessed against A and B as transferees there were applied the overpayments of income taxes made by them for the year 1918.

An assessment under section 280 can not be regarded as creating a liability on the part of the transferees greater than that which would have been created by a judgment obtained against them under the "trust fund theory" (applied in *United States v. Boss & Peake Automobile Co.*, 285 Fed., 410, Treasury Decision 3442 (C. B. II-1, 43), and in other similar decisions), which is that where, upon dissolution of a corporation, its assets are distributed among the stockholders, the latter become liable to creditors of the corporation in an amount not to exceed the value of the property received by them. This principle applies to taxes due the Government upon the dissolution of a corporation.

Section 280 provides that the amount of the liability, at law or in equity, of a transferee, *in respect of the tax imposed upon the transferor*, shall be assessed. Since the individuals against whom the assessments under the provisions of section 280 of the Revenue Act of 1926 were made were not technically taxpayers (the transferor corporation alone being such in this case) but were merely liable as transferees for the payment of the transferor corporation's tax, and since the statute does not change or make their liability a tax liability but simply provides for the assessment of the amount of a liability at law or in equity, section 284 of the Revenue Act of 1926, providing that where there has been an overpayment of tax the amount of such overpayment shall be credited against any tax then due from the taxpayer, is no authority for crediting overpayments by individual

taxpayers against the amounts of their liability at law or in equity assessed against them under section 280 of that Act. As it appears, however, that the overpayments made by A and B for the year 1918 were with their consent applied against the assessments made against them as transferees, the effect of the action taken was to allow in the case of each individual a refund and then to pay the amount thereof by applying it against the liability assessed against him under section 280.

In view of the foregoing, it appearing that there were no taxes due from A or B against which the overpayments for 1918 could be credited, this office is of the opinion that A and B are entitled to interest on their overpayments for 1918 up to the date of the allowance of the refunds of said amounts.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

SECTION 283.—TAXES UNDER PRIOR ACTS.

SECTION 283.

VIII-29-4278
Ct. D. 80

INCOME TAX—REVENUE ACTS OF 1918 AND 1926—DECISION OF SUPREME COURT.

1. SUIT—JURISDICTION—CIRCUIT COURT OF APPEALS—REVIEW OF DECISION OF BOARD OF TAX APPEALS—CONSTITUTIONALITY.

Proceedings before the Circuit Courts of Appeals or the Court of Appeals of the District of Columbia on a petition to review a decision of the United States Board of Tax Appeals are judicial, since the elements of a case or controversy within the purview of Article III of the Constitution are present, even in an appeal pending before the Board at the time of the enactment of the Revenue Act of 1926 and decided subsequent thereto, as adequate finality is provided in respect to the action of such courts. The certification to the Supreme Court of a question of law by a Circuit Court of Appeals which the latter deemed necessary for a proper decision of a pending cause is an invocation of the appellate jurisdiction of the Supreme Court, and, therefore, within the Constitution.

2. INCOME—INCOME TAX PAID BY EMPLOYER.

Income taxes assessed against an employee and paid by his employer in part consideration for services constitutes additional income to the employee under the Revenue Act of 1918.

3. DECISION AFFIRMED.

The decision of the United States Board of Tax Appeals (7 B. T. A., 648) affirmed.

SUPREME COURT OF THE UNITED STATES.

Old Colony Trust Co. et al., Executors, v. Commissioner of Internal Revenue.

On certificate from the United States Circuit Court of Appeals for the First Circuit,

[June 3, 1929.]

OPINION.

Mr. Chief Justice TAFT delivered the opinion of the court.

We have before us for consideration two questions certified from the same Circuit Court of Appeals, No. 130 and No. 129. They are presented upon

different statements of facts and the cases reach the certifying court in different ways, but the questions are so nearly alike that the certifying judges deemed it convenient to present them in consolidated form. We prefer to separate the questions, discuss and decide No. 130 first, and then consider No. 129.

No. 130 comes here by certificate from the Circuit Court of Appeals for the First Circuit. The action in that court was begun by a petition to review a decision of the United States Board of Tax Appeals. The petitioners are the executors of the will of William M. Wood, deceased. On June 27, 1925, before Mr. Wood's death, the Commissioner of Internal Revenue notified him by registered mail of the determination of a deficiency in income tax against him for the years 1919 and 1920, under the Revenue Act of 1918. The deficiency was revised by the Commissioner August 18, 1925. An appeal was taken to the Board of Tax Appeals, which was filed October 27, 1925. A hearing before the Board April 11, 1927, resulted in a decision November 12, 1927. The Board approved the action of the Commissioner and found a deficiency in the Federal income-tax return of Mr. Wood for the year 1919 of \$708,781.93, and for the year 1920 of \$350,837.14. The petition for review was perfected December 23, 1927, pursuant to the Revenue Act of 1926 (sec. 283(j) and secs. 1001 to 1005, ch. 27, 44 Stat., 9, 65, 109) and rule 38 of the First Circuit Court of Appeals.

The facts certified to us are substantially as follows:

William M. Wood was president of the American Woolen Co. during the years 1918, 1919, and 1920. In 1918 he received as salary and commissions from the company \$978,725, which he included in his Federal income-tax return for 1918. In 1919 he received as salary and commissions from the company \$548,132.87, which he included in his return for 1919.

August 3, 1916, the American Woolen Co. had adopted the following resolution, which was in effect in 1919 and 1920:

"Voted: That this company pay any and all income taxes, State and Federal, that may hereafter become due and payable upon the salaries of all the officers of the company, including the president, William M. Wood; the comptroller, Parry C. Wiggin; the auditor, George R. Lawton; and the following members of the staff, to wit: Frank H. Carpenter, Edwin L. Heath, Samuel R. Haines, and William M. Lasbury, to the end that said persons and officers shall receive their salaries or other compensation in full without deduction on account of income taxes, State or Federal, which taxes are to be paid out of the treasury of this corporation."

This resolution was amended on March 25, 1918, as follows:

"Voted: That, referring to the vote passed by this board on August 3, 1916, in reference to income taxes, State and Federal, payable upon the salaries or compensation of the officers and certain employees of this company, the method of computing said taxes shall be as follows, viz:

"The difference between what the total amount of his tax would be, including his income from all sources, and the amount of his tax when computed upon his income excluding such compensation or salaries paid by this company."

Pursuant to these resolutions, the American Woolen Co. paid to the collector of internal revenue Mr. Wood's Federal income and surtaxes due to salary and commissions paid him by the company, as follows:

Taxes for 1918 paid in 1919-----	\$681, 169. 88
Taxes for 1919 paid in 1920-----	351, 179. 27

The decision of the Board of Tax Appeals here sought to be reviewed was that the income taxes of \$681,169.88 and \$351,179.27 paid by the American Woolen Co. for Mr. Wood were additional income to him for the years 1919 and 1920.

The question certified by the circuit court of appeals for answer by this court is:

"Did the payment by the employer of the income taxes assessable against the employee constitute additional taxable income to such employee?"

The first point presented to us is that of the jurisdiction of this court to answer the question of law certified. It requires us to examine the original statute providing for the Board of Tax Appeals under the Revenue Act of 1924, and the amending Act of 1926.

The Board of Tax Appeals, established by section 900 of the Revenue Act of 1924 (Title IX, ch. 234, 43 Stat., 253, 336), was created by Congress to

provide taxpayers an opportunity to secure an independent review of the Commissioner of Internal Revenue's determination of additional income and estate taxes by the Board in advance of their paying the tax found by the Commissioner to be due. Before the Act of 1924 the taxpayer could only contest the Commissioner's determination of the amount of the tax after its payment. The Board's duty under the Act of 1924 was to hear, consider, and decide whether deficiencies reported by the Commissioner were right.

Section 273 of that Act defined a "deficiency" to be the amount by which the tax imposed exceeded the amount shown by the return of the taxpayer after the return was increased by the amounts previously assessed or disallowed. There was under the Act of 1924 no direct judicial review of the proceedings before the Board of Tax Appeals. But each party had the unhindered right to seek separate action by a court of competent jurisdiction to test the correctness of the Board's action. Such court proceedings were to be begun within one year after the final decision of the Board.

Section 274(b) provided that if the Board determined there was a deficiency, the amount so determined should be assessed and paid upon notice and demand from the collector. No part of the amount determined as a deficiency by the Commissioner, but disallowed as a deficiency by the Board, could be assessed, but the Commissioner was at liberty, notwithstanding the decision of the Board against him, to bring a suit in a proper court against the taxpayer to collect the alleged deficiency.

On the other hand, by section 900(g) it was provided that in any suit brought by the Commissioner, or by the taxpayer to recover any amounts paid in pursuance of a decision of the Board, the findings of the Board were *prima facie* evidence of the facts.

By the Revenue Act of 1926 this procedure was changed and a direct judicial review of the Board's decision was substituted.

The Act of 1926 also enlarged the original jurisdiction of the Board of Tax Appeals to consider deficiencies beyond those shown in the Commissioner's notice, if the Commissioner made such a claim at or before the hearing (section 274(e)), and also to determine that the taxpayer not only did not owe the tax but had overpaid (section 284(e)).

The chief change made by the Act of 1926 was the provision for direct judicial review of the Board's decisions by the filing by the Commissioner or the taxpayer of a petition for review in a Circuit Court of Appeals or the Court of Appeals of the District of Columbia under rules adopted by such courts.

It is suggested that the proceedings before the Circuit Courts of Appeals or the District Court of Appeals on a petition to review are and can not be judicial, for they involve "no case or controversy," and without this a circuit court of appeals, which is a constitutional court (*ex parte Bakelite Corporation*, No. 17, Original, decided May 20, 1929), is incapable of exercising its judicial function. This view of the nature of the proceedings we can not sustain.

The case is analogous to the suits which are lodged in the circuit courts of appeals upon petition or finding of an executive or administrative tribunal. It is not important whether such a proceeding was originally begun by an administrative or executive determination, if when it comes to the court, whether legislative or constitutional, it calls for the exercise of only the judicial power of the court upon which jurisdiction has been conferred by law. The jurisdiction in this cause is quite like that of circuit courts of appeals in review of orders of the Federal Trade Commission. (*Federal Trade Commission v. Eastman*, 274 U. S., 623; *Silver Co. v. Federal Trade Commission*, 292 Fed., 752.) There are other instances of a like kind which can be cited. (*United States v. Ritchie*, 17 How., 525, 534; *Interstate Commerce Commission v. Brimson*, 154 U. S., 447, 469; *Stephens v. Cherokee Nation*, 174 U. S., 445, 477.) See also *Fong Yue Ting v. United States* (149 U. S., 698, 714).

It is not necessary that the proceeding to be judicial should be one entirely *de novo*. It is enough that before the judgment which must be final has been invoked as an exercise of judicial power it shall have certain necessary features. What these are has been often declared by this court. Perhaps the most comprehensive definitions of them are set forth in *Muskrat v. United States* (219 U. S., 346, 356), where this court entered into the inquiry what was the exercise of judicial power as conferred by the Constitution. There was cited there a definition by Mr. Justice Field, in *Re Pacific Railway Commission* (32 Fed., 241, 255), which has been generally accepted as accurate. He said:

"The judicial article of the Constitution mentions cases and controversies. The term 'controversies,' if distinguishable at all from 'cases,' is so in that it is less comprehensive than the latter; and includes only suits of a civil nature. (*Chisholm v. Georgia*, 2 Dall., 431, 432; 1 Tuck. Bl. Comm. App., 420, 421.) By cases and controversies are intended the claims of litigants brought before the courts for determination by such regular proceedings as are established by law or custom for the protection or enforcement of rights, or the prevention, redress, or punishment of wrongs. Whenever the claim of a party under the Constitution, laws, or treaties of the United States takes such a form that the judicial power is capable of acting upon it, then it has become a case. The term implies the existence of present or possible adverse parties whose contentions are submitted to the court for adjudication."

In *Osborn v. United States Bank* (9 Wheat., 738), Chief Justice Marshall construed Article III of the Constitution as follows (p. 819) :

"This clause enables the judicial department to receive jurisdiction to the full extent of the Constitution, laws, and treaties of the United States, when any question respecting them shall assume such a form that the judicial power is capable of acting on it. That power is capable of acting only when the subject is submitted to it, by a party who asserts his rights in the form prescribed by law. It then becomes a case, and the Constitution declares that the judicial power shall extend to all cases arising under the Constitution, laws, and treaties of the United States."

The circuit court of appeals is a constitutional court under the definition of such courts as given in the *Bakelite* case, *supra*, and a case or controversy may come before it, provided it involves neither advisory nor executive action by it.

In the case we have here, there are adverse parties. The United States or its authorized official sues to establish its right to the payment by a taxpayer of a tax due from him to the Government, and the taxpayer is resisting that payment or is seeking to recover what he has already paid as taxes when by law they were not properly due. That makes a case or controversy, and the proper disposition of it is the exercise of judicial power. The courts are either the Circuit Court of Appeals or the District of Columbia Court of Appeals. The subject matter of the controversy is the amount of the tax claimed to be due or refundable and its validity, and the judgment to be rendered is a judicial judgment.

The Board of Tax Appeals is not a court. It is an executive or administrative board, upon the decision of which the parties are given an opportunity to base a petition for review to the courts after the administrative inquiry of the Board has been had and decided.

It is next suggested that there is no adequate finality provided in respect to the action of these courts. In the first place, it is not necessary, in order to constitute a judicial judgment, that there should be both a determination of the rights of the litigants and also power to issue formal execution to carry the judgment into effect, in the way that judgments for money or for the possession of land usually are enforced. A judgment is sometimes regarded as properly enforceable through the executive departments instead of through an award of execution by this court, where the effect of the judgment is to establish the duty of the department to enforce it. (*La Abra Silver Mining Co. v. United States*, 175 U. S., 423, 457, 461.) The case of *Fidelity National Bank & Trust Co. v. Swope* (274 U. S., 123, 132) shows clearly that there are instances where the award of execution is not an indispensable element of a constitutional case or controversy. In that decision there are collected familiar examples of judicial proceedings resulting in a final adjudication of the rights of litigants without it.

But even if a formal execution be required, we think power to resort to it is clearly shown with respect to the enforcement of the action of the courts here involved by sections 1001 to 1005.

By the first, the decision of the Board of Tax Appeals rendered after the passage of the Act of 1926 may be reviewed by the Circuit Court of Appeals or the District Court of Appeals if a petition for such review is filed either by the Commissioner or the taxpayer within six months after the decision is rendered. The courts are to adopt rules for the filing of the petition, the preparation of the record, and the conduct of the proceedings upon such review. The review is not to operate as a stay of assessment or collection of any portion of the amount of the deficiency determined by the Board, unless a petition for review is filed by the taxpayer, or unless the taxpayer has filed a so-called jeopardy bond which

when enforced will operate finally to settle the rights of the parties as found by the courts.

By section 1002, it is provided in what venue the decision may be reviewed. In section 1003, the Circuit Courts of Appeals and the Court of Appeals of the District are given exclusive jurisdiction to review the decisions of the Board, and it is declared that their judgments shall be final except that they shall be subject to review by the Supreme Court of the United States, on certificate or by certiorari in the manner provided in section 240 of the Judicial Code as amended, and in such review the courts shall have the power to affirm, or if the decision of the Board is not in accordance with law, to modify or reverse the decision of the Board, with or without remanding the case for a rehearing as justice may require.

By section 1004, the same courts are given power to impose damages in any case where the decision of the Board is affirmed and it appears that the petition was filed merely for delay.

By section 1005, the decision of the Board is to become final in respect to all the numerous instances which in the course of the review may naturally end further litigation. In the provisions of these sections, the legislation prescribes minute details for the enforcement of the judgments that are the result of these petitions for review in the several courts vested with jurisdiction over them. The complete purpose of Congress to provide a final adjudication in such proceedings, binding all the parties, is manifest and demonstrates the unsoundness of the objection.

We have before us, however, for actual inquiry a case different from one just considered in the regular course of a petition for review of a decision of the Board, begun and decided all after the enactment of the Act of 1926. It is one in which the appeal to the Board of Tax Appeals had been taken, but the appeal had not been decided by the Board before the passage of the Act of 1926. That presents what involves a troublesome exception or duplication in the procedure. This occurs because of the last excepting clause of section 283(b) of the amending Act of 1926, which is as follows:

"If before the enactment of this Act any person has appealed to the Board of Tax Appeals under subdivision (a) of section 274 of the Revenue Act of 1924 * * * and the appeal is pending before the Board at the time of the enactment of this Act, the Board shall have jurisdiction of the appeal. In all such cases the powers, duties, rights, and privileges of the Commissioner and of the person who has brought the appeal, and the jurisdiction of the Board and of the courts, shall be determined, and the computation of the tax shall be made in the same manner as provided in subdivision (a) of this section, except as provided in subdivision (j) of this section and except that the person liable for the tax shall not be subject to the provisions of subdivision (d) of section 284."

The provisions of section 284(d) are those which deny to the taxpayer the power to bring any suit against the United States for the recovery of the tax after he has adopted the procedure of appealing to the Board of Tax Appeals or to the Circuit Court of Appeals.

By this last exception in 283(b), there seems still open to the taxpayers who have filed a petition under the law of 1924 and have not had a decision by the Board before the enactment of the law of 1926, the right to pay the tax and sue for a refund in the proper district court (par. 20 of sec. 24 of the Judicial Code, as amended by sec. 1310(c), ch. 136, 42 Stat., 311, U. S. Code, Title 28, sec. 41). *Emery v. United States* (27 F. (2d), 992) and *Old Colony R. R. v. United States* (27 F. (2d), 994) hold that the petitioner still retains this earlier remedy.

The truth seems to be that in making provision to render conclusive judgments on petitions for review in the circuit courts of appeals Congress was not willing, in cases where the Board of Tax Appeals had not decided the issue before the passage of the Act of 1926, to cut off the taxpayer from paying the tax and suing for a refund in the proper district court. But the apparent conflict in such cases can be easily resolved by the use of the principles of *res judicata*. If both remedies are pursued, the one in a district court for refund and the other on a petition for review in the circuit court of appeals, the judgment which is first rendered will then put an end to the questions involved and in effect make all proceedings in the other court of no avail. Whichever judgment is first in time is necessarily final to the extent to which it becomes a judgment. There is no reason, therefore, in the case before us to decline to take jurisdic-

tion. (See *Bryar v. Campbell*, 177 U. S., 649; *Kline v. Burke Construction Co.*, 260 U. S., 226, 230; *Stanton v. Embrey*, 93 U. S., 548, 554.)

Second. The jurisdiction here is based upon the certificate of a question of law. That is, whether the payment by the employer of the income taxes assessed against the employee constitutes additional returnable taxable income to such employee. The certification of such a question by the circuit court of appeals is an invocation of the appellate jurisdiction of this court and therefore within the Constitution.

Third. Coming now to the merits of this case, we think the question presented is whether a taxpayer having induced a third person to pay his income tax or having acquiesced in such payment as made in discharge of an obligation to him may avoid the making of a return thereof and the payment of a corresponding tax. We think he may not do so. The payment of the tax by the employers was in consideration of the services rendered by the employee and was a gain derived by the employee from his labor. The form of the payment is expressly declared to make no difference (sec. 213, Revenue Act of 1918, ch. 18, 40 Stat., 1065). It is therefore immaterial that the taxes were directly paid over to the Government. The discharge by a third person of an obligation to him is equivalent to receipt by the person taxed. The certificate shows that the taxes were imposed upon the employee, that the taxes were actually paid by him, and that the employee entered upon his duties in the years in question under the express agreement that his income taxes would be paid by his employer. This is evidenced by the terms of the resolution passed August 3, 1916, more than one year prior to the year in which the taxes were imposed. The taxes were paid upon a valuable consideration, namely, the services rendered by the employee and as part of the compensation therefor. We think therefore that the payment constituted income to the employee.

This result is sustained by many decisions. (*Providence & Worcester R. R. Co.*, 5 B. T. A., 1186; *Houston Belt & Terminal Ry. Co. v. Commissioner*, 6 B. T. A., 1364; *West End Street Railway Co. v. Malley*, 246 Fed., 625; *Rennselaer & S. R. Co. v. Irwin*, 249 Fed., 726; *Northern R. Co. of New Jersey v. Lowe*, 250 Fed., 856; *Houston Belt & Terminal Ry. Co. v. United States*, 250 Fed., 1; *Bialock v. Georgia Ry. & Electric Co.*, 246 Fed., 387; *Hamilton v. Kentucky & Indiana Terminal R. R.*, 289 Fed., 20 [T. D. 3518, C. B. II-2, 58]; *American Telegraph & Cable Co. v. United States*, 61 Ct. Cl., 326 [T. D. 3799, C. B. V-1, 295]; *United States v. Western Union Telegraph Co.*, 19 Fed. (2d), 157; *Estate of Levalley*, 191 Wis., 356; *Estate of Irwin*, 196 Cal., 366.)

Nor can it be argued that the payment of the tax in No. 130 was a gift. The payment for services, even though entirely voluntary, was nevertheless compensation within the statute. This is shown by the case of *Noel v. Parrott* (15 F. (2d), 669 [T. D. 3908, C. B. V-2, 149]). There it was resolved that a gratuitous appropriation equal in amount to \$3 per share on the outstanding stock of the company be set aside out of the assets for distribution to certain officers and employees of the company and that the executive committee be authorized to make such distribution as they deemed wise and proper. The executive committee gave \$35,000 to be paid to the plaintiff taxpayer. The court said (p. 672):

"In no view of the evidence, therefore, can the \$35,000 be regarded as a gift. It was either compensation for services rendered, or a gain or profit derived from the sale of the stock of the corporation, or both; and, in any view, it was taxable as income."

It is next argued against the payment of this tax that if these payments by the employer constitute income to the employee, the employee will be called upon to pay the tax imposed upon this additional income, and that the payment of the additional tax will create further income which will in turn be subject to tax, with the result that there would be a tax upon a tax. This it is urged is the result of the Government's theory, when carried to its logical conclusion, and results in an absurdity which Congress could not have contemplated.

In the first place, no attempt has been made by the Treasury to collect further taxes, upon the theory that the payment of the additional taxes creates further income, and the question of a tax upon a tax was not before the circuit court of appeals and has not been certified to this court. We can settle questions of that sort when an attempt to impose a tax upon a tax is undertaken but not now. (*United States v. Sullivan*, 274 U. S., 259, 264 [T. D. 4028, C. B. VI-2, 177]; *Yazoo & Mississippi Valley R. R. v. Jackson Vinegar Co.*,

226 U. S., 217, 219.) It is not, therefore, necessary to answer the argument based upon an algebraic formula to reach the amount of taxes due. The question in this case is, "Did the payment by the employer of the income taxes assessable against the employee constitute additional taxable income to such employee?" The answer must be "Yes."

SECTION 284.—CREDITS AND REFUNDS.

ARTICLE 1305: Limitations upon the crediting
and refunding of taxes paid.

VIII-38-4362
G. C. M. 5983

REVENUE ACT OF 1926.

A waiver filed by a taxpayer prior to the enactment of the Revenue Act of 1928 but after the running of the statute of limitations, and after liability on the part of the taxpayer to pay a deficiency in tax was extinguished under the provisions of section 1106(a) of the Revenue Act of 1926, is a nullity and does not operate to extend the time within which to determine and assess a deficiency in tax or to extend the time within which to file a claim for refund.

An opinion has been requested in connection with the application for reopening the claim for refund filed under the facts herein-after stated on July 14, 1926, covering income taxes paid for the calendar year 1920.

The material facts, briefly stated, are that A died in 1919, leaving a will subsequently duly admitted to probate; that the executors of the decedent's estate on behalf thereof filed an income tax return for the calendar year 1920 on March 15, 1921, and paid the total tax shown to be due thereon in quarterly installments in 1921; that said estate was closed and the executors discharged in 1922; and that, subsequent to such discharge and more than five years after the 1920 tax return was due and more than four years after such tax was paid, said former executors joined with the sole residuary legatee in executing an instrument, filed June 9, 1926, intended to be a waiver, and also executed and filed on June 14, 1926, a claim for refund of the above-mentioned taxes which were alleged to have been erroneously paid.

Based upon the foregoing facts, it was stated in General Counsel's Memorandum 2022A (C. B. VI-2, 103) :

The purported waiver was filed before June 15, 1926, and said refund claim was filed before April 1, 1927, in compliance with the above-quoted statutory provision. These instruments, as hereinabove stated, were executed and filed after the estate had been closed and the executors discharged. Each was signed and filed by both the former executors and the sole residuary legatee. The M organization has been advised that said waiver was not properly filed for the reason that neither the former executors nor the sole residuary legatee was the "taxpayer," as required by section 284(g), supra. Such advice is in accord with the opinion expressed in Solicitor's Memorandum 4870 (C. B. V-1, 124), interpreting sections 2(a)9 and 281(e) of the Revenue Act of 1924. A comparison of these sections with the corresponding sections of the Revenue Act of 1926, sections 2(a)9 and 284(g), reveals their material similarity. The construction applied in Solicitor's Memorandum 4870 is applicable to the similar provisions of the Revenue Act of 1926, and it is the opinion of this office that the conclusion therein reached is a sound and correct interpretation of the statutory provisions. It follows, therefore, that neither the former executors nor the sole residuary legatee may, in the instant case, be said to have been the "taxpayer" at the time the instrument purporting to be a waiver was filed. The purported waiver does not comply with section 284(g), supra, and the claim for refund should, therefore, be rejected.

In July, 1928, an application for the reopening of the claim referred to was filed, based upon the decisions rendered in the cases of *Walter G. Davis et al., as Executors and as Individuals, v. United States*, decided April 6, 1928 (27 Fed. (2d), 630), and *Mary S. Aldridge, Executrix of the Last Will and Testament of W. O. Aldridge, Deceased, v. United States* (64 Ct. Cls., 424, T. D. 4251, C. B. VII-2, 215).

Without considering the question of whether, under the above-mentioned decisions, the waiver was properly executed in this case, it would appear that, even if we assume that it was properly executed, there is no authority for making a refund of the amount of tax overpaid. It will be noted that, under the facts in the case, the period of limitation upon the assessment and collection of any deficiency in tax expired on March 15, 1926, and that the period of limitation upon the right to claim a refund expired on the same date, which was after the enactment of the Revenue Act of 1926. It would therefore appear that in the absence of a waiver or a claim filed before that date any liability on the part of the taxpayer or the Government became extinguished by virtue of the provisions of section 1106(a) of the 1926 Act. After the said date, however, the purported waiver and claim for refund, above referred to, were filed on June 9, 1926, and June 14, 1926, respectively. It is contended that the filing of such waiver extended the time in which a valid claim for refund could be filed in accordance with section 284(g) of the Revenue Act of 1926. That section reads in part as follows:

If the taxpayer has, *within five years* from the time the return for the taxable year 1917 was due, *filed a waiver of his right* to have the taxes due for such taxable year *determined and assessed* within five years after the return was filed, * * * then such credit or refund relating to the taxes for the year in respect of which the waiver was filed shall be allowed or made if claim therefor is filed either on or before April 1, 1925, or within four years from the time the tax was paid. * * * If the taxpayer has, on or before June 15, 1926, *filed such a waiver* in respect of the taxes due for the taxable year 1920 or 1921, then such credit or refund relating to the taxes for the taxable year 1920 or 1921 shall be allowed or made if claim therefor is filed either on or before April 1, 1927, or within four years from the time the tax was paid. [Italics supplied.]

Prior to the enactment of the foregoing provisions, as first introduced in the statute by an amendment of the 1921 Act, approved March 4, 1923, instances arose where, pursuant to waivers executed by taxpayers, their tax liability as determined after the expiration of the 5-year period disclosed overpayments of tax, which overpayments were then found not to be refundable because of the bar of the statute. Manifestly, it was unfair to the taxpayer, where he had waived the time within which to determine and assess any tax due, for the Commissioner to later determine the correct tax liability and then set up the bar of the statute, and properly so under the law as it then existed, against the taxpayer's right to recover any overpayment disclosed by such later determination. The foregoing provisions were intended to alleviate the harsh situation which thus existed. It will be noted, however, that the time for the filing of a claim is extended only in the case where a taxpayer has filed "such a waiver," meaning "a waiver of his right to have the taxes due" for the taxable year 1920 "determined and assessed within five years

after the return was filed." In the instant case such a waiver was never filed. At the time the instrument given was executed and filed the right to waive the statute of limitations no longer existed, for the reason that the bar of the statute had already become complete, both as to the remedy and the liability, and the Commissioner could no longer determine and assess a deficiency in tax, even if one existed. The waiver, therefore, was a nullity and did not have the effect of extending the time within which to determine and assess any tax that might be due and with respect to which liability had become extinguished (see G. C. M. 5601 (C. B. VIII-1, 126)), nor did it have the effect of extending the time within which to file a claim for refund on account of a liability on the part of the Government, which, if one ever existed, had already become extinguished. (Section 1106(a) of the 1926 Act.) The provisions of section 284(g), supra, are clearly intended to confer reciprocal rights upon both the taxpayer and the Commissioner (see report of the Committee on Finance of the Senate on the revenue bill of 1926, page 33), and, where the waiver did not have the effect of extending the period within which to determine and assess the tax, it likewise did not have the effect of extending the period within which to file a claim for refund. While it is true that the provisions of that section refer to the filing of a waiver on or before June 15, 1926, that date merely represents the latest date upon which "such a waiver" (a waiver of the taxpayer's "right to have the taxes due * * * *determined and assessed* within five years *after the return was filed*") may be filed for the purpose of obtaining an extension of time as therein prescribed.

The conclusion herein reached is not affected by the retroactive repeal of section 1106(a) of the Revenue Act of 1926 by section 612 of the Revenue Act of 1928 (see G. C. M. 5601, supra).

In view of the foregoing, it is the opinion of this office that the application for the reopening of the claim should be denied.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

SECTION 1117.—INTEREST ON JUDGMENTS.

SECTION 1117.

VIII-52-4483
Ct. D. 143

INTERNAL REVENUE TAX—REVENUE ACT OF 1926—DECISION OF COURT.

JUDGMENT—INTEREST.

The allowance of interest in any judgment against a collector for an internal revenue tax illegally collected, rendered after the enactment of the Revenue Act of 1926 and before the enactment of the Revenue Act of 1928, is controlled exclusively by section 1117 of the Revenue Act of 1926, which provides for interest upon the amount of such tax only to the date of entry of the judgment.

COURT OF APPEALS OF THE DISTRICT OF COLUMBIA.

Andrew W. Mellon, Secretary of the Treasury; John Raymond McCarl, Comptroller General; and Robert H. Lucas, Commissioner of Internal Revenue, appellants, v. The United States of America, Ex rel. Arthur D. Hill, as Surviving Executor of the Will of Peter C. Brooks, Deceased, appellee.

Before MARTIN, Chief Justice, and ROBB and VAN ORSDER, Associate Justices.

[December 2, 1929.]

OPINION.

ROBB, Associate Justice: Appeal from a judgment in the Supreme Court of the District directing the issuance of a writ of mandamus requiring the Commissioner of Internal Revenue and the Comptroller General to approve forthwith payment to appellee out of the Treasury of the United States the sum of \$37,642.73, alleged to be due him for interest on a judgment (between its date and date of payment) entered in his favor on August 1, 1927, in the District Court of the United States for the District of Massachusetts in a suit against the collector of internal revenue for that district for the erroneous or illegal assessment and collection of internal revenue taxes; a certificate of probable cause having been filed. The writ further directs the Secretary of the Treasury to pay forthwith the sum mentioned.

Upon the filing of the petition for the writ, a rule to show cause issued; appellants filed a joint and several answer. Appellee demurred. Upon hearing, the demurrer was sustained. Appellants electing to stand on their answer, the writ as prayed was directed to be issued.

Appellants contend, first, that subsection (b) of section 177 of the Judicial Code, as amended by section 1117 of the Revenue Act of 1926 (44 Stat., 9, 119), controlled the allowance of interest on appellee's judgment, and that interest was allowable from the date of the payment or collection of the taxes only "to the date of entry of such judgment." Interest was computed and paid accordingly. Second, that the writ of mandamus may not issue to compel the payment of money from the Treasury of the United States where there is another plain, adequate, and complete remedy. Third, that the Comptroller General may not be compelled by writ of mandamus to allow a claim never presented to him for payment prior to the filing of the petition for mandamus and to certify it for payment from an appropriation which does not authorize such payment.

Section 1117 of the Revenue Act of 1926 (44 Stat., 9, 119) provides:

"Section 177 of the Judicial Code, as amended, is amended to read as follows:

"Sec. 177. (a) No interest shall be allowed on any claim up to the time of the rendition of judgment by the Court of Claims, unless upon a contract expressly stipulating for the payment of interest, except as provided in subdivision (b).

"(b) In any judgment of any court rendered after the enactment of the Revenue Act of 1926 (whether against the United States, a collector or deputy collector of internal revenue, a former collector or deputy collector, or the personal representative in case of death) for any internal-revenue tax erroneously or illegally assessed or collected, or for any penalty collected without authority or for any sum which was excessive or in any manner wrongfully collected, under the internal-revenue laws, interest shall be allowed at the rate of 6 per centum per annum upon the amount of such tax, penalty, or sum, from the date of the payment or collection thereof to the date of entry of such judgment or, if such judgment is reviewed by an appellate court, to the date of entry of final judgment."

The judgment in question having been rendered after the enactment of the Revenue Act of 1926, it is at once apparent that if the provisions of that Act control, appellee was not entitled to interest beyond the date of the entry of the judgment.

Section 966, R. S., provides for the allowance of interest on all judgments in civil causes recovered in circuit or district courts in cases where, by the law of the State in which the court is held, interest may be levied under process of execution on judgments recovered in the courts of such State, and

that it shall be calculated from the date of judgment "at such rate as is allowed by law on judgments recovered in the courts of such State."

The suit in this case against the collector was personal (*Sage v. United States*, 250 U. S., 83), but a certificate of probable cause was issued. Under section 989, R. S., after the issuance of such certificate, "no execution shall issue against such collector or other officers, but the amount so recovered shall upon final judgment be provided for and paid out of the proper appropriation from the Treasury." Until the issuance of the certificate the Government assumes "no part of the liability of the defendant." Upon the issuance of the certificate, "the claim of the plaintiff in the suit is practically converted into a claim against the Government. But not until then." (*United States v. Sherman*, 98 U. S., 565, 567; *Schell v. Cochran*, 107 U. S., 625, 627.)

Internal revenue taxes having been "erroneously or illegally assessed or collected," interest was allowable to appellee under the express provisions of the Revenue Act of 1926 "at the rate of 6 per centum per annum upon the amount of such tax, penalty, or sum, from the date of the payment or collection thereof to the date of entry of such judgment." [Italics ours.] That the Act of 1926 applied can not be doubted, but appellee insists "that the statute only has to do with interest up to the time of judgment, and it is only by implication that it can be stretched to cover interest after judgment." We think the maxim, "*expressio unius est exclusio alterius*," applies. See *Wilbur v. United States* (58 App. D. C., 347, 30 Fed. (2d), 871); *Stephens v. Smith* (10 Wall., 321); *Raleigh & G. R. Co. v. Reid* (13 Wall., 269); *Ford v. United States* (273 U. S., 593, 47 Sup. Ct. Rep., 531).

Congress is presumed to have known that under section 966, R. S., in a personal action interest is allowable on a judgment at such rate as is allowed by the law on judgments recovered in the courts of the State where the judgment is rendered. In section 1117 of the Revenue Act of 1926, Congress was not dealing with the general subject of interest, as in section 966, R. S., but with the special subject of interest "on any judgment of any court * * * for any internal-revenue tax erroneously or illegally assessed or collected * * *." The language of this section is comprehensive and specific, and in our view it would be a strained construction to rule that Congress did not intend it to be exclusive. See *Burrows v. Woodworth* (11 F. (2d), 777 [T. D. 3900, C. B. V-2, 230]).

That such was the intent of Congress is further indicated by section 615 of the Revenue Act of 1928, approved May 29, 1928 (44 Stat., 877), again amending section 177 of the Judicial Code, and providing that "in any judgment of any court rendered (whether against the United States, a collector or deputy collector of internal revenue, * * *) for any overpayment in respect of any internal-revenue tax, interest shall be allowed at the rate of 6 per centum per annum upon the amount of the overpayment, from the date of the payment or collection thereof to a date preceding the date of the refund check by not more than 30 days, such date to be determined by the Commissioner of Internal Revenue." Apparently Congress concluded that the Act of 1926, being exclusive, did not adequately protect those from whom internal revenue taxes had been erroneously collected, and therefore extended the period within which interest on judgments for such overpayments would be allowable to a date within 30 days of the actual payment.

Counsel for appellee attaches importance to the fact that the mandate of the Supreme Court of the United States in *Nichols v. Ooolidge* (374 U. S., 531 [T. D. 4072, C. B. VI-2, 351]) (where the facts were similar to the facts in this case, except that in this case no appeal was taken from the judgment of the district court) required the payment of interest on the final judgment to the actual date of payment. There is no indication in the opinion of the court that section 1117 of the Act of 1926 was brought to its attention. Moreover, rule 30 of the rules of that court provides for the allowance of interest "at the same rate that similar judgments bear interest in the courts of the State where such judgment was rendered." This rule, the court has indicated, is in harmony with section 1010, R. S., authorizing the court to adjudge to the respondent-in-error just damages for the delay of the plaintiff-in-error. (*Schell v. Cochran*, 107 U. S., 625, 627.)

The judgment of appellee having been fully satisfied, there was no basis for the issuance of the writ of mandamus. It is, therefore, unnecessary to consider other questions raised by appellants.

Judgment is reversed, with costs, and cause remanded for further proceedings.
Reversed.

SECTION 1127.—ENFORCEMENT OF TAX LIENS.

SECTION 1127.

VIII-42-4397
Ct. D. 119

INTERNAL REVENUE LAWS—TAX LIEN—DECISION OF COURT.

1. LIEN—SUIT—COLLECTOR AS PARTY.

A collector has no interest in a tax lien created by section 3186, Revised Statutes, as amended, which is in favor of the United States. The United States is a necessary party to a suit respecting it and can not be sued without its consent.

2. LIEN—ENFORCEMENT—RIGHTS OF SURETY.

Section 3207, Revised Statutes, as amended, relating to the enforcement of tax liens, provides an exclusive remedy and a person having no interest in real estate upon which the United States has a lien is not a proper party to a suit respecting it. The execution and delivery to a collector of a bond conditioned to pay the tax does not confer upon him or the obligors any rights under that section in respect to the lien.

3. SAME—SUBROGATION—EXONERATION.

Where the tax has not been paid a surety upon a bond conditioned to pay the tax has no right on principles of subrogation or exoneration to have a tax lien enforced.

DISTRICT COURT OF THE UNITED STATES FOR THE EASTERN DISTRICT OF SOUTH
CAROLINA.

Maryland Casualty Co. v. Charleston Lead Works et al.

OPINION.

HALE, District Judge: The complainant, Maryland Casualty Co., a Maryland corporation, brings its bill in equity against the Charleston Lead Works, a South Carolina corporation, and against John F. Jones, a citizen of South Carolina, alleging that he is a citizen of the United States and resident of the State of South Carolina, and ever since and prior to the year 1925 has held the office of collector of United States internal revenue for the district of South Carolina, and is sued in his own right and as such collector. After stating the jurisdictional facts, the bill alleges that the Commissioner of Internal Revenue assessed a deficiency income tax for 1917 in the amount of \$2,484.79 against the Charleston Lead Works, one of the defendants, which amount was entered on the assessment list for April, 1921, transmitted by the Commissioner of Internal Revenue to the then collector of United States internal revenue for the district of South Carolina, which assessment thereby became, and has since remained, a lien upon all of the real and personal property of the Charleston Lead Works, a description of the property owned by that defendant being set out; that, while said lien was in full force and effect, May 1, 1922, the Charleston Lead Works executed a mortgage to the South Carolina Loan & Trust Co., as trustee, also one of the defendants, to secure an issue of \$90,000 of bonds, what part thereof having been issued or outstanding the complainant alleging want of knowledge; that the complainant is informed and believes that the mortgage was taken by the South Carolina Loan & Trust Co. with actual knowledge of the lien for Federal taxes; that on March 15, 1925, the complainant, as surety, and the Charleston Lead Works, as principal, executed a bond in the amount of \$3,500 to John F. Jones, as collector of internal revenue for the district of South Carolina, or his successors in office, to secure to the principal an extension of six months' time for the payment of the 1917 taxes, the condition being that the said principal should indemnify the defendant John F. Jones, collector of internal revenue, district of South Carolina, or his successors in office, against loss, costs, damages, or expense to which he might be put by reason of granting such extension of time.

It is further averred that the principal, the Charleston Lead Works, has failed to pay the tax, and that the said collector, on November 19, 1925, made demand on complainant for the amount due on account thereof; that the Charleston Lead Works is believed to be insolvent and wholly unable to pay the tax, that the persons who made application to the complainant to become surety on the bond are insolvent, and complainant is without adequate remedy against them.

Upon these facts, the complainant alleges that it is entitled to be exonerated as surety upon said bond, and to have the lien of the United States for said tax enforced as a lien prior to the mortgage in favor of the South Carolina Loan & Trust Co., as trustee, and the proceeds arising from sale of the property be first applied to the satisfaction of said tax.

Appearing specially for that purpose, John F. Jones has filed his motion to dismiss this action as against him upon the ground that it appears upon the face of the complaint that he has no interest in the action whatever, or in the subject matter thereof; that he has no lien on the property described in the complaint; that the lien referred to is in favor of the United States; and that, while he is named as defendant, the real party in interest is the Government of the United States; that the United States has a lien on the property described in the complaint; and that the United States may not be sued in this action without its consent, which consent has not been given.

It will be seen that the bill alleges assessment of an income tax against the Charleston Lead Works; that the Government acquired a lien upon the real and personal property of the Charleston Lead Works, and, while the lien was in force and effect, May 1, 1922, the Charleston Lead Works executed a mortgage to the South Carolina Loan & Trust Co. upon certain real estate; that the United States has a lien for taxes on this property; that John F. Jones, as collector of internal revenue, has a bond to secure these taxes; and, in the action against Jones, "sued in his own right as such collector," the complainant seeks to have itself placed in the position of the United States with reference to the lien, to exercise the right of the United States to enforce the lien by sale of the premises, and to have the proceeds of the sale applied to the satisfaction of the taxes, so that the obligation of the bond may be extinguished.

It is not alleged that the United States has given its consent to being made a party to the action, and it is claimed that such consent is not required, because the action is against Jones personally and as collector. The complainant seeks the processes and remedy of the equity court in a suit between private persons in discharging a debt which, it claims, is an obligation arising from its alleged contract with Jones, who was alleged to be a mere private person, and that the words "collector of internal revenue" are merely descriptive of such person. To establish the responsibility of Jones as a private person, the plaintiff cites section 3184, Revised Statutes; Act of July 13, 1866, chapter 184, sections 9, 14 Stat., 106; March 2, 1867, chapter 169, sections 8, 14 Stat., 473; December 24, 1872, chapter 13, sections 2, 17 Stat., 402 (26 U. S. C. A., section 104; Comp. St., section 5906). These statutes direct collectors of internal revenue to collect taxes in their several districts. The learned counsel for the complainant cites further statutes providing that the collector shall be charged with the amount of taxes. These statutes cited appear to be administrative provisions. Their direction to collect taxes and record an account for them are, I think, intended to give such power to collectors by virtue of their office, and not as private persons. But from these provisions, which I think are administrative, the learned counsel for the complainant seeks to establish the proposition that the collector of internal revenue is personally liable for all internal revenue taxes assessed in his district, that the bond executed to him to secure these taxes is a bond to him personally, and that a suit involving such bond is properly brought against him personally. The complainant brings to my attention cases holding that an officer of the United States may be sued in matters where the rights asserted and the relief asked for are against the defendants as individuals.

The lien in question is based upon section 3186 (amended by section 3, Act of March 1, 1879 (20 Stat., 327), and Act of March 4, 1913 (37 Stat., 1016; 26 U. S. C. A., section 115; Comp. St., section 5908)), which provides: "If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount shall be a lien in favor of the United States from the time when the assessment list was received by the collector."

(1) It will be seen that, by virtue of this statute, the lien attached spontaneously when the assessment list was received and upon neglect and failure

to pay the taxes on demand. No action is required by the collector to effect the lien. No action by the collector is referred to except such as relates to giving such notice as will be effective against mortgages, purchasers, and judgment creditors. The lien is a statutory lien, and I think it clear that it is a right of the United States. The section of the statute quoted makes no provision for relief from this lien except the payment of the tax; and the complaint shows that the tax has not been paid. The Revenue Act of 1926, section 1127, reenacted in section 3207 of the Revised Statutes, as amended (26 U. S. C. A., section 136), provides that the Commissioner of Internal Revenue may direct the filing of a bill in equity "to enforce the lien of the United States," and provides that "all persons having liens upon or claiming any interest in the real estate sought to be subjected as aforesaid, shall be made parties"; and it provides that, in all cases where a claim or interest of the United States therein is established, the court "shall decree a sale of such real estate," and "a distribution of the proceeds of such sale according to the findings of the court in respect to the interests of the parties and of the United States."

By section 1030 of the Revenue Act of 1924 (26 U. S. C. A., section 136), reenacted as section 1127 of the Revenue Act of 1926, section 3207 is amended. Paragraph (a) of the amended statute is a repetition of the original statute, with only such change as to recognize the later judicial organization. Paragraph (b) extends to "any person having a lien upon or any interest in such real estate, notice of which has been duly filed of record in the jurisdiction in which the real estate is located, prior to the filing of notice of the lien of the United States as provided by section 3186 of the Revised Statutes as amended, or any person purchasing the real estate at a sale to satisfy such prior lien or interest," to request the Commissioner of Internal Revenue to direct the filing of a bill in chancery to enforce the Federal tax lien, and upon his failure so to do within six months, the person so entitled may file his petition in the proper court for leave to file a bill for the "final determination of all claims to or liens upon the real estate in question." The district court may upon hearing the petition grant leave to file the bill. "The United States and all persons having liens upon or claiming any interest in the real estate shall be made parties." Consistently with this language, provision is made for service on the United States in the manner provided by sections 5 and 6 of the Act of March 3, 1887 (28 U. S. C. A., sections 762, 763), entitled "An Act to provide for the bringing of suits against the Government of the United States." Further, it is provided that, "for the purpose of such adjudication, the assessment of the tax upon which the lien of the United States is based shall be conclusively presumed to be valid."

It appears then that this statute creates a lien in favor of the United States; or the language of it indicates that the tax lien is a right of the United States; that the United States may file its bill in chancery for its enforcement; and that no other party may do so until after the United States has failed to file such bill after demand made; and that, when such other party having taken the steps provided for, to vest himself with the right to file a bill, begins his suit, he must make the United States a party defendant, and must serve it with process, as in other cases of suits against the United States; and that he may not question the validity of the assessment upon which the lien of the United States is founded.

It appears that section 3207 grants a remedy to persons other than the Government, but only to such persons as have liens upon or interest in the real estate prior to the filing of the lien of the United States, or to persons purchasing the real estate at a sale to satisfy such prior lien or interest.

(2, 3) In the case at bar, the complainant shows no interest whatever in the real estate nor any demand upon the United States to enforce the lien. The lien is strictly a statutory one, and I think section 3207 of the Revised Statutes is intended to provide the exclusive remedy for a judicial determination of the lien involved in the case. This bill of complaint does not plead facts which give it a right to enforce its lien. The lien is, then, a right of the United States, and no collector of internal revenue has, I think, any right to dispose of it.

(4-6) The complainant does not, I think, state any case entitling it to a right based upon subrogation; for the bill affirmatively pleads that the taxes due to the United States, and for which there is a lien in its favor, remain unpaid, and that the complainant has not complied with the conditions of the bond. It is clear that, in order that a surety may have subrogation, the debt must be paid in full. (*Columbia Finance & Trust Co. v. Kentucky Union R. Co.* (C. C. A.), 60 F., 794.)

Nor does the complaint show that the complainant has a right to relief on principles of exoneration, for the right to exoneration arises between parties who are liable for the same debt, by which, when a party secondarily liable, has paid the principal's obligation, or any part thereof, he is entitled to be reimbursed by the principal debtor, and can bring a bill in equity to enforce that right. It is not alleged that anything has been paid in this case. (*Comstock v. Corbin et al.*, 191 Mich., 639, 158 N. W., 106.)

(7-8) The matter now before the court is the motion of Jones for "a dismissal of the complaint as against him." It seems clear to me that the subject matter of the complaint is one in which the United States is a necessary party in interest, and as to which the court may not act without the United States being made a defendant. The United States can not be sued without its consent. As I have already found, the only consent which it can have in cases of this sort is found in section 3207 as amended, and the complaint affirmatively disclosed that this complainant is not within the class of persons entitled to the favor of that statute. The statute creating a lien clearly gives no right to the collector with regard to its enforcement or otherwise. Nor does the remedy provided in section 3207 contemplate any order affecting the collector. In *Belknap v. Schild* (161 U. S., 10, 17, 16 S. Ct., 443, 445 (40 L. ed., 599), speaking for the court, Mr. Justice Gray, in his opinion, says:

"A public officer is not personally liable on a contract, although under his own hand and seal, made by him in the line of his duty, by legal authority, and on account of the Government, and inuring to its benefit, and not to his own. (*Hodgson v. Dexter*, 1 Cranch, 345, 2 L. ed., 130.) See, also, *Macbeath v. Haldimand* (1 T. R., 172); *Unwin v. Wolseley* (1 T. R., 674); *Palmer v. Hutchinson* (6 App. Cas., 619)."

See, also, *Leather et al. v. White* (C. C. A.) (296 F., 477).

I am constrained to find that the complaint charges no acts of John F. Jones, either official or personal, with reference to the lien in question which require him to answer or which make him a proper party to any decree of this court. He clearly is not, then, a party in interest in the proceeding; and it is ordered that the complaint be dismissed as to him. A decree may be submitted, not inconsistent with this opinion.

SECTION 1211.—SALARIES OF STATE AND MUNICIPAL OFFICERS.

SECTION 1211.

REVENUE ACT OF 1926.

Independent contractor. (See Ct. D. 114, page 287.)

INCOME TAX RULINGS.—PART III.**REVENUE ACT OF 1924.**

TITLE II.—INCOME TAX.

PART I.—GENERAL PROVISIONS.

**SECTION 201.—DISTRIBUTIONS BY
CORPORATIONS.****ARTICLE 1541: Dividends.****VIII-34-4321
Ct. D. 93****INCOME TAX—REVENUE ACT OF 1924—DECISION OF COURT.****1. DIVIDEND—TAXABILITY—STOCK PURCHASED WITH DIVIDEND—
REORGANIZATION.**

Where a national bank formulates a plan for creating a trust company to engage in business not permitted to be done by it under the National Banking Act in accordance with which the bank declares a cash dividend and the stockholders, that accept the plan, agree to allow the dividend to be used in payment for stock in the trust company and to allow the stock to be deposited with trustees for their benefit and the beneficial interest to pass with the transfer of stock in the bank, the amount of the dividend received by a stockholder consenting to the plan and so used in payment for stock in the trust company is taxable as a dividend. The transaction is not a reorganization within the meaning of section 203(c) of the Revenue Act of 1924, which provides, under the conditions therein stated, for the recognition of no gain to a distributee from the receipt of stock pursuant to a plan of reorganization.

2. DECISION AFFIRMED.

The decision of the United States Board of Tax Appeals (11 B. T. A., 659) is affirmed.

UNITED STATES CIRCUIT COURT OF APPEALS, EIGHTH CIRCUIT.***John G. Lonsdale v. Commissioner of Internal Revenue.***

On petition to review decision of United States Board of Tax Appeals.

[April 18, 1929.]

VAN VALKENBURGH, Circuit Judge, delivered the opinion of the court.

This is a petition to review a decision of the United States Board of Tax Appeals. The Commissioner of Internal Revenue, on August 19, 1926, found that there was a deficiency in the amount of petitioner's income tax for the year 1924 in the sum of \$3,766.91. This deficiency was held to arise from the exclusion of a 10 per cent dividend declared by the National Bank of Commerce of St. Louis, Mo., which said dividend was applied to the purchase of stock in the Federal Commerce Trust Co. of that city. The petition of appellant, for appeal from this ruling to the United States Board of Tax Appeals, states that the National Bank of Commerce of St. Louis was advised "that as a national bank it could not engage in various financial endeavors advantageous for banks to undertake and in which State banks and trust companies may freely engage. It felt that

the National Banking Act so restrained its endeavors that it was handicapped in competing with State banks and trust companies. For this reason said National Bank of Commerce in the year 1923 concluded that it would be advantageous to its business to organize a Missouri corporation to engage in the business in which it was restricted or handicapped by the National Banking Act and the rules and regulations thereunder. Thereupon said bank, through its president, under date of June 18, 1923, addressed a circular letter to its stockholders advising them of its purpose and setting forth its plan for the organization of a new company."

This circular letter reads as follows:

NATIONAL BANK OF COMMERCE,
St. Louis, June 18, 1923.

To the Stockholders of the National Bank of Commerce in St. Louis:

As you know, we have established a savings department, which now has nearly 50,000 depositors, with total deposits of over eight millions. We have also put in a bond department, which is doing a very satisfactory business. By special permission of the Federal Reserve Board, the bank qualified to act in a fiduciary capacity, and our trust department is now handling a large volume of trust matters. We have also taken over and are now operating our safe deposit vaults.

There are, however, some financial matters that can not be transacted through a National bank, and yet are allied with commercial banking so closely that we have realized for some time the necessity of having a way to take care of this business. And so, at a recent meeting of the board of directors, the officers of the bank were directed to formulate a plan for creating a company to be called Commerce company or some other suitable name which will have the power of dealing in all kinds of securities, including first mortgage on real estate, real estate, and other matters of like character, it being the purpose that the charter of this company shall be broad enough to enable the company to supplement the service now performed by the bank.

The new company is to be owned by the stockholders of the bank in proportion to their holdings of stock in the bank. We have examined a number of different plans that have been adopted by national banks throughout the country, and have concluded that the best is that known as the Chicago plan. Under this plan, the directors of this bank will declare a 10 per cent cash dividend, amounting to a million dollars, and the stockholders will be asked to subscribe for stock in the new company in an amount equal to this dividend and authorize the committee to apply the proceeds in payment of their stock in the new company. In this way, each subscribing shareholder in the bank will have one-tenth of a share of fully paid stock in the new company for each share of stock in the bank.

Believing that the interests of the stockholders of this bank will best be served if their interests in the bank and the new company are kept identical, the plan of organization provides that the stock in the new company shall be held by the trustees named in the agreement for the benefit of the subscribers, except a few shares that may be necessary for the directors to qualify. While such trust continues, the beneficial interest in the stock of the new company deposited with the trustees will pass with the transfer of the stock in this bank.

Each stockholder, therefore, is requested to sign the inclosed acceptance and power of attorney so that the new company may be promptly organized and put in operation. The gentlemen named in the power of attorney are directors and large stockholders in the bank.

Yours, very truly,

[Signed] JOHN G. LONSDALE, *President.*

A form for acceptance and power of attorney which the stockholders were requested to sign was inclosed with this letter.

Prior to January 2, 1924, stockholders of the National Bank of Commerce owning in excess of 80 per cent of the stock of the bank had signed the acceptance and power of attorney; of these the petitioner Lonsdale was one. January 22, 1924, the dividend of 10 per cent was declared, the resolution to that effect reciting that this was done in order "that each stockholder so minded may, with said dividend, cause the payment in full of his interest" in said new company. Under the terms of the letter to stockholders of June 18, 1923, the dividend thus declared was to be a cash dividend applying to all stockholders, and, while declared for the express purpose of being devoted, at the will of the stockholders, to payment of their subscription to the capital stock of the new com-

pany, it followed necessarily that those stockholders who refused to accept the proposition made, and to apply their dividend to the purchase of such stock, would, and must, receive the same in cash. The Commissioner of Internal Revenue ruled that the petitioner received a taxable dividend of \$14,100 upon his stock in the bank in the transaction above recited.

The petitioner contends, that because of their agreement, the assenting stockholders of the National Bank of Commerce were not entitled to cash under the dividend resolution; that by reason of the trust under which the stock of the Federal Commerce Trust Co. was placed, appellant received nothing in the nature of income. Furthermore, that the transaction constituted a reorganization of the National Bank of Commerce under section 203 of the Revenue Act of 1924, which excludes the recognition of gain. Upon appeal to the Board of Tax Appeals the ruling of the Commissioner was affirmed.

Section 203 of the Revenue Act of 1924, in so far as it has present application, reads as follows:

"(c) 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.

"(h) As used in this section and in sections 201 and 204, (1) the term 'reorganization' means * * * or (B) 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 stockholders, or both, are in control of the corporation to which the assets are transferred, * * * (2) The term 'a party to a reorganization' includes a corporation resulting from a reorganization and includes both corporations in the case of an acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all classes of stock of another corporation."

"What is or is not 'income' within the meaning of the amendment must be determined in each case according to truth and substance, without regard to form.

"Income may be defined as the gain derived from capital, from labor, or from both combined, including profit gained through sale or conversion of capital." (*Eisner v. Macomber*, 252 U. S., 189 [T. D. 3010, C. B. 3, 25].)

"Substance and not form should control in the application of the sixteenth amendment and the income tax laws enacted under it." (*United States v. Phellis*, 257 U. S., 156 [T. D. 3270, C. B. 5, 37].)

Appellant received a distinct individual gain by the declaring of the dividend in question. The fact that he did not receive the cash in hand, but permitted the cash dividend thus declared to be used in the purchase of stock in another and distinct corporation, did not alter the substantial effect of the transaction; nor is it important that he could not presently sell and dispose of his stock in the new company without at the same time selling his stock in the bank. Whenever such a disposition shall be made there will be an increment of gain corresponding to the value of the new corporation stock which was purchased with the dividend declared. This dividend was segregated from the capital assets of the bank, and, when declared, was the property of the stockholder, and not of the bank. Any stockholder might, if so minded, have received his portion of the dividend in money and have refused acceptance of the plan. The fact that appellant reinvested it in the stock of the new corporation, organized to do a distinct business which the bank was not authorized to do, renders that dividend no less an item of income. It is the inherent nature of the dividend itself that controls.

Referring now to the claim of reorganization whereby it is urged that the transaction falls within the terms of section 203 of the Revenue Act of 1924 above quoted, it will be observed that the procedure adopted does not conform to controlling features of the provisions of that Act. This section obviously has reference either to a complete reorganization of the original corporation by a transfer of its entire assets to another, then existing or newly organized, or to a transfer of a part of the assets in such manner that the corporations may thereafter be under one control and may be operated substantially as one in the prosecution of their business. It can not properly, and does not, we think, refer to the organization of an independent company—although with substantially the same stockholders and officers—which is authorized by its charter to

transact business and engage in dealings which are prohibited to the original corporation. It will be observed that both corporations operate independently along the lines prescribed in their charters and recognized by the laws of their existence. Furthermore, the Act in question presumes a transfer of assets by the corporation itself. It does not include the application of dividends which, when declared, are the property of the stockholders. If the new company be considered as a reorganization of the bank, or that the two companies standing together constitute such a reorganization, and such a unit of corporate existence, then the bank is thus indirectly empowered to do that which in the petition of appellant it is conceded to be without authority to do. No theory of reorganization which involves necessarily such a palpable evasion of law can be indulged. To accomplish thus indirectly what the bank was not permitted to do directly, it has adopted a plan which brings its stockholders clearly within the purview of the income tax law. This conclusion is sustained by the rule announced in *Rockefeller v. United States* (257 U. S., 176 [T. D. 3271, C. B. 5, 34]) and *Murr v. United States* (268 U. S., 536 [T. D. 3755, C. B. IV-2, 116]). The contention that section 203 of the Act of 1924, as applied to the facts before us, reverses the doctrine announced in the cases cited can not be sustained. The further contention that the bank and the trust company are so identical in ownership and united in management that one is but the *alter ego* of the other is met by the language of the Supreme Court in *Corsicana National Bank v. Johnson* (251 U. S., 68-88), as follows:

"We can not accede to either contention in the extreme. Because the bank and the loan company were distinct legal organizations, operating under separate charters derived from different sources, and possessing independent powers and privileges, we are constrained to hold that, notwithstanding the identity of stock ownership and their close affiliation in management, for some purposes they must be regarded as separate corporations, * * *"

The cases of *United States v. Mellon* (281 Fed., 645) and *United States v. Davison* (9 Fed. (2d), 1022) have been examined, and found to have no application here. The National Bank of Commerce continues as before, its capital stock and the nature of its business unimpaired and unchanged by this transaction.

It follows, in our opinion, that the judgment of the Board of Tax Appeals that the dividend in question constituted taxable income to the petitioner and that there is a deficiency for the year 1924, in the amount of \$3,766.91, should be affirmed, and it is so ordered.

SECTION 204.—BASIS FOR DETERMINING GAIN OR LOSS, DEPLETION, AND DEPRECIATION.

ARTICLE 1591: Basis for determining gain or loss from sale.

REVENUE ACT OF 1924.

Dower or statutory interest, value not having been returned to widow before her death. (See I. T. 2480, page 141.)

ARTICLE 1599: Dividend stock.

VIII-47-4434
T. D. 4274

Article 1599 of Regulations 65, article 1599 of Regulations 69, and article 600 of Regulations 74 amended.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, D. C.

To Collectors of Internal Revenue and Others Concerned:

Article 1599 of Regulations 65 is hereby amended to read as follows:

ART. 1599. *Stock or securities distributed in reorganization.*—In the case of stock or securities acquired by a shareholder after December 31, 1923, in connec-

tion with a transaction described in section 203(c) and article 1576, the basis in the case of the stock in respect of which the distribution was made shall be apportioned between such stock and the stock or securities distributed to the shareholder. The basis for the old shares and the new shares or securities shall be determined in accordance with the following rules:

(1) Where the stock distributed in reorganization consists solely of stock in the distributing corporation and is all of substantially the same character and preference as the stock in respect of which the distribution is made, the basis of each share will be the quotient of the cost or other basis of the old shares of stock divided by the total number of the old and new shares.

(2) Where the stock distributed in reorganization is in whole or in part stock in a corporation a party to the reorganization other than the distributing corporation, or where the stock distributed in reorganization is in whole or in part stock of a character or preference materially different from the stock in respect of which the distribution is made, or where the distribution consists wholly or partly of securities other than stock, the cost or other basis of the stock in respect of which the distribution is made shall be apportioned between such stock and the stock or securities distributed in proportion, as nearly as may be, to the respective values of each class of stock or security, old and new, at the time of such distribution, and the basis of each share of stock or unit of security will be the quotient of the cost or other basis of the class of stock or security with which such share or unit belongs, divided by the number of shares or units in the class. Within the meaning of the foregoing provision, securities are different in class from stocks, stocks or securities in one corporation are different in class from stocks or securities in another corporation, and, in general, any material difference in character or preference or terms sufficient to distinguish one stock or security from another stock or security so that different values may properly be assigned thereto, will constitute a difference in class. The application of this rule is subject to the limitation that the portion of the cost or other basis of the stock in respect of which the distribution is made to be attributed to the stock or securities distributed in reorganization shall in no case exceed the fair market value of such stock or securities as of the time of their distribution.

(3) Where the stock in respect of which a distribution in reorganization is made was purchased at different times and at different prices, and the identity of the lots can not be determined, any sale of the original stock will be charged to the earliest purchases of such stock (see article 39), and any sale of the stock or securities distributed in reorganization will be presumed to have been made from the stock or securities distributed in respect of the earliest purchased stock.

(4) Where the stock in respect of which a distribution in reorganization is made was purchased at different times and at different prices, and the stock or securities distributed in reorganization can not be identified as having been distributed in respect of any particular lot of such stock, then any sale of the stock or securities distributed in reorganization will be presumed to have been made from the stock or securities distributed in respect of the earliest purchased stock.

Article 1599 of Regulations 69, as amended by Treasury Decision 4144 (C. B. VII-1, 55), is hereby further amended to read as follows:

ART. 1599. *Stock or securities distributed in reorganization.*—In the case of stock or securities acquired by a shareholder after December 31, 1923, in connection with a transaction described in section 203(c) and article 1576, the basis in the case of the stock in respect of which the distribution was made shall be apportioned between such stock and the stock or securities distributed to the shareholder. The basis for the old shares and the new shares or securities shall be determined in accordance with the following rules:

(1) Where the stock distributed in reorganization consists solely of stock in the distributing corporation and is all of substantially the same character and preference as the stock in respect of which the distribution is made, the basis of each share will be the quotient of the cost or other basis of the old shares of stock divided by the total number of the old and new shares.

(2) Where the stock distributed in reorganization is in whole or in part stock in a corporation a party to the reorganization other than the distributing corporation, or where the stock distributed in reorganization is in whole or in part stock of a character or preference materially different from the stock in

respect of which the distribution is made, or where the distribution consists wholly or partly of securities other than stock, the cost or other basis of the stock in respect of which the distribution is made shall be apportioned between such stock and the stock or securities distributed in proportion, as nearly as may be, to the respective values of each class of stock or security, old and new, at the time of such distribution, and the basis of each share of stock or unit of security will be the quotient of the cost or other basis of the class of stock or security with which such share or unit belongs, divided by the number of shares or units in the class. Within the meaning of the foregoing provision, securities are different in class from stocks, stocks or securities in one corporation are different in class from stocks or securities in another corporation, and, in general, any material difference in character or preference or terms sufficient to distinguish one stock or security from another stock or security so that different values may properly be assigned thereto, will constitute a difference in class.

(3) Where the stock in respect of which a distribution in reorganization is made was purchased at different times and at different prices, and the identity of the lots can not be determined, any sale of the original stock will be charged to the earliest purchases of such stock (see article 39), and any sale of the stock or securities distributed in reorganization will be presumed to have been made from the stock or securities distributed in respect of the earliest purchased stock.

(4) Where the stock in respect of which a distribution in reorganization is made was purchased at different times and at different prices, and the stock or securities distributed in reorganization can not be identified as having been distributed in respect of any particular lot of such stock, then any sale of the stock or securities distributed in reorganization will be presumed to have been made from the stock or securities distributed in respect of the earliest purchased stock.

Article 600 of Regulations 74 is hereby amended to read as follows:

ART. 600. *Stock or securities distributed in reorganization.*—In the case of stock or securities acquired by a shareholder after December 31, 1923, in connection with a transaction described in section 112(g) and article 576, the basis in the case of the stock in respect of which the distribution was made shall be apportioned between such stock and the stock or securities distributed to the shareholder. The basis for the old shares and the new shares or securities shall be determined in accordance with the following rules:

(1) Where the stock distributed in reorganization consists solely of stock in the distributing corporation and is all of substantially the same character and preference as the stock in respect of which the distribution is made, the basis of each share will be the quotient of the cost or other basis of the old shares of stock divided by the total number of the old and new shares.

(2) Where the stock distributed in reorganization is in whole or in part stock in a corporation a party to the reorganization other than the distributing corporation, or where the stock distributed in reorganization is in whole or in part stock of a character or preference materially different from the stock in respect of which the distribution is made, or where the distribution consists wholly or partly of securities other than stock, the cost or other basis of the stock in respect of which the distribution is made shall be apportioned between such stock and the stock or securities distributed in proportion, as nearly as may be, to the respective values of each class of stock or security, old and new, at the time of such distribution, and the basis of each share of stock or unit of security will be the quotient of the cost or other basis of the class of stock or security with which such share or unit belongs, divided by the number of shares or units in the class. Within the meaning of the foregoing provision, securities are different in class from stocks, stocks or securities in one corporation are different in class from stocks or securities in another corporation, and, in general, any material difference in character or preference or terms sufficient to distinguish one stock or security from another stock or security so that different values may properly be assigned thereto, will constitute a difference in class.

(3) Where the stock in respect of which a distribution in reorganization is made was purchased at different times and at different prices, and the identity of the lots can not be determined, any sale of the original stock will be charged to the earliest purchases of such stock (see article 58), and any sale of the

stock or securities distributed in reorganization will be presumed to have been made from the stock or securities distributed in respect of the earliest purchased stock.

(4) Where the stock in respect of which a distribution in reorganization is made was purchased at different times and at different prices, and the stock or securities distributed in reorganization can not be identified as having been distributed in respect of any particular lot of such stock, then any sale of the stock or securities distributed in reorganization will be presumed to have been made from the stock or securities distributed in respect of the earliest purchased stock.

ROBT. H. LUCAS,

Commissioner of Internal Revenue.

Approved November 13, 1929.

A. W. MELLON,

Secretary of the Treasury.

SECTION 206.—NET LOSSES.

ARTICLE 1625: Net losses of partnerships, estates and trusts, and insurance companies.

REVENUE ACT OF 1924.

Net loss of beneficiary under a trust governed by section 704(b), Revenue Act of 1928, or a trust similar to one considered in General Counsel's Memorandum 4120 (C. B. VII-2, 108). (See G. C. M. 6630, page 179.)

SECTION 208.—CAPITAL GAINS AND LOSSES.

ARTICLE 1651: Definition and illustration of capital net gain.

REVENUE ACT OF 1924.

Stock called in or bond redeemed before maturity date. (See I. T. 2488, page 127.)

ARTICLE 1653: Partnerships, estates, and trusts.

REVENUE ACT OF 1924.

Profit derived from sale of land covered by a trust governed by section 704(b), Revenue Act of 1928, or a trust similar to one considered in General Counsel's Memorandum 4120 (C. B. VII-2, 108). (See G. C. M. 6630, page 179.)

PART II.—INDIVIDUALS.

SECTION 213(a).—GROSS INCOME DEFINED:
INCLUSIONS.ARTICLE 32: Compensation for personal
services.VIII-39-4369
G. C. M. 6822

REVENUE ACT OF 1924 AND PRIOR ACTS.

The effect of the promulgation of I. T. 2202 (C. B. IV-2, 41) was by implication to revoke I. T. 1243 (C. B. I-1, 70), so that the latter ruling can no longer be regarded as in effect.

An opinion is requested as to whether I. T. 2202 revokes I. T. 1243. It is held in I. T. 2202 that income "taxes assessed on the salaries of judges of the United States courts, both after as well as before retirement, are illegal and are refundable in accordance with the provisions of the law."

At the time I. T. 2202 was under consideration the basis upon which I. T. 1243 was predicated, i. e., a Federal judge "having resigned, is no longer 'in office' within the constitutional or statutory provisions for the exemption of compensation which he receives under section 714, Revised Statutes," was disapproved. The effect of the promulgation of I. T. 2202 was therefore by implication to revoke I. T. 1243, so that the latter ruling can no longer be regarded as in effect.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

ARTICLE 39: Sale of stock and rights.

REVENUE ACT OF 1924.

Rights to subscribe to bonds. (See I. T. 2494, page 76.)

ARTICLE 48: Improvements by lessees.

VIII-52-4484
T. D. 4281

INCOME TAX.

Article 48 of Regulations 65 and article 48 of Regulations 69 amended.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, D. C.

To Collectors of Internal Revenue and Others Concerned:

Article 48 of Regulations 65 and article 48 of Regulations 69 are hereby amended to read as follows:

ART. 48. *Improvements by lessees.*—When buildings are erected or improvements made by a lessee in pursuance of an agreement with the lessor, and such buildings or improvements are not subject to removal by the lessee, the lessor

may at his option report the income therefrom upon either of the following bases:

(a) The lessor may report as income at the time when such buildings or improvements are completed the fair market value of such buildings or improvements subject to the lease.

(b) The lessor may spread over the life of the lease the estimated depreciated value of such buildings or improvements at the expiration of the lease and report as income for each year of the lease an aliquot part thereof.

Except in cases where the lessor has exercised the option to report income upon basis (b), if the lease is terminated so that the lessor comes into possession or control of the property prior to the time originally fixed for the expiration of the lease, the lessor derives no income by reason thereof, and, just as when the lessor comes into possession or control of the property upon the expiration of the lease, the basis for determining gain or loss to the lessor from the subsequent sale or other disposition of the buildings or improvements and for depreciation in respect of such property is the amount previously reported as income by the lessor because of the erection of the buildings or improvements, except that if the buildings or improvements were acquired prior to March 1, 1913, the basis shall be their value subject to the lease when acquired or their value subject to the lease on March 1, 1913, whichever is greater. If the buildings or improvements are destroyed prior to the expiration of the lease, the lessor is entitled to deduct as a loss for the year when such destruction takes place the amount previously reported as income because of the erection of such buildings or improvements, less any salvage value subject to the lease to the extent that such loss is not compensated for by insurance or otherwise. If the buildings or improvements destroyed were acquired prior to March 1, 1913, the deduction shall be based on their value subject to the lease when acquired or their value subject to the lease on March 1, 1913, whichever is greater, less any salvage value subject to the lease to the extent that such loss is not compensated for by insurance or otherwise. (See articles 110 and 164.)

In all cases where the lessor has exercised the option to report income upon basis (b), if the lease is terminated so that the lessor comes into possession or control of the property prior to the time originally fixed for the expiration of the lease, the lessor derives additional income for the year in which the lease is so terminated to the extent that the value of such buildings or improvements when he becomes entitled to such possession exceeds the amount already reported as income on account of the erection of such buildings or improvements. No appreciation in value due to causes other than the termination of the lease shall be included. If the buildings or improvements are destroyed prior to the expiration of the lease, the lessor is entitled to deduct as a loss for the year when such destruction takes place the amount previously reported as income because of the erection of such buildings or improvements, less any salvage value subject to the lease to the extent that such loss is not compensated for by insurance or otherwise.

ROBT. H. LUCAS,

Commissioner of Internal Revenue.

Approved December 19, 1929.

OGDEN L. MILLS,

Acting Secretary of the Treasury.

SECTION 213(b).—GROSS INCOME DEFINED: EXCLUSIONS.

ARTICLE 89: Additional exclusions from gross income.

REVENUE ACT OF 1924.

Amendment of article 89, Regulations 65, to include Greece in the list of countries which satisfy the equivalent exemption requirement of section 213(b)8 of the Revenue Act of 1924. (See T. D. 4269, page 146.)

SECTION 214(a)1.—DEDUCTIONS ALLOWED INDIVIDUALS: BUSINESS EXPENSES.

ARTICLE 112: When charges deductible.
(Also Section 281, Article 1301.)

VIII-47-4437
Ct. D. 130

INCOME TAX—REVENUE ACTS OF 1921 AND 1924—DECISION OF COURT.

1. DEDUCTION—EXPENSES—WHEN DEDUCTIBLE.

Where a taxpayer keeps his accounts on the basis of cash receipts and disbursements, amounts are not deductible in 1922, 1923, and 1924 which were paid in 1926 following a judicial determination in the latter year that they were expenses due from the taxpayer for the former years.

2. REFUND—SUIT—BY WHOM BROUGHT—SUBROGEE.

A claim for taxes is not assignable and is not a debt within the meaning of the subrogation laws and a subrogee can not maintain a suit for the recovery of a tax paid by its subrogor.

DISTRICT COURT OF THE UNITED STATES FOR THE WESTERN DISTRICT OF PENNSYLVANIA.

Fidelity Title & Trust Co., Miriam C. Hostetter, and Helene Hostetter, Executors of the Will of D. Herbert Hostetter, Deceased, for Use of The Pittsburgh & West Virginia Railway Co., plaintiffs, v. D. B. Heiner, Collector of Internal Revenue, defendant.

[March 22, 1929.]

OPINION.

McVICAR, J.: This case comes before us on an affidavit of defense raising questions of law.

D. Herbert Hostetter made a return of his income taxes for the years 1922 and 1923; the executors of his estate made a return for the year 1924, Hostetter having died September 28, 1924. The return was made on a cash basis and included income from a certain building situated at the corner of Water and Ferry Streets, in the city of Pittsburgh.

The Pittsburgh & West Virginia Railway Co. furnished the Hostetter Building with electric power and steam during the years 1922, 1923, and 1924, under contract. In February, 1925, it was discovered that there had been a mistake in the meter readings, and the railway company claimed that there was an additional amount due it on account thereof. This claim was resisted by the executors of the estate, and an action was brought in the Orphans' Court of Allegheny County, Pa. The executors defended the action, and claimed further that if any amount should be found due the railway company, that the estate was entitled to a credit for the additional income paid during the aforementioned years. The orphans' court aforesaid, on June 3, 1926, entered a decree in favor of the railway company, and also decided in favor of the estate as to the set-off for income taxes.

The Hostetter estate, which has been fully administered, made a claim to the Commissioner of Internal Revenue for a refund of the taxes to which it had been given a credit by the Orphans' Court of Allegheny County. This claim was rejected, and subsequently the action in this case was brought by the executors of the Hostetter estate for the use of the Pittsburgh & West Virginia Railway Co.

The defendant, in his affidavit of defense raising questions of law, alleges that the plaintiffs are not entitled to recover, for the reason that it appears on the face of the statement of claim that the income tax reports were made on the basis of cash receipts and disbursements, and that the amount sought to be recovered in this action was a deduction allowable (if at all) subsequent to the year 1924.

There was no overpayment of taxes for the years 1922, 1923, and 1924, so far as the facts in this case appear. The taxpayer chose to make his return and to pay his taxes upon the basis of cash actually received and disbursed instead

of upon the accrual basis. The credits which he now seeks were not judicially determined, nor actually paid until the year 1926, hence the credits claimed were not proper credits for the taxable years aforementioned. (Sanford & Brooke Co., 11 B. T. A., 452; *Consolidated Tea Co. v. Bowers*, 19 Fed. (2d), 382 [T. D. 4020, C. B. VI-1, 214]; *Jackson v. Smetanka*, 272 Fed., 970 [T. D. 3159, C. B. 4, 96].) Even if plaintiff's position was correct, it would be necessary that it appear that the additional credit claimed for each year would have been paid that year, even if he had knowledge thereof. There is no such averment in the statement of claim.

The defendant also alleges that the plaintiffs are not entitled to recover for the reason that it appears on the face of the statement of claim that no right of subrogation to the Hostetter estate could be exercised by the Pittsburgh & West Virginia Railway Co. The legal plaintiffs in this case, the executors of the Hostetter estate, have no interest in the claim for refund of the taxes for which this action is brought, as they have received a credit therefor in the orphans' court and the estate has been fully administered. The claim for taxes is not assignable. It is not a debt within the meaning of the subrogation laws. See *Carleton Dry Goods Co. v. U. S.*, 1928 (T. D. 4209 [C. B. VII-2, 172]), which is a decision by the District Court of the United States for the Eastern District of Missouri.

The affidavit of defense raising questions of law is sustained.

SECTION 214(a)3.—DEDUCTIONS ALLOWED INDIVIDUALS: TAXES.

ARTICLE 131: Taxes.

VIII-49-4452
I. T. 2511

REVENUE ACT OF 1924.

I. T. 2157 (C. B. IV-1, 35) is revoked in so far as it holds that the motor vehicle fuel tax imposed by the State of Maryland is deductible only by the dealers. (See G. C. M. 7167, page 110.)

ARTICLE 132: Federal duties and excise taxes.

VIII-45-4424
Ct. D. 129

INCOME TAX—REVENUE ACTS OF 1918, 1921, AND 1924—DECISION OF COURT.

1. DEDUCTION—TAX ADDED TO COST OF GOODS—AMENDED RETURN.

Where a taxpayer adds import duties to the cost of merchandise with respect to which they are paid and makes income tax returns accordingly, it may not thereafter file amended returns deducting such duties from gross income as taxes and thereby become entitled to a refund.

2. SAME.

Where there are two methods of making an income tax return, either one of which is legal and proper and the taxpayer has made his return in accordance with one of these methods, then, if the return is accepted and the tax paid accordingly, the taxpayer can not subsequently change to the other method of making a return and thereby become entitled to a refund.

COURT OF CLAIMS OF THE UNITED STATES.

Lebolt & Co. v. The United States.

[April 1, 1929.]

OPINION.

GREEN, Judge, delivered the opinion of the court.

The plaintiff in this case is an importer and in carrying on its business paid duties on goods imported from foreign countries during the years 1920 to 1924, inclusive. The amount of duty so paid was carried to a "duty account" on its books, and that part of the customs duties applicable to goods sold during a particular year was charged to plaintiff's profit and loss account and deducted from income, while the remaining amount of customs duties paid during a particular taxable year was added to plaintiff's inventory at the end of that year. This method was equivalent to adding the amount paid as duties to the cost of the goods and making its returns accordingly. During the four years in question plaintiff made its tax returns on this basis and paid taxes in accordance therewith. It now seeks to make amended returns which, instead of including the duties paid in the cost of goods, would deduct the amount of the duties from the gross income in the same manner as other taxes paid. The Commissioner of Internal Revenue refused to accept the amended returns made in this manner and to allow plaintiff's claim for refund. The question involved in the case is whether the plaintiff, having originally made its returns as above stated, can now change its method for the years under consideration and thereby secure a refund of taxes.

The weight of authority is to the effect that where there are two methods of making an income-tax return, either one of which is legal and proper, and the taxpayer has made his return in accordance with one of these methods, then, if the return is accepted and taxes paid accordingly, the taxpayer can not subsequently change to the other method of making a return and thereby become entitled to a refund. But if there is only one legal and proper method of making a return and the taxpayer erroneously makes his return by some other method, then, even though the return has been accepted and the taxes paid, he may file an amended return correcting the error, and if this return shows an overpayment, he becomes entitled to a refund.

Counsel for defendant contend that there were two proper methods of making a return in the case at bar, and that the plaintiff could either add the duties paid to the cost of the goods imported and make its return accordingly, or it could deduct the amount of the duties paid from its gross income and make its return on that basis. On behalf of the plaintiff, it is insisted that there was but one correct method of making the return, and that was to include the duties paid among the deductions from gross income.

Regulations 45 and 62 made by the Commissioner of Internal Revenue prescribe the manner of treating import duties in article 132, which is as follows:

"ART. 132. *Federal duties and excise taxes.*—Import or tariff duties paid to the proper customs officers, and business, license, privilege, excise, and stamp taxes paid to internal revenue collectors, are deductible as taxes imposed by the authority of the United States, provided they are not added to and made a part of the expenses of the business or the cost of articles of merchandise with respect to which they are paid, in which case they can not be separately deducted."

It is evident that under this article either method might be used, and it would seem that the authorities on accounting lend some support to this regulation in that it appears that the method originally adopted by plaintiff is in accordance with good accounting practice.

In article 23 of the above-mentioned regulations it is said that:

"Approved standard methods of accounting will ordinarily be regarded as clearly reflecting income."

The plaintiff, however, insists that there is no authority in law for the regulation or the method which it followed in originally making its returns, and in support of this contention cites a part of section 234(a)3 of the Revenue Acts of 1918 (40 Stat., 1077) and 1921 (42 Stat., 254), to the effect that taxes paid or accrued within the taxable year "shall be allowed as deductions" in computing the net income of a corporation.

This the plaintiff says is mandatory, and gives the Commissioner no discretion. Hence it is said that any return purporting to set forth the taxable net income of a corporation is not correct if, in computing the taxable income, it does not show a deduction of all taxes paid or accrued within the taxable year, with certain exceptions not necessary to specify here.

We do not think this provision is mandatory. While it says that taxes paid shall be allowed as deductions, we think this means that they shall be so allowed if claimed as deductions from gross income and a benefit therefrom is not claimed in some other way. While the words "to allow" or "allowance" do not necessarily refer to a case in which a claim has been made, the dictionaries indicate that it is frequently so used, and we think it was used in such a sense in that portion of the statute under consideration.

Items of expense in connection with the purchase of goods are almost invariably added to the cost of goods by accountants; and when it becomes necessary to determine a cost of goods for the purpose of making an income-tax return, there would ordinarily be no question of the propriety of thus making up the account for income-tax purposes. The plaintiff made up its inventory on the basis of cost. While the question is not free from doubt, we think that it might properly do so and make its returns accordingly.

It follows that plaintiff's petition must be dismissed, and it is so ordered.

SECTION 214(a)9.—DEDUCTIONS ALLOWED INDIVIDUALS: DEPLETION.

ARTICLE 202: Amount returnable through depletion and depreciation deductions in the case of an operating owner.

REVENUE ACT OF 1924.

Computation basis. (See G. C. M. 6746, page 119.)

SECTION 219.—ESTATES AND TRUSTS.

ARTICLE 341: Estates and trusts.

REVENUE ACT OF 1924.

Annuity payments to widow in lieu of her dower or statutory interest. (See I. T. 2480, page 141.)

ARTICLE 343: Decedent's estate during administration.

REVENUE ACT OF 1924.

Royalties under a coal lease in Pennsylvania during period decedent's estate was in process of administration. (See G. C. M. 6906, page 205.)

ARTICLE 347: Income of trusts taxable to grantor.

VIII-30-4286
Ct. D. 83

INCOME TAX—REVENUE ACT OF 1924—DECISION OF COURT.

INCOME—TRUST—TAXABLE TO GRANTOR—CONSTITUTIONALITY—RETROACTIVITY.

Subdivisions (g) and (h) of section 219 of the Revenue Act of 1924, requiring that the income of a trust which is subject to revocation by the grantor or which is for the benefit of the grantor shall be included in computing the net income of the grantor, are constitutional even as applied to the income of such a trust created before the effective date of that section.

UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

Charles A. Cortliss, plaintiff-appellant, v. Frank K. Bowers, as Collector of Internal Revenue for the Second District of New York, defendant-appellee.

Appeal from the District Court for the Southern District of New York. Action to recover income taxes paid by the plaintiff under duress. On motion, a judgment was entered dismissing the complaint; plaintiff appeals. Judgment affirmed.

Before MANTON, L. HAND, and CHASE, Circuit Judges.

[June 24, 1929.]

OPINION.

MANTON, Circuit Judge: On December 29, 1922, appellant delivered a trust indenture to the trustee therein named, the Bankers Trust Co. of New York City, together with corporate stocks and securities listed in the schedules annexed to the indenture. It was a trust revocable at any time at the will of the settlor. The trustee was obligated to collect the income from the securities and pay them to the appellant's wife for the term of her life. Upon her death the principal of the trust was then to be paid in equal shares to the appellant's children then living and the issue of any deceased child or children, and in default thereof, to such persons as appellant's wife might designate and appoint. The trust was conceded to be valid under the laws of the State of New York. By its terms, the appellant reserved the right, in addition to revocation, to modify or alter in any manner, in whole or in part, the indenture and trust created thereby. The trust remained in this form in 1924, when the income for that year was paid by the trustee to the appellant's wife. The appellant received none of it. In appellant's report of his income for that year, he made note of this trust and the amount of the income, but claimed exemption from tax. He was later assessed \$44,687.43 with interest on the income so paid to his wife, which he has paid under protest and now sues to recover it.

The appellant's contention is that section 219 (g-h) of the Act of 1924 (43 Stat., 277), under which this assessment was made, is unconstitutional because it requires him to pay a tax upon the income of another, and, if it be constitutional, it is retroactive and therefore invalid as applied to income for 1924 upon the trust created in 1922. Section 219 provides:

"(g) Where the grantor of a trust has, at any time during the taxable year, either alone or in conjunction with any person not a beneficiary of the trust, the power to revest in himself title to any part of the corpus of the trust, then the income of such part of the trust for such taxable year shall be included in computing the net income of the grantor.

"(h) Where any part of the income of a trust may, in the discretion of the grantor of the trust, either alone or in conjunction with any person not a beneficiary of the trust, be distributed to the grantor or be held or accumulated for future distribution to him, or where any part of the income of a trust is or may be applied to the payment of premiums upon policies of insurance on the life of the grantor (except policies of insurance irrevocably payable for the purposes and in the manner specified in paragraph (10) of subdivision (a) of section 214), such part of the income of the trust shall be included in computing the net income of the grantor."

The moneys paid to the appellant's wife, as income from this trust, were taxable to her (*Irwin v. Gavit*, 268 U. S., 161 [T. D. 3710, C. B. IV-1, 123]) prior to the 1924 Act. The trust indenture vested the legal title to the corpus of the estate in the trustee. (*Jones v. Clifton*, 101 U. S., 225; *The Farmers' Loan & Trust Co. v. Bowers*, 29 Fed. (2d), 14 [T. D. 3988, C. B. VI-1, 318].) The present estate vested in the beneficiary, created by this revocable trust, was valid until the power of revocation was exercised. The question here is whether Congress had the power to tax the grantor of the trust for income paid to the beneficiary where the money, as income in the hands of the trustee, was paid to the beneficiary therein named. In *Taft v. Bowers* (278 U. S., 470 [Ct. D. 49, C. B. VIII-1, 226]), an increase in the value of a gift accruing prior to the time gift was made, while in the hands of the donor, was held to be subject to a tax to be paid by the donee when she, at a later date, sold the securities. A husband was held subject to the payment of a tax upon the whole of the

income of community property held under a State statute of California and owned jointly by husband and wife in *United States v. Robbins* (269 U. S., 315 [T. D. 3817, C. B. V-1, 188]).

Section 219, according to the legislative debates, was enacted to "secure clarity and prevent the evasion of taxes by means of estates and trusts." (House of Representatives, volume 1, Sixty-eighth Congress, first session, dealing with H. R. 6715 (1924) Revenue Act; Senate reports, volume 1, page 25 (1924); Sixty-eighth Congress, first session, volume 4, pages 19-20.) Congress, by the sixteenth amendment, was granted power to lay and collect taxes on incomes, and we think, under the principle of the cases referred to, it could command a settlor of a revocable trust to pay a tax on income paid to a beneficiary in the scheme of lawful taxation if the method devised by Congress does not become arbitrary or capricious and violate the fifth amendment. A settlor of a revocable trust has a sufficient interest in the income of the trust and a relation thereto to justify the claim of a necessity for a fair and proper tax imposition requiring the settlor to pay. He, at all times, has the power to make the income derived from the trust, his own. To defeat tax evasion, at least the higher surtax, Congress, by this statute, has determined that a grantor who may change or modify the gift, even to putting an end to its continuance, must pay. By such a trust indenture, the grantor gives and the grantee receives with knowledge of who shall bear the burden of taxation. There is no constitutional reason against subjecting the settlor to such a tax and the sixteenth amendment grants very general taxing power. (*Brushaber v. Union Pacific R. R. Co.*, 240 U. S., 1; *Frew v. Bowers*, 12 Fed. (2d), 625 [T. D. 3789, C. B. IV-2, 258].) If the taxation involves reasonableness to meet the desired ends of fair play, it is valid. (*Nichols v. Coolidge*, 274 U. S., at 542 [T. D. 4072, C. B. VI-2, 351].) And when the tax is arbitrary or capricious by reason of the terms of the taxing statute, it becomes void under the fifth amendment. Where the trust is revocable, it is not unfair to tax the person who always has a will he may exercise and divert from the recipient a part or all of the income. As was said by us in *Mitchell v. Bowers* (15 Fed. (2d), 287 [T. D. 3982, C. B. VI-1, 244]), "throughout the period the right of disposition remained."

By section 145 of the New York real property law (where this indenture was made), when the grantor in the conveyance reserves to himself for his own benefit a power of revocation, he is deemed the absolute owner of the estate conveyed so far as the rights of creditors and purchasers are concerned, illustrating how little the beneficiary obtains apart from the income. Under the Federal estate tax law, the term "gross income" includes trust funds conveyed by a revocable indenture. (*Reinecke v. Northern Trust Co.*, 278 U. S., 339 [T. D. 4261, C. B. VIII-1, 305]; *Chase Natl. Bank v. United States*, 278 U. S., 327 [Ct. D. 40, C. B. VIII-1, 308].) This is because the grantor at all times had the power to make the funds his and the nonexercise of the power is as much evidence of testamentary disposition as the exercise would be. The settlor might, if he wished, make each income payment under the grant his own. This he could do by exercising his power of revocation. Congress has expressed a sufficient reason and, from the viewpoint of a Revenue Act, it is reasonable, if not commendable. This exercise of power, based upon reason for taxation, is within the power of Congress in its desire to prevent evasion and gives practical effect to the exercise of its admitted power. (*Nichols v. Coolidge*, *supra*.)

The tax involved here is for the year 1924 and the indenture was made in 1922. It is argued that even if the statute is valid, it can not be constitutional as applied to a trust created prior to its effective date. This assumed retroactivity does not invalidate the statute. The statute deals with the present condition with revocability residing in the settlor. Each payment of income which takes place after the passage of the statute is subject to its terms. Therefore, after the effective date of the taxing statute, this income was subject to taxation under its requirements. The taxing statute is not retroactive. (*Reinecke v. Northern Trust Co.*, *supra*; *Chase Natl. Bank v. United States*, *supra*; *Saltonstall v. Saltonstall*, 276 U. S., 260.)

Judgment affirmed.

SECTION 222.—CREDIT FOR TAXES IN CASE OF INDIVIDUALS.

ARTICLE 381: Analysis of credit for taxes.

VIII-31-4293
I. T. 2485

REVENUE ACTS OF 1918, 1921, AND 1924.

In view of the Commissioner's acquiescence in the decision of the United States Board of Tax Appeals in the appeal of Herbert Ide Keen (15 B. T. A., 1243 see on page 27), Office Decision 1093 (C. B. 5, 194) and Solicitor's Memorandum 3155 (C. B. IV-1, 45), holding that the tax imposed by France under the income tax laws of France at income tax rates upon an amount arbitrarily fixed at seven times the rental value of the residence of the taxpayer is not such a tax as may be credited against a taxpayer's Federal income tax, are revoked.

PART III.—CORPORATIONS.

SECTION 238.—CREDIT FOR TAXES IN CASE OF CORPORATIONS.

ARTICLE 611: Credit for foreign taxes.

REVENUE ACT OF 1924.

Computation of credit for foreign taxes of affiliated group of corporations. (See G. C. M. 6640, page 212.)

SECTION 240.—CONSOLIDATED RETURNS OF CORPORATIONS.

ARTICLE 631: Affiliated corporations.

REVENUE ACT OF 1924.

Computation of credit for foreign taxes. (See G. C. M. 6640, page 212.)

PART V.—PAYMENT, COLLECTION, AND REFUND OF TAX AND PENALTIES.

SECTIONS 277 AND 278.—PERIOD OF LIMITATION UPON ASSESSMENT AND COLLECTION OF TAX.

ARTICLE 1271: Period of limitation upon assessments of tax.

VIII-35-4328
G. C. M. 6050

REVENUE ACTS OF 1918, 1921, AND 1924.

In view of the decision of the United States Court of Claims in *Mary S. Aldridge, Executrix, v. United States* (64 Ct. Cls., 424, T. D. 4251 (C. B. VII-2, 215)), and the decision of the United States

Board of Tax Appeals in *Estate of John F. Dodge, deceased, v. Commissioner* (13 B. T. A., 201), Solicitor's Memorandum 2300 (C. B. III-2, 298), holding that "Waivers filed by executors or administrators on behalf of estates of decedents for 1918 will not operate to extend the period for filing claims for refund or credit, as provided in section 281(e) of the Revenue Act of 1924, unless the executor or administrator is authorized to waive a statute of limitations under the laws of the particular jurisdiction," and all other memoranda, in so far as they are inconsistent with the decisions in the Aldridge and Dodge cases, are revoked.

Prior to the enactment of the Revenue Act of 1926 it was the position of the Bureau (see S. M. 2300) that the validity of waivers executed by executors and administrators was governed by the law of the jurisdiction in which the fiduciary was acting.

Under date of January 16, 1928, the United States Court of Claims, in the case of *Mary S. Aldridge, Executrix of the Last Will and Testament of William O. Aldridge, deceased, v. United States*, held that a waiver executed by an executrix is valid irrespective of the State law, stating in its opinion: "The tax system of the United States is regulated by Federal statutes and practice, and is not controlled by State enactments. * * * Congress having undertaken to regulate the whole subject, its legislation is necessarily exclusive." The case involved a suit based on a claim for refund which had been rejected by the Commissioner on the ground that the executrix had no authority to execute a waiver which would give validity to the refund claim.

The United States Board of Tax Appeals in the case of the *Estate of John F. Dodge, deceased, v. Commissioner* followed the decision in the Aldridge case, *supra*, and held that an assessment was valid which was made within the time prescribed in a waiver executed by the administrator of the estate, and that the State law had no effect upon the right of the personal representative to waive the statute of limitations.

In view of the two decisions referred to, Solicitor's Memorandum 2300, *supra*, and all other memoranda of this office, in so far as they are inconsistent with the decisions in the Aldridge and Dodge cases, *supra*, are revoked.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

ARTICLE 1271: Period of limitation upon assessments of tax.

VIII-36-4338
Ct. D. 98

INCOME AND PROFITS TAXES—REVENUE ACT OF 1924—DECISION OF COURT.

1. WAIVER—ACCEPTANCE—WITHDRAWAL—NOTICE.

A consent in writing, filed by a taxpayer pursuant to section 250(d) of the Revenue Act of 1921, to a determination, assessment, and collection of taxes irrespective of any statutory period of limitation remains open to acceptance by the Commissioner at any time prior to the expiration of the statutory period unless previously withdrawn by notice to the Commissioner. If the Commissioner executes the waiver before the taxpayer withdraws it and before the statutory period for assessment has run, the waiver is executed as the statute requires, a notice to the taxpayer of the Commissioner's execution being unnecessary.

2. UNLIMITED WAIVER—EXPIRATION.

A waiver in terms unlimited as to time expires only after the taxpayer gives notice to the Commissioner that he will regard the waiver as at an end after a reasonable time.

3. COLLECTION—LIMITATION—WAIVER.

A waiver consenting to a determination, assessment, and collection of taxes, irrespective of any statute of limitation, extends the time for collecting the taxes beyond the statutory period therefor, although the waiver was given after the taxes were assessed.

4. UNLIMITED WAIVER—EXPIRATION BY COMMISSIONER'S RULING.

A waiver filed by a taxpayer consenting to the determination, assessment, and collection of taxes for the years 1917 to 1920, inclusive, irrespective of any period of limitation, remained in effect for the years 1918 and 1919 after a date fixed by the Commissioner in an official ruling as to the time of expiration of waivers for the year 1917.

5. DECISION AFFIRMED.

The decision of the United States Board of Tax Appeals (9 B. T. A., 1281) affirmed.

UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

The Greylock Mills v. Commissioner of Internal Revenue.

Appeal from the United States Board of Tax Appeals.

[April 1, 1929.]

OPINION.

SWAN, Circuit Judge: From an order determining deficiencies in income and profits taxes for the six-months period ending June 30, 1918, and for the fiscal year ending June 30, 1919, the taxpayer, a Massachusetts corporation, has invoked the jurisdiction of this court by petition to review, pursuant to section 1002(d) of the Revenue Act of 1926. (44 Stat., 110.) The opinion below is reported in 9 B. T. A., 1281. Affirmed.

The validity of the contested taxes turns upon the statute of limitations and an alleged waiver thereof by the taxpayer. Notice of the deficiency assessments was mailed to the taxpayer on December 18, 1925. This was too late unless the time was extended by the waiver, because the 5-year period for assessment, provided by section 250(d) of the Revenue Act of 1921 (42 Stat., 265), and reaffirmed by section 277(a)2 of the Revenue Act of 1924 (43 Stat., 299), expired in respect to taxes for the six-months period of 1918 on June 15, 1924, and in respect to taxes for the 1919 fiscal year on September 19, 1924. The waiver in question was filed with the Commissioner on February 6, 1923, and recited that, pursuant to section 250(d) of the Revenue Act of 1921, the taxpayer and the Commissioner "hereby consent to a determination, assessment, and collection of the amount of income, excess-profits, and war-profits taxes due under any return made by or on behalf of the said corporation for the years 1917-1920, * * * irrespective of any period of limitations."

The validity of the waiver is assailed upon the ground that it was never duly executed by the Commissioner. Section 250(d) of the Revenue Act of 1921 requires assessment within five years after the return was filed "unless both the Commissioner and the taxpayer consent in writing to a later determination, assessment, and collection of the tax." The waiver bore the signature of the taxpayer when it was filed. The precise date when the Commissioner's signature was affixed by his authorized agent does not appear, but the Board has found on sufficient evidence that it was within a reasonable time and prior to September, 1923. The legislative purpose in requiring the Commissioner to consent in writing to a later assessment is not apparent. The taxpayer waives the statute. What consideration the Commissioner gives in exchange is hard to see. It has not been suggested that such a waiver when signed by the Commissioner binds him to postpone the assessment until after the 5-year period has run, but unless

it does he binds himself to nothing which he is not already bound to do by his official duty. But even if the statute be deemed to contemplate a contract between the Commissioner and the taxpayer, there is nothing in the principles of contract law which would prevent the Commissioner from accepting the taxpayer's offer at any time while it remains open. Viewing the waiver filed by the taxpayer as an offer for a contract, we should construe it as intended to remain open to acceptance at any time prior to the running of the statutory period, unless previously withdrawn by notice to the Commissioner.

It is also contended that the Commissioner's execution of the waiver was invalid because he gave the taxpayer no notice of his acceptance of it and the taxpayer obtained no knowledge of its having been signed by the Commissioner until a conference between them on October 19, 1925. The statute says nothing as to when the Commissioner shall sign nor as to giving notice when he does so. If he signs before the taxpayer withdraws his waiver and before the statutory period for assessment has run, the waiver is executed as the statute requires. Nothing more is needed to give the waiver validity.

It is next argued that the waiver expired on April 1, 1924. This is based upon the Commissioner's ruling of April 11, 1923, known as "Mimeograph 3085" [C. B. II-1, 174]. It reads:

"The form of waiver now in use extends the time in which assessments of 1917 income and excess profits taxes may be made to one year from the date of signing by the taxpayer. Inasmuch as there are many waivers on file signed by taxpayers containing no limitation as to the time in which assessments for 1917 may be made, all such unlimited waivers will be held to expire April 1, 1924."

The ruling clearly relates exclusively to waivers as to 1917 taxes. The appellant's waiver was in legal effect a separate waiver as to taxes for each of the years therein mentioned. The argument that because these separate waivers were incorporated in a single memorandum all were affected by the ruling which affected one is so transparently without merit that we mention it merely to indicate it has not been overlooked.

Of similar character is the argument that the waiver as to 1918 taxes related to taxes for a full year and does not cover taxes for the six-month period ending June 30, 1918.

The next contention is that a waiver unlimited in time must be construed as authorizing action by the Commissioner only within a reasonable time and that a reasonable time for action had expired before December 18, 1925. Assuming without decision that the waiver requires action under it within a reasonable time, it is fallacious to begin to measure the time from the date of filing on February 6, 1923. The waiver begun to operate as an extension of the Commissioner's authority only after the 5-year period for assessment had ended, namely, June 15, 1924, as to the 1918 taxes and September 19, 1924, as to the 1919 taxes. The most the taxpayer can claim is that it expired within a reasonable time after those dates respectively. We are asked to rule that in no event could assessments made more than one year thereafter be deemed to be within a reasonable time. We are not disposed to adopt a standard so inflexible. The Board of Tax Appeals has found that a letter asserting a deficiency was sent to the taxpayer on August 27, 1925, resulting in negotiations, and that the parties were corresponding about the taxes in controversy as late as December 1, 1925. It found as a fact that the Commissioner acted within a reasonable time. We could hardly say this was error as a matter of law and we might rest our affirmance upon this ground. But there is also another ground equally fatal to appellant's contention. If waivers which are in terms unlimited are to be limited at all, we think they should expire only after the taxpayer gives notice to the Commissioner that he will regard the waiver as at an end after a reasonable time, say, three or four months, from the date of such notice. In such a rule there is no harshness to either party; on the contrary, it seems to us the most reasonable one. An analogy may perhaps be found in the case of contracts for the sale of land where time does not ordinarily become of the essence, unless expressly so stated, until notice is given by one party and an opportunity afforded to the other to act. (See *Myers v. DeMier*, 52 N. Y., 647; *Scudder v. Lehman*, 142 N. Y. App. Div., 631; *Brede v. Rosedale Terrace Co.*, 216 N. Y., 246, 250; *Boston & Worcester St. Ry. v. Rose*, 194 Mass., 142; *Martindale v. Waas*, 8 F., 854 (C. C. Minn.)) In the instant case, no such notice was given to the Commissioner and we think the waiver remained outstanding, so that he was entitled to act at his leisure.

Finally, the taxpayer challenges the collection by distraint on October 5, 1925, of \$28,298.98, being taxes shown to be due by its return for the fiscal year 1919, with interest thereon. These taxes were assessed November 26, 1919. It is claimed that in the absence of a waiver they could not be collected after September 19, 1924, five years from the date of the filing of the return. It is further claimed that the aforesaid waiver did not extend the time for collecting taxes already assessed. We think the waiver should be read disjunctively so as to authorize assessment or collection of any tax due for the fiscal year 1919. (See *Bowers v. N. Y. & Albany [Lighterage] Co.*, 273 U. S., 346, 351 [T. D. 4009, C. B. VI-1, 268].)

The order of the Board of Tax Appeals is affirmed.

ARTICLE 1271: Period of limitation upon assessments of tax.

VIII-48-4442
G. C. M. 7123

REVENUE ACT OF 1924.

The provisions of section 277(b)2 of the Revenue Act of 1924, extending the period of limitation in cases where an appeal is filed with the Board of Tax Appeals, refer only to an appeal filed within the 60-day period. The act of the taxpayer in filing the appeal after the elapse of the 60-day period did not make it any less the duty of the Commissioner to make the assessment in accordance with section 274(c) of the Revenue Act of 1924.

An opinion is requested as to whether an assessment for 1919 income taxes, made in August, 1925, was made within the statutory period of limitation properly applicable thereto.

The taxpayer's return for 1919 was filed on March 12, 1920. Upon audit of the return the Commissioner determined that there was a deficiency in tax, and under date of October 17, 1924, sent the taxpayer a 60-day letter notifying him of the deficiency. On December 17, 1924, the taxpayer filed an appeal with the Board of Tax Appeals, but the appeal was dismissed by the Board in April, 1925, for the reason that it had not been filed within the statutory period.

The deficiency in tax for 1919 was assessed in August, 1925, and the tax, including penalty and interest, was paid under protest on October —, 1925. No waiver was filed in respect of the taxes due for the taxable year 1919.

The taxpayer filed a claim for refund based on the ground that the deficiency was assessed after the expiration of the period of limitation allowed by the statute.

Section 280 of the Revenue Act of 1924 provides that any deficiency under the Revenue Act of 1918 shall be computed as though the 1924 Act had not been enacted, but when computed shall be assessed and collected as in the case of taxes imposed by Title II of the 1924 Act, except as otherwise provided in section 277 of that Act.

Section 277(a)2 of the Revenue Act of 1924 provides that the amount of income taxes imposed by the Revenue Act of 1918 shall be assessed within five years after the return was filed.

Section 274 (a) and (c) of the Revenue Act of 1924 reads as follows:

(a) If, in the case of any taxpayer, the Commissioner determines that there is a deficiency in respect of the tax imposed by this title, the taxpayer, except as provided in subdivision (d), shall be notified of such deficiency by registered mail, but such deficiency shall be assessed only as hereinafter provided. Within 60 days after such notice is mailed the taxpayer may file an appeal with the Board of Tax Appeals established by section 900.

(c) If the taxpayer does not file an appeal with the Board within the time prescribed in subdivision (a) of this section, the deficiency of which the taxpayer has been notified shall be assessed, and shall be paid upon notice and demand from the collector.

Section 277(b) of the 1924 Act reads as follows:

(b) The period within which an assessment is required to be made by subdivision (a) of this section in respect of any deficiency shall be extended (1) by 60 days if a notice of such deficiency has been mailed to the taxpayer under subdivision (a) of section 274 and no appeal has been filed with the Board of Tax Appeals, or, (2) if an appeal has been filed, then by the number of days between the date of the mailing of such notice and the date of the final decision by the Board.

From the foregoing it is apparent that under the provisions of section 274(a) the taxpayer had 60 days from the mailing of the notice of deficiency within which to file its appeal with the Board, and that during that time the Commissioner could not assess the tax. But section 274(c) requires the Commissioner to assess the tax if the taxpayer allows the 60-day period to elapse without filing an appeal with the Board. As the taxpayer did not file its appeal with the Board until after the expiration of the 60-day period, the Commissioner was required by law to assess the deficiency in tax for 1919 within a period of 5 years and 60 days after the return was filed, this 60-day extension being allowed by the provisions of section 277(b)1.

The provisions of section 277(b)2, extending the period of limitation in cases where an appeal is filed with the Board, refer only to an appeal filed within the 60-day period. An appeal not filed within the prescribed period would consequently not extend the time allowed for making an assessment. The act of the taxpayer, in filing the appeal after the elapse of the 60-day period, did not make it any less the duty of the Commissioner to make the assessment in accordance with section 274(c). The period of 5 years plus 60 days, reckoned from March 12, 1920, would establish May 11, 1925, as the end of the period within which the deficiency could have been legally assessed. Inasmuch as the assessment in the instant case was not made until August, 1925, the assessment was made after the period of limitation prescribed by the statute. Accordingly the taxpayer's claim for refund should be allowed.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

SECTION 281.—CREDITS AND REFUNDS.

ARTICLE 1301: Authority for abatement, refund, and credit of tax.

REVENUE ACT OF 1924.

Suit by subrogee for recovery of tax paid by subrogor. (See Ct. D. 130, page 246.)

ARTICLE 1307: Limitations upon the crediting
and refunding of taxes paid.VIII-30-4287
Ct. D. 84

INCOME TAX—REVENUE ACT OF 1924—DECISION OF COURT.

REFUND—LIMITATION.

A claim for refund of an overpayment of tax filed after the prescribed period based upon a ground entirely different and distinct from the grounds asserted in another claim filed within the prescribed period can not relate back so as to be considered amendatory of the latter claim and thus provide a basis for a refund of the tax within the authority contained in section 281 of the Revenue Act of 1924.

COURT OF CLAIMS OF THE UNITED STATES.

Jonesboro Grocer Co. v. The United States.

[December 3, 1928.]

OPINION.

Moss, Judge, delivered the opinion of the court.

On March 23, 1918, plaintiff, Jonesboro Grocer Co., filed its income and excess profits tax return for the year 1917, and paid the taxes shown to be due thereon, amounting to \$19,708.79. On July 23, 1919, plaintiff filed an amended return for the said year 1917, and at the same time filed a claim for refund of \$424.35, this amount being the difference between the tax shown on its original and its amended returns. The claim was rejected. The Commissioner of Internal Revenue determined, however, that plaintiff had overpaid its tax for 1917, and allowed an overassessment for that year of \$1,322.16, and that there was an additional tax due of \$3,543.39 for the year 1918, making a net total of tax due amounting to \$2,227.23, which was credited to plaintiff's taxes for the year 1918. On March 15, 1924, almost six years after the payment of the tax for 1917, plaintiff filed a second claim for refund in which it was requested that its profits tax be redetermined under the provisions of section 210 of the Revenue Act of October 3, 1917, on the ground that the tax assessed against it was higher than that paid by representative competitive concerns, due to unusual and abnormal conditions affecting plaintiff's income and capital. In a letter dated April 18, 1924, the Commissioner of Internal Revenue advised plaintiff that its application had been granted and that a recomputation of its tax under section 210 showed an overassessment of \$5,725.70, and that such overassessment would be made the subject of certificates of overassessment, which would be forwarded in due course through the office of the collector of internal revenue for plaintiff's district. Thereafter, plaintiff was advised by letter dated December 30, 1924, that prior to scheduling the certificates in question to the collector of internal revenue it was disclosed that "no claim for the refund of the 1917 indicated overassessment was filed within the limitation imposed by section 281 of the Revenue Act of 1924, and both certificates were held in abeyance pending the determination of this fact.

"You are, therefore, advised that since no claim for assessment under section 210 * * * was filed within the limitation imposed by section 281 of the Revenue Act of 1924, the 1917 indicated overassessment may not be adjusted * * *." The claim was, in terms, rejected.

It is provided in section 281(b) (43 Stat., 301) as follows:

"Except as provided in subdivisions (c) and (e) in this section, (1) no such credit or refund shall be allowed or made after four years from the time the tax was paid, unless before the expiration of such four years a claim therefor is filed by the taxpayer, * * *."

It seems to be the contention of plaintiff that the claim upon which this suit is predicated is controlled by the provisions of section 252 of the Revenue Act of 1921 (42 Stat., 268). In order to obtain a clearer understanding of the purpose and intent of Congress in the enactment of section 252, that section must be considered in connection with section 250(b) of the same Act, which reads as follows: "As soon as practicable after the return is filed, the Com-

missioner shall examine it. If it then appears that the correct amount of the tax is greater or less than that shown in the return, the installments shall be recomputed. If the amount already paid exceeds that which should have been paid on the basis of the installments as recomputed, the excess so paid shall be credited against the subsequent installments; and if the amount already paid exceeds the correct amount of the tax, the excess shall be credited or refunded to the taxpayer in accordance with the provisions of section 252." Section 252, omitting irrelevant portions, reads as follows: "That if upon examination of any return of income made pursuant to * * * the Revenue Act of 1917 * * * it appears that an amount of income, war-profits or excess-profits tax has been paid in excess of that properly due, then, notwithstanding the provisions of section 3228 of the Revised Statutes, the amount of the excess shall be credited against any income, war-profits or excess-profits taxes, or installment thereof, then due from the taxpayer under any other return, and any balance of such excess shall be immediately refunded to the taxpayer: *Provided*, That no such credit or refund shall be allowed or made after five years from the date when the return was due, unless before the expiration of such five years, a claim therefor is filed by such taxpayer." It is obvious, we think, that section 252 was intended to relate to mistakes in overpayment appearing on the face of the return itself, discoverable by the examination provided for in section 250(b), directing the proper credit of the excess payment, and the immediate refund to the taxpayer of any balance of such excess. It means that Congress intended that the examination by the Commissioner of such return should not, in any event, be prolonged beyond the period of five years from the date of the return, and that said Commissioner should not, after that period, allow such refund unless a claim therefor had been filed within the five years. The contention is urged that the words "claim therefor" as used in the above proviso refers to the words "amount paid in excess of that properly due," and that the plaintiff complied with the requirements of section 252 when it filed in 1919 its claim for the refund of a stated sum, or "such greater amount as is legally refundable." The contention that the later claim for refund should relate back to the 1919 claim is illogical and unsound. The 1919 claim, although specifically rejected, was adjusted to the perfect satisfaction of the taxpayer, as shown by a letter dated April 12, 1921, in which it was stated: "Relative to the year 1917 we are making no exception to the adjustments made for this year, and will accept the recommendation for overpayment in the amount stated of \$1,322.16." The controversy growing out of that claim was thus effectually closed. The language, "or such greater amount as is legally refundable," must be held to relate to the matters relied upon in the claim for refund. Certainly it can not reasonably be contended that a claim for refund based upon the right to relief under the special assessment section could have any sort of relation to the grounds asserted in the 1919 claim for the refund of \$424.35. If the principle contended for by plaintiff on this point is correct, the limitations imposed by Congress on the time within which claims for refund may be asserted, and actions thereon instituted, would be completely annulled.

Plaintiff's claim sued on herein is specifically barred by the very section on which plaintiff relies—section 252 of the Act of 1921. In the language "no such credit or refund shall be allowed," etc., *such credit or refund* can refer only to the credit or refund for which plaintiff is now contending, and the only claim for same was filed almost six years after the return was made. Section 3228 of the Revised Statutes as amended by section 1014 of the Revenue Act of 1924 (43 Stat., 343) provides that "No such suit * * * shall be begun * * * after the expiration of five years from the date of the payment of such tax * * * unless such suit * * * is begun within two years after the disallowance of the part of such claim to which such suit or proceeding relates." [Our italics.]

The claim of July, 1919, does not include any part of the claim to which this suit relates. The claim to which this action relates was filed March 15, 1924, long after the prescribed period for filing a claim for refund.

Plaintiff's legal status is not affected in any manner by the action of the Commissioner in advising plaintiff that consideration had been given to its second claim under section 210 and that a recomputation and audit showed an overassessment of \$5,725.70. The final action of the Commissioner was the rejection of the claim, due to the fact that no claim for such refund had been filed within the prescribed time. A few of the cases which sustain defendant's

contention are as follows: *Nichols v. United States* (7 Wall., 122, 130), *Cheatham et al. v. United States* (92 U. S., 85), *Hicks v. James* (48 Fed., 542) (this case was affirmed by the United States Supreme Court in *James v. Hicks*, 110 U. S., 272), *Kings County Savings Institution v. Blair* (116 U. S., 200), *Rock Island A. & L. R. R. Co. v. United States* (254 U. S., 141 [Ct. D. 2, C. B. 4, 342]). Plaintiff is not entitled to recover, and it is so adjudged and ordered.

TITLE X.—GENERAL ADMINISTRATIVE PROVISIONS.

SECTION 1016.—DISTRAINT OF BANK ACCOUNTS.

SECTION 1016.

VIII-42-4391
I. T. 2504

REVENUE ACT OF 1924.

Money on deposit in a bank represented by certificates of deposit in the hands of a taxpayer is within the scope of "bank accounts" made subject to distraint by section 3187 of the Revised Statutes, as amended by section 1016 of the Revenue Act of 1924.

A ruling is requested as to the status of bank accounts represented by certificates of deposit under section 3187 of the Revised Statutes, as amended by section 1016 of the Revenue Act of 1924.

The taxpayer holds two certificates of deposit issued by a bank. The body of each certificate reads as follows (omitting the respective amounts) :

——— has deposited in this bank —— dollars, payable to the order of himself on return of this certificate properly indorsed, with interest at 4 per cent per annum.

A note at the bottom of the certificates shows that the bank reserves the right to require 30 days' notice before paying the certificates "in accordance with the provisions of section 19 of the Federal Reserve Act."

Inquiry is made as to whether a bank is taking any more responsibility in honoring a levy under a distraint warrant against the account of a delinquent taxpayer which is evidenced by certificates of deposit than it would take if the amounts for which certificates of deposit were issued had been deposited in an account subject to check.

The position of the Bureau with reference to distraint upon bank accounts in general is stated at some length in Solicitor's Memorandum 3804A (C. B. V-1, 110) and need not be restated. It is sufficient to say that under section 3187 of the Revised Statutes, as amended, "bank accounts," *eo nomine*, without discrimination as to the character of an account or deposit, are subject to the process of distraint. Moreover, under section 1114(e) of the Revenue Act of 1926, a person who is in possession of property or rights to property subject to distraint upon which a levy has been made is liable in his own person and estate for failure or refusal to surrender the same to the collector or deputy collector making the levy.

As above indicated, section 3187 of the Revised Statutes, as amended, does not differentiate as between moneys held by a bank subject to check and moneys held by it subject to outstanding cer-

tificates of deposit. As a matter of fact, there appears to be no essential difference between the two classes of deposits. The receipt for money deposited subject to check ordinarily is entered in a pass book by bank officials or acknowledged by them on a duplicate deposit slip. Whether one or the other of these methods is used, the depositor receives from the bank an acknowledgment in writing of the sum deposited by him. In its essence a certificate of deposit is no more than this, for it is a written statement from the bank that the party named therein has deposited with it the amount of money specified in the instrument, and that the same is held for him subject to the terms thereof.

The chief distinction between the two forms of deposit is that where a deposit is made subject to check the depositor can draw on it at his own election up to the amount of the deposit, whereas when a certificate of deposit is issued, the amount thereof can not be withdrawn except in accordance with the terms and conditions of the certificate. Ordinarily a certificate of deposit bears interest at a higher rate than is allowed, if allowed at all, on a checking account, but this is a difference in degree and does not affect the real character of the deposit.

Since section 3187 of the Revised Statutes, as amended, makes no distinction between checking accounts and certificate of deposit accounts, but uses the term "bank accounts" without qualification, it is concluded that both classes of accounts are within the scope of the statute, and a collector's levy under a warrant of distraint against the bank account of a delinquent taxpayer covers both classes of deposits. It follows, for the reasons set forth in Solicitor's Memorandum 3804A, already referred to, that a depositary on which a warrant of distraint is served must honor the levy, whether the account carried by the delinquent taxpayer is a checking or certificate of deposit account. Otherwise, the depositary would subject itself to the liability imposed by section 1114(e) of the Revenue Act of 1926.

TITLE XII.—REDUCTION OF INCOME TAX PAYABLE IN 1924.

SECTION 1200.

VIII-42-4392
Ct. D. 115

INCOME TAX—REVENUE ACT OF 1924—DECISION OF COURT.

INCOME TAX—25 PER CENT REDUCTION—PAYMENT AT SOURCE— OBLIGOR OF TAX-FREE COVENANT BONDS.

The obligor of tax-free covenant bonds which has paid to the collector the full amount of the taxes for the calendar year 1923, withheld under sections 221(b) and 237 of the Revenue Act of 1921, is not a taxpayer within the meaning of section 1200(a) of the Revenue Act of 1924 and is not entitled to a refund of 25 per cent of such payments under the provisions of section 1200(a).

UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

Union Pacific Railway Co., appellant, v. Frank K. Bowers, appellee.

Oregon Short Line Railroad Co., appellant, v. Frank K. Bowers, appellee.

Oregon-Washington Railroad & Navigation Co., appellant, v. Frank K. Bowers, appellee.

The St. Joseph & Grand Island Railway Co., appellant, v. Frank K. Bowers, appellee.

Michigan Central Railroad Co., appellant, v. Charles W. Anderson, appellee.

Appeals from five judgments of the District Court for the Southern District of New York dismissing complaints at law. The plaintiffs sued the collector for money unlawfully collected by him under the guise of a tax. The collector moved to dismiss the complaints for insufficiency in law upon their face, and the district court granted the motion.

Before MANTON, L. HAND, and SWAN, Circuit Judges.

[May 13, 1929.]

OPINION.

L. HAND, Circuit Judge: The complaints alleged that the plaintiffs in March, 1924, made income tax returns for the year 1923, in which they charged themselves with 2 per cent upon interest paid by them to certain holders of their bonds. They had promised to pay this interest without deduction for any tax which they might be required or permitted to pay or retain under any law of the United States, and they agree that sections 221 and 237 of the Revenue Act of 1921 required them to return and pay the amount which they included. Section 1200(a) of the Revenue Act of 1924 provided that "any taxpayer making return, for the calendar year 1923, of the tax imposed by Parts I and II of Title II of the Revenue Act of 1921 shall be entitled to an allowance by credit or refund of 25 per centum of the amount shown as the tax upon his return." After June 2, 1924, when the Act of 1924 took effect, the plaintiffs deducted one-quarter of the tax returned and paid the balance. This deduction the collector refused to allow and the plaintiffs paid the balance under protest.

Section 2(9) of Title I of the Revenue Act of 1921 contains general provisions not relevant here. Section 1 of the Act defines a "taxpayer" as "any person, trust or estate subject to a tax imposed by this Act." Part II of Title II levies the individual income tax, of which section 221(b) is the provision here important. This provides that " * * * where bonds * * * contain a contract or provision by which the obligor agrees * * * to pay the interest without deduction for any tax which the obligor may be required or permitted to pay thereon or to retain therefrom under any law of the United States, the obligor shall deduct and withhold a tax equal to 2 per centum of the interest." Subdivision (c) requires a return of the amount so withheld and makes the corporation "liable for such tax"; subdivision (d) requires the obligee to return the full income but allows him to deduct the amount paid.

The plaintiffs' first argument is that as they were made "liable for such tax" under section 221(c), they were "taxpayers" under section 1200(a) of the Act of 1924 and under section 1 of the Act of 1921, and that they were therefore entitled to the reduction *eo nomine*. But in no event can the obligor be regarded as "the taxpayer," though he is "liable for such tax." This is not a paradox, but a constitutional necessity. While interest when received is income of the obligee, it is not income of the obligor; it is a debt, and debts are not a part of the debtor's income. He could be taxed only upon such income as he might use to pay the interest, which is indeed exempt under section 234(b). But the debt is due regardless of his income, and if he is a "taxpayer," the tax could not be unconditionally levied upon the sum paid. It would be constitutionally necessary to limit it to so much as was shown to be income. The statute of course meant nothing of the sort, and would not have reached the interest in all cases if it had. It taxed the obligee and him alone. It made the obligor "liable for such tax" only because of his promise to the obligee, a promise to discharge the obligee's liability to another. The Government could have enforced that promise at common law or in equity, the procedure differing in different jurisdictions. All the statute did was to substitute a single summary remedy.

This does not, however, answer the question at bar. The obligor might still perhaps be entitled to a refund or an allowance upon a reduction of the tax, though it was levied on the obligee. Suppose for example that the statute had imposed the whole normal tax at the source, so that the obligor must pay it all, as was the case before October 3, 1917, when section 3 of the Revenue Law of 1917 first introduced a limitation of the amount to be so collected. It would be unjust to hold that a reduction should go to the obligee, who would in that case use the covenant, not as an indemnity, but to get a bonus. But in such a case the obligor and the obligee have not divided the burden of the tax between them. When they have, as they always have since October 3, 1917, another question arises. Has Congress allocated the reduction proportionately between their shares, or has it given the whole allowance to the obligee?

The plaintiffs insist upon the first alternative, relying upon section 1200(b) and section 281(d) of the Act of 1924. Section 1200(b) provides that if the 1923 tax has been paid before June 2, 1924, when the Act of 1924 took effect, the taxpayer shall get a credit or a refund for his allowance under section 281. Section 281 provides in general for refunding overpayments, and subdivision (d), that when the overpayment has been of a tax levied under section 221, the refund shall go to the withholding agent. Perhaps the plaintiffs are right in urging that the equity of this section should extend to section 1200(a); at any rate, we shall assume so arguendo. That really does not advance matters until we know whether there has been an overpayment under section 221, or, what is the same thing for these purposes, an overreturn. But that in turn depends upon how Congress intended to marshal the allowance, which is the question at issue. Section 281(d) certainly applies when there has been an overpayment of the 2 per centum tax, but there is none unless Congress intended proportional reduction between obligor and obligee.

It seems to us clear that Congress did not so intend. The obligor in such bonds has always had to bear 2 per centum of the obligee's tax, at least since 1916. Since 1917 the whole tax has been varied, being reduced in recent times, though never to 2 per centum. It seems to us plain nearly to a demonstration that Congress could not have intended to relieve him for the year 1923 by such language as that relied upon. The purpose was to relieve individual taxpayers, not corporations, as appears by the limitation of section 1200(a) to Part II of Title II. We should have to assume that through inaptness of expression the statute had gone further than its apparent purpose. This might indeed be a necessary conclusion if the obligor was a "taxpayer," but it does not follow from any language used in section 281(d).

Judgments affirmed.

INCOME TAX RULINGS.—PART IV.

REVENUE ACT OF 1921 OR PRIOR REVENUE ACTS.

TITLE I.—GENERAL DEFINITIONS.

SECTION 2.—GENERAL DEFINITIONS.

ARTICLE 1504: Association distinguished from trust.

VIII-42-4393
Ct. D. 118

INCOME TAX—REVENUE ACT OF 1918—DECISION OF COURT.

1. TRUST—TAXABILITY AS CORPORATION.

An organization, designated a trust, conducting a business through trustees in quasi corporate form pursuant to the purpose for which it was created as set forth in a declaration of trust, is an association within the meaning of section 1 of the Revenue Act of 1918 and is subject to income tax as a corporation under section 230 of that Act.

2. JUDGMENT AFFIRMED.

The judgment of the district court (T. D. 4246 [C. B. VII-2, 221]) affirmed.

UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

Little Four Oil & Gas Co., a Trust, Pittsburgh, Pa., appellant, v. D. B. Heiner, Collector of Internal Revenue, Twenty-third District of Pennsylvania, appellee.

Little Four Oil & Gas Co., a Trust, Pittsburgh, Pa., appellant, v. C. G. Lewellyn, Formerly Collector of Internal Revenue, Twenty-third District of Pennsylvania, Pittsburgh, Pa., appellee.

[September 26, 1929.]

OPINION.

WOOLLEY, Circuit Judge: The defendant collectors of internal revenue (in office at different periods) assessed against the plaintiff company taxes at the corporation rate on its net income and profits for the years 1919 and 1920. The company paid the taxes under protest and, after its claim for refund had been made and rejected, brought these suits to recover the same. On questions of law arising from the pleadings as though on demurrer under the Pennsylvania practice act, the district court entered the judgments against the company, which, by these appeals, it brings here for review. These questions—compressed into one—are whether the Little Four Oil & Gas Co., describing itself as a trust and acting through trustees, was, during the tax years, a trust of the nature of Massachusetts trust, not doing business but merely receiving and distributing profits and therefore not subject to taxation at the corporation rate upon its net income, or was an association or joint-stock company and as such liable for taxes on its net income as a corporation in accordance with sections 1, 230, and 231 of the Revenue Act of 1918, which declared that the term "corporation" includes "associations" and "joint-stock companies" and prescribed that they should pay taxes as such.

The answer to this question turns, we think, on the facts stated and admitted in the pleadings rather than on any novel aspect of law, for the law has from time to time been declared by the courts on the cited provisions of the Revenue Act of 1918 (40 Stat., 1057) and on the same and kindred provisions of the Revenue Acts of 1916, 1921, and 1924.

The formation of associations and trusts of the character of the one here involved, whereby escape from taxes is sought and sometimes obtained, was stimulated generally by the decision in *United States v. Emery et al.* (237 U. S., 28 [T. D. 2188]), where it was held that a concern engaged simply in collecting and distributing rent and income is not doing business within the meaning of the Corporation Tax Law of 1909, and particularly by the decision in *Crocker v. Malley* (249 U. S., 223 [T. D. 3595, C. B. III-1, 489]), where it was held with reference to a "Massachusetts trust" that neither the trustees nor the beneficiaries, nor all together, could be regarded as a joint-stock association within the meaning of the Income Tax Law of 1913 and that dividends upon stock in the hands of the trustees were not subject to the extra tax imposed by G(a) of that Act. But the court did not by this decision hold that all trusts, or indeed all Massachusetts trusts, are so exempt from taxation, for later it recognized the distinction stated in *III Cook on Corporations*, 2251, in respect to trusts, even of the Massachusetts type, that they are of two classes—one, where the trustees merely collect dividends or interest, or rentals, and distribute them among the shareholders—a simple common-law trust similar in legal effect and in exemption from certain taxation to a trust under a will where the trustee merely collects income and distributes it among beneficiaries; the other, where a trust is organized or declared for business purposes and the trustees carry on an active business for profit, regarded as a plain unincorporated joint-stock association and liable for taxes at the corporation rate. The theory that the distinction between trusts of these classes and their consequent liability for taxes is based on the powers exercised by the shareholders—great or little—is no longer seriously regarded. The real test is whether the shareholders or trustees, or both combined, carry on business for profit, and, if they do, they constitute a business trust—in legal effect, an association or a joint-stock company—with liability for taxes. The Supreme Court made this test with reference to trusts in *Hecht v. Malley* (265 U. S., 14 [T. D. 3595, C. B. III-1, 489]), distinguishing *Crocker v. Malley* (249 U. S., 223), and with reference to unincorporated joint-stock associations in *Burke-Waggoner Assn. v. Hopkins* (269 U. S., 110). An illuminating discussion of the subject with supporting authorities may be found in *Hornblower v. White* (27 Fed. (2d), 82), where the District Court for the District of Massachusetts held, on one state of facts, an association a trust, not a corporation, and therefore not subject to the taxes imposed, affirmed by the Circuit Court of Appeals for the First Circuit, in 27 Fed. (2d), 777, and in *Neal v. United States* (26 Fed. (2d), 708), where the district court for the same district held an association a trust, not a corporation and not subject to the taxes imposed, but the circuit court of appeals for the same circuit reversed its decision on authority of the law of the *Hornblower* case as applied to the different state of facts.

So, as stated at the beginning, the question in this case, primarily one of law, turns on the facts and is to be determined from the facts pleaded and admitted, viewed in the light of the law, the test being whether the trust is a business concern and the trustees are operating it in active business for profit.

The appellant in its brief frankly states that:

"The trust (in this case) was created for the purpose of buying and selling real estate and mining and drilling for oil and gas thereon. * * * The trust engaged in business pursuant to the purpose as set forth in the declaration of trust, during the years in question."

While these concessions might be enough, we prefer briefly to state the facts on which our decision will be grounded. These appear in a declaration of trust, made in 1916 and amended in 1918. Briefly summarized, they are as follows:

G. A. Gill acquired by lease certain lands in Pennsylvania with the right and "for the purpose of leasing, mining, and operating for oil and gas and in laying pipe lines and building tanks, stations, and structures thereon to take care of said products." Gill assigned all his rights to Friday, Seybold, Ballard, and to himself. These four men then assigned the same to themselves upon a trust which (first reciting that they had entered into an agreement with two others for the purpose of drilling for oil and gas on the premises described and had assigned the agreement to themselves as trustees) they declared as follows: That the name of the trust shall be Little Four Oil & Gas Co.; that its capital stock shall consist of 200 shares of preferred and 200 shares of common, later enlarged to 1,000 shares without preference; that the trustees shall issue to

each of themselves 50 shares of the common stock—all the original issue; that they may invite and receive cash or property in payment for interests in the trust fund, in other words, sell stock for cash or property; that the shares of stock, variously and successively held, shall be transferable and that death of a holder of shares shall not operate to terminate the trust; that the trustees shall make report of receipts and disbursements to the stockholders, declare dividends, acquire, set up, and use a surplus entirely within their discretion, and in all matters be substantially independent of control by the stockholders; that the trustees shall appoint, remove, or reappoint such officers and agents as they shall determine, defining their duties and fixing their compensation; that all contracts in relation to the business of the trust shall be made by the trustees and signed by three of them; that property presently held and thereafter acquired shall be for the benefit of stockholders, not as partners but in trust, without personal liability of either the trustees or stockholders for the debts of the trust; that the trust shall continue for 21 years and the trustees be self-perpetuating. That the trust earned in the oil and gas business the income and profits which it stated in its income tax return and on which the tax was assessed and collected was not disputed.

As the character of the trust, whether or not a subject of Federal taxation, is to be determined not by the broad powers of the trustees or by the limited powers of the stockholders but by what the trust was actually doing through its trustees, we hold on these facts that the collectors were right in regarding this organization, however named, as an unincorporated association conducting a business for profit in quasi corporate form, liable for taxes at the corporation rate by force of the provisions of the applicable Revenue Act, and that the judgments of the district court sustaining the collectors must be affirmed.

TITLE II.—INCOME TAX.

PART I.—GENERAL PROVISIONS.

SECTION 200.—DEFINITIONS.

ARTICLE 1523: Personal service corporation.

VIII-50-4464
Ct. D. 137

INCOME AND EXCESS PROFITS TAXES, REVENUE ACTS OF 1917 AND 1918—
DECISION OF COURT.

CORPORATION—PERSONAL SERVICE CLASSIFICATION—NOMINAL CAPITAL—COMMISSION LIVE STOCK DEALERS.

A corporation, engaged in the business of selling live stock received on consignment and buying live stock to fill orders of customers, which requires a substantial reserve in the bank to meet expenses of yardage, feeding, and watering borne by it until the stock is sold, which borrows large amounts from its stockholders and from banks to carry shipments for customers and to buy cattle to carry out orders to buy, these transactions constituting a substantial part of its business, and which has a large percentage of its gross income represented by interest on loans and discounts, is not a corporation described in section 209 of the Revenue Act of 1917 as one "having no invested capital or not more than a nominal capital," and it is not entitled to classification as a personal service corporation under section 200 of the Revenue Act of 1918.

UNITED STATES CIRCUIT COURT OF APPEALS, EIGHTH CIRCUIT.

*F. M. Hatch et al., appellants, v. United States of America, appellee.**Frank M. Hatch et al., appellants, v. United States of America, appellee.*

Appeals from the District Court of the United States for the Northern District of Iowa.

[August 26, 1929.]

OPINION.

BOOTH, Circuit Judge, delivered the opinion of the court.

In the court below the United States brought two suits in equity to recover from former stockholder distributees of a dissolved corporation additional income and profits taxes assessed against the corporation for the calendar years 1917, 1918, and 1919, in the respective amounts \$1,216, \$4,508.24, and \$3,548.65, with interest. The first suit (No. 8447 here) involved the years 1917 and 1918; the second suit (No. 8448 here) involved the year 1919. The four stockholder distributees of the corporation, F. M. Hatch, H. H. Holmes, H. U. Carpenter, and James Volin, were defendants in the first suit. Holmes died before the trial, and Laura M. Holmes was substituted, as his sole devisee. The same persons were defendants in the second suit, except that Laura M. Holmes was named as executrix of the will of H. H. Holmes.

The two suits were consolidated for trial. No proof was offered that the estate of H. H. Holmes was solvent, or as to the value of the estate, or that any property of the estate had come into the hands of Laura M. Holmes. Both cases were therefore dismissed as to her. Decree was entered against the other three defendants, adjudging that they were liable as distributees and that each should make restitution in amounts which are not here questioned if liability existed. From this decree, considered as a separate decree in each suit, the three defendants have taken the present appeals.

The contention of the appellants is that during the year 1917 the corporation was one having "not more than a nominal capital" within the meaning of section 209 of the Revenue Act of 1917 (40 St., 300, 307), and therefore was not liable for the additional tax assessed against it for that year; and that during the calendar years 1918 and 1919 the corporation was a "personal service corporation" within the meaning of section 200 of the Revenue Act of 1918 (40 St., 1057, 1058), and therefore was not liable for the additional tax assessed for those years.

So far as these appeals are concerned, there is no substantial difference between a "nominal capital corporation" under section 209 of the Revenue Act of 1917 and a "personal service corporation" under section 200 of the Revenue Act of 1918.

It is conceded by the Government that if the corporation was of the character claimed, it was not liable for the additional taxes assessed.

There was substantial evidence tending to support the following facts:

During the years in question the corporation was engaged in business as a live-stock commission agency, having its principal place of business at Sioux City, Iowa. During the years 1917 and 1918 it had a paid-up capital of \$10,000; during the year 1919 of \$20,000. At the beginning of 1917 it had surplus of \$16,149; at the beginning of 1919 of \$13,650. About \$4,000 of the capital was invested in memberships of the Sioux City Live Stock Exchange, and a small amount in office furniture and equipment. During the year 1917 the corporation earned a gross income of \$59,102, of which \$4,705 represented interest on loans and discounts; net income, \$9,220. In 1918 the gross income was \$66,462, of which \$987 represented interest received; net income, \$15,906. In 1919 the gross income was \$80,421, of which \$7,264 was for interest received; net income, \$28,018. The business of the corporation was of two kinds—selling live stock received on consignment and buying live stock to fill orders of customers. Under the first class of business the expenses of yardage, feeding, and watering were borne by the corporation until the stock was sold. To handle these shipments the corporation had to have a reserve in the bank of from \$25,000 to \$30,000. It borrowed both from its stockholders and from banks. Sometimes it borrowed as much as \$50,000 at a time. The money borrowed was used to carry the various shipments for customers, and this was a substantial part of the business. In a few instances the company carried customers on notes. Under the second class of business the corporation, on receiving an order to buy, would carry out the order by buying cattle—sometimes not more than one or two at a

time—until the order was filled. In order to carry out these transactions capital was required and used. This buying was also a substantial part of the business.

It is the claim of the defendants that this money so used was not the capital of the corporation, but accumulations of profits belonging to members and allowed to remain for use in the business; and it is further claimed that the loans made were in fact personal loans made by members of the corporation and not by the corporation itself, the individual transactions being entered upon the books of the corporation for convenience. It appears, however, that the income derived from these loans—that is, the interest in the amounts above stated—were treated by the corporation on its books as income belonging to it; and these amounts were reported on its income tax returns; and the same is true with respect to income from real estate in the year 1919, amounting to about \$5,800. In the balance sheets of the company at the close of the years 1917, 1918, and 1919 the notes receivable exceeded the accounts payable to members of the corporation by very substantial amounts. The conclusion is that the corporation was either loaning these excess amounts to its customers on its own account, or else it was carrying its customers to that extent; in either case making use of capital.

The court found that the capital of the corporation was material income-producing factor. We think that this finding of ultimate fact is fully justified by the above recited primary facts, which are themselves amply sustained by the testimony and exhibits in the case. In many of its facts the case at bar is similar to the cases of *Dreyer Commission Co. v. Hellmich* (25 F. (2d), 408 (C. C. A. 8)), *Denver Livestock Commission Co. v. Commr.* (29 F. (2d), 543 (C. C. A. 8)), *Conklin-Zonne-Loomis Co. v. Commr.* (29 F. (2d), 698 (C. C. A. 8)), *Feeders Supply Co. v. Commr.* (31 F. (2d), 274 (C. C. A. 8)), *St. Paul Abstract Co. v. Commr.* (32 F. (2d), 225 (C. C. A. 8)). See also *Hubbard-Ragsdale Co. v. Dean* (15 F. (2d), 410, *affd.* 15 F. (2d), 1013 [T. D. 3904, C. B. V-2, 134]). And the conclusion here reached finds support in those cases.

One other matter remains to be noticed. Error is assigned because of the exclusion of certain testimony. The witness Frank E. Scott was asked:

“Q. Have you, due to your 29 years of experience, formed an opinion, Mr. Scott, as to whether or not the use of \$100,000 could be made to be material income-producing factor in a live-stock commission business conducted as the business is at Sioux City, Iowa?”

Objection was made to the question, and the objection was sustained. The witness Howard G. Pierce was asked:

“Q. During your years of experience on the Sioux City market have you had occasion to observe whether or not the use of capital up to \$20,000 used by a commission merchant for the purpose of loaning money to cattle raisers was a material help in building up the commission business?”

Objection was made to the question, and the objection was sustained.

There are several reasons why reversible error can not be predicated upon these rulings: First, because no offer to prove was made after the rulings. This was necessary. (*Federal Sur. Co. v. Standard Oil Co.*, 32 F. (2d), 119 (C. C. A. 8), and cases cited.) Second, even if the testimony of the witnesses could be considered as expert testimony, which we do not decide, yet the allowance or rejection of expert testimony rested largely in the discretion of the trial judge, and no abuse of discretion is shown. Third, the questions called for conclusions of the witnesses as to the ultimate fact which the court was called upon to find, and for that reason the exclusion was proper.

We think the decree as entered was right and it is affirmed.

SECTION 201.—DIVIDENDS.

ARTICLE 1541: Dividends.
(Also Section 250, Article 1012.)

VIII-50-4465
Ct. D. 138

INCOME TAX—ACT OF OCTOBER 3, 1913, AND REVENUE ACT OF 1921—DECISION OF COURT.

1. INCOME—DIVIDEND—SURPLUS DISTRIBUTED IN STOCK AND NOTES OF NEW CORPORATION.

Where a corporation transfers to a new corporation a part of its surplus assets which are credited on the books of the latter to the

individual stockholders of the transferor corporation in proportion to their respective stock holdings therein, which credits are canceled by the payment by the transferee corporation of cash and the distribution of its stock and debenture notes, the assets transferred are taxable as a dividend to the stockholders of the old corporation in the amount of their value when transferred.

2. WAIVER—VALIDITY—EXECUTED AFTER BAR OF STATUTE.

A consent in writing by a taxpayer to waive the statute of limitations operating against the collection of a tax is valid and binding upon such taxpayer even when the waiver is executed after the expiration of the statutory period.

3. WAIVER—ASSESSMENT—COLLECTION.

A consent by a taxpayer to waive the statute of limitations on the assessment of a tax contemplates also the collection of the tax and waives the bar of the statute as to the collection thereof.

COURT OF CLAIMS OF THE UNITED STATES.

Charles H. Stange v. The United States.

[November 4, 1929.]

OPINION.

GREEN, Judge, delivered the opinion of the court.

This case involves taxes for the calendar year of 1914 assessed under the Revenue Act of 1913, and for which an income-tax return was filed by the plaintiff on February 19, 1915. The other facts material to the decision may be summarized as follows:

A. H. Stange, father of plaintiff, prior to March 24, 1914, was the owner of 1,780 shares of the 2,500 shares of the stock in the A. H. Stange Co., a corporation, the remainder of this stock being held by his sons and daughters, or daughters and sons-in-law. On March 24, 1914, A. H. Stange organized a corporation known as the Union Land Co., and on May 29, 1914, another corporation known as the Kinzel Lumber Co. On the last-named date the 2,500 shares of the capital stock of the A. H. Stange Co. were reapportioned between Mr. Stange and his children in such manner as to give Mr. Stange and each of his sons and daughters (or daughters and sons-in-law) one-seventh of the said 2,500 shares. Prior to the reapportionment the plaintiff owned 120 shares in said company, and after it was made, 357.

On June 10, 1914, pursuant to a resolution adopted by the board of directors, the A. H. Stange Co. transferred to the Union Land Co. cash in the amount of \$60,000 and other property having a book value of \$1,059,667.15, or a total of \$1,119,667.15, and also in the same manner to the Kinzel Lumber Co. cash and bills receivable in the total amount of \$300,000 and a parcel of real estate valued on the books at \$5,000. When these assets were transferred to the two companies the surplus account of the Stange company was debited with the value of said assets. The Union Land Co. entered on its books the assets so transferred to it at a total valuation of \$3,491,382.61, and the Kinzel Lumber Co. in the same manner entered on its books the assets which it received in the total sum of \$305,000.

The assets conveyed to the two companies were credited to the individual stockholders thereof in proportion to their respective interest in the A. H. Stange Co. as shown by their stock holdings. In this manner the plaintiff was credited with \$45,000 on the books of the Kinzel Lumber Co. on June 2, 1914, and \$497,000 on the books of the Union Land Co. on June 13, 1914. At the last-named date the plaintiff withdrew from the Union Land Co. \$5,000 in cash, which was charged to his account, and the company issued to him capital stock of a par value of \$35,000, which was also charged to his account. On June 16 he withdrew the further cash sum of \$2,000, and on July 23, 1914, the company issued to him debenture notes in the sum of \$455,000, both of which items were debited to his account. The total of all these debits balanced and extinguished the original credit of \$497,000 in the plaintiff's account. In the same manner plaintiff's credit account with the Kinzel Lumber Co. was balanced by issuing to him stock of the par value of \$15,000, cash \$10,000, and debenture notes \$20,000.

On November 14, 1922, the plaintiff executed and filed with the Bureau of Internal Revenue a written waiver of statutory limitations approved and accepted by the Commissioner as set forth in Finding XI. The Commissioner of Internal Revenue determined that the total value of all assets transferred by the Stange company to the Union Land Co. and the Kinzel Lumber Co. to be \$4,494,968.81, and allocated one-seventh of this value (\$642,138.40) as taxable income to the plaintiff for the year 1914, and thereon in February, 1924, made an additional assessment of income taxes for 1914, which together with interest amounted to \$30,779.76, which the plaintiff paid under protest on March 19, 1925. Thereafter, on March 30, 1926, and on June 8, 1927, the plaintiff submitted to the Commissioner of Internal Revenue a claim for refund and a supplement thereto. These claims for refund give rise to the following objections which the plaintiff makes to the validity of the tax assessed:

(1st) That the transaction involved constituted the distribution of the assets of the A. H. Stange Co. and was not a taxable dividend.

(2d) That the waiver of the statute of limitations was confined merely to the assessment of the tax and did not waive the bar of the statute as to the collection thereof, and was executed after the expiration of the period of limitation.

(3d) That in any event plaintiff's taxable income as a result of the transactions involved could have been no greater than the amount credited to him on the books of the transferee companies, being a total of \$542,000 instead of the amount of \$642,138.40.

(4th) That the several acts of A. H. Stange and the corporations controlled by him herein involved were merely steps taken at the direction of the said A. H. Stange to effectuate a gift to his son, the plaintiff herein, and for that purpose constituted one transaction, and that the property received by plaintiff was nontaxable gift from father to son to the extent of 237/357 thereof.

We will first consider the claim of the plaintiff that the stock, cash, and debentures received by him, as above set forth, constituted a distribution in partial liquidation of the assets of the A. H. Stange Co.

It seems to be conceded in argument by both parties that the various acts by which certain property of the A. H. Stange Co. was transferred into cash, debenture notes, and stock in the Union Land Co. and the Kinzel Lumber Co. constituted in reality one transaction, and the findings of fact so state. Plaintiff contends that this was a distribution in partial liquidation of the assets of the Stange company. The 1928 Revenue Act defines "amounts distributed in partial liquidation" as—

"A distribution by a corporation in complete cancellation or redemption of a part of its stock, or one of a series of distributions in complete cancellation or redemption of all or a portion of its stock."

A regulation to this effect had been in force for some time prior to the passage of the last-named Act, and the part of the Act which we have quoted, as we think, was merely the adoption in the statute of a principle of accounting already well settled. At all events, we think the instant case is controlled in this respect by the case of *Rockefeller v. United States* (257 U. S., 176 [T. D. 3271, C. B. 5, 34]), an exactly parallel case with the one at bar. In the Rockefeller case a corporation engaged in producing, buying, and selling crude petroleum and transporting it through its pipe lines formed a new corporation to which the pipe-line property was conveyed. In consideration for this conveyance, and as a part of the transaction, the new corporation issued all of its capital stock to the stockholders of the old corporation pro rata. The old company remained in business and retained sufficient assets to cover its capital obligations, and the transfer of assets to the new corporation did not result in a reduction of its outstanding stock. The slight difference in the nature of the facts between that case and the one at bar is immaterial to the legal questions involved. It appeared in the Rockefeller case, *supra*, that the stock of the new corporation was a consideration for the conveyance. In the instant case the record is silent on the subject of consideration except as may be inferred from the facts. The whole transaction was a family matter carried out in pursuance of a plan of A. H. Stange, the father, as a result of which certain property of the A. H. Stange Co. passed to the two other corporations and the plaintiff received in lieu of the interest which he possessed therein as a stockholder of the A. H. Stange Co. cash, debenture notes, and stock of the new corporations. That it was a distribution of a

part of the surplus of the A. H. Stange Co. is quite clear. In fact, this is conceded in argument by the plaintiff, but plaintiff says that the distribution was not in the way of a dividend but in partial liquidation. The fact is that there was no cancellation or redemption of any part of the stock of the A. H. Stange Co. We think this was necessary to sustain the claim that there was partial liquidation, and in this we are sustained by the decision in the Rockefeller case, wherein a practically similar transaction was held to be a dividend. In that case the court said:

"We deem it to be too plain for dispute that * * * the new pipe line company shares were in substance and effect distributed by the oil company to its stockholders; * * * in effect a dividend out of the accumulated surplus."

In the case at bar, after transfers were made by the A. H. Stange Co. it still had a surplus of \$362,560.78.

In *Lynch v. Hornby* (247 U. S., 339) it was held that the 1913 Revenue Act imposed a tax upon—

"* * * all dividends declared and paid in the ordinary course of business by a corporation to its stockholders after the taking effect of the Act (March 1, 1913), whether from current earnings, or from the accumulated surplus made up of past earnings or increase in value of corporate assets, notwithstanding it accrued to the corporation in whole or in part prior to March 1, 1913"—

and a distinction is drawn between this case and the case of *Lynch v. Turrish* (247 U. S., 221), relied upon by plaintiff's counsel. It follows that if we are correct in holding the distribution to be in effect a dividend, it was taxable under the 1913 Act, notwithstanding the distribution was of the accumulated surplus made up of past earnings or increase in the value of corporate assets.

We have hereinabove referred to the acts which resulted in the distribution of certain of the surplus of the A. H. Stange Co. among the children of A. H. Stange as one transaction. The plaintiff insists that, beginning with the redistribution of the stock of the A. H. Stange Co. whereby the children and children-in-law of A. H. Stange received more stock than they had heretofore held, there was only one transaction. We do not consider this material. What we are here concerned with is the distribution of the surplus of the A. H. Stange Co. to its stockholders. The gift from A. H. Stange to his children was not taxable. The distribution of the surplus of the A. H. Stange Co. to its stockholders was taxable, whether it was only part of some inclusive transaction or not. There seems to have been some confusion of thought on this point. What we are holding was subject to a tax is not a gift but the distribution of property by a corporation. A. H. Stange was merely a stockholder in the A. H. Stange Co. He could not give away any of the property of this company or distribute it in any manner. That had to be done by an act of the corporation itself, and the fact that A. H. Stange practically controlled the corporation's acts does not alter the legal effect.

It is also contended by plaintiff that the only amount that is taxable is the credit which was given the plaintiff on the books of the new companies, but what the plaintiff got in the distribution was stock, cash, and debenture notes. So far as the value of the property of the A. H. Stange Co. which was distributed is concerned, there is no question but that the Commissioner put a moderate valuation thereon. All of this property so distributed went to the new companies and plaintiff and the other heirs held the same proportionate interest therein through stock that they held in the A. H. Stange Co. It is quite evident that it was intended by the several transactions to so distribute the property that each of the heirs would receive his proportionate value of the property received by the new companies. Whether we place the calculation of the dividend upon the value of the property conveyed to the new companies or whether we place it upon the value of the stock, cash, and debenture notes received, the result is the same, for there is no proof that the combined value of what was received by the plaintiff in the end was not equal to the value of his interest in the property conveyed. Indeed, the nature of the transaction indicates that it was.

The plaintiff's argument that the collection of the tax was barred by the statute of limitations is based on the claim that the waiver signed by plaintiff and the Commissioner of Internal Revenue was invalid because made after the expiration of the statutory period; and because by the terms thereof it was confined to the assessment of the tax, whereas the statute required the Commissioner and taxpayer to "consent in writing to a later determination, assessment, and collection of the tax." The latter objection will be first considered.

The ordinary meaning of the word "assess," when used in connection with matters of taxation, is to fix the amount to be paid by the taxpayer. An assessment can only be made if the taxpayer is liable for the tax, and if liable for the payment of the tax, it follows that it was collectible. In other words, a prerequisite of the right to assess is the right to collect the tax when assessed. It would seem, therefore, that an agreement for an assessment was based upon the understanding that the tax was collectible if assessed. However this may be, we think that a waiver of the statute of limitations is a contract, and that even if the statute has run, the moral obligation to pay a tax properly imposed is sufficient to constitute a consideration. The waiver in the case at bar, which is set out in Finding XI, set out a special consideration under which the Commissioner agreed to exercise "deliberate, intensive, and thorough consideration" of the liability of plaintiff for the taxes which were to be assessed. Possibly this was the Commissioner's duty in any event, and it might also be said that the statutes give him no authority to make a special agreement of this kind; but there was, as we have already seen, a consideration for the waiver, and an understanding, as there always is when waivers are executed, that further time will be taken for the consideration of the taxpayer's claims. In construing the waiver, the rules with reference to the construction of contracts should be applied. If the waiver did not authorize the collection of the tax, its execution was an idle performance—it was nothing but a useless scrap of paper. Whether plaintiff so intended or not, he and his attorneys must have known that the Commissioner accepted the waiver believing that it authorized the collection of any tax properly assessed. In such case, the rule with reference to contracts is—

"The language of a contract in case of ambiguity should be interpreted in the sense that the promisor knew or had reason to know that the promisee understood it." (13 C. J., sec. 484c, page 523, and cases cited, page 526.)

It should be said also that the words "assess" and "assessment," when used with reference to taxes, often include the collection thereof as a necessary sequence. In fact, the term "assess" is used at times to include all the steps involved in imposing a tax on property (*Allen v. McKay*, 120 Cal., 332), and "to assess" often means to levy a tax (see cases cited under note 76, 5 C. J., 813), the two words being used with practically the same meaning (*Idem.*, 76(b)), and the words "to levy" always include the collection of a tax. The same rule applies to the word "assessment," and the parties evidently intended that the word "assessment" should also cover the collection of the tax.

For the reasons stated above, we think that the waiver removed the bar of the statute of limitations not only as to assessment but as to collection of the tax.

It is further insisted that the statute providing for waivers had no application to waivers executed after the running of the statute of limitations, and the case of *Joy Floral Co. v. Commissioner* (29 Fed. (2d), 865), overruling 7 B. T. A., 800, is cited as so holding. In the case at bar the tax was assessed under section 250(d) of the Revenue Act of 1921, which provided that as to taxes due for any prior year, they "shall be determined and assessed within five years after the return was filed, unless both the Commissioner and the taxpayer consent in writing to a later determination, assessment, and collection of the tax." The *Joy Floral Co.* case, *supra*, discusses similar provisions contained in section 278 of the Revenue Act of 1924, under which the assessment was made in that case, and section 276 of the Revenue Act of 1928. In the two last-named sections the words "have consented" are used instead of the word "consent" in section 250(d) of the act of 1921. We do not think the difference is material, for reasons hereinafter given, but the *Joy Floral Co.* case holds that the Commissioner had no authority to enter into an agreement with the taxpayer for a waiver of the statute of limitations after the expiration of its limitation. The argument made in support of this decision is that the Commissioner's signature, after the statute of limitations had run, was unimportant. This statement loses its force when it is considered that it is just as important at that period as it would have been before the limitation had run. In the absence of a statutory provision either before or after the running of the statute of limitations, the taxpayer could by a mere oral statement waive the running of the statute. Even after the running of the statute, the moral obligation to pay any taxes that were properly levied would be a sufficient consideration for the waiver. The reason for hav-

ing the Commissioner sign the waiver had, in our opinion, nothing to do with its validity. The purpose of the statutory provision was to do away with the uncertainties of oral agreements. An oral statement on the part of the taxpayer would be subject to dispute and controversy as to its form and meaning, but Congress made it clear and definite that the taxpayer should not be bound unless written evidence of such waiver could be produced. On the part of the Government, it was always understood, if not by implication agreed, that the execution of these waivers would stay proceedings for the collection of the tax until the Government could properly consider the claims of the taxpayer. Congress did not intend that the Government should be bound in any way by the acceptance of waivers made by numerous collectors and revenue agents scattered all over the country but only in case the agreement was signed by the Commissioner of Internal Revenue. It was necessary for the orderly conduct of the Government's business that the Commissioner should have full knowledge of the action taken. In this we find abundant reason for the requirement of the signature of the officer, and, as we think, the only reason why it was required. To hold that the statute requires the Commissioner to consent to the waiver before the expiration of the period of limitation is to engraft upon the statute something which certainly is not contained within its provisions, nor, as we think, is there any reason to infer that such was the intent of Congress.

In the same case of the Joy Floral Co., *supra*, much stress was laid upon the fact that in the Revenue Acts of 1924 and 1928 the statute provided in effect that the waiver would only be effectual where both the Commissioner and the taxpayer "have consented" thereto in writing, and it is said the provisions just mentioned should be considered as interpretive of the language used in the 1921 Act. It appears to have been thought that the use of the word "have" before the word "consented" implied that this action must have been taken before the expiration of the period of limitation. If Congress had intended that the waiver must be executed before the period of limitation had expired, we think it would have said so. But it did not, and we see no justification for this construction, which we think is neither grammatical nor logical. Whether the word "consent" is used alone, as it was in the 1921 Act, or the words "have consented" are used, as in the 1924 and 1928 acts, is immaterial. If a prior "consent" is required, then the parties must "have consented." The latter expressions are merely a paraphrase. In any event, the parties must "have consented" to the waiver prior to the time of the collection of the tax, and the words in the later statutes merely express the natural sequence of the two events. This is true even though the 1921 Act be construed literally and strictly. In our opinion, the decision of the Board of Tax Appeals is supported by the better reasoning, and the objections of the plaintiff to the validity of the waiver must be overruled.

From what we have stated above, it follows that the plaintiff's petition must be dismissed, and it is so ordered.

BOOTH, Chief Justice, concurs.

GRAHAM, Judge, concurs in the findings and the result.

SECTION 202.—BASIS FOR DETERMINING GAIN OR LOSS.

ARTICLE 1561: Basis for determining gain or
loss from sale.

VIII-27-4263
Ct. D. 76

INCOME TAX—REVENUE ACT OF 1918—DECISION OF SUPREME COURT.

INCOME—GAIN—PROCEEDS OF LIFE INSURANCE—POLICY PAID UP BEFORE MARCH 1, 1913.

Where an insured, having a nonassignable policy of insurance upon his own life which was fully paid up before March 1, 1913, exercises an option in 1919, at the end of a tontine period of 20 years, of receiving the face value of the policy and in addition the accumulated cash dividends applicable to it which were set aside or ascertainable on the books of the insurance company each year but

were payable only at the end of the tontine period and only to holders of policies still in force at that time, the taxable gain realized by him upon the surrender of the policy, ascertained under section 202(a)1 of the Revenue Act of 1918, is the amount by which the proceeds of the policy exceed the sum of the insurance reserve liability and the dividend accumulations provisionally apportioned to the policy on March 1, 1913.

SUPREME COURT OF THE UNITED STATES.

Robert H. Lucas, Collector of Internal Revenue for the District of Kentucky, petitioner, v. Kate Holloway Alexander et al., etc.

On writ of certiorari to the United States Circuit Court of Appeals for the Sixth Circuit.

[May 20, 1929.]

OPINION.

Mr. Justice STONE delivered the opinion of the court.

This case is here on certiorari, granted November 19, 1928 (278 U. S., 594), to review a judgment of the Court of Appeals for the Sixth Circuit (27 F. (2d), 237), affirming a judgment of the District Court for Western Kentucky (21 F. (2), 68), allowing recovery from the collector of internal revenue of Federal income taxes alleged to have been illegally exacted.

On May 19, 1899, respondents' testator procured two life insurance policies for \$50,000 each upon his own life and payable to his estate. On May 19, 1908, they became fully paid-up policies, upon the payment of the last of 10 annual premiums aggregating, for both policies, \$78,100. Each policy stipulated that in the event of death within 10 years the amount payable should be \$50,000 and, from the eleventh to the twentieth year, inclusive, an annually increasing amount ranging from \$50,700 in the eleventh year to \$72,150 in the twentieth year. The death benefit on each policy during the year ending May 19, 1913, was \$59,300. The policies participated in the surplus of the company and "dividends" properly allocable to each were set aside or ascertainable on its books each year, but were payable only at the end of the tontine period of 20 years, and only to holders of policies still in force at that time.

The insured was given an option at the end of the period of receiving on each policy the sum of \$50,000 "and in addition the cash dividend then apportioned by the company." The insured elected to exercise this option May 19, 1919, receiving as proceeds of the two policies \$120,797, representing \$100,000 face value plus \$20,797 dividends. The gain to him over his total premium expenditure was thus \$42,697. The Commissioner assessed this amount as taxable income under the Revenue Act of 1918 (ch. 18, 40 Stat., 1057).

Both the district court and the court of appeals thought that, under section 202(a)1 of the Act, only so much of the proceeds of the policies as exceeded their value on March 1, 1913, was subject to tax. They found that the amount provisionally set aside by the company as surplus accumulations applicable to the two policies on that date was \$13,600, and that it was then evident that the rate of accumulation, although not certain, would probably be greater during the later years of the tontine period than before March 1, 1913. Even at the same rate, the accumulation at the end of the period would amount to \$19,428.57. Both courts, therefore, concluded that the insured might reasonably have anticipated that the policies would have been worth on their maturity date, if then in force, their face value plus the anticipated accumulations, or a total for both policies of \$119,428.57. Since, under the sliding scale, the death benefits would have been even proportionately larger had the insured died before the end of the period, they decided that the combined value of the policies on March 1, 1913, was the smaller amount discounted at the rate of 4 per cent compounded annually to that date, or \$93,587.81. The taxable gain on the policies, accordingly, was taken to be the difference between this amount and the actual proceeds of the policies, or \$27,209.19. A recovery was allowed of the difference between the tax as assessed and that as computed on the gain after March 1, 1913, so ascertained.

As respondents did not ask certiorari, we may disregard their argument that the judgment below was erroneous in that the proceeds of an insurance policy

paid to the insured are not taxable income, except as the determination of that question may be involved in passing upon the assignments of error of petitioner. See *Federal Trade Commission v. Pacific Paper Ass'n.* (273 U. S., 52, 66).

By the expenditure of \$78,100 in premiums, the insured secured a return of \$120,797, resulting in an economic and realized money gain to him of \$42,697. The question of liability for the tax on this gain is different from that mooted by counsel, but not decided, in *United States v. Supplee-Biddle Hardware Co.* (265 U. S., 189, 194 [T. D. 3604, C. B. III-1, 112]), which was whether insurance upon the life of a corporate officer, paid at his death to the corporation, could be constitutionally subjected to a tax on income. Here the amount paid was not a death benefit or in the nature of a gift to a beneficiary and was in no sense an indemnity for, or repayment of, an economic loss suffered by the insured, but was a profit or gain upon his premium investment, and would seem to be plainly embraced within the provisions of section 213 taxing "gains or profits and income derived from any source whatever" and not exempted as such from tax by any other provision of the Act. (See *Penn. Mutual Co. v. Lederer*, 252 U. S., 523, 532, 534 [T. D. 3046, C. B. 3, 249]; *Eisner v. Macomber*, 252 U. S., 189, 207 [T. D. 3010, C. B. 3, 25]; *Merchants' Loan & Trust Co. v. Smietanka*, 255 U. S., 509, 518 [T. D. 3173, C. B. 4, 34].)

But of this total gain received by the insured, a part is attributable to and accrued during the period before the effective date of the sixteenth amendment (February 25, 1913), and of the first law taxing the income of individuals (March 1, 1913), and hence, for income-tax purposes, must be deemed an accretion to capital not taxable by the Income Tax Acts enacted under the sixteenth amendment. (See *Southern Pacific Co. v. Lowe*, 247 U. S., 330, 334; cf. *Doyle v. Mitchell Bros. Co.*, 247 U. S., 179; *Lynch v. Turrish*, 247 U. S., 221.) Whether or not such accretions may be constitutionally subjected to tax, we have no occasion to decide. The present Act, at least, does not attempt it. But the question presented necessarily involves a determination of what part of the total gain received by the taxpayer accrued to him after March 1, 1913. In answering it, provisions of the taxing statute enacted as aids in arriving at the answer must be construed with an eye to possible constitutional limitations so as to avoid doubts as to its validity. (*United States v. Delaware & Hudson Co.*, 213 U. S., 366, 407, 408; *United States v. Standard Brewery*, 251 U. S., 210, 220; *Texas v. Eastern Texas R. R. Co.*, 258 U. S., 204, 217; *Bratton v. Chandler*, 260 U. S., 110, 114; *Panama R. R. Co. v. Johnson*, 264 U. S., 375, 390.)

Section 202 of the Revenue Act of 1918 provides:

"(A) That for the purpose of ascertaining the gain derived or loss sustained from the sale or other disposition of property, real, personal or mixed, the basis shall be:

"(1) In the case of property acquired before March 1, 1913, the fair market price or value of such property as of that date."

The Government insists that the policies, being nonassignable except to persons having an insurable interest in the life of the insured, had no market price and their combined value as of March 1, 1913, did not exceed their loan or cash surrender value on that date, which alone could be realized on them, of \$74,600, Regulations 45 (1920), article 87, and that any greater value assigned to them as of that date must be rejected as contingent and speculative. But in view of the provisions of section 213(b)2 of the Act (see Regulations 45 (1920), article 72(b)), exempting from taxation the return of premiums on the maturity of the policy, it concedes that the taxable gain of the insured may be taken at the amount, fixed by the Commissioner, by which the proceeds of the policies exceeded \$78,100, the total premiums paid.

Plainly, in the present case, the \$42,697 gained over premium cost of the two policies, which accrued to the taxpayer through a period of 20 years, did not all accrue in the 6 years following March 1, 1913. If the value on that date, for the purpose of ascertaining taxable gain, was greater than the total premium expenditure which had been completed more than 4 years before, there is no reasonable basis for determining the taxable gain which accrued after March 1, 1913, by deducting from the total amount received the total premium payments.

Nor can we accept the contention of the Government that the value of the policies on March 1, 1913, did not exceed their loan value as of that date. The purpose of ascertaining the value of the taxpayer's property on March 1, 1913, is, as section 202 states, to measure that part of his total gain which has arisen

or accrued after the enactment of any of the statutes taxing income and thus to arrive at his gain which may be taxed as income. (*Lynch v. Turrish*, supra.) Value as of that date may be disregarded unless it serves that purpose. (*United States v. Flannery*, 268 U. S., 98 [T. D. 3703, C. B. IV-1, 106]; *Goodrich v. Edwards*, 255 U. S., 527 [T. D. 3174, C. B. 4, 40]; *Walsh v. Brewster*, 255 U. S., 536 [T. D. 3176, C. B. 4, 41].)

Under the statute, market price of the taxpayer's property on that date, where ascertainable, may be resorted to as generally a sufficiently definite and trustworthy gauge of the gain which has later accrued. But where the property has no market value, the statute must be interpreted in the light of its purpose to ascertain taxable gains accruing since March 1, 1913. Hence, in such a case its fair value on the critical date is not necessarily what might then have been realized upon it by a forced liquidation by accepting the unfavorable loan or cash surrender value. Having in mind the purpose of the statute, we think it must be taken rather to be that part of the amount actually realized by the taxpayer which, by the use of appropriate accounting methods, can fairly be said to have accrued before March 1, 1913—its value then as compared with the value in fact later realized by the taxpayer taken as a standard.

In applying section 202(a)1 to an insurance policy having no market value, we are not required either by circumstances or any positive provision of statute to determine its value on March 1, 1913, by making a prediction as of that time based upon an estimate of future possibilities, as is the case in valuing for purposes of inheritance tax an interest of uncertain duration passing at the death of the testator. (See *Ithaca Trust Co. v. United States*, No. 267, October term, 1928, — U. S., — [Ct. D. 61, C. B. VIII-1, 313].) There the value as of the date of death is the very thing taxed and can usually be determined only by speculation as to future events. Here, 1913 value is at most merely a method of allocating a known income to the periods in which it actually accrued. It is never necessary to speculate, as did the court below, as to what might later be realized from his property by the taxpayer, nor as to what might have been realized if, on March 1, 1913, he had made some forced disposition of the property which would have precluded any taxable gain. For the necessity of ascertaining value as of March 1, 1913, can never arise until some later date when income has been produced by converting the property into money or money's worth and the amount actually realized is known, and then, as we have said, only for the purpose of apportioning the total gain which has accrued between the periods before and after March 1, 1913.

It is familiar knowledge that the source of dividend accumulations upon insurance policies is interest upon investments of the company and savings effected from estimated future expenses and from death payments covered by premiums, with appropriate "loadings" to give a margin of safety, which the policyholders have paid. In accordance with the usual practice of life insurance companies, under the system of accounting employed by the insurer in the present case, the amount of reserve set aside by the company to meet its policy liability and dividend accumulations provisionally apportioned to each policy was ascertained or ascertainable on the books of the company at the end of each year. During the policy year which included March 1, 1913, the insurance reserve liability thus ascertained on each of the present policies was \$40,600 and the dividend accumulation on each, which both courts below found had accrued on March 1, 1913, was \$6,800, making a total of reserve and accumulations applicable to each policy of \$47,400. These items, with subsequent annual additions totaled at the maturity of each policy, for the former \$50,000 and for the latter \$10,398.50, which, taken together, made up the total payment received by the taxpayer on each policy. They constitute a complete record and determination of the actual economic gain annually accruing upon the policies which was ultimately realized by the taxpayer and they provide an adequate basis for ascertaining the proportion of the total value realized which had accrued on March 1, 1913. The sum of the insurance reserve liability and the dividend accumulations provisionally apportioned to the two policies on March 1, 1913, their accrued value on that date, was \$94,800. As that valuation is larger than that found by either of the lower courts and is supported by reliable data, we may, in the absence of other evidence, accept it as sufficiently establishing that the value found below was not more than that required to be ascertained by the statute and so did not prejudice the rights of petitioner. It is unnecessary to consider the question mooted whether upon other evidence, not here presented, a larger value as of March 1, 1913, might have been found.

The court below, by discounting the total estimated value of the policies at their maturity at 4 per cent, arrived at a rough approximation of their accrued value on that date. This method, however, did not ascertain that value or the taxable gain with accuracy, since it was based on an assumed instead of the actual value of the policies at maturity. It discounted the assumed value at a flat rate of interest instead of at that actually earned, and it left out of account savings from estimated expenses and death losses which, as well as actual interest earned, were taken into account in determining dividend accumulations annually ascertained and credited to the policies on the books of the company. But, as the accuracy of the computation is not questioned here, and as it gave a result of which petitioner can not complain, the judgment will be affirmed.

ARTICLE 1561: Basis for determining gain or loss from sale.

REVENUE ACT OF 1921 AND PRIOR REVENUE ACTS.

Dower or statutory interest, value not having been returned to widow before her death. (See I. T. 2480, page 141.)

ARTICLE 1561: Basis for determining gain or loss from sale. VIII-32-4304 Ct. D. 89

INCOME TAX—REVENUE ACT OF 1921—DECISION OF COURT.

GAIN OR LOSS—DEPRECIATION.

In the determination of the amount of gain on the sale of a building by a testamentary trustee under section 202 of the Revenue Act of 1921, the cost or other basis must be decreased on account of the aggregate allowance for depreciation of the building to which the trust was entitled since March 1, 1913, whether actually deducted or not in the returns of the trust.

DISTRICT COURT OF THE UNITED STATES, DISTRICT OF MASSACHUSETTS.

Old Colony Trust Co. v. White.

[January 29, 1929.]

OPINION.

LOWELL, J.: This case raised the question of the right of the Commissioner of Internal Revenue in determining the profit on the sale of a building to take into account the amount of depreciation which the building had suffered during the years before its sale. Two buildings were held by a trustee under a will which provided that the income should be paid to a life tenant. They were both rented, and for three of the years depreciation was claimed and allowed, but for the other years it was not claimed. The contention is that the trustee could not legally deduct in his annual returns any amounts for depreciation in value, and therefore that to take account of such depreciation in determining the profit on the sale of a building would amount to double taxation, as the life tenant during the years when such deduction was not claimed would pay a tax on the entire rent from the buildings, without any deduction for depreciation. The contention seems sound, but the reasoning of the opinion in *United States v. Ludey* (274 U. S., 295 [T. D. 4046, C. B. VI-2, 157]) invalidates it. In that case an oil well was sold after having been worked for some time, and in determining the loss from the sale the Commissioner took account of the depletion of the well. The depletion had been accounted for in the annual returns; the court mentions this fact and says that if it is not accounted for on the sale there will be a double deduction. The facts in the Ludey case are therefore not the same as in the case at bar, but in determining the question the court said:

"The depreciation charge permitted as a deduction from the gross income in determining the taxable income of a business for any year represents the reduc-

tion, during the year, of the capital assets through wear and tear of the plant used. The amount of the allowance for depreciation is the sum which should be set aside for the taxable year, in order that, at the end of the useful life of the plant in the business, the aggregate of the sums set aside will (with the salvage value) suffice to provide an amount equal to the original cost." (274 U. S. at p. 300.)

The theory on which the Ludey case was decided is applicable to the case at bar—that when a property subject to depletion or depreciation has been sold at the end of a period of years, the property is a different one from that which was owned by the taxpayer at the beginning. In the case of the oil well, a large part of the oil had been withdrawn; in the case of the manufacturing plant, which the judge mentions, the plant had depreciated in value by wear and tear. Since the Ludey case the Court of Appeals for the Second Circuit has decided the case of *Hardwick Realty Co. v. Commissioner*, December 3, 1928, not yet reported, which in its facts corresponds to the case at bar.

In view of the reasoning of the Ludey case as applied in the *Hardwick* case, I am constrained to decide that the Government's contention is correct. See also *Rieck v. Heiner* (25 F. (2d), 453 [T. D. 4161, C. B. VII-1, 200]); Appeal of *Even Realty Co.* (1 B. T. A., 355).

The further contention of the plaintiff that the terms of the Act of 1921, under which this tax was imposed, do not allow the consideration of deductions in determining the profit on a sale is unfounded. The plaintiff admits that his contention would apply only to property bought before March 1, 1913, and it is not a reasonable construction of the congressional statute that a different rule should apply to sales of property bought before and after that date.

Judgment for defendant.

ARTICLE 1561: Basis for determining gain or
loss from sale.

VIII-51-4476
Ct. D. 142

INCOME TAX—REVENUE ACT OF 1916—DECISION OF COURT.

DEDUCTION—LOSS—SALE—PROPERTY ACQUIRED BEFORE MARCH 1,
1913.

No deductible loss is sustained under the provisions of the Revenue Act of 1916 where property purchased prior to March 1, 1913, is sold thereafter for less than cost but more than its fair market value on that date.

UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT.

*Malcolm E. Nichols, Collector of Internal Revenue, Defendant, appellant, v.
Sumner Smith, Executor, Plaintiff, appellee.*

Appeal from the District Court of the United States for the District of Massachusetts.

[November 22, 1929.]

OPINION.

BINGHAM, J.: This is an action at law brought by the plaintiff, appellee, against the collector of internal revenue to recover the sum of \$4,868.72 and interest from date of payment, that sum being an additional tax for the year 1917, claimed to have been illegally assessed and collected. The tax was paid under protest and refund was duly claimed and rejected. The additional tax was based on the amount of an alleged loss incurred by the plaintiff in the sale of certain stock.

In the district court judgment was rendered in favor of the plaintiff and this appeal was taken.

It was found that in 1903 the taxpayer purchased certain shares of stock for \$26,910; that their fair market value on March 1, 1913, was \$7,020; and that he sold the stock in 1917 for \$14,040. In his income tax return for the calendar year 1917 the taxpayer deducted as a loss the sum of \$12,870, that being the difference between the cost of the stock in 1903 and the sale price in 1917. The Commissioner disallowed this sum as a deductible loss, on the ground that

none of it occurred after March 1, 1913, and assessed an additional tax of \$4,868.72 on the \$12,870, regarding that as net income.

The only question is whether the \$12,870 was a loss which the taxpayer could deduct from his gross income, the fair market value of the stock on March 1, 1913, being less than its cost in 1903. There was an actual loss. Was there a deductible one that was sustained after March 1, 1913, the date on which the income tax law became effective?

The Revenue Act of 1916 provides:

"SEC. 2. (c) For the purpose of ascertaining the gain derived from the sale or other disposition of property, real, personal, or mixed, acquired before March 1, 1913, the fair market price or value of such property as of March 1, 1913, shall be the basis for determining the amount of such gain derived.

"SEC. 5. (a) Fourth * * * *Provided*, That for the purpose of ascertaining the loss sustained from the sale or other disposition of property, real, personal, or mixed, acquired before March 1, 1913, the fair market price or value of such property as of March 1, 1913, shall be the basis for determining the amount of such loss sustained." (39 Stat., 756.)

The Supreme Court, in construing these provisions of law, has held that no gain can be taxed and no loss deducted in computing the taxpayer's income unless there is an actual gain or an actual loss. *Goodrich v. Edwards* (255 U. S., 527 [T. D. 3174, C. B. 4, 40]); *Walsh v. Brewster* (255 U. S., 536 [T. D. 3176, C. B. 4, 41]); *Lucas v. Alexander* (279 U. S., 573 [see Ct. D. 76, on page 273]) (cases relating to gains under section 2 above quoted); and *United States v. Flannery* (268 U. S., 98 [T. D. 3703, C. B. IV-1, 106]); *McCaughn v. Ludington* (268 U. S., 106 [T. D. 3705, C. B. IV-1, 110]); and *Heiner v. Tindle* (276 U. S., 582 [T. D. 4212, C. B. VII-2, 272]) (cases relating to losses under section 5(a)); that, as to property acquired prior to March 1, 1913, and disposed of subsequent to that date, section 2(c) imposes a tax upon *actual gain*, but only to the extent that it accrued during the period that elapsed between March 1, 1913, and the time of the sale (cases above cited as to gain); and that as to property acquired before March 1, 1913, and disposed of subsequent to that date, section 5(a)4 allows a deduction for an *actual loss*, but only to the extent it was incurred during the period that elapsed between March 1, 1913, and the time of the sale or disposition of the property. (Cases cited above as to losses.)

It has also held that where the transaction shows an *actual gain* and the March 1, 1913, value is *less* than the cost, the *taxable gain* is ascertained by subtracting the cost from the selling price (this was the holding as to the second transaction in *Walsh v. Brewster*, supra); and that where there is an *actual gain*, and the March 1, 1913, value is *greater* than the cost, the *taxable gain* is ascertained by subtracting the March 1, 1913, value from the selling price. This was the holding as to the first transaction in *Goodrich v. Edwards*, supra; and in the single transaction involved in *Lucas v. Alexander*, supra.

Now as to losses: In *United States v. Flannery*, supra, the taxpayer undertook to deduct as a loss the difference between the sale price and the March 1, 1913, value. This was disallowed, for the reason that the sale price showed a gain over the cost, and the court held that, as there was no actual loss, there was no deductible one. But in cases where the transaction involved disclosed an actual loss and that the March 1, 1913, value was *greater* than the cost, it has been held that the *deductible loss* is ascertained by subtracting the sale price from the cost. This was the conclusion as to the transaction involved in *McCaughn v. Ludington*, supra, where there was an actual loss, and the March 1, 1913, value was greater than the cost. And the same proposition was affirmed in the case of *Heiner v. Tindle* (276 U. S., 582, 587), decided April 9, 1928.

It has also been held by the Supreme Court, in the case of property acquired before March 1, 1913, and sold after that date, at an actual loss, that, when the March 1, 1913, value is *less* than the cost, the deductible loss is ascertained by subtracting the sale price from the March 1, 1913, value. (*Heiner v. Tindle*, 276 U. S., 582, 587.) In that case the property involved was a dwelling house. It was purchased in 1892 at a cost of \$172,000. In 1901 the taxpayer ceased to use it as a residence, and on October 1, 1901, devoted it exclusively to the production of taxable income in the form of rentals, a transaction for profit. He continued to lease it until 1920, when it was sold for \$73,000. The fair market value of the property on March 1, 1913, was \$120,000. Its value on October 1, 1901, when it was exclusively devoted to the production of in-

come, was not found. In his tax return for 1920, the taxpayer deducted as a loss \$47,000, the difference between the March 1, 1913, value (\$120,000) and the sale price (\$73,000). The Commissioner disallowed the deduction and assessed an additional tax upon the \$47,000. The tax was paid under protest, and suit was brought in the district court to recover the additional tax. In that court the action of the collector in disallowing the deduction was affirmed, but in the circuit court of appeals the judgment of the district court was reversed and the deduction of \$47,000 allowed. The Supreme Court reversed the judgment of the court of appeals, on the ground that one essential fact, the cost or value of the property on October 1, 1901, when it was exclusively devoted to a production of income, had not been found. It remanded the case for a new trial on that question, with instructions that if the value of the property on March 1, 1913, was less than its cost or value on October 1, 1901, the deduction of \$47,000, the difference between the March 1, 1913, and the sale price, should be allowed. But that if the value of the property on March 1, 1913, was greater than its cost or value on October 1, 1901, then the difference between the October 1, 1901, value or cost and the sale price was to be deducted.

From the foregoing it is apparent that the decision in *Hetner v. Tindle*, as stated in the instructions to the lower courts, included two possible situations. One such as that considered in *McCaughn v. Ludington*, where the March 1, 1913, value was greater than the cost price. And one like that involved in the present case, where the March 1, 1913, value is less than the cost price—in which situation the court points out that the deductible loss is the difference between the value on March 1, 1913, and the sale price. We must conclude, therefore, that the district court, on the facts here presented, erred in allowing the difference between the cost in 1903 and sale price in 1917 as a deductible loss. The facts clearly show that all the loss was incurred prior to March 1, 1913; and as only losses occurring subsequent to that date are deductible, this was not.

As under the income tax statute only gains accruing subsequent to March 1, 1913, are taxable as income, we fail to see wherein the statute can be regarded as unconstitutional, if construed as providing that losses sustained prior to that date shall not be allowed as deductions.

The judgment of the district court is reversed, and the case is remanded to that court with directions to enter judgment for the defendant, with costs.

SECTION 206.—CAPITAL GAIN.

ARTICLE 1651: Definition and illustration of capital net gain.

REVENUE ACT OF 1921.

Stock called in or bond redeemed before maturity date. (See I. T. 2488, page 127.)

ARTICLE 1651: Definition and illustration of capital net gain.

VIII-36-4339
Ct. D. 97

INCOME TAX—REVENUE ACT OF 1921—DECISION OF COURT.

1. CAPITAL GAIN—CAPITAL ASSETS—RENTS—MINERAL LEASE.

Where an owner in fee executes an instrument by which he grants, demises, and leases described land for the sole purpose of mining oil and gas for a specified term and as long thereafter as oil or gas is produced from the land by the lessee, the lease does not constitute a sale of minerals in place but a grant of the privilege of entering upon the land and developing and removing the minerals therefrom. Accordingly, the consideration received from the lessee is not the sales price of "capital assets" within the meaning of section 206 of the Revenue Act of 1921, the net gain from the sale of which is taxable at the limited rate therein provided, but rents or royalties the net income from which is taxable at the ordinary rates provided by sections 210 and 211 of that Act.

2. DECISION AFFIRMED.

The decision of the United States Board of Tax Appeals (6 B. T. A., 1287) affirmed.

COURT OF APPEALS OF THE DISTRICT OF COLUMBIA. No. 4697.

Henry L. Berg and Rose Berg, His Wife, v. Commissioner of Internal Revenue.

Appeal from the United States Board of Tax Appeals.

[June 3, 1929.]

OPINION.

GEORGE E. MARTIN, Chief Justice Court of Appeals of the District of Columbia.

This proceeding is brought by appellant-taxpayers for the review of a decision of the Board of Tax Appeals reported in 6 B. T. A., 1287, which affirms a deficiency in the income tax liability of appellants as determined by the Commissioner of Internal Revenue. The return was made for the year 1922 under the Revenue Act of 1921.

The income of appellants herein involved was derived from certain oil and gas leases upon lands owned by them in fee, and they claim that the income was received as a consideration for the sale of the oil and gas in and under the leased premises. They claim that it should be taxed as gain derived from the sale of capital assets at the limited rate provided by section 206 of the Act, and not as ordinary income at the rates provided by sections 210 and 211. The Commissioner of Internal Revenue, however, held that the receipts were rents taxable as ordinary income under sections 210 and 211 of the Act. This resulted in the determination of a deficiency in the tax liability of appellants for the year 1922 in the sum of \$10,655.92. The Board of Tax Appeals sustained this determination.

The term "capital gain" is defined by section 206 of the Act as meaning "taxable gain from the sale or exchange of capital assets." The term "capital assets" as used in the section is defined as meaning property acquired and held by the taxpayer for a certain period for profit or investment, whether or not connected with his trade or business.

The oil and gas leases in question are similarly drawn. In each of them it recited that the lessor in consideration of a cash payment, and of the covenants following, does grant, convey, demise, and lease unto the lessee a certain described tract of land, for the sole and only purpose of mining and operating for oil and gas, and for laying pipe lines, etc., to produce, save, and take care of such products. It is provided that the lease shall remain in force for a specified term, and as long thereafter as oil or gas, or either of them, is produced from the land by the lessee. The lessee is to deliver to lessor one-eighth of all oil produced and saved from the leased premises, and to pay a certain sum annually for all gas used off the premises. If no well is commenced on the land within a specified time, or within 12 months after the first well is drilled should it prove to be a dry hole, the lease shall terminate, unless the lessee makes certain payments which shall be credited as rentals.

The sole point at issue in this appeal is whether the consideration received by appellants under the oil and gas leases aforesaid falls within the classification of gain from the sale of capital assets within the sense of the statutory definition of that term; in other words, whether the leases constituted a sale of the minerals in situ in the land.

The reported cases upon this subject are not in accord, but the controlling authority is to the effect that such a lease is not a sale or conveyance of the minerals within the sense of the taxing statutes. It follows accordingly that the consideration received by appellants from the lessees is not the purchase price paid by the latter for the oil and gas produced under the lease, but is rent or royalty paid for the development rights granted to the lessees thereby.

In *Von Baumbach v. Sargent Land Co.* (242 U. S., 503) the Supreme Court dealt with mining leases which provided that the owners of the described lands demised the same to the lessees exclusively for the purpose of exploring for, mining, and removing the merchantable iron ore which might be found therein, for and during the period named, usually 50 years. The lessees were given exclusive right to occupy and control the demised premises and to erect all

necessary buildings, structures, and improvements thereon. The lessees agreed to mine and ship a specified quantity of ore each year or in default to pay a certain sum to lessors. The right was reserved by lessors to terminate the contract upon failure of the lessees to comply with the terms thereof.

The question arose in the case whether the moneys received by the land-owners during the years in question in payment for iron ore, under the contracts covering the mineral lands, were gross income, or whether they represented, in whole or in part, the conversion of the investment of the owners from ore into money. The court held that the leases in question were not equivalent to sales of property, and that the moneys paid by the lessees to the owners were not converted capital, but rents or royalties, and as such were income, proper to be included in measuring their taxes under the corporation tax law. (Citing *Stratton's Independence v. Howbert*, 231 U. S., 399; *Stanton v. Baltic Mining Co.*, 240 U. S., 103.) Mr. Justice Day, in delivering the opinion of the court, cites with implied approval the cases of *State v. Evans* (99 Minn., 220), *Roeding v. Owsley* (122 Minn., 190), and *State v. Royal Mineral Association* (132 Minn., 232), which are to the effect that leases for the purpose of developing and working mines do not constitute a sale of any part of the lands, and that the amounts stipulated to be paid by the lessees are rents.

In *United States v. Biscanik Mining Co.* (247 U. S., 116), the Supreme Court had before it a lease whereby the defendant acquired the right for the term of 50 years and 3 months from the 1st day of May, 1898, to explore for, mine cut, and remove the merchantable shipping iron ore which might be found upon the lands described in the lease upon the payment of a royalty of 30 cents for each ton mined. The expression "merchantable ore" was defined as including "all ores which grade 55 per cent and above in metallic iron regardless of other ingredients." The lessee contracted to mine and remove at least 300,000 tons of ore annually or to make certain payments in default thereof. Any failure to keep or perform any of the covenants or conditions of the lease gave to the lessor the option to take immediate possession of the premises. The deposit of ore on the leased premises was of such a character that its quality and quantity were capable of determination with extraordinary accuracy by drilling and shafts, and the defendant had calculated the tonnage remaining on the land at the time in question as 6,874,695 tons, all of which could be easily removed within the term of the lease.

The court held that such a lease was not a conveyance of the ore in place, although the latter could be measured with substantial accuracy, but was a grant of the privilege of entering upon, discovering and developing, and removing the minerals from the land, and that the lessor's income from such operations was subject to taxation under the Corporation Tax Act of August 5, 1909.

The present case in our opinion is governed by those just cited. We hold accordingly that the income of appellants under the leases in question was received as rent or royalty and not as the purchase price of the oil or gas produced from the lands by the lessees. The receipts therefore were not to be taxed as gains from the sale of capital assets but as ordinary income under the Revenue Act of 1921.

The decision of the Board of Tax Appeals is affirmed with costs.

ARTICLE 1653: Partnerships, estates, and trusts.

REVENUE ACT OF 1921.

Profit derived from sale of land covered by a trust governed by section 704(b), Revenue Act of 1928, or a trust similar to one considered in General Counsel's Memorandum 4120 (C. B. VII-2, 108). (See G. C. M. 6630, page 179.)

PART II.—INDIVIDUALS.

SECTION 212.—NET INCOME OF INDIVIDUALS DEFINED.

ARTICLE 23: Bases of computation.

REVENUE ACT OF 1918.

Commissioner's determination as to basis on which books are kept.
(See Ct. D. 124, on page 320.)

ARTICLE 23: Bases of computation.

VIII-49-4453
Ct. D. 134

INCOME TAX—REVENUE ACTS OF 1916, 1918, AND 1919—DECISION OF COURT.

INCOME—METHOD OF ACCOUNTING—ROAD CONSTRUCTION CONTRACT.

Where a taxpayer, keeping its books on the accrual basis, is engaged in constructing roads under contracts each of which requires it to maintain the road covered by the contract free of defects at its expense for a period of five years after its completion and the payment of the last installment of the contract price, a method of bookkeeping that keeps a given contract open and defers the disclosure of a profit or a loss from the contract until the end of the maintenance period does not clearly reflect income for the purpose of income taxation.

UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

George Vang and George Lanz, Receivers of Thomas Cronin Co., A Corporation, appellants, v. C. G. Lewellyn, Formerly Collector of Internal Revenue, Twenty-third District of Pennsylvania, appellee.

George Vang and George Lanz, Receivers of Thomas Cronin Co., A Corporation, appellants, v. D. B. Heiner, Collector of Internal Revenue, Twenty-third District of Pennsylvania, appellee.

[September 27, 1929.]

OPINION.

WOOLLEY, Circuit Judge: Thomas Cronin Co., after payments made under protest, brought these suits against collectors of internal revenue in office at different periods to recover corporation income and excess-profits taxes assessed and collected for the years 1917 to 1922 under provisions of the Revenue Acts of 1917, 1918, and 1921. The cases were tried to the court without a jury mainly on facts stipulated. The defendants had judgments and the plaintiff appealed.

Of the court's many findings of fact the controlling ones will be compressed into the following statement:

The plaintiff company during the tax years in question was engaged in constructing roads for the city of Pittsburgh and the county of Allegheny under contracts calling for payments by installments as work progressed. Generally the construction work was finished within the year it began; sometimes it extended into the next year. Taking one contract as an illustration of what was done under all, when work had been finished and the last installment of the contract price paid, the company offset expenditures against receipts and regarded the difference as profit or loss on that job. As under each contract the company was required, at its own expense, to maintain the road free of all defects arising from materials or construction for a period of five years after completion, it estimated probable maintenance costs and set aside an esti-

mated reserve to cover them. This it deducted from the profits it had actually made on the contract and, in its original tax returns, reported the difference as taxable net income for the year the work was finished. The Commissioner, however, disallowed the estimated reserves for maintenance as deductions, holding that the company's liability for maintenance was contingent, not fixed, and therefore not within the law of allowable deductions. Then the company filed amended returns by which it showed that it kept its accounts on the basis of completed contracts, represented that a contract was not completed until the end of the maintenance period, declared its income from the contract received at that time, and calculated its tax at the rate then prevailing.

The trouble in these cases arose out of confusion in the use of the term "lawful method of bookkeeping." The taxpayer's method was for its own purposes entirely lawful, but for tax purposes it was not lawful unless it clearly reflected income. What the company did finally, as shown by its amended returns on which it makes its last stand, was to regard a contract as not completed (and therefore its profits and gains not income subject to tax) until the end of the five years' period of maintenance following the full completion of the work and full payment of the contract price when final maintenance costs had become definitely known. It then put this theory of postponed completion of work and postponed taxable income into bookkeeping operation by carrying installments received on account of the contract price as liabilities and construction expenditures as credits, and also maintenance expenditures as credits, until at the end of the maintenance period it adjusted the books and struck a balance which disclosed a profit or a loss.

The practical result of this method of bookkeeping was, at different periods, to reflect a loss when no loss had been incurred, conceal profits when profits had been made or were in the making, and postpone completion of the contract and final determination of profits as taxable income to the end of the maintenance period and postpone payment of taxes on income actually received years earlier when taxes were higher until years when they were lower. Even so, the method of bookkeeping was lawful for tax purposes if it truly reflected income. Did it?

Oddly enough, moneys coming in as partial payments for work done were by this method treated as liabilities or as moneys going out, and moneys going out in the way of expenditures were treated as credits or moneys coming in. As this did not reflect what actually happened, it did not reflect income. While this method of bookkeeping was entirely honest and was plain enough to the plaintiff and capable of readjustment in the future, it did not show profits and losses, that is, income or lack of it, on a given contract until, at the plaintiff's will, such readjustment was made. What actually happened was the receipt of income by payment of the contract price upon the completion of the work, whether within or beyond the year. We hold that when the construction work was finished and the contract price paid and the road turned over to the city or county, the contract was completed, disclosing definitely gain or loss in the transaction. This was how the company itself first regarded it when it made and set aside estimated reserves to cover costs of maintenance on its many contracts and then claimed them as deductions from income received in the year the transactions came to an end by payment and delivery. The company's engagement to maintain the work in good condition for five years after completion as a pledge of its workmanship was clearly a contingent liability which might or might not cost money—it occurred in only 3 out of every 12.5 jobs—and, accordingly, might or might not reduce the net income from a contract closed by final payment long before. Cost of maintenance, if any, would of course be a subject for reduction from income in the year in which income was received, but such costs, having no effect upon or relation to the final payment of the contract price at the end of the work, would not keep the contract open and postpone payment of the tax on the income received.

Nor does the fact that the company kept its books on the accrual basis help it, for, however looked at, the liability for maintenance was contingent upon the need of maintenance. When books are kept on an accrual basis a liability must be fixed either in terms or by the occurrence of events from which it is determined before it can be deducted. (*United States v. Anderson and United States v. Yale & Towne Mfg. Co.*, 269 U. S., 422 [T. D. 3839, C. B. V-1, 179]; *United States v. Guinzburg*, 278 Fed., 363 [Ct. D. 23, C. B. I-1, 15].)

We affirm the judgments in these two cases on the reasoning of the learned trial court as it related to the tax question. But in *Vang v. Lewellyn*, the

learned court gave an additional reason for the judgment in that case, to the effect that this personal action against the former collector can not be maintained, as the suit should have been brought against the United States. (*Semple & Co. v. Lewellyn*, 1 Fed. (2d), 745; *Sage v. United States*, 250 U. S., 33.) This question is moot, in view of the court's decision on the other ground and of our affirmance of its decision on that ground.

SECTION 213(a).—GROSS INCOME DEFINED:
INCLUSIONS.

ARTICLE 32: Compensation for personal services.

REVENUE ACT OF 1913.

Income tax paid by employer for employee. (See Ct. D. 80, page 222.)

ARTICLE 32: Compensation for personal services.

VIII-39-4370
I. T. 2496

REVENUE ACT OF 1921.

I. T. 1243 (C. B. I-1, 70), holding that the salary which a Federal judge receives under section 714, Revised Statutes, subsequent to his resignation is income subject to tax, is hereby expressly revoked. (See G. C. M. 6822, page 244.)

ARTICLE 32: Compensation for personal services.

REVENUE ACT OF 1921 AND PRIOR ACTS.

Effect of promulgation of I. T. 2202 (C. B. IV-2, 41) on I. T. 1243 (C. B. I-1, 70). (See G. C. M. 6822, page 244.)

ARTICLE 39: Sale of stock and rights.

REVENUE ACT OF 1921 AND PRIOR ACTS.

Rights to subscribe to bonds. (See I. T. 2494, page 76.)

ARTICLE 48: Improvements by lessees.

VIII-52-4485
T. D. 4280

INCOME TAX.

Article 48 of Regulations 62 amended.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, D. C.

To Collectors of Internal Revenue and Others Concerned:

Article 48 of Regulations 62 is hereby amended to read as follows:

ART. 48. *Improvements by lessees.*—When buildings are erected or improvements made by a lessee in pursuance of an agreement with the lessor, and such

buildings or improvements are not subject to removal by the lessee, the lessor may at his option report the income therefrom upon either of the following bases:

(a) The lessor may report as income at the time when such buildings or improvements are completed the fair market value of such buildings or improvements subject to the lease.

(b) The lessor may spread over the life of the lease the estimated depreciated value of such buildings or improvements at the expiration of the lease and report as income for each year of the lease an aliquot part thereof.

Except in cases where the lessor has exercised the option to report income upon basis (b), if the lease is terminated so that the lessor comes into possession or control of the property prior to the time originally fixed for the expiration of the lease, the lessor derives no income by reason thereof, and, just as when the lessor comes into possession or control of the property upon the expiration of the lease, the basis for determining gain or loss to the lessor from the subsequent sale or other disposition of the buildings or improvements is the amount previously reported as income by the lessor because of the erection of the buildings or improvements, except that if the buildings or improvements were acquired prior to March 1, 1913, the basis shall be their value subject to the lease when acquired or their value subject to the lease on March 1, 1913, as the case may be. See article 1561. If the buildings or improvements are destroyed prior to the expiration of the lease, the lessor is entitled to deduct as a loss for the year when such destruction takes place the amount previously reported as income because of the erection of such buildings or improvements, less any salvage value subject to the lease to the extent that such loss is not compensated for by insurance or otherwise. If the buildings or improvements destroyed were acquired prior to March 1, 1913, the deduction shall be based on their value subject to the lease when acquired or their value subject to the lease on March 1, 1913, whichever is lower, less any salvage value subject to the lease to the extent that such loss is not compensated for by insurance or otherwise. See articles 109 and 164.

In all cases where the lessor has exercised the option to report income upon basis (b), if the lease is terminated so that the lessor comes into possession or control of the property prior to the time originally fixed for the expiration of the lease, the lessor derives additional income for the year in which the lease is so terminated to the extent that the value of such buildings or improvements when he becomes entitled to such possession exceeds the amount already reported as income on account of the erection of such buildings or improvements. No appreciation in value due to causes other than the termination of the lease shall be included. If the buildings or improvements are destroyed prior to the expiration of the lease, the lessor is entitled to deduct as a loss for the year when such destruction takes place the amount previously reported as income because of the erection of such buildings or improvements, less any salvage value subject to the lease to the extent that such loss is not compensated for by insurance or otherwise.

ROBT. H. LUCAS,

Commissioner of Internal Revenue.

Approved December 19, 1929.

OGDEN L. MILLS,

Acting Secretary of the Treasury.

ARTICLE 48: Improvements by lessees.

VIII-52-4486
T. D. 4279

INCOME TAX.

Article 48 of Regulations 45 (1920 edition) amended.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, D. C.

To Collectors of Internal Revenue and Others Concerned:

Article 48 of Regulations 45 (1920 edition), as amended by Treasury Decision 3206 (C. B. 5, 92), is hereby amended to read as follows:

ART. 48. Improvements by lessees.—When buildings are erected or improvements made by a lessee in pursuance of an agreement with the lessor, and such buildings or improvements are not subject to removal by the lessee, the lessor derives income at the time when such buildings or improvements are completed, to the extent of the fair market value of such buildings or improvements subject to the lease. If the lease is terminated so that the lessor comes into possession or control of the property prior to the time originally fixed for the expiration of the lease, the lessor derives no income by reason thereof, and, just as when the lessor comes into possession or control of the property upon the expiration of the lease, the basis for determining gain or loss to the lessor from the subsequent sale or other disposition of the buildings or improvements is the amount previously reported as income by the lessor because of the erection of the buildings or improvements, except that if the buildings or improvements were acquired prior to March 1, 1913, the basis shall be their value subject to the lease when acquired or their value subject to the lease on March 1, 1913, as the case may be. See article 1561. If the buildings or improvements are destroyed prior to the expiration of the lease, the lessor is entitled to deduct as a loss for the year when such destruction takes place the amount previously reported as income because of the erection of such buildings or improvements, less any salvage value subject to the lease to the extent that such loss is not compensated for by insurance or otherwise. If the buildings or improvements destroyed were acquired prior to March 1, 1913, the deduction shall be based on their value subject to the lease when acquired or their value subject to the lease on March 1, 1913, whichever is lower, less any salvage value subject to the lease to the extent that such loss is not compensated for by insurance or otherwise. See articles 109 and 164.

ROBT. H. LUCAS,

Commissioner of Internal Revenue.

Approved December 19, 1929.

OGDEN L. MILLS,

Acting Secretary of the Treasury.

SECTION 213(b).—GROSS INCOME DEFINED: EXCLUSIONS.

ARTICLE 88: Compensation of State officers
and employees.

VIII-41-4384
Ct. D. 114

INCOME TAX—REVENUE ACTS OF 1921 AND 1926—DECISION OF COURT.

1. INCOME — EXEMPTION — STATE EMPLOYEE — INDEPENDENT CONTRACTOR.

No exact rule can be laid down to fit every condition of facts in determining whether a person employed by another is a mere employee or is an independent contractor. The test generally stated is whether power is reserved not only to direct what shall be done but how it shall be done, an independent contractor not being subject to control by the employer except as to the result of the work.

2. SAME—STATE INSTRUMENTALITY.

Where under a cost-plus construction contract with a State the contractor has no regular employment and may accept concurrent employment, has no engagement for any specific period of time, has no working hours, receives no salary or wages, may not have his employment terminated except upon failure properly to perform his contract and then only upon certificate of such failure by the architect, can demand arbitration in certain cases, can demand damages for delays and is liable for damages caused by delay, employs his own men, pays them, selects the material used and pays for it, the status of such a contractor is that of an independent contractor and not that of a State employee whose compensation for personal service as such employee is exempt from income tax by virtue of section

1211 of the Revenue Act of 1926. A provision as to the right of the architect by order of the owner to order suspension of the work at any time he might desire does not amount to the retention of control as to the means or method by which the work should be carried out and is not sufficient to destroy the independent character of the contractor. Neither is the contractor exempt from Federal tax as an instrumentality of the State nor is the imposition of a tax upon the income from such a contract invalid on the ground that its amount impairs the efficiency or operation of the State government.

3. DECISION AFFIRMED.

The decision of the United State Board of Tax Appeals (7 B. T. A., 777) is affirmed.

UNITED STATES CIRCUIT COURT OF APPEALS, EIGHTH CIRCUIT.

A. C. Kreipke v. Commissioner of Internal Revenue.

On petition to review decision of the United States Board of Tax Appeals.

[April 19, 1929.]

OPINION.

KENYON, Circuit Judge, delivered the opinion of the court:

This is an appeal from a decision of the United States Board of Tax Appeals holding that the profits derived by appellant under certain construction contracts made with the State of Oklahoma were not exempt from Federal income taxes.

From 1919 to 1922 appellant was a member of a partnership known as Kreipke-Schafer Co., which partnership entered into eight contracts with the State of Oklahoma for the erection or repair of certain buildings and repairs to other property of the State. These projects and the profits derived therefrom were as follows:

Description.	Amount of profit.
Enid Dam-----	\$4,541.36
Goodwill Science Hall-----	2,552.85
Livingston School Building-----	2,784.71
Repairs—State Capitol Building-----	73.68
Pauls Valley Training School-----	5,024.71
Stillwater School Building-----	15,283.25
Tonkawa Wilkin Hall-----	390.04
Warehouse—Adjutant general-----	4,004.37
	34,654.97

Each project was covered by a separate contract, which was executed on the same kind of printed form and designated: "Uniform contract adopted and recommended for general use by the American Institute of Architects and the National Association of Builders." As these contracts will hereinafter be referred to, no detailed description thereof is necessary at this time. The profits therefrom amounted to \$34,654.97, which the Commissioner of Internal Revenue held was taxable income, and a tax of \$5,593.12 was assessed as a deficiency income tax for the year 1922. The case before the Board of Tax Appeals seems to have been tried on the theory either that the profits of the partnership belonged to appellant or that he received the \$34,654.97 from the partnership. As this does not seem to be questioned, we accept the theory on which the case proceeded before the Board of Tax Appeals. It should be stated, however, that appellee does question whether or not such profits were compensation for personal service.

The Revenue Act of 1921 (ch. 136, p. 237, 42 Stat. L.) provides as follows:

"SEC. 213. That for the purposes of this title (except as otherwise provided in section 233) the term 'gross income'—(a) Includes gains, profits, and income derived from salaries, wages, or compensation for personal service * * * of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, * * * or gains or profits and income derived from any source whatever."

This statute is broad enough to cover the compensation received by appellant from the State of Oklahoma.

Appellant claims exemption, however, from the tax by virtue of section 1211 of the Revenue Act of 1926 (Title 26, section 1065b, U. S. C. A.), which is as follows:

"1065b. Salaries of State and municipal officers; abatement, credit or refund of taxes thereon. Any taxes imposed by the Revenue Act of 1924 or prior Revenue Acts upon any individual in respect of amounts received by him as compensation for personal services as an officer or employee of any State or political subdivision thereof (except to the extent that such compensation is paid by the United States Government directly or indirectly), shall, subject to the statutory period of limitations properly applicable thereto, be abated, credited, or refunded."

If appellant was an officer or employee of the State of Oklahoma or a political subdivision thereof, he is exempt from the tax in question. To discuss the question as to whether or not he is an officer of the State under said section would be a waste of time. He was not. (*United States v. Hartwell*, 6 Wall., 385; *United States v. Germaine*, 99 U. S., 508; *Hall v. Wisconsin*, 103 U. S., 5; *Metcalf & Eddy v. Mitchell*, 269 U. S., 514 [T. D. 3824, C. B. V-1, 2181].)

Was he an employee of the State under the terms of section 1065b, supra, or was he an independent contractor?

He had been engaged in the contracting business for some 35 years and was in control of an organization consisting of a graduate structural engineer, a heating and plumbing engineer, an auditor, a bookkeeper, a stenographer, and various superintendents of construction. If appellant was an independent contractor, then he is not within the exemption of the statute relied on. Much has been written on the subject of whether a person employed by another is a mere employee or is an independent contractor. No exact rule can be laid down to fit every condition of facts. Difficult questions arise under the application of any rule to varied circumstances, and fine shades of distinction often are determinative of the question. In *Railroad Co. v. Hanning* (15 Wall., 649, 657), the test is stated to be whether the power is reserved "not only to direct what shall be done, but how it shall be done." In *Singer Manufacturing Co. v. Rahm* (132 U. S., 518, 523), the court says "the relation of master and servant exists whenever the employer retains the right to direct the manner in which the business shall be done, as well as the result to be accomplished, or, in other words, 'not only what shall be done, but how it shall be done.'" The same test is laid down in *Chicago, R. I. & P. Ry. Co. v. Bond* (240 U. S., 449), where a person was held not to be an employee of the company, but an independent contractor, because while the railroad did retain control of what should be done by him, it had no control as to how the work should be done. In *Casement v. Brown* (148 U. S., 615, 622), the court said: "Obviously, the defendants were independent contractors. The plans and specifications were prepared and settled by the railroad companies; the size, form, and place of the piers were determined by them; and the defendants contracted to build piers of the prescribed form and size and at the places fixed. They selected their own servants and employees. Their contract was to produce a specified result. They were to furnish all the material and do all the work, and by the use of that material and the means of that work were to produce the completed structures. The will of the companies was represented only in the result of the work, and not in the means by which it was accomplished." *Metcalf & Eddy v. Mitchell*, supra, is an important and controlling case on the questions here involved. Plaintiffs there, Metcalf & Eddy, were consulting engineers employed to advise States or subdivisions with reference to proposed water supply and sewage disposal systems. They claimed exemption from income taxes by virtue of the same section of the statute as appellant relies on. The court held they were not employees within the meaning of the statute but were independent contractors, pointing out that the performance of their contract involved the use of judgment and discretion on their part; that there was no such right of control by the employer as to differentiate them from independent contractors and make them employees.

A succinct definition of independent contractor is to be found in 14 Ruling Case Law, page 67, as follows: "An independent contractor is one who, exercising an independent employment, contracts to do a piece of work according to his own methods, and without being subject to the control of his employer

except as to the result of his work." (See also *Storm v. Thompson* (Iowa), 170 N. W., 403; *Norton v. Day Coal Co.* (Iowa), 180 N. W., 905; *Petrow & Giannou et al. v. Shewan* (Neb.), 187 N. W., 940; *Jensen v. Barbour* (Mont.), 39 Pac., 906; *Whitney & Starrett Co. v. O'Rourke* (Ill.), 50 N. E., 242.)

Whether appellant is an independent contractor or a mere employee of the State of Oklahoma is to be determined by a construction of the contracts. The contract with relation to Pauls Valley Training School was introduced in evidence as a type of the contracts entered into. It is to be observed that under this contract there was no regular employment of appellant, no engagement for any specific period of time. He was not compelled to devote all his time to the work. There were no working hours. He was not on any pay roll. He did not receive a salary or wages; he could accept concurrent employment; his employment could not be terminated except upon failure to properly perform the contract, and then only upon certificate of such failure by the supervising architect; could demand arbitration in certain cases; could demand damages for delays; was liable for damages caused by delay; employed and paid his own men; selected and paid for the material used. As sustaining its theory that the relationship created was that of employer and employee, appellant contends that under the contract the State and its subdivisions possessed the right to control the manner and means of performance, especially because the contracts were cost-plus contracts; that as the State finally paid all the bills it would naturally exercise supervision of the specific matter creating each bill; that appellant occupied a position identical with a superintendent; that the State could change the plans and could substitute different material, and through its architect suspend the work at any time it deemed advisable; that while ordinarily a bond was required by the State where contracts of this nature were made, appellant gave no bond.

In considering these provisions which are urged to show control on the part of the State inconsistent with the relation of independent contractor, it must be borne in mind that the work was done under written specifications and plans, and the State had the right under the contract through its architect to see that the results provided for by the said written specifications and plans should be reached and the contractual obligations fulfilled. The control reserved to the State architect was merely to see that the obligations of the contract were carried out. It was not a detailed control as to the manner and method of doing the work—it related only to what should be done, not to how it should be done. While the provision as to the right of the architect by order of the owner to order suspension of the work at any time he might desire is broad, we think when taken in connection with all the other provisions of the contract that it does not amount to the retention of control as to the means or method by which the work should be carried out, and is not enough to destroy the independent character of the contractor. The will of the employer was represented by the contractor only as to results and not as to methods. By all proper legal tests the conclusion of the Board of Tax Appeals that appellant was an independent contractor and not an employee of the State was correct.

Another point urged by appellant is that he or his partnership constituted an agency by and through which the government of the State immediately and directly exercised its sovereign powers, and that the taxation provided by the Revenue Act of 1921 is a material and substantial interference with the action of such State agency. Of course, neither the Federal Government nor the State government can tax the means or instrumentalities employed by the other in carrying out its constitutional powers (*Panhandle Oil Co. v. Knox*, 277 U. S., 218), but the mere fact that one has a contract to perform some service to the Federal or State government does not transform him into an instrumentality of government. In *Metcalf & Eddy v. Mitchell* (269 U. S., 514, 522, 523) the court said: "Just what instrumentalities of either a State or the Federal Government are exempt from taxation by the other can not be stated in terms of universal application. But this court has repeatedly held that those agencies through which either government immediately and directly exercises its sovereign powers are immune from the taxing power of the other. * * * When, however, the question is approached from the other end of the scale, it is apparent that not every person who uses his property or derives a profit, in his dealings with the Government, may clothe himself with immunity from taxation on the theory that either he or his property is an instrumentality of government within the meaning of the rule." It would be a far-fetched doctrine to hold that every person, partnership, or corpora-

tion entering into a contract with a State government to do repair work on State buildings or buildings of political subdivisions of the State becomes an instrumentality of the State government and entitled to claim immunity from all Federal taxation.

Appellant and his partnership were independent contractors and in no way instrumentalities or agencies of the State. The cases cited by appellant on this point are not applicable to the situation here presented.

It is further insisted that even if appellant is not an employee or agency of the State, the tax of \$5,593.12 on the profit of \$34,654.97 derived from the contracts would be a "material and substantial" interference with the governmental functions of the State and its political subdivisions, and appellant relies on *Metcalf & Eddy v. Mitchell*, supra, and the statement of the court there, page 523, as follows: "But neither government may destroy the other nor curtail in any substantial manner the exercise of its powers. Hence the limitation upon the taxing power of each, so far as it affects the other, must receive a practical construction which permits both to function with the minimum interference each with the other; and that limitation can not be so varied or extended as seriously to impair either the taxing power of the government imposing the tax * * * or the appropriate exercise of the functions of the government affected by it. * * * Nor are we to be understood as laying down any rule that taxation might not affect agencies of this character in such a manner as directly to interfere with the functions of government and thus be held to be void."

The National Government can not impose such taxes as necessarily interfere in a substantial way with the functions of a State government. The test is not the size of the tax, but the result thereof. The fact that appellant in making the contract did not understand that his income therefrom was subject to the Federal income tax is not sufficient ground on which to base an argument that the tax was a substantial interference with the ability of complainant to carry out the obligations to the State provided in the contracts. The same question was before the Supreme Court in *Metcalf v. Mitchell*, and it said with reference to the particular tax there in question and its relationship to the functions of the State government, "we do not find that it impairs in any substantial manner the ability of plaintiffs in error to discharge their obligations to the State or the ability of a State or its subdivisions to procure the services of private individuals to aid them in their undertakings." That language covers the situation here presented. We fail to see how this tax in any way impairs the efficiency or operation of the State government. We are unable to agree with any of the theories advanced by appellant to exempt him from the tax in question. The judgment of the Board of Tax Appeals is therefore affirmed.

ARTICLE 89: Additional exclusions from gross income under the Revenue Act of 1921.

REVENUE ACT OF 1921.

Amendment of article 89, Regulations 62, to include Greece in the list of countries which satisfy the equivalent exemption requirement of section 213(b)8 of the Revenue Act of 1921. (See T. D. 4269, page 146.)

SECTION 214(a)1.—DEDUCTIONS ALLOWED: BUSINESS EXPENSES.

ARTICLE 101(a): Traveling expenses.

VIII-29-4277
I. T. 2481

REVENUE ACT OF 1921.

The amount expended by the taxpayer, a university professor, for traveling expenses, including meals and lodging, while rendering professional services elsewhere than in the city in which he maintained his home, is deductible in computing net income.

Advice is requested relative to a claim for refund submitted by A by reason of the disallowance of a deduction for traveling expenses in his return for the calendar year 1923.

It appears that the taxpayer was a university professor, maintaining his home in the city of R, who traveled to the city of S, where he spent 56 days in 1923 tutoring; that he was paid 7x dollars for his services; and that he claimed as a deduction in his 1923 return x dollars, the amount of his traveling expenses (including meals and lodging) during his sojourn.

Section 214(a)1 of the Revenue Act of 1921 provides, in part, that in computing net income there shall be allowed as deductions:

* * * traveling expenses (including the entire amount expended for meals and lodging) while away from home in the pursuit of a trade or business.

The term "business" is used in the section of the statute, above quoted, in its broad sense as meaning that which occupies the time, attention, and the labor of men for the purpose of livelihood or profit. As such it manifestly includes the professions. It follows, therefore, that the entire amount expended for railroad fares or other means of transportation and for meals and lodging by a professor while away from home in order to perform services for which compensation is received, may be deducted by the individual in computing his net income for the year in which the expenditure was made. Accordingly, A's claim for refund should be allowed.

ARTICLE 105: Compensation for personal services.

VIII-30-4289
Ct. D. 85

INCOME TAX—REVENUE ACTS OF 1918, 1921, AND 1926—DECISION OF COURT.

1. DEDUCTION—SALARIES—DISTRIBUTIONS—BURDEN OF PROOF.

Amounts alleged to have been expended for salaries are not deductible under section 234(a)1 of the Revenue Acts of 1918 and 1921 unless they are salaries in fact and not divisions or distributions of income to stockholders, and the burden is upon the taxpayer to make proof of such fact.

2. FINDINGS OF FACT—UNITED STATES BOARD OF TAX APPEALS—CONCLUSIVENESS OF FINDINGS.

The finding of the United States Board of Tax Appeals that amounts disallowed as deductions for salaries were paid not as salaries but as distributions to stockholders is one of fact and the finding of the Board on a question of fact will not be examined by a circuit court of appeals beyond ascertaining if there is any evidence to support such finding.

3. DEDUCTION—SALARIES—DISTRIBUTIONS—EVIDENCE.

Where the evidentiary facts are that increases in salaries were based solely upon the amount of stock holdings and were out of all proportion to the character or amount of services rendered and in no wise based upon either, that one of the resolutions of the directors provided for a salary bonus resulting in a lump-sum distribution to the stockholders, that the increases were effective without respect to the net sales of the corporation and were in effect in one of the years involved although those sales were less than the yearly sales for several previous years before the increases were in effect, the evidence affords support for the ultimate fact found by the Board of Tax Appeals that amounts claimed as deductions by the corporation were not paid as salaries but as distributions to stockholders.

4. DECISION AFFIRMED.

The decision of the United States Board of Tax Appeals (6 B. T. A., 1238) is affirmed.

UNITED STATES CIRCUIT COURT OF APPEALS, EIGHTH CIRCUIT.

Twin City Tile & Marble Co. v. Commissioner of Internal Revenue.

On petition to review decision of United States Board of Tax Appeals.

[March 25, 1929.]

OPINION.

STONE, Circuit Judge, delivered the opinion of the court.

This is a petition to review the determination of the Board of Tax Appeals denying certain allowances claimed on account of salaries paid by the petitioner in the years 1919, 1920, and 1921.

This controversy involves the proper construction of section 234(a)1 of the Revenue Acts of 1918 and 1921, which provide that in computing the net income of a corporation there shall be allowed to the corporation certain deductions from its gross income, among which is included "a reasonable allowance for salaries or other compensation for personal services actually rendered."

The essential facts found by the Board of Appeals and treated here as the facts are as follows: Prior to March, 1911, James Taylor, Arne Verlo, Frank Armstrong, F. O. Streed, E. W. Streed, and H. B. Watson were a partnership engaged in procuring and performing contracts for installation of tile and marble work in buildings. In March, 1911, the above individuals formed the corporation, here the petitioner, and became stockholders with various holdings. In 1917, T. G. Hidding became a stockholder. In 1919, Watson sold his common stock, retaining certain preferred stock which bore 7 per cent interest. In 1919, F. A. Streed became a stockholder. All of these stockholders were employed by and devoted their time to the business of petitioner, most of them being officials thereof. From 1911 on, each was paid a salary. Until 1918, the amounts of these salaries were not increased except in two instances, to wit, Taylor's salary was increased from \$1,800 to \$2,100 for the year 1917 and that of F. A. Streed (who was a mere draftsman) was progressively increased from \$1,020 in 1911 to \$1,500 in 1916, which amount continued through 1918, while he was merely an employee and not a stockholder. The net sales of the company amounting to over \$112,000 in 1911, increased in 1912, reached over \$239,000 in 1913, and then gradually dropped to something over \$197,000 in 1917. For the next four years these sales were over \$260,000 for 1918, over \$212,000 for 1919, over \$346,000 for 1920, and over \$585,000 for 1921. August 14, 1918, a resolution was passed authorizing a monthly salary increase to the stockholders equal to 9 per cent of the common stock held by them and dated back to January 1, 1918. Another resolution of May 18, 1920, provided a similar increase of 8½ per cent. Two other resolutions of September 6, 1920, and November 14, 1921, while not prescribing that the increase should be based specifically on stock ownership, yet actually used that as a basis in determining the amounts of increase. In short, the amount of common stock owned by each stockholder was the sole criterion or measure of the four increases of salary. The result of these resolutions was materially to increase all the salaries. For example, salaries for 1917, 1918, 1919, 1920, and 1921 were respectively as follows: F. O. Streed, president, \$2,400, \$3,300, \$3,546, \$7,823.96, and \$9,759.96; James Taylor, vice president, \$2,100, \$3,000, \$3,402, \$8,313.94, and \$10,505.04; T. G. Hidding, secretary-treasurer, \$750, \$2,286, \$2,611, \$6,070.04, and \$9,127.50; Frank Armstrong, superintendent, \$1,602.95, \$2,560, \$2,505.60, \$6,298.08, and \$7,746.58; Arne Verlo, superintendent, \$1,751.04, \$2,666.66, \$2,707.21, \$6,480.08, and \$8,150.58; E. W. Streed, superintendent, \$1,731.18, \$2,631.18, \$2,492.82, \$6,168.66, and \$7,966.58.

The petitioner claimed that all of these amounts so paid were salaries and properly deductible under section 234 above. The Commissioner made reductions in each salary aggregating about 25 per cent in 1919, more than 50 per cent in 1920, and about 70 per cent in 1921. The amounts so disallowed form the basis of the tax here involved and the controversy is as to the propriety of the disallowances. The petitioner claims that the compensations allowed by the

petitioner were salaries within the meaning of the Act; that they were reasonable in amount; that the Board has refused to make a finding upon the reasonableness thereof and, therefore, contends that the disallowances were improper. The opposed contentions of the Government are that the statute requires that sums claimed as deductions on account of salaries be such, in fact, and not disguised divisions or distributions of income to stockholders; that the burden is upon the taxpayer to make proof of such fact; that the finding of the Board that the sums disallowed were paid not as salaries but as distributions to stockholders is a question of fact and that such finding of fact by the Board will not be disturbed by this court if there is any evidence to support it.

We think the position of the Government is correct. Of course, a corporation may pay its stockholders, who are also officers or employees, such compensation for their services as it may see fit. However, the question here is not as to the power of the corporation but is solely as to the deductions from taxable income of a corporation permitted by section 234. It is entirely possible to distribute profits to stockholders who are employees or officers under the guise of salaries and to permit such to be done would be to defeat the statute. Therefore, it is open to inquiry whether the payment claimed by the taxpayer as a deductible salary is, in fact, such or is, in whole or part, merely a distribution of profits to stockholders (*Botany Worsted Mills v. United States*, 278 U. S., 282, decided by Supreme Court on January 2, 1929 [Ct. D. 39, C. B. VIII-1, 279]), and the burden is upon the taxpayer to establish his right to such a deduction which has been denied by the Commissioner. (*Botany Worsted Mills v. United States*, supra.) Whether such payments are true salaries or are disguised distributions is a matter purely of fact. The determination by the Board of a pure question of fact will not be examined by this court beyond ascertaining if there is any evidence to support such finding. (*St. Paul Abstract Co. v. Commissioner*, decided March 25, 1929, this court; *Feeders' Supply Co. v. Commissioner*, 31 F. (2d), 274, decided February 20, 1929, this court; *Denver Live Stock Comm. Co. v. Commissioner*, 29 Fed. (2d), 543, 544, this court; *Kendrick Coal & Dock Co. v. Commissioner*, 29 Fed. (2d), 559, 563, this court.) In this case there is not only some evidence but very substantial evidence to sustain the finding that these increases were disguised distributions made to avoid the heavy corporation taxes which became effective in 1918. Some of this evidence is as follows: The increases were based solely upon the amount of common stock holdings and out of all proportion and in no wise based upon the character or amount of services rendered; the increases were effective without respect to the net sales of the company, although in 1919 those sales dropped below the sales for any of the years 1913-1916, inclusive; the resolution of November 14, 1921, took the form of a salary bonus resulting in a lump distribution to the seven stockholders of more than \$25,000.

Objection is made that there was no specific finding of fact as to what were reasonable salaries for the services rendered by those to whom these payments were made. The question here really is not concerned with what is a reasonable salary. The evidence shows a distribution of dividends under the guise of salaries. The Commissioner might well have disallowed the entire amounts on the ground that they were not truly salary payments but were disguised distribution of dividends. Any allowance, by him, of any part of such payments was a concession which, under the evidence, he might well have omitted. Certainly, petitioner can not complain of such action unduly favorable to it. The Board of Tax Appeals well stated the matter as follows:

"The first question to determine is whether the amounts which were disallowed by the respondent as compensation to officers and stock-holding employees were paid by the corporation as compensation for services rendered. If the amounts were in fact distributions of profits as determined by the respondent, they would not be allowed as deductions in determining the petitioner's net income. It may be that if the amounts had been paid as compensation, they would have been allowed as being reasonable. In determining whether the amounts were compensation for services or were distributions of profits, all the facts and circumstances must be considered and not merely the fact that the amounts were reasonable. * * * Conceding for the sake of argument that the services of individuals in this case were fairly worth the amounts they received, this fact alone is not sufficient to constitute the amounts compensation. They must have been intended and paid as such. * * *

"We are of the opinion after a consideration of all of the evidence that the petitioner has not shown that the amounts which were disallowed by the

respondent were in fact compensation for services rendered and not distributions of profits."

The petition for review should be and is dismissed.

ARTICLE 111: When charges deductible.

VIII-27-4265
Ct. D. 77

INCOME TAX—REVENUE ACT OF 1918—DECISION OF COURT.

1. DEDUCTION—CONTINGENT COMPENSATION.

Where a corporation, keeping its books of account on the accrual basis, enters into a contract with certain of its employees to pay each additional compensation for the year 1919 based on a certain percentage of the net profits for the year, subject to the condition that all sums to which the employees might become entitled under the agreement should not be withdrawn for a period of five years, except by authority of the president, but should remain in the business at the risk of the business for that time, and should be subject to pro rata deductions in the event of losses incurred in the business during the 5-year period, it may not deduct from gross income in 1919 the amounts of such compensation credited to the employees in that year.

2. DECISION AFFIRMED.

The decision of the United States Board of Tax Appeals (8 B. T. A., 589) affirmed.

COURT OF APPEALS OF THE DISTRICT OF COLUMBIA. No. 4768.

S. Naitove & Co., Inc., v. Commissioner of Internal Revenue.

Appeal from the Board of Tax Appeals.

[May 6, 1929.]

OPINION.

VAN ORSDER, Associate Justice: Appellant, a New York corporation engaged in buying and selling woolen, silk, and cotton goods, had five employees who constituted the entire buying and selling staff of the business. These employees, dissatisfied with their compensation, threatened to go into business for themselves. To retain them, an agreement was entered into by the appellant and the employees under which they were to participate in the profits of the business. The agreement was expressed in a resolution passed by the board of directors on February 10, 1919, as follows:

"Resolved, That additional compensation for the year 1919 be paid to the following officers and employees of the company in accordance with the practice of the company on the following basis:

"Mr. Moe Naitove, 10 per cent of the net profits for the year 1919;

"Mr. Nat Naitove, 10 per cent of the net profits for the year 1919;

"Mr. Jack Naitove, 10 per cent of the net profits for the year 1919;

"Mr. Moe Turnan, 5 per cent of the net profits for the year 1919;

"Mr. George Naitove, 5 per cent of the net profits for the year 1919.

"Provided, however, that any and all sums to which the above-named officers and employees may become entitled under the terms of this resolution shall remain in the business at the risk of the business for a period of five years, and that prior to the expiration of such period said officers and employees shall be entitled to demand and receive payment of the sums to which they may become entitled only to the extent that drawings against such sum may be authorized by the president of the company, it being the intention of this resolution that any and all contingent compensation to which said officers and employees may become entitled under the terms of this resolution be at the

risk of the business in the sense that it shall be subject to pro rata deductions in the event that losses are incurred by the business during the period within which such sums are to remain at the risk of the business; and provided, further, that no officer or employee shall at any time be entitled to withdraw any sums credited to him under the terms of this resolution, except as hereinabove provided, unless he shall remain in the employ of S. Naitove Co., Inc., during the entire period during which the credits mentioned are to remain at the risk of the business, and in the event of the discharge of any such officer or employee or withdrawal during such period, all right, title, or interest of such officer or employee in or to any sums credited to said officer or employee under the terms of this resolution shall revert to this corporation."

Appellant kept its books on an accrual basis of accounting, and, in closing the books of December 31, 1919, the entry as to those five employees was computed as follows:

" Charge, selling and commission-----	\$116,548.44
" Credit Moe Naitove-----	29,137.11
Nat Naitove-----	29,137.11
Jack Naitove-----	29,137.11
George Naitove-----	14,568.56
Moe Turnan-----	14,568.55

additional compensation as per agreement."

The resolution was continued in force during the year 1920 on the same basis as in the year 1919, but in 1920 appellant suffered a loss of approximately \$90,000; and pursuant to the resolution the books as of December 31, 1920, showed, as to the participation by the five employees, the following accruals:

Charge Moe Naitove 10 per cent-----	\$10,441.42
Nat Naitove 10 per cent-----	10,441.42
Jack Naitove 10 per cent-----	10,441.42
George Naitove 5 per cent-----	5,220.71
Moe Turnan 5 per cent-----	5,220.71
Credit surplus account-----	41,765.68

Appellant in its return for the year 1919 deducted as expenses from its income the sum of \$116,548.44, which represented the portion of the earnings which accrued to said employees pursuant to the terms and conditions of the agreement set forth in the resolution by the board of directors. The Commissioner disallowed this deduction, and on August 19, 1925, notified appellant corporation of a deficiency in its income and profits taxes for the calendar year 1919 of \$59,049.33.

From the ruling of the Board of Tax Appeals, sustaining the Commissioner, the case comes here on appeal.

The tax in controversy was imposed under the provisions of the Revenue Act of 1918 (40 Stats., 1057).

"Sec. 212. (b) The net income shall be computed upon the basis of the taxpayer's annual accounting period (fiscal year or calendar year, as the case may be) in accordance with the method of accounting regularly employed in keeping the books of such taxpayer; but if no such method of accounting has been so employed, or if the method employed does not clearly reflect the income the computation shall be made upon such basis and in such manner as in the opinion of the Commissioner does clearly reflect the income.

* * * * *

"Sec. 232. That in the case of a corporation subject to the tax imposed by section 230 the term 'net income' means the gross income as defined in section 233 less the deductions allowed by section 234, and the net income shall be computed on the same basis as is provided in subdivision (b) of section 212 or section 226.

* * * * *

"Sec. 234. (a) That in computing the net income of a corporation subject to the tax imposed by section 230 there shall be allowed as deductions: (1) All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered, and including rentals or other payments required to be made as a condition to the continued

use or possession of property to which the corporation has not taken or is not taking title, or in which it has no equity."

The accounts under the agreement were kept on the books of appellant on an accrual basis, under which system these items of expense could not accrue until all the events occurred from which liability could be determined and become fixed. In pursuance of this system appellant credited on its books as of December 31, 1919, to its five employees \$116,548.44. This represented the portion of appellant's earnings for that year to which the employees would be entitled, in the event the credits equaled or exceeded that amount during the remaining four years. But in 1920 the credits to the employees dropped to \$41,765.68, thus demonstrating the total impossibility of determining until the expiration of the 5-year period the amount of expense appellant would be entitled to deduct for compensation paid these employees.

Construing the provisions of the income tax law here involved, we are of the opinion that under the accrual system of accounting income may be said to be accrued when it is definitely received, and that likewise liabilities or expenses will be considered to have accrued only when the events have occurred from which liability or expense can be determined and fixed, even though payment is not yet due. This principle was involved in *United States v. Anderson et al.* (269 U. S., 422 [T. D. 3839, C. B. V-1, 179]). In that case it appeared that the Yale & Towne Manufacturing Co. was in 1916 engaged in the manufacture of munitions. The tax was imposed upon the profits on the munitions manufactured and sold during that year, but which became due and was paid in 1917. In making its return for the year 1917, the company deducted from its income the munitions tax thus paid. The Commissioner of Internal Revenue held that the tax paid in 1917 should have been deducted from appellee's gross income in its return for 1916. The books of the company were kept under the accrual system. The court, in disposing of this case, said:

"Only a word need be said with reference to the contention that the tax upon munitions manufactured and sold in 1916 did not accrue until 1917. In a technical legal sense it may be argued that a tax does not accrue until it has been assessed and becomes due; but it is also true that in advance of the assessment of a tax, all the events may occur which fix the amount of the tax and determine the liability of the taxpayer to pay it. In this respect, for purposes of accounting and of ascertaining true income for a given accounting period, the munitions tax here in question did not stand on any different footing than other accrued expenses appearing on appellee's books. In the economic and bookkeeping sense with which the statute and Treasury decision were concerned, the taxes had accrued. * * *

It will be observed that this case turned upon the fact that on the books of the company the munitions profits had accrued in 1916, though not payable until 1917. We think, however, that in the present case, where the facts establish a situation exactly the converse, that the opinion is decisive in that it implies that if the profits had not become fixed and determined in 1916, though not payable until a later date, they would not have been subject to taxation until such time as the profits had accrued and become fixed and determined.

To the same effect is *American National Co., Receiver, v. United States* (274 U. S., 99 [T. D. 4099, C. B. VI-2, 193]), where the corporation was engaged in the business of making and selling loans on 5-year notes and mortgages. It derived its income from commissions in the form of 2-year notes made by the borrowers, and in selling loan notes to investors in which it agreed, as an inducement, to pay them on loans sold, bonuses of a specified per cent yearly during the life of the loans. It was held that, under section 13(d) of the Revenue Act of 1916, and regulations of the Treasury pursuant thereto, according to the method of accounting, that inasmuch as the aggregate of the commission notes and the accrued bonus contracts made during the year became fixed and determined, though not due and payable, they properly could be deducted from the gross commissions for the ascertainment of taxable income.

But it will be observed that in this case, as in the *Anderson* case, the amount deductible was fixed and determined, which distinguishes these cases from the case at bar. The resolution in the present case amounts to nothing more than an offer to pay additional compensation to certain employees under a conditional contract which could only mature into an obligation and become binding upon appellant company on complete performance by its employees of the acts called for therein, and which could not be ascertained until the expiration of the 5-year period fixed by the agreement.

In the case of *Edwards v. Keith* (231 Fed., 110 (certiorari denied, 243 U. S., 638)) the question involved was whether income had accrued on a contract with a life insurance agent under which he sold policies on which he was to receive a percentage of each annual renewal payment when the same was paid by the insured. It was contended by the plaintiff that the entire income from this source accrued at the time the policy was sold. The court, rejecting this theory, said:

"If an agent for a life insurance company does a particular job, e. g., persuades John Doe to insure in the company on July 1, 1915, and receives as part compensation for that work a certain sum when Doe pays his first premium in July, 1915, surely he includes that in his income return for 1915. That certainly is income. If under this arrangement with the company he receives a further sum of money as compensation for the same job in July, 1916, when John Doe pays his second premium, we can not see why that is not income for 1916—in the ordinary sense of the word. Why it is not within the language of the Act 'income arising or accruing in the calendar year 1916' and 'derived from personal services' we are entirely at a loss to understand. The statute does not provide that the 'personal services,' compensation for which is to be considered income, must be rendered in the same year in which the compensation is received. It may be noted that, although fully earned by work already done, there is no certainty that the sum conditionally promised for an ensuing year will ever be paid or will accrue or come due; John Doe may die within the first year, or at its expiration may refuse to renew his policy, in which event the company is not obligated to pay its agent anything beyond the amount already paid him; the obligation to pay does not arise until John Doe actually pays his renewal premium in cash."

The decision of the court in the above case is conclusive, we think, to the effect that in a unilateral or conditional contract, as the one here involved, the liability incurred is not to be deducted as expense until it has become fixed and determined, and it is then deductible as of the year when that event occurs; in the instant case, at the expiration of the 5-year period.

Closely analogous to the present case is *United States v. Block & Kohner Mercantile Co., a corporation*, decided in the United States District Court for the Eastern District of Missouri on January 10, 1929. In that case defendant corporation on February 1, 1919, made a contract with one Weinbach and wife in which Weinbach agreed to work for the company on a salary of \$4,800 per annum, payable monthly. In addition he was to receive one-third of the net profits of defendant's business during the life of the contract. If net losses resulted from the business, one-third of such losses were to be deducted from a \$5,000 fund deposited by the wife for this purpose. One-third of the profits for the year 1919 amounted to \$5,193.27, which was credited on the books of the company to Weinbach, but the losses for 1920 and 1921 exceeded the profits for 1919, leaving nothing due Weinbach at the termination of the contract.

The company sought to deduct from its income for 1919 as expense the amount credited that year to Weinbach. The court, holding that this could not be done, said: "The defendant's books, at the end of the year 1919, reflected this credit to Weinbach. It did not represent the sum due the salesman at that time. It represented a sum that would become due the salesman for the year 1919, provided the business continued to show a profit for each of the subsequent years of the life of the contract. If the business had shown a loss for either year of 1920 or 1921, then the above share of the profits credited to Weinbach would have been reduced by his share of the loss. This is what actually occurred. The business did show a loss during both of these subsequent years, so that the defendant actually never became liable to the salesman for any amount of profits. * * * Under the facts of this case it can not be said that the defendant incurred this item of expense for the year 1919. The defendant was not entitled to deduct this amount from its gross income for that year. This view is sustained by *United States v. Anderson* (269 U. S., 422), *Edwards v. Keith* (231 Fed., 110), *Holmes Federal Taxes* (6th ed.), page 1248."

It will be observed that under the contract as set forth in the resolution all sums to which the employees might become entitled during the period of five years should remain in the business, and should be subject to pro rata deductions in the event of losses incurred in the business during the 5-year period. Appellant paid out nothing. It took nothing from its business. The entry on the books represented only a possible future liability. In other words, the profits and losses credited and charged to the account of each of the employees

should be accounted at the end of the 5-year period, and if the credits exceed the losses the excess would represent the amount to which the employee would be entitled. On the other hand, if the losses exceeded the credits, the employee would be entitled to nothing. It follows that the events which were to determine and fix appellant's liability to its employees could not occur until the expiration of five years; and, by the terms of the agreement, if an employee was discharged or left the employ during the period of five years, he should take nothing under the agreement, whether the credits were in his favor or not. It follows, therefore, that the events which were to determine and fix appellant's liability did not occur in the year 1919, and could not occur so as to admit of a final determination until the end of the 5-year period, at which time the definitely fixed and accrued expense could be deducted and credit taken on its tax in the current year.

The decision of the Board of Tax Appeals is affirmed with costs.

ARTICLE 111: When charges deductible.

VIII-32-4305
Ct. D. 90

INCOME TAX—REVENUE ACT OF 1918—DECISION OF COURT.

DEDUCTION—CONTINGENT COMPENSATION.

Where a taxpayer, keeping its books of account on the accrual basis, enters into a contract with an employee to pay him in addition to a fixed salary a percentage of the profits of the business over a period of three years, to be reduced by a percentage of any losses that might result from the operation of the business during the period, the contract providing for an accounting of the profits and losses at its termination, the taxpayer may not deduct from gross income, as a business expense, for the first year of the contract the amount of the profits credited to the employee at the end of that year.

UNITED STATES DISTRICT COURT FOR THE EASTERN DIVISION OF THE EASTERN
JUDICIAL DISTRICT OF MISSOURI.

*United States of America, plaintiff, v. Block & Kohner Mercantile Co., a
Corporation, defendant.*

[January 10, 1929.]

OPINION.

DAVIS, District Judge: This is an action to recover the sum of \$1,691.94, with interest, income and profit taxes alleged to be due from the defendant for the calendar year of 1919. The parties have waived a jury and filed an agreed statement of facts.

The defendant, on February 1, 1919, entered into a written contract with one Jake Weinbach and wife, in which it was agreed that Weinbach would enter the employ of the defendant at a salary of \$4,800 a year, payable monthly. It was further agreed that Weinbach's wife was to deposit \$5,000 with the defendant, and that in addition to the salary one-third of the net profits realized by the defendant during the continuance of the contract should be paid to Weinbach and his wife. The term of the contract was three years, unless the parties mutually agreed to terminate it sooner, or one of the parties gave six months' notice to the other of his intention to terminate it. It was also provided that if net losses resulted from the operation of the business during the period of the contract, one-third of any such losses should be deducted by the defendant from the \$5,000 deposited with it.

Weinbach entered into the employ of the defendant on February 1, 1919, under the terms of the contract, and worked continuously until May 17, 1921, when, because of the losses sustained in the business, the contract was terminated by mutual agreement of the parties. One-third of the net profits of the defendant from February 1, 1919, to December 31, 1919, amounted to \$5,193.27. The defendant credited this amount on its books to Weinbach as of December

31, 1919, and deducted this amount from its gross income as a deduction for ordinary and necessary expense for carrying on a trade or business. At the end of 1920, one-third of the losses sustained in that year was debited to Weinbach's account, and upon the termination of the contract on May 27, 1921, one-third of the losses for the remaining period, between January 1, 1921, and May 27, 1921, was also debited to Weinbach's account. The losses so debited in 1920 and 1921 were then deducted from the profits, and, as they exceeded the profits realized in 1919, the result was that Weinbach received nothing from the corporation as a share in the profits, while, on the other hand, the amount of \$5,000 deposited as a guarantee to share in the net losses was practically consumed.

The statute involved in this case is the Revenue Act of 1918, section 234:

"SEC. 234. (a) That in computing the net income of a corporation subject to the tax imposed by section 230 there shall be allowed as deductions:

(1) All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered, and including rentals or other payments required to be made as a condition to the continued use or possession of property to which the corporation has not taken or is not taking title, or in which it has no equity."

The question that has arisen is whether or not the defendant corporation was entitled under the above statute to deduct as an ordinary and necessary expense, for the year 1919, the amount of \$5,193.27, credited to the account of Weinbach in that year under the contract to share profits and losses.

The statute provides that a taxpayer in computing its net income shall be allowed to deduct "all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business." So, that the question directly involved is whether the sum of \$5,193.27, credited to the account of the salesman Weinbach was an ordinary and necessary expense incurred during the year of 1919.

The word "incur" means "to become liable or subject to; to bring down upon ones self; as, to incur debt, danger, displeasure, penalty, responsibility, etc."—Webster's New International Dictionary. "Incur" is said to be synonymous with the word "accrue."

Under the terms of the contract set out in the agreed statement of facts, the accounting of profits or losses between Weinbach and the defendant was to be made at the termination of the contract. The contract was terminated by mutual agreement on May 17, 1921, at which time the parties adjusted their accounts and ascertained that losses had been sustained, and Weinbach's part of the said losses were deducted from the deposit which his wife had made with the defendant. However, during the first year of the contract, 1919, the defendant had made a profit and Weinbach's proportion of that profit was \$5,193.27. So, the defendant on its books credited Weinbach's account for the year 1919 with this sum and deducted it as an expense in computing its net income for that year. It did not pay that sum to the defendant during that year, or at any other time. It did not become liable to pay this sum to its salesman because profits or losses were not to be annually adjusted, but to await the end of the whole period of the contract.

The defendant's books, at the end of the year 1919, reflected this credit to Weinbach. It did not represent a sum due the salesman at that time. It represented a sum that would become due the salesman for the year 1919, provided the business continued to show a profit for each of the subsequent years of the life of the contract. If the business had shown a loss for either year of 1920 or 1921, then the above share of the profits credited to Weinbach would have been reduced by his share of the loss. This is what actually occurred. The business did show a loss during both of these subsequent years, so that the defendant actually never became liable to the salesman for any amount of profits.

Reliance is placed on the fact that the defendant kept its books on the accrual basis, that is, by charging against income earned during the taxable period the expenses incurred in the process of earning income during that period, and not upon the basis of actual receipts and disbursement. It is essential under any system of keeping books that before an item can be set up as an expense, that it must represent an actual outlay or an actual obligation to make an outlay. The plaintiff will permit the taxpayer to adopt its own method of keeping books, but whatever the system, the entries are not to be regarded as

conclusive. The taxpayer is required to make a return upon its actual income. In so far as its books reveal the actual condition they are to be accepted, but not otherwise. See section 212 of the Revenue Act of 1918.

Under the facts of this case it can not be said that the defendant incurred this item of expense for the year 1919. The defendant was not entitled to deduct this amount from its gross income for that year. This view is sustained by *United States v. Anderson* (269 U. S., 422 [T. D. 3839, C. B. V-1, 179]), *Edwards v. Keith* (231 Fed., 110), *Holmes Federal Taxes* (6th ed.), page 1248. Judgment for plaintiff.

Tax due-----	\$1, 691. 94
6 per cent interest February 26, 1926, to January 10, 1929-----	291. 80
	1, 983. 74

ARTICLE 111: When charges deductible.

VIII-42-4394
Ct. D. 117

INCOME TAX—REVENUE ACT OF 1916—DECISION OF COURT.

DEDUCTION—REBATES.

Where a manufacturer, keeping its books on the accrual basis, in 1917 sells and delivers goods and receives the invoiced prices therefor with the understanding that the purchasers will be insured against loss from declines in market price, and in 1918 the manufacturer is required to make payments to purchasers on account of such declines in 1918, an amount so refunded in the year 1918 did not accrue as a liability in the year 1917 and is not deductible from gross income in 1917.

UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT. No. 3989.

Highland Milk Condensing Co., appellant, v. D. W. Phillips, Collector, appellee.

Before BUFFINGTON and WOOLLEY, Circuit Judges, and FAKE, District Judge.

[September 10, 1929.]

OPINION.

BUFFINGTON, J.: In the court below the Highland Milk Condensing Co. brought suit against the collector to recover income tax alleged to have been wrongfully assessed and collected under protest. By stipulation jury trial was waived and the case tried by a judge. In his finding of facts and opinion the whole matter is stated in detail and need not be here related, as the question involved narrows itself to this: Where a manufacturer sells and delivers goods and receives the invoiced prices therefor, with the understanding that the purchasers will be insured against loss from declines in market price, and in a subsequent year the manufacturer is required to make payments to purchasers on account of such declines, do such payments represent deductible losses for the year in which they are made? On this question the conclusion of the court was:

"First: The sum of \$43,402.20, credited and refunded by plaintiff to jobbers on account of declines in the price of evaporated milk in the year 1918, did not accrue as a liability until 1918, and, therefore, is not deductible from plaintiff's gross income for the year 1917.

"Second: The Federal income and profits tax assessed against and paid by the plaintiff for the year 1917 was properly and legally assessed and paid.

"Third: Judgment must, therefore, be entered in favor of the defendant."

And in addition:

"It is clear that the sum of \$43,402.20, refunded by the plaintiff to jobbers on account of declines in the price of evaporated milk in the year 1918, did not accrue as a liability in the year 1917, but in the year 1918, and, therefore, is not deductible from plaintiff's gross income for the year 1917.

"The court's opinion and the conclusions of law herein are clearly supported by the following authorities: Appeal of Helvetia Milk Condensing Co., United

States Board of Tax Appeals, volume 5, November 5, 1926, No. 4, page 271; *Ed. Schuster & Co., Inc., v. Williams, Internal Tax Collector* (283 Fed., 115)." (2 Am. Fed. Tax Rep., 1768.)

We find no error in the court's so holding. The crucial questions were: What was the income the taxpayer received during the year 1917? Was there anything during that year which lessened such 1917 income? To these questions there could be no other answers than those embodied in the court's judgment. What happened in the following year could not affect the status of the tax year 1917. We think this conclusion is in line with the taxing principles enforced in *Lewellyn v. Electric* (275 U. S., 243), and afterwards followed in *Ithaca v. United States* (279 U. S., 151 [Ct. D. 61, C. B. VIII-1, 313]).

ARTICLE 111: When charges deductible.

REVENUE ACT OF 1921.

Amounts paid following a judicial determination that they were expenses due for former years. (See Ct. D. 130, page 246.)

SECTION 214(a)3.—DEDUCTIONS ALLOWED: TAXES.

ARTICLE 132: Federal duties and excise taxes.

REVENUE ACTS OF 1918 AND 1921.

Amended returns claiming as deductions duties which originally were added to cost of merchandise on which duties were paid. (See Ct. D. 129, page 247.)

SECTION 214(a)8.—DEDUCTIONS ALLOWED: DEPRECIATION.

ARTICLE 161: Depreciation.

(Also Section 326, Article 831; Section 327,
Article 901.)

VIII-47-4438

Ct. D. 131

INCOME AND EXCESS PROFITS TAXES—REVENUE ACT OF 1918—DECISION OF COURT.

1. DEDUCTION—EXHAUSTION OF CONTRACT.

Where the United States negotiates with a person for the erection of a plant suitable for the manufacture of guns and agrees that an order will be placed with him for a certain number at a fixed profit, and he turns over to a corporation as consideration for its capital stock his rights under the negotiations, which represent no expense to him of which there is definite evidence, there is no cost basis for an allowance of a deduction, under section 234(a)7 of the Revenue Act of 1918, for the exhaustion of the contract for the manufacture of the guns which the corporation and the United States entered into after the corporation had been organized and the stock issued.

2. INVESTED CAPITAL.

Where rights under negotiations for a contract that represent no capital investment are transferred to a corporation in exchange for its capital stock, the corporation as a result of the transfer has no invested capital at the time of organization under section 331 of the Revenue Act of 1918.

8. INVESTED CAPITAL—SPECIAL ASSESSMENT—NO INVESTED CAPITAL.

A corporation without invested capital is not a case, within the purview of section 327(a) of the Revenue Act of 1918, "where the Commissioner is unable to determine the invested capital as provided in section 326," and the absence of invested capital does not, therefore, entitle it to a special assessment under section 328.

4. INVESTED CAPITAL—SPECIAL ASSESSMENT—COST-PLUS CONTRACT.

Where a contract with the Government provides for the payment of the entire cost of producing guns plus a fixed and not a percentage profit for each gun manufactured and delivered, the income therefrom is derived on a cost-plus basis within the meaning of section 327(d) of the revenue Act of 1918, and the corporation whose entire income is derived from such contract is not entitled to a special assessment under that subdivision.

5. DECISION AFFIRMED.

The decision of the United States Board of Tax Appeals (8 B. T. A., 132) affirmed.

COURT OF APPEALS OF THE DISTRICT OF COLUMBIA. No. 4766.

Symington-Anderson Co. v. Commissioner of Internal Revenue.

Appeal from the Board of Tax Appeals.

[June 3, 1929.]

OPINION.

VAN ORSDEL, Associate Justice: This appeal is from the decision of the Board of Tax Appeals affirming the finding of the Commissioner of Internal Revenue assessing a deficiency tax against appellant company for the year 1918, in the amount of \$76,174.96.

It appears that early in 1917, after the declaration of war between the United States and Germany, one T. H. Symington, a recognized authority in the manufacture of guns and munitions, was summoned to Washington for the purpose of negotiating a contract for the manufacture of three thousand 3-inch artillery guns. The negotiations extended for several months, during which Symington made repeated trips to Washington at considerable time and expense. A rather voluminous correspondence is set out in the record, which resulted in an agreement that Symington should erect a plant suitable for the manufacture of guns; and that an order would be placed with him for three thousand 3-inch artillery guns, to be completed by March 1, 1919.

Under the agreement Symington was to receive a fixed profit of \$390 over and above the estimated cost of \$2,625 on each gun manufactured. It was also stipulated that for any saving affected under the estimated cost price, Symington was to receive one-third of such saving. If, however, the cost of each gun was greater than the estimated amount, the minimum amount which Symington was to receive was fixed at \$340 for each gun manufactured. In the contract it was stipulated for adjustments in case of loss and partially completed materials.

In August, 1917, Symington, with the approval of the Government, organized appellant corporation. In consideration of his assignment to it of his contract and agreement with the Government he received 7,500 shares of the capital stock of the corporation. The remaining 2,500 shares was issued to M. H. Anderson, in consideration for services he rendered in preparing for the construction of the plant and organizing the work prior to the incorporation. Anderson was an expert in manufacturing ability, and it is alleged that his future services were an element entering into the consideration for the issue of the stock to him.

During the year 1918, 687 guns were manufactured and delivered on the contract, on which it was found that the corporation realized a net income of \$324,874.85 and a tax liability thereon of \$257,864.88. The Commissioner held that appellant company was not entitled to any allowance or deduction for exhaustion or depreciation of the contract acquired from Symington, and that the taxpayer's only source of income was from the manufacture of guns under the provisions of the contract.

The Board of Tax Appeals, approving the ruling of the Commissioner, held that the contract had no market value for the purpose of depreciation, and that petitioner's invested capital was nonexistent and tax thereon could not be determined under the provisions of section 328 of the Revenue Act of 1918 (40 Stat., 1058).

It will be observed that what Symington in fact turned over to the corporation for 7,500 shares of nonpar value stock was an agreement with the Government for a contract which materialized on August 31, 1917, after the corporation had been organized and the stock issued. We deem it unnecessary in disposing of this case to decide whether the correspondence and negotiations between Symington and the Government, prior to the organization of the corporation, amounted to an enforceable contract or not, since in any event the corporation is not in position to avail itself of the relief here sought.

The assets, if they may be denominated as such, which Symington and Anderson turned over to the corporation as consideration for the stock, did not establish such a basis of capital as would permit the corporation to avail itself of allowance for exhaustion under section 234(a)7 of the Revenue Act of 1918. The annual deduction, permitted under this provision of the Act, is based upon the cost of the exhaustible assets, on the theory that the corporation is entitled to set aside each year, as exempt from taxation, that portion of the assets used up or exhausted in the trade or business during the year, so that at the end of its useful life the aggregate of the sums deducted equal the original cost.

The difficulty in the present case is that the contract, assuming it to be such, possessed no actual cost value. It represented no capital investment. At the time of its assignment to the corporation it amounted to nothing more than a paper agreement for a contract. This, we think, can not be considered as invested capital or as equivalent to actual cash value of tangible or intangible property exchanged for stock or shares. Indeed, it is significant that as late as March 13, 1924, appellant corporation, through its assistant secretary and treasurer, advised the Commissioner of Internal Revenue as follows: "The Symington-Anderson Co. does hereby agree that the sum of \$324,874.85 is a proper net income for the year 1918, and further agrees that within the meaning of the Revenue Act of 1918 the said company had no invested capital whatsoever."

But it is insisted that Symington had incurred expenses in conducting the negotiations which preceded the organization of the corporation, and that such expenses at least entered into the cost of the contract, and as such should be regarded as a capital charge; but these items seem to have been too uncertain and indefinite for the basis of any claim, since Symington in his testimony referred to them as follows: "To a very small extent I paid these obligations. I paid the preliminary expenses myself but I can not state to what extent." Thus there was no tangible proof upon which a finding as to the amount of the expenses could be determined. These items of expense, if proved, would constitute the only assets available to appellant within the limitations of section 331 of the Revenue Act, which provides as follows:

"In the case of the reorganization, consolidation, or change of ownership of a trade or business, or change of ownership of property, after March 3, 1917, if an interest or control in such trade or business or property of 50 per centum or more remains in the same persons, or any of them, then no asset transferred or received from the previous owner shall, for the purpose of determining invested capital, be allowed a greater value than would have been allowed under this title in computing the invested capital of such previous owner if such asset had not been so transferred or received: *Provided*, That if such previous owner was not a corporation, then the value of any asset so transferred or received shall be taken at its cost of acquisition (at the date when acquired by such previous owner) with proper allowance for depreciation, impairment, betterment or development, but no addition to the original cost shall be made for any charge or expenditure deducted as expense or otherwise on or after March 1, 1913, in computing the net income of such previous owner for purposes of taxation."

Measured by this provision of the statute, all that Symington conveyed to the corporation which can be regarded as invested capital was the actual expense he had incurred in securing this agreement for a contract. To this expense the statute limits the value of the invested capital when, as here, more

than 50 per centum of the stock remains in Symington, the previous owner, in lieu of the agreement transferred.

A more insurmountable objection to the right of appellant's claim is presented in section 327 of the Revenue Act. It is claimed that appellant comes within subdivision (a), which provides in substance that where the Commissioner is unable to determine the invested capital as provided in section 326, the tax shall be determined under section 328 by comparison "with representative corporations whose invested capital can be satisfactorily determined under section 326 and which are, as nearly as may be, similarly circumstanced with respect to gross income, net income, profits per unit of business transacted and capital employed, the amount and rate of war profits or excess profits, and all other relevant facts and circumstances." Before, however, the right of comparison can be invoked there must be an existing invested capital capable of calling for the exercise of this discretion on the part of the Commissioner. As we have observed, the rights acquired from Symington had no value as invested capital, since the amount of their cost to him is limited to certain indefinite expenses not established.

Nor can appellant, through the medium of subdivision (d) of section 327, invoke the discretionary relief afforded in section 328, since its income for the taxable year consisted of profits derived on a cost-plus basis from a Government contract. The contract in this case called for a certain number of guns to be manufactured and delivered, for which appellant was to be paid the entire cost of producing the guns, plus a fixed profit for each gun so manufactured and delivered. We are of the opinion that this constituted a cost-plus contract, and for that reason alone appellant can not prevail.

The decision of the Board of Tax Appeals is affirmed with costs.

ARTICLE 161: Depreciation.

VIII-51-4473
Ct. D. 139

INCOME TAX—REVENUE ACTS OF 1916 AND 1918—DECISION OF COURT.

(1) DEDUCTION—DEPRECIATION—LESSEE—LEASE EXECUTED BEFORE MARCH 1, 1913.

A lessee of a building under a 99-year lease, having no capital investment therein, is not entitled to a deduction for its depreciation, even though the lease was executed before March 1, 1913.

(2) DECISION FOLLOWED.

The decision of the Supreme Court of the United States in the case of *Weiss v. Wiener* (279 U. S., 333 [Ct. D. 60, C. B. VIII-1, 257]) followed.

UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

The Brevoort Hotel Co., appellant, v. Mabel G. Reinecke, as Collector of Internal Revenue for the First District of Illinois, appellee.

Appeal from the District Court of the United States for the Northern District of Illinois, Eastern Division.

[November 26, 1929.]

OPINION.

EVANS, C. J.: Appellant brought this suit to recover income taxes by him paid under protest.

The facts are free from dispute. Appellant leased for a period of 99 years property situated in Chicago and commonly known as the Brevoort Hotel. The lease provided for the annual payment of \$60,000 as rent. Appellant claimed the right to deduct certain sums for depreciation of the building covered by the lease. Its claim was disallowed by the United States internal revenue collector. Thereafter appellant paid its tax and brought this suit to recover the amount paid under protest and which sum represented the difference between the amount paid and the amount that it would have been required to pay had its claim for depreciation been allowed.

The question presented here was settled by the recently decided case of *Weiss v. Wiener* (279 U. S., 333). In that case the court said:

"The diminution in the value of a mine to the lessee is conspicuous, necessary, and intended, and is the very source of the gross income of the lessee from which it is deducted, whereas the wear and tear of a house or shop in any given year may be only recognizable by theory and, as has happened in this case, may cost the lessee nothing while the premises are in his hands."

Counsel seeks to distinguish the instant case from the *Weiss* case in that the lease under consideration was executed prior to March 1, 1913, while the lease in the *Weiss* case was executed subsequent to that date. We fail to see any pertinency in this distinguishing fact.

The decree is affirmed.

ARTICLE 162: Depreciable property.

VIII-34-4322

Ct. D. 94

INCOME TAX—REVENUE ACT OF 1918—DECISION OF COURT.

1. DEDUCTION — DEPRECIATION — WATERWORKS — ITEMS OF VALUE ELIMINATED.

Amounts representing preliminary cost, miscellaneous inventories, engineering and supervision, administrative costs, contingent costs, and lost interest during construction are not a part of the value of waterworks properties for the purpose of computing allowances for exhaustion, wear and tear, and obsolescence, the deduction under section 234(a)7 of the Revenue Act of 1918 being limited to property subject, in fact, to depreciation.

2. DECISION AFFIRMED.

The decision of the United States Board of Tax Appeals (5 B. T. A., 1067) is affirmed.

COURT OF APPEALS OF THE DISTRICT OF COLUMBIA. No. 4778.

Paducah Water Co. v. Commissioner of Internal Revenue.

Appeal from a decision of the Board of Tax Appeals involving income and profit taxes for the calendar years 1919, 1920, and 1921.

[June 3, 1929.]

OPINION.

ROBB, Associate Justice: The sole issue here is whether the Board erred in holding that the basis for the determination of depreciation allowances for the taxable years on waterworks properties owned by appellant on March 1, 1913, was the remainder of the total fair market value of the property as of that date, after subtracting from such total value sums representing the following items: Preliminary cost; miscellaneous inventories; engineering and supervision; administrative costs; contingent costs; lost interest during construction; the Board having found this remainder to be the value of appellant's properties subject to exhaustion, wear and tear, and obsolescence.

Section 234(a)7 of the Revenue Act of 1918 (40 Stat., 1057, 1077, 1078) provides:

"That in computing the net income of a corporation subject to the tax imposed by section 230 there shall be allowed as deductions: * * * A reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence."

Section 234(a)7 of the Revenue Act of 1921 (42 Stat., 227, 254, 255) provides:

"That in computing the net income of a corporation subject to the tax imposed by section 230 there shall be allowed as deductions: * * * A reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence. In the case of such property acquired before March 1, 1913, this deduction shall be

computed upon the basis of its fair market price or value as of March 1, 1913."

Appellant insists that the "fair market value" of the property for the purpose of computing "exhaustion, wear and tear" and obsolescence is the same as the fair market value for computing profits on a sale and includes every element of value in the property. The Treasury Department, on the other hand, has construed section 234(a)7 as limiting depreciation allowances to depreciable property, and excluded assets not of that character. Article 162 of Treasury Regulations 45, Revenue Act of 1918, in part provides: "The necessity for a depreciation allowance arises from the fact that certain property used in the business gradually approaches a point where its usefulness is exhausted. The allowance should be confined to property of this nature." This contemporaneous construction of section 234(a)7 of the Act of 1918 has been adopted in identical language in article 162 of Treasury Regulations 62, 65, and 69, promulgated under the Revenue Acts of 1921 (42 Stat., 227, 255), 1924 (43 Stat., 253, 284), and 1926 (44 Stat., 9, 42), respectively, reenacting, without substantial change, section 234(a)7. Apparently, therefore, the executive construction of this statute has received legislative approval. See *Komada v. United States* (215 U. S., 392); *National Lead Co. v. United States* (252 U. S., 140).

We agree with the Treasury Department that the value of appellant's property as a unit or going concern is not the proper basis for computing "a reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence." While the eliminated items enter into the value of the plant, they are not depreciable in fact, and, hence, were properly eliminated in fixing the value of depreciable property.

Decision affirmed, with costs.

ARTICLE 163: Depreciation of intangible property.

VIII-30-4285

Ct. D. 82

INCOME TAX—REVENUE ACT OF 1921—DECISION OF COURT.

DEDUCTION—OBsolescence—SECRET PROCESS.

No deduction can be taken for obsolescence of a secret process under section 214(a)8 of the Revenue Act of 1921, which limits the allowance for obsolescence to such property as is susceptible to exhaustion, wear and tear by use in the business.

COURT OF CLAIMS OF THE UNITED STATES.

Charles E. Kaltenbach v. The United States.

[January 7, 1929.]

OPINION.

SINNOTT, Judge, delivered the opinion of the court.

This is a tax case and relates to the year 1921. It is the companion case of *Charles E. Kaltenbach v. The United States*, No. D-583, relating to the year 1919. Both cases involve the same contract, set forth in Finding IV. In case No. D-583, decided by this court on this date against the contention of plaintiff, it was held that said contract was a license for the use of plaintiff's process and not a sale.

In the present case, No. D-584, in the event that the court does not sustain plaintiff's contention with respect to the sale of his process, plaintiff presents an alternative claim for the refund of the taxes paid, because of the obsolescence of his process in the year 1921. Plaintiff cites as applicable the deductions allowed in section 214(a)8 of the Revenue Act of 1921 (42 Stat., 240):

"(8) A reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence. In the case of such property acquired before March 1, 1913, this deduction shall be computed upon the basis of its fair market price or value as of March 1, 1913;"

It is the contention of defendant that the secret process of plaintiff for the tin weighting of silk is not susceptible to exhaustion, wear and tear, or obsolescence, within the purview of (8), *supra*. We think defendant's contention is well taken. Language identical with (8), in the Revenue Act of 1918, was construed in a well-considered opinion by the Circuit Court of Appeals, Eighth Circuit, in *Red Wing Maltting Co. v. Willcuts* (15 Fed. (2d) Series, 626, 631 [T. D. 3980, C. B. VI-1, 225]), wherein the court said:

"It seems to us that the language 'including a reasonable allowance for obsolescence' is but a part of and an enlargement of the previous phrase of the said subsection (7) relating to exhaustion, wear and tear, and that the first part of the sentence was intended to cover the subject matter thereof. It does not add a new kind of deduction, but merely permits the inclusion of an additional element, namely, obsolescence of such property used in the business as is subject to exhaustion, wear and tear. The allowance for obsolescence was intended to be in connection with the allowance for exhaustion, wear and tear, that being at times insufficient to restore the proper basis of capital values."

According to the ruling in the *Red Wing* case, *supra*, it is evident that a secret process for the weighting of silk by the use of chemicals or metals can not be subject to exhaustion, wear and tear, and therefore is not subject to obsolescence, within the purview of (8). In *Red Wing Maltting Co. v. Willcuts*, *supra*, certiorari was denied by the Supreme Court (273 U. S., 763).

It is further contended in plaintiff's brief that section 214(a)4 of the Revenue Act of 1921 (42 Stat., 240) is applicable to his case:

"(4) Losses sustained during the taxable year and not compensated for by insurance or otherwise, if incurred in trade or business."

It is questionable whether the language of (4) is before us for construction. It does not appear that plaintiff predicated his claim for refund before the Commissioner of Internal Revenue on (4). On the contrary, it appears in Finding XI, which was one of the findings of the commissioner of this court, and which was not objected to by plaintiff, that plaintiff's claim for refund, aside from the claim of sale, was predicated solely on obsolescence, under (8). This identical point was commented upon by the court in *Red Wing Maltting Co. v. Willcuts*, *supra*, where the court said:

"It does not appear from the record that any claim under subsection (4) for refund covering the loss of good will as a sustained loss during the taxable year was presented to the Commissioner of Internal Revenue prior to bringing this action and a refund requested. The application for refund does not appear in the record. Such application is a condition precedent to the jurisdiction of this court in matters of this character. The precise ground upon which the refund is demanded must be stated in the application to the Commissioner, and we think, if that is not done, a party can not base a recovery in the court upon an entirely different and distinct ground from that presented to the Commissioner."

However this may be, we do not think that (4) is applicable in this case. It does not appear that plaintiff suffered actual loss, within the purview of (4), when his secret process was superseded by the Swiss process referred to in Finding VI. Plaintiff's process was discovered and developed by himself. Its cost to him was problematical. It does not appear in the record. If the language of (4) were properly before us for construction we would feel compelled to hold, under the authority of *United States v. Flannery* (268 U. S., 98, 105 [T. D. 3703, C. B. IV-1, 106]), that plaintiff sustained no actual loss, within the purview of (4).

We have reached the conclusion that the Commissioner of Internal Revenue was correct in denying plaintiff's claim for refund. It is therefore ordered and adjudged that plaintiff's petition be dismissed.

SECTION 214(a)10.—DEDUCTIONS ALLOWED: DEPLETION.

ARTICLE 202: Amount returnable through depletion and depreciation deductions in the case of an operating owner.

REVENUE ACTS OF 1918 AND 1921.

Computation basis. (See G. C. M. 6746, page 119.)

SECTION 218.—PARTNERSHIPS AND PERSONAL SERVICE CORPORATIONS.

ARTICLE 332: Distributive shares of partners.
(Also Section 219, Article 343.)

VIII-35-4329
G. C. M. 6658

REVENUE ACT OF 1921.

Where both a partner and a partnership of which he was a member kept their accounts on the cash receipts and disbursements basis, and each had the same accounting year, upon the death of a partner, the decedent's executors should return for income tax purposes on behalf of the decedent the share of the decedent in the partnership income for the period ending with his death. Appeal of R. W. Archbald, jr., et al., executors (4 B. T. A., 483, C. B. VI-1, 1) and General Counsel's Memorandum 2308 (C. B. VI-2, 229) distinguished.

An opinion is requested as to whether the facts in the following case bring it within the principle of the decision of the United States Board of Tax Appeals in the appeal of R. W. Archbald, jr., et al., executors, and General Counsel's Memorandum 2308, based thereon.

The facts in the instant case are as follows:

A died December 6, 1923. The decedent kept his accounts on the cash receipts and disbursements basis and filed his returns on the calendar-year basis. Prior to his death the decedent was a partner in the M partnership, owning a 50 per cent interest therein. This partnership kept its books and filed its returns on the calendar-year basis. For the calendar year 1923 the income of the partnership was 12.2*x* dollars. The decedent would have been entitled to 6.1*x* dollars of this income had he lived to the end of the taxable year. Inasmuch as he died on December 6, his income to that date was considered to be 5.7*x* dollars. Under date of December —, 1924, his income tax return for the period from January 1 to December 6, 1923, was examined and the 5.7*x* dollars was treated as taxable income to him. On February —, 1929, his executor filed a claim for refund, on the theory that this amount was not taxable to the decedent, and in support thereof cited the decision of the Board of Tax Appeals in the case of R. W. Archbald, jr., executors (*supra*), and General Counsel's Memorandum 2308. The 5.7*x* dollars was set up in the estate tax report as part of the corpus of the decedent's estate and inheritance tax paid thereon.

Attention is invited to the decision of the Board of Tax Appeals in the case of *Maurice L. Goldman et al., executors, v. Commissioner* (15 B. T. A., 1341). In this case the Board of Tax Appeals held that where both a partner and a partnership of which he was a member kept their accounts on the cash receipts and disbursements basis, and each had the same accounting year, upon the death of a partner, the decedent's executors should return for income tax purposes on behalf of the decedent the share of the decedent in the partnership income for the period ending with his death. In concluding its opinion in this case the Board said:

The decision of the Board in the appeal of R. W. Archbald, jr., et al., executors, *supra*, on which reliance is placed by the petitioners, involved certain facts which are not present in the case at bar. In that case, a partner, who had regularly made his income tax return on a calendar-year basis, was a member of a partnership which had kept its accounts on the basis of fiscal

years ending January 31 of each year. The partner died on August 15, 1920. The question presented was whether the executors of a deceased partner should return for the year 1920 not only the share of decedent in the partnership income for the fiscal year ending January 31, 1920, but also the share of the profits of the partnership from February 1, 1920, to August 15, 1920, the date of decedent's death, and the consequent dissolution of the partnership. The Board held that the only income from the partnership to be included in the return for the decedent for the calendar year 1920 was the distributive share of the partnership to which he was entitled for the fiscal year ended January 31, 1920. There is not involved in the case at bar any conflict on account of the partnership being on a fiscal-year basis and the partner on a calendar-year basis; here the accounting periods coincide. Nor is there involved the question of a partner being required to report more than 12 months' income on account of the operations of a partnership. To the extent, however, that the views expressed in the Archbald case are in conflict with the views herein expressed, the Archbald case is overruled.

In view of the foregoing, it is the opinion of this office that the facts in the instant case do not bring it within the principle of the decision of the Board of Tax Appeals in the appeal of R. W. Archbald, jr., and General Counsel's Memorandum 2308.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

SECTION 219.—ESTATES AND TRUSTS.

ARTICLE 341: Estates and trusts.

REVENUE ACT OF 1921 AND PRIOR REVENUE ACTS.

Annuity payments to widow in lieu of her dower or statutory interest. (See I. T. 2480, page 141.)

ARTICLE 343: Decedent's estate during administration.

REVENUE ACT OF 1921.

Share of decedent in partnership income for period ending with his death. (See G. C. M. 6658, page 309.)

SECTION 221.—PAYMENT OF INDIVIDUAL'S TAX AT SOURCE.

ARTICLE 361: Withholding tax at source.

VIII-46-4428
I. T. 2508

REVENUE ACT OF 1921.

The clause, "both the principal and interest of this bond are payable without deduction for any United States, State, municipal or other tax or taxes," contained in the bonds of the M Company is a tax-free covenant within the meaning of section 221(b) of the Revenue Act of 1921, and interest on such bonds is subject to the withholding requirements of the statute.

A ruling is requested relative to the first and refunding mortgage 5 per cent gold bonds issued by the M Company.

On November 1, 1908, the M Company executed an indenture securing the bonds in question, each of which contains the following provision:

Both the principal and interest of this bond are payable without deduction for any United States, State, municipal or other tax or taxes which said M Company may be required to pay, under or by reason of any present or future law, the said company hereby agreeing to pay said tax or taxes.

The question presented is whether the above-quoted provision of the bonds constitutes a tax-free covenant within the meaning of section 221(b) of the Revenue Act of 1921. In this connection attention is called to the fact that the bonds are dated November 1, 1908, at a time when income taxes and a withholding tax were not in the public mind. It is also pointed out that the bonds do not contain the words, "or permitted to pay thereon, or to retain therefrom," which are a part of section 221(b).

The taxpayer contends that the bonds in question do not contain a tax-free covenant, and that the company did not agree to pay any part of the income tax that might be assessed against the bondholders upon the interest on the bonds; and also that the only kind of tax the company agreed to pay was a tax that might be assessed against it directly and as its direct obligation.

Section 221(b) of the Revenue Act of 1921 reads, in part, as follows:

(b) In any case where bonds, mortgages, or deeds of trust, or other similar obligations of a corporation contain a contract or provision by which the obligor agrees to pay any portion of the tax imposed by this title upon the obligee, or to reimburse the obligee for any portion of the tax, or to pay the interest without deduction for any tax which the obligor may be required or permitted to pay thereon, or to retain therefrom under any law of the United States, the obligor shall deduct and withhold a tax equal to 2 per centum of the interest upon such bonds, mortgages, deeds of trust, or other obligations, whether such interest is payable annually or at shorter or longer periods and whether payable to a nonresident alien individual or to an individual citizen or resident of the United States or to a partnership * * *.

For convenient reference the alternative requirements of section 221(b), as to the nature of the contract or covenant which the debtor corporation must undertake, may be stated as follows:

1. To pay any portion of the tax imposed by this title upon the obligee, or
2. To reimburse the obligee for any portion of the tax, or
3. To pay the interest without deduction for any tax which the obligor may be required or permitted to pay thereon, or to retain therefrom, under any law of the United States.

The requirements of the statute may be met by the employment of the identical language of the statute, but this method of compliance therewith is not exclusive. It is sufficient if the substance of the requirements enumerated in the statute is found in the particular clause under consideration. The third requirement is met if the clause in question either designates a tax which is in fact the sort of tax contemplated by the statute or contains a general description of taxes broad enough to include a tax such as mentioned in the statute, although it may include others also.

In Solicitor's Memorandum 3317 A (C. B. IV-2, 195) there are contained several examples of clauses found in corporate bonds relative to the payment of taxes. Among them are the following:

2. This bond and its coupons are payable without deduction of any tax or taxes.

3. Both the principal and interest of this bond are payable without deduction, defalcation, or abatement to be made of anything for or in respect of any taxes, charges, or assessments whatsoever.

Both clauses were held to be tax-free covenants for the reason that the expression "any taxes" is clearly broad enough to include any tax contemplated by the third requirement of the statute.

The clause, "both the principal and interest of this bond are payable without deduction for any United States, State, municipal or other tax or taxes," contained in the bonds of the M Company, is broad enough to bring it within the class of tax-free covenants without the additional covenant of the company "which said M Company may be required to pay, under or by reason of any present or future law, the said company hereby agreeing to pay said tax or taxes." The fact that the bonds do not contain the words "or permitted to pay thereon or to retain therefrom" does not negative the effect of the clause as a tax-free covenant.

Relative to the statement that the bonds were issued in 1908 before the enactment of a Federal income tax law, attention is invited to I. T. 2153 (C. B. IV-1, 195), wherein it is stated that in the opinion of this office the third requirement of section 221(b) of the Revenue Act of 1921 was inserted in the Act to cover cases of bonds issued before the income tax laws were passed, as bonds issued prior to the income tax laws would have no reference to income taxes.

It is held, therefore, that the bonds of the M Company contain a tax-free covenant within the meaning of section 221(b) of the Revenue Act of 1921, and that the interest on such bonds is subject to the withholding requirements of the statute.

SECTION 222.—CREDIT FOR TAXES IN CASE OF INDIVIDUALS.

ARTICLE 381: Analysis of credit for taxes.

REVENUE ACTS OF 1918 AND 1921.

Revocation of Office Decision 1093 (C. B. 5, 194) and Solicitor's Memorandum 3155 (C. B. IV-1, 45). (See I. T. 2485, page 252.)

PART III.—CORPORATIONS.

SECTION 230.—TAX ON CORPORATIONS.

ARTICLE 503: Corporations liable to tax.

VIII-42-4398
Ct. D. 120

INCOME TAX—REVENUE ACT OF 1918—DECISION OF COURT.

1. INCOME TAX—INCOME FROM EXPORTS—CONSTITUTIONALITY.

An income tax levied under the Revenue Act of 1918 upon the net income of a corporation from its business of exporting goods from the United States and selling them in foreign countries, while corporations organized in Porto Rico and the Philippine Islands are exempted from tax, by virtue of sections 1 and 233(b) of that

Act, on profits from sales in foreign countries of goods purchased in the United States, does not deprive a domestic corporation of its property without due process of law in violation of the fifth amendment of the Constitution of the United States.

2. SAME.

An income tax levied upon net income from the business of exporting goods from the United States and selling such goods in foreign countries is not a tax laid on articles exported from any State in violation of Article I, section 9, clause 5, of the Constitution of the United States.

UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

Neuss, Hesslein & Co., Inc., appellant, v. William H. Edwards, as Collector of Internal Revenue for the Second District of New York, appellee.

Appeal from a judgment of the District Court for the Southern District of New York dismissing a complaint at law for insufficiency upon its face.

Before MANTON, L. HAND, and AUGUSTUS N. HAND, Circuit Judges.

[February 4, 1929.]

OPINION.

The plaintiff, a New York corporation, was engaged in the business of exporting and selling abroad goods bought within the United States. There are corporations organized under the laws of Porto Rico and the Philippines which do the same, and which therefore compete with it. The plaintiff was taxed under section 213(a) of the Revenue Law of 1918, upon its income derived from the profits of its sales abroad, while its insular competitors were exempted by virtue of section 1 and section 233(b). The complaint charges that the discrimination so created makes the tax void under the fifth amendment, since the taxes local to the islands do not include income received outside their borders and do not therefore neutralize the handicap.

The plaintiff paid the tax assessed under protest and sued the collector for money had.

L. HAND, Circuit Judge: The suit is a supposed corollary to the reasoning of the Supreme Court in *National Paper & Type Co. v. Bowers* (266 U. S., 373 [T. D. 3677, C. B. IV-1, 203]) and *Barclay & Co. v. Edwards* (267 U. S., 442 [T. D. 3691, C. B. IV-1, 207]), answering a similar argument based upon the exemption of foreign corporations from the same tax. The court there suggested as a justification for the distinction that foreign corporations unlike domestic could not invoke the protection of the United States in their dealings abroad; the plaintiff now argues because corporations of Porto Rico and the Philippines are entitled to the same protection abroad as State corporations, that this excuse fails, that the exemption is arbitrary, and the tax confiscatory within the fifth amendment.

In the first place, it by no means follows that the law is necessarily invalid because there is no warrant for the exemption and the unequal incidence of the tax. It is notoriously difficult to lay taxes equally and Congress has the widest latitude in the exercise of this, the most vital of its powers. Indeed, it used to be said that in those fields where the power itself was undoubted, its exercise was wholly beyond the limitations of the fifth amendment; Congress might throw the burden as it chose (*Veazie Bank v. Fenno*, 8 Wall., 533; *Treat v. White*, 181 U. S., 264, 269; *McCray v. U. S.*, 195 U. S., 27; *U. S. v. Doremus*, 249 U. S., 86; *Billings v. U. S.*, 232 U. S., 261, 282; *Flint v. Stone Tracy Co.*, 220 U. S., 107, 158). To-day this would be too broad a statement, for, starting with intimations in *Brushaber v. Union Pac. R. R. Co.* (240 U. S., 1, 24, 25) and *Lewellyn v. Frick* (268 U. S., 238, 251, 252 [T. D. 3715, C. B. IV-1, 322]), it is now held that retroactive tax may operate with so much injustice as to come within the amendment and be invalid for that reason (*Nichols v. Coolidge*, 274 U. S., 531 [T. D. 4072, C. B. VI-2, 351]; *Blodgett v. Holden*, 275 U. S., 142 [T. D. 4117, C. B. VII-1, 324]; *Untermeyer v. Anderson*, 276 U. S., 440 [T. D. 4157, C. B. VII-1, 326]). As yet, however, mere inequality of incidence has never been held enough, and much has been tolerated (*Brushaber v. Union Pac. R. R. Co.*, 240 U. S., 1, 25, 26; *La Belle Iron Works v. U. S.*, 256 U. S., 377, 392, 393 [T. D. 3181, C. B. 4, 373]). Except for any implications to be drawn from the

discussion in *Brushaber v. Union Pac. R. R. Co.* and *Barclay Co. v. Edwards*, there has been not even a suggestion that taxes are invalid because they bear unequally. We do not find it necessary to consider the point here, because we think that there were sufficient reasons for the exemption.

It arises because by section 1 of the Revenue Act of 1918, Porto Rico and the Philippines are classed as foreign territory. That of course was a definition only for the purposes of the Act (*DeLima v. Bidwell*, 182 U. S., 1), but it corresponded with a real difference in constitutional status. The ambiguities resulting from the opinions in *Downes v. Bidwell* (182 U. S., 244) have since been cleared, and it is settled law that until formally incorporated into the United States, the Constitution, or at least the whole of it, does not extend to annexed territory *ex proprio vigore* (*Dorr v. U. S.*, 195 U. S., 138; *Dowdell v. U. S.*, 221 U. S., 325, 332; *Balzac v. People of Porto Rico*, 258 U. S., 298, 305). Porto Rico and the Philippines have never been so incorporated, and moreover, like Alaska and Hawaii, which have (*Rasmussen v. U. S.*, 197 U. S., 516; *Alaska v. Troy*, 258 U. S., 101; *Farrington v. Tokushige*, 273 U. S., 284), do not share politically in the Government. They govern themselves in whole or in part only by Act of Congress under section 3 of Article IV of the Constitution, though they have for long had independent systems of taxation and have been exempted from the general income tax. We do not understand that the plaintiff challenges the propriety of that exemption or complains of the competition between itself and insular corporations so far as they buy in the islands and sell abroad (*Porto Rico Coal Co. v. Edwards*, 275 Fed. Rep., 104, 108, 109). Its complaint is that when they buy in the United States in immediate competition with domestic corporations they should be put on a parity with them; the Revenue Act should have imposed a tax upon the income so derived, which presumably would be assessed and collected within the States and at the place where they bought the goods.

As a purely fiscal policy there can be no doubt that Congress may prefer the Territories, imposing the resulting burdens on the States at large, just as it may directly tax them and cover the proceeds into the Treasury (*Binn's v. U. S.*, 194 U. S., 486). The fifth amendment does not reach such inequalities, for the preference granted is to a section which has no voice in the result; the States can not oppress themselves, and may grant favors to those dependent on their will, if the resulting deficit be equally distributed. Nor does it make a difference that the preference extends to transactions taking place within the States themselves. The same reasons apply as before; the discrimination is not imposed upon those who have no political power, but is assumed by those who have it.

The gist of the plaintiff's complaint can not therefore rest upon fiscal discrimination, but upon its indirect results; that is, upon the handicap to its trade which arises from the differential. But the Constitution does not require taxes to be laid in such a way as to keep all taxpayers at industrial and commercial parity, any more than it looks into the distribution of the taxes when collected (*Dane v. Jackson*, 258 U. S., 589, 598, 599; *Knights v. Jackson*, 260 U. S., 12). Such an ideal is impossible in practice in any case, and so far as it is not, courts have no means of realizing it, and no power, if they had means. Taxation inevitably involves the compromise of conflicting interests of whose pressures the final action must be the resultant. These can be adjusted only by that body which is properly responsive to their social importance and that body is Congress, not the courts. Such controversies can not be accommodated by general rules or economic absolutes, or without a scrutiny and valuation which go far beyond the scope of judicial inquiry.

A subsidiary point is that the tax is upon exports. Concededly, if it be not unduly discriminatory, it is not (*Peck & Co. v. Lowe*, 247 U. S., 165). The second question is therefore answered with the first.

Judgment affirmed.

SECTION 231.—CONDITIONAL AND OTHER EXEMPTIONS OF CORPORATIONS.

ARTICLE 514: Fraternal beneficiary societies.

REVENUE ACT OF 1918.

Employees' relief organization. (See Ct. D. 75, page 371.)

SECTION 233.—GROSS INCOME OF CORPORATIONS DEFINED.

ARTICLE 547: Income from leased property.

VIII-26-4252
Ct. D. 73

INCOME TAX—REVENUE ACT OF 1916—DECISION OF SUPREME COURT.

INCOME—LESSOR—RENTAL—INCOME TAXES PAID BY LESSEE.

Income taxes assessed against a lessor and paid by the lessee pursuant to the terms of the lease constitute additional income to the lessor under the Revenue Act of 1916.

• SUPREME COURT OF THE UNITED STATES.

The United States of America v. Boston & Maine Railroad Co.

[June 3, 1929.]

OPINION.

Mr. Chief Justice TAFT delivered the opinion of the court.

As indicated in *Old Colony Trust Co. v. Commissioner of Internal Revenue*, No. 130, just decided, this case comes here by certificate from the Circuit Court of Appeals for the First Circuit and on the following statement:

"This action is brought by the Boston & Maine Railroad to recover income taxes for the year 1917, claimed to have been erroneously collected. In the District Court (for the District of Massachusetts) the plaintiff recovered a judgment for the full amount of its demand—\$3,920.55 and interest.

"June 30, 1900, the Fitchburg Railroad Co. leased all its railroad and property of every description to the Boston & Maine Railroad for the term of 99 years. In the lease the lessee covenanted to pay specified rentals, to maintain and replace the leased properties in manner indicated, to pay all operating expenses, and to pay 'all taxes of every description, Federal, State, and municipal, upon the lessor's property, business, indebtedness, income, franchises, or capital stock, or said rental,' and to pay divers other charges. In 1918 an income-tax return, under the provisions of the Revenue Acts of 1916 and 1917, was filed on behalf of the Fitchburg Railroad Co. for the calendar year 1917, upon which taxes amounting to \$61,422.06 were assessed. These taxes were paid to the Commissioner of Internal Revenue by the Boston & Maine Railroad pursuant to the term of the lease. The Fitchburg Railroad Co. was consolidated with the Boston & Maine Railroad in 1919.

"In 1921 the Commissioner of Internal Revenue assessed an additional income tax against the Fitchburg Railroad Co. of \$3,920.55. In doing this he treated the payment of \$61,422.06 made by the Boston & Maine Railroad to the collector of internal revenue as additional taxable income to the Fitchburg Railroad Co. to the extent of \$65,342.61. This additional tax of \$3,920.55 was paid to the collector of internal revenue by the Boston & Maine Railroad in July, 1921.

"The claim for refund of this additional tax was duly filed with the Commissioner of Internal Revenue, but was never formally acted upon, and more than six months having passed after it was filed, this action was brought for the recovery of the tax so paid (under paragraph 20, section 24 of the Judicial Code, as amended by section 1310(c), chapter 136, 42 Stat., 310)."

The judgment of the district court was appealed to the Circuit Court of Appeals for the First Circuit, and upon the facts recited, and under section 239 of the Judicial Code, as amended by the Act of February 13, 1925 (ch. 229, 43 Stat., 936, 938), the court of appeals has asked the instruction of the Supreme Court upon the following question:

"Did the payment by the lessee of the income taxes assessable against the lessor constitute additional taxable income to such lessor?"

The merits of this case must be disposed of in accord with the rule already laid down in the *Old Colony* case just decided. Like that, it is one in which the lessee has paid to the Government the taxes due under the law from the

lessor. The payment is made in accord with the contract of lease, and is merely a short cut whereby that which the lessee specifically agreed to pay as part of the rental effects that payment by discharging the obligation of the lessor to pay the tax to the Government.

Our conclusion is in accordance with the practice of the Department. Treasury Decision 2620 (19 Treas. Dec. 411). In answer to a question suggested by this court, the Commissioner states, in the appendix to the Government's brief on reargument in No. 130, that it has been the uniform practice to treat taxes paid, where by agreement between the parties the tax laid upon the income actually received by one of them has been paid by the other. He refers to the decision of the Circuit Court of Appeals for the First Circuit in the case of *West End Railway Co. v. Malley* (246 Fed., 625), where the dividends paid by a lessee corporation directly to the stockholders of the lessor corporation were held to be income to the lessor under the Revenue Act of October 3, 1913. It was carried into Regulations 33, promulgated January 2, 1918, as article 102, reading as follows:

"ART. 102. *Leased properties.*—When a corporation shall have leased its property in consideration that the lessee shall pay in lieu of rental an amount equivalent to a certain rate of dividends on its capital stock or the interest on its outstanding indebtedness, together with taxes, insurance, or other fixed charges, such payments shall be considered rental payments and shall be returned by the lessor corporation as income, notwithstanding the fact that the dividends and interest are paid by the lessee direct to the stockholders and bondholders of the lessor. The lessee, in making these payments direct to the bondholders and the stockholders, does so as the agent of the lessor, and the latter is none the less liable to return the amounts thus paid as income and to pay any tax that may be due thereon."

Article 102 of Regulations 33 has been substantially embodied in all subsequent regulations, as article 546 of Regulations 45, article 547 of Regulations 62, 65, and 69, and article 70 of Regulations 74, promulgated under the Revenue Acts of 1918, 1921, 1924, 1926, and 1928, respectively.

Article 109 of Regulations 45, promulgated January 28, 1921, reads as follows:

"Taxes paid by a tenant to or for a landlord for business property are additional rent and constitute a deductible item to the tenant and taxable income to the landlord, the amount of the tax being deductible by the latter."

This provision is also found in article 109 of Regulations 62, article 110 of Regulations 65 and 69, and article 130 of Regulations 74.

In addition to the foregoing general provisions, a specific ruling on this question was published in May, 1920, as Appeals and Review Memorandum 16 (C. B. 2, page 62). The facts in that case are stated by the Commissioner as follows:

"A contract was entered into in July, 1917, between the P Company and the M Company, whereby the latter agreed to sell certain goods on a cost-plus basis. It was provided that the P Company should pay Federal taxes assessed on the profits accrued from this contract to the M Company. Performance under the contract was made by the M Company during 1918. In October, 1918, the P Company closed its books upon an accrual basis and made no provision for any taxes arising out of the contract. It was there held that the amount of taxes of the M Company paid by the P Company was income to the M Company for the year for which such payment was made. This ruling was followed not only in the case in which rendered but also as a precedent in all other similar cases."

The Commissioner says that no single instance has been found where the Bureau has departed from this general practice of construing taxes paid under the present circumstances to be income to the taxpayer whose tax liability has been discharged in such a manner.

The Commissioner says that it was the purpose of the instructions to establish a consistent policy, and that if they have not been followed in individual cases, it is due to an unauthorized departure from the Bureau's instructions. More than this, it should be added that neither before nor since 1923 has any algebraic formula been used by the Bureau in computing taxes.

Not only, therefore, is the conclusion that the question must be answered "Yes" sustained by the practice of the Department under all of the Revenue Acts, but the cases cited in the Old Colony case require the same view.

SECTION 234.—DEDUCTIONS ALLOWED CORPORATIONS.

ARTICLE 561: Allowable deductions.
(Also Section 326, Article 831.)

VIII-35-4332
Ct. D. 96

INCOME AND EXCESS PROFITS TAXES—REVENUE ACT OF 1918—DECISION OF COURT.

1. DEDUCTION—CORPORATION—COMMISSIONS FOR SALE OF STOCK.

Commissions paid by a corporation for the sale of its capital stock are not deductible as a business expense under section 234(a)1 of the Revenue Act of 1918.

2. INVESTED CAPITAL—COMMISSIONS FOR SALE OF STOCK.

An amount representing commissions paid by a corporation for the sale of its capital stock is properly excluded in the computation of invested capital under section 326 of the Revenue Act of 1918.

3. DECISION AFFIRMED.

The decision of the United States Board of Tax Appeals (8 B. T. A., 631) affirmed.

UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT.

Simmons Co. v. Commissioner of Internal Revenue.

Appeal from Board of Tax Appeals.

[May 31, 1929.]

OPINION.

ANDERSON, J.: On December 15, 1924, the Commissioner of Internal Revenue notified the petitioner of deficiencies in its income and profits taxes for 1919 of \$222,319.71, and for 1920 of \$61,327.77. On appeal to the Board of Tax Appeals, the deficiencies for 1919 and 1920 were redetermined as \$188,383.20 and \$29,298.62, respectively. On appeal to this court, the main contentions are: That commissions paid by the taxpayer on the sale of its own capital stock are—under section 234(a)1 of the Revenue Act of 1918 (ch. 18, 40 Stat., 1057, 1077, 1092)—“deductible as ordinary and necessary expenses incurred * * * in carrying on” its “trade or business”; and that if not so deductible, such commissions should be included as part of its invested capital. Thus included, they increase the amount on which the taxpayer is entitled to normal profits and hence tend to reduce its tax.

The facts out of which this appeal grows are as follows: In 1917 the petitioner issued 20,000 shares of preferred stock (\$2,000,000 par value), which were sold to bankers for \$87.50 per share. The bankers sold this stock to the public at \$95 per share. The corporation actually received \$1,750,000. It charged the difference of \$250,000 as an expense.

In August, 1919, the petitioner redeemed the entire 20,000 shares at 110, and made a new issue of 70,000 shares, paying the bankers \$525,255 in connection with the sale of this stock. This sum was also charged as an expense. This stock was in part sold to the public at \$97 per share and in part exchanged for the old issue on terms not now material.

Deducting the discount of 3 points on 70,000 shares (\$210,000), the net commission to the bankers was \$315,255. This sum, petitioner strenuously urges, should be deducted from its gross income for 1919 as an “ordinary and necessary” expense within the meaning of section 234(a), *supra*.

(1) The Board adhered to its previous rulings in the appeal of Charles H. Lilly Co. (2 B. T. A., 1058) and Emerson Mfg. Co. (3 B. T. A., 932), and held that bankers' commissions paid for a sale of shares were not deductible as “ordinary and necessary expenses in carrying on the business.”

We think this ruling was right, for the reasons adequately stated in the Emerson Mfg. Co. case (3 B. T. A., 932). While expenses for organization

or for obtaining additional capital are frequent in growing and successful enterprises, we think it clear that they are not "ordinary and necessary expenses" in the productive operations of such concerns within the meaning of the tax laws.

If the language used seemed to us doubtful (as it does not), the practically contemporaneous construction by the Treasury Department in its regulations would require us to exclude expenses incident to the organization of a corporation and the sale of its capital stock as being within the fair meaning of "ordinary and necessary expenses incurred in carrying on the business" of such corporation. In effect, the regulations limit deductible expenses to the current operating expenses incurred in producing the income. See articles 21, 101, 582. The case in that regard falls under the familiar rule that contemporaneous construction given to an Act of Congress by the executive officers charged with its enforcement, though not controlling, is entitled to great weight. (*Baltzell v. Mitchell*, 3 Fed. (2d), 428, 430 [T. D. 3668, C. B. IV-1, 191].) Compare *National Lead Co. v. United States* (252 U. S., 140, 146), where the Supreme Court points out the additional weight attaching to such construction from the fact that Congress has, by subsequent legislation, given it implied approval. The construction that only operating expenses are deductible under section 234(a)1 was being applied by the Treasury Department when Congress reenacted the provision, in unchanged form, in the Revenue Acts of 1921, 1924, 1926, and 1928. (42 Stat., 254; 43 Stat., 283; 44 Stat., 41; 45 Stat., 799.) See also *Brewster v. Gage* (30 Fed. (2d), 604, 606 [Ct. D. 50, C. B. VIII-1, 229]).

(2) The petitioner's second contention (illustrated by its claim), that the payment of \$150,000 as a commission for the sale of the first issue of \$2,000,000 of preferred stock is "something in the nature of an intangible asset in some way or other associated with the dollars it was expended to secure," seems to us an untenable, far-fetched notion—inconsistent with the plain meaning of the tax statutes.

We agree with the reasoning of the Board of Tax Appeals by which it reaches the conclusion that invested capital can not be increased by commissions paid for the sale of its stock or by discount from par to the purchasers of the stock. Section 326(a) reads:

"That as used in this title the term 'invested capital' for any year means * * *:

- "(1) Actual cash bona fide paid in for stock or shares;
- "(2) Actual cash value of tangible property, other than cash, bona fide paid in for stock or shares, * * *;
- "(3) Paid-in or earned surplus and undivided profits; not including surplus and undivided profits earned during the year;
- "(4) Intangible property bona fide paid in for stock or shares prior to March 3, 1917, * * *;
- "(5) Intangible property bona fide paid in for stock or shares on or after March 3, 1917, * * *."

By necessary implication, this enumeration of items of what is "invested capital" excludes commissions paid by a corporation for the sale of its own stock. Such commissions obviously decrease the amount of capital available for the business operations of the concern. They contrast with the ideas contained in "actual cash," "actual cash value of tangible property," "paid in or earned surplus and undivided profits." All these add to the resources of the corporation. Commissions paid for marketing stock simply diminish the net return from the stock issue. Financially, they are equivalent to an issue of stock at a discount from par; the par value must be carried as a liability without an off-setting equal amount of cash or property.

The statutory concept as to what is "invested capital" is clear. See *La Belle Iron Works v. United States* (256 U. S., 377 [T. D. 3181, C. B. 4, 373]); *Willcuts v. Milton Dairy Co.* (275 U. S., 215 [T. D. 4148, C. B. VII-1, 283]), reversing the Court of Appeals for the Eighth Circuit in 15 Fed. (2d), 814.

The language used in *La Belle Iron Works v. United States* (256 U. S., 377, 378), quoted with approval in *Willcuts v. Milton Dairy Co.* (275 U. S., 215, 219, 220), is conclusive against the petitioner's contention.

The decision of the Board of Tax Appeals is affirmed.

ARTICLE 561: Allowable deductions.

VIII-37-4353
Ct. D. 105

INCOME TAX—REVENUE ACTS OF 1918 AND 1921—DECISION OF COURT.

1. INCOME—CONTINGENT COMPENSATION.

Where a taxpayer, keeping its books on the accrual basis, contracts with an employee to pay him a bonus equal to a percentage of the amount by which the net profits of the business for the entire 5-year term of the contract, calculated on a certain basis, exceeded another certain amount, calculated upon another basis, which bonus could not be calculated and was not paid before the expiration of the contract in 1923, the taxpayer may not deduct a certain part of the bonus as an ordinary and necessary expense for the years 1920 and 1921 under section 234(a)1 of the Revenue Acts of 1918 and 1921.

2. DECISION AFFIRMED.

The decision of the United States Board of Tax Appeals (11 B. T. A., 949) affirmed.

UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

Kaufman Department Stores, Inc., v. Commissioner of Internal Revenue.

Petition for review from the United States Board of Tax Appeals.

[August 9, 1929.]

OPINION.

BUFFINGTON, J.: This tax case involves the ascertainment of the meaning and effect of a lengthy contract made by the taxpayer with a manager for compensation dependent on five years' service and the profit inuring at the end of the term to the taxpayer as a result of such service. The case turns on the terms of this particular contract. The facts of the case and the individual features of the agreement are fully set forth in the findings and opinion of the Tax Board, and by reference thereto we avoid needless repetition. Finding no error in the decree of the Board, we limit ourselves to approving its action.

ARTICLE 561: Allowable deductions.

VIII-37-4355
Ct. D. 107

INCOME TAX—REVENUE ACT OF 1918—DECISION OF COURT.

DEDUCTION—TAX—BONUS ON INCREASE OF CAPITAL STOCK.

An amount paid by a corporation to the State of Pennsylvania as a bonus on an increase of its capital stock under the provisions of the Pennsylvania act of May 3, 1899 (P. L., 189), is not deductible as a tax under section 234(a)3 of the Revenue Act of 1918.

DISTRICT COURT OF THE UNITED STATES FOR THE WESTERN DISTRICT OF PENNSYLVANIA.

Greensburg Coal Co. v. United States of America.

[April 9, 1929.]

OPINION.

SCHOONMAKER, Judge: The plaintiff sues the United States to recover \$628.67, alleged additional income and profits tax for the calendar year 1920 collected by the collector of internal revenue of the twenty-third district of Pennsylvania on February 28, 1928.

This is an action over which this court has concurrent jurisdiction under paragraph 20(a), section 24 of the Judicial Code, as amended February 24, 1925 (43 Stat., 972, ch. 309).

The facts of the case are not in dispute. They are as follows:

On February 1, 1927, the Commissioner of Internal Revenue assessed an additional tax of \$1,495.74 against the plaintiff, which it paid under protest to the collector of internal revenue of the twenty-third district on February 28, 1927.

In making the computation of this additional tax, the Commissioner refused to allow as a deduction an amount of \$1,366.67 which the plaintiff paid to the State of Pennsylvania as a bonus on an increase of its capital stock under the provisions of the Pennsylvania act of May 3, 1899 (P. L., 189).

On June 27, 1928, the plaintiff filed a claim for refund in the amount of \$628.67, which represented the approximate amount of the increase of tax added by the Commissioner by reason of his refusal to allow the deduction claimed by the plaintiff of \$1,366.67 for bonus paid to the State of Pennsylvania.

On August 31, 1928, the Commissioner of Internal Revenue disallowed this claim for refund.

Under these facts, we hold as a matter of law that the plaintiff is not entitled to recover.

In support of this conclusion, we need only say that the court of appeals of this circuit has ruled that the capital stock bonus paid by Pennsylvania corporation is not a tax: *Re York Silk Mfg. Co.* (188 Fed., 735); *Penn'a v. York Silk Mfg. Co.* (192 Fed., 81).

Let judgment be entered in this case in favor of defendant.

ARTICLE 562: Donations.

(See also Sections 212 and 236 and Articles 23 and 831.)

VIII-43-4406

Ct. D. 124

INCOME AND PROFITS TAXES—REVENUE ACTS OF 1916, 1917, AND 1918. DECISION OF COURT.

1. DEDUCTIONS—CORPORATION—CHARITABLE CONTRIBUTIONS.

Contributions by a corporation to the Red Cross are not deductible from gross income as ordinary and necessary expenses under section 12 of the Revenue Act of 1916 and section 234(a)1 of the Revenue Act of 1918.

2. BASIS OF COMPUTATION—COMMISSIONER'S DETERMINATION.

The Commissioner's determination that the taxpayer's books were kept on the accrual basis is presumptively correct and must be sustained where it does not satisfactorily appear that he was in error. Accordingly, the taxpayer is not entitled to a credit in 1918, under section 238 of the Revenue Act of 1918, for British income tax paid in that year and assessed on account of income received in previous years.

3. INVESTED CAPITAL—EARNED SURPLUS.

An amount entered on the taxpayer's books as earned surplus representing the difference between the cash purchase price of stock and its par value is properly excluded in computing invested capital under section 207 of the Revenue Act of 1917 and section 326 of the Revenue Act of 1918, where the value of the stock at the time of its purchase was not in excess of the cost.

COURT OF CLAIMS OF THE UNITED STATES.

Niles Bement Pond Co. v. The United States.

[May 13, 1929.]

OPINION.

GRAHAM, Judge, delivered the opinion of the court.

This is a suit to recover taxes for which a claim for refund had been filed. It embraces three grounds of recovery. The first grows out of the claimed

right to deduct income and excess profits taxes paid by plaintiff's branch in England to the British Government. The second involves invested capital for each of the years 1917, 1918, and 1919, and the question whether the value of certain stock purchased by the plaintiff in 1901 should be allowed as a part of its surplus, and the third, whether the plaintiff should be allowed deductions for amounts donated to the American Red Cross and other organizations of a similar character.

We will take up the last of these questions first, as to the donations to the American Red Cross. The facts and the principle of the applicable statutes are for all purposes no different from those in *Consolidated Gas, Electric Light & Power Co. v. United States* (65 C. Cls., 252, 257, et seq. [T. D. 4182, C. B. VII-2, 294]), where a certiorari was denied on October 15, 1928, and the case of *Alfred J. Sweet, Inc., v. United States* [Ct. D. 55, C. B. VIII-1, 266], decided by this court February 4, 1929. It therefore must be held that as to the credit for donations to the Red Cross and other organizations the plaintiff can not recover.

We will next take up the first question of the right to a credit for taxes paid the British Government. The right to recover depends in this instance upon whether the plaintiff kept its books on an accrual or cash basis. An examination of its books and its system of accounts by the Commissioner of Internal Revenue satisfied that official that they were kept on an accrual basis within the meaning of the statute, and he so ruled. It is admitted that no system of bookkeeping will probably be found which is on a 100 per cent accrual basis. In almost every case where books are kept on an accrual basis, as a general principle of business, there are instances where certain accounts, small and sometimes covering a small percentage, are kept on a cash basis. We therefore concur in the ruling of the Commissioner that the books were kept on an accrual basis.

The court has found that while it appears that some of the accounts of the plaintiff were kept upon a cash basis and the British account among them, it does not clearly appear what proportion was kept on the accrual basis, or that the greater proportion of its business was not kept upon the accrual basis as held by the Commissioner of Internal Revenue, and it does not satisfactorily appear that the Commissioner was in error in concluding that the books were kept upon an accrual basis.

Without entering into a discussion of when a tax accrues, we conclude from what has just been said that the holding of the Commissioner that the books were kept upon an accrual basis must be sustained, it not satisfactorily appearing that in this he was in error, especially as it does not appear that the plaintiff presented any proof of the character of its general books of account in the United States either in 1918 or prior thereto. The presumption is in favor of the Commissioner's finding and must be overcome. (*United States v. Rindskopf*, 105 U. S., 418; *United States v. Anderson*, 269 U. S., 422 [T. D. 3839, C. B. V-1, 179].) Where only a relatively small part has been on the cash basis it must be held that the income should have been returned upon an accrual basis. (*United States v. Anderson*, supra; *W. S. Barstow & Co., Inc., v. Bowers*, 15 Fed. (2d), 75 [T. D. 3931, C. B. V-2, 144]; *Theodore Stanfield et al.*, 8 B. T. A., 787, 823; *Hyams Coal Co. v. United States*, 26 Fed. (2d), 805; and the *Max Schott* case, 5 B. T. A., 79.)

Pratt & Whitney stock.—The plaintiff is here asking for a refund, which was refused, growing out of the following facts: The Commissioner of Internal Revenue, in computing the income and excess-profits taxes of the plaintiff for the years 1917, 1918, and 1919, decreased the plaintiff's invested capital by reducing its earned surplus in the sum of \$1,370,579.06, which represented the difference between the cash paid, \$154,420.94, for 15,250 shares of the stock of the Pratt & Whitney Co., which the plaintiff took over, and the par value of that stock, \$100, which the plaintiff claims was its value at the time of the purchase. The plaintiff had deducted from this par value the cash purchase price actually paid and had passed the difference, the said sum of \$1,370,579.06, to earned surplus. The Commissioner held that it was not earned surplus, that the stock was worth the cash sum which the plaintiff paid for it at the time it was purchased, and reduced its earned surplus accordingly, and upon this basis assessed a deficiency tax for each of these years.

The question is whether the Commissioner was justified in the action which he took.

The court has found that the Pratt & Whitney Co. stock at the time of the purchase was worth no more than what the plaintiff paid for it, viz, \$154,420.94,

that it did not cost the plaintiff any more than this sum, nor was there anything other than the cash paid for it contributed by the plaintiff as consideration for it, and that the value of the stock at the time it was purchased and sold to the plaintiff was the cash sum paid for it. In view of this finding of the court, the case is ruled by *La Belle Iron Works v. United States* (256 U. S., 377, 387, 388, 391 [T. D. 3181, C. B. 4, 373]). These considerations dispose of this branch of the plaintiff's claim, and the action of the Commissioner of Internal Revenue is upheld as to this claim.

It follows from the foregoing that the plaintiff is not entitled to recover on any one of the three claims set forth in its petition. The petition should be dismissed, and it is so ordered.

ARTICLE 573: Deductions allowed foreign corporations.

VIII-32-4302
G. C. M. 6601

REVENUE ACT OF 1918.

Where a foreign corporation has established that it constructed or acquired vessels for transportation of men or articles contributing to the prosecution of the war, it is entitled to claim a deduction for amortization, but only to the extent that such deduction is connected with income arising from a source within the United States.

Computation of amortization deduction allowed foreign corporations.

An opinion is requested on certain questions arising under the Revenue Act of 1918 in connection with a claim for amortization as a deduction from gross income from sources within the United States.

The taxpayer is a foreign corporation engaged in rendering oceanic transportation services. It appears that during the period the United States was engaged in the prosecution of the World War, the taxpayer constructed or acquired certain vessels for the purpose of transporting men or articles contributing to the prosecution of the war, and that such transportation services were actually rendered during such war period. Not all of the vessels so constructed or acquired came into commerce with the United States during the war period. The issues presented for consideration are:

(1) Whether a foreign corporation engaged in the oceanic transportation business is entitled, as a matter of law, to claim amortization as a deduction from gross income from sources within the United States, and

(2) In the event such a deduction is authorized by the taxing statutes, how should the deduction be computed under Treasury Decision 3387 (C. B. I-2, 153), as amended by Treasury Decision 4201 (C. B. VII-2, 133), as it is retroactively applied with the approval of the Secretary of the Treasury to years prior to 1921.

(1) The pertinent provisions of the Revenue Act of 1918 are as follows:

SEC. 234. (a) That in computing the net income of a corporation subject to the tax imposed by section 230 there shall be allowed as deductions:

(8) In the case of buildings, machinery, equipment, or other facilities, constructed, erected, installed, or acquired, on or after April 6, 1917, for the production of articles contributing to the prosecution of the present war, and in the case of vessels constructed or acquired on or after such date for the transportation of articles or men contributing to the prosecution of the present war, there shall be allowed a reasonable deduction for the amortization of such part of the cost of such facilities or vessels as has been borne by the taxpayer, but not again including any amount otherwise allowed under

this title or previous Acts of Congress as a deduction in computing net income. * * *

(b) In the case of a foreign corporation the deductions allowed in subdivision (a), except those allowed in paragraph (2) and in clauses (a), (b), and (c) of paragraph (3), shall be allowed only if and to the extent that they are connected with income arising from a source within the United States; and the proper apportionment and allocation of the deductions with respect to sources of income within and without the United States shall be determined under rules and regulations prescribed by the Commissioner with the approval of the Secretary.

Since the deduction for amortization provided for by section 234(a)8 is not excepted by section 234(b), it follows that a foreign corporation is entitled to claim the deduction to the extent provided in section 234(b). The right of a foreign corporation to claim amortization under the corresponding provisions of the Revenue Act of 1921 was expressly recognized by the Bureau in Treasury Decision 3448 (C. B. II-1, 102), amending article 184 of Regulations 62.

It is therefore the opinion of this office that where a foreign corporation has established that it constructed or acquired vessels for the transportation of men or articles contributing to the prosecution of the war, it is entitled to claim a deduction for amortization, but only to the extent that such deduction is connected with income arising from a source within the United States.

(2) It is the taxpayer's contention in connection with the second issue that amortization is allowable not only upon amortizable ships engaged in commerce with the United States, but that since amortization is a general deduction it must be allowed on all amortizable ships in the taxpayer's fleet, irrespective of the fact that not all such vessels came into commerce with the United States during the war period.

The taxpayer's contention in this respect raises two questions:

(a) Whether any deduction for amortization may be taken in connection with vessels which never came into commerce with the United States, and

(b) The proper treatment of the deduction as to those vessels which did come into commerce with the United States.

(a) As to the vessels which never came into commerce with the United States during the amortization period, the taxpayer attempts to bring itself within the provision of the statute to the effect that the deduction must be connected with income from a source within the United States by contending that amortization is a general deduction to be treated in the nature of an overhead expense, and that that proportion of the amortization upon the taxpayer's entire fleet which the gross income from sources within the United States bears to the total gross income should be allowed as a deduction from gross income from sources within the United States.

With this contention this office can not agree. This office does not consider the deduction for amortization as being any more general in its nature than the other deductions allowed by section 234 of the Revenue Act of 1918. Furthermore, it seems evident that Congress by section 234(b) expressly recognized that foreign corporations should not be permitted to treat such deductions as being of a general nature, but that they must be specifically limited and allowed only to the extent that they are connected with income from sources within the United States.

The provisions of Treasury Decision 3387, as amended, hereinafter noted, specifically carry this intention into practice. That Treasury decision applies only to a foreign corporation carrying on the *business of transportation service between points in the United States and points outside the United States*. The repeated reference in the Treasury decision to "such transportation business" can therefore only mean the service between points in the United States and points outside the United States. Subdivision (4) of Treasury Decision 3387, as amended, reads as follows:

(4) If a foreign corporation subject to this article is also engaged in a business other than that of providing transportation service between points in the United States and points outside the United States, the costs and expenses (including taxes) properly apportioned or allocated to such other business should be excluded both from the deductions and from the apportionment process prescribed in (1) above; but, for the purpose of determining net income, a ratable part of any general expenses, losses or deductions which can not definitely be allocated to some item or class of gross income, may be deducted from the gross income from sources within the United States, after the amount of such gross income has been determined. Such ratable part should ordinarily be based upon the ratio of gross income from sources within the United States to the total gross income.

As this language is construed by this office, it means that where costs and expenses are incurred by a foreign corporation in carrying on commerce with any country other than the United States, such costs and expenses should be excluded entirely from both the deductions and the apportionment process prescribed in the Treasury decision, and that it is only as to the costs and expenses which can not definitely be so allocated that the ratio of gross income from sources within the United States to total gross income is to be applied. It follows that when a foreign corporation uses an amortizable vessel exclusively in commerce with countries other than the United States, the amortization upon such vessel is a cost or expense which is properly allocable to such service, and as such, should be excluded both from the deductions and from the apportionment process prescribed in Treasury Decision 3387, as amended.

This is manifestly fair. The gross income against which the basic ratio under the Treasury decision is applied is only the gross income from the transportation service between points within the United States and points outside the United States. Furthermore, the gross income from sources within the United States should not be burdened with deductions for costs and expenses incurred in and attributable to other services.

(b) With respect to the amortizable vessels which actually came into commerce with the United States, the question presented is whether the amortization should be prorated on the basis of the number of days the ships were within the territorial limits of the United States to the number of days on voyage, or whether the amortization on such vessels should be prorated on the basis of gross income from sources within the United States to total gross income from the transportation service between points within the United States and points outside the United States.

The taxpayer renews its contention that amortization can not definitely be allocated to any particular item or class of gross income and that the second alternative above mentioned should therefore be used.

Although allowance for amortization is generally considered as an extraordinary method of granting relief from excessively high war costs and high war taxes, nevertheless, it is comparable to depreciation and obsolescence. (See Holmes Federal Income Tax, 6th edition, page 1081, where amortization is defined as a kind of extraordinary depreciation or obsolescence.) Each of these deductions furnishes a method whereby the taxpayer is assured a return of his capital. The deductions are mutually exclusive, in that when a taxpayer has recovered his capital back by one method, he may not thereafter have a recovery of the same capital by the use of one of the other methods provided for by the statute. (Cf. Appeal of Jamestown Worsted Mills, 1 B. T. A., 659, C. B. IV-1, 2.) The taxpayer's contention as to the treatment of amortization is no more convincing than it would be if advanced with respect to depreciation.

Under Treasury Decision 3387, as amended, depreciation is computed on a voyage basis—that is to say, the amount of depreciation on a particular vessel for one day is first determined. This amount, multiplied by the number of days the vessel was actually within the territorial limits of the United States, constitutes the depreciation deduction allowable against gross income from sources within the United States. For the purpose of determining the basic ratio provided for in Treasury Decision 3387, as amended, the depreciation deduction so computed is included in the numerator and the depreciation for one day multiplied by the number of days the vessel was used in transportation between points in the United States and points outside the United States, i. e., the round trip voyage, is included in the denominator.

The method of determining the depreciation deduction provided for by Treasury Decision 3387, as amended, and as outlined above, is considered generally fair and equitable, and in the opinion of this office a similar method would be proper in determining the deduction for amortization upon amortizable vessels which came into commerce with the United States during the war period.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

SECTION 238.—CREDIT FOR TAXES IN CASE OF CORPORATIONS.

ARTICLE 611: Credit for foreign taxes.

REVENUE ACT OF 1921.

Computation of credit for foreign taxes of affiliated group of corporations. (See G. C. M. 6640, page 212.)

ARTICLE 611: Credit for foreign taxes.

VIII-40-4377

I. T. 2499

REVENUE ACT OF 1918.

Taxes paid to Peru on sugar exported from that country in 1918 and 1919 under laws Nos. 2143 and 2727 are export taxes rather than income taxes, and may not be claimed as a credit under section 238 of the Revenue Act of 1918.

SECTION 240.—CONSOLIDATED RETURNS OF CORPORATIONS.

ARTICLE 631: Affiliated corporations.

REVENUE ACT OF 1921.

Computation of credit for foreign taxes. (See G. C. M. 6640, page 212.)

ARTICLE 632: Consolidated returns.

VIII-36-4342
Ct. D. 101

INCOME TAX—REVENUE ACT OF 1921—DECISION OF COURT.

CONSOLIDATED RETURN—SEPARATE RETURNS—CHANGE OF BASIS—
COMMISSIONER'S DISCRETION.

Where affiliated corporations elect to file separate returns pursuant to section 240(a) of the Revenue Act of 1921, it is within the discretion of the Commissioner to refuse to allow them to file thereafter a consolidated return, and his refusal is not reviewable by the courts.

UNITED STATES CIRCUIT COURT OF APPEALS, NINTH CIRCUIT.

Alameda Investment Co., Hawley Investment Co., Pacific Nash Motor Co., appellants, v. John P. McLaughlin, Collector of Internal Revenue, California, appellee.

[June 3, 1929.]

OPINION.

RUDKIN, Circuit Judge: Throughout the year 1922 the Hawley Investment Co., the Pacific Nash Motor Co., and the Alameda Investment Co. were corporations organized and existing under the laws of the State of California. During that period Stuart S. Hawley owned or controlled substantially all of the capital stock of the Hawley company; the Hawley company owned or controlled substantially all of the capital stock of the Motor company; and Hawley and the Hawley company owned or controlled 73½ per cent of the capital stock of the Alameda company. An additional 25 per cent of the capital stock of the Alameda company was owned by members of the Meek family, related to Hawley by marriage. During the year in question the Hawley company and the Motor company suffered net losses aggregating in excess of \$250,000, while the Alameda company earned a net income in excess of \$120,000. In March of 1923 the three corporations made separate income tax returns for the year 1922, under the Revenue Act of 1921, showing losses and gain as above indicated, and upon the return of the Alameda company there was paid in taxes during the year 1923 the sum of \$15,087.72. On June 11, 1924, the three corporations applied to the Commissioner of Internal Revenue for permission to file a consolidated return of income for the year 1922, pursuant to section 240 of the Revenue Act of 1921 (42 Stat., 260), which provides:

"(a) That corporations which are affiliated within the meaning of this section may, for any taxable year beginning on or after January 1, 1922, make separate returns or, under regulations prescribed by the Commissioner with the approval of the Secretary, make a consolidated return of net income for the purpose of this title, in which case the taxes thereunder shall be computed and determined upon the basis of such return. If return is made on either of such bases, all returns thereafter made shall be upon the same basis unless permission to change the basis is granted by the Commissioner."

The Commissioner permitted the Hawley company and the Motor company to file a consolidated return, but denied the like privilege to the Alameda company, on the ground that it was not affiliated with the other two corporations within the meaning of the law. The present action was thereafter instituted

against the collector of internal revenue to recover the taxes paid by the Alameda company on its separate return, and from a judgment in favor of the defendant the plaintiffs have appealed.

It will be observed that under the Revenue Act of 1921 corporations which are affiliated within the meaning of the law may make separate returns or at their option a consolidated return, under regulations prescribed by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, and the basis upon which the return is made for the year 1922 controls in succeeding years unless permission to change the basis is granted by the Commissioner. The separate and consolidated returns differ widely in form, with different results to both the taxpayers and the Government, and it would seem obvious that when the taxpayers have once made their election, filed their returns—separate or consolidated—and paid their taxes, the election is binding on all parties concerned. We have not lost sight of the fact that the complaint-alleged that the separate returns were made through inadvertence and without knowledge that the taxpayers were entitled to make a consolidated return; but the allegation was denied by answer and no proof whatever was offered in its support. Here the Alameda company made its separate return and paid its taxes. The return was regular in form, the taxes were due the Government and were lawfully collected, and the right or power of the Commissioner of Internal Revenue to thereafter impose an obligation on either the Government or the collector to refund the taxes by permitting a complete change in the return would seem to admit of grave doubt, to say the least. But if it be conceded that the Commissioner had such power in any case, he was under no legal obligation to exercise it in behalf of the appellants, and his refusal so to do is not subject to review in the courts. Regardless, therefore, of whether the appellants might have made a consolidated return in the first instance, the judgment must be affirmed.

It is so ordered.

ARTICLE 633: When corporations are affiliated.

VIII-34-4318

Ct. D. 95

INCOME TAX—REVENUE ACT OF 1918—PROCEEDING OF COURT.

CONSOLIDATED RETURN—AFFILIATION.

Two corporations are not entitled to claim affiliation, under section 240(b)2 of the Revenue Act of 1918, where persons owning 30 per cent of the capital stock of one of the corporations own no capital stock of the other.

DISTRICT COURT OF THE UNITED STATES, DISTRICT OF MASSACHUSETTS.

Goldstein Bros. Amusement Co. v. Thomas W. White, Collector.

[July 15, 1929.]

OPINION.

MORTON, J.: This is an action at law to recover income and profits taxes alleged to have been illegally assessed and collected. It is submitted on the pleadings and a statement of agreed facts. The question is whether the plaintiff was affiliated during the tax years 1919 and 1920 with the Natsam Features Co. and the Victory Theatre Co., so that the three corporations were entitled to make a consolidated return.

Nathan E. Goldstein and Samuel Goldstein, two brothers, owned 994 shares out of 1,000 in the plaintiff company. In the Natsam company they owned 60 shares out of 100; the other 40 shares were owned by persons who stood in close personal or business relations with them. In the Victory company all the stock was owned by the Goldsteins during the year 1919 and up to 15 September, 1920; the Government concedes affiliation with the plaintiff up to that date. At that time stock was sold to the public; and thereafter to the end of the year the Goldsteins owned 68 or 70 per cent of the total stock.

The Goldsteins were managers of theatrical enterprises. The corporations here concerned were part of their general business organization and were oper-

ated and controlled by them. They made no charge for clerical or management services against either the Natsam company or the Victory company and advanced money to them from time to time without interest. They indorsed notes of the Victory company to a substantial amount. All parties interested in these corporations had confidence in the Goldsteins and left the management entirely in their hands.

The question depends on the Revenue Act of 1918, section 240(b). Under this statute affiliation exists "(1) if one corporation owns directly or controls through closely affiliated interests or by a nominee or nominees substantially all the stock of the other or others, or (2) if substantially all the stock of two or more corporations is owned or controlled by the same interests."

The Amusement company as a corporation had no stock interest or control in these other companies. The plaintiff's contention is that substantially all the stock of the Amusement company, the Natsam company, and the Victory company was owned or controlled by the same interests. The "interests" referred to are the Goldstein brothers and stockholders associated with them.

The regulations provide that "The words 'the same interests' shall be deemed to mean the same individual or partnership or the same individuals or partnerships, but when the stock of two or more corporations is owned or controlled by two or more individuals or by two or more partnerships a consolidated return is not required unless the percentage of stock held by each individual or each partnership is substantially the same in each of the affiliated corporations." (Art. 633, Regulations 45.) Applying this test to the Natsam company, the Goldstein brothers did not own more than 60 per cent of its stock, and the other stockholders owned no stock (practically speaking) in the Amusement company. In the Victory company, after 15 September, 1920, the Goldsteins owned directly or through the Amusement company 68 or 70 per cent of the stock; the other 30 or 32 per cent of the stockholders had no interest in the Amusement company. Evidentially the same interests, as defined by the regulations did not own substantially all the stock of both corporations in the case either of the Natsam company and the plaintiff or of the Victory company and the plaintiff. As to what is meant by "control" of stock under this statute there has been a difference of judicial opinion. In the *Great Lakes Hotel Co. v. Commissioner* (30 F. (2d), 1, C. C. A. 7th), the test is thus stated: "They (the corporation) were guided in their action by a common interest and their common object was attained by all corporations pursuing the same methods through the same agencies. In addition to owning more than one-half of the stock, these 'closely affiliated interests' controlled other stock." (Evans, J.; 30 F. (2d), at 4.) The relations between the Goldsteins and the minority stockholders in the Natsam company and the Victory company were of such character that under the principle of this decision the companies were in my opinion affiliated.

In the second circuit the statute has been differently interpreted. "The test is not declared to be control of the business or the policies of the subsidiary corporation, but substantial identity of interest in the enterprise. The theory of affiliation, resulting in a consolidated return for taxes, is that the income and invested capital are really the income and capital of a single enterprise, though carried on through the instrumentality of several corporations. (Citing authorities.) Only when the outside interest—that is, the interest of the minority—is so small as to be practically negligible are the two corporations to be treated as in receipt of a single income, requiring a consolidated return." (Swan, J.; *Ice Service Co. v. Com'r.*, 30 F. (2d), 230 at 231.) "The management of the business of the corporation is not the control required by the statute. It refers to stock control. The fact that the minority is acquiescent, and permits the majority to manage the business, does not prove actual control over the minority interest. Nor does a control based upon friendship or professional relations satisfy the statute. The control of the stock owned by the same interest refers to beneficial interest." (Manton, J.; *Com'r. v. Hirsch*, 30 F. (2d) at 646 [Ct. D. 86, C. B. VIII-1, 267].)

In my opinion, the Ice Service Co. and the Hirsch cases represent the correct view of the statute. If so, there was clearly no affiliation between the plaintiff and the Natsam company for either of the years in question, nor between the plaintiff and the Victory company for the period from 15 September, 1920, to 31 December, 1920. There was affiliation between the plaintiff and the Victory company through the year 1919 and during the year 1920 to September 15.

Judgment accordingly.

ARTICLE 633: When corporations are affiliated.

VIII-39-4371

Ct. D. 112

EXCESS PROFITS TAX—REVENUE ACT OF 1917—DECISION OF COURT.

1. CONSOLIDATED RETURN—AUTHORITY OF COMMISSIONER.

The Commissioner is authorized by the Revenue Act of 1917 to require a consolidated return of affiliated corporations for the purpose of the excess profits tax. The Act, as so interpreted by the Commissioner and as so construed by section 1331 of the Revenue Act of 1921, is constitutional.

2. SAME—AFFILIATION.

Where a corporation engaged in the manufacture and sale of candy owns 94.33 per cent of the stock of another corporation which produces and supplies corn sirup, an essential portion of its raw material, the two corporations are affiliated within the meaning of the Revenue Act of 1917 as construed by section 1331 of the Revenue Act of 1921.

3. SUIT—CLAIM FOR REFUND.

The precise ground upon which the refund of taxes is demanded must be stated in the application to the Commissioner and a suit in court to recover the tax can not be based upon an entirely different and distinct ground from that presented to the Commissioner.

COURT OF CLAIMS OF THE UNITED STATES.

National Candy Co. v. The United States.

[February 4, 1929.]

OPINION.

Moss, Judge, delivered the opinion of the court.

Plaintiff, National Candy Co., was organized in 1902 and was engaged in the manufacture and sale of candy. In 1906 plaintiff organized the Clinton Sugar Refining Co. (now called the Clinton Corn Syrup Refining Co.) and acquired \$566,000 of the \$600,000 in par value of the common stock of same. Plaintiff and the Clinton Sugar Refining Co. filed separate tax returns for the calendar year 1917. The Commissioner of Internal Revenue determined that during that year the two companies were affiliated within the meaning of the War Revenue Act of 1917 and the regulations promulgated thereunder, and computed and assessed the excess-profits tax for 1917 against the two corporations on a consolidated basis, which resulted in the payment by plaintiff of an additional tax. Claim for refund was duly filed and was rejected. This action is for the recovery of the additional tax.

Section 201, Title II, of the Revenue Act of 1917 (40 Stat., 303), which is the Act creating the excess-profits tax, contains the following provision:

"For the purpose of this title every corporation or partnership not exempt under the provisions of this section shall be deemed to be engaged in business, and *all the trades and businesses in which it is engaged shall be treated as a single trade or business, and all its income from whatever source derived shall be deemed to be received from such trade or business.*" [Our italics.]

Under authority expressly provided in this Act the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, promulgated certain regulations for the administration of the Act. Article 77 of said regulations provides that every corporation shall describe in its returns all its intercorporate relationships with other corporations, and will furnish such information in relation thereto as will enable the Commissioner of Internal Revenue to properly compute the tax on the basis of an equitable accounting. It also provides that "For the purpose of this regulation two or more corporations will be deemed to be affiliated (1) when one such corporation owns, directly or controls through closely affiliated interests or by a nominee or nominees, all or *substantially all* of the stock of the other or others, or when

substantially all of the stock of two or more corporations is owned by the same individual or partnership, and both or all of such corporations are engaged in the same or a closely related business; * * *." [Our italics.] Article 78 authorizes the Commissioner to require the filing of consolidated returns of net income and invested capital whenever necessary to more equitably determine the invested capital or taxable income, and it further provided that if such corporations, when requested to file such consolidated returns, shall neglect or refuse to do so, the Commissioner may cause an examination of the books of such corporations to be made and a consolidated statement to be made therefrom. In cases where the consolidated returns are accepted, the total tax will be computed as a unit upon the basis of the consolidated return, and will be allocated to the respective affiliated companies in such portions as may be agreed among them. But if no such agreement is made, the tax will be assessed by the Commissioner upon each such corporation in accordance with the net income and invested capital properly assignable to it.

It was under the authority of these regulations that the Commissioner determined that the two companies involved herein were affiliated. We are unable to agree with plaintiff's contention that articles 77 and 78 were unauthorized, because contrary to the provisions of the statute. It is a well-established rule that a departmental regulation will be upheld unless, in the judgment of the court, it is "plainly and palpably inconsistent with law." (*Boske v. Comingore*, 177 U. S., 459.) It can not reasonably be contended that the regulations in question requiring consolidated returns by affiliated corporations were inconsistent with the provisions of the Act of 1917. On the contrary, such regulations appear to be entirely appropriate for the ends and purposes of said Act. Furthermore, it should be noted that the interpretation of the Act by the Commissioner of Internal Revenue, as expressed in the foregoing regulations, was approved by Congress in the subsequent enactment of the Revenue Act of 1918, which embodied in its terms the essential requirements and provisions of said regulations. (40 Stat., 1081, 1082.) It will further be observed that by the Revenue Act of 1921, section 1331(c) (42 Stat., 319), Congress again incorporated the requirements and provisions of said regulations, and provided that "The provisions of this section are declaratory of the provisions of Title II of the Revenue Act of 1917." The theory of consolidated returns by affiliated corporations is now a well-established principle of our taxing system. It is not an attempt, as plaintiff urges, to assess a tax against one taxpayer measured by the income of another taxpayer. The principle upon which it is based is succinctly stated in article 631 of Treasury Regulations 69, as follows:

"Consolidated returns are based upon the principle of levying the tax according to the true net income of a single enterprise, even though the business is operated through more than one corporation. Where one corporation owns the capital stock of another corporation or other corporations, or where the stock of two or more corporations is owned by the same interests, a situation results which is closely analogous to that of a business maintaining one or more branch establishments. In the latter case, because of the direct ownership of the property, the net income of the branch forms a part of the net income of the entire organization."

The constitutionality of the requirement for consolidated returns by affiliated corporations, as provided by the Revenue Act of 1918, was upheld in the case of *United States v. Whyel* (19 Fed. (2d), 260), wherein the court said: "There is no question as to the right of two or more corporations to become affiliated, and, where such relations are voluntarily assumed by the companies, there would appear no valid objection to the application of the statute, as the total tax is computed as a unit. The authority to distribute the tax equitably is vested in the corporations themselves, and it is by no means apparent that any hardship or injustice can result from such an arrangement."

We conclude, therefore, that the Act of 1917, as interpreted by the Commissioner and as construed by section 1331 of the Act of 1921, is not in violation of the Constitution of the United States in any respect.

Plaintiff owned 94.33 per cent of the stock of the Clinton Sugar Refining Co. That this percentage brings the case within the meaning of the term "substantially all," in the light of the authorities, scarcely needs argument. In *Mahoning Coal Railroad Co.* (4 B. T. A., 923), a holding of 81 per cent of stock was held sufficient, and in *Watsontown Brick Co.* (3 B. T. A., 85), a holding of 93.6 per cent was determined to be sufficient. There are numerous other decisions to the same effect.

With regard to the question as to whether or not plaintiff and the Clinton Sugar Refining Co. were, in 1917, engaged in the same or a "closely related business," it must be remembered, in the first place, that plaintiff itself organized the Clinton Sugar Refining Co. in 1906 to meet a situation which at that time was threatening serious embarrassment to plaintiff in the matter of supply of corn sirup. The "Corn Products Refining Co." at that time had a monopoly on the production of corn sirup, which is one of the principal ingredients in the manufacture of candy, constituting 16 per cent in value of the total of raw materials used in such manufacture. There were also rumors that said Corn Products Refining Co. was endeavoring to secure control of the important users of corn sirup. In these circumstances plaintiff was unable to obtain prompt and satisfactory supplies of corn sirup, and determined upon the policy of manufacturing its own supply of that material; and it was to effectuate that purpose that plaintiff organized the Clinton Sugar Refining Co. It will also be noted that the officers and directors of the two companies were the same, and they held the same relative positions in each company, except that the Clinton Sugar Refining Co. had two vice presidents, only one of whom was vice president in plaintiff's company, and plaintiff had four directors, only three of whom were directors in the Clinton Sugar Refining Co. Plaintiff company, as stated above, owned 94.33 per cent of the stock. It is impossible to conceive of a more striking example of a "closely related business" than that which is afforded by the facts in the instant case. And the fact that the Clinton Sugar Refining Co., organized by plaintiff for the purpose of supplying an essential ingredient for the production of candy, and managed and controlled by the same officers, developed a capacity for the production of a much larger supply of the raw material than was needed by plaintiff, and was able to engage in a profitable business with the outside trade, does not affect the principle. In legal effect, the relationship between the corporations remains precisely the same as if the original purpose of supplying plaintiff's own needs for corn sirup had been adhered to. Inasmuch as the purpose of the organization and operation of the Clinton Sugar Refining Co. was, in a large part, to produce and supply an essential portion of plaintiff's raw material, it is not merely a "closely related business," but might logically be construed as a part of the same business.

Plaintiff makes the further contention that there should have been added to its invested capital, as an alleged organization expense, the sum of \$385,000. This contention is not supported by the record. The entire common stock of plaintiff company was carried on the books of the company as good will. Two of the items contained in the good will account were as follows:

To promoter.....	\$324,500
To purchasers of first preferred stock, as bonus.....	1,465,500

The first item of \$324,500 represents a block of common stock, of the actual value of \$64,900, which was issued to one Edwin Carbin for services in promoting the organization of the National Candy Co. The second item of \$1,465,500 represents a block of the common stock of the actual value of \$293,100, which was issued to the Mississippi Valley Trust Co., *as a bonus*. This company paid to plaintiff the sum of \$1,000,000 in cash, and received therefor all of the first preferred stock issued by plaintiff company, together with the block of common stock mentioned above. These two issues of common stock were of the value of \$20 a share, or a total of \$358,000. Plaintiff contends that these two items represent organization expenses and should be added to invested capital. It will first be noted that the items are different in character. The stock issued to Edwin Carbin was for services in the promotion and organization of plaintiff company, while as to the other item, the Mississippi Valley Trust Co., which had underwritten the first preferred stock of plaintiff company, amounting to \$1,000,000, paid that amount in cash for all of said preferred stock, which was issued and delivered to said company, together with a *bonus* of the common stock of the actual value of \$293,100. It is not made to appear that any part of said stock was issued in consideration of promotion services. Assuming, however, that both items represent a total organization expense of \$358,000 as contended, the elimination of that sum from the good will account, and the addition of same to organization expense, would not affect the amount of invested capital. However, plaintiff can not recover on this item, for the reason that same constituted no part of the claims for refund presented by plaintiff. In the case of *Tucker v. Alexander*

(15 Fed. (2d), 356, 275 U. S., 228 [T. D. 3973, C. B. VI-1, 287]) the circuit court said:

"The evident purposes and objects of this condition (filing of claim) are to afford the Commissioner an opportunity to correct errors made by his office and to spare the parties and the courts the burden of litigation in respect thereto. Unless the claimant were required to present to the Commissioner *all* of the grounds upon which he relies for refund, the above purposes and objects would be partially or entirely defeated." [Our italics.]

While this case was reversed by the Supreme Court on the ground that the failure to state the ground in the claim for refund had been waived, the principle announced by the circuit court, as above quoted, remains unaffected. In the case of *Red Wing Malting Co. v. Willcuts* (15 Fed. (2d), 626 [T. D. 3980, C. B. VI-1, 225]), in which certiorari was denied, the same court said:

"The *precise* ground upon which the refund is demanded *must be stated in the application to the Commissioner*, and we think if that is not done, a party can not base a recovery in the court upon an entirely different and distinct ground from that presented to the Commissioner." [Our italics.]

It is further contended by plaintiff that the Commissioner failed to properly allocate the excess-profits tax between plaintiff and the Clinton Sugar Refining Co. This particular question was brought to the attention of plaintiff in a letter from the defendant, dated March 27, 1920, in which it is stated:

"In the absence of specific instructions as to how you desire to allocate the excess-profits tax, the entire excess-profits tax is credited to the consolidated income and the additional tax found due, charged to you. In this case any adjustment desired may be made between the companies on your books."

No objection whatever was made to this suggestion, nor was there any request for a different allocation, and no complaint was presented to the Commissioner in any claim for refund. Plaintiff is therefore precluded from asserting same at this time. See *Tucker v. Alexander* and *Red Wing Malting Co. v. Willcuts*, above cited.

We have reached the conclusion that the action of the Commissioner in determining that the two companies involved herein were affiliated in the year 1917, and in computing and assessing the tax accordingly, was correct. The petition will therefore be dismissed.

ARTICLE 633: When corporations are affiliated.

VIII-42-4400
Ct. D. 121

INCOME TAX—REVENUE ACT OF 1918—DECISION OF COURT.

CONSOLIDATED RETURN—AFFILIATION—CONTROL.

Where a corporation owns 80 per cent of the capital stock of another and has an agreement with the remaining stockholder that he will not sell his shares to outside interests without first offering them to it, the corporation does not own or control substantially all the stock of the other so as to authorize affiliation under section 240(b)1 of the Revenue Act of 1918.

COURT OF CLAIMS OF THE UNITED STATES.

Wadhams & Co. v. The United States.

SPECIAL FINDINGS OF FACT.

I.

The plaintiff, Wadhams & Co., is a corporation organized under the laws of the State of Oregon.

II.

During the year 1922 and prior years the plaintiff company was engaged in the wholesale grocery business and also in the manufacturing business. During 1918 the plaintiff company organized the Perfection Manufacturing Co., a corporation, for the manufacture of ice-cream cones, and took over all of its stock,

for which it paid cash and tangible assets. Prior to 1918 it gave 20 per cent of the stock of the Perfection Manufacturing Co. to one Ben Opitz in consideration of his services as an inventor, retaining 80 per cent of the stock of that company. Opitz represented himself as being an inventor and an expert mechanic and he was to develop certain machinery and certain patents which he was at that time working on. He was also to further the interests of the Perfection Manufacturing Co., and to assist in making it a financial success. There was an agreement in writing between Opitz and the taxpayer, Wadhams & Co., whereby Opitz agreed not to sell his stock to outsiders without first offering it to Wadhams & Co. In September, 1918, Opitz left the employ of the Perfection Manufacturing Co., because his plans had not materialized and his ideas had not worked out successfully and because the corporation had no further use for his services. He did not offer his stock to Wadhams & Co. and Wadhams & Co. had made no effort to secure it and it continued to stand in the name of Opitz.

III.

The plaintiff, Wadhams & Co., for the year 1920 filed a consolidated income tax return, including therein the income of the Perfection Manufacturing Corporation. During 1920 the Perfection Manufacturing Co. had sustained a loss of \$13,514.01; which loss reduced the amount of the consolidated net income of the two companies to that extent. The Commissioner of Internal Revenue held that the companies were not affiliated within the meaning of the Act of 1920 and that Wadhams & Co. should file a separate return, thus increasing its income to the extent of \$13,514.01.

IV.

During the year 1920, Wadhams & Co. owned 80 per cent of the stock of the Perfection Manufacturing Co. The remaining 20 per cent of the stock was that which had been given to Ben Opitz by Wadhams & Co. and was still held by him under the agreement whereby he was not to sell the stock to outsiders without first offering it to Wadhams & Co. Opitz was not employed by the Perfection Manufacturing Co. during 1920. He did not offer his stock to the corporation, and the corporation made no effort to secure it. The stock of the Perfection Manufacturing Co. was of no value in 1920, for Wadhams & Co. had advanced to the Perfection Manufacturing Co. all moneys required by the Perfection Manufacturing Co. for the original acquisition of the machinery needed by them in the operation, as well as all money needed subsequently to the extent of \$35,531.72 before the end of 1920, which had not been repaid and which considerably exceeded the value of the tangible assets of the Perfection Manufacturing Co. During the year 1920, the Perfection Manufacturing Co. was operated as a department of Wadhams & Co. The officers of the Perfection Manufacturing Co. were all selected by Wadhams & Co. or its directing officials. The Perfection Manufacturing Co. occupied a building owned by Wadhams & Co.; it occupied no other quarters, and rent was not charged by Wadhams & Co. Products of the Perfection Manufacturing Co. were marketed by Wadhams & Co., involving the employment of some 25 salesmen and practically the entire time of a sales manager of Wadhams & Co. No charge was made against the Perfection Manufacturing Co. by Wadhams & Co. for this expense involved in marketing its products except \$25 a month paid to the secretary of the Perfection Manufacturing Co. by Wadhams & Co. The by-laws of the Perfection Manufacturing Co. provided for the decision of any question arising at a stockholders' meeting by a majority of the stockholders present.

V.

September 15, 1924, the Commissioner of Internal Revenue found an additional tax liability of \$1,351.40 against Wadhams & Co. for 1920, growing out of the disallowance of the affiliated status. From this decision the plaintiff duly appealed November 12, 1924, to the United States Board of Tax Appeals. September 9, 1925, the United States Board of Tax Appeals approved the determination of the Commissioner. Thereafter, upon demand, the plaintiff on December 11, 1925, paid the sum of \$1,351.40 to the collector of internal revenue at Portland, Oreg. Claim for refund of the same was duly filed May 15, 1926, and was rejected by the Commissioner of Internal Revenue July 15, 1926.

VI.

The plaintiff has at all times borne true allegiance to the Government of the United States and has not in any way aided, abetted, or given encouragement to rebellion against said Government. It is the sole and absolute owner of the claim herein presented and has made no transfer or assignment of said claim or any part hereof.

CONCLUSIONS OF LAW.

Upon the foregoing special findings of fact, which are made part of the judgment herein, the court decides, as a conclusion of law, that plaintiff is not entitled to recover and its petition is therefore dismissed.

Judgment is rendered against the plaintiff in favor of the United States for the cost of printing the record in this case, the amount thereof to be ascertained by the clerk and collected by him according to law.

[March 11, 1929.]

OPINION.

GREEN, Judge, delivered the opinion of the court.

The facts in the case are clearly and briefly stated in the findings. The case involves the construction of section 240 of the Revenue Act of 1918 (40 Stat., 1057), and particularly that portion thereof which reads as follows (p. 1082) :

"(b) For the purpose of this section two or more domestic corporations shall be deemed to be affiliated (1) if one corporation owns directly or controls through closely affiliated interests or by a nominee or nominees substantially all the stock of the other or others, * * *."

The plaintiff did not "own directly or control through closely affiliated interests" or otherwise "substantially all the stock" of the Perfection company. Optitz owned 20 per cent of it and was under no obligations to sell it to the plaintiff. In fact, he did not even offer to sell it, nor did the plaintiff endeavor to buy it. True, the plaintiff managed the business of the Perfection company and controlled its operations, but in order to come within the provisions of the statute the control must be of substantially all the *stock*, and we think there were reasons for this language. The Boston Structural Steel Co. case (1 B. T. A., 1004) is not an authority to the contrary. In that case there was control of all the stock through a right to purchase at any time at a fixed price.

The cases deciding what corporations are affiliated are very numerous, but no definite rule can be derived from them. In fact, they can not be entirely harmonized. The ultimate conclusion is that the decision must depend largely on the particular facts in the case under consideration.

We think the petition should be dismissed, and it is so ordered.

ARTICLE 636: Consolidated net income of affiliated corporations.

VIII-26-4253
G. C. M. 6223

REVENUE ACT OF 1918.

No part of the compensation received by a subsidiary from the parent for transportation services rendered by the subsidiary for the parent may be allowed as a deduction under section 23, Merchant Marine Act.

An opinion is requested as to the proper computation in the case of the M Company of such deduction as may be allowable under section 23 of the Merchant Marine Act, 1920 (41 Stat., 997), for the purpose of computing net income subject to the profits taxes imposed by the Revenue Act of 1918.

Section 23 of the Merchant Marine Act provides as follows:

That the owner of a vessel documented under the laws of the United States and operated in foreign trade shall, for each of the 10 taxable years while so operated, beginning with the first taxable year ending after the enactment of this Act, be allowed as a deduction for the purpose of ascertaining his net income subject to the war-profits and excess-profits taxes imposed by Title III of the Revenue Act of 1918 an amount equivalent to the net earnings of such vessel during such taxable year, determined in accordance with rules and regulations to be made by the board: *Provided*, That such owner shall not be entitled to such deduction unless during such taxable year he invested, or set aside under rules and regulations to be made by the board in a trust fund for investment, in the building in shipyards in the United States of new vessels of a type and kind approved by the board, an amount, to be determined by the Secretary of the Treasury and certified by him to the board, equivalent to the war-profits and excess-profits taxes that would have been payable by such owner on account of the net earnings of such vessels but for the deduction allowed under the provisions of this section: *Provided further*, That at least two-thirds of the cost of any vessel constructed under this paragraph shall be paid for out of the ordinary funds or capital of the person having such vessel constructed. * * *

At all times during the taxable year 1920 the O Company (hereinafter called the parent corporation) owned 100 per cent of the shares of the capital stock of the M Company (hereinafter called the subsidiary corporation). The parent corporation and the subsidiary corporation were accordingly affiliated within the meaning of section 240, Revenue Act of 1918, and articles 631 and 637, Regulations 45 (1920 edition), and were required to, and did, file a consolidated return thereunder. Both the parent corporation and the subsidiary corporation regularly employed the accrual method of accounting in keeping their books. The subsidiary corporation, during the taxable year 1920, owned a vessel or vessels documented under the laws of the United States and operated in foreign trade. The subsidiary corporation "invested [or otherwise set aside] * * * an amount * * * equivalent to the war-profits and excess-profits taxes [for the taxable year 1920] that would have been payable by such owner on account of the net earnings of such vessels but for the deduction allowed" under section 23 of the Merchant Marine Act. The subsidiary corporation, during the taxable year 1920, transported for the parent corporation sundry products in the said vessel or vessels documented under the laws of the United States and operated in foreign trade, and as a result thereof certain earnings accrued to the subsidiary corporation for the services.

Under these facts the issue is raised whether a deduction is allowable under section 23, Merchant Marine Act, of the amount of the earnings accrued to the subsidiary corporation during the taxable year 1920 for transportation services rendered by it to the parent corporation through the medium of vessels owned by the subsidiary corporation which were documented as American vessels and operated in foreign trade.

Article 631, Regulations 45 (1920 edition), provides:

The provision of the statute requiring affiliated corporations to file consolidated returns is based upon the principle of levying the tax according to the true net income and invested capital of a single business enterprise, even though the business is operated through more than one corporation. * * *

Article 637, Regulations 45 (1920 edition), provides:

Subject to the provisions covering the determination of taxable net income of separate corporations, and subject further to the elimination of intercompany transactions, the consolidated taxable net income shall be the combined net

income of the several corporations consolidated, except that the net income of corporations coming within the provisions of article 635 shall be taken out. In respect of the statement of gross income and deductions and the several schedules required under Form 1120, a corporation filing a consolidated return is required to prepare and file such statements and schedules in columnar form to the end that the details of the items of gross income and deductions for each corporation included in the consolidation may be readily audited.

And see, generally, section 240, Revenue Act of 1918.

The payment of, or agreement to pay, compensation for the rendition by the subsidiary of transportation services to the parent was clearly an intercompany transaction. Its elimination pursuant to article 637, *supra*, precluded the amount thereof from becoming a part of the net income of the subsidiary corporation shown in the consolidated return. It follows that the amount thereof never became a part of the consolidated net incomes of the parent and the subsidiary. Therefore, no part thereof was subject to tax under the provisions of the Revenue Act of 1918 or the regulations prescribed pursuant thereto. The taxpayer contends nevertheless that it is entitled to deduct from the consolidated net income of the affiliated corporations the full amount of the net earnings of the subsidiary from the transportation services rendered to the parent. The contention is without merit.

To allow a deduction in respect of such earnings would be to allow a double deduction; first, through the elimination of intercompany transactions and, second, under section 23 of the Merchant Marine Act. Did Congress intend through a double deduction twice to exempt the owner from taxation as to the earnings of its American ships operated in foreign trade? As in double taxation, Congress must clearly express its intention so to do. (See *United States v. Ludey*, 274 U. S., 295 (T. D. 4046, C. B. VI-2, 157) (double deduction); *Crocker v. Malley*, 249 U. S., 223; *Hellmich v. Hellman*, 276 U. S., 233; *Patton v. Brady*, 184 U. S., 608; *Cream of Wheat Co. v. Grand Forks*, 253 U. S., 325 (double taxation).) There is nothing in the language of section 23 upon which can be predicated any such intention. On the contrary, section 23 speaks explicitly of "the war-profits and excess-profits taxes that would have been payable by such owner on account of the net earnings of such vessels but for the deduction allowed under the provisions of this section." The conclusion necessarily follows that if there are no earnings which would be subject to tax but for the deduction allowed by section 23 of the Merchant Marine Act, there can be no deduction under that section.

It has already been noted that under article 637, *supra*, all intercompany transactions are eliminated, thus effectuating the principle announced in article 631, *supra*, that the tax in the case of affiliated corporations should be levied "according to the true net income and invested capital of a single business enterprise, even though the business is operated through more than one corporation." As was said in General Counsel's Memorandum 2817 (C. B. VI-2, 23), an intercompany transaction is "productive of neither taxable gain nor deductible loss in computing the consolidated income of the affiliated group." The expenses to the subsidiary of the transportation services rendered by it to the parent are, of course, reflected in the consolidated net income, but they are there reflected as expenses of the single business enterprise carried on, the consolidated net income of

which is computed. The profits accrued to the affiliated group and entering into the consolidated net income are invariably profits from the sale or disposition of the article transported (dealings in the property with persons outside the affiliation); they are not profits arising from transportation and are not earnings of the vessels as such at all. As respects a single corporation transporting for itself products produced, manufactured, or processed by it, in so far as there is any increment as respects transportation in its vessels by the owner in comparison with transportation by another person, the increment is a saving—neither profits nor earnings—and hence never chargeable to tax as income. (Cf. Appeal of Anderson & Co., 6 B. T. A., 713.) The result in the case of transportation by one of an affiliated group for another (transportation by the subsidiary for the parent) under the principles of articles 631 and 637, *supra*, is in all substance the same. Transportation by the subsidiary results in a saving to the affiliated group, but it does not result in earnings, profits, or income as such, and hence there is nothing to be charged to tax.

Under the regulation-making power conferred upon the United States Shipping Board by section 23, it has prescribed that:

For the purposes of this section and until other rules and regulations are promulgated by the United States Shipping Board, the "net earnings" of vessels for the taxable year involved shall be determined in accordance with rules and regulations of the Bureau of Internal Revenue for the determination of net income, for income tax purposes generally. (Article 1, paragraph 7, rules and regulations relating to section 23 of the Merchant Marine Act, 1920, adopted by the United States Shipping Board June 13, 1922.)

The principles enunciated by, and consistently applied under, section 240, Revenue Act of 1918, and articles 631 to 637, inclusive, Regulations 45 (1920 edition), as to the computation of consolidated net income must, therefore, be applied under section 23, Merchant Marine Act.

Accordingly, in the opinion of this office, no part of the compensation received by the subsidiary from the parent for transportation services rendered by the subsidiary corporation to the parent corporation may be allowed as a deduction under section 23 of the Merchant Marine Act.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

PART IV.—ADMINISTRATIVE PROVISIONS.

SECTION 250.—PAYMENT OF TAXES.

ARTICLE 1011: Compromise of tax cases.

VIII-36-4340
Ct. D. 99

FEDERAL TAXES—COMPROMISE—DECISION OF COURT.

COMPROMISE—SUIT—DEFENSE—NULLIFYING PROVISION.

Where a taxpayer "in order to compromise and settle all controversies, claims, and liabilities" offers, pursuant to section 3229 of the Revised Statutes, to pay an amount "in full settlement and compromise" of all civil and criminal liabilities in connection with

taxes, which offer is duly accepted by the authorized officers of the Government, the executed compromise agreement precludes a recovery of any part of the taxes alleged to have been illegally collected. A provision added to the letter and offer of the taxpayer that "neither this offer of compromise, nor any payment made or action taken thereunder, shall be used as an admission by, or offer in evidence against, Herbert Du Puy * * * in any future action or proceeding of any nature whatsoever" is repugnant to the main purpose of the compromise agreement and is nugatory and unenforceable.

COURT OF CLAIMS OF THE UNITED STATES.

Herbert Du Puy v. The United States.

[April 1, 1929.]

OPINION.

GREEN, Judge, delivered the opinion of the court.

This action is a suit to recover income taxes alleged to have been wrongfully assessed against the plaintiff for the years 1916, 1917, 1918, and 1919, as a deficiency. The plaintiff paid the amount of the deficiency assessment, filed a claim for refund, and asks judgment for the amount paid. The defendant pleads full settlement and compromise of the taxes involved, and also that the taxes were due and rightfully collected from the plaintiff.

The assessments involved grew out of transactions which the plaintiff had with certain corporations and for the most part pertained to income from property which the plaintiff had transferred to them without consideration. As far back as 1908, plaintiff and his wife, both of whom possessed great wealth, contemplated providing their four children with independent means and incomes by means of transfers of property to them directly, or to corporations for their use and benefit. In pursuance of this purpose, large amounts of property were transferred without consideration directly to their children, or to corporations created or controlled by the plaintiff. In the years 1917, 1918, and 1919 property which had a market value of nearly \$12,000,000 was transferred to three corporations controlled by the plaintiff, the stock of which, however, eventually was held by the children. The total amount transferred to these corporations from 1908 to 1920 approximated \$25,000,000 in value.

The particular assessments that are in controversy are set out in Finding XIX, and they apply to the taxes of 1916, 1917, 1918, and 1919. An examination of the statements with reference to the taxes in controversy contained in this finding will show that they were made chiefly upon income derived from property which the plaintiff had transferred to these corporations consisting of dividends, interest, and rentals; also profits on the sale of stocks and securities held by these corporations and obtained from the plaintiff or claimed to be his property, the theory of the Government officials being that the transfers made by plaintiff were not in good faith and were invalid for that reason, or, at least, that the property had been transferred to corporations which were controlled by him and used after the enactment of the Federal income tax for the purpose of evading its provisions. There was also a claim on behalf of the Government that interest which was paid to these corporations by the plaintiff on money alleged to have been borrowed from them was not in fact paid, and therefore the deduction which plaintiff had taken in his income tax by reason thereof was disallowed; and the Commissioner also disallowed a deduction made by plaintiff in his return for 1919 on account of a loss alleged to have been sustained on a sale by him of bonds for a small sum at public auction to one of these corporations controlled, as before stated, by himself. In short, the Government contended that all of these transactions set out in Finding XIX as being in dispute were part of a fraudulent scheme of the plaintiff to defeat the Government in the collection of income taxes justly due from him for the years named. In support of their respective contentions as to the facts, the plaintiff and defendant introduced at great length both oral and documentary evidence, the latter largely in the form of account-book entries. It would require too much space to even summarize this evidence. The plaintiff paid all of the taxes specified in Finding XIX as being in dispute, together with a penalty thereon, at the time of entering into a contract with the defendant, which the defendant alleges was in full settlement of all

of the additional taxes and penalties assessed against plaintiff and his wife. Subsequently, and within the time prescribed by the statute of limitations, he filed a claim for refund of the whole amount of additional taxes and penalty paid for his own account. He now vigorously insists that he acted in good faith in all of the transactions involved, and that none of these additional taxes or penalties were due and owing from him at the time they were paid. Having within the period of limitations filed a claim for refund, he now asks judgment for the whole amount paid for taxes and penalties assessed against him at the time of the alleged settlement, which he insists is not binding upon him. The respective contentions of the plaintiff and the defendant with respect to the separate items of assessments present numerous questions of law and fact which in many instances are inextricably mingled.

The plaintiff had a right to give his property to his children or to a corporation for their benefit, either as stockholders or otherwise, and thereafter the income from the property transferred could not be rightfully assessed against him. It was only necessary that the transfers should be in good faith and that the corporations should not be used as a device for enabling the plaintiff to escape income taxes while he in fact kept control and had the use of the property. It would have been perfectly easy for the plaintiff to have so conducted these transactions and to have had the accounts so kept on his own books and the books of the corporations as to demonstrate that the transfers were made in good faith and without any purpose to play fast and loose with the Government if such was the fact. Either through misfortune or design in many instances this was not done, and his oral testimony is so general in its nature that it affords little assistance in explanation of the transactions which are attacked by the Government. On the other hand it must be said that there are some of them which need no explanation, as they afford no basis for any claim of fraud or illegality.

We do not, however, find it necessary to review the voluminous testimony offered and analyze the indefinite and involved entries that appear on the account books with reference to these transactions in order to determine whether, as counsel for defendant contend, the plaintiff was not acting in good faith with reference to certain of these transfers and other transactions in connection with the corporations, and whether they, or some of them, were in fact made or entered into for the purpose of defrauding the Government, and had in law that effect. In any event, as stated in the letters hereinafter mentioned, a controversy arose between plaintiff and the defendant as to the validity of the assessments and taxes involved herein and a contract was entered into between the parties, the terms of which control the decision in the case, as will be shown hereinafter.

The plaintiff and defendant entered into an agreement for full settlement and compromise of the taxes involved in the case by and through an offer contained in a letter dated November 9, 1920, addressed to the collector of internal revenue at Pittsburgh, Pa., by the plaintiff, a copy of which is set out in Finding XV, and an acceptance thereof contained in a reply to this letter dated November 12, 1920, signed by the Commissioner of Internal Revenue. The plaintiff, however, contends that by reason of a provision included in his letter and offer, no evidence thereof can be received or considered by the court. It must be conceded that if the next to the last paragraph of the letter of plaintiff is applied literally the plaintiff's objection to any evidence of a settlement or a payment thereunder, or anything done in relation thereto, must be sustained, and the situation is as if the contract and agreement had never been executed. The terms of this paragraph are broad and sweeping, and are as follows:

"Neither this offer of compromise, nor any payment made or action taken thereunder, shall be used as an admission by, or offer in evidence against, Herbert Du Puy, Amy H. Du Puy, Morewood Realty Holding Co., Lansing Realty Holding Co., or Goodwin Sand & Gravel Co., or their successor or successors, or representatives, or any of them, in any future action or proceeding of any nature whatsoever."

We think it needs no argument to prove that a so-called settlement of which no evidence can be given, either in writing or orally, on behalf of one of the parties thereto, is in fact no settlement at all, and if this paragraph must control the decision of the court, defendant's plea of settlement at once comes to an end. But as this provision completely nullifies the former provisions in plaintiff's letter containing the offer to pay \$1,972,016.81, which was made "in order to compromise and settle all controversies, claims, and liabilities," and

"in full settlement and compromise" of all civil and criminal liability in connection with taxes for the years 1916, 1917, 1918, and 1919, it becomes necessary to consider whether such a provision in a contract of settlement is enforceable.

In this connection it should be kept in mind that the parties had been for some months endeavoring to effect a settlement of the taxes in question, and frequent conferences between them had been held; and that finally a basis of agreement had been found and the parties came to a mutual understanding that the taxes and penalties assessed against plaintiff and his wife, Amy H. Du Puy, could be settled for the amount stated above. In fact, if oral evidence is admissible with relation to the payment and the terms thereof, the oral evidence of the settlement is abundant; but as the provision under consideration excludes any evidence of payment, the oral evidence, if this provision be followed, is incompetent, and on account of the requirements of the statute with reference to settlements, it may be that it could not be used in any event.

The question involved has often been considered by the courts, with, so far as we have been able to ascertain, perfect unanimity of opinion with reference to the construction of contracts in which a clause or proviso is found wholly nullifying the main provisions thereof and rendering them of no force and effect.

Davis v. Fraizer (150 N. C., 447) is a leading case. The opinion therein quotes with approval from Bishop on Contracts, section 386, as follows:

"After interpretation has exhausted itself in harmonizing the several clauses and words, if there is a residue which can not be reconciled, the repugnancy must be got rid of by rejecting what will free the writing from it."

Also from the same author, section 387:

"If the main body of the writing is followed by a proviso wholly repugnant thereto, it must necessarily be rejected, because otherwise the entire contract will be rendered null; but where it can be construed to qualify the main provisions so that all may stand together, it will be permitted to be retained."

Also quoting from *Jones v. Pennsylvania Casualty Co.* (140 N. C., 262):

"It is an undoubted principle that * * * a subsequent clause irreconcilable with a former clause and repugnant to the general purpose and intent of the contract will be set aside."

The oral evidence leaves no doubt that the general purpose and intent of the contract was to make a settlement. On two different occasions, once by Mr. Whitaker, special counsel for the Government, and at another time by the Commissioner, the representatives of the plaintiff were informed that only a final settlement would be agreed to on behalf of the Government. It may be claimed that the oral evidence is incompetent. If so, we need only consider the contract itself, which provides for "full settlement and compromise," using the strongest and most explicit terms. If the contention of the plaintiff is to be sustained, nothing was settled. The two provisions of the contract are so utterly repugnant that both can not stand. The first expresses the general purpose of the contract, as is shown by both the oral evidence and the contract itself.

Moreover, if there was not to be a settlement there was no possible object in the contract. It accomplished nothing, was unenforceable, and without consideration. It bound neither plaintiff nor defendant, and became merely a scrap of paper.

Beam v. Aetna Life Insurance Co. (111 Tenn., 186) is another leading case on the construction of conflicting clauses in a contract. In the decision in this case it is said:

"When two clauses of a contract are in conflict, the first governs rather than the last."

And quoting from Blackstone:

"If there be two clauses so totally repugnant that they can not stand together, the first will be received and the last rejected."

Also from *Wisconsin Marine, etc., Bank v. Wilkin* (95 Wis., 111):

"The law is so well settled on the subject that it can not be contended but that if the last clause of the contract is so repugnant to the first that both can not stand, the first must be taken as expressing the contract between the parties."

To the same effect is 2 Parsons on Contracts, 513, and *Straus v. Wanamaker* (175 Pa., 213).

Where a construction can be given the latter clause which will be consistent with the other terms of the contract and its main purposes, the courts hold that

such a construction should be given it, but this rule does not apply where the latter clause is utterly repugnant to the main purposes of the contract and would nullify it. The rule as above stated in such cases is simply that the latter clause will be rejected and the contract will stand.

It is suggested that a construction might be given the paragraph under consideration which would not be in conflict with the agreement for a settlement and compromise. This suggestion is made on the ground that such was the intention of the parties. On this point it is sufficient to say that if such a construction could properly be given this paragraph of the agreement, it would be as fatal to the plaintiff's cause of action herein as if this paragraph of plaintiff's letter were disregarded entirely.

The plaintiff also contends that the agreement for a compromise and settlement is void, for the reason that no consideration was received for it. We do not think this contention merits extended discussion. Plaintiff is correct in saying that the evidence shows that when the final figure for compromise and settlement was reached, the representatives of the Government had come to the conclusion that no larger amount of taxes than the amount fixed for this item and included in the total to be paid could be legally collected, and it is therefore said that the Government yielded or gave up nothing as a consideration for the agreement. It is not necessary for us to decide whether a consideration would be found in the fact that the Government officials, as the conferences progressed, had been yielding one point after another. Any consideration, however small, will support a contract for compromise and settlement. Plaintiff's agreement to compromise and settle was not simply based on the amount of taxes which the Government officials agreed to accept. There were two other very important and moving considerations. The Government agreed to accept in compromise of the penalties a sum which not only was more than a million dollars less than the amount of penalties originally assessed, but was many thousands less than the statutory amount of penalties on the taxes as finally computed. Besides this it was agreed, on behalf of the Government, that all right to institute any criminal proceedings or charges would be relinquished, and that all liabilities of any nature whatever in connection with the taxes or penalties due or claimed to be due, either from the plaintiff or his wife, were to be extinguished. It is immaterial whether the plaintiff could in fact be legally subjected to these penalties, or whether he was subject to criminal prosecution. It is sufficient if the representatives for the Government believed that such was the case, as they undoubtedly did, and we hold that there was not only sufficient but ample consideration for the agreement.

There was also a still further consideration for the settlement. Part at least of the income which was in controversy upon which, under the settlement, the plaintiff was to pay taxes had theretofore been assessed against corporations to which the property had been transferred and taxes paid thereon by them. The contract of settlement provided that these taxes should be refunded to the corporations. (See last paragraph of plaintiff's letter of November 9, 1920.) This, of course, was proper to prevent the income being taxed both against the corporations and the plaintiff, but the Government had the money and it was nevertheless a consideration. The fact that there was some delay about this payment is immaterial. The corporations had some time before filed a claim for refund, and by the settlement the Government contracted to pay them the refund.

It is also urged on behalf of the plaintiff that in executing the contract of settlement he acted under duress. It is true that the Government officials refused to accept the sum finally agreed upon unless it was paid without protest and in compromise and full settlement of the amount claimed. But we can not believe that the attorneys on either side were so ignorant as not to know that the plaintiff, had he so desired, could have paid or at least tendered this sum without making any agreement of settlement; and that whether this amount was received by the Government or not, the result would be the same. With the exception of the criminal proceedings mentioned in the agreement and the balance of the penalty, the Government could have proceeded no further and the plaintiff could have sued for a refund if the payment was accepted on behalf of the Government. We repeat that there could have been no object in making the contract unless it was for the purpose of a final settlement of both civil and criminal liability, and the assurance that the Government would not attempt to exact more in either case.

It seems to be contended also that the proceedings of the Government with reference to collecting the tax and in the negotiations show duress. We need

not determine whether any courtesies were required in making an examination of plaintiff's books or whether at the time this was done the plaintiff was given a full opportunity to investigate the case on behalf of the Government. Certain it is that as the subsequent conferences between the two parties progressed the additional assessments against the plaintiff were discussed item by item and were fully understood by him. At these conferences what was said with reference to criminal prosecution appears to have been brought in by the plaintiff, who wanted to have the settlement cover this matter. It is well settled that the fact that one party to a settlement entered into it reluctantly will not void it, and it has even been held that the fact that plaintiff is under arrest at the time the compromise is entered into will not be sufficient to defeat it; and, as a matter of course, the fact that one of the parties signed the settlement to avoid the trouble and expense of a lawsuit does not amount to intimidation or duress, for that is ordinarily the purpose of a settlement. The seizure of property by legal process on a claim made in good faith will not invalidate a compromise settlement. In *United States v. Child & Co.* (12 Wall., 232, 244), it is said:

"But no case can be found, we apprehend, where a party who, without force or intimidation and with a full knowledge of all the facts of the case, accepts on account of an unliquidated and controverted demand, a sum less than what he claims and believes to be due him, and agrees to accept that sum in full satisfaction, has been permitted to avoid his act on the ground that this is duress."

The principle upon which this statement is based applies equally to the converse of the case, where a party, with full knowledge, pays a sum greater than what he claims he should and believes that he ought to pay, and pays it in full settlement. The facts in the Child's case much nearer approach duress than in the case at bar. Like the instant case, a very large sum was involved, but unlike the instant case, it was stated in the opinion of the Court of Claims, from which an appeal had been taken, that the action of the Government had "reduced them (Child & Co.) to the verge of bankruptcy," and it appeared that the plaintiff did not sign the receipt voluntarily, but under protest. In the case at bar the plaintiff, during the negotiations for settlement, was represented by able attorneys, and both they and the plaintiff knew before the settlement was signed everything that they know now. In order to successfully defend on the ground of force or duress it must be shown that the party benefited thereby constrained or forced the action of the injured party, and even threatened financial disaster is not sufficient. (*McCormick v. St. Louis*, 166 Mo., 315, 334.) That plaintiff, who was at the time under indictment in connection with the tax return of the Crucible Steel Co., made the settlement to avoid some threatened or possible embarrassment or inconvenience is quite plain, but in the case last cited this is said to be usually the moving influence in bringing about a settlement. There is nothing in the evidence to show any threats or intimidation on the part of the Government officials.

If the counsel for the Government had acted in bad faith, the conclusion would be different, but there is nothing in the evidence to show bad faith on their part.

The defendant also urges that the payment of \$1,972,016.81 accompanying the letter of offer was made without protest, and at the time when it was paid a protest was necessary to recover any of it back. It is true that Du Puy stated to the collector in substance that he proposed to "push the matter to the end," but this statement was not contained in his letter which went on to Washington for determination of whether his offer should be accepted. Moreover, it was expressly stated at the conferences at which the settlement was made that this amount would not be received as paid under protest. In fact, that was one of the conditions which the Government officials insisted upon if a settlement was to be made.

The plaintiff could have simply paid what the Government officials demanded and made a protest if he had desired, without the settlement. He did not see fit to do this, and, consequently, must be held to have paid without protest. It was not until about three years after the payment that a suit could be maintained to recover a tax without protest. This was provided by the Revenue Act of 1924, section 1014 (43 Stat., 343). The payment was a voluntary one, as we have before found, and we think that plaintiff's suit is also precluded by reason of a lack of protest. (*United States v. N. Y. & Cuba Mail S. S. Co.*, 200 U. S., 488; *Fox v. Edwards*, 280 Fed., 413.)

The conclusions which we have reached with reference to the contract for settlement and the lack of protest make it unnecessary to determine whether the taxes paid by the plaintiff were legally due and owing to the Government. It follows that his petition must be dismissed, and it is so ordered.

ARTICLE 1011: Compromise of tax cases.

VIII-36-4348

Ct. D. 102

FEDERAL TAXES—COMPROMISE—DECISION OF COURT.

COMPROMISE—SUIT—DEFENSE.

Where a deficiency has been assessed consisting of an additional tax plus the 50 per cent fraud penalty provided by section 250(b) of the Revenue Act of 1918, and the taxpayer, pursuant to section 3229 of the Revised Statutes, offers "in compromise of all civil and criminal liabilities" an amount equal to 5 per cent of the deficiency and the payment of the additional tax proper in full, the acceptance of such offer by the authorized officers of the Government precludes the taxpayer from recovering back any part of the tax so paid.

UNITED STATES CIRCUIT COURT OF APPEALS, EIGHTH CIRCUIT.

Ely & Walker Dry Goods Co., a Corporation, appellant, v. United States of America, appellee.

Appeal from the District Court of the United States for the Eastern District of Missouri.

[July 29, 1929.]

OPINION.

PHILLIPS, Circuit Judge, delivered the opinion of the court.

This is an action by Ely & Walker Dry Goods Co. against the United States to recover, under the provisions of Title 28, section 41, subdivision 20, United States Code, the sum of \$465,741.10, with interest, on account of income and profits taxes alleged to have been erroneously and illegally assessed and collected from the Dry Goods company for the fiscal year ending November 30, 1918. The case was tried upon an agreed statement of facts. The district court entered judgment for the United States and this is an appeal therefrom.

The facts are as follows:

On June 16, 1919, the Dry Goods company filed its original income and profits tax return for its fiscal year ending November 30, 1918, showing a total tax liability of \$1,999,273.04. The gross income shown by such return was computed on the basis of inventories which were incorrect. Thereafter, on October 28, 1919, the Dry Goods company voluntarily filed an amended income and profits tax return for such year showing an additional tax liability of \$340,356.02. Such additional tax resulted from the inclusion in the Dry Goods company's gross income of inventories omitted from the original return. On December 2, 1919, the Dry Goods company filed a claim for abatement in the amount of \$108,161.58 of the income and profits taxes assessed against it for the fiscal year ending November 30, 1918. Thereafter, in April, 1920, an additional tax of \$299,706.32 was assessed by the Commissioner of Internal Revenue, together with a penalty of \$320,031.17, such penalty being 50 per cent of the taxes assessed in addition to the taxes shown in the original return. Such additional tax resulted in part from a further correction of the Dry Goods company's inventories made under the direction of the internal revenue agent in charge at St. Louis. Such penalty was assessed on account of the admitted understatement of the inventories in the original return of the Dry Goods company.

On May 6, 1920, the Dry Goods company addressed a letter to the Commissioner of Internal Revenue, which read, in part, as follows:

"SIR: Ely & Walker Dry Goods Co., a corporation within the city of St. Louis and State of Missouri, hereby offers in compromise of all civil and criminal liability of itself, its officers, directors and employees, in connection with its returns for all income, excess and war profits taxes for the fiscal year ending

November 30, 1918, the sum of \$32,003.12, being 5 per cent of the deficiency in its taxes for 1918.

"It will cause to be deposited on May 7, 1920, with the collector of the first district of Missouri, at St. Louis, the sum of \$331,709.44, being the amount of the tax that remains unpaid, viz, \$299,706.32 and \$32,003.12, as above stated, said sum to be accepted by said collector if this offer in compromise is accepted by the Commissioner."

The remaining portions of the letter consisted of statements refuting the claim of intentional fraud on the part of the Dry Goods company and were submitted as grounds for reducing the penalties.

Thereafter, and on May 7, 1920, the Dry Goods company delivered to the collector of internal revenue at St. Louis its check for \$32,003.12, accompanied by the following letter:

"As stated in our offer in compromise of May 6, 1920, addressed to the Commissioner of Internal Revenue, we now hand you herewith certified check for \$32,003.12, which amount we tender in compromise of all liability, both civil and criminal, of this corporation and all of its officers, employees, and agents for tax liability arising under the Revenue Act of 1918 for our fiscal year ending November 30, 1918."

On May 10, 1920, it delivered to the collector its check for \$299,706.32, the balance due and unpaid on the deficiency taxes for the year ending November 30, 1918, exclusive of penalty. On May 27, 1920, the Commissioner of Internal Revenue was formally notified by the collector that a sum totaling \$331,709.44 had been paid to him by the Dry Goods company. Such "offer in compromise was accepted by the Commissioner of Internal Revenue by and with the consent of the Secretary of the Treasury on October 20, 1920." On October 27, 1920, the Commissioner of Internal Revenue directed the following communication to the Dry Goods company, advising it of such acceptance:

"OCTOBER 27, 1920.

"ELY & WALKER DRY GOODS Co.,

"St. Louis, Mo.

"GENTLEMEN: I have considered the proposition submitted by you on May 27, 1920, through the collector of internal revenue at St. Louis, Mo., as a compromise of liabilities on account of your alleged filing of a false and fraudulent income and profits tax return for the year 1918, and have decided, with the advice and consent of the Secretary of the Treasury, to close the case by the acceptance of the following terms: \$32,003.12 in compromise of all civil and criminal liability of Ely & Walker Dry Goods Co., its officers, directors, and employees, in connection with its returns for income, excess and war profits taxes for the fiscal year ended November 30, 1918."

In this letter the Commissioner made the reference, to wit, "the proposition submitted by you on May 27, 1920, through the collector of internal revenue at St. Louis, Mo.," wholly because the payments were reported by the collector to the Commissioner on May 27, 1920.

The sole defense set up by the Government to the claim of the Dry Goods company was that the taxes had been compromised pursuant to section 158, Title 26, United States Code, which reads as follows:

"The Commissioner of Internal Revenue, with the advice and consent of the Secretary of the Treasury, may compromise any civil or criminal case arising under the internal-revenue laws instead of commencing suit thereon; and, with the advice and consent of the said Secretary and the recommendation of the Attorney General, he may compromise any such case after a suit thereon has been commenced. Whenever a compromise is made in any case there shall be placed on file in the office of the Commissioner the opinion of the Solicitor of Internal Revenue, or of the officer acting as such, with his reasons therefor, with a statement of the amount of tax assessed, the amount of additional tax or penalty imposed by law in consequence of the neglect or delinquency of the person against whom the tax is assessed, and the amount actually paid in accordance with the terms of the compromise."

In the agreed statement of facts, the parties stipulated, if, upon the consideration of the special defense of compromise, the court should find the Dry Goods company was entitled to recover, that the amount of the judgment should be \$410,185.45, with interest.

The trial court found that the Dry Goods company had entered into a compromise of its tax liability for the fiscal year ending November 30, 1918, and that such compromise constituted a valid defense to its action.

The contention of the Dry Goods company is that the compromise related solely to its civil and criminal liability for filing a false return, that the amount of penalty only was compromised, and that the additional tax was voluntarily paid.

Section 250(b) of the Revenue Act of 1918, in part, provides:

"If the understatement is false or fraudulent with intent to evade the tax, then, in lieu of the penalty provided by section 3176 of the Revised Statutes, as amended, for false or fraudulent returns willfully made, but in addition to other penalties provided by law for false or fraudulent returns, *there shall be added as part of the tax 50 per centum of the amount of the deficiency.*" [Italics ours.]

It will be noted that under this statute the penalty is added to and becomes part of the tax.

In the instant case, the Commissioner determined that there was a normal tax deficiency of income and excess profits taxes amounting to \$640,062.34 and found that the original return was false and fraudulent with intent to evade the tax. He therefore added a fraud penalty of 50 per cent thereof, or \$320,031.17, and assessed a total tax deficiency of \$960,093.51.

Under section 250(b) of the Revenue Act of 1918 this fraud penalty was added to and became an integral part of the deficiency tax. The normal tax and the penalty were constituent parts of the whole deficiency tax, which under the statute constituted a single liability and not an aggregation of separate items of liability.

When the negotiations for a compromise were initiated the Commissioner had assessed a deficiency tax of \$960,093.51 and the Dry Goods company had paid thereon the amount of additional taxes admitted by its first amended return, or \$340,356.02, leaving a balance due of \$619,737.49, according to the assessment made by the Commissioner.

Therefore when the parties undertook to agree upon a compromise they necessarily dealt not merely with what amount should be paid as penalty, but what amount of the total tax deficiency of \$960,093.51 should be paid, because the Government's claim constituted a single liability of the taxpayer and not several distinct items of liability, and such, in our opinion, was the intention of the parties. The second paragraph of the letter of May 6, 1920, reads:

"It will cause to be deposited on May 7, 1920, with the collector of the first district of Missouri, at St. Louis, the sum of \$331,709.44, being the amount of the tax that remains unpaid, viz, \$299,706.32 and \$32,003.12, as above stated, said sum to be accepted by said collector if this offer in compromise is accepted by the Commissioner."

It will be noted that in this paragraph the Dry Goods company used the language "the sum of \$331,709.44," and, referring thereto, further says "said sum to be accepted by said collector if this offer in compromise is accepted by the Commissioner."

Furthermore, in its letter of May 7, 1920, referring to the offer contained in its letter of May 6, 1920, the Dry Goods company used this language:

"As stated in our offer in compromise of May 6, 1920, * * * we tender in compromise of all liability, both civil and criminal, of this corporation * * * for tax liability arising under Revenue Act of 1918 for our fiscal year ending November 30, 1918." [Italics ours.]

In this letter written one day after the offer of compromise was written, at a time when no thought of a suit to recover any of these taxes assessed for the fiscal year ending November 30, 1918, was in the mind of the representative of the Dry Goods company, when he came to construe and restate its offer of compromise contained in the letter of May 6, 1920, he plainly said that such offer was to compromise not penalty merely, but all tax liability of the Dry Goods company for the fiscal year ending November 30, 1918.

While the Dry Goods company, in its letter of May 6, segregated its offer into two amounts, one the balance of the tax proper after deducting payments already made, namely, \$299,706.32, and the other 5 per cent of the additional normal taxes added by the amended returns of \$32,003.12, it offered to pay, and actually did pay, the total thereof, to wit, "the sum of \$331,709.44" to the collector on the condition that "said sum" should be accepted by the collector if the offer in compromise was accepted by the Commissioner. No doubt the Dry Goods company had in mind and was seeking a reduction in the penalty assessed, and offered to pay on the basis of the tax proper plus a penalty of 5

per cent, instead of 50 per cent, yet after segregating the items in its letter, it finally treated both taxes proper and penalty as a single liability, namely, "the sum of \$331,709.44," and offered to pay that sum in compromise of its civil, criminal, and tax liability. We think it clear from the language employed that the Dry Goods company intended to deal with the total tax deficiency of \$960,093.51 and offered to pay in compromise of such total deficiency the sum of \$331,709.44. This offer the Commissioner, with the requisite statutory approval, accepted in the terms it was made.

Counsel for the Dry Goods company assert that it in no wise disputed liability for the additional normal taxes and was only disputing the amount of penalty that should be assessed. They lose sight of the fact that in assessing such deficiency the Commissioner assessed a penalty which became a part of the deficiency tax and constituted one whole liability. When they admit there was a dispute as to the amount of penalty to be added, they admit there was a dispute as to the whole liability of which the penalty was an integral part.

But there was a dispute as to the tax liability considered separately and apart from the penalty. The amended return of the Dry Goods company, filed October, 1919, showed only an additional tax liability of \$340,356.02. On the 2d of December, 1919, the Dry Goods company filed a petition for abatement of \$108,161.58 of its taxes for the fiscal year 1918. In April, 1920, the Commissioner assessed an additional tax of \$299,706.32. No part of the additional tax assessed in April, 1920, had been paid when the offer in compromise was made. That offer tendered "the sum of \$331,709.44, being the amount of the tax that remains unpaid, viz, \$299,706.32 and \$32,003.12, * * * said sum to be accepted by said collector if this offer in compromise is accepted by the Commissioner."

The Dry Goods company did not admit that \$299,706.32 was due and unpaid on the tax liability proper. It did not offer to pay or tender these additional taxes proper unconditionally. On the contrary, it offered to pay and tendered the full amount of the unpaid taxes proper upon the express condition that its offer in compromise should be accepted. When the offer was accepted, there was a settlement of the tax liability proper, concerning which theretofore there had been a dispute.

Counsel for the Dry Goods company further lay stress upon the fact that the Commissioner, in his letter of acceptance, referred only to the amount of \$32,003.12. However, the stipulation is to the effect that the offer made on May 6, 1920, was duly accepted on October 20, 1920—seven days before this letter was written. Furthermore, the Commissioner's letter and the offer contained in the letter of May 6 must be read together and in the light of the payment tendered, and when so read, in our judgment, clearly evinces an intent on the part of the Dry Goods company and the Commissioner to compromise both the tax liability proper and penalty.

We accordingly conclude that the deficiency tax included the penalty and constituted an entire, single liability, that this single liability, treated as such by the parties, was duly compromised, and that such compromise is a bar to this action.

Affirmed.

ARTICLE 1012: Assessment of tax.

REVENUE ACTS OF 1918 AND 1921.

Validity of waiver executed by fiduciary not dependent upon State law. (See G. C. M. 6050, page 252.)

ARTICLE 1012: Assessment of tax.

REVENUE ACT OF 1921.

Collection of tax where waiver for assessment purposes only was given after the expiration of statutory period. (See Ct. D. 138, page 268.)

TITLE III.—WAR-PROFITS AND EXCESS-PROFITS TAX FOR 1921.

PART V.—INVESTED CAPITAL.

SECTION 326.—INVESTED CAPITAL.

ARTICLE 831: Meaning of invested capital.

REVENUE ACT OF 1918.

Commissions paid for sale of corporation's own stock. (See Ct. D. 96, page 317.)

ARTICLE 831: Meaning of invested capital.

VIII-42-4399
Ct. D. 122

EXCESS PROFITS TAX—REVENUE ACT OF 1918—DECISION OF COURT.

INVESTED CAPITAL—DEBENTURE NOTES—CORPORATE LIABILITIES.

Debenture notes given by a corporation to several of its stockholders to take up outstanding accounts due them for property conveyed to it can not be included in computing invested capital under section 326 of the Revenue Act of 1918.

COURT OF CLAIMS OF THE UNITED STATES.

Union Land Co., a Corporation, and its affiliated corporations, A. H. Stange Co., Kinzel Lumber Co., E. W. Ellis Lumber Co., and Mount Emily Timber Co., v. The United States.

[May 6, 1929.]

OPINION.

GREEN, Judge, delivered the opinion of the court.

The plaintiffs in this case are affiliated corporations and as such filed a consolidated corporation income-profits-tax return for the calendar year 1918. The Commissioner of Internal Revenue made an additional assessment of taxes in the amount of \$41,520.07 above the amount shown to be due by this return. The plaintiff, the Union Land Co., paid the amount of this additional assessment under protest, and having duly filed a claim for refund, brings this suit to recover the amount so paid.

The evidence shows that in 1914 the A. H. Stange Co., one of the plaintiffs, transferred to the Union Land Co. and the Kinzel Lumber Co., also a plaintiff, a large amount of property, including some cash. The two last-named corporations had the same stockholders as the A. H. Stange Co., and the stockholders held their stock in the same proportions. The property transferred to the Union Land Co., not including cash to the amount of \$60,000, was entered on the books of this company at a value of \$3,431,382.61, although in fact its value was much greater. The property and cash transferred to the Kinzel company amounted to \$305,000, and after this transfer its total assets were in book value \$315,000. The property so transferred to these companies, respectively, was carried upon their books as an asset. The Union Land Co. had, including cash, assets of a total book value of \$3,491,382.61. Against this book value of assets the books showed that capital stock to the amount of \$245,000 had been issued and the several stockholders had been credited with accounts payable in a total amount of \$3,234,000. Against these stockholders' accounts the Union Land Co. issued debenture notes to its stockholders of a face value of \$3,185,000, leaving a balance of \$49,000 on the accounts, which was

paid to the stockholders. The Kinzel Lumber Co. issued capital stock to the amount of \$105,000. Its books showed accounts payable to its stockholders to the amount of \$210,000. Having distributed the amount of \$70,000 in cash, the Kinzel company issued debenture notes to its stockholders in proportion to their stock holdings to the amount of \$140,000, and thereby extinguished the accounts. All of these transactions occurred in 1914.

The debenture notes so issued were payable on or before 20 years from date, were a lien on the property of the corporation which issued them, and might be registered. Otherwise, it was provided that they should pass by delivery and without indorsement.

In making its consolidated income-tax return for 1918 the Union Land Co. listed as a liability as then outstanding debenture notes of the Union Land Co. in the amount of \$2,940,000 and of the Kinzel Lumber Co. \$140,000, and also in its schedule of capital, surplus, and undivided profits included the same amount of debenture notes for each company. The controversy in this case is wholly as to whether the amount of these debenture notes could properly be included in the invested capital of the companies which issued them. The Commissioner held that they could not, and by reason thereof assessed the additional tax which the plaintiffs now seek to recover.

We know of no valid principle under which the amount of these notes could be held to be part of invested capital. The plaintiffs argue that their issuance was not equivalent to making a dividend. We do not think that the issuance of these notes to take up outstanding accounts due the stockholders constituted a dividend, but this does not bring the notes within the definition of invested capital.

The Revenue Act of 1918 (40 Stat., 1057) stated very definitely what items could be included in invested capital. There is nothing in these notes or the transactions through which they were issued that can even remotely be connected with the items described and set forth in this statute as constituting invested capital. Among other things, the statute says that—

“Actual cash value of tangible property, other than cash, bona fide paid in for stock or shares, at the time of such payment, * * *” (section 326(a)2) is within the meaning of “invested capital” as used in the title under consideration, and it seems to be claimed that these notes are covered by this provision.

The debenture notes, as before stated, were given to take up and extinguish open accounts due the stockholders. The credits given by these accounts, it is true, arose by reason of property being transferred to the corporation by the stockholders, but neither these accounts nor the notes which were given to take them up were property “paid in for stock or shares.” In fact, neither the accounts nor the notes were the property of the corporation. The notes passed by delivery and without indorsement and became the property of whoever held them. Although these notes did not mature for 20 years, they constituted an indebtedness and were a liability of the corporation and were, as before stated, listed as a liability in plaintiffs’ return for the year involved. Under no sound theory can an ordinary liability such as a bill or bills payable become a part of invested capital.

As the statute also provides that borrowed money shall not constitute a part of invested capital, the plaintiffs seek to show that neither these notes nor the indebtedness represented by them represented borrowed money. In the case of *Unterberg & Co. v. United States* (64 C. Cls., 197, 204 [T. D. 4121, C. B. VII-1, 2801]), a case quite similar to the one at bar, this court held that the fund for which the debenture notes involved therein were executed was borrowed money, but we do not find it necessary to determine the question in the instant case. The provision of the statute with reference to borrowed money was evidently intended merely to remove any possible doubt as to the status of money which had been borrowed. It did not in any way enlarge the meaning of the words “invested capital,” as otherwise defined by the statute, and the plaintiffs, in order to justify their contention, must show that the debenture notes were within this definition. This they have failed to do. It follows that plaintiff, the Union Land Co., was not entitled, in making its consolidated return, to deduct from [include in?] its invested capital the amount of the debenture notes, and that it and its affiliated corporations can not recover herein.

Judgment will be entered dismissing plaintiffs’ petition.

ARTICLE 831: Meaning of invested capital.**REVENUE ACT OF 1918.**

Amount included in earned surplus representing difference between cash purchase price of stock and its par value where the value of stock at the time of its purchase was not in excess of cost. (See Ct. D. 124, page 320.)

ARTICLE 831: Meaning of invested capital.**REVENUE ACT OF 1918.**

Rights under negotiations for a contract that represent no capital investment transferred to a corporation in exchange for its capital stock. (See Ct. D. 131, page 302.)

ARTICLE 851: Intangible property paid in.

VIII-36-4345
Ct. D. 103

PROFITS TAX—REVENUE ACT OF 1918—DECISION OF COURT.**INVESTED CAPITAL—WAR-PROFITS CREDIT—REORGANIZATION—GOOD-WILL VALUATION.**

Where in the case of a reorganization coming under section 330 of the Revenue Act of 1918 good will was in existence both during the taxable year and the pre-war years and is included in invested capital for the taxable year but is not reflected in invested capital for the pre-war years, the good will must be included in invested capital for the pre-war period at the same valuation employed in including it in the computation of invested capital for the taxable year and subject to the limitations contained in section 326(a)4.

UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

Loft, Inc., plaintiff, v. Frank K. Bowers, Collector of Internal Revenue of the United States for the Second District of New York, defendant.

In error to the District Court of the United States for the Southern District of New York

[December 20, 1928.]

OPINION.

Action by Loft, Inc., against Frank K. Bowers, collector of internal revenue to recover a war-profits tax alleged to have been illegally collected. Judgment for defendant, and plaintiff brings error. Affirmed.

AUGUSTUS N. HAND, Circuit Judge: This action was brought to recover \$36,772.99 war-profits taxes for the year 1918 alleged to have been illegally exacted. Prior to the year 1916 the candy business now conducted by the plaintiff company was owned by George W. Loft, who did not carry good will as an asset on his books. In January, 1916, the business was incorporated with an authorized and issued capital of \$4,000,000. In computing the taxes for the year 1918 the Commissioner allowed a value on good will for invested capital purposes of \$1,000,000, or 25 per cent of the par value of the capital stock of the corporation outstanding. In determining the value of the good will in the pre-war period for invested capital purposes the Commissioner fixed \$1,000,000—the same figure that he had used for the year 1918. The proof showed that the cash value of the good will January, 1911 (the beginning of the pre-war

period), was \$477,653.35, and that the value on January 1, 1916, when the business was incorporated, was \$1,200,390, but there was issued against the good will stock of the par value of \$2,367,816.76. It was never purchased for cash but arose from the business.

The purpose of the war-profits tax was to subject to a peculiar burden of taxation the income of any business which exceeded what was regarded as a normal return upon the capital embarked in it. In order to reach the so-called war profit and tax it at 80 per cent under the "third bracket" of section 306 of the Revenue Act of 1918, which applied to this case, it was necessary to compare the earnings of the business between the pre-war period and the war period. The tax provided in the third bracket is: "The sum, if any, by which 80 per centum of the amount of the net income in excess of the war profits credit (determined under section 311) exceeds the tax computed under the first and second brackets."

Section 311 provides:

"That the war-profits credit shall consist of the sum of:

- "(1) A specific exemption of \$3,000; and
- "(2) An amount equal to the average net income of the corporation for the prewar period, plus or minus, as the case may be, 10 per centum of the difference between the average invested capital for the prewar period and the invested capital for the taxable year."

It was provided in article 781 of Regulations 45 as follows:

"*War profits credit.*—Ordinarily the war profits credit consists of the sum of the specific exemption of \$3,000 and an amount equal to the average net income of the corporation for the prewar period, plus 10 per cent of the excess of the invested capital for the taxable year over the average invested capital for the prewar period, or minus 10 per cent of the excess of the average invested capital for the prewar period over the invested capital for the taxable year."

Under the regulation above the corporation is entitled to a credit of 10 per cent of the amount by which the invested capital for the taxable year exceeds the average invested capital for the prewar years. Thus the lower the invested capital for the pre-war year, the higher the amount of 10 per cent war-profits credit. Manifestly then the valuation of the good will of the plaintiff at more than its real worth for the pre-war period correspondingly decreased the credit and increased the war-profits tax.

The correctness of the computation of the Commissioner in his valuation of the item of good will depends upon the method to be adopted in valuing invested capital for the pre-war and taxable years. The basis for determining invested capital for any year appears in section 326 of the Act. 4(a) and 5 of that section includes in invested capital:

"(4) Intangible property bona fide paid in for stock or shares prior to March 3, 1917, in an amount not exceeding (a) the actual cash value of such property at the time paid in, (b) the par value of the stock or shares issued therefor, or (c) in the aggregate 25 per centum of the par value of the total stock or shares of the corporation outstanding on March 3, 1917, whichever is lowest;

"(5) Intangible property bona fide paid in for stock or shares on or after March 3, 1917, in an amount not exceeding (a) the actual cash value of such property at the time paid in, (b) the par value of the stock or shares issued therefor, or (c) in the aggregate 25 per centum of the par value of the total stock or shares of the corporation outstanding at the beginning of the taxable year, whichever is lowest: *Provided*, That in no case shall the total amount included under paragraphs (4) and (5) exceed in the aggregate 25 per centum of the par value of the total stock or shares of the corporation outstanding at the beginning of the taxable year;"

The pre-war period is defined in section 310 of the Act and means the calendar years 1911, 1912, and 1913. The value of the good will and intangibles during the pre-war years is taken at \$477,653.35 and during the taxable year at \$1,200,390.

In *La Belle Iron Works v. United States* (256 U. S., 377 [T. D. 3181, C. B. 4, 373]), where an appreciation in value of ore lands over the purchase price had occurred and the book value of this asset was increased and a stock dividend was issued against the increased value, it was held that the appreciation could not be treated as "invested capital" before computation of the war excess-profits tax levied under the Act of October 3, 1917. The Act of 1917 closely

resembles the one now before us and the case cited is controlling authority for the proposition that a mere appreciation in value of an asset whether tangible or intangible is not "invested capital." Such has been held to be the rule applicable to the Act of 1918 in *Lee Hardware Co. v. United States* (25 Fed. (2d), 42 [T. D. 4205, C. B. VII-2, 310]); *Gauley Mt. Coal Co. v. Commissioner of Internal Revenue* (23 Fed. (2d), 574). See also *Willcuts v. Milton Dairy Co.* (275 U. S., 215 [T. D. 4148, C. B. VII-1, 283]).

The statutory provisions of the Act of 1918 which we have cited related to a continuous corporation existing during and after the pre-war period. To cover the case of an individual conducting a business during the pre-war period which he afterwards incorporated (designated as "change of ownership" in the statute) section 330 was enacted. The pertinent clauses are as follows:

"That in the case of the reorganization, consolidation, or change of ownership after January 1, 1911, of a trade or business now carried on by a corporation, the corporation shall for the purposes of this title be deemed to have been in existence prior to that date, and the net income and invested capital of such predecessor trade or business for all or any part of the prewar period prior to the organization of the corporation now carrying on such trade or business shall be deemed to have been the net income and invested capital of such corporation.

"If such predecessor trade or business was carried on by a partnership or individual the net income for the prewar period shall, under regulations prescribed by the Commissioner with the approval of the Secretary, be ascertained and returned as nearly as may be upon the same basis and in the same manner as provided for corporations in Title II, including a reasonable deduction for salary or compensation to each partner or the individual for personal services actually rendered.

* * * * *

"If any asset of the trade or business in existence both during the taxable year and any prewar year is included in the invested capital for the taxable year but is not included in the invested capital for such prewar year, or is valued on a different basis in computing the invested capital for the taxable year and such prewar year, respectively, then under rules and regulations to be prescribed by the Commissioner with the approval of the Secretary such readjustments shall be made as are necessary to place the computation of the invested capital for such prewar year on the basis employed in determining the invested capital for the taxable year."

The plaintiff contends that the concluding words of section 330, providing that in a case like the present such "readjustments shall be made as are necessary to place the computation of the invested capital for such pre-war year on the basis employed in determining the invested capital for the taxable year," require the good will, which was valued at \$1,000,000, or 83 per cent of its actual value of \$1,200,390, for the taxable year to be valued at the like ratio of 83 per cent of \$477,655.35, the actual value for the pre-war year. It is manifest that if such a *basis* were taken an entirely different rule would be adopted for taxation of a corporation having a continuous existence during the pre-war and taxable period and a business conducted by an individual during the pre-war period and afterwards taxed as a corporation for war profits under the statutory provisions we have mentioned. Such a result affords the strongest reason for rejecting plaintiff's claim.

The object of the tax in question was to reach abnormal profits due to the war and to render them, to a large extent, available to meet the enormous expenses of the Government in prosecuting it. A vague intangible like good will was not only most difficult to value fairly but was most likely to increase in value because of war conditions. How carefully an inflation of its value was guarded against is seen from the provisions of section 326(a)4. It would seem quite impossible after the decision of *La Belle Iron Works v. United States*, *supra*, to suppose that an appreciation of the value of such an item could be taken as a part of plaintiff's invested capital for the reduction of its war profits.

Now, section 330 makes the invested capital of the predecessor business for the pre-war period "prior to the organization of the corporation * * * the invested capital of such corporation." In other words, it carries back the later valuations for the earlier period. Had there been a continuous corporation the pre-war valuations would have been taken for the taxable period. By either method the same result would have obtained, namely, the disregard

of increased values for the purpose of increasing the war-profits credit. The provision of the last clause of section 330 that "such readjustments shall be made as are necessary to place the computation of the invested capital for such pre-war year on the basis employed in determining the invested capital for the taxable year" in cases where any asset is included in the invested capital for the taxable year but is not included in the invested capital for the pre-war year or is valued on a different basis for the taxable year and the pre-war year, is to be construed with the prior clauses of the section. It means for present purposes that any asset which has appreciated in value shall be taken just as its value is computed in the invested capital of the taxable year.

Section 326(a)4 prescribes just how the good will shall be valued as a part of invested capital for the taxable year. The actual cash value at the time it was paid in was \$1,200,390; the par value of the stock issued therefor was \$2,367,316.76; 25 per cent of the par value of the total stock of the corporation outstanding on March 3, 1917 (being \$4,000,000), was \$1,000,000. By the provisions of the section the lowest of the three figures must be selected, i. e., \$1,000,000. This amount was properly taken by the Commissioner both for the pre-war and the 1918 valuation of good will as an item of the invested capital. By this computation the appreciation in value was not regarded and the plaintiff was placed in the position of an ordinary corporation in existence during the entire period. Any other adjustment of values would have relieved a war profit from taxation and made an unfounded discrimination in favor of individuals who incorporated their business.

It is said that if it had been intended that the same amount should be used for both the pre-war year and the taxable year, the statute would have so provided. The invested capital for the two periods is in fact usually different because new assets paid in for stock as well as accumulated earnings are likely to have arisen since the pre-war period. The Act, however, did not provide that the invested capital for both periods should be valued at the same amount but on the same *basis*; that is, under the rules laid down in section 326, *supra*, and without taking into account appreciations in value.

Judge Knox, who presided at the trial, rightly directed a verdict for the defendant and the judgment is affirmed.

ARTICLE 864: Affiliated corporations: invested capital.

VIII-43-4408
Ct. D. 126

EXCESS PROFITS TAX—REVENUE ACT OF 1917—DECISION OF COURT.

DEDUCTION—INTERCOMPANY LOSSES.

The loss to a parent corporation of its investment in the capital stock of an affiliated company, which went into liquidation, and its loss of an amount due from its subsidiary on an open account are intercompany losses and are not allowable as deductions in determining the excess profits tax of the affiliated corporations under the Revenue Act of 1917.

COURT OF CLAIMS OF THE UNITED STATES.

Utloa Knitting Co. v. The United States.

[May 6, 1929.]

OPINION.

SINNOTT, Judge, delivered the opinion of the court.

The plaintiff seeks to recover \$29,997.36, with interest, paid as excess-profits tax for the year 1917, on the ground that the Commissioner of Internal Revenue refused to allow a deduction of \$127,658.31 represented as a loss sustained by plaintiff in its transactions with one of its subsidiary companies.

As we view it, the sole question in the case is whether it is proper to eliminate intercompany transactions among affiliated corporations in determining the excess-profits tax for the calendar year 1917 under the provisions of

Title II of the Revenue Act of October 3, 1917 (40 Stat., 302), and section 1331 of the Revenue Act of November 23, 1921 (42 Stat., 319).

On May 24, 1912, the plaintiff organized a company known as the "Airy-knit Co.," which name was later changed to "Unitee Knitwear Co.," with a capital stock of \$100,000. The plaintiff transferred to the newly organized company its patent rights in a special mesh-knitting machine, which had cost plaintiff \$50,000, and plaintiff received therefor \$50,000 par value of the capital stock of the new company. Thereafter capital stock of the new company was acquired by the plaintiff in the par value of \$20,000, for cash; also goods and merchandise were transferred to the new company and paid for by the transfer of \$30,000 of its capital stock at par. In this manner the plaintiff between August 3, 1912, and December 31, 1912, became the owner of all the capital stock of the Unitee Knitwear Co.

While it was not so stipulated, both the plaintiff and the Unitee Knitwear Co. engaged in the manufacture of knit underwear. This is shown by plaintiff's consolidated income tax return for the year 1917 and by the testimony of Henry Fischer, bookkeeper of plaintiff.

In June, 1915, the board of directors of the Unitee Knitwear Co. resolved that the company should go into liquidation. As a result thereof the company wound up its business and affairs during the month of December, 1917.

During the year 1917 the Unitee Knitwear Co. manufactured no products; incurred no expenses or liabilities; had no receipts, except \$821.06 from transactions prior to this year; made no disbursements, except \$10.21 in payment of debts incurred prior to this year; and no sales of property or service were made, except to the plaintiff.

On January 1, 1917, there was due the plaintiff on open account from the Unitee Knitwear Co. \$56,015.30. Between March 7, 1917, and December 24, 1917, this account was reduced by transfer of property of the Unitee Knitwear Co. to plaintiff, and payments in cash, as set forth in Finding IX, leaving a balance due the plaintiff as of December 31, 1917, of \$27,616.36 due on the open account, and \$100,000 on account of the stock of the Unitee Knitwear Co.

On or about April 1, 1918, the plaintiff duly filed its income and profits tax returns for the year 1917, claiming certain deductions, and paid the taxes therein disclosed. Further taxes were paid and adjustments of the taxpayer's accounts were made.

On January 10, 1924, the plaintiff filed a claim for refund in regard to its 1917 taxes, upon the ground, among others, that the Commissioner of Internal Revenue had failed to allow as a loss its investment of \$100,000 in the stock of the Unitee Knitwear Co., and the unpaid balance on the open account, amounting to \$27,623.27, as a deduction for the year 1917, both for income and excess-profits tax purposes.

Upon the audit of the plaintiff's income tax return for 1917, in connection with the January 10, 1924, claim for refund, the Commissioner of Internal Revenue allowed the sum of \$127,658.31 as a deduction on account of the loss sustained by the plaintiff in its transactions with the Unitee Knitwear Co. However, in the audit of the plaintiff's consolidated-profits tax return for 1917 the Commissioner of Internal Revenue disallowed the deduction of said sum for excess-profits tax purposes on the ground that such deduction could only be allowed for normal tax purposes and could not be considered in determining the excess-profits tax of the consolidation.

We think that the Commissioner of Internal Revenue was correct in disallowing the sum of \$127,658.31 as a deduction, with reference to plaintiff's excess-profits tax, on account of the loss sustained by plaintiff in its transaction with its subsidiary and affiliated company, the Unitee Knitwear Co.

Plaintiff's excess-profits tax for the year 1917 became due under Title II of the Revenue Act of October 3, 1917 (40 Stat., 302). Section 1331 of the Revenue Act of 1921 (42 Stat., 319) requires consolidated returns, under said Title II of the Revenue Act of 1917, for affiliated corporations.

The following are the pertinent provisions of said section 1331:

"CONSOLIDATED RETURNS FOR YEAR 1917.

"SEC. 1331. (a) That Title II of the Revenue Act of 1917 shall be construed to impose the taxes therein mentioned upon the basis of consolidated returns of net income and invested capital in the case of domestic corporations and domestic partnerships that were affiliated during the calendar year 1917.

"(b) For the purpose of this section a corporation or partnership was affiliated with one or more corporations or partnerships (1) when such corporation or partnership owned directly or controlled through closely affiliated interests or by a nominee or nominees all or substantially all the stock of the other or others, or (2) when substantially all the stock of two or more corporations or the business of two or more partnerships was owned by the same interests: *Provided*, That such corporations or partnerships were engaged in the same or a closely related business, * * *.

"(c) The provisions of this section are declaratory of the provisions of Title II of the Revenue Act of 1917."

The plaintiff and its subsidiary, the Unitee Knitwear Co., were clearly affiliated, under the terms of said section 1331. The plaintiff owned all the stock of the subsidiary company. Both companies were engaged in the same business, namely, the manufacture of knit underwear.

We can not agree with the contention of plaintiff that the fact that the subsidiary company in 1917 manufactured no products, incurred no expenses or liabilities, that its sole activities were to collect certain accounts and to pay certain debts, to wind up its affairs, and to turn over to plaintiff all its property, in any way relieves plaintiff and its subsidiary from the provisions of section 1331, above quoted. The relations between plaintiff and the Unitee Knitwear Co. continued, and they were a unit until the latter company was finally liquidated in December, 1917.

It would be an extremely technical evasion of the purpose of the statute to hold that a conceded affiliation ceases when the subsidiary ceases to sell and manufacture goods, while at the same time the parent company owns all the stock of the subsidiary, and the subsidiary continues in business for the purpose of winding up its affairs, turning over its property to the parent, collecting its accounts and paying its debts, which very debts and accounts arose out of the knitwear business in which both the parent company and the subsidiary were engaged.

The Commissioner was correct in refusing to consider the intercompany transactions between plaintiff and its subsidiary, with reference to the excess-profits tax. The very purpose of section 1331 of the Revenue Act of 1921, *supra*, was to treat affiliated corporations as an entity, or a business unit, and to eliminate intercompany transactions.

This purpose is well stated in Senate Report No. 617, Sixty-fifth Congress, third session, pages 8, 9, in explaining section 240 of the Revenue Act of 1918 (40 Stat., 1081), as follows:

"Provision has been made in section 240 for a consolidated return, in the case of affiliated corporations, for purposes both of income and profits taxes. A year's trial of the consolidated return under the existing law (referring to articles 77 and 78 of Regulations 41, wherein the Commissioner of Internal Revenue may require affiliated corporations to file consolidated returns for the purpose of computing their excess-profits tax liability for the taxable year 1917) demonstrated the advisability of conferring upon the Commissioner explicit authority to require such returns.

"So far as its immediate effect is concerned, consolidation increases the tax in some cases and reduces it in other cases, but its general and permanent effect is to *prevent evasion which can not be successfully blocked in any other way*. Among affiliated corporations it frequently happens that the accepted intercompany accounting assigns too much income or invested capital to company A and not enough to company B. This may make the total tax for the corporation too much or too little. If the former, the company hastens to change its accounting method; if the latter, there is every inducement to retain the old accounting procedure, which benefits the affiliated interests, even though such procedure was not originally adopted for the purpose of evading taxation. As a general rule, therefore, improper arrangements which increase the tax will be discontinued, while those which reduce the tax will be retained. [*Italics ours.*]

"Moreover, a law which contains no requirements for consolidation puts an almost irresistible premium on a segregation or a separate incorporation of activities which would normally be carried as branches of one concern. Increasing evidence has come to light demonstrating that the possibilities of evading taxation in these and allied ways are becoming familiar to the taxpayers of the country. While the committee is convinced that the consolidated return tends to conserve, not to reduce, the revenue, the committee recommends its adoption not primarily because it operates to prevent evasion of taxes or be-

cause of its effect upon the revenue, *but because the principle of taxing as a business unit what in reality is a business unit is sound and equitable and convenient both to the taxpayer and to the Government.*" [Italics ours.]

In appeal of *H. S. Crocker Co.* (5 B. T. A., 537); appeal of *Farmers Deposit National Bank and Affiliated Banks* (5 B. T. A., 520); and *United Drug Co. v. Nichols* (21 Fed. (2d), 160), it was held that the Commissioner of Internal Revenue could not tax as income the gain on intercompany transactions. Also, in *Mackechine Bread Co. v. Commissioner* (5 B. T. A., 888); appeal of *United States Trust Co.* (1 B. T. A., 901); appeal of *Thomas Publishing Co.* (3 B. T. A., 686), the Commissioner of Internal Revenue was sustained in disallowing intercompany losses. On the general proposition that intercompany transactions should be eliminated in computing consolidated net income and consolidated invested capital, see *Buffalo Forge Co. et al. v. Commissioner* (5 B. T. A., 947); appeal of *Hartford & Connecticut Railroad Co.* (2 B. T. A., 211); appeal of *Gould Coupler Co.* (5 B. T. A., 499, 517-519); *Gulf Oil Corporation v. Lewellyn* (248 U. S., 71).

We are of the opinion that the plaintiff and the Unitee Knitwear Co. were affiliated in the year 1917, and that the Commissioner was correct in refusing to deduct the intercompany loss of plaintiff in the sum of \$127,658.31, and that plaintiff's petition should be dismissed. It is so ordered and adjudged.

SECTION 327.—SPECIAL CASES.

ARTICLE 901: Treatment of special cases.

VIII-44-4414
Ct. D. 127

EXCESS PROFITS TAX—REVENUE ACT OF 1918—DECISION OF COURT.

SPECIAL ASSESSMENT—REPRESENTATIVE CORPORATIONS—COMMISSIONER'S DISCRETION.

In computing the tax in the case of a special assessment under section 328 of the Revenue Act of 1918, the selection by the Commissioner as therein provided of the representative corporations engaged in a like or similar trade or business is an act of administrative discretion which is not reviewable by the courts.

COURT OF CLAIMS OF THE UNITED STATES.

Chicago Frog & Switch Co. v. The United States.

[May 6, 1929.]

MEMORANDUM.

The petition shows that the plaintiff is a corporation which paid income and excess-profits taxes for the year 1918, and upon this payment it claims to be entitled to a refund. More specifically, the petition alleges that plaintiff is entitled to recover \$192,592.95 for taxes and interest overpaid, which were wrongfully and illegally assessed against the plaintiff by the Commissioner of Internal Revenue. The basis of this allegation, as stated in the petition, is that the Commissioner undertook to assess its profits tax for the year 1918 in the manner prescribed by section 328 of the Revenue Act of 1918 (40 Stat., 1057), but that said profits tax was not the amount which bore the same ratio to the net income of plaintiff (in excess of the specific exemption of \$3,000) for the calendar year 1918 as the average tax of representative corporations, engaged in a like or similar trade or business, whose invested capital could be satisfactorily determined under section 326 of said Act and which were, as nearly as may be, similarly circumstanced as compared with plaintiff within the meaning of section 328, bore to their average net income for the taxable year 1918, all as required by said section 328. The petition further alleges in substance that the Commissioner did not select the proper corporations for comparison and determination of plaintiff's profits tax.

The decision in the case at bar is controlled by the case of *Williamsport Wire Rope Co. v. United States* (277 U. S., 551 [T. D. 4172, C. B. VII-2, 323]).

In the instant case it will be observed that the plaintiff was granted a special assessment under the provisions of section 328, but alleges that by reason of the proper comparatives not being taken its tax was wrongfully computed. In other words, the plaintiff claims, in the language of the statute, that "representative corporations engaged in a like or similar trade or business" were not selected as required by the statute. But in the *Williamsport Wire Rope Co.* case, *supra*, it was held that this presented a question of administrative discretion which is not reviewable by this court.

The demurrer must be sustained and the petition dismissed. It is so ordered.

ARTICLE 901: Treatment of special cases.

REVENUE ACT OF 1918.

Corporation without invested capital. (See Ct. D. 131, page 302.)

ARTICLE 901: Treatment of special cases.

REVENUE ACT OF 1918.

Corporation's entire income derived from Government contract on cost-plus basis. (See Ct. D. 131, page 302.)

SECTION 328.—COMPUTATION OF TAX IN SPECIAL CASES.

ARTICLE 911: Computation of tax in special cases.

VIII-42-4395
Ct. D. 116

EXCESS PROFITS TAX—REVENUE ACT OF 1918—DECISION OF COURT.

SPECIAL ASSESSMENT—NET LOSS—COMPUTATION OF TAX.

Where the excess profits tax for the year 1918 is to be computed in the case of a special assessment under section 328 of the Revenue Act of 1918 and the taxpayer has sustained a net loss for the year 1919 which is deducted from net income for 1918 under section 204 of that Act, the rate of tax should be applied to the net income which results after the deduction of the net loss.

COURT OF CLAIMS OF THE UNITED STATES.

Bell & Co. and Hollings-Smith Co., Affiliated Corporations, v. The United States.

[October 22, 1928.]

OPINION.

Moss, Judge, delivered the opinion of the court.

Plaintiffs, *Bell & Co. and Hollings-Smith Co.*, were affiliated corporations, and as such they were required to and did file joint consolidated income and profits tax returns for the years 1918 and 1919. They had a joint net income for the year 1918 of \$74,766.78. The Commissioner found that plaintiffs were entitled to a special assessment under section 328 of the Revenue Act of 1918 (40 Stat., 1093), which provides in substance that in cases of abnormality with reference to invested capital, or where the commissioner is unable to ascertain the invested capital, the taxpayer should be required to pay only that

sum as profits tax as would be the same percentage of its net income as the average profits tax paid by fairly comparable concerns.

For the year 1919 plaintiffs' return showed a net loss of \$35,933.62. Section 204 of the Act of 1918 (40 Stat., 1060), in so far as applicable, is as follows:

"If for any taxable year beginning after October 31, 1918, and ending prior to January 1, 1920, it appears upon the production of evidence satisfactory to the Commissioner that any taxpayer has sustained a net loss, the amount of such net loss shall under regulations prescribed by the Commissioner with the approval of the Secretary be deducted from the net income of the taxpayer for the preceding taxable year; and the taxes imposed by this title and by Title III for such preceding taxable year shall be redetermined accordingly. Any amount found to be due to the taxpayer upon the basis of such redetermination shall be credited or refunded to the taxpayer in accordance with the provisions of section 252. If such net loss is in excess of the net income for such preceding taxable year, the amount of such excess shall, under regulations prescribed by the Commissioner with the approval of the Secretary, be allowed as a deduction in computing the net income for the succeeding taxable year."

In pursuance of the plain directions of this statute the Commissioner deducted from plaintiffs' net income for 1918 the net loss for 1919 and "redetermined" the tax, applying the proper tax rate as determined by the Commissioner under the special assessment provision to the newly ascertained net income. (See Finding VI.)

Plaintiffs contend that Congress intended to provide by sections 204 and 328 two separate and distinct methods of relief, and that the taxpayer can receive the benefit of both remedies only by a separate computation. Their contention can best be illustrated by setting forth in this connection the calculation incorporated in plaintiffs' petition. It is as follows:

Net income for 1918.....	\$74,766.78
Profits tax under section 302.....	48,913.42
Comparative companies paid 40.95 per cent of their net income in profits tax; 40.95 per cent of \$74,766.78 would be.....	30,617.00
A reduction in profits tax under section 328 alone of.....	18,296.42
Plaintiffs suffered a net loss in 1919 of \$35,933.62. Deducting this from 1918 net income leaves.....	38,833.16
Profits tax redetermined on this sum under section 301.....	20,166.53
A reduction in profits tax under section 204 alone of.....	28,746.89
Adding reductions due to both sections together makes.....	47,043.21
Deduct total reduction from profits tax under section 302.....	1,879.11

INCOME TAX.

Deducting the correct profits tax of \$1,870.11 from that exacted by the Commissioner of \$15,902.76 leaves additional sum subject to 12 per cent corporation tax of.....	14,032.65
Income tax at 12 per cent thereon is.....	1,683.92

Deducting additional income tax due from overpayment of profits tax leaves net overpayment of total tax by plaintiffs	12,348.73
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Plaintiffs' theory is manifestly incorrect. Sections 327 and 328 operated only to *reduce the rate* of profits tax to the average rate paid by fairly comparable concerns. This rate, once determined by the Commissioner, is to be applied to plaintiffs' net income, whatever that net income is finally determined to be. "Net income" is, in effect, the gross income less certain authorized deductions. A proven net loss for the year 1918 [1919] is an authorized deduction from the net income for 1918. We are of the opinion that the Commissioner correctly computed plaintiffs' tax liability. The petition will be dismissed and it is so ordered and adjudged.

SALES TAX RULINGS.

TITLE II. PART III.—EXCISE TAXES. (1928)

SECTION 424.—REFUND OF AUTOMOBILE ACCESSORIES TAX.

REGULATIONS 47(1924), SECTION 600(3): Auto-
mobile parts and accessories.

VIII-40-4379
Ct. D. 113

EXCISE TAXES—REVENUE ACT OF 1928—DECISION OF COURT.

SUIT—BAR—TAXES ON "PARTS" OR "ACCESSORIES."

Section 424 of the Revenue Act of 1928 precludes a recovery, in a suit against a collector instituted subsequent to April 30, 1928, for taxes paid on parts or accessories for automobiles imposed by section 900(3) of the Revenue Acts of 1918 and 1921 and section 600(3) of the Revenue Act of 1924. The discretionary power vested in the Commissioner by section 424, in respect to the refund of such taxes, is constitutional and its exercise is not reviewable by the courts.

DISTRICT COURT OF THE UNITED STATES FOR THE NORTHERN DISTRICT OF OHIO,
EASTERN DIVISION.

Sterling Spring Co., plaintiff, v. C. F. Routzahn, defendant.

[May 8, 1929.]

OPINION.

JONES, J.: The defendant has filed a motion to dismiss the taxpayer's suit because recovery is precluded under section 424 of the Revenue Act of 1928, which provides as follows:

"SEC. 424 (Act of 1928). (a) No refund shall be made of any amount paid by or collected from any manufacturer, producer, or importer in respect of the tax imposed by subdivision (3) of section 600 of the Revenue Act of 1924, or subdivision (3) of section 900 of the Revenue Act of 1921 or of the Revenue Act of 1918, unless either—

"(1) Pursuant to a judgment of a court in an action duly begun prior to April 30, 1928; or

"(2) It is established to the satisfaction of the Commissioner that such amount was in excess of the amount properly payable upon the sale or lease of an article subject to tax, or that such amount was not collected, directly or indirectly, from the purchaser or lessee, or that such amount, although collected from the purchaser or lessee was returned to him; or

"(3) The Commissioner certifies to the proper disbursing officer that such manufacturer, producer, or importer has filed with the Commissioner, under regulations prescribed by the Commissioner with the approval of the Secretary, a bond in such sum and with such sureties as the Commissioner deems necessary, conditioned upon the immediate repayment to the United States of such portion of the amount refunded as is not distributed by such manufacturer, producer, or importer, within six months after the date of the payment of the refund, to the persons who purchased for purposes of consumption (whether from such manufacturer, producer, importer, or from any other person) the articles in respect of which the refund is made, as evidenced by the affidavits (in such forms and containing such statements as the Commissioner may prescribe) of such purchasers, and that such bond, in the case of a claim allowed after February 28, 1927, was filed before the allowance of the claim by the Commissioner."

The plaintiff's action is for the recovery of taxes alleged to have been unlawfully collected under subdivision (3) of section 900 of the Revenue Act of 1921 and subdivision (3) of section 600 of the Revenue Act of 1924.

The district court has original jurisdiction of cases arising under the revenue laws generally and except as special legislation provides otherwise. Where the United States is to be made liable to the payment of money by suit or otherwise, Congress has power to withhold or grant such liability. Suit and judgment against the collector of internal revenue for taxes wrongfully assessed, while in the nature of a personal action against such collector, is nevertheless a vain proceeding without the certificate of probable cause transferring his liability to the United States. With respect to so-called excise taxes imposed under the Acts covered by section 424 of the Act of 1928, the collector seems to have been protected against liability for taxes wrongfully collected, unless such liability is in the form of a judgment obtained in an action duly begun prior to April 30, 1928.

The Congress has the right by law to grant exclusive power to the Commissioner to exercise discretionary and final jurisdiction respecting the tax liability (*Williamsport Wire Rope Co. v. United States*, 277 U. S., 551 [T. D. 4172, C. B. VII-2, 323]), and as to taxes of the character here sought to be recovered has clearly done so in section 424 of the Revenue Act of 1928. This is special legislation to limit the refund and actions therefor of taxes collected and paid under the applicable sections of the Revenue Acts of 1918, 1921, and 1924.

The motion to dismiss will be sustained and exceptions granted to the plaintiff.

TITLE V.—TAX ON ADMISSIONS AND DUES. (1924)

TAX ON DUES.

REGULATIONS 43-II, ARTICLE 5: Social clubs.

VIII-31-4297

Ct. D. 87

TAX ON DUES—REVENUE ACTS OF 1921 AND 1924—DECISION OF COURT.

SOCIAL CLUB—CHARACTER OF ORGANIZATION.

The Bohemian Club of San Francisco, Calif., whose articles of incorporation state that its object is the promotion of social and intellectual intercourse among journalists and other writers, artists, actors, and musicians, whose constitution states that it is instituted for the association of gentlemen connected professionally with literature, art, music, and the drama, and also those who, by reason of their love and appreciation of those objects, may be deemed eligible, which has a large and well-appointed club building and a complete service of a kind that goes with a fully equipped club where members live and spend their time and whose activities embrace sports, entertainment of distinguished guests, concerts, and dramatic exhibitions, is a social club within the meaning of section 801 of the Revenue Act of 1921 and section 501 of the Revenue Act of 1924, the dues to which are taxable under those sections.

COURT OF CLAIMS OF THE UNITED STATES.

William M. Abbott v. The United States.

[January 7, 1929.]

OPINION.

SINNOTT, Judge, delivered the opinion of the court.

The amount directly involved in this case is \$32, but, as we understand, indirectly an amount in excess of \$100,000 is involved. The question before us in this case is whether or not the Bohemian Club of San Francisco, Calif., is a social club within the intent and meaning of section 801 of the Revenue Act of 1921 (42 Stat., 227) and section 501 of the Revenue Act of 1924 (43 Stat.,

253). The pertinent provision of each of said Acts imposes a tax on the amount paid as initiation fees, or dues, "to any social, athletic, or sporting club or organization." The pertinent Treasury regulations appear in Regulations 43, part 2, article 4, where it is provided that "every club or organization having social, athletic, or sporting features, is presumed to be included within the meaning of the phrase, 'any social, athletic, or sporting club or organization,' until the contrary has been proved, and the burden of proof is upon it." Article 5 of the same regulations provides that "any organization which maintains quarters or arranges periodical dinners or meetings, for the purpose of affording its members an opportunity of congregating for social intercourse, is a 'social * * * club or organization' within the meaning of the Act, unless its social features are not a material purpose of the organization but are subordinate and merely incidental to the active furtherance of a different and predominant purpose, such as, for example, religion, the arts, or business. The tax does not attach to dues or fees of a religious organization, singing society, chamber of commerce, commercial club, trade organization, or the like, merely because it has incidental social features, but, if the social features are a material purpose of the organization, then it is a 'social * * * club or organization' within the meaning of the Act."

Plaintiff was a member of the Bohemian Club and as such member paid the taxes in question, the Commissioner of Internal Revenue holding "that the social features" of said club "are a material purpose of the organization and are of such nature and importance as to bring it within the class of social clubs" named in the several Revenue Acts providing for the assessment of taxes on dues of members of a social, sporting, or athletic club.

The articles of incorporation of the club state that "it is designed to be, and is, a moral, beneficial association, and that its objects are the promotion of social and intellectual intercourse between journalists and other writers, artists, actors, and musicians (professional and amateur) and others associated by reason of knowledge and appreciation of polite literature, science, and the fine arts; and also the collection and preservation of records, memento, and archives illustrating the progress of literature, science, and art on the Pacific coast, and calculated to perpetuate the memory of those who have been, or shall be, instrumental in promoting such progress." The constitution subsequently adopted states its objects to be for the association of gentlemen connected professionally with literature, art, music, the drama, and also those who by reason of their love or appreciation of these objects may be deemed eligible.

Membership in the club is not confined to the professions above named. The so-called nonprofessional membership exceeds the professional membership, as is shown in Finding V.

The club has a large, well-appointed, and comfortable club building in the city of San Francisco, of the value of \$950,000, which contains a dining room, seating approximately 350 persons, where the periodical dinners of the club are held. It also has kitchens, storerooms, checking rooms, a barber shop, and a general lounging room, with papers and periodicals on the tables. It also has a card room. A house staff of approximately 86 employees is maintained, including a manager, librarian, chefs, bell boys, etc. On the second and third floors of the club are 40 bedrooms, some of which are reserved for transient members. Approximately 30 or 35 of the unmarried members of the club occupy rooms therein. The plaintiff herein admitted that the club has the "complete service that goes with a fully equipped club, where members live and spend their time." Prior to prohibition the club had a bar and wine room which made an average profit of \$1,000 a month. A part of this bar has been cut away for a candy and cigar display stand, where nonalcoholic beverages are served.

Finding VI indicates that the club building is well adapted to social entertainment. Members may enjoy the use of the private dining rooms for the entertainment of their guests. The house rules provide that members of clubs entitled to reciprocal relations with the Bohemian Club shall have the privilege of the club for the period of three months. The by-laws provide that on request of a member a card may be issued to a nonresident of the city of San Francisco living more than a hundred miles therefrom, which shall entitle him to the privilege of the club for a period of two weeks.

The club's annual report for the year 1920 discusses with apprehension the effect of prohibition upon the club's activities and financing, as well as upon the club's social entertainments, as is shown in Finding VII. The probative force of this on the issues herein is obvious, without comment, as a mere reading of Finding VII will disclose.

The club reports list among the club's activities annual golf tournaments, trap shooting, and water sports. The club has entertained many distinguished visitors. Such entertainment was not limited to actors, musicians, authors, and the like. Soldiers, sailors, explorers—in fact, any man who is deemed worthy of being entertained—have been guests of the club. These guests, as a rule, at the entertainment in turn entertained the club. We can see little in the evidence in this case to differentiate the facilities of the club house for entertainment from the facilities for entertainment of the club house in the case of *Faculty Club of the University of California v. The United States* (65 C. Cls., 754 [T. D. 4228, C. B. VII-2, 335]) and *John Fister v. The United States*, decided by the Court of Claims, October 8, 1928 [Ct. D. 45, C. B. VIII-1, 301], except for the lack of bowling, tennis, and billiards.

One of the predominant purposes of the club, as described in the articles of incorporation, is "the promotion of social and intellectual intercourse between journalists and other writers, artists, actors, and musicians," etc.

The above excerpt from the articles of incorporation of the Bohemian Club brings the club clearly within the purview of the language employed by Judge Moss in the *Faculty Club of the University of California* case, *supra*, where he states:

"The predominant purpose of this club as described in its constitution is to promote mutual acquaintance and fellowship among the officers of instruction of the university. This is plainly the expression of a purely social purpose."

Judge Moss makes the further pertinent comment, which is applicable to the Bohemian Club:

"To hold that 'its social features are not a material purpose of the organization,' or that its purposes and activities are 'merely incidental to the active furtherance of a different and predominant purpose,' would be contrary to the declared purposes of its organization and to the usual and customary social activities of the club throughout the 26 years of its existence."

We are not unmindful of the contention of plaintiff that the predominant purposes of the Bohemian Club are the furtherance of art, literature, music, and the drama, and that it is an association of gentlemen connected professionally with literature, art, music, and the drama, and also those who by reason of their love or appreciation of these objects may be deemed eligible, and that the few social features it has are merely incidental and that it is in no sense a social club.

We have carefully examined the record, in view of this contention, but are unable to agree with it. The record justifies us in applying to the Bohemian Club the language of Judge Green with reference to the Manufacturers' Club of Philadelphia in the case of *John Fister v. The United States*, *supra*:

"It is probable that there are few clubs of a purely social nature anywhere in this country that make such elaborate provisions for social enjoyment."

We have carefully read "The Annals of the Bohemian Club," the three volumes, nearly 800 pages (plaintiff's Exhibits 7, 7A, and 7B), which delightfully depict the history of the club from 1872 to 1895. They fully justify the claim that the social features of the club are a material purpose of the organization. The social activities therein shown were so extensive as to make it clear that they were a material part of the activities of the club organization. These "Annals" present repeated appeals and references by club members to the spirit of "good fellowship." While the "Annals" chronicle many activities on the part of the club in the furtherance of "art for art's sake," at the same time they present a picture of "feasts convivial," of skits, travesties, and burlesques, of Gridiron Club standard and excellence, of—

"Sport that wrinkled care derides
And laughter holding both his sides."

To ignore the picture presented by the club functions and in the "Annals" and thereby to hold that the social features therein depicted were not a material purpose of the organization would be to ignore common knowledge of the traits, customs, and habits of man as a gregarious "social animal." We can not entertain the view that such social activities were all incidental and subordinate to the furtherance of art, literature, etc., and consequently were not material purposes of the organization.

We have reached the conclusion that the Bohemian Club is a social club within the meaning of the taxing statutes. It is ordered and adjudged that plaintiff's petition be dismissed.

TITLE VI.—EXCISE TAXES. (1921 AND 1924)

REGULATIONS 47(1924), ARTICLE 7: Who is a
manufacturer.VIII-32-4306
Ct. D. 91

EXCISE TAXES—REVENUE ACTS OF 1921 AND 1924—DECISION OF COURT.

“MANUFACTURER” OR “PRODUCER.”

Where a corporation, having an exclusive license to manufacture, sell, and distribute lenses, does not itself actually perform the labor necessary to produce them but has an arrangement with factories, at all times subject to its orders, to furnish specified quantities of the lenses as needed to keep its stock intact, and the lenses are made, at prices determined by the corporation, from its molds according to the patented designs and specifications furnished by it and can be made only for the corporation which maintains exclusive control of its designs, specifications, and molds, such corporation is a “manufacturer” or “producer” within the meaning of section 900 of the Revenue Act of 1921 and section 600 of the Revenue Act of 1924.

COURT OF CLAIMS OF THE UNITED STATES.

Warner-Patterson Co., a Corporation, v. The United States.

[June 10, 1929.]

OPINION.

SINNOTT, Judge, delivered the opinion of the court.

Plaintiff seeks to recover \$6,109.97, with interest, alleged to have been erroneously exacted by the United States as excise taxes on articles known as the Warner lens and Patterson lens, between the dates of June, 1923, and June, 1925, inclusive, under provisions of section 900 of the Revenue Act of 1921 (42 Stat., 227, 291) and section 600 of the Revenue Act of 1924 (43 Stat., 253, 322).

Plaintiff, during the period covered by the claim involved in this suit, had an exclusive license to manufacture, sell, and distribute said lenses. Plaintiff during said period purchased the patent for the Warner lens. During the period in question plaintiff sold all the lenses which are the subject of this suit. It did not, however, actually perform the labor necessary to the finished product. That labor was performed by three factories under the following arrangement:

Plaintiff endeavored to keep a sufficient stock of the various sizes of the lenses in question on hand at all times. Occasionally, however, purchasers did place orders with plaintiff which could not be filled from the stock. On such occasions it was plaintiff's practice to transmit the orders to one of the three factories, which would either ship the finished product when completed to plaintiff or to the purchaser, according to the direction of the plaintiff. On other occasions plaintiff directed the Kelly Reasner Agency, which purported to be the agent for all three of the factories, to furnish specified amounts as needed by plaintiff to keep its stock intact, and at the time of so directing the agency determined the prices to be paid for making the lenses. This price varied according to the fluctuating price of glass. When the price of glass was high plaintiff paid the factories correspondingly higher for the lenses shipped to plaintiff, or the purchasers from plaintiff.

The lenses in question were made from plaintiff's molds, according to the patented designs, and the specifications furnished by plaintiff to the factories. These factories could make the lenses in question only for the plaintiff and for nobody else, and at all times the record shows the factories to have been subject to the plaintiff's orders, and plaintiff at all times maintained exclusive control of its designs, specifications, and molds.

Plaintiff was the only one who could contract for the sale of the lenses in question, and also made the profits from the sales of these lenses, and from

these profits paid to the factories the cost of raw material, which varied, plus a certain specified profit, as well as the cost of labor.

The Patterson lenses were sold exclusively for use on automobiles and trucks. According to one witness 60 per cent and according to another 70 per cent of the Warner lenses were sold to the automotive trade.

On July 28, 1925, plaintiff filed a claim for refund with the Commissioner of Internal Revenue for manufacturer's excise tax so paid on the lenses in question for the period from June, 1923, to June, 1925, inclusive, in the amount of \$6,109.97. This claim was rejected by the Commissioner of Internal Revenue on December 2, 1925.

Said claim was based solely on the ground that plaintiff was not the manufacturer or producer of the lenses in question. (Finding V.) Plaintiff in its petition seeks to add another ground for its claim, namely, that the lenses in question are not parts or accessories of automobiles. This ground was not urged as a basis for refund before the Commissioner of Internal Revenue and can not be urged here. See *Kaltenbach v. United States*, No. D-584 [see Ct. D. 82, on page 307], decided by this court January 7, 1929, quoting from *Redwing Malling Co. v. Willcuts* (15 Fed. (2d), 626 [T. D. 3980, C. B. VI-1, 225]), where the court said:

"The precise ground upon which the refund is demanded must be stated in the application to the Commissioner, and we think, if that is not done, a party can not base a recovery in the court upon an entirely different and distinct ground from that presented to the Commissioner."

The sole question for decision is whether plaintiff is a "manufacturer" or "producer" of the lenses in question, within the meaning of section 900 of the Revenue Act of 1921, and section 600 of the Revenue Act of 1924, *supra*.

The taxing Acts provide that the taxes with which this suit is concerned—

"* * * shall be * * * paid by the manufacturer, producer, or importer."

Plaintiff contends that it was not the "manufacturer" or "producer" of the articles in question, because it did not do the actual labor necessary to produce the finished product.

Article 7 of the Treasury Regulations 47, under the Revenue Act of 1921, defines a manufacturer as follows:

"A manufacturer is generally a person who (1) actually makes a taxable article, or (2) by changes in the form of an article produces a taxable article, or (3) by the combination of two or more articles produces a taxable article. Under certain circumstances, however, the person who actually makes, produces, or assembles the taxable article is not the manufacturer for the purpose of the tax. There may be several stages of manufacture and several manufacturers, each of whom must pay a tax. In such cases the tax attaches on successive sales, subject to the provisions as to credits. (See art. 6.) The following examples are merely illustrative:

* * * * *

"Example 3. 'A,' a dealer or jobber, contracts with 'B' for the manufacture of a taxable article, whereby 'B' receives from 'A' the cost of materials and labor plus a specified profit. 'A' is the manufacturer.

* * * * *

"Example 5. 'A,' a dealer or jobber, owns a patent, trade-mark, formula, or recipe for a taxable article, and contracts with 'B' for the manufacture thereof, the contract specifying that 'B' can manufacture the article only for 'A'; that 'A' will take the entire output; and that it will be sold by 'A' as the manufacturer, 'B's' name not appearing on the article. 'A' is the manufacturer."

Article 7 of Regulations 47, under section 600 of the Revenue Act of 1924, provides substantially the same.

It is apparent that plaintiff is clearly within the examples cited above.

The regulations above cited seem to us to be reasonably adapted to the enforcement of the Act in question, and do not appear to be in conflict with the expressed statutory provisions in question.

The examples cited in the regulations seem to be based upon the maxim "*Qui facit per alium facit per se*."

The record shows conclusively that during the period in question plaintiff was in the same position as the owner of the patents, and no one else could manufacture the lenses without the consent of the plaintiff. For all practical

purposes the three companies occupied the position of plaintiff's factories for the production of the lenses. Plaintiff had at all times exclusive control of the designs which it submitted to the factories, and none of the factories could produce the lenses from these designs without the consent of the plaintiff. Plaintiff also saw to it that these lenses were made according to the specifications as submitted to the three factories. Plaintiff also submitted molds from which the lenses were made. These molds were also subject to the exclusive control of plaintiff. It is apparent to us from the record that the three factories were the factory agents of the plaintiff for the production of the lenses.

In *Foss-Hughes Co. v. Lederer* (287 Fed., 150) the court said, with reference to the meaning of the words "manufacturer" and "producer," in section 600 of the Revenue Act of 1917 (40 Stat., 316):

"There is no claim that the plaintiff imports, and none that he is a manufacturer, except in the sense in which one who has something made for him by others, to be sold by him, may be said to be a manufacturer. This is doubtless the sense in which Congress used the word 'producer,' and was also doubtless the occasion for its use."

Plaintiff cites in its brief, on the point that the terms "producer" and "manufacturer" are synonymous, *Hancock v. State* (40 S. E., 317; 114 Ga., 439).

What the court said in that case would seem to be against plaintiff's contention, as it held not only that said words were synonymous but also that a manufacturer is one who causes an article to be made:

"We hold that the word 'producer,' as used in the special act, is identical in meaning with 'manufacturer'; and the latter term, of course, applies both to him who actually makes the wine, and to him who causes it to be made." (*Hancock v. State*, 40 S. E., 318.)

The case of *Carbon Steel Co. v. Lewellyn* (251 U. S., 501) is a case in point on the meaning of the word "manufacturer." In that case petitioner contended that it did not manufacture munitions; that the munitions were manufactured by independent contractors.

The Supreme Court held as follows:

"The Act is explicit in its declaration; perplexity and controversy come over its application. One must be a 'person manufacturing' to incur the tax, but who is to be regarded as such person in the sense of the Act? Or to put it another way, when is 'manufacturing' (the word of the Act) done, and when is 'manufactured' (the word of the Act) attained? In elucidation of the words, the specifications enumerate nine operations to produce a shell, that is a completed shell (except for explosive charge and detonating device), such as petitioner contracted to deliver to the British Government. And all of the operations are asserted to be necessary and all must be performed seemingly by the same person in order that he may be designated as a 'person manufacturing.' We put aside for the purpose of testing the contention the provision of the Act making a person manufacturing 'any part of any of the articles mentioned' subject to 'a tax.'

"The contention reduces the Act to a practical nullity on account of the ease of its evasion. Besides, petitioner minimizes what it did. It was the contractor for the delivery of shells, made the profits on them, and the profits necessarily reimbursed all expenditures on account of the shells. It was such profits that the Act was intended to reach—profits made out of the war and taxed to defray the expenses of the war. Or, as expressed by the court of appeals, Congress 'felt that the large abnormal profits incident to these war contracts created a remunerative field for temporary taxation.' Petitioner, it is true, used the services of others, but they were services necessary to the discharge of its obligations and to the acquisition of the profits of such discharge. And petitioner kept control throughout—never took its hands off, was at pains to express the fact, and retained its ownership of all of the materials furnished by it, and the completed shell belonged to it until delivered to the British Government. * * *

"We recognize the rule of construction but it can not be carried to reduce the statute to empty declarations. And, as we have already said, petitioner's contention would so reduce it. How universal must the manufacturing be? Will the purchase of an elemental part destroy it? And how subsidiary must the work of the subcontractor be not to relieve the contractor—take from him the character of a 'person manufacturing'? And such is the tangle of inquiries

we encounter when we undertake to distinguish between what a contractor to deliver a thing does himself and what he does through others as subsidiary to his obligation.

"It is after all but a question of the kind or degree of agency—the difference, to use counsel's words, between 'servants and general agents' and 'brokers, dealers, middlemen, or factors.' And this distinction between the agents counsel deems important and expresses it another way, as follows: "Every person manufacturing" means the person doing the actual work individually, or through servants or general agents, and that the ownership of the material worked upon does not alter this meaning of the word."

"We are unable to assent to this meaning of the word. It takes from the Act a great deal of utility and makes it miss its purpose. Of course, it did not contemplate that a 'person manufacturing' should use his own hands—it contemplated the use of other aid and instrumentalities, machinery, servants, and general agents, availing thereby of the world's division of labor; but it contemplated also the world's division of occupations, and, in this comprehensive way, contemplated that all of the world's efficiency might be availed of, and, when availed of for profits, the latter could not thereby escape being taxed. And where, indeed, was the hardship of it? The tax was on profits and measured by them."

We must conclude that plaintiff was a manufacturer or producer, within the meaning of the taxing Act. Plaintiff's petition will be dismissed. It is so ordered.

TITLE VI.—EXCISE TAXES. (1924)

SALES BY THE MANUFACTURER.

REGULATIONS 47(1924), ARTICLE 16: Definition
of "parts or accessories."

VIII-37-4356
Ct. D. 108

EXCISE TAXES—REVENUE ACTS OF 1918, 1921, AND 1924—DECISION OF COURT.

"PARTS" OR "ACCESSORIES"—WINDOW CLOCKS—WINDOW ANTIRATTLERS.

Window clocks and window antirattlers designed and primarily adapted for use in connection with automobiles, advertised as automobile accessories and sold for the special purpose of being so used, are taxable as "parts" or "accessories" for automobiles under sections 900(3) of the Revenue Acts of 1918 and 1921 and 600(3) of the Revenue Act of 1924.

COURT OF CLAIMS OF THE UNITED STATES.

E. Edelmänn & Co. v. The United States.

[June 3, 1929.]

OPINION.

SINNOTT, Judge, delivered the opinion of the court.

Plaintiff, a corporation of the State of Illinois, engaged in the manufacture and sale of automobile accessories, filed suit on February 27, 1928, to recover the sum of \$8,535.65 with interest from dates of payment alleged to have been illegally exacted by the United States as excise tax on the sales of window antirattlers and clocks, and from the assessment of taxes in excess of the required rates and from rejections of claims for credits on rescinded sales and returned goods made and sold by plaintiff between the dates of August, 1919, and February, 1926.

The bases of the claims are as follows:

On August 14, 1926, plaintiff filed its claim for refund No. 355136 of manufacturer's excise tax so paid on window antirattlers and automobile clocks for the period August, 1919, to February, 1926, inclusive, in the amount of \$5,302.33,

which was duly rejected by the Commissioner of Internal Revenue on May 5, 1927.

On January 10, 1927, plaintiff filed its claim for refund No. 2365 of claimed excess over 5 per cent legal rate of manufacturer's excise tax so paid for the period August, 1919, to August, 1923, inclusive, in the amount of \$2,159.85, which was duly rejected by the Commissioner of Internal Revenue on July 5, 1927.

On January 10, 1927, plaintiff filed its claim for refund No. 2366 of claimed excess over 5 per cent legal rate of manufacturer's excise tax so paid for the period September, 1923, to July, 1924, inclusive, in the amount of \$707.90, which was duly rejected by the Commissioner of Internal Revenue on July 5, 1927.

On July 13, 1927, plaintiff filed its claim for refund No. 11173 of manufacturer's excise tax so paid on returned goods for the period May, 1923, to December, 1923, inclusive, in the amount of \$365.57, which was duly rejected by the Commissioner of Internal Revenue on October 1, 1927.

The findings herein leave the sole question involved in this case, whether the window antirattlers and clocks in question are taxable under section 900 of the Revenue Act of 1918 (40 Stat., 1122), section 900 of the Revenue Act of 1921 (42 Stat., 291), and section 600 of the Revenue Act of 1924 (43 Stat., 253, 322).

Section 900 of the Revenue Act of 1918, *supra*, provides:

"That there shall be levied, assessed, collected, and paid upon the following articles sold or leased by the manufacturer, producer, or importer, a tax equivalent to the following percentages of the price for which so sold or leased:

"(1) Automobile trucks and automobile wagons (including tires, inner tubes, parts, and accessories therefor, sold on or in connection therewith or with the sale thereof), 3 per centum;

"(2) Other automobiles and motorcycles (including tires, inner tubes, parts, and accessories therefor, sold on or in connection therewith or with the sale thereof), except tractors, 5 per centum;

"(3) Tires, inner tubes, parts, or accessories, for any of the articles enumerated in subdivision (1) or (2), sold to any person other than a manufacturer or producer of any of the articles enumerated in subdivision (1) or (2), 5 per centum."

The pertinent sections of the Revenue Act of 1921, *supra*, and the Revenue Act of 1924, *supra*, are the same, with the exception that the Act of 1924 reduced the amount of tax from 5 per cent to 2½ per cent.

Treasury Regulations No. 47, article 15, defines "part" or "accessory"—

"* * * Articles, however, which ordinarily would be classed as commercial commodities become parts when, because of their design or construction, they are primarily adapted for use as component parts of such vehicles.

"Component parts of articles taxable under this definition are taxable when sold separately if they have reached such stage of manufacture that they are primarily adapted for use as a component part. * * *"

Article 16 provides for the taxation of—

"* * * any article designed to be attached to or used in connection with such vehicle to add to its utility or ornamentation or which is primarily adapted for use in connection with such vehicle, whether or not essential to its operation."

Plaintiff's clocks and antirattlers are clearly within the purview of the statute and the above Treasury regulations. They were designed and were primarily adapted for and were advertised and sold for the special purpose of being used as automobile accessories. They perhaps could be used to some extent independent of automobile usage, but the record does not establish such use, except in two or three isolated instances.

Plaintiff made no sales of these articles except for automobile purposes. We can reach no other conclusion but that the devices in question were automobile accessories, taxable under the statute.

With reference to plaintiff's claim, referred to in paragraphs 2 and 3 of Finding V, wherein plaintiff contends that it should have been taxed upon the invoice price, less the tax, instead of upon the total invoice price, it is questionable whether this position is well taken, under the authority of *Lash's Products Co. v. United States* (278 U. S., 175 [T. D. 4259, C. B. VIII-1, 303]). However, the record concerning this matter is unsatisfactory. It does not establish the difference in tax, were it computed upon the sales price after deducting the fractional part stamped on the invoices as tax with reference to payments made after January 10, 1923, payments on or before said date being barred by the statute of limitations.

With reference to plaintiff's claim predicated upon returned goods, referred to in the last paragraph of Finding V, the record is likewise unsatisfactory, as the total amount of such items with reference to sales included in returns made for taxes paid after July 13, 1923, is not established by the record, payments on or before July 13, 1923, being barred by the statute of limitations. See Revenue Act of 1921 (42 Stat., 314-315) and the Revenue Act of 1924 (43 Stat., 342).

The petition will be dismissed. It is so ordered.

TITLE IX.—EXCISE TAXES. (1921)

SALES BY THE MANUFACTURER.

REGULATIONS 47(1924), ARTICLE 16: Definition of
"parts or accessories."

VIII-36-3241
Ct. D. 100

EXCISE TAXES—REVENUE ACTS OF 1921 AND 1924—DECISION OF COURT.

"PARTS" OR "ACCESSORIES"—TOOL KITS.

An aggregation of tools of general utility and of a kind that was manufactured before the advent of the automobile, which are incased separately in a canvas roll, packed in an individual carton, and advertised and sold as an indispensable kit for automobiles to meet emergencies and maintain their workability is properly classified as "parts" or "accessories" for automobiles and taxable as such under section 900(3) of the Revenue Act of 1921 and section 600(3) of the Revenue Act of 1924.

COURT OF CLAIMS OF THE UNITED STATES.

The Fairmount Tool & Forging Co., a Corporation, v. The United States.

[June 3, 1929.]

OPINION.

BOOTH, Chief Justice, delivered the opinion of the court.

Section 900 of the Revenue Act of 1918 (40 Stat., 1057, 1122) provides as follows:

"That there shall be levied, assessed, collected, and paid upon the following articles sold or leased by the manufacturer, producer, or importer a tax equivalent to the following percentages of the price for which so sold or leased—

"(1) Automobile trucks and automobile wagons (including tires, inner tubes, parts, and accessories therefor, sold on or in connection therewith or with the sale thereof), 3 per centum.

"(2) Other automobiles and motorcycles (including tires, inner tubes, parts, and accessories therefor, sold on or in connection therewith or with the sale thereof), except tractors, 5 per centum.

"(3) Tires, inner tubes, parts, or accessories for any of the articles enumerated in subdivision (1) or (2), sold to any person other than a manufacturer or producer of any of the articles enumerated in subdivision (1) or (2), 5 per centum."

The Revenue Acts of 1921 (42 Stat., 227, 291) and 1924 (43 Stat., 253, 322), in so far as the issue involved in this case is concerned, in nowise change the law.

The plaintiff, an Ohio corporation, manufactures and sells to jobbers and dealers a great variety of standard mechanics' and machinists' tools. The segregated units which occasion this litigation are accurately described in Finding III. As a typical illustration, "Kit 10-F" will suffice. This aggregation is set forth in plaintiff's catalogue as "designed particularly for use on Ford and Willys Overland cars," and is made up of 10 individual tools, embracing a hammer, pliers, 6 wrenches, and 2 screw drivers, incased separately in a canvas roll designed for compactness and convenience and packed for the dealers

in an individual carton, with a list price of \$5 printed thereon. Kits of more extensive make-up and costing more are also advertised and commented on as possessing superior advantages.

The Commissioner of Internal Revenue assessed and collected a manufacturer's excise tax upon the foregoing "kits," justifying the collection under the above revenue laws. The plaintiff filed a claim for refund, which was denied, and hence this suit to recover the amount claimed.

The plaintiff seeks to escape taxation, upon a contention that the regulations of the Commissioner with respect to automobile accessories are too comprehensive and therefore illegal in including such general purpose articles, which when sold separately are concededly nontaxable, but become so when segregated in units and advertised for use on an automobile.

The regulations challenged go much into detail and read, so far as pertinent here, as follows:

"ART. 14. * * * Any article which has reached a state of manufacture wherein it is in itself a component part or accessory, and is of such a nature that it may be used or attached by an ordinary repair man or individual user as distinguished from a manufacturer or producer, is subject to tax as a 'part' or 'accessory.'"

"ART. 15. * * * any article designed or manufactured for the special purpose of being used as or to replace a component part of any such vehicle and which by reason of some peculiar characteristic is not such a commercial commodity as would ordinarily be sold for general use and which is primarily adapted only for use as component part of such vehicle."

"Articles, however, which ordinarily would be classed as commercial commodities become parts when, because of their design or construction, they are primarily adapted for use as component parts of such vehicles."

"Component parts of articles taxable under this definition are taxable when sold separately, if they have reached such stage of manufacture that they are primarily adapted for use as such a component part."

"ART. 16. * * * any article designed to be attached to or used in connection with such vehicle to add to its utility or ornamentation and which is primarily adapted for use in connection with such vehicle, whether or not essential to its operation."

"Articles which have a general commercial use and which are not especially designed and peculiarly adapted for use in connection with automobile trucks, automobile wagons, other automobiles, or motor cycles are not subject to tax as 'parts' or 'accessories.'"

"Parts or accessories for automobile trucks, automobile wagons, other automobiles, or motor cycles primarily adapted for use on or in connection therewith when sold for any other purpose are not taxable, provided the purchaser files with his order a statement that such parts or accessories are to be used on or in connection with another article of commerce not enumerated or included in subdivisions (1), (2), or (3) of section 900. For example, a self-starter primarily adapted for use on an automobile, if sold to a manufacturer of motor boats, such manufacturer stating in his order that it is to be used in the manufacture of a motor boat and not upon an automobile, is not taxable."

The machinery of an automobile necessitates the employment of a variety of accessories. Article 16, quoted above, expresses the general conception of the Commissioner in dealing with the class of articles. Tools of general utility, i. e., capable of use for a variety of purposes, may not escape classification as an automobile accessory upon this single fact. This, we think, is apparent. Ordinary monkey wrenches, pliers, hammers, etc., may serve a variety of useful purposes; but when set aside and singled out for an especial purpose, the very necessity of so doing emphasizes the correctness of classifying them as accessories to the purpose. The plaintiff, in order to appeal to a special demand, an essential demand, segregates from his large stock of merchandise the particular units which serve the customers' especial necessities, and gives to the public the merits of his offering by assuring him in public advertisements that the "kits" meet all the especial emergencies that may be remedied by the use of the tools purchased. It is only when this is done that the Commissioner taxes the articles. The fact that tools of this design, functioning as these tools do, were manufactured prior to the advent of the automobile, and are not now, nor never were,

especially designed for use on an automobile, is not in and of itself determinative. (See *Cole Storage Battery Co. v. United States*, 65 C. Cls., 164 [T. D. 4159, C. B. VII-1, 299]; *Walker Mfg. Co. v. United States*, 65 C. Cls., 394 [T. D. 4188, C. B. VII-2, 342]; *Advance Automobile Accessories Corporation v. United States*, 66 C. Cls., 304 [Ct. D. 63, C. B. VIII-1, 296].)

The issue to be solved is dependent upon the facts of each case, and if a manufacturer offers to the automobile trade an essential accessory, one which is universally recognized as an indispensable accompaniment to meet emergencies or maintain the integrity and workability of the car, he surely falls within the classifications set forth in the regulations of the Commissioner. The individual tools which compose the "kits" here involved would be instantly recognized by a car owner at all familiar with its mechanism as both essential and indispensable when needed for use. It is only when so advertised and segregated from the general lot that the taxing Acts are invoked by the Commissioner. Manufacturers have a definite and express way of avoiding the tax when sold for other and different purposes. (See *Magone v. Wiederer*, 159 U. S., 555.)

The plaintiff alleges in its petition the right to recover \$1,688.72, with interest. The statute of limitations precludes a recovery of any sum in excess of \$964.56, with interest. The findings disclose the situation with respect to this fact, and the plaintiff has not challenged the correctness of the same.

The petition will be dismissed. It is so ordered.

REGULATIONS 47(1922), ARTICLE 19: Candy.

VIII-36-4346
Ct. D. 104

EXCISE TAXES—REVENUE ACTS OF 1918 AND 1921—DECISION OF COURT.

1. CANDY—COMMISSIONER'S DEFINITION—BURDEN OF PROOF.

The burden of proof is upon a taxpayer to show that its product, admittedly "candy" as defined by the Commissioner in regulations promulgated by him, is not "candy" within the meaning of section 900(9) of the Revenue Act of 1918 and 900(6) of the Revenue Act of 1921.

2. CANDY—CRACKER JACK.

A product, known as Cracker Jack, consisting of pop corn and peanuts mixed with sirup which after cooking crystallizes, is candy within the meaning of section 900(9) of the Revenue Act of 1918 and section 900(6) of the Revenue Act of 1921.

COURT OF CLAIMS OF THE UNITED STATES.

The Cracker Jack Co., plaintiff, v. The United States, defendant.

[February 4, 1929.]

OPINION.

GRAHAM, Judge, delivered the opinion of the court.

The Revenue Act of 1918 (40 Stat., 1122), section 900(9), taxed "candy" at 5 per cent of the price at which sold, and the Act of 1921 (42 Stat., 291), section 900(6), taxed "candy" at 3 per cent of the price at which sold. These are the applicable statutes in this case.

There is no dispute about the amount of the tax paid.

The statutes authorized the Commissioner to make proper regulations for carrying them into effect. This was necessary, because it was impracticable for Congress to provide general regulations for the various details of statutes of this kind, and while it may be difficult at times to define the line which separates the legislative power to make laws and administrative authority to make regulations, that question is not involved here.

The plaintiff's product is admitted to be within the regulations (see Findings X and XI) of the Commissioner defining "candy," and there is therefore no question about the meaning of the regulations. The only question is whether the regulations are in violation of the express provisions of the statutes, and, if not, whether they are reasonably adapted to the enforcement of the Acts and in conformity with their purpose and spirit. See *Maryland Casualty Co. v. United*

States (251 U. S., 342, 349). If they are in reasonable conformity with the Acts and not in violation of their express provisions, they will have the force of law. The plaintiff's product being within the terms of the regulations and taxable, the burden of showing that the regulations are not in conformity with the statutes is upon the plaintiff; in other words, the burden is not upon the defendant to show that the plaintiff's product is candy as it is defined in the regulations, but upon the plaintiff to show that it is not, or, more broadly stated, that the burden is on the plaintiff "to prove the facts establishing the invalidity of the tax." (*United States v. Anderson*, 269 U. S., 422, 443 [T. D. 3839, C. B. V-1, 179].) Doubt as to the meaning of a word can be removed by considering the general purpose and intent of a statute. See *American Security & Trust Co. v. District of Columbia* (224 U. S., 491).

It is also true that the findings of administrative officers and their practice are presumed to be based upon conclusions which are the result of investigation. Congress having used the word "candy" without definition, it becomes necessary as an administrative act for the Commissioner of Internal Revenue to define it by regulations for the information of taxpayers. The representatives of the manufacturers of candies, confections, sweetmeats, etc., were before Congress prior to the passage of these Acts and were heard. The clerk of the House Ways and Means Committee, where these hearings took place, was a Mr. Walker, who at the time of the making of the regulations (see Findings X and XI) defining "candy" was Deputy Commissioner of Internal Revenue, and by reason of his service as clerk was generally acquainted with what took place before the committee. The Deputy Commissioner of Internal Revenue and the manufacturers had a conference, and the representative of the National Confectioners Association, which embraced about four-fifths of the manufacturers of candies, candied fruits, nuts, pop corn, and similar articles, had conferences with Mr. Walker before, and was present at, the hearing where the Commissioner of Internal Revenue was represented by Mr. Walker, deputy commissioner, the Solicitor of Internal Revenue, and one of the attorneys in his office. After the hearing the regulations (Findings X and XI) embodying the definition of "candy" were promulgated by the Commissioner. This definition is in substantial conformity with a definition suggested at the hearing by the National Confectioners Association. So that it clearly appears that this definition was not reached until after careful hearing and consideration, which must necessarily increase the presumption as to its reasonableness. That it is not in conflict with the express language of the Acts is clear. But, more than this, a reading of both Acts, and particularly section 900 of each, above mentioned, shows that the purpose of these sections was to tax luxuries—that is, to tax articles the use or consumption of which would ordinarily be considered indulgence in a luxury rather than a necessary article of food.

A description of the product and the process of its manufacture we think shows that its consumption is indulgence in a luxury. The plaintiff's product, known as Cracker Jack, consisted of pop corn mixed with a sirup, which after cooking crystallized. The sirup consisted of dissolved sugar, corn sirup, and molasses. It was cooked for a short time, and to it, while cooling, was added a small quantity of peanuts. After further cooking, this mixture of sirup and peanuts was poured into a tub containing pop corn and stirred and the mixture placed in reels, where it was allowed to cool. The process of mixing and cooling was of such character that, after cooling, each kernel of pop corn was separated from the mass, but as separated had a coating of crystallized sirup. It was then automatically boxed in an air and moisture tight wax paper carton and in this form sold. The proportions of the mixture were as follows: Popped corn, 32.9 per cent; peanuts, 8.3 per cent; sugar, corn sirup, and molasses, 58.8 per cent. It will be seen that this product is of the same kind and class as peanut brittle, candied fruit, and similar articles.

We are of the opinion that the purchase and consumption of this product were indulgence in a luxury as distinguished from a necessary article of food, and that the regulations (Findings X and XI) defining it as candy were reasonable in their provisions and in conformity with the spirit and intent of the Acts, and further that it has not been satisfactorily shown that the product is not "candy" within the intent of the statutes, the burden of so doing being upon the plaintiff.

The plaintiff's petition should be dismissed, and it is so ordered.

TITLE V.—TAX ON TRANSPORTATION AND OTHER FACILITIES, AND ON INSURANCE. (1918)

INSURANCE.

REGULATIONS 58, ARTICLE 21: Insurers exempt from tax.

VIII-26-4257
Ct. D. 75

PREMIUM TAXES—REVENUE ACT OF 1918—DECISION OF COURT.

1. ASSOCIATION—RELIEF ORGANIZATION.

A voluntary unincorporated organization composed of employees of a corporation whose primary object is to establish and maintain a trust fund for the payment of benefits to its members in case of disability or death, whose affairs are managed by executive officers with duties similar to corporate officers, and which has an advisory committee exercising executive supervision analagous to that of the board of directors of a corporation is an "association" within the meaning of section 1 of the Revenue Act of 1918.

2. CONTRACT OF LIFE INSURANCE.

A contract with the employees joining the relief department of a railroad providing for payments of money to beneficiaries in case of death in consideration of premiums paid by the members of the department by an assignment of a portion of their wages while in the employ of the company or by payment in cash after their severance of employment is a contract of life insurance within the meaning of section 503(a) of the Revenue Act of 1918.

3. EXEMPTION.

An association of employees of a railroad possessing none of the indicia of a fraternal beneficiary society or order operating under the lodge system which issues contracts of disability and life insurance to its members in consideration of premiums paid by them which are held in trust for the payment of the insurance benefits is not exempt from income tax either as a fraternal beneficiary society under subdivision 3 of section 231 of the Revenue Act of 1918, or as a charitable organization under subdivision 6, or as a "like organization" under subdivision 10, and it is, therefore, not exempt from taxes upon the issuance of insurance policies under section 503 of that Act.

COURT OF CLAIMS OF THE UNITED STATES.

Atlantic Coast Line Railroad Co., a Corporation, v. The United States.

[December 3, 1928.]

OPINION.

SINNOTT, Judge, delivered the opinion of the court.

The plaintiff, the Atlantic Coast Line Railroad Co., seeks to recover the sum of \$2,642.37, with interest thereon from April 14, 1924, which sum plaintiff claims was illegally collected from it by the Commissioner of Internal Revenue, under authority of section 503 of the Revenue Act of 1918 (40 Stat., 1104), as taxes on policies of insurance claimed by the Commissioner to have been issued by plaintiff.

During all the time herein involved plaintiff was a common carrier by railroad in interstate commerce, operating railroads or lines of transportation in the States of Virginia, North Carolina, South Carolina, Georgia, Florida, and Alabama. In April, 1899, there was organized, and has since been maintained, under the general auspices of the plaintiff, a certain voluntary association, composed of the employees of plaintiff, known as the "Relief Department of the Atlantic Coast Line Co."

Plaintiff alleges in its petition: "The primary object of this association was to create a trust fund out of which the members contributing thereto and becoming the beneficial owners thereof might be paid certain sums in case of sickness or disability on account of personal injury, and out of which trust fund, in the case of the death of any members, certain sums might be paid to the beneficiary or next of kin designated by such member."

Employees of the company were permitted voluntarily to become members of the relief fund by filing an application with the superintendent of the department and passing a satisfactory physical examination. When this application was approved by the superintendent there was issued a certificate to the employee, of which the following is a copy:

— "ATLANTIC COAST LINE RAILROAD CO. RELIEF DEPARTMENT.

"Certificates of Membership in the Relief Fund.

"This certifies that _____, employed by the Atlantic Coast Line Railroad Co., is a member of the Relief Fund of the Relief Department of the Atlantic Coast Line Railroad Co. and is entitled to the benefits provided by the regulations of the relief department for a member of the ---- class with ----- additional death benefits of the first class."

There are five classes of members, the classification being based upon the regular or usual monthly pay received by the employee.

On the death of a member of the relief fund, payments were made to his beneficiary in varying amounts from \$250 to \$1,250, according to the member's classification. In order to become a member the employee agreed to pay, by assignment in advance, into the trust fund of the relief department of the Atlantic [Coast Line] Railroad Co. a certain portion of his wages.

A member who had been continuously in plaintiff's service for three years and a member of the relief fund for one year immediately preceding the termination of his employment could retain his membership for the minimum death benefit only held by him during the last year of his employment by payment, quarterly in advance, in cash, of the necessary amount to cover death benefits only.

Out of something over 20,000 employees of plaintiff there were about 10,000 members of said relief fund. About 400 former employees retained their membership in said relief department as to death benefits. The regulations covering said relief fund provided that an advisory committee shall have general supervision of the operation of said relief department. The advisory committee consisted of plaintiff's general manager, ex officio a member and chairman, and 12 other members, 6 chosen annually by plaintiff's board of directors and 6 chosen annually by ballot by members of the relief fund.

Plaintiff alleges in its complaint:

"6. Your petitioner as an incident of its business as a common carrier, in order to afford the care and protection to its employees for which such association was organized, undertakes on behalf of the beneficial owners of such fund—

"(a) To collect and hold in trust the contributions or subscriptions made by the members thereof;

"(b) To pay all expenses of administering the fund so held, including salaries of officers and employees of the relief department; and

"(c) Guarantee to the members or beneficial owners of such fund that it shall be sufficient to provide the necessary hospital and medical treatment and, in the case of the disability of any member, to pay to him the sum to which he thereby becomes entitled, or, in the case of his death, to pay to his beneficiaries or next of kin the amount to which they thereby become entitled.

"7. For the service thus rendered to the employees who are members of such association in administering said fund, for the guarantee set forth in paragraph 6 of this petition, and for the payment of advances made thereunder, your petitioner receives no monetary consideration, but treats all such sums paid for salaries or for other administrative expenses of said fund, and all sums that it is called upon from time to time to pay into said fund to cover any deficiencies therein, as operating expenses of your petitioner."

The Revenue Act of 1918 contains the following provisions pertaining to the issues in the case at bar:

"SEC. 1 (40 Stat., 1057). That when used in this Act—

"The term 'person' includes partnerships and corporations, as well as individuals;

"The term 'corporation' includes associations, joint-stock companies, and insurance companies;

* * * * *

"SEC. 503 (40 Stat., 1104). That from and after April 1, 1919, there shall be levied, assessed, collected, and paid, in lieu of the taxes imposed by section 504 of the Revenue Act of 1917, the following taxes on the issuance of insurance policies; * * *

"(a) Life insurance: A tax equivalent to 8 cents on each \$100 or fractional part thereof of the amount for which any life is insured under any policy of insurance, or other instrument, by whatever name the same is called: * * *

* * * * *

"(d) Policies issued by any corporation enumerated in section 231, and policies of reinsurance, shall be exempt from the taxes imposed by this section.

"SEC. 504 (40 Stat., 1104). That every person issuing policies of insurance upon the issuance of which a tax is imposed by section 503 shall make monthly returns under oath, in duplicate, and pay such tax to the collector of the district in which the principal office or place of business of such person is located. Such returns shall contain such information and be made at such times and in such manner as the Commissioner, with the approval of the Secretary, may by regulation prescribe. * * *

"SEC. 231 (40 Stat., 1076). That the following organizations shall be exempt from taxation under this title:

* * * * *

"(3) Fraternal beneficiary societies, orders, or associations (a) operating under the lodge system or for the exclusive benefit of the members of a fraternity itself operating under the lodge system, and (b) providing for the payment of life, sick, accident, or other benefits to the members of such society, order, or association or their dependents;

* * * * *

"(6) Corporations organized and operated exclusively for religious, charitable, scientific, or educational purposes, or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private stockholder or individual;

* * * * *

"(10) Farmers' or other mutual hail, cyclone, or fire insurance companies, mutual ditch or irrigation companies, mutual or cooperative telephone companies, or like organizations of a purely local character the income of which consists solely of assessments, dues, and fees collected from members for the sole purpose of meeting expenses;"

Plaintiff contends that sections 504 and 503 of the Revenue Acts of 1917 and 1918, respectively, were intended to be, and are, merely reenactments of similar provisions in the Spanish War Revenue Act of June 13, 1898 (30 Stat., 448). It is unquestionable that section 503 of the Revenue Act of 1918 is a reenactment of section 504 of the Revenue Act of 1917, but there is a marked difference between the language covering exemptions in said sections 504 and 503 and that in the Spanish War Revenue Act of 1898 (30 Stat., 416).

While the language covering fraternal, beneficiary societies, orders, and associations operating under the lodge system is very similar in the three Acts, there is a marked difference, in that the Act of 1898 specifically mentions and exempts "farmers' purely local cooperative company or association, or employees' relief associations operated on the lodge system, or *local co-operation plan*, organized and conducted solely by the members thereof for the exclusive benefit of its members and not for profit." (30 Stat., 461.) [Italics ours.]

Here it will be seen that in the Act of 1898 exemption is given to "farmers'" purely local cooperative companies or associations and "employees' relief associations," operating not only on the lodge system but also on the *local cooperative plan*. [Italics ours.]

As we have before stated, the exemptions in section 503(d) of the Revenue Act of 1918 (40 Stat., 1076) are a practical reenactment, in so far as the issues in this case are concerned, of the exemptions in section 11(a) of the Revenue Act of 1916 (39 Stat., 766), and also of those in the Revenue Act of

1917 (40 Stat., 316, section 504(d)), for the Act of 1917 embraces by reference thereto the exemptions contained in section 11(a) of the Revenue Act of 1916 (39 Stat., 766).

It is disclosed in plaintiff's brief that when the Revenue Act of 1917 was reported to the House it contained the following provision, taken from the Revenue Act of 1898, as the committee report discloses:

"SEC. 504. That from and after the 1st day of June, 1917, there shall be levied, assessed, collected, and paid the following taxes on the issuance of insurance policies:

"(a) Life insurance: A tax equivalent to 8 cents on each \$100 or fractional part thereof of the amount for which any life is insured under any policy of insurance, or other instrument by whatever name the same is called: *Provided*, That the provisions of this subdivision shall not apply to any fraternal, beneficiary society or order, or farmers' purely cooperative company or association or employees' relief associations operated on the lodge system or local cooperative plan, organized and conducted solely by the members thereof for the exclusive benefit of its members and not for profit." [Italics ours.]

Had this provision referring specifically to "employees' relief associations" remained in the bill, it might well be argued, discarding for the moment any question as to the meaning of the phrase "local cooperative plan," that it would relieve plaintiff from the tax in question; but it was stricken from the bill by amendment, and in its place the exemptions of section 11(a) (Third) of the Revenue Act of 1916 (39 Stat., 766) were incorporated in the 1917 Act, by reference thereto, as follows:

"SEC. 11. (a) Third. Fraternal beneficiary society, order, or association, operating under the lodge system or for the exclusive benefit of the members of a fraternity itself operating under the lodge system, and providing for the payment of life, sick, accident, or other benefits to the members of such society, order, or association or their dependents; * * *

We have shown that the exemptions in section 231 of the Revenue Act of 1918 (40 Stat., 1076) were a practical reenactment of section 11(a) of the Revenue Act of 1916 (39 Stat., 766), and that the 1917 Act also included the provisions of said section 11(a).

It seems to us that the elimination of the specific provisions in the Revenue Act of 1917, as first reported to the House, exempting "employees' relief associations operated on the lodge system or local cooperative plan, organized and conducted solely by the members thereof for the exclusive benefit of its members and not for profit," is very persuasive as indicating the intention that they were not to be exempt, unless they may be classed as fraternal beneficiary associations operating on the "lodge system," which will be discussed hereafter. Yet, as we understand the plaintiff's contention, it claims that section 231 of the Act of 1918 and section 11(a) of the Act of 1916, which are practically identical, mean the same thing as the omitted clause.

"The rejection by Congress of a specific provision contained in an Act as originally reported is most persuasive to the conclusion that the Act should not be so construed as in effect to include that provision." (First Fed. Stat. An., 2d ed., sec. 45.)

"The fact that this provision measuring the amount of recovery by rebate was omitted from the Act, as finally reported to both Houses and passed, is not only significant, but so conclusive against the contention of the plaintiff that it quotes—not the report of the conference committee—but a statement, made by a member of the Senate conference committee, to support the present argument that section 8 means the same thing as the omitted clause. But while they may be looked at to explain doubtful expressions, not even formal reports—much less the language of a member of a committee—can be resorted to for the purpose of construing a statute contrary to its plain terms, or to make identical that which is radically different." (*Penna. R. R. Co. v. International Coal Co.*, 230 U. S., 184, 198.)

"But it is a familiar canon of interpretation that all former statutes on the same subject, whether repealed or unrepealed, may be considered in construing the provisions that remain in force." (*Viterbo v. Friedlander*, 120 U. S., 707, 725.)

(See also *U. S. v. Saunders*, 22 Wall., 492; *U. S. v. Farden*, 99 U. S., 10.)

Plaintiff's brief shows that when the Revenue Act of 1898 was under discussion in the Senate the provision with reference to life insurance in the bill contained the following exemption:

"That the provisions of this section shall not apply to any fraternal beneficiary society or order operated on the lodge system which is organized and conducted by the members thereof for the sole benefit of its members and not profit."

The above provision is similar to that in (3), section 231, of the Revenue Act of 1918.

Plaintiff sets forth in its brief the discussion which took place with reference to the question whether the above exemption embraced "employees' relief associations" when conducted for their own benefit and not for profit. Senators Aldrich and Wolcott expressed the opinion that they were within the exemptions.

Plaintiff quotes Senator Aldrich as saying:

"And I understand the lodge system to be an aggregation of employees or farmers or anybody else who carry on beneficiary insurance simply for their own benefit. That language was used in the statute heretofore and it has been construed to apply to that class of organization."

Plaintiff quotes Senator Spooner as saying:

"I think the Senator has drawn this so as to include a great many that ought not to be taxed."

Without entering into a discussion of how far the courts will go in considering the debates in Congress in interpreting statutes, we may observe that Senator Aldrich's view was not accepted is indicated by the fact that the provision was subsequently amended to read specifically referring to "employees' relief associations" operating both under the "lodge system" and "local cooperative plan," viz:

"Provided further, That the provisions of this section shall not apply to any fraternal, beneficiary society, or order, or farmers' purely local cooperative company or association, or employees' relief associations operated on the lodge system, or local cooperation plan, organized and conducted solely by the members thereof for the exclusive benefit of its members and not for profit." (30 Stat., 461.)

We are not content to rest our decision on any conclusion we may draw from the elimination of specific reference to "employees' relief associations" from the Act of 1917, or its insertion in the Act of 1898, however significant or persuasive such action on the part of Congress may appear.

We shall consider whether plaintiff is within any of the exemptions mentioned in (d) of section 503 of the Act of 1918, which provides that "policies issued by any corporation enumerated in section 231 and policies of reinsurance shall be exempt from the taxes embodied by this section."

Section 1, *supra*, of the Act of 1918 provides that when used in this Act—

"The term 'person' includes partnerships and corporations, as well as individuals;

"The term 'corporation' includes associations, joint-stock companies, and insurance companies; * * *

Plaintiff alleges in its petition that "for the benefit and protection of its employees a certain voluntary association was organized under the general auspices of your petitioner known as the 'relief department.'" At other places in the petition the "association" is referred to. In the regulations the "relief department" is referred to as "a department of the company's service, of the nature of a mutual benefit association." Approximately 10,000 employees of plaintiff were members. The affairs of the relief department were managed by executive officers, with duties similar to corporate officers, with an advisory committee exercising executive supervision analogous to that of the board of directors of a corporation.

Plaintiff's relief department is certainly within the purview of the language employed by Judge Graham in *Hardware Underwriters et al. v. The United States* (65 C. Cls., 267 [T. D. 4189, C. B. VII-2, 347]), where he states:

"The association is not incorporated, but this does not alter the fact that it is, in substance and in result of its operations, a mutual insurance company or a reciprocal association for the purpose of making insurance, and securing protection and paying losses. * * *

"To say that such an association is a mere place is to say that a written constitution that has been put in operation is still nothing more than a scrap of paper. This association is not a mere place; it is a living entity doing an insurance business through cooperation of its subscribers with the attorney in fact and advisory committee and performs all those things necessary to carry on effectively the business of making insurance.

* * * * *

"An 'association' has been defined, with approval by the Supreme Court, 'as a body of persons organized for the prosecution of some purpose, without a charter but having the general form and mode of procedure of a corporation.' It is clear in this case that the individuals or subscribers were engaged in the prosecution of a common enterprise, to wit, the business of a mutual insurance company, and had the general purpose and accomplished the same end as a formally incorporated association."

See also *Hecht v. Malley* (285 U. S., 144 [T. D. 3595, C. B. III-1, 489]); *Pickering v. Attea-Nichols Co.* (21 Fed. (2d), 501 [T. D. 4096, C. B. VI-2, 814]); and *Philadelphia & Reading Relief Association* (4 B. T. A., 713, 722).

Plaintiff contends that the contract entered into between the members of the relief department and itself is not a contract of insurance but one of beneficial relief, and cites, in support of this contention, *Beck v. Penna. Railroad* (63 N. J. L., 232), as a leading case on the subject involving a relief department similar to plaintiff's relief department.

Plaintiff's brief, in quoting from the above decision in the Beck case, italicizes the following: "*the contract between them is not of insurance but of beneficial relief.*" And also italicizes the following: "*not one of insurance, within the laws appealed to.*"

In order to estimate the weight to be given to the Beck case, we think that there should be applied to it the observation of Chief Justice Marshall in the case of *Cohens v. Virginia* (6 Wheat., 399):

"It is a maxim not to be disregarded, that general expressions, in every opinion, are to be taken in connection with the case in which those expressions are used. If they go beyond the case, they may be respected but ought not to control the judgment in a subsequent suit when the very point is presented for decision. The reason of this maxim is obvious. The question actually before the court is investigated with care, and considered in its full extent. Other principles which may serve to illustrate it, are considered in their relation to the case decided, but their possible bearing on all other cases is seldom completely investigated."

Also the following from *Corpus Juris* 15, page 941:

"Accordingly, in applying the rule of *stare decisis* to a former decision, the language of the opinion in the earlier case must be construed with reference to the particular facts presented in that case."

In the Beck case, Plaintiff Beck sued the railroad company to recover for a personal injury. The regulations governing the relief department of the railroad and the application for membership provided that the acceptance of benefits from the relief fund for injury or death should operate as a release for all claim for damage arising from injury or death.

Plaintiff Beck objected to the introduction of the release in evidence, on the ground that under the laws of New Jersey no contract to indemnify any person against loss by casualty to property or health or life could be made except by one incorporated for that purpose under the laws of a State or a foreign corporation formed for that purpose, which has complied with the State laws and obtained authority to transact its business in the State.

The trial judge excluded the evidence. The court of errors and appeals reversed the lower court and held the evidence admissible, and in addition to the excerpt from the opinion quoted in plaintiff's brief said:

"The purpose of the legislation appealed to is to regulate the business of insurance of various kinds by corporations who propose to do such business, and who hold themselves out as ready to contract for insurance with any person who applies, and agrees to the terms on which they offer to insure. If it be conceded that such business is a proper subject of legislative regulation, it is obvious that such regulations are not to be extended beyond the business intended to be regulated." (63 N. J. L., 241.)

It is apparent that the New Jersey court held merely that the contract of insurance with Beck was not one of insurance within the meaning of laws of

New Jersey prohibiting the execution of such contracts except by corporations authorized for that purpose. The effect of the holding was merely that the contract between Beck and the railroad company did not fall within the regulation of the insurance laws. We can not consider the Beck case applicable, in view of the very comprehensive language in section 503(a), *supra*, of the Act of 1918, which is as follows:

"(a) Life insurance: A tax equivalent to 8 cents on each \$100 or fractional part thereof of the amount for which any life is insured under any policy of insurance, or other instrument, *by whatever name the same is called.* * * * [Italics ours.]

Whatever may be the pertinency of the Beck case, the comment of the court in *Boston & M. R. R. v. United States* (265 Fed., 578) is in point, and equally applicable to State decisions, as well as to State statutes,

"If the principle were once accepted that the express terms of a Federal law imposing a Federal tax may be abridged, or enlarged, by force of local statutes, the General Government, as a result, would be forced to adopt different standards, and differing rules of taxation among the States—varying in accordance with the differing statutes of the various States, though the power to tax for Federal purposes resides with a single entity and emanates from a central and paramount Government. And, as a result of such diversity, there would be no uniformity, though governments exercise the essential and necessary power to impose the burdens of taxation under the impulse of the rightful and governing principle involved in the cardinal idea of uniformity."

Plaintiff's contract with the employees joining the relief department provided for payments ranging from \$250 to \$1,250 in case of death. To deny that this was a contract of life insurance under "any policy of insurance, or other instrument, *by whatever name the same is called,*" is to deny the obvious meaning of language.

Plaintiff's contract certainly meets all the requirements of various definitions of a contract of insurance. Premiums were paid for insurance by members of the relief department, by an assignment of their wages, while they were in the employ of the company, if they were on the wage roll, if not by payments in cash, and after their severance of employment with the company, by payment of premiums in cash. In case of death their beneficiaries are paid as stated before.

Mr. Justice Gray, in *Commonwealth v. Wetherbee* (105 Mass., 149), defines a contract of insurance as follows:

"A contract of insurance is an agreement, by which one party, for a consideration (which is usually paid in money, either in one sum, or at different times during the continuance of the risk), promises to make a certain payment of money, upon the destruction or injury of something in which the other party has an interest. In fire insurance and marine insurance, the thing insured is property; in life or accident insurance, it is the life or health of a person. * * * All that is requisite to constitute such a contract is the payment of the consideration by the one, and the promise of the other to pay the amount of the insurance upon the happening of injury to the subject by a contingency contemplated in the contract."

Joyce on Insurance, volume 1, section 7, defines life insurance as follows:

"Life insurance is a contract dependent upon human life, whereby one for a consideration agrees to pay another a certain sum of money upon the happening of a given contingency, or upon the termination of a specified period."

"A 'contract of life insurance' is an agreement between insurer and insured, whereby the insurer undertakes to pay a certain sum of money to a certain person, who may be and usually is a person other than the insured, upon the happening of a particular event, usually the death of insured, in consideration of payment by insured of certain premiums made at stated periods." (*Baltimore Life Insurance Co. v. Floyd*, 5 Boyce (Del.), 201, 91 Atl., 653.)

See also *Ritter v. Mutual Life Insurance Co.* (169 U. S., 139); *State v. Alley* (96 Miss., 720, 51 South, 487).

It remains to be seen whether, within the intent and meaning of any of the provisions of section 231 of the Revenue Act of 1918, plaintiff is exempt from the payment of the taxes imposed.

The following provisions, covering exemptions, are thought to be applicable by plaintiff:

"SEC. 231. That the following organizations shall be exempt from taxation under this title:

* * * * *

"(3) Fraternal beneficiary societies, orders, or associations, (a) operating under the lodge system or for the exclusive benefit of the members of a fraternity itself operating under the lodge system, and (b) providing for the payment of life, sick, accident, or other benefits to the members of such society, order, or association or their dependents;

* * * * *

"(6) Corporations organized and operated exclusively for religious, charitable, scientific, or educational purposes, or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private stockholder or individual;

* * * * *

"(10) Farmers' or other mutual hail, cyclone, or fire insurance companies, mutual ditch or irrigation companies, mutual or cooperative telephone companies, or like organizations of a purely local character, the income of which consists solely of assessments, dues, and fees collected from members for the sole purpose of meeting expenses."

It is well to refer here to some of the principles which have guided the courts in determining whether the taxpayer is entitled to exemption.

"Statutes and provisions exempting persons or property from taxation are strictly construed. * * *

"Legislation which is claimed to relieve any species of property from its due proportion of the general burdens of government should be so clear that there can be neither reasonable doubt nor controversy about its terms." Sutherland "Statutory Construction," section 539.

"The claim for exemption must be clearly made out. Taxes being the sole means by which the State can maintain its existence, any claim on the part of anyone to exemption from the full payments of his share of taxes on any portion of his property must on that account be clearly defined and founded upon plain language. There must be no doubt or ambiguity in the language upon which the claim is based. It has been said that where there is a well-founded doubt it is fatal to the claim." (*Hardware Underwriters et al. v. The United States*, 65 C. Cls., 267.)

This court said in *New York Trust Co. v. U. S.* (63 C. Cls., 102 [T. D. 4045, C. B. VI-2, 1891]):

"Plaintiff is claiming the benefit of an exemption from taxation, and the burden is upon it to show clearly that it is within the exemption claimed. (*Phoenix Fire & Marine Insurance Co. v. Tennessee*, 161 U. S., 174; *Chicago, Burlington & Kansas City R. R. v. Guffey*, 120 U. S., 569, 575; and *Metcalf & Eddy v. Mitchell*, supra [T. D. 3824, C. B. V-1, 218])."

The language of the Supreme Court in *Bank of Commerce v. Tennessee* (161 U. S., 134, 146) is very pertinent to the case at bar, in determining the applicability to plaintiff of the provisions above cited, from section 231 of the Act of 1918:

"These cases show the principle upon which is founded the rule that a claim for exemption from taxation must be clearly made out. Taxes being the sole means by which sovereignties can maintain their existence, any claim on the part of anyone to be exempt from the full payment of his share of taxes on any portion of his property must on that account be clearly defined and founded upon plain language. There must be no doubt or ambiguity in the language used upon which the claim to the exemption is founded. It has been said that a well-founded doubt is fatal to the claim; no implication will be indulged in for the purpose of construing the language used as giving the claim for exemption, where such claim is not founded upon the plain and clearly expressed intention of the taxing power."

The remarks of the court in *Cornell v. Coyne* (192 U. S., 418, 431) are very pertinent both as to the strictness of the rule to which the taxpayer is held who claims a statutory exemption and as a reply to the argument in plaintiff's brief in the case at bar:

"A literal interpretation of this statute, therefore, leads to the illogical conclusion that Congress intended to impose a tax upon the issuance of any kind of insurance policy, but permitted a certain class of persons to issue any kind of insurance policy without being subject to the tax."

In *Cornell v. Coyne* the court said:

"Clearly there is nothing in the body of the Act exempting exported filled cheese from the ordinary manufacturing tax on other filled cheese. But if there were a doubt as to the meaning of the statute, that doubt should be resolved in favor of the Government. Whoever claims a privilege from the Government should point to a statute which clearly indicates the purpose to grant the privilege.

"But if there be any doubt as to the proper construction of this statute (and we think there is none), then that construction must be adopted which is most advantageous to the interests of the Government. The statute being a grant of a privilege must be construed most strongly in favor of the grantor. (*Gildart v. Gladstone*, 12 East, 668, 675; *Charles River Bridge v. Warren Bridge*, 11 Pet., 420, 544; *Dubuque & Pacific Railroad v. Litchfield*, 23 How., 66; *The Binghamton Bridge*, 3 Wall., 51, 75; *Rice v. Railroad Co.*, 1 Black, 358, 380; *Leavenworth, Lawrence & Galveston Railroad v. United States*, 92 U. S., 733; *Fertilizing Co. v. Hyde Park*, 97 U. S., 659; *Hannibal, &c., Railroad Co. v. Packet Co.*, 125 U. S., 260, 271.)

"Why Congress should grant an exemption from manufacturing tax in the case of exported tobacco and not in the case of exported filled cheese, is not for us to determine. Doubtless the reasons which prompted such difference were satisfactory. It is enough that no exemption has been made in favor of the latter."

It is plaintiff's contention that Congress intended to impose the tax in question only on the issuance of policies by those engaged in the insurance business for profit.

The same contention was made in *Bankers' & Planters' Mut. Ins. Ass'n v. Walker* (279 Fed., 53 [T. D. 3318, C. B. 1-1, 259]), involving the identical provisions under the Revenue Act of 1917, but the circuit court of appeals held:

"This contention is unsound, because this is a purely life insurance arrangement and business, and section 504 does not require profits or dividends as a prerequisite to this tax."

Plaintiff's "relief department" possesses none of the indicia of a fraternal beneficiary society, order, or association, operating under the lodge system, to bring it within the provisions of (3), section 231, supra.

We think that article 514 of Regulations 45 of the Treasury Department, under the Revenue Act of 1918, properly defines "fraternal beneficiary societies operating under the lodge system" as they are ordinarily understood:

"Fraternal beneficiary societies: A fraternal beneficiary society is exempt from tax only if operated under the 'lodge system,' or for the exclusive benefit of the members of a society so operating. 'Operating under the lodge system' means carrying on its activities under a form of organization that comprises local branches, chartered by a parent organization and largely self-governing, called lodges, chapters, or the like. In order to be exempt it is also necessary that the society have an established system for the payment to its members or their dependents of life, sick, accident, or other benefits."

The decision of the Board of Tax Appeals, where a similar claim for exemption was made, is in point:

"In dealing with cases coming under section 231 of the Revenue Act of 1918, the character of the organization must be judged by its articles of incorporation, constitution, and by-laws, or by what other instrument it is governed. (*Corley v. Travelers' Protective Association*, supra; *Berry v. Knights Templars' & Masons' Life Indemnity Co.*, supra.) Search the petitioner's governing regulations as we may (it is the only instrument which has been offered to us), we are unable to discover, even in a remote degree, a single fraternalistic feature in its organization. It is entirely without any social features. Its membership is made up of individuals whose vocations are as numerous and diverse as the classifications of employment of a great railway system; the section hand, the freight hustler, the brakeman, the conductor in charge of a fast transcontinental train, the locomotive engineer, the train dispatcher, the clerk in the office, all are entitled to membership in the association for the mere asking, expressed in written application, provided no disability exists; and yet none of these look

to the petitioner for any betterment in social and laboring conditions. There is no fraternal object which moves them to seek membership in the association, but rather the motive is mercenary. The petitioner has neither lodges, rituals, ceremonial, or regalia; and it owes no allegiance to any other authority or jurisdiction. It is not a 'fraternal beneficiary association' operating under the lodge system, within the meaning of section 231(3) of the Revenue Act of 1918, and, therefore, is not entitled to exemption under the provisions of that section." (Appeal of Philadelphia & Reading Relief Association, 4 B. T. A., 713, 726.)

It is equally clear that plaintiff can not escape the tax under (6), section 231, supra, which exempts religious, charitable, scientific, and educational organizations. Obviously, plaintiff does not come within any of these four classes. Nor can we see how plaintiff falls within the exemptions of (10), section 231, aside from any question as to whether plaintiff's "relief department," operating in six different States, may be considered an organization of a "purely local character."

(10) provides for exemptions for—

"Farmers' or other mutual hail, cyclone, or fire insurance companies, mutual ditch or irrigation companies, mutual or cooperative telephone companies, or like organizations of a purely local character, the income of which consists solely of assessments, dues, and fees collected from members for the sole purpose of meeting expenses."

It could not be contended, with any degree of plausibility, that farmers' organizations, other than those operated under the lodge system, could be exempt from the life insurance tax under section 231, and certainly not under (10); for under that subdivision the farmers' organizations are granted an exemption for hail, cyclone, and fire insurance.

Under the principle of *expressio unius est exclusio alterius*, exemption for farmers' organizations could not be extended to life insurance under (10). Then, how can it be successfully urged that life insurance tax exemption is extended to the "like organizations" referred to in (10)?

It will be recalled, as above stated, that when the bill which became the Act of 1917 was reported to the House it contained a specific provision exempting "farmers' purely cooperative company or association or employees' relief associations operated on the * * * local cooperative plan * * *."

This provision was stricken from the bill, and, in lieu thereof, that which is substantially section 231 of the Act of 1918 was inserted. We do not find any life insurance tax exemption left in section 231 for farmers' organizations operating on the local cooperative plan, as distinguished from those operating under the lodge system, for (10) confines the farmers' exemptions to mutual hail, cyclone, and fire insurance companies. It would, indeed, be singular to read into (10) a life insurance tax exemption extended to employees' relief associations and not to the farmers' companies.

In *Neal v. Clark* (95 U. S., 708) the court says:

"It is a familiar rule in the interpretation of written instruments and statutes that 'a passage will be best interpreted by reference to that which precedes and follows it.' So, also, 'the meaning of a word may be ascertained by reference to the meaning of words associated with it.'"

The court further quotes from Broom's Legal Maxims:

"In the construction of statutes, likewise, the rule *noscitur a sociis* is very frequently applied; the meaning of a word, and consequently the intention of the legislature, being ascertained by reference to the context, and by considering whether the word in question and the surrounding words are, in fact, *eiusdem generis*, and referable to the same subject matter.

"It is a familiar rule in the construction of terms to apply to them the meaning naturally attaching to them from their context. *Noscitur a sociis* is a rule of construction applicable to all written instruments. Where any particular word is obscure or of doubtful meaning, taken by itself, its obscurity or doubt may be removed by reference to associated words. And the meaning of a term may be enlarged or restrained by reference to the object of the whole clause in which it is used." (*Virginia v. Tennessee*, 148 U. S., 519.)

"It would ignore the fact that the meaning of words is affected by their context and violate the settled rule that words which standing alone might have a wide and comprehensive import will, when joined with those defining specific acts, be interpreted in their narrower sense and understood to refer

to things of the same nature as those described in the associated list, enumeration, or class." (Cf. *Virginia v. Tennessee*, 148 U. S., 503, 519; *United States v. Chase*, 135 U. S., 255, 258; *Neal v. Clark*, 95 U. S., 704, 708; *United States v. Salen*, 235 U. S., 249.)

In *Bankers' & Planters' Mut. Ins. Ass'n v. Walker* (279 Fed., 53), passing on the identical provision in the Revenue Act of 1917, the court held that Congress did not intend to include life insurance in the expression "like associations." The court said:

"It is also evident that plaintiff does not come within the 'like organization of a purely local character, the income of which consists solely of assessments, dues, and fees collected from members for the sole purpose of meeting its expenses,' as set out in subdivision 'tenth' of section 11(a), above quoted. This is not a 'purely local' organization; its income is not collected for the mere purpose of 'meeting its expenses,' but goes much beyond this and covers insurance payments; and it is not a 'like organization,' such organizations being 'farmers' or other mutual hail, cyclone or fire insurance company, mutual ditch or irrigation company, mutual or cooperative telephone company. Life insurance is too well known and important for us to suppose that Congress would detail hail, cyclone, and fire insurance, and intend life insurance to be included in the general expression of 'like associations.' The plaintiff is clearly liable to the tax."

Our view that (10) of section 231 of the Act of 1918 did not include life insurance is strengthened by the fact that when said section 231 was reenacted in the Revenue Act of 1924 (43 Stat., 282), life insurance was added to the provisions of (10), as follows:

"(10) Benevolent life insurance associations of a purely local character, farmers' or other mutual hail, cyclone, casualty, or fire insurance companies, mutual ditch or irrigation companies, mutual or cooperative telephone companies, or like organizations; but only if 85 per centum or more of the income consists of amounts collected from members for the sole purpose of meeting losses and expenses."

"It is an accepted principle that for purposes of statutory construction, within certain limits, resort may be had to subsequent statutes." (*Douglas v. Edwards*, 298 Fed., 229, 238. Citing, with other cases, *Smietanka v. First Trust & Savgs. Bank*, 257 U. S., 602 [T. D. 3321, C. B. I-1, 210], and *Shwab v. Doyle*, 258 U. S., 529 [T. D. 3339, C. B. I-2, 312].)

In the *Smietanka* case, supra, Mr. Chief Justice Taft said:

"It is obvious that, in the Acts subsequent to that of 1913, Congress sought to make specific provision for the *casus omissus* in the earlier Act."

"This case is not unlike that of *United States v. Field* (255 U. S., 257). The Revenue Act of 1916 imposed a tax on the estate of a decedent at the time of his death. The Government sought to tax property passing under a decedent's testamentary execution of a general power of appointment. It was held that, while in equity, property passing under such a power might be treated as assets of the donee for the use of his creditors if executed in favor of a volunteer, it was not subject to distribution as part of the estate of the donee and was not taxable. In the later Act, such property was expressly included. This was thought by the court to show at least a legislative doubt whether the earlier Act included such property."

In *Shwab v. Doyle*, supra, the Supreme Court said:

"In the Revenue Act of 1918 (40 Stat., 1097) it reenacted section 202 of the Act of September 8, 1916, and provided that the transfer or trust should be taxed whether 'made or created before or after the passage of' the Act. And we can not accept the explanation that this was an elucidation of the Act of 1916, and not an addition to it, as averred by defendant, but regard the Act of 1918 rather as a declaration of a new purpose; not the explanation of an old one."

We are of the opinion that plaintiff's petition should be denied. Petition will be dismissed. It is so ordered and adjudged.

ESTATE TAX RULINGS.

TITLE III.—ESTATE TAX. (1926)

SECTION 303(a)1.—GENERAL.

REGULATIONS 70, ARTICLE 36: Claims against the estate.

Deduction on account of a subscription by the decedent to a corporation organized and operated exclusively for charitable purposes. (See G. C. M. 4784, page 385.)

REGULATIONS 70, ARTICLE 37: Taxes.

Deduction on account of a subscription by the decedent to a corporation organized and operated exclusively for charitable purposes. (See G. C. M. 4784, page 385.)

PROPERTY PREVIOUSLY TAXED.

REGULATIONS 70, ARTICLE 43: Property acquired in exchange.

VIII-42-4401
Ct. D. 123

ESTATE TAX—REVENUE ACT OF 1918—DECISION OF COURT.

DEDUCTION—TRANSFER PREVIOUSLY TAXED—IDENTIFICATION.

Where a statement shows the decedent's deposits, withdrawals, and daily bank balance from the date of the first receipt of securities from the estate of a prior decedent to the time of her death, the origin of each deposit, whether from sales of securities of the prior decedent or from other sources, and the purpose of cash withdrawals, whether for the purchase of securities whose value is claimed as a deduction or for other purposes, the value of the securities, which, at the time of her death, is deductible from the gross estate under section 403(a)2 of the Revenue Act of 1918, granting a deduction for property "which can be identified as having been acquired by the decedent in exchange for property" received from the prior decedent, can be ascertained on the following basis:

Where a withdrawal is made for a purchase of securities it is assumed that this money came from the sources other than the proceeds of securities which were a part of the prior decedent's estate, if there is a sufficient balance of that nature with which to make the purchase of securities. Where withdrawals are made for other purposes, it is assumed that the withdrawals came from the proceeds of securities which were a part of the prior decedent's estate to the extent that there are sufficient funds for that purpose.

DISTRICT COURT OF THE UNITED STATES FOR THE EASTERN DISTRICT OF
PENNSYLVANIA.

*United States of America v. Elmer E. Rodenbough, Executor of the Estate of
Elizabeth McCahan Rodenbough.*

[March 15, 1929.]

OPINION.

KIRKPATRICK, J.: This is an action brought by the United States to recover the balance of a deficiency assessment of estate tax in the estate of Elizabeth McCahan Rodenbough. A jury trial was waived by the parties. The facts were not in controversy and at the first trial the court found the law in favor of the plaintiff and entered judgment for the plaintiff for \$144,849.04. An appeal was taken to the circuit court of appeals, which court reversed this court in an opinion reported at 25 Fed. (2d), 13, and remanded the case with instructions. The case has been retried and is now before the court for findings and judgment.

The tax claimed was assessed under the Revenue Act of 1918. Since the decision of the circuit court of appeals in this case, the District Court for the District of Delaware has decided that, by reason of the repealing clause in the Revenue Act of 1921, the Revenue Act of 1918 was inoperative as to the estate of a decedent who died within a year prior to the enactment of the Act of 1921. (*Wilmington Trust Co. v. U. S.*, 28 Fed. (2d), 205.) This decision applies to the case now before the court, and the defendant contends that he is entitled to judgment on the law as announced in it.

I am unable to agree with the defendant that the point discussed and decided by Judge Morris in the case referred to can properly be considered by me at this time. The decision of the circuit court of appeals already rendered is the law of this case. The general principle is a familiar one, and is stated in *Thompson v. Maxwell Land Grant Co.* (168 U. S., 451), as follows: "It is the settled law of this court, as of others, that whatever has been decided on one appeal or writ of error can not be reexamined on a second appeal or writ of error brought in the same suit. The first decision has become the settled law of the case." (See also 4 C. J., page 1093, et seq.)

The principle is broad enough to apply to all questions necessarily involved in the decision of the former appeal, although some of them may not have been specifically dealt with in the opinion of the court. Whether it applies to a question like the present one, which was not even raised by the defendant (although the record now is exactly the same as it was at the time of the first trial and the question now raised could have been presented then), is a question for the circuit court of appeals on a subsequent appeal of this case. So far as the trial before me is concerned, I am precluded from considering the new issue by a corollary to the general rule above stated, which limits the duty of the inferior court on a remanded case to carrying out the terms of the mandate as sent down.

"Whatever was before the (appellate) court, and is disposed of, is considered as finally settled. The inferior court is bound by the decree as the law of the case; and must carry it into execution, according to the mandate. They can not vary it, or examine it for any other purpose than execution; nor give any other or further relief; nor review it upon any matter decided on appeal for error apparent; nor intermeddle with it, further than to settle so much as has been remanded." (*Sibbald v. U. S.*, 12 Peters, 488.) (See also *Illinois v. Ill. Cen. Ry. Co.*, 184 U. S., 77; *United States v. Camou*, 184 U. S., 572; *United States v. New York Indians*, 173 U. S., 464.)

In executing the mandate, reference may be had to the opinion of the appellate court. In this case, the circuit court of appeals said, "But at the trial of this case before the district court, the defendant * * * raised the issue of identification, which * * * the district court did not try out * * *. The case therefore must be remanded for trial on this issue, * * *." It is thus clear that the mandate requires this court to retry the case on one issue only, namely, what part of the securities claimed as exempt can be identified as "having been acquired by the decedent in exchange for property" received from the decedent's father's estate. Upon this issue no new evidence has been submitted, and the only thing bearing upon it before the court is therefore the statement (in evidence as Exhibit F) showing the decedent's deposits, withdrawals, and daily bank balance from the date of the

first receipt of securities from her father's estate, December 11, 1918, to the time of her death, October 17, 1921. The statement also shows the origin of each deposit, whether from sales of securities of her father's estate, or from other sources, and the purpose of cash withdrawal, whether for the purchase of securities whose value was claimed as a deduction or for other purposes.

Without discussing the theory of identification presented by the Government, we may say generally that it is clear from the opinion of the circuit court of appeals, first, that it was not the intention of that court to limit the exemption only to cases where the item claimed as a deduction can be traced to some other specific item of the estate of the prior decedent. The circuit court of appeals said: "If * * * the only evidence available is that stipulated in the form of the decedent's deposits, withdrawals and balances shown in her bank account, it will devolve on him (the defendant) to convince the court that, when properly analyzed, they distinguish between the *two* money sources and show figures by which the securities last purchased can be traced to the *father's estate* and be thus identified." This expression, together with the rationale of the entire opinion, makes it perfectly clear that all that is required is that the deduction claimed be identified as having been purchased with money which can be traced as having come from the sale of securities belonging to the estate of the decedent's father, without the necessity of showing what particular securities it came from. Second, it is also clear from the partial analysis of the statement of bank balances (Exhibit F) made by the circuit court of appeals that the method of computation for the purpose of tracing which this court was directed to adopt is that now contended for by the defendant. That method is stated in the defendant's brief, as follows: "Where a withdrawal is made for a purchase of securities it is assumed that this money came from the sources other than the proceeds of securities which were a part of the prior decedent's estate, if there is a sufficient balance of that nature with which to make the purchase of securities. Where withdrawals are made for other purposes, it is assumed that the withdrawals came from the proceeds of securities which were a part of the prior decedent's estate to the extent that there are sufficient funds for that purpose." A calculation was made in accordance with this method by the plaintiff's accountants and submitted to the defendant. It results in a tax due of \$22,335.36.

The defendant, while agreeing that the calculation is made in accordance with his views, so far as the method adopted is concerned, now claims that it should be corrected at three points: The first of these involves an item of withdrawal of \$103,725, withdrawn by the decedent from the bank on January 9, 1919. On that date, the decedent had in bank a deposit in excess of that amount, made up partly of money received from the sale of securities of her father's estate and partly of money received from other sources. The accountant treated the item as a withdrawal for the general purpose of the decedent and, in accordance with the theory of the computation, deducted it from that part of the decedent's balance which was derived from the sales of securities of her father's estate. The defendant claims that this is wrong, and that it should be deducted from the part of the balance which arose from general outside sources.

The item is entered in the column of withdrawals "for other purposes." A note appended to the stipulation, however, states that it is for the "purchase of securities not deducted under 403(a)2." This can be taken to mean more than that, with the item in question, the decedent bought some securities which her executor did not or does not now claim as deductible. The defendant goes further, however, and says that the securities purchased with this money were on hand at the time of the decedent's death. The reason why a deduction as to them was not claimed is not stated, but, as he says, that is immaterial. The only evidence which he can point to which might indicate that they are on hand is Schedule B-2, to his executor's decedent's executor, in which it appears that he returned "\$100,000 Philadelphia City 4½s due 1948, January and July 1, at 96.49, Philadelphia Exchange." Since the plaintiff does not admit that this item represents the \$103,725 in question or agree to the defendant's statement with regard to it, the matter must be determined by the evidence, and there is absolutely no evidence in the record now before the court to show that the securities purchased with the \$103,725 were the Philadelphia city bonds returned by the executor and no evidence to show that the securities so purchased were retained by the decedent or came into the hands of the defendant as her executor. For all that appears, whatever securities were purchased might have been sold the day after their purchase, and the money used for the decedent's personal expenses. I can not agree with the statement of the defend-

ant made on page 5 of his brief that the hypothesis on which the analysis is based requires *all* withdrawals for the purchase of securities to be treated as drawn from funds derived from sources other than the estate of the prior decedent. They should be so treated only when the securities in question are shown to be on hand at the decedent's death, and thus at least available as a claim for deduction whether actually so claimed or not. The other two items as to which the defendant contends that the analysis submitted by the plaintiff's accountants should be corrected fall into exactly the same category. None of the corrections or modifications contended for by the defendant in the analysis will be allowed, and the analysis will be accepted by the court as the basis for entry of judgment.

In accordance with the foregoing, judgment may be entered for the plaintiff in the sum of \$22,335.36, with interest from October 15, 1922.

TRANSFERS FOR PUBLIC, CHARITABLE, RELIGIOUS, ETC., USES.

REGULATIONS 70, ARTICLE 44: Transfers for
public, charitable, religious, etc., uses.
(Also Section 303(a)1, Articles 36 and 37.)

VIII-34-4319
G. C. M. 4784

The deduction authorized by section 303(a)1 of the Revenue Act of 1926 on account of claims against the estate and unpaid mortgages upon, or any indebtedness in respect to, property is limited to the extent that such claims, mortgages, or indebtedness were incurred or contracted bona fide and for an adequate and full consideration in money or money's worth received therefor by the decedent.

No deduction is authorized by section 303(a)3 of the Revenue Act of 1926 on account of a subscription for charitable purposes.

The question is presented to this office for an opinion whether, in determining the net estate for Federal estate tax under the Revenue Act of 1926, deduction may be made in the amount of x dollars on account of a subscription by the decedent to a corporation organized and operated exclusively for charitable purposes. The subscription, under the laws of the State, constituted a legal obligation of the decedent enforceable against his estate and payment thereof was made about 14 months after his death.

Deduction was claimed pursuant to section 303(a)1 of the Revenue Act of 1926, which provides:

For the purpose of the tax the value of the net estate shall be determined—
(a) In the case of a resident, by deducting from the value of the gross estate—

(1) Such amounts for * * * claims against the estate, unpaid mortgages upon, or any indebtedness in respect to, property (except, in the case of a resident decedent, where such property is not situated in the United States), to the extent that such claims, mortgages, or indebtedness were incurred or contracted bona fide and for an adequate and full consideration in money or money's worth * * * as are allowed by the laws of the jurisdiction * * * under which the estate is being administered * * *.

The precise question presented for determination under that subdivision is this: Does that subdivision require, as a condition to deduction on account of a valid claim against the estate, that such claim must have been incurred or contracted for an adequate and full consideration in money or money's worth, which moved or passed to the decedent?

Under the canons of construction it is settled that phrases similar in character repeated in a statute will be given the same meaning wherever used in the statute unless a different intent appears. Ac-

cordingly, the limiting phrase, " * * * to the extent that such claims, mortgages, or indebtedness were incurred or contracted bona fide and for an adequate and full consideration in money or money's worth * * *" contained in section 303(a)1 must be given the same meaning which is given to the corresponding phrases, similar in character, contained in section 302 (c), (d), (f) of the said Revenue Act. Under the referred to subdivisions of section 302, property transferred by trust or otherwise or affected by powers created, exercised, or relinquished by a decedent in contemplation of or intended to take effect at or after his death, is included in the gross estate "except in case of a bona fide sale for an adequate and full consideration in money or money's worth."

Subdivision (i) of section 302 provides:

If any one of the transfers, trusts, * * * or powers, enumerated and described in subdivisions (c), (d), and (f) of this section is made, created, exercised, or relinquished for a consideration in money or money's worth, but is not a bona fide sale for an adequate and full consideration in money or money's worth, there shall be included in the gross estate only the excess of the fair market value at the time of death of the property otherwise to be included on account of such transaction, over the value of the consideration *received therefor by the decedent*. [Italics supplied.]

Section 302 (c), (d), (f), and (i), it will be seen, contemplates that property transferred by trust or otherwise, or affected by powers created, exercised, or relinquished by a decedent in contemplation of or intended to take effect at or after his death, is taxable only to the extent that the transaction involving such property was not a bona fide sale for an adequate and full consideration in money or money's worth *received therefor by the decedent*.

In view of this situation, it is held that deduction is authorized by section 303(a)1 of the Revenue Act of 1926 on account of claims against the estate and unpaid mortgages upon, or any indebtedness in respect to, property only to the extent that such claims, mortgages, or indebtedness were incurred or contracted bona fide and for an adequate and full consideration in money or money's worth *received therefor by the decedent*.

It follows that inasmuch as the decedent received no consideration in money or money's worth for the subscription, no part of the amount subscribed may be deducted pursuant to section 303(a)1.

The executors suggested that if deduction could not be made pursuant to section 303(a)1, it might be made pursuant to section 303(a)3, which authorizes that there shall be deducted from the gross estate of a resident decedent:

The amount of all bequests, legacies, devises, or transfers * * * to or for the use of any corporation organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes * * *. The amount of the deduction under this paragraph for any transfer shall not exceed the value of the transferred property required to be included in the gross estate * * *.

Article 44 of Regulations 70, relating to the deduction authorized by paragraph (3), provides:

Deduction may be taken of the value of all property transferred by will or by the decedent in his lifetime not to exceed the value of the transferred property required to be included in the gross estate where * * * the property was transferred * * * to or for the use of any corporation or association organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes * * *.

Manifestly, the subscription does not come within the purview of paragraph (3) of section 303(a) and of article 44 of the regulations. Pursuant to this paragraph only the value of the property transferred by will or by the decedent in his lifetime is deductible. It is clear that the x dollars which were subscribed were not transferred to the charitable organization by the will of the decedent. It is also clear that after the subscription had been made, the decedent continued to hold the title to, and remained in the possession and enjoyment of, the x dollars until his death, when his title thereto and possession and enjoyment thereof passed to his executors. Such title, possession, and enjoyment were retained by the executors to the time when they paid the x dollars to the charitable organization, about 14 months after the death of the decedent, when the title to, as well as the possession and enjoyment of, the x dollars passed to the charitable organization and the transfer (of x dollars) was made.

Since the amount subscribed was neither transferred by will nor by the decedent in his lifetime to the charitable organization, the transfer of the x dollars does not come within the provisions of section 303(a)3 of the Act and of article 44 of Regulations 70, and deduction of that amount is not authorized by that section.

In view of the foregoing, no deduction from the gross estate may be made on account of the subscription in question.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

TITLE III.—ESTATE TAX. (1924)

GROSS ESTATE—GENERAL.

REGULATIONS 70, ARTICLE 10: Character of interests included. ARTICLE 14: Dower and curtesy.	VIII-33-4312 Ct. D. 92
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ESTATE TAX—REVENUE ACT OF 1924—DECISION OF COURT.

GROSS ESTATE—WIDOW'S STATUTORY INTERESTS—NEBRASKA—CONSTITUTIONALITY.

The value of the interest which a widow receives from the estate of her deceased husband under the laws of Nebraska should be included in determining the value of the decedent's gross estate under section 302 of the Revenue Act of 1924. The Federal estate tax on the transfer of such interest is constitutional.

UNITED STATES CIRCUIT COURT OF APPEALS, EIGHTH CIRCUIT.

A. B. Allen, Collector of Internal Revenue for the District of Nebraska, appellant, v. George F. Henggeler, Administrator, etc., appellee.

Appeal from the District Court of the United States for the District of Nebraska.

[March 25, 1929.]

OPINION.

McDERMOTT, District Judge, delivered the opinion of the court.

The plaintiff below (appellee here) brought this action against the collector of internal revenue of Nebraska to recover \$1,240.71, paid by the plaintiff as administrator of the estate of George Henggeler on account of the Federal estate tax. The collector declined to deduct the widow's one-third share set apart by the statutes of Nebraska. The plaintiff claims that such one-third interest vested in the wife at the time of her marriage; that it came to her, not

by reason of her husband's death, but by virtue of the statutes of Nebraska and her marriage; that Congress has no power to assess her property upon the occasion of her husband's death; that such is a direct tax, in violation of section 9, Article I of the Constitution, and in violation of the due process clause of the fifth amendment. It is alleged in the petition that the Supreme Court of Nebraska, in construing the statutes of Nebraska, has held that the wife "was, during the lifetime of said George Henggeler, vested with an absolute title inchoately to one-third of all of said estate, and that, as to such one-third interest, the said George Henggeler, deceased, until his death, held the title thereto for the use and benefit of the said Magdalena Henggeler, as the beneficial owner thereof, and, at his death, the absolute ownership and right to the possession thereof became complete in the said Magdalena Henggeler, by right and because of the marriage relation, and not by inheritance."

Plaintiff then alleges that section 302 of the Revenue Act of 1924 should not be construed to include such interest of the widow, and if construed to so include it, the section is violative of the constitutional provisions above referred to, and also section 2 of Article I, which provides that direct taxes must be apportioned among the States according to population. It is further alleged that the 1924 law can not constitutionally operate on a property interest which vested in her prior to its enactment. The petition does not disclose how much of this estate is in personal or real property.

The trial court overruled a demurrer to the petition; the defendant declined to further plead, and judgment was rendered as prayed for. This appeal follows.

Section 302 of the Revenue Act of 1924 provides:

"SEC. 302. The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated—

"(a) To the extent of the interest therein of the decedent at the time of his death which after his death is subject to the payment of the charges against his estate and the expenses of its administration and is subject to distribution as part of his estate;

"(b) To the extent of any interest therein of the surviving spouse, existing at the time of the decedent's death as dower, curtesy, or by virtue of a statute creating an estate in lieu of dower or curtesy."

Paragraph (a) above has been construed to be in the conjunctive; to fall within it, the deceased must have (1) an interest in property at the time of his death; which must be (2) subject to charges against his estate; and (3) which must be subject to distribution. (*United States v. Field*, 255 U. S., 257.) It has been held that a life estate in a decedent is not subject to the tax, for such estate is neither subject to the payment of debts, nor subject to distribution. (*Blount v. U. S.*, 59 Ct. Cls., 328.) In the present case, the husband undeniably has an "interest" in this property at the time of his death; the Nebraska statute in terms makes the interest "subject to his or her debts"; and likewise in terms provides, as to real estate, that it "shall descend * * * to the husband or wife," etc. As to personal property, the Nebraska statute expressly provides that it "shall be applied and distributed * * * in the same proportion to the same persons as prescribed for the descent of real estate." The statute further provides that "her right to inherit" may be cut off by antenuptial contract. There is no need to resort to judicial construction of such plain and unambiguous provisions. The property here involved is subject to the payment of debts of the deceased, and subject to distribution.

Paragraph (b) reaches expressly the interest of the surviving spouse, as dower, curtesy, or by virtue of any statute creating an estate in lieu of dower or curtesy. Unless this paragraph be unconstitutional, the Government must prevail. The appellee relies upon *Nichols v. Coolidge* (274 U. S., 531 [T. D. 4072, C. B. VI-2, 351]), in which it was held that Congress could not tax property in which the deceased had no interest at his death, and which had not been transferred in anticipation of death. If the decedent had no interest in this property which ceased at his death, Congress can not tax it. Our inquiry should be directed to the question of whether the deceased had any interest in this one-third at his death; if he did, it is taxable under either (a) or (b); and if so, whether the measure of the tax is unconstitutionally arbitrary.

The case was argued on the assumption that there is a conflict between the State and Federal decisions. There is no room for conflict in this case. Each jurisdiction has its own field, and in that field it is supreme. That the State statutes and decisions are binding on the Federal courts, as to the interest

which the wife and husband have in his property, is not open to dispute. (*Warburton v. White*, 176 U. S., 484; *U. S. v. Robbins*, 269 U. S., 315 [T. D. 3817, C. B. V-1, 188].)

Where the State courts have construed community property statutes to mean that husband and wife are substantially tenants in common, the Federal courts will so treat the husband's interest. (*Bek v. Miller*, 8 F. (2d), 797; T. Ds. 3138 [C. B. 4, 258], 3596 [C. B. III-1, 101], 3891 [C. B. V-2, 232].) While if the State courts, under similar statutes, hold the husband's title is more than that of a cotenant, the Federal courts will so treat his interest. (*Talcott v. U. S.*, 23 F. (2d), 897 [T. D. 4032, C. B. VI-2, 355].) In every case, the State statutes and State decisions are looked to for the purpose of determining the quantity and quality of the decedent's interest in property left by him.

But when that quantity and quality is found, then the Federal courts must determine whether such interest is taxable under the Federal estate tax law. It would indeed be unthinkable to hold that, under this Federal taxing law, an identical interest of the decedent (as determined by the State courts) should be taxed in Kansas and not in Nebraska, because the courts of the two States differently construe their own State inheritance tax laws.

Our first task, then, is to ascertain the interest of the *decedent*, if any, in and to the wife's one-third which ceased at his death. The amount and character of the wife's interest in such one-third, how and when it arose, is not the primary inquiry here. The inquiry here is, What interest did the *husband* have in this property which ceased at his death? The wife's interest is of importance only as it may cut down the husband's interest, for, of course, there can not be more than one whole interest.

It has been conclusively determined that the Federal estate tax is not levied on the right of inheritance; it is levied and measured by the interest or rights cut off by death. In *Y. M. C. A. v. Davis* (264 U. S., 47) the Supreme Court said:

"It was not a tax upon succession and receipt of benefits under the law or the will. It was death duties as distinguished from a legacy or succession tax. What this law taxes is not the interest to which the legatees and devisees succeeded on death, but the interest which ceased by reason of the death. (*Knowlton v. Moore*, 178 U. S., 41, 48, 49.)"

And in *Edwards v. Slocum* (264 U. S., 61 [T. D. 3584, C. B. III-1, 479]):

"It comes into existence before and is independent of the receipt of the property by the legatee. It taxes, as Hanson, Death Duties, puts it in a passage cited in 178 U. S., 49, 'not the interest to which some person succeeds on a death, but the interest which ceased by reason of the death.'"

To the same effect see *N. Y. Trust Co. v. Eisner* (256 U. S., 345) and *Chase National Bank v. U. S.*, decided January 2, 1929 [Ct. D. 40, C. B. VIII-1, 308].

Decisions under State laws taxing the right of succession or taxing property which passes by will or inheritance are therefore not in point; neither are decisions which declare that the rights of the widow are more than those of an heir, in that the latter may be cut off by conveyance or will. Decisions of this and other circuits, that a dower right is a valuable consideration for a contract involving its surrender, are of no assistance in determining the interest of the husband.

Starting with the proposition that all of the incidents of ownership are in the owner, we find that the Nebraska statute in question has impaired them to this extent: (1) Real estate of which the husband is seized of an estate of inheritance during the marriage, or in which he possessed either a legal or equitable interest at death, which has not been conveyed by husband and wife while residents of the State, or by the husband while the wife was a nonresident, and which has not been sold on execution or judicial sale, and which has not been lawfully devised, shall descend (under the circumstances here) one-third to the wife.

It is then provided that "the right of a married man or woman to inherit a part or all of the real estate * * * may be barred by a conveyance executed" as above provided, and "by the sale of such real estate under execution or other judicial sale, during the lifetime of the owner of the title."

(2) Personal property, of which the husband shall die possessed, and not lawfully disposed of by will, shall be distributed as provided therein. (It will be noted that there is no provision for the resident wife joining in a conveyance of personal property, and the statute does not operate on personal property of which the husband was possessed "during his marriage" as in the case of real estate.)

(3) The right is given the widow to elect to take under the law, notwithstanding any will.

(4) The wife's interest in both real and personal property is subject first to the payment of the debts of the husband's estate, which includes the costs of administration.

The Nebraska decisions have done no violence to the plain intentment of these statutes. The supreme court of that State held that the wife's interest was not subject to the State inheritance tax law, in a case which is the backbone of appellee's position. The court said:

"Under the present law the interest of the wife in the personal property of her husband is similar to that of a silent partner. The husband is, in effect, the managing agent and has control of the property. He can sell and dispose of it, or he may exchange it for other property. But at his death her interest therein comes to her in her own right. It does not pass to her by will, or by the intestate laws of the State. The husband can not deprive her of that right. (*Gaster v. Estate of Gaster*, 92 Neb., 6.)

"It has been held by the great weight of authority that dower is not immune because it is dower, but because it, like the right to the homestead, and to the distributive share of the widow of the estate of her deceased husband, belonged to her inchoately during his life, and vested fully in her at his death. The widow's share of the estate of her deceased husband, by the present inheritance law, is given to her in lieu of dower, and it follows that the interest of the appellant in her deceased husband's estate, both real and personal, comes within the test of immunity.

"Under the present statute the wife takes her interest in the estate of her deceased husband by operation of law. She can not be deprived of that interest by his will. It is something which belongs to her absolutely and independently of any right of inheritance or succession. Strictly speaking, the widow's share should be considered as immune, rather than exempt, from an inheritance tax. It is free, rather than freed, from such tax. It is not excepted from the taxable class because it never was in such class. Like all debts, taxes, costs, expenses, and other similar items, it is deducted before any inheritance tax is assessed. The share of the realty and personality, which under our law go to the widow independent of any will or act of the husband, is not, so to speak, a part of his estate, and is no more liable to a succession tax at his death than is her individual property, derived from her own ancestors and held in her own name, though the husband may have had the management and control of the estate during his lifetime." (In re Strahan, 93 Neb., 328.)

This is the most favorable description of the wife's rights in the Nebraska decisions. Yet there is nothing in that decision, or any other, that alters the very substantial rights which, under the Nebraska statute, the husband enjoys in this one-third interest, during his lifetime, and which cease at his death; and, it must always be remembered, the Federal estate tax law operates on rights that cease, and not rights that accrue, upon death. Giving full weight to the Nebraska court's description of the wife's interest, the facts still remain that the husband has at least the following very substantial rights in such property:

He has the exclusive right of possession; the exclusive right to the income incident thereto; all of it can be taken for his debts; he has therefore the exclusive right to use it as a basis for credit; he has the right to have it all applied to the payment of his debts upon his death; as to the personal property he has the further and exclusive right of transfer and disposition and of gift, and can likewise convey real estate if his wife is not a resident of Nebraska; he has the power to convey real estate, without his resident wife's signature, and put his purchaser into possession, and if his wife predeceases him, the title is absolute. He has every right of ownership, save that he can not will it without her consent; and as to real estate with a resident wife, his deed is conditioned on him outliving her; and, perhaps, he can not give away or dissipate property in fraud of her.

These rights of the husband are among the most valuable incidents of ownership. The right of possession and enjoyment of the income, the right to use it as a basis for credit, and the right to pay his debts with it, are most important attributes of ownership. And these are all "interests" which he enjoys in his own property, under the statutes and decisions of Nebraska, and which cease at his death.

As a matter of fact, the Nebraska statutes and decisions are very much like those of many other States, and it is matter of common knowledge that a widow has much greater rights in her one-third or one-half, as the case may be, after

death than she does before. Upon the death of her husband, she "comes into" her property. The very substantial rights which her husband has in the one-third cease at his death.

Upon argument, counsel for the appellee stressed the point that her rights sprang from her marriage and the statute, and his death was but the occasion of the enjoyment. This argument has been fully met and completely answered, since the argument, by the Supreme Court in the case of *Chase Nat. Bank v. U. S.*, supra. In that case, the decedent had taken out life insurance payable to his wife, with the right reserved in him to change the beneficiary. The face value of the policies was held to be subject to the estate tax. The arguments against taxing this insurance money were almost identical with the arguments made in this case. In fact, the plaintiff in the Nyberg case, infra, relied largely on the analogy to life insurance, and the decision in *Frick v. Lewellyn* (298 Fed., 803), holding such proceeds not taxable. In the Chase National Bank case, the court dealt with section 402, Revenue Act of 1921, which includes the proceeds of life insurance policies, as the corresponding section 302 of the Act of 1924 includes the "interest of the surviving spouse." The same constitutional objections were made there as here, and denied. It was urged there that the wife's right came from the contract with the insurer and not from the decedent; just as it is urged here that the wife's right comes from the statute and not from the death of her husband. That was admitted but held to be immaterial. It was urged there that the wife's right "vested" prior to her husband's death, just as is urged here. The court held, that even if that were so, it would not be material. The court, upon the matter of vesting, said, quoting from *Saltonstall v. Saltonstall* (276 U. S., 260):

"So long as the privilege of succession has not been fully exercised it may be reached by the tax. (See *Cahen v. Brewster*, 203 U. S., 543; *Orr v. Gilman*, 183 U. S., 278; *Chanler v. Kelsey*, supra; *Moffit v. Kelly*, supra; *Nickel v. Cole*, supra.) And in determining whether it has been so exercised technical distinctions between vested remainders and other interests are of little avail, for the shifting of the economic benefits and burdens of property, which is the subject of a succession tax, may even in the case of a vested remainder be restricted or suspended by other legal devices. A power of appointment reserved by the donor leaves the transfer, as to him, incomplete and subject to tax. (*Bullen v. Wisconsin*, 240 U. S., 625.) The beneficiary's acquisition of the property is equally incomplete whether the power be reserved to the donor or another."

Other similarities might be pointed out. The court, however, decides this case, when it ruled:

"The precise question presented is whether the termination at death of that power and the consequent passing to the designated beneficiaries of all rights under the policies freed of the possibility of its exercise may be the legitimate subject of a transfer tax, as is true of the termination by death of any of the other legal incidents of property through which its use or economic enjoyment may be controlled.

"A power in the decedent to surrender and cancel the policies, to pledge them as security for loans, and the power to dispose of them and their proceeds for his own benefit during his life which subjects them to the control of a bankruptcy court for the benefit of his creditors, and which may, under local law applicable to the parties here, subject them in part to the payment of his debts, is by no means the least substantial of the legal incidents of ownership, and its termination at his death so as to free the beneficiaries of the policy from the possibility of its exercise would seem to be no less a transfer within the reach of the taxing power than a transfer effected in other ways through death.

"Termination of the power of control at the time of death inures to the benefit of him who owns the property subject to the power and thus brings about, at death, the completion of that shifting of the economic benefits of property which is the real subject of the tax, just as effectively as would its exercise, which latter may be subjected to a privilege tax. (*Chanler v. Kelsey*, 205 U. S., 466.) 'To make a distinction between a general power and a limitation in fee is to grasp at a shadow while the substance escapes.'"

And, later on, the court said the question of whether there was a "vesting" was not determinative; that "the freeing of the remainder of the possibility of the exercise of that power" was sufficient to subject property to a tax. So, if the wife's interest was vested but inchoate, as alleged in the petition (a question assumed but not decided), it is of no moment.

In an effort to distinguish this case, it was argued that the insured in the cited case could, by changing the beneficiary, entirely wipe out the wife's interest; he has the same power in Nebraska as to personal property, and also as to real estate by the simple expedient of changing his legal residence to Council Bluffs, Iowa, or any other State. But aside from that, the fact still remains that in the case at bar the decedent had many important rights in this property, which ceased at his death. The same principle, under different facts, was applied in *Reinecke v. Northern Trust Co.*, decided by the Supreme Court on January 2, 1929 [T. D. 4261, C. B. VIII-1, 305].

The Court of Claims arrived at the same conclusion in an identical case from Nebraska, on June 18, 1928, in *Nyberg v. United States* [T. D. 4230, C. B. VII-2, 362]. Certiorari was denied November 26, 1928.

The rights of a Nebraska wife are certainly not greater than the rights of a California wife in community property; yet the Supreme Court held that the husband was taxable on its income as if he were the sole owner. (*U. S. v. Robbins*, 269 U. S., 315 [supra].)

Decisions cited by appellee from some of the other community property States are not in point, for in those States the wife has an estate in the property not unlike that of a tenant in common; her interest is subject to her separate devise, and under certain circumstances the property is subject to partition; she is entitled to a joint enjoyment of the income; such community property is immune from his debts incurred without her consent; and there are other incidents of a common ownership. But in Nebraska this property is subject to his debts, and not hers; is for his enjoyment, and not hers. Her interest comes into realization after his death, after the payment of his debts, is subject to certain family allowances, and her interest may not be in fact identified, in many cases, until the debts are proven, the costs of administration ascertained, and the election of the widow made.

A secondary contention is made to the effect that, even if it be taxable, the tax is not properly measured. The answer may be found in *Chase Nat'l Bank v. U. S.* (supra), *U. S. v. Robbins* (269 U. S., 315), *Brushaber v. U. P. R. R. Co.* (240 U. S., 1), *Flint v. Stone Tracy Co.* (220 U. S., 107), *Maxwell v. Bugbee* (250 U. S., 525), and in other cases. It can not be said that the action of Congress, in measuring the tax by the value of the property that is freed from the decedent's interests and rights and powers, is so arbitrary as to amount to confiscation. Again it should be recalled that the widow is not being taxed for the privilege of succession; the estate is taxed upon the occasion of the cessation of rights of the decedent.

The case will be reversed and remanded for further proceedings in consonance with this opinion.

TITLE III. PART II.—GIFT TAX.

REGULATIONS 67, ARTICLE 1: Transfers reached.

VIII-51-4474

Ct. D. 140

GIFT TAX—REVENUE ACT OF 1924—DECISION OF SUPREME COURT.

GIFT TAX—CONSTITUTIONALITY.

The tax imposed by the Revenue Act of 1924, upon a transfer of property by gift inter vivos, not made in contemplation of death, is constitutional.

SUPREME COURT OF THE UNITED STATES.

Joseph H. Bromley v. Blakely D. McCaughn, Collector of Internal Revenue for the First District of Pennsylvania.

On certificate from the United States Circuit Court of Appeals for the Third Circuit.

[November 25, 1929.]

OPINION.

Mr. Justice STONE delivered the opinion of the court.

In this case, pending in the Court of Appeals for the Third Circuit, that court has certified to this questions of law concerning which it asks instructions

for the proper disposition of the cause. Judicial Code, section 239, as amended by Act of February 13, 1925.

Bromley, a resident of the United States, brought the present suit in the District Court for Eastern Pennsylvania, to recover a tax alleged to have been illegally exacted, upon gifts made by him after the effective date of section 319(a) of the Revenue Act of 1924 (43 Stat., 253, 313), as amended by section 324(a) of the Revenue Act of 1926 (44 Stat., 9, 26). This section imposes a graduated tax "upon the transfer by a resident by gift" during the calendar year "of any property wherever situated * * *". In computing the amount of the gift subject to the tax, section 321, in the case of a resident, exempts gifts aggregating \$50,000, gifts to any one person which do not exceed \$500, and certain gifts for religious, charitable, educational, scientific, and like purposes. The questions certified are:

1. Are the provisions of sections 319-324 of the Revenue Act of 1924, as amended by section 324 of the Revenue Act of 1926, when applied to transfers of property by gift inter vivos, made after the effective dates of the cited Revenue Acts and not made in contemplation of death, invalid, because they violate (a) the third clause of section 2 and (b) the fourth clause of section 9 of Article I of the Constitution in that the tax they impose is a direct tax and has not been apportioned?

2. Are the cited provisions, when applied to transfers of property made in like circumstances, invalid because they violate (a) the fifth amendment to the Constitution and (b) the first clause of section 8 of Article I of the Constitution in that they impose a tax which is graduated and subject to exemptions and therefore lacks uniformity, and also deprive a person of his property without due process of law?

1. The first question was mooted by counsel, but not decided in *Blodgett v. Holden* (275 U. S., 142 [T. D. 4117, C. B. VII-1, 324]), and *Untermeyer v. Anderson* (276 U. S., 440 [T. D. 4157, C. B. VII-1, 326]). The general power to "lay and collect taxes, duties, imposts and excises" conferred by Article I, section 8, of the Constitution, and required by that section to be uniform throughout the United States, is limited by section 2 of the same article, which requires "direct" taxes to be apportioned, and section 9, which provides that "no capitation or other direct tax shall be laid unless in proportion to the census" directed by the Constitution to be taken. As the present tax is not apportioned, it is forbidden if direct.

The meaning of the phrase "direct taxes" and the historical background of the constitutional requirement for their apportionment have been so often and exhaustively considered by this court (*Hylton v. United States*, 3 Dall., 171; *Pollock v. Farmers Loan & Trust Co.*, 157 U. S., 429, 158 U. S., 601; *Knowlton v. Moore*, 178 U. S., 41; *Nicol v. Ames*, 173 U. S., 509, 515) that no useful purpose would be served by renewing the discussion here. Whatever may be the precise line which sets off direct taxes from others, we need not now determine. While taxes levied upon or collected from persons because of their general ownership of property may be taken to be direct (*Pollock v. Farmers Loan & Trust Co.*, 157 U. S., 429, 158 U. S., 601), this court has consistently held, almost from the foundation of the Government, that a tax imposed upon a particular use of property or the exercise of a single power over property incidental to ownership, is an excise which need not be apportioned, and it is enough for present purposes that this tax is of the latter class. (*Hylton v. United States*, supra, cf. *Vezie Bank v. Fermo*, 8 Wall., 533; *Thomas v. United States*, 192 U. S., 363, 370 [T. D. 3170, C. B. 4, 25]; *Billings v. United States*, 232 U. S., 261; *Nicol v. Ames*, supra; *Patton v. Brady*, 184 U. S., 608; *McCrary v. United States*, 195 U. S., 27; *Scholey v. Rew*, 23 Wall., 331; *Knowlton v. Moore*, supra; see also *Flint v. Stone-Tracy Co.*, 220 U. S., 107; *Spreckels Sugar Refining Co. v. McClain*, 192 U. S., 397; *Stratton's Independence v. Houbert*, 231 U. S. 399; *Doyle v. Mitchell Bros. Co.*, 247 U. S., 179, 183; *Stanton v. Baltic Mining Co.*, 240 U. S., 103, 114.)

It is a tax laid only upon the exercise of a single one of those powers incident to ownership, the power to give the property owned to another. Under this statute all the other rights and powers which collectively constitute property or ownership may be fully enjoyed free of the tax. So far as the constitutional power to tax is concerned, it would be difficult to state any intelligible distinction, founded either in reason or upon practical consideration of weight, between a tax upon the exercise of the power to give property *inter vivos* and the disposition of it by legacy, upheld in *Knowlton v. Moore*,

supra, the succession tax in *Scholey v. Rew*, supra, the tax upon the manufacture and sale of colored oleomargarine in *McCray v. United States*, supra, the tax upon sales of grain upon an exchange in *Nicol v. Ames*, supra, the tax upon sales of shares of stock in *Thomas v. United States*, supra, the tax upon the use of foreign-built yachts in *Billings v. United States*, supra, the tax upon the use of carriages in *Hylton v. United States*, supra; compare *Veazie Bank v. Fenno*, supra, 545, *Thomas v. United States*, supra, 370.

It is true that in each of these cases the tax was imposed upon the exercise of one of the numerous rights of property, but each is clearly distinguishable from a tax which falls upon the owner merely because he is owner, regardless of the use or disposition made of his property. (See *Billings v. United States*, supra; cf. *Pierce v. United States*, 232 U. S., 290.) The persistence of this distinction and the justification for it rest upon the historic fact that taxes of this type were not understood to be direct taxes when the Constitution was adopted and, as well, upon the reluctance of this court to enlarge by construction limitations upon the sovereign power of taxation by Article I, section 8, so vital to the maintenance of the National Government. (*Nicol v. Ames*, supra, 514, 515.)

It is said that since property is the sum of all the rights and powers incident to ownership, if an unapportioned tax on the exercise of any of them is upheld, the distinction between direct and other classes of taxes may be wiped out, since the property itself may likewise be taxed by resort to the expedient of levying numerous taxes upon its uses; that one of the uses of property is to keep it, and that a tax upon the possession or keeping of property is no different from a tax on the property itself. Even if we assume that a tax levied upon all the uses to which property may be put, or upon the exercise of a single power indispensable to the enjoyment of all others over it, would be in effect a tax upon property (see *Dawson v. Kentucky Distilling & Warehouse Co.*, 255 U. S., 288), and hence a direct tax requiring apportionment, that is not the case before us.

The power to give can not be said to be a more important incident of property than the power to use, the exercise of which was taxed in *Billings v. United States*, and even though differences in degree may be carried to a point where they produce distinctions in kind, the present levy falls so far short of taxing generally the uses of property that it can not be likened to the taxes on property itself which have been recognized as direct. It falls, rather, into that category of imposts or excises which, since they apply only to a limited exercise of property rights, have been deemed to be indirect and so valid although not apportioned.

2. The uniformity of taxation throughout the United States enjoined by Article I, section 8, is geographic, not intrinsic. A graduated tax, on legacies, granting exemptions (*Knowlton v. Moore*, supra), or on incomes (*Brushaber v. Union Pacific R. R.*, 240 U. S., 1) does not violate this clause of the Constitution, nor are such taxes infringements on the fifth amendment. (*Knowlton v. Moore*, supra, 109; *Brushaber v. Union Pacific R. R.*, supra, 24, 25.) Graduated taxes on inheritances or successions, with provisions for exemptions, have so often been upheld as not violating either the due process or the equal protection clauses of the fourteenth amendment (*Stebbins v. Riley*, 268 U. S., 137) as to leave little ground for supposing that taxation by Congress embracing these features, and otherwise valid, could be deemed a denial of the due process clause of the fifth. See *Van Oster v. Kansas* (272 U. S., 465, 468).

It is suggested that the schemes of graduation and exemption in the present statute, by which the tax levied upon donors of the same total amounts may be affected by the size of the gifts to individual donees, are so arbitrary and unreasonable as to deprive the taxpayer of property without due process. But similar features of State death taxes have been held not to infringe the fourteenth amendment, since they bear such a relation to the subject of the tax as not "to preclude the assumption that the legislature, in enacting the statute, did not act arbitrarily or without the exercise of judgment and discretion which rightfully belong to it." (*Stebbins v. Riley*, supra, 145.) No more can they be a basis for holding that the graduation and exemption features of the present statute violate the fifth amendment.

The answer to both questions is, No.

TITLE IV.—ESTATE TAX. (1918, 1921, AND 1924)

GROSS ESTATE—GENERAL.

REGULATIONS 68, ARTICLE 10: Character of interests included. ARTICLE 14: Dower and curtesy.

VIII—28—4270
Ct. D. 79

ESTATE TAX—REVENUE ACTS OF 1918 AND 1921—DECISION OF COURT.

GROSS ESTATE—WIDOW'S STATUTORY INTEREST—MISSOURI.

The value of the interest which a widow receives under the laws of Missouri in the estate of her deceased husband should be included in the value of the gross estate under section 402 of the Revenue Acts of 1918 and 1921.

UNITED STATES CIRCUIT COURT OF APPEALS, EIGHTH CIRCUIT.

United States of America, appellant, v. A. H. Waite et al., appellees.

Noah Crooks, Collector of Internal Revenue for the Western District of Missouri, appellant, v. A. H. Waite et al., appellees.

Noah Crooks, Collector of Internal Revenue for the Western District of Missouri, appellant, v. Mary Z. Hibbard, Administratrix of the estate of Charles D. Zook, Deceased, appellee.

Appeal from the District Court of the United States for the Western District of Missouri.

[May 30, 1929.]

OPINION.

Scott, District Judge, delivered the opinion of the court.

The three foregoing entitled cases were argued and submitted together. They involve identical questions. Nos. 8425 and 8426 grow out of an estate tax assessed and paid on the estate of Alfred H. Rogers, deceased, under the Revenue Act of 1918. The reason for two cases is that certain payments of the tax assessed were paid to George F. Crutchley, collector of internal revenue for the western district of Missouri, who, before subsequent payments were made, died. Recovery for excess of such payments are attempted in case No. 8425, brought in the court below against the United States. Subsequent payments were made to Noah Crooks, collector of internal revenue for said district, and recovery of alleged excess payments to him are attempted in case No. 8426, brought in the court below against said Crooks, as collector. Case No. 8427 grows out of certain alleged excess payments of estate tax assessed and paid on the estate of Charles D. Zook, deceased, under the Revenue Act of 1918. The material allegations of the petitions in the three cases are substantially the same, *mutatis mutandis*. We shall, therefore, state them without repetition.

Taking the petition in case No. 8425, as an illustration, plaintiffs in their petition allege in substance that they are the duly qualified executors of the estate of Alfred H. Rogers, deceased, who died March 6, 1920, leaving surviving him, as heirs, his widow, Katherine C. Rogers, a son, Harrison C. Rogers, and a daughter, LeClaire Rogers Estes. That Alfred H. Rogers died testate but that within the time required by the statutes of Missouri, and on July 30, 1920, Katherine C. Rogers, widow, filed in the Probate Court of Jasper County, Mo., a rejection of said will, by the terms of which she refused to accept the provisions thereof and elected to take under the statutes of said State, and reserved to herself in the estate of the decedent her marital rights, to wit, a child's part in lieu of the provisions made by said will. (Then follows certain allegations relative to the widow's rights under State statutes, and certain proceedings in the State courts over State inheritance tax assessments, and the result of such proceedings, all of which we do not deem of importance here, being argumentative only.) That pursuant to the terms of the Revenue Act of 1918, on the 22d day of January, 1921, plaintiffs filed with the collector of internal revenue

for the western district of Missouri a return on Form 23A by which they showed that A. H. Rogers was possessed at the time of his death of an estate of \$892,389.97, on which there was due a tax of \$42,891.20, which said tax within the time required by statute was by the plaintiffs paid to the collector of internal revenue for said district. That subsequently an examiner, representing the Treasury Department, examined said estate, and on the 11th day of April, 1923, the Deputy Commissioner of Internal Revenue notified plaintiffs of an additional tax liability of \$25,549.23, based upon an increase of valuation. That subsequently and within the time required by statute and provided by the rules of the Treasury Department, they filed pleas *sic* in abatement directed to the question of the valuation of the property, and claiming an exemption of that part of the tax which was assessed against the marital rights of Katherine C. Rogers, and that the tax assessed was excessive and illegal. That said plea *sic* in abatement based upon the contention that the interest of Katherine C. Rogers was not subject to tax and the tax was illegal was overruled by the Department on the 26th day of December, 1923, and the plea *sic* in abatement based on the original valuation was overruled in part and allowed in part on the 24th day of November, 1923, and that plaintiffs were required to pay an additional sum of \$23,665.11. That said additional tax was on the 25th day of February, 1924, paid. That on the — day of September, 1924, and within the time allowed by statute, plaintiffs filed a claim for refund with the Treasury Department asserting that the collection of tax by the Department was illegal and erroneous, and claiming a refund of \$34,759.80 on account of payment of taxes upon that part of the estate of A. H. Rogers, which under the laws of the State of Missouri belonged to Katherine C. Rogers. That subsequently on the 4th day of December, 1924, said claim for refund was rejected. That plaintiffs paid to George F. Crutchley, collector, etc., a total sum of \$42,891.20. That they paid to Noah Crooks, collector, etc., the sum of \$24,755.75, making a total tax payment of \$65,546.95, the amount being assessed by the Internal Revenue Department against said estate. (The above alleged payment to Noah Crooks, collector, is the payment for which recovery is asked in case No. 8426.)

Plaintiffs then plead that the following provision of the Revenue Act of 1918—

"Sec. 402. That the value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated—

* * * * *

"(b) To the extent of any interest therein of the surviving spouse, existing at the time of the decedent's death as dower, courtesy, or by virtue of a statute creating an estate in lieu of dower or courtesy;"

should not be construed to authorize or require the inclusion as part of the gross estate of said decedent subject to said estate tax the interest in the property above described belonging to and vesting in Katherine C. Rogers as aforesaid; that in so far as said provision has been so construed by the taxing authorities and said authorities have assumed to require the said interest as surviving wife of the decedent to be included as part of the said gross estate, that said Act of Congress and the provisions thereof aforesaid, as well as the construction and application thereof by the taxing authorities, were and are in conflict with the following provisions of the Constitution of the United States, to wit, that part of section 2, Article I, providing as follows:

"Representatives and direct taxes shall be apportioned among the several States which may be included within this Union, according to their respective numbers, which shall be determined by adding to the whole number of free persons, including those bound to service for a term of years, and excluding Indians not taxed, three-fifths of all other persons. The actual enumeration shall be made within three years after the first meeting of the Congress of the United States, and within every subsequent term of 10 years, in such manner as they shall by law direct"

and that part of section 9, Article I, as follows, to wit:

"No capitation, or other direct, tax shall be laid, unless in proportion to the census or enumeration herein before directed to be taken."

That the imposition of the said Federal estate tax upon the interest of Katherine C. Rogers in said property was, in substance and effect, a direct tax upon said property not laid, imposed, or apportioned in accordance with the foregoing provisions of the Constitution of the United States, but in violation thereof, and was not and is not a tax or excise upon property derived by

Katherine C. Rogers from the said decedent through descent, transfer, inheritance, devise, or gift. That the material rights of Katherine C. Rogers in the property of Alfred H. Rogers, deceased, was of the value of \$396,880.28, and that deducting that amount from the total value of said estate, the amount of legal tax due would be \$32,787.15. That the collection of \$34,759.80 additional was erroneous and without warrant of law. That of that sum \$25,441.50 was paid by plaintiffs to Noah Crooks, collector, etc., and that suit has been instituted against Noah Crooks (No. 8426) to recover said excessive collection, and that said sum \$8,131.40 was paid to George F. Crutchley, collector, etc. That George F. Crutchley has departed this life, and as in such case made and provided, this suit is instituted against the United States of America for the purpose of recovering said excess and erroneous tax. A prayer then follows for judgment for \$8,131.40.

In cases No. 8426 and 8427 the prayers are for the respective amount of the alleged excess. In No. 8427, the amount involved is \$15,377.99, alleged to have been erroneously assessed upon the interest of Emma D. Zook, widow, in the estate of Charles D. Zook.

To the respective petitions in these cases the defendants demurred upon the ground that the petitions failed to state facts sufficient to constitute causes of action. These demurrers were all overruled and the defendants elected to stand upon the demurrers. In each case judgment was entered against the defendants for the respective sums prayed for, and exceptions duly preserved. From the judgments so entered the United States and Noah Crooks, collector of internal revenue for the western district of Missouri, respectively, have appealed.

The Revenue Act of 1918 provides:

"SEC. 401. That (* * *) a tax equal to the sum of the following percentages of the value of the net estate (determined as provided in section 403) is hereby imposed upon the transfer of the net estate of every decedent dying after the passage of this Act;

* * * * *

"SEC. 402. That the value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated—

"(a) To the extent of the interest therein of the decedent at the time of his death which after his death is subject to the payment of the charges against his estate and the expenses of its administration and is subject to distribution as part of his estate;

"(b) To the extent of any interest therein of the surviving spouse, existing at the time of the decedent's death as dower, courtesy, or by virtue of a statute creating an estate in lieu of dower or courtesy."

The following are sections from the Revised Statutes of Missouri, 1919, relating to the estate of decedents, and previously existing in other publications during the period material to this discussion:

"SEC. 303. *Real and personal estate descends, to whom.*—When any person having title to any real estate or inheritance, or personal estate undisposed of, or otherwise limited by marriage settlement, shall die intestate as to such estate, it shall descend and be distributed in parcenary, to his kindred, male and female, subject to the payment of his debts and the widow's dower, in the following course: First, to his children, or their descendants, in equal parts; second, if there be no children, or their descendants, then to his father, mother, brother, and sister, and their descendants in equal parts; third, if there be no children, or their descendants, father, mother, brother, or sister, nor their descendants, then to the husband or wife; if there be no husband or wife, then to the grandfather, grandmother, uncles and aunts, and their descendants, in equal parts; fourth, if there be no children or their descendants, father, mother, brother, sister, or their descendants, husband or wife, grandfather, grandmother, uncles, aunts, nor their descendants, then to the great-grandfathers, great-grandmothers, and their descendants, in equal parts; and so on, in other cases, without end, passing to the nearest lineal ancestors and their children, and their descendants, in equal parts.

"SEC. 315. *Dower in real estate.*—Every widow shall be endowed of the third part of all the lands whereof her husband, or any other person to his use, was seized of an estate of inheritance, at any time during the marriage, to which she shall not have relinquished her right of dower, in the manner prescribed by law, to hold and enjoy during her natural life. Dower in leasehold

estate for a term of 20 years or more shall be granted and assigned as in real estate; for a less term than 20 years, shall be granted and assigned as in personal property.

"SEC. 319. *Share of widow or widower in personal estate.*—When the husband or wife shall die, leaving a child or children or other descendants, the widow or widower shall be entitled absolutely to a share in the personal estate belonging to the husband or wife at the time of his or her death equal to the share of a child of such deceased husband or wife.

"SEC. 324. *Child's part, when taken in lieu of dower.*—When the husband shall die, leaving a child or children or other descendants, the widow, if she has a child or children by such husband living, may, in lieu of dower of the one-third part of all lands whereof her husband died or shall die seized of an estate of inheritance, to hold and enjoy during her natural life, elect to be endowed absolutely in a share of such lands equal to the share of a child of such deceased husband. The provisions of this section shall be subject to the payment of her husband's debts."

A decision of these cases involves consideration of three questions:

1. What is the character of the tax imposed; is it a direct tax on property, or an excise or a death duty upon the transfer of property?

2. Assuming that the tax is not direct, was there a transfer within the meaning of the Revenue Act in question of the shares of the respective widows in the real estate and personal estate of the deceased husbands?

3. Did the respective classes of property taken by the widows under the statutes of Missouri fall within the requirements of sections 401 and 402 of the Revenue Act of 1918?

We shall discuss these questions in the order stated. The late Chief Justice White, then Mr. Justice White, in *Knowlton v. Moore* (178 U. S., 41), in premising the opinion of the court in that case, said: "The inquiry whether the taxes are direct or indirect must involve the prior determination of the objects or rights upon which by law they are imposed and assessed, since it becomes essential primarily to know what the law assesses and taxes in order to completely learn the nature of the burden." The quoted statement was made, however, some 30 years ago before the path was beaten to the objective of the inquiry. The case of *Knowlton v. Moore*, supra, and the numerous cases following since its time, we think have settled the question and fully determined that the tax imposed by the sections of the Revenue Act in question was not intended to be a direct tax, but an excise or death duty in the sense in which those terms have been understood since the time when provision for the imposition of taxes of that character first found place in the legislation of this country. Mr. Justice White, in the case cited, further said: "Taxes of this general character are universally deemed to relate, not to property *eo nomine*, but to its passage by will or by descent in cases of intestacy, as distinguished from taxes imposed on property, real or personal, as such, because of its ownership and possession." And again: "What it taxes is not the interest to which some person succeeds on a death, but the interest which ceased by reason of the death." And again in the same opinion: "Confusion of thought may arise unless it be always remembered that, fundamentally considered, it is the power to transmit or the transmission or receipt of property by death which is the subject levied upon by all death duties." We are not advised that the Supreme Court of the United States has ever departed from the principle announced in *Knowlton v. Moore*, supra, when considering the character of the tax in question. On the contrary, that principle seems to have been observed in all of the following cases: *United States v. Field* (255 U. S., 257); *New York Trust Co. v. Eisner* (256 U. S., 345); *Edwards v. Slocum* (264 U. S., 61 [T. D. 3584, C. B. III-1, 479]); *Nichols v. Coolidge* (274 U. S., 531 [T. D. 4072, C. B. VI-2, 351]); *Reinecke v. Northern Trust Co.* (49 S. Ct., 123 [T. D. 4261, C. B. VIII-1, 3051]); *Chase National Bank v. United States* (49 S. Ct., 126 [Ct. D. 40, C. B. VIII-1, 308]); and a legion of other cases. Indeed, there seems to be no contention in these cases that the tax in question was intended to be other than an excise or death duty. The contention, however, seems to be rather that the imposition of the tax in question upon the particular interest of a surviving spouse under the statutes of Missouri makes it equivalent of a direct tax because it is contended there was no transfer as to such interests. We shall discuss this phase of the case under the second question.

Taking up the second question, Was there a transfer, within the meaning of the Revenue Act, of the shares of the respective widows in the real estate and personal estate of the deceased husbands?

In determining this question we must consider not only the language of the Act itself and pronouncements of the Supreme Court in those instances in which that court has given interpretation and limitation to that particular term, but also the nature of the interest of the decedent at the time of his death, and the nature of the interest of the surviving spouse both before and after the death of the decedent. This is particularly true because these cases are pioneer cases, no cases having heretofore arisen so far as we are advised under statutes similar to the Missouri statutes in question. Careful examination and analysis of the sections of the Missouri statutes quoted bring us to the conclusion that the language of section 315, "Every widow shall be endowed of the third part of all the lands whereof her husband, or any other person to his use, was seized of an estate of inheritance, at any time during the marriage, to which she shall not have relinquished her right of dower in the manner prescribed by law, to hold and enjoy during her natural life," implies common law dower. "Common law dower is an estate of freehold, not of inheritance. Dower is measured by the husband's interest in the land, and can rise no higher. The common law right of dower entitles the wife to a life estate, and a life estate only, in one-third of all the lands and tenements of which the husband was seized of an estate of inheritance at any time during the coverture." (19 C. J., 460.) "The seizin at common-law must have been of an estate of inheritance, with a freehold vested in the deceased husband." (19 C. J., 465.) "For no estate of freehold can commence *in futuro*; because it can not be created at common law without livery of seizin, or corporal possession of the land; and corporal possession can not be given of an estate now, which is not to commence now, but hereafter." (2d Cooley's Blackstone, 143 (*144).) "Since it is within the power of the legislature to diminish, alter, or abolish dower so long as the right thereto is merely inchoate, but not after it becomes consummate by the death of the husband, it follows as a general rule that the widow's right to dower in lands of which the husband died seized is governed by the law in force at the time of his death." (19 C. J., 461.) (Citing numerous Missouri cases among others.) We quote the foregoing texts in order to emphasize the characteristics of common law dower not only so far as that right pertains to the surviving spouse, but as it pertains to the estate of the husband upon which the right of the surviving spouse rests. So considered it is quite clear that a surviving widow's right of dower under the statutes of Missouri while inchoate, has not all the attributes of absolute property. This is true not only when considering constitutional guaranties, but when considering the right of a legislature to abolish or modify the right. Much has been said in the briefs and in oral argument about the widow's right under the statutes of Missouri, as construed by the supreme court of that State, being her absolute property and subject neither to the husband's disposition or his debts. Yes, quite true. But *what* was her absolute property? Manifestly the right of common law dower; and the alternative right to elect to relinquish that right of common law dower and take a child's share in the estate of the decedent with its incident, liability for the payment of the husband's debts, and distribution as a part of his estate.

Recurring again to the language of the Supreme Court in *Knowlton v. Moore*, supra: "What it taxes is not the interest to which some person succeeds on a death, but the interest which ceased by reason of the death." Measured and tested by the characteristics of common law dower, let us inquire what was the interest that ceased by reason of death and what was its characteristic? To constitute foundation for common law dower the husband must not only have been seized of an estate of inheritance, but he must have had the freehold estate and that freehold estate ceased on his death, and immediately there ripened the freehold estate for life in the surviving widow. Whatever verbal quibbles and controversies may be indulged in, a more plain case of transfer by death can not well be imagined, when we consider the freehold estate for life in the husband which is the essential foundation for dower and the freehold estate for life thereafter in the widow which is the estate of common law dower. Under section 303, real estate of inheritance descends to the husband's kindred subject to the widow's dower. We think that simply means that on the death of a freehold estate for life in one-third of the lands vested in the surviving widow. All of the rest of such estate, including the remainder in the one-third part assigned to the widow as dower, passed to the kindred. We therefore come to the conclusion that on the death of a husband intestate seized of an estate of inheritance in lands and leaving a widow surviving there is under section 315 of the Missouri statutes quoted a transfer within the meaning of

section 401 of the Revenue Act of 1918, subject in case a child or children also survive, to the right of such widow to elect to take in lieu of such dower under section 324 of the Missouri statutes, the share of a child.

Now, what was the share of a child? Manifestly it is that share provided in section 303 of the Missouri statutes, supra, which the child takes in any real estate inheritance of which the deceased had title at the time of his death and which the child takes absolutely and to the extent of the estate of inheritance of which the father was seized. The widows in the instant cases elected to take the shares of a child under section 324, supra. The share of the child in the real estate upon such election thereupon vested absolutely rather than "to hold and enjoy during her natural life," but "subject to the payment of her husband's debts." We think there was no less a transfer of this child's share on the death of the husband and the election of the widow than in case there had been no such election. On the contrary, it would seem that in the latter case if possible the transfer is more apparent, for here the widow takes the entire estate in the portion assigned in lieu of dower.

But what we have said does not entirely dispose of the question. Most if not all of the decisions of the Supreme Court where the inclusion of the subject was questioned because of the contention that it was not a part of the estate of the decedent, turned upon the power and right of disposition during the life of the decedent rather than upon the power and right of use and enjoyment during that period. That was true in *Reinecke v. Northern Trust Co.*, supra, and in *Chase National Bank v. United States*, supra, and in many of the cases cited in the opinions in those cases. But the present cases it would seem must turn upon the power and right of use and enjoyment in the husband during life. That is, Do the "economic benefits" which may be the subject of the tax necessarily include the power and right of disposition in the decedent during his lifetime, where there is a power and right of use and enjoyment during life? In answering this question it must be borne in mind that the estate, gross and net, is an estate defined by the Act of Congress. It must be further borne in mind that dower and estates created in lieu of dower are expressly included in the estate so defined by Congress. Therefore, it would seem that in the last analysis we are brought to the question, Had Congress the power to so define the estates, and would so doing, in effect, as applied to such property, make the tax a direct tax? The decisions turning upon the power of disposition have frequently arisen in case of trusts, but we have found no case and none has been called to our attention where a trust has been created reserving a life use to the settlor, but not reserving power of disposition. While the question is a close one, we are not prepared to say that Congress has not the power to levy an excise tax or death duty where only the use and enjoyment remained vested during the lifetime of the decedent. To so hold would at least conflict with the Supreme Court's approval in *Knowlton v. Moore*, supra, of the text in Hanson's Death Duties that "What it taxes is not the interest to which some person succeeds on death, but the interest which ceased by reason of the death."

We come now to the third question, Did the respective classes of property taken by the widows under the statutes of Missouri fall within the requirements of sections 401 and 402 of the Revenue Act of 1918? The petition in none of the cases makes it clear whether there is personal estate involved. The burden of the arguments on the briefs proceeds on the question of dower rights existing under the Missouri statutes. However, there is discussion which indicates there is both real and personal property involved, but how much of each class does not appear on the face of any of the petitions demurred to. We shall assume, however, for the purpose of this opinion, that there is both real and personal property. In this connection it is argued on the briefs that the real estate is not subject to the payment of expenses of administration and hence does not fall within the requirements of subdivision (a), section 402. We think the answer to this contention is that the real estate is not necessarily required to fall within the scope of that subdivision. Subdivision (b) expressly says: "To the extent of any interest therein of the surviving spouse, existing at the time of the decedent's death as dower, courtesy, or by virtue of a statute creating an estate in lieu of dower or courtesy." This language seems to expressly cover the interest of the widow in the real estate involved in these cases, as the portion taken by election is clearly an estate created in lieu of dower. Indeed, section 324 of the Missouri statutes expressly says "in lieu of dower of the one-third part of all lands whereof her husband died or shall die seized of an estate of inheritance," etc. It is next contended that the widow's share in the personal property does not fall within the requirements of subdivision (a) in

that it is not subject to the payment of charges against the estate. We think this contention is not sound. Section 319 of the Missouri statutes provides as follows: "When the husband or wife shall die, leaving a child or children or other descendant, the widow or widower shall be entitled absolutely to a share in the personal estate belonging to the husband or wife at the time of his or her death equal to the share of a child of such deceased husband or wife." Supreme Court of Missouri in *Messersmith v. Messersmith* (264 Mo., 610, 175 S. W., 914) held that under this section (then Revised Statutes, 1909, section 349) the widow takes as a distributee and not as a doweress, citing *Howard v. Strode* (242 Mo., 218, 146 S. W., 792) and *Lich v. Lich* (158 Mo. App., 424, 138 S. W., 565). Indeed, when we recur to section 303, supra, we find that the child's share is expressly made subject to the payment of debts. But counsel contend that the Supreme Court of Missouri in *re Rogers' Estate* (250 S. W., 576), decided that the share of the widow given by section 319 is not subject to the payment of the husband's debts. We do not think the Missouri court in that case so decided. No such question was involved in *In re Rogers' Estate*. The only question there involved was whether the widow's share should be included in the valuation in assessing the State inheritance tax, and the statute creating that tax did not require as an essential to its imposition that the property be liable for the debts of the decedent. The remarks of Mr. Judge White that "the provision in section 324 is subject to the payment of the husband's debts, while that of section 319 is not," seems to have been made merely in passing, and we think purely *obiter dictum*. The reason for not mentioning liability for payment of debts in section 319 is quite obvious, for the "child's share" had been expressly made liable for the payment of debts in section 303, while the widow's dower in that section was in effect relieved of liability for the payment of debts, and hence the further necessity for special mention in section 324, when a child's share is taken in lieu of dower. But the widow's shares in the personal property in the instant cases were not taken in lieu of dower under section 324, but under section 319, and we think in that case the widow's rights were measured by the rights of a child. We do not think we are bound to follow the *dictum* of the opinion in *In re Rogers' Estate*. The Supreme Court of the United States in *Carroll v. Lessee of Carroll* (16 How., 275), Mr. Justice Curtis speaking for the court, said: "If the construction put by the court of a State upon one of its statutes was not a matter in judgment, if it might have been decided either way without affecting any right brought into question, then, according to the principles of the common law, an opinion on such a question is not a decision. To make it so, there must have been an application of the judicial mind to the precise question necessary to be determined to fix the rights of the parties and decide to whom the property in contestation belongs."

"And therefore this court and other courts organized under the common law, has never held itself bound by any part of an opinion, in any case, which was not needful to the ascertainment of the right or title in question between the parties." We think that so far as the personal estate of the respective decedents are concerned, that they come within the requirements of subdivision (a) of section 402, supra.

It follows from the conclusions reached in this opinion that the district court was in error in each of the cases under consideration in overruling the demurrers and in rendering judgment in favor of the plaintiffs. Each of the cases is therefore reversed, and the respective causes remanded with direction to the district court to sustain the respective demurrers.

Reversed and remanded.

VAN VALKENBURGH, Circuit Judge, concurring.

I concur in the conclusion reached by Judge Scott in the foregoing opinion, but the conditions presented in these cases differ so materially from those in cause No. 8325, *United States v. Gould Dietz*, just decided by us, that I desire to state some of my reasons for so doing.

In causes No. 8425 and No. 8426, Alfred H. Rogers died testate, leaving a widow and two children surviving him. The will was probated and the widow rejected the terms thereof and elected to take a child's share of the estate. Whether the estate consisted of personal property alone, or both real and personal, does not appear. As the main argument is addressed to the inherent nature of dower, the latter situation may be presumed. The estate then would fall under sections 319 and 324 R. S. Mo., 1919.

In No. 8427, Charles D. Zook died intestate, leaving his widow and a daughter surviving him. The widow elected to take a child's share of the realty. The estate consisted of both real and personal property, the value of each class not pleaded. The widow also takes, without the necessity of election, a child's share in the personality. Here, again, sections 319 and 324 apply.

The Supreme Court of Missouri in *Howard v. Strobe* (242 Mo., 210, 219, 221) holds specifically that the portion of the husband's personality given to the widow by section 349 (319) is not dower; that the wife, under that section, is not a doweress but a distributee; that as such distributee, she takes subject to debts of the husband, and her interest can be ascertained only upon final settlement of the estate. Furthermore, that as such distributee, she stands in the same relation to the personal estate as does a child. *Weindel v. Weindel* (126 Mo., 640) is cited with approval to the same effect. In that case (l. c. 650, 651) it is assumed that the widow's share in the personality under section 4517 R. S. Mo., 1889 (sections 349 and 319) is subject to the debts of her deceased husband. In *re Estate of Messersmith* (264 Mo., 610, 619), *Howard v. Strobe*, supra, is cited and approved as to the character, capacity, and relationship of the widow under section 349 (319). These cases dispose of the holding of the St. Louis Court of Appeals in *Schaper's Executor v. Schaper* (158 Mo. App., 605) that, under section 349 (319), the widow takes the share of a child in respect to quantity only, and does not take in the character and capacity of a child, and speak more authoritatively with respect to subjecting to the husbands' debts personality taken under section 319 than does the casual and unnecessary reference in *In re Rogers' Estate* (250 S. W., 577). Section 558 R. S. Mo., 1919, imposed a tax upon transfer of property "when the transfer is by will or by the intestate laws of this State from any person dying possessed of the property while a resident of the State." The opinion proceeds to demonstrate that the laws by which the widow elected to take, on renunciation of the will, are not intestate laws" and, therefore, the property which she acquired was not subject to the State inheritance tax. It will thus be seen that the question there presented was entirely different from that before us. Furthermore, there can be no conflict between State and Federal jurisdiction in this regard. Each is supreme in its own field. (*Allen, Collector, v. Henggeler, Admin.*, C. C. A., 8, decided March 25, 1929.) It is true that the law of the State fixes "the quantity and quality of the decedent's interest in property left by him"; but, in determining whether any interest is taxable under Federal law, "the Act of Congress has its own criteria, irrespective of local law, that look to rather severe tests of liability and exemption." (*Weiss v. Wiener*, 279 U. S., 333, decided April 22, 1929, Ct. D. 60 [C. B. VIII-1, 257].)

I confess that prior to the decisions of the Supreme Court in *Reinecke v. Northern Trust Co.* (49 Sup. Ct. Rep., 123) and in *Chase National Bank v. United States* (49 Sup. Ct. Rep., 126), I should have thought that the absolute and indefeasible character of the estate vested in the wife under the Missouri statutes, as construed by the supreme court of that State, would exempt that estate from inclusion in the gross estate of a decedent under the provisions of section 402 of the Revenue Act of 1918. Sections 315, 319, 324, 325, and 326 R. S. Mo., 1919; *Collier on Bankruptcy* (13th ed.), volume 2, page 1697; *Hoit v. Hanley* (244 Mo., 352); *Blevins v. Smith* (104 Mo., 583); *McCalnahan v. Porter* (10 Mo., 746); *Roberts v. Nelson* (86 Mo., 21); *Davis v. Evans et al.* (102 Mo., 164); *McCrillis v. Thomas* (110 Mo. App., 699); *Porter v. Lazaer* (109 Mo., 84); *Marine National Bank v. Swigart* (C. C. A., 6) (262 Fed., 854); *Thomas v. Woods* (C. C. A., 8) (173 Fed., 585, 586, 592); and that the following language in *Nichols v. Coolidge* (274 U. S., 531, 542, 543) would have controlling application:

"And we must conclude that section 402(c) of the statute here under consideration, in so far as it requires that there shall be included in the gross estate the value of property transferred by a decedent prior to its passage merely because the conveyance was intended to take effect in possession or enjoyment at or after his death, is arbitrary, capricious, and amounts to confiscation."

It may be added that the great weight of prior decision, both State and Federal, was to this effect. It is true that the subject matter under consideration in the *Chase National Bank* and *Reinecke* cases differs in marked degree from that now before us, but the language employed in those opinions is susceptible of wide application and would seem to be decisive of the cases at bar if so extended. "The determination by death of any of the other legal

incidents of property through which its use or economic enjoyment may be controlled" is pronounced a "transfer" and is made the legitimate subject of this tax. It is stated that the word "transfer" is not used in the commonly understood and restricted sense of the transmission of property directly from decedent to a transferee, and that:

"Termination of the power of control at the time of death inures to the benefit of him who owns the property subject to the power and thus brings about, at death, the completion of that shifting of the economic benefits of property which is the real subject of the tax."

Possession, use, enjoyment, or control by the decedent are evidently made the test. The property here involved responds thereto. As to real estate, the husband has full possession, use and enjoyment during his lifetime, and control, short of conveyance or incumbrance in hostility to the dower interest. The personal property he may use and dispose of as he pleases, in regular course. It follows, then, under the cases cited, that the three conditions conjunctively essential to render an estate taxable under clause (a) of section 402, to wit, (1) an interest of the decedent at the time of his death, (2) subject after his death to the payment of charges against his estate and expenses of administration, and (3) subject to distribution as part of his estate, are all present. (*United States v. Field*, 255 U. S., 257.)

In deference to the latest rulings of the Supreme Court, as I construe them, I am constrained to concur in the reversal of these judgments.

TITLE IV.—ESTATE TAX. (1921)

DEDUCTIONS—GENERAL.

REGULATIONS 70, ARTICLE 29: Deduction of claims, expenses, etc.

VIII-44-4416
Ct. D. 128

ESTATE TAX—REVENUE ACT OF 1921—DECISION OF COURT.

(1) DEDUCTION—AMOUNT STIPULATED IN ANTENUPTIAL CONTRACT IN LIEU OF DOWER.

Where a widow elects to accept the provision of the will of her deceased husband in her favor in lieu of the amount provided by an antenuptial contract for payment to her upon his death out of his estate in lieu of dower and other marital rights, the amount so stipulated in the antenuptial agreement is not deductible from the gross estate of the decedent, under section 403 of the Revenue Act of 1921, as a claim against his estate.

(2) DECISION AFFIRMED.

The decision of the United States Board of Tax Appeals (9 B. T. A., 636) affirmed.

UNITED STATES CIRCUIT COURT OF APPEALS, EIGHTH CIRCUIT. No. 8249.—MAY TERM, A. D. 1929.

Jacob A. Jacobs, George G. Gambrill, and Henry C. Hain, Executors of the Last Will of Morris Eisenstadt, Deceased, appellants, v. Commissioner of Internal Revenue, appellee.

On petition to review decision of United States Board of Tax Appeals.

[July 23, 1929.]

Morris Eisenstadt, now deceased, in his lifetime entered into an antenuptial contract with his widow, Marie Eisenstadt, then Marie Johnston, by which it was agreed that if she survived him she should be paid out of his estate the

sum of \$75,000 and that said sum should be in lieu of all her rights of dower and other marital rights. He died on July 27, 1923. His will contained a provision that his widow at her election, in lieu of the \$75,000 stipulated in the antenuptial contract to be paid her from his estate upon his death, should be paid during her natural life the net income from \$250,000 of his estate to be placed in trust for such purpose. The widow on September 17, 1924, notified the executors of the estate that she elected to accept the provision of the will in her favor in lieu of the \$75,000 stipulated in the antenuptial contract. On September 24, 1924, the executors made return of the Federal estate tax due from the estate and in their return deducted this \$75,000 from the value of the gross estate in determining the value of the net estate upon which to calculate the tax. The Commissioner of Internal Revenue disallowed the deduction, and was sustained by the Board of Tax Appeals (9 B. T. A., 636). The matter is now before this court upon the petition of the executors for a review of the decision of the Board of Tax Appeals.

The statute involved is section 403 of the Revenue Act of 1921 (ch. 136, 42 Stat., 279), which so far as material reads:

"That for the purpose of the tax the value of the net estate shall be determined—(a) In the case of a resident, by deducting from the value of the gross estate—(1) Such amounts for funeral expenses, administration expenses, claims against the estate, unpaid mortgages upon, or any indebtedness in respect to, property," etc.

The contentions of the respective parties are—on behalf of the estate:

(1) That the antenuptial agreement was a valid and subsisting contract and gave the widow the right to demand and receive the \$75,000 stipulated therein from the estate of her husband. The following cases are cited in the brief in support of this contention: *Vogel v. Vogel's Admr.* (22 Mo., 161), *Matter of Baker* (83 App. Div., 530 (affirmed 178 N. Y., 575)), *In matter of Vanderbilt* (184 App. Div., 661 (affirmed 226 N. Y., 638)), *Hill v. Treasurer and Receiver General* (227 Mass., 331).

This contention of the executors of the estate is conceded by the Government. Its brief contains this statement:

"It seems to be the settled law of the State of Missouri, as it is generally, that an antenuptial contract, for the payment of money or property in consideration for the release by a wife of her dower and other rights growing out of her marital status, is a valid contract which may be enforced against the estate of the deceased husband. (*Vogel v. Vogel's Admr.*, 22 Mo., 161.)

"However, that proposition, so much relied upon by petitioners, is not determinative of this case."

In the brief of the executors the above proposition is modified and as modified is made the minor premise of counsel's argument, the statute as construed by counsel being the major premise. The argument as stated in the brief is:

"Since the claim of Mrs. Eisenstadt under the antenuptial contract was a subsisting and enforceable claim against the estate of her husband *at the time of his death*, its amount was deductible from his gross estate in the determination of the amount of his net estate.

"This follows from the express provisions of the Federal statutes. Section 403 of the Revenue Act of 1921, which was in force at the time of the death of Mr. Eisenstadt, directs that 'claims against the estate' shall be deducted from the gross estate in computing the amount of the net estate. This direction is absolute, and it applies to all claims against the estate without any limitation whatsoever. The courts can not supply a limitation by construction.

"By 'claims against the estate' must have been intended *claims existing at the time of death*; for all of the provisions of the statute which enter into the determination of the amount of value of the taxable estate relate to that time. Indeed, the net value of the estate at any given time is the value at that time of all the property belonging to the estate, less the amount of the charges against the estate at that time. To fix the value of the property as of one time, and the amount of the charges as of another time, would not be the determination of the net value of the estate at either time; and section 402 of the Revenue Act of 1921 provides expressly 'that the value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated.'" [Italics ours.]

In support of this argument the following cases are cited: *Young Men's Christian Association v. Davis* (264 U. S., 47), *Edwards v. Slocum* (264 U. S., 61

[T. D. 3584, C. B. III-1, 479]), *Nichols v. Coolidge* (274 U. S., 531 [T. D. 4072, C. B. VI-2, 351]), and commented upon.

The Government states its contention in its brief in this language:

"The will of Morris Eisenstadt created an interest in lieu of the amount agreed to be paid by the antenuptial contract. This provision preserved the \$75,000 as part of the estate, and gave the widow a life interest in a trust fund. Under those circumstances, a duty to elect arose, which, until exercised, left the status of the estate unsettled, and when exercised in favor of the bequest, canceled, as of the death of Morris Eisenstadt, the claim arising out of the antenuptial contract.

"The Congress was taxing net estates remaining after all valid claims were satisfied, and did not intend to authorize deductions, for estate tax purposes, of amounts not deductible in law or in fact."

This contention of the Government is elaborated in the argument and the following cases are cited in support of the proposition that when the widow elected to accept the provision made for her in the will her election "canceled, as of the death of Morris Eisenstadt, the claim arising out of the antenuptial contract," viz: *Woods v. Conqueror Trust Co. et al.* (178 S. W., 201 (Mo.)), *Sparks v. Dorrell* (131 S. W., 761 (Mo.)), *Moseley v. Bogy* (198 S. W., 847 (Mo.)).

An analysis of the respective arguments reveals that the contention in behalf of the estate is built upon the antenuptial contract and the moment of the death of the deceased as the chief corner stones of the structure. The argument in behalf of the Government, on the other hand, makes the election of the widow to take under the provision of the will the decisive fact in the case.

The fact that the matter for decision lies within narrow limits does not render its solution less difficult; and for the same reason that it is more difficult to cross a stream over a foot pole than over a bridge. The foot pole is so narrow that balancing is difficult and the slightest misstep hazardous; the bridge so broad that one is not conscious of balancing and a misstep usually of no moment. The principle or principles controlling a narrow case are usually uncertain and elusive. In a case of broader scope the threads leading toward a correct solution are usually numerous and to be encountered at many points.

The contentions of the parties are irreconcilable and neither satisfying. Their consideration has led to the conclusion that the case turns upon what Congress intended to include by the phrase "claims against the estate" found in the statute rather than upon the antenuptial contract and the moment of the death of the deceased, put forward by the estate, or upon the election of the widow, put forward by the Government.

The Supreme Court of the United States (*Nichols v. Coolidge*, 274 U. S., 541) has said:

"Taxes are very real things and statutes imposing them are estimated by practical results."

In *New York Trust Co. v. Eisner*, Justice Holmes remarked that: "A page of history is worth a volume of logic."

Tax laws deal with actualities and the rules prescribed by Congress are intended to produce practical results when applied by untechnical men. We think actuality was the thought foremost in the mind of Congress when it put the phrase "claims against the estate" in this and other Revenue Acts. The claims which Congress intended to be deducted were actual claims, not theoretical ones. Indeed, a claim without a claimant is a sort of legal figment which has the tendency to produce intellectual dizziness comparable to that felt when gazing down into running water from an insecure footing. The widow never claimed anything from the estate under the antenuptial contract and the gross estate was not decreased one single cent by reason of the \$75,000 stipulated in the antenuptial contract. All the logic in the world can not change these facts. If an executor or administrator leaves his statutory fees in the estate, can it be said that they should nevertheless be deducted in determining this tax? If a father or mother holding an obligation of a deceased child refuses to demand payment from his or her estate, would the obligation nevertheless be a claim against the estate to be deducted in determining this tax? In our opinion a claim without a claimant was not in the mind or purpose of Congress when the words "claims against the estate" were written into the revenue statutes. The administration of an estate necessarily extends over a period of months, sometimes of years, and always under State laws requiring the orderly presentation and allowance of claims against it. It was in our opinion claims presented

and allowed or otherwise determined as valid against the estate and actually paid or to be paid that Congress had in mind when it provided for the deduction from the gross estate of "claims against the estate" in determining the value of the net estate for taxing purposes.

In 11 C. J., page 817, it is said:

"The word (claim) is a broad and comprehensive term, and in its legal use has been understood in a somewhat enlarged sense, being defined as a demand of some matter as of right by one person on another to do or to forbear to do some act or thing as a matter of duty, embracing every species of legal demand, and including 'demand' and 'debt.'"

On page 819 it is said:

"In statutes providing for the administration of the estates of deceased persons, requiring a presentation of claims against the estate, it is generally construed by the authorities as referring to demands of a pecuniary nature, which could have been enforced against the deceased in his lifetime, and when so used the word has been judicially defined as the asserted liability of decedent and his estate to pay a sum of money; a legal demand for money to be paid out of an estate."

In *Knutson v. Krook* (127 N. W., 13) the Supreme Court of Minnesota uses this language:

"The word 'claim,' as generally employed, has a broad and comprehensive meaning, embracing every species of legal demand. (7 Cyc., 180.) But, as employed in a particular statute, its meaning is often restricted and limited, and in statutes providing for the administration of the estates of deceased persons, requiring a presentation of claims against the estate, are by the authorities generally construed as referring to demands of a pecuniary nature, and which could have been enforced against the deceased in his lifetime."

See also Words and Phrases, Volume 1, second series, pages 727-728.

Of course there are deductions which are determined, as claimed by the executors, by the facts and conditions existing at the date of the death. The Supreme Court of the United States, in *Ithica Trust Co., executor, etc., v. The United States* (279 U. S., 151), has held that the value of gifts to charity which were subject to the life estate of the widow should be determined by the use of mortuary tables notwithstanding the death of the widow before the tax was in fact ascertained. The court said:

"The estate so far as may be is settled as of the date of the testator's death. See *Hooper v. Bradford* (178 Mass., 95, 97). The tax is on the act of the testator, not on the receipt of property by the legatees. (*Young Men's Christian Association v. Davis*, 264 U. S., 47, 50; *Knowlton v. Moore*, 178 U. S., 41, 49, and *passim*; *New York Trust Co. v. Eisner*, 256 U. S., 345, 348, 349; *Edwards v. Slocum*, 264 U. S., 61.) Therefore the value of the thing to be taxed must be estimated as of the time when the act is done."

Some of the cases cited in the opinion, it will be observed, are relied upon in this case by the executors. But in the *Ithica Trust Co.* case the court was dealing with the present value of a gift to charity postponed by the life estate of the widow. Such gifts are authorized to be made as deductions by paragraph (3) of section 403. We are concerned in this case with paragraph (1) of that section. Of course we accept without reservation the definition of the tax and the rules governing its assessment stated by the Supreme Court in these cases. But that court has not said that the deductions authorized by paragraph (1) of section 403 must be determined solely by the facts and conditions existing on the day of the death, and we are confident that court will never say so in view of the provisions of paragraph (1). Paragraph (1) not only allows as deductions claims against the estate—which it is true are liabilities of the estate at least at the moment of the death—but also allows as deductions funeral and administration expenses, which have no existence until after the death. All these, funeral expenses, administration expenses, and claims against the estate, under this paragraph were intended by Congress to be determined in the course of an orderly administration of the estate in and by the State courts. This intention is taken for granted in the provisions of section 405 of the statute, which reads:

"That if no administration is granted upon the estate of a decedent, or if no return is filed as provided in section 404, or if a return contains a false or incorrect statement of a material fact, the collector or deputy collector shall make a return and the Commissioner shall assess the tax thereon."

Our interpretation of the statute is in harmony with the practice of the Treasury Department, which is charged with the administration of the Act. Article 32 of Regulations 63, 1922 edition, provides that:

"Deduction of claims, expenses, etc.—In order to be deductible under the foregoing provision of the statute, the item must fall within one of the several classes of deductions specifically enumerated therein, and must also, except in the case of deductible losses during the administration of the estate, be one the payment of which out of the estate is authorized by the laws of the jurisdiction under which the estate is being administered. * * * An item may be entered on the return for deduction though the exact amount thereof is not then known, provided it is ascertainable with reasonable certainty, and will be paid. No deduction may be taken upon the basis of a vague or uncertain estimate. When an uncertain or contingent liability was undetermined at the time of audit of the return by the Commissioner, and, as a consequence, deduction was not allowed therefor in such audit, the remedy is by a claim for abatement or refund when the liability and the amount thereof becomes fixed and determined."

Articles 33 to 38 following deal with the subject in the same practical manner.

In our opinion, the Department in its regulations has correctly construed the statute, and in this case we are convinced the Commissioner and the Board of Tax Appeals correctly applied it. The petition for review is dismissed.

TITLE IV.—ESTATE TAX. (1918 AND 1921)

GENERAL PROVISIONS.

REGULATIONS 63, ARTICLE 105: Scope of repeal.

VIII-49-4454

Ct. D. 135

ESTATE TAX—REVENUE ACT OF 1921—DECISION OF COURT.

1. TAX.—REPEAL—"SAVING CLAUSE"—MEANING OF "ACCRUED."

The tax upon the estate of a decedent who died within one year prior to November 23, 1921, the date of the enactment of the Revenue Act of 1921, accrued under the Revenue Act of 1918 within the meaning of "saving clause" contained in section 1400(b) of the Revenue Act of 1921, which provided that parts of the Revenue Act of 1918 which were repealed by the Revenue Act of 1921 remained in force for the assessment and collection of all the taxes which had accrued under the Revenue Act of 1918 at the time such parts ceased to be in effect.

2. SUITS.—CLAIM FOR REFUND.

The precise ground upon which the refund of taxes is demanded must be stated in the application to the Commissioner and a suit in court to recover the tax can not be based upon an entirely different and distinct ground from that presented to the Commissioner.

COURT OF CLAIMS OF THE UNITED STATES.

Howard M. Hanna, as Executor of the Last Will and Testament of H. Melville Hanna, Deceased, v. The United States.

[November 4, 1929.]

SUPPLEMENTAL OPINION ON MOTION FOR A NEW TRIAL.

GREEN, Judge, delivered the opinion of the court.

The motion for a new trial being based upon a ground neither argued nor stated at the time of the submission of the original case, and being supported by a decision of a United States district court, would seem to be entitled to an expression of the opinion of this court thereon.

Although the point was not raised on the original submission of the case, it is now insisted by plaintiff that under the Revenue Act of 1921 (42 Stat., 227), estates of decedents dying within one year prior to the enactment of the Revenue Act of November 23, 1921, are not subject to the Federal estate tax.

The Act of 1921 repealed that portion of the 1918 Revenue Act which imposed an estate tax and enacted in lieu thereof a different estate tax applicable when the new statute went into force. The Act of 1921, however, contained what is commonly referred to as a "saving clause," similar to one which was contained in the 1918 Act, the purpose of which was plainly to continue in force the provisions of the 1918 Act until the 1921 Act could apply. This provision was contained in section 1400(b) of the later Act, which provided:

"(b) The parts of the Revenue Act of 1918 which are repealed by this Act shall (unless otherwise specifically provided in this Act) remain in force for the assessment and collection of all taxes which have accrued under the Revenue Act of 1918 at the time such parts cease to be in effect, and for the imposition and collection of all penalties or forfeitures which have accrued or may accrue in relation to any such taxes. In the case of any tax imposed by any part of the Revenue Act of 1918 repealed by this Act, if there is a tax imposed by this Act in lieu thereof, the provision imposing such tax shall remain in force until the corresponding tax under this Act takes effect under the provisions of this Act."

The contention of plaintiff is that there is no provision for the Act of 1918 to "remain in force for the assessment and collection of all taxes" unless those taxes have "accrued," and that the decedent in this case having died within one year prior to the enactment of the 1921 Act, no taxes had "accrued" against his estate. If this theory be correct, then estates of those who died more than one year prior to the enactment of the 1921 Act would be taxed, and estates of those who died after the enactment of the 1921 Act would also be taxed, but in the case of those who died in the intervening period no tax would be imposed. No one would claim that Congress ever intended to enact a law having such absurd and inequitable results, but, however justifiable the presumption may be that it did not so intend, it is not necessary for us to indulge in it in order to ascertain the purpose of this "saving clause." A casual survey of the provision set forth above clearly shows that the intent and purpose of Congress was that the estates of all of those who died prior to the enactment of the 1921 Act should be taxed under the 1918 statute, and the estates of those who died after the enactment of the 1921 Act taxed under the provisions of the later Act. In fact, this intent is so plain that "he who runs may read" and understand. It needs no citation of authorities to show that when the intent of the legislative body is manifest it becomes our duty to so construe the Act as to carry out that intention unless such a construction can not reasonably be placed upon the language of the Act. A careful examination of the whole of the Revenue Act of 1921 leads us to conclude that defendant's case is even stronger than his principle requires, and the only reasonable construction which can be given the provision in question is one which would sustain the tax in controversy.

It will be observed that the argument of plaintiff is based upon a definition of the word "accrue" or "accrued," and it is claimed that the construction for which plaintiff contends is supported by the decisions of the Supreme Court in *United States v. Woodward* (256 U. S., 632 [T. D. 3195, C. B. 4, 153]) and *United States v. Mitchell* (271 U. S., 9, 10 [T. D. 3865, C. B. V-1, 233]). In connection with the application of these decisions some confusion of thought seems to have arisen. The question for determination in the case at bar is not how the word "accrued" may have been used in some part of the 1918 statute, but how it is used and what meaning should be given it in the provisions of the 1921 statute which we are called upon to construe. When this is kept in mind, we think it will clearly appear that these cases do not support the position of plaintiff.

The word "accrue" as used in the law has two meanings: It is often applied to a present enforceable demand, and as often, if not more often, means simply to arise or to come into existence. In *Emerson v. The Shawano City* (10 Wis., 433), it is said:

"The verb 'to accrue' is often and properly used to convey the same idea as the verb 'to arise.' * * * A cause of action may be said to arise when the contract out of which it grows is entered into or made."

In *Page v. Skinner* (298 Fed., 731, 735 [T. D. 3600, C. B. III-1, 485]) the circuit court of appeals had occasion to pass on the meaning of a provision in the Act of February 24, 1919, commonly referred to as the Revenue Act of 1918. The 1918 Act, by section 1400(a) thereof, repealed the estate tax of 1916, but in (b) of the same section provided:

"(b) Such parts of Acts shall remain in force for the assessment and collection of all taxes which have *accrued* thereunder, and for the imposition and collection of all penalties or forfeitures which have accrued and may accrue in relation to any such taxes, * * *." [Italics ours.]

Although the wording is slightly changed, there can be no question but that the word "accrued" is used in the same sense as in the similar provision of the 1921 Act, which has heretofore been set out, and the circuit court of appeals said further in the last-named case with reference to the 1918 Act:

"Neither are we in doubt as to the meaning of the word 'accrued,' found in subparagraph (b); as contended by counsel amici curiae, who appear for another estate in like conditions, that it is equivalent to *arising under* and refers to all taxes, including estate taxes, * * * and is not a restriction to those that were due and payable prior to February 25."

With this construction of the 1918 Act we entirely agree, and applying the same rule to the provision of the 1921 Act under consideration in the case at bar, it follows that the position now taken by the plaintiff in support of the motion for a new trial is not well founded. In view, however, of the fact that the case of the *Wilmington Trust Co. v. United States* (28 Fed. (2d), 205), cited by counsel, holds to the contrary, it is considered that our reasons for following the case of *Page v. Skinner*, supra, ought to be fully set forth, and they accordingly follow.

We do not need to cite authorities to show what the words "accrue," "accrued," or "accrual" mean in a bookkeeping or economic sense. It is well settled both by works on accounting and judicial decisions that books kept on the "accrual" basis include items as to which a liability has arisen or exists either for or against the concern for which the books are kept, although these items matured in the future and were not yet due and payable.

It is said that the provisions of section 214(a)3 of the Act of 1921 indicated the intention of Congress as to how this word should be construed, and that that construction is the one for which plaintiff contends.

The provision upon which plaintiff relies in support of this contention, under the heading of "Deductions allowed individuals" (parts not material to this case omitted), is as follows:

"(3) Taxes paid or accrued within the taxable year * * *. *For the purpose of this paragraph* estate, inheritance, legacy, and succession taxes accrue on the due date thereof except as otherwise provided by the law of the jurisdiction imposing such taxes." [Our italics.]

It will be observed that this provision applies only to "deductions allowed individuals" and that it is only "for the purpose of this paragraph." The purpose of the paragraph was the allowance of deductions of taxes which had accrued, and for this purpose, and this purpose only, it is provided that estate taxes shall accrue on the due date thereof. The clear implication is that elsewhere the word "accrue" should be taken, when applied to taxes, as meaning the time when they were imposed or established as a liability by the law, at least unless the context otherwise indicates. In fact, it would seem that the maxim *expressio unius est exclusio alterius* here applies, the statute having specifically stated that for the purposes of making deductions estate taxes should accrue on the due date thereof, excludes this meaning for other purposes—that is, for the purposes of the remainder of the Act. (Broom's Legal Maxims, 664.) The maxim is a rule of construction. (*United States v. Barnes*, 222 U. S., 513.)

Of course, the context might indicate a different meaning, but, as we have already seen, the context in section 1400(b) of the Act of 1921 plainly indicated the intention of Congress that the application of the estate tax should be continuous, and that the 1921 Act did not create new exemptions from the tax of 1918.

In this connection it should be noted that exactly the same language is used under the heading of "Deductions allowed corporations," in section 234(a)3 of the 1921 Act. Here again Congress made it clear that it fixed the due date as the time when estate taxes should accrue merely for the purposes of that para-

graph; that is, for the purpose of fixing the time when the deductions on account of such taxes should be made.

In the cases of *United States v. Woodward*, supra, and *United States v. Mitchell*, supra, the Supreme Court was construing certain provisions of the Revenue Acts of 1916 and 1918. The Act of 1921 did not enter into either of these cases. In the instant case we are called upon to construe the Act of 1921, with additional and different provisions which are controlling, and the decision is governed entirely thereby. The two decisions of the Supreme Court cited above have no application, having been rendered not only under a different statute but in a different connection.

In the case of *United States v. Anderson* (269 U. S., 422, 441) the case of *United States v. Woodward*, supra, was reviewed, and it is shown that it was decided on the provisions of the Act of 1918. One question in the Anderson case was as to when the munitions tax which was imposed in 1916 accrued, and although the tax was not payable until 1917, it was held that "in the economic and bookkeeping sense with which the statute and Treasury decision were concerned, the taxes had accrued" in 1916, thus recognizing that the word "accrue" was generally used in the statute with reference to taxes in the economic and bookkeeping sense; that is, as referring to the time when the liability is established instead of the time when it becomes due and payable, if that is a different date. So in this case the estate taxes in question had already "accrued" when the 1921 statute was passed. It was further held in the Anderson case, supra, that when the books of the corporation were kept on an accrual basis, the deduction for the taxes of 1916 should be made in that year; and that there was nothing in the Woodward case to controvert this holding. In fact, an examination of the opinions in the Anderson case and the Mitchell case shows that in each the application of the Woodward case was strictly and expressly restricted to the particular question before the court in that case, which was a very different one from the one now being considered.

As the tax became due and payable one year after the decedent's death, it is obvious that it was intended that it should be assessed before the expiration of the year, and it is quite plain from other provisions of the 1918 Act that the tax might be assessed under regulations made by the Commissioner even before six months had elapsed since the death of the owner of the estate, provided the regulations so required. The Act further provided that the tax should be a lien for 10 years upon the gross estate of the decedent. No date is fixed in the statute from which this 10 years should run, but it seems to have been universally considered that it ran from the date of death of the testator, and the regulations so provided. (Regs. 68, art. 88.) Obviously the lien could not attach at the time of death unless a liability for the tax then came into existence.

It seems unnecessary to carry the argument further, but section 1400(b), in addition to the particular part thereof which has been discussed above, contained the following:

"In the case of any tax imposed by any part of the Revenue Act of 1918 repealed by this Act, if there is a tax imposed by this Act in lieu thereof, the provision imposing such tax shall remain in force until the corresponding tax under this Act takes effect under the provisions of this Act."

Title IV, Estate tax, of the Act of 1918 was repealed by the Act of 1921; and Title IV, Estate tax, of the Act of 1921 was enacted in lieu thereof. The provisions imposing the tax therefore remained in full force and effect up until the time of the enactment of the 1921 Act, and the tax having by reason thereof accrued, then under the provisions with reference to taxes which had accrued the provisions of the 1918 Act remained in force for the assessment and collection thereof. The provision last quoted becomes entirely meaningless if the construction contended for by the plaintiff be adopted. It would have no application except to cases where the tax was due and payable when the 1921 Act was adopted, and for that purpose it would be entirely unnecessary and useless.

For the reasons above stated, we decline to accept the views expressed in the case of the *Wilmington Trust Co. v. United States*, supra, and hold that the tax in question had accrued when the 1921 Act went into effect.

Another feature of the case should be noted. The claim of the plaintiff for refund upon which this suit is based stated that the assessment in the sum of \$2,049,326.97 was made in respect to certain property of which the decedent had made a transfer on May 9, 1912, to trustees under a deed of trust, the aggregate value of which the Commissioner found to be \$10,514,250. The claim for refund further recited:

"Upon the execution and delivery of said trust deed, the legal title to all of the securities constituting the trust fund passed to the trustees named therein and the interest in remainder in such trust fund vested in the issue of the decedent immediately, subject only to be divested in certain contingencies provided for in said deed; and inasmuch as the said vested interests of such remainderman were never so divested, pursuant to the provisions of said deed, the undersigned now claims that said transfer so made by said decedent on May 9, 1912, is not subject to tax under the United States estate tax law, pursuant to which this return is made."

It will be observed that while it was claimed that the trust fund was "not subject to tax under the United States estate tax law," the basis of this claim was as stated in the foregoing paragraph, which does not refer in any way to the claim now made, nor was there elsewhere in the claim for refund any reference to it. That the claim originally made is not the same as the one now argued is shown by the argument contained in the application for refund, which is based on the cases of *Shwab v. Doyle* (258 U. S., 529) and *Nichols v. Coolidge* (4 Fed. (2d), 112 [T. D. 4072, C. B. VI-2, 351]). These cases had some bearing on the original claim made in the application for refund, but it will not be contended that they have the slightest application to the claim now made by the motion for a new trial.

We think the claim now made by plaintiff on motion for a new trial which has been set out and discussed in this opinion is a different and distinct ground from that presented to the Commissioner. If we are correct in this, the plaintiff is in any event barred from recovery herein under the rule laid down in *Kaltenbach v. United States* (66 C. Cls., 581 [see Ct. D. 82, on page 307]); *Warner-Patterson Co. v. United States* (68 C. Cls. [see Ct. D. 91, on page 362]); and *Red Wing Matting Co. v. Willcuts* (15 Fed. (2d), 626 [T. D. 3980, C. B. VI-1, 225]).

It follows that the motion for a new trial must be overruled, and it is so ordered.

TRANSFER BY DECEDENT IN HIS LIFETIME.

REGULATIONS 70, ARTICLE 18: Reservation of income or an annuity. ARTICLE 19: Power to change enjoyment.

VIII-29-4279
Ct. D. 81

ESTATE TAX—REVENUE ACT OF 1918—DECISION OF COURT.

GROSS ESTATE—TRANSFER TO TAKE EFFECT AT DEATH.

Where a deed of trust provides that the income shall be paid to the grantor during his lifetime or until a certain date, whichever first occurs, and he reserves a power of revocation, the transfer is one "intended to take effect in possession or enjoyment at or after his death" within the meaning of section 402(c) of the Revenue Act of 1918.

UNITED STATES CIRCUIT COURT OF APPEALS, SIXTH CIRCUIT.

United States, appellant, v. Edgar Stark, Executor of Jacob G. Schmidlapp et al., appellees.

Appeal from the District Court for the Southern District of Ohio, Western Division.

[May 7, 1929.]

OPINION.

DENISON, Circuit Judge: The Schmidlapp estate recovered judgment against the United States for refund of an inheritance tax thought to have been erroneously assessed, pursuant to section 402(c) of the Revenue Act of 1918—the assessment having been on the theory that a certain trust conveyance by Mr. Schmidlapp was one that would take effect in possession or enjoyment upon his death. The decision below was in reliance upon *Nichols v. Coolidge* (274 U. S., 531 [T. D. 4072, C. B. VI-2, 351]), and held the Act could not constitutionally have the retroactive effect necessary to support the assessment. The Supreme Court having now held, in *Chase National Bank v. U. S.* (278 U. S., 327 [Ct. D.

40, C. B. VIII-1, 308), that where the grantor in trust reserves the power of revocation, as Schmidlapp did, retroactive effect could rightly be given, the only question now remaining is whether the Schmidlapp trust was one which had the specified testamentary character. The income of the trust and the right to revoke the same were reserved to the grantor during his life. The trust was to be ended and distribution was to be made at the end of an 8-year term or upon Schmidlapp's prior death. When he made the deed he was in good health; the conveyance was not made in expectation of his death; his reasonable expectation of life was much more than eight years; and it is said to be true, and may be assumed, that everyone concerned actually expected that the possession and enjoyment would pass to the beneficiaries at the end of the specified term of years. We therefore have a case of a conveyance which was to take effect in possession and enjoyment on a specified future date and thus as to which no inheritance tax could be imposed by retroactive statute, and which also was to take effect upon the death of the donor, and thus as to which such a tax therefore could be imposed. Which character dominates?

We are not aware of any controlling decision. Counsel for the trustee rely upon the rule stated in *Fearne on Remainders* (4th Am. Ed., vol. 1, sec. 114), that where a future estate is limited upon a term for years but "the term is rendered determinable by means of * * * the dropping of a life or lives, and it is for so few years that there is a common possibility of the life or lives enduring beyond it," the remainder is one limited upon the term of years and not upon the life estate; "for in such cases the freehold interest is in fact limited on the contingent expiration of the term, because the dropping of the life or lives is an event which may not happen before the term has already expired by effluxion of time; but where there is no common possibility of the life enduring beyond the term of years, then the freehold estate is considered as dependent on the life estate and not upon an estate for years." The argument further is that Congress must be deemed to have used the statutory phrase in view of this anciently settled definition.

The argument is forceful, but upon the whole we think it should not prevail. Of course, the question must be decided in the aspect it had the day the conveyance was made; to give force to the fact that Schmidlapp did die during the term so that it turned out that the future estate took full effect upon his death would be "inaccurate thinking." (Mr. Justice Holmes, in *Ithaca Trust Co. v. U. S.*, Supreme Court, April 8, 1929.) Disregarding this consideration, the persuasive element to our minds is that the general purpose and intent of the Act in this respect were to reach dispositions which were really testamentary; and that the reserved power of revocation gave to this conveyance that character—as the Supreme Court has held in the Chase case. Whether the future estate ever would take effect by expiration of the term depended, until the moment of Schmidlapp's death, upon his continued voluntary non-exercise of his power of revocation. We think this situation gives the dominant character, and hence that the tax was properly assessed.

The case was tried without a jury and there was a full finding of facts. They did not support the judgment rendered for the plaintiff, which therefore must be reversed. In the typical case of a reversal at law, a new trial is awarded; but when the facts as found affirmatively establish a complete defense, the reviewing court will direct the entry of that judgment which should have been rendered. (*Fort Scott v. Hickman*, 112 U. S., 150, 165.)

Accordingly, the judgment is reversed with direction to enter a judgment for defendant.

GROSS INCOME—INSURANCE.

REGULATIONS 70, Article 27: Insurance receivable by other beneficiaries.

VIII-26-4255
Ct. D. 74

ESTATE TAX—REVENUE ACT OF 1918—DECISION OF COURT.

1. GROSS ESTATE—INSURANCE PAID TO EXECUTOR—CONSTITUTIONALITY.

Subdivision (f) of section 402 of the Revenue Act of 1918, in so far as it requires the inclusion in the gross estate of the amount received by the executor as insurance under policies taken out by the decedent upon his own life, is constitutional.

2. SAME—INSURANCE PAID TO ASSIGNEE.

Where the decedent makes an absolute and unconditional assignment of a policy of insurance upon his own life, no part of the proceeds received by the assignee need be included in determining the value of the gross estate.

COURT OF CLAIMS OF THE UNITED STATES.

Martha A. Guettel and Arthur Guettel, individually, and Martha A. Guettel and Henry A. Auerbach, trustees for Edward Guettel under the will of Henry A. Guettel, deceased, v. The United States.

[May 6, 1929.]

OPINION.

Moss, Judge, delivered the opinion of the court.

On January 14, 1920, the New York Life Insurance Co. issued three policies of insurance on the life of Henry A. Guettel, who died testate in August, 1921, each of said policies payable to the estate of decedent. On March 25, 1920, said decedent assigned one of said policies to his wife, and there was paid to her upon the death of the insured the proceeds of same, \$100,815. In determining the amount of the estate tax due from decedent's estate the Commissioner included in the gross estate the proceeds of the three policies, less the deduction provided for in section 402, subsection (f), of the Revenue Act of 1918 (40 Stat., 1096), the pertinent provisions of which read as follows:

"That the value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated * * *.

"(f) To the extent of the amount receivable by the executor as insurance under policies taken out by the decedent upon his own life; and to the extent of the excess over \$40,000 of the amount receivable by all other beneficiaries as insurance under policies taken out by the decedent upon his own life."

Plaintiff's chief contention is that the statute fixing the measure of the tax, in so far as it includes the proceeds of the insurance policies, is unconstitutional. That question was involved in the case of *The Chase National Bank of the City of New York v. The United States*, decided January 2, 1929 (278 U. S., 327 [Ct. D. 40, C. B. VIII-1, 308]), after the preparation of the briefs in the instant case. That case went to the Supreme Court of the United States on certified questions of law concerning which instructions were requested for the proper disposition of the case. The facts as certified, and as briefly set out in the opinion, are as follows: "On September 13, 1922, after the effective date of the Revenue Act of 1921, Herbert W. Brown procured three insurance policies on his life aggregating \$200,000, each naming his wife as beneficiary. Each policy reserved to the insured the right to change the beneficiary. All premiums on the policies were paid by the insured. On April 10, 1924, he died testate, leaving the plaintiff below his executor and an estate subject to the estate tax imposed by the Revenue Act of 1921 (ch. 136, 42 Stat., 227). The tax as assessed by the Commissioner included \$9,146.76 imposed by reason of the inclusion in the estate of the proceeds of the three insurance policies, less \$40,000 exemption authorized by the statute. The executor paid the tax and upon denial of a claim for refund brought the present suit in the Court of Claims to recover the tax as illegally assessed."

The questions certified were stated as follows:

"Question I: Whether the tax imposed by the final clause of section 402(f), Revenue Act of 1921 (42 Stat., 278), on life insurance policies payable in terms to beneficiaries 'other than the decedent or his estate' is a direct tax on property and void because not apportioned.

"Question II: Whether the \$9,146.76 tax imposed bears such an unreasonable relation to the subject matter of the tax as to render it void."

Both questions were answered in the negative.

Defendant contends that the decision in the Chase National Bank case (278 U. S., 327) is controlling as to each of the three policies involved herein. We are in agreement with the defendant's contention as to the two policies payable to the estate of Henry A. Guettel, and hold that the value of said two policies was properly included in the decedent's gross estate under the authority of

that case. We must, however, disagree with defendant's contention as to the policy payable to decedent's estate and thereafter assigned by plaintiff to his wife. It was an absolute and unconditional assignment of the policy "for value received," and the insurance company paid to the assignee at the death of the insured the full proceeds of the policy, \$100,815. By this assignment the insured was divested of all right and title to the policy, and all beneficial interest therein passed to the assignee. After the assignment the insured was without authority to change the beneficiary or to exercise any control whatever over said policy during the existence of the assignment. See 37 Corpus Juris (sec. 146), 2, page 435, and cases cited thereunder.

The language "*all other beneficiaries*," used in the statute, can not be fairly construed as applying to the *assignee* of a policy payable to a designated beneficiary. Such a construction would be an unwarranted extension of the meaning of the statute here involved. Taxing statutes may not be extended by implication beyond the clear import of the language used. (*Gould v. Gould*, 245 U. S., 151; *United States v. Merriam*, 263 U. S., 179 [T. D. 3535, C. B. 11-2, 87].)

We have reached the conclusion that the policy assigned to decedent's wife was improperly included in decedent's gross estate. Plaintiff is entitled to judgment as provided in the conclusion of law herein.

TITLE II.—ESTATE TAX. (1916)

GROSS ESTATE—PROPERTY HELD JOINTLY.

REGULATIONS 70, Article 22: Property held jointly or as tenants by the entirety.

VIII-31-4295
Ct. D. 86

ESTATE TAX—REVENUE ACT OF 1916—DECISION OF COURT.

GROSS ESTATE—ESTATE BY THE ENTIRETY—CONSTITUTIONALITY.

Section 202(c) of the Revenue Act of 1916 requires that the value of property transferred by the decedent to himself and another as tenants by the entirety be included in determining the value of the decedent's gross estate and as so construed the section is constitutional.

UNITED STATES CIRCUIT COURT OF APPEALS, FOURTH CIRCUIT.

United States of America, appellant, v. James E. Tyler, jr., and William G. Tyler, Administrators of the estate of James E. Tyler, Deceased, appellees.

Appeal from the District Court of the United States for the District of Maryland, at Baltimore.

OPINION.

PARKER, Circuit Judge: This is an appeal from a verdict and judgment rendered in favor of the administrators of James E. Tyler, deceased, who paid under protest a portion of the Federal estate tax assessed against the estate which came into their hands and instituted suit to recover it back as allowed by statute. The portion of the tax disputed is that assessed against the estate because of including in the value thereof property which was held by decedent and his wife as tenants by the entireties, and which upon the death of decedent vested in the wife as sole and exclusive owner. The facts in the case are few and undisputed. In November, 1917, decedent transferred 349 shares of stock in the Kimball-Tyler Co. to himself and wife, creating therein under the laws of Maryland an estate by the entireties in their favor. On his death in 1918, his wife became vested under the Maryland law with the sole ownership of the shares of stock. The value of the stock was \$59,193.42 and it was included for taxation as a part of the gross estate of decedent, the total of which was \$207,454.60. The estate tax was increased by reason of its inclusion in the amount of \$3,337.67.

The administrators contended that estates by the entireties were not embraced within the terms of the taxing statute, and also that, if the statute should be construed as embracing them, it would be void as violative of the provisions of

the Constitution which require the apportionment of direct taxes and of the due process clause of the fifth amendment. The learned district judge held that the terms of the statute required the inclusion of estate by entireties in the determination of the gross estate for the purposes of taxation, but that in so far as it did this it violated the provisions of the Constitution upon which the administrators relied.

We think that the learned judge was correct in holding that estates by the entireties were embraced within the terms of the taxing statute. See Revenue Act of 1916 (39 Stat., 756, 778). Section 201 of that Act provided that a tax according to a graduated scale should be imposed upon the transfer of the net estate of every decedent dying after its passage, and that the value of the net estate should be determined as provided in section 203. The latter section provided for the deduction of an exemption of \$50,000 and certain other items from the value of the "gross estate." And section 202 provided that the value of the "gross estate" should be determined by including the value at the time of the death of decedent of all property, real or personal, tangible or intangible, (a) to the extent of his interest therein at the time, (b) to the extent of any interest which he had transferred in contemplation of death, (c) and to the extent of the interest held jointly or as tenant by the entireties with another, the exact wording of clause (c) of section 202 being as follows:

"(c) To the extent of the interest therein held jointly or as tenants in the entirety by the decedent and any other person, or deposited in banks or other institutions in their joint names and payable to either or the survivor, except such part thereof as may be shown to have originally belonged to such other person and never to have belonged to the decedent."

The administrators rely upon the decision of the Board of Tax Appeals in the appeal of Susie M. Root (5 B. T. A., 696 [C. B. VII-2, 51]), and certain expressions in the opinion of the Court of Claims in *Blount v. U. S.* (59 Court of Claims, 328), for the position that, as section 201 of the statute imposes the tax upon transfers of the net estate, and as an estate by entireties is not transferred to the surviving spouse, there was no intention to tax such an estate, and that the language in the statute must be held to be confined to joint tenancies. The answer to this, however, is that in section 201 the tax is imposed upon the transfer of the net estate as *determined under subsequent provisions*, and subsequent provisions require that estates by the entireties be included. The word "entirety" as applied to estates has had for centuries a well understood meaning in the law; and we must assume that Congress employed the language which it did in the light of that meaning. We attach no importance to the fact that the statute uses the language "tenants in the entirety" instead of the customary "tenants by the entirety." The same language appears in the Act of 1921 (42 Stat., 278), and it is worthy of note that it is referred to in the opinion of the Supreme Court in *Reinecke v. Northern Trust Co.* (278 U. S., 339, 49 Sup. Ct., 123, 126 [T. D. 4261, C. B. VIII-1, 305]) as embracing an estate "by the entirety."

While it is true that an estate by entireties is vested in husband and wife at the time of the conveyance to them and that technically there is no transfer to the survivor when one of them dies, nevertheless, as a practical matter, there is a transfer to the survivor of all the rights which the decedent had in the estate, and Congress no doubt had this in mind in requiring estates by entireties to be included with the other property of decedent in determining the taxable value of his estate. Whether the vesting of the entire estate in the survivor be technically a transfer or not, Congress clearly intended that it should be treated as a transfer for the purpose of estate taxation. Joint tenancies and gifts made in contemplation of death were included. Why omit estates under which property could be jointly enjoyed by a man and his wife during their joint lives and, upon the death of one, inure to the sole benefit of the survivor? It is not reasonable to assume that, after being so careful about other matters, Congress would have left open so wide an avenue for evasion of the tax. We feel certain that it has not done so when the language used is given its reasonable interpretation.

As the language of the Act, therefore, requires that the value of estates by the entireties be included in the valuation of estates for the purpose of taxation, the only question that remains to be decided is whether Congress had the power to make such requirement. We think that it had. No question is raised as to the general power of Congress under the Constitution to levy an estate tax, and none can be raised. Such a tax is not a direct tax requiring apportion-

ment, but falls within the classification of "imposts, duties and excises" which Congress is authorized to levy by section 8, clause 1, of Article I of that instrument. (*Scholey v. Rew*, 23 Wall., 331; *Magoun v. Illinois Trust, etc., Bank*, 170 U. S., 283, 287; *Knowlton v. Moore*, 178 U. S., 41; *New York Trust Co. v. Eisner*, 256 U. S., 345; *Chase Nat. Bank v. U. S.*, 278 U. S., 327, 49 Sup. Ct., 126 [Ct. D. 40, C. B. VIII-1, 308].) It is imposed, not on property, but on the privilege of transferring it, and is measured by the value of the interest transferred or which ceases at death. (*Y. M. C. A. v. Davis*, 264 U. S., 47; *Chase Nat. Bank v. U. S.*, supra.)

The statute, in so far as it requires the inclusion of estates by entireties in the valuation of the estates of decedents for purposes of estate taxation, is said to violate the Constitution because it is contended that in the case of an estate by the entireties there is no transfer to the survivor and consequently no basis for the imposition of an estate tax, and from this it is argued that the tax must be considered as a direct tax upon the property itself. We think, however, that this gives too narrow a meaning to "transfer" and ascribes too much importance to what are pure fictions of the law. It is true that husband and wife are said to be seized of the estate by entireties "per tout et non per my," that is to say, each during their joint lives is deemed seized of the whole estate and not of a moiety thereof; and it is true that, upon the death of one, the survivor is said to take no new interest because originally vested with the entirety. But these doctrines are pure fictions based upon the fiction of the unity of husband and wife. (*Marburg v. Cole*, 49 Md., 402, 33 Am. Rep., 266; *Ades v. Caplan*, 132 Md., 66, L. R. A., 1918D, 276.) As a matter of fact, husband and wife are not one person but two persons, and neither has absolute right in or control over the property so long as the other lives. Only upon the death of one does the other acquire absolute ownership with the right to sole and unrestricted use and possession and the right to alien and convey. Whatever form of technical expression be used, therefore, and whatever sophistries indulged, the fact remains that, upon the death of one of the parties, the survivor by operation of law succeeds to the interest which the decedent had in the property. As said by the Court of Appeals of Maryland in *Brewer v. Bowersox* (92 Md., 567, 573, 48 Atl., 1060, 1062), "The right of survivorship, which is one of its chief incidents, can not be destroyed except by the joint act of the two; and upon the death of either the other succeeds to the entire property or fund." [Italics ours.] It is the transfer of interest involved in this "succession" which is the basis of taxation under the statute.

We see no reason why the casting of the entire estate upon the survivor, which takes place by operation of law in case of the death of one of the tenants by entireties, can not be made the basis of taxation as well as the casting of succession upon the heir, which takes place in the case of interstate succession. The surviving spouse receives an enlargement of his interest in the property in the one case just as the heir receives an interest in the property in the other; and in both cases it comes by operation of law. As stated above, it is no answer to say that because of the unity of husband and wife the survivor has, after the death of the other, what he has always had; for, as we have seen, the interest of the deceased spouse, from a practical standpoint, has been vested by law in the survivor. So long as both are living, neither can convey the property without the joinder of the other. Neither is entitled to use and enjoy it to the exclusion of the other. Neither has any right in it beyond his own life unless he survives the other. If the parties should be divorced, the estate would be dissolved, and neither would succeed to the whole property even if he should survive. Upon the death of one of the parties, however, all of his rights in the property are by operation of law transferred to the other so as to create a sole and unconditional estate therein. To deny that there is a transfer of property in such case resulting from death, is to lose the substance of legal rights while grasping at the shadow.

What we have said answers the contention that the statutory provision violates the due process clause of the fifth amendment. This contention is based upon the theory that the statute, in so far as it includes tenancies by the entireties, measures the tax upon decedent's estate by property which belongs to another. But, as we have seen, the property does not belong to the other in the sense of his having unconditional and sole ownership thereof until the death of decedent.

In the recent case of *Chase Nat. Bank v. U. S.*, supra, the Supreme Court considered whether it was proper to include insurance policies within the taxable estate as required by the statute. The contention was made there, as here,

that the interest of the beneficiary had vested prior to the death of insured and that consequently there was no transfer to be taxed, but the court held that the policies should be included. The question in the case was stated as follows:

"It is true, as emphasized by plaintiff, that the interest of the beneficiaries in the insurance policies effected by decedent 'vested' in them before his death and that the proceeds of the policies came to the beneficiaries, not directly from the decedent, but from the insurer. But until the moment of death the decedent retained a legal interest in the policies which gave him the power of disposition of them and their proceeds as completely as if he were himself the beneficiary of them. The precise question presented is whether the termination at death of that power and the consequent passing to the designated beneficiaries of all rights under the policies freed of the possibility of its exercise may be the legitimate subject of a transfer tax, as is true of the termination by death of any of the other legal incidents of property through which its use or economic enjoyment may be controlled."

And, answering the question thus propounded, the court said:

"Termination of the power of control at the time of death inures to the benefit of him who owns the property subject to the power and thus brings about, at death, the completion of that shifting of the economic benefits of property which is the real subject of the tax, just as effectively as would its exercise, which latter may be subjected to a privilege tax."

There can be no question in this case that we have the termination of the power of decedent over the property, and that this inures to the benefit of the surviving spouse, whose ownership prior to the death of decedent was subject to the rights of decedent therein. And there can be no question, also, that we have a "shifting of the economic benefits of property which is the real subject of the tax." As said in *Nichols v. Coolidge* (274 U. S., 531, 541 [T. D. 4072, C. B. VI-2, 351]), "Taxes are very real things and statutes imposing them are to be estimated by practical results."

We have carefully considered the cases which have reached a different conclusion, but, with great respect to the tribunals which rendered them, we do not think that they are sound. We have likewise considered the district court cases relating to the validity of the statute requiring that the value of the widow's dower be included in the value of the estate for the purpose of taxation. Without passing upon that question, which is not before us, it is worthy of note that the Circuit Court of Appeals of the Eighth Circuit has decided that the value of dower allotted under the Nebraska statute should be included in the valuation of the estate. (*Allen, Collector, v. Henggeler* (C. C. A., 8th), 32 Fed. (2d), 69.)

For the reasons stated, we think that the learned judge below erred in holding that the provision of the statute in question was violative of the Constitution. The judgment in favor of the administrators will accordingly be reversed and the case will be remanded for further proceedings not inconsistent with this opinion.

Reversed.

THE NET ESTATE.

REGULATIONS 70, ARTICLE 36: Claims against the estate. ARTICLE 40: Support of dependents. VIII-49-4455
Ct. D. 136

ESTATE TAX—REVENUE ACT OF 1916—DECISION OF COURT.

GROSS ESTATE—DEDUCTION—AMOUNT PAID FOR SURRENDER OF WIDOW'S STATUTORY RIGHTS.

An amount paid by the executor to the widow of a decedent, in addition to her rights under his will, in settlement for the surrender of her right to a year's support and her statutory rights in respect to the realty and personalty is properly included in his gross estate under section 202(a) of the Revenue Act of 1916 and is not deductible from the gross estate under section 203(a)1 as a claim or charge against the estate.

UNITED STATES CIRCUIT COURT OF APPEALS, SIXTH CIRCUIT.

Lucy G. Briscoe, Ernest J. Briscoe, P. J. Briscoe, jr., and S. V. Carter, as Executors and Trustees of the Estate of Daniel Briscoe, deceased, plaintiffs in error, v. E. B. Craig, Collector of Internal Revenue, defendant in error.

Error to the District Court for the Eastern District of Tennessee.

[April 5, 1929.]

OPINION.

MACK, Circuit Judge: In an action to recover estate tax payments, tried before the district judge without a jury, judgment was rendered for the defendant under the following circumstances:

Daniel Briscoe, a resident of Tennessee, died on February 7, 1918, survived by a wife, aged 57, and 8 children. His estate, consisting of local realty valued at about one-half million dollars and personal property amounting to \$700,000, was devised and bequeathed in trust to distribute the income, after deduction of certain charges, in equal shares among his wife and the 8 children, each to receive one-ninth thereof, and to divide the principal at a date so distant that the widow was not likely to be then surviving and thus to share therein, except upon improbable contingencies.

Soon after testator's death, the widow announced her dissatisfaction with the will and her intention, pursuant to Tennessee statutes, to dissent from the will in open court and thereupon to become entitled to dower in one-third of the real estate and a one-ninth absolute interest in the personal property, together with the equivalent of one year's support (Shannon's Code, secs. 4139, 4146-4147). Within the statutory period for such dissent, a settlement was entered into with the executors, acting in good faith, under which the widow agreed to refrain from dissenting from the will and in return received, in addition to her interest thereunder, the sum of \$75,000, for surrender of her right to a year's support and her statutory rights in respect to the realty and personalty. The tax involved on this review is in respect to the \$75,000, which defendant included in the valuation of the Briscoe estate.

A demurrer to the complaint was overruled in the District Court for the Middle District of Tennessee. In addition to certain palpably erroneous grounds of demurrer, it was assigned that "a settlement made by executors of an estate is not a claim or charge against the estate" and that "a provision in lieu of dower is taxable." The complaint sought recovery of other taxes besides the one now in issue. The cause was then transferred to the Northern Division of the Eastern District; all orders previously made were continued in force. The district judge for that district, after hearing the evidence, dismissed the action, on the ground that since the widow had not dissented from the will in open court, she necessarily took under the will; she could not and did not receive anything by way of dower or year's support. No proof was introduced at the trial bearing upon the value of the dower in Briscoe's estate; in moving for a new trial, however, plaintiffs offered to produce such evidence.

Both sides accept the holding in *Randolph v. Craig* (267 Fed., 993), that under the Revenue Act of 1916, sections 202-203, an estate tax is not payable upon dower and the value of a year's support when actually received by the widow. Therefore, plaintiffs contend, the amount paid by the executors on a settlement in order to relieve an estate of dower must likewise be free from the estate tax. In this we can not concur.

If the widow stands upon her statutory rights, then in so far as dower interest is concerned she claims adversely to the estate. What she receives in that event is no part of the estate; by relation back it existed at the moment of death as something over which deceased had no power of transfer, and against which not even creditors had any claim. For this reason it was held in the *Randolph* case that no estate tax is payable in respect to such interest under the 1916 Act, although the contrary rule has been adopted in later legislation. But this reasoning is not applicable except where dower has actually been taken. If the widow allows all the property left by the deceased to pass as part of his estate, then, regardless of the fact that an adverse interest might have been asserted, the entire property does pass as part of deceased's estate and as such is taxable. It has been so held where the widow, failing to renounce, accepted the provisions of the will; in such

cases the tax was sought to be deducted in respect to the value of the dower that she could have had if she had renounced. (*Title Guarantee & Trust Co. v. Edwards*, 290 Fed., 617, followed in *Jacobs v. Commissioner*, B. T. A. No. 3916 [see Ct. D. 128, on page 403]; *Schuette v. Bowers*, S. D. N. Y., January 29, 1929 [Ct. D. 57, C. B. VIII-1, 317].) We agree with these holdings; and plaintiffs themselves apparently concur therein, as they have not asked for any deduction for the amounts Mrs. Briscoe received as bequests under the will.

Plaintiffs, however, contend that the \$75,000 paid to the widow by the executors from the funds of the estate must be exempt from the estate tax because, even though the money was not paid to a creditor, it was paid to relieve the estate of the burden of dower. We pass the question whether this contention is maintainable on the present record, containing as it does no proof of the value of the dower interest. Plaintiffs invoke the analogy of money paid by the executors to one who, though not a creditor, nevertheless has a subcontractor's lien upon property belonging to the estate. The exemption in that case is specifically provided for by section 203(a)1, which allows deduction for "claims against the estate, unpaid mortgages * * * and such other charges against the estate as are allowed by the laws of the jurisdiction." An unexercised right to admeasurement of dower is of substantial value to the widow; her relinquishment of it is a valuable consideration for, and makes her a purchaser and not a mere donee of, the testamentary provisions accepted in lieu thereof (cf. *Overton v. Lea*, 24 Pickle, 505, 68 S. W., 250; *Warner v. Walsh*, 15 Fed. (2d), 367 [T. D. 3822, C. B. V-1, 191]); but that right does not make her a creditor of the estate or give her a lien thereon. In our judgment, her claim does not come within the terms of the above quoted statute. Apart from the statute, there is no general principle that because the exercised dower right or its value is exempt, therefore a payment to relieve the estate from a just claim to dower must likewise be exempt. If this proposition were maintainable, it would follow that the value of the provisions made in the will and accepted in lieu of dower and thereby like the cash payment relieving the estate from the dower claim, would also be exempt; a conclusion that is contrary to the cases above cited, with which cases we agree.

We conclude that, under the 1916 Act, there is no ground for exemption from the estate tax in respect to this money payment in settlement of a dower right, as no dower interest has been effectively asserted pursuant to the Tennessee statutes.

Estate of Graves (242 Ill., 212, 89 N. E., 978), Matter of Reed's Estate (162 N. Y. Supp., 412), and similar decisions cited on behalf of defendant are, however, in our judgment not in point, as in these cases the persons with whom the compromise was made did not claim to take adversely to the estate.

In the instant case there is a further objection to recovery of the estate tax. Rights in personalty acquired by a widow upon dissenting from the will can not fall within the decision of *Randolph v. Craig*, because they are subordinate to the claim of creditors. (*Cannon v. Apperson*, 14 Lea, 553, 592-594.) They are not claims against the estate but only interests in the net estate and thus not adverse to the estate as a whole. In this, they are unlike dower rights which have priority over the claims of creditors. (*Combs v. Young*, 4 Yerg., 218.) Although clearly part of the \$75,000 was paid in compromise of these rights in the personalty, plaintiffs have not shown any way in which the total sum paid could be allocated between the settlement of the dower and that of the personalty rights; they made no offer so to do even upon the motion for a new trial. Only if the whole sum were allocable to the dower, as it clearly is not, could the offer of proof made after judgment have been deemed in any way relevant for this purpose, and even in that event, the trial judge's discretionary refusal of a new trial in these circumstances would not have been assignable error.

Judgment affirmed.

CAPITAL STOCK TAX RULINGS.

TITLE VII.—SPECIAL TAXES. (1924)

REGULATIONS 64(1924), ARTICLE 11: Basis of the
tax: "Carrying on or doing business."

VIII-51-4475
Ct. D. 141

CAPITAL STOCK TAX—REVENUE ACTS OF 1921 AND 1924—DECISION OF COURT.

"DOING BUSINESS."

Where a landowning company leases land and advances money to a coal company which conducts a mining business, sells, on several occasions, bonds it held for investment, and builds up a large profit and loss account consisting mostly of bonds, the land company is "doing business" within the meaning of section 1000 of the Revenue Act of 1921 and section 700 of the Revenue Act of 1924. A fortiori it is "doing business" in view of the fact that the two corporations are owned by the same person through whom the land company is assisting in the coal operations of the coal company, both corporations being operated in effect as one business.

COURT OF CLAIMS OF THE UNITED STATES.

Morrisdale Land Co. v. The United States.

[February 4, 1929.]

OPINION.

GRAHAM, Judge, delivered the opinion of the court.

This is a suit to secure the refund of certain capital-stock taxes paid by the plaintiff for the years ending June 30, 1922, 1923, 1924, and 1925. The taxes were assessed and collected upon the theory that during these taxable years the plaintiff was "carrying on or doing business" within the meaning of section 1000 of the Revenue Act of 1921 (42 Stat., 227) and section 700 of the Revenue Act of 1924 (43 Stat., 325).

One F. H. Wigton, prior to the year 1914, owned 2,666 acres of coal land, upon which were a derrick, miners' houses, and other buildings necessary to the conduct of mining operations, and he also owned the Morrisdale Coal Co., a coal operating company. In 1914 the said Wigton organized and had incorporated the plaintiff corporation, under the laws of the State of Pennsylvania, with a capital stock of \$5,000, and the declared purpose of "purchasing, holding, leasing, and selling real estate." Immediately after its organization the said Wigton conveyed title to the said coal lands to plaintiff and received therefor in payment \$200,000 in its bonds and all of its capital stock of \$5,000.

It will be seen, therefore, that the said Wigton, while owning all of the stock of the Morrisdale Coal Co., at the same time owned all of the stock and bonds of the plaintiff; that is to say, both companies were owned by the same person, and for all practical purposes this person was in each case the company. Immediately after it was incorporated the plaintiff leased to the Morrisdale Coal Co.—that is to say, Wigton in effect leased to himself—the coal lands which had been conveyed to the plaintiff, and also continued certain existing leases then held by the Morrisdale Coal Co. The latter conducted a mining business, the plaintiff did not, and it will be readily seen had no occasion for

doing so, as Wigton was already, through the Morrisdale Coal Co., conducting the coal business.

Wigton, in the management of the two companies, arranged that the plaintiff should get its income from the rents and royalties received from these leases and from its profits and interest on the securities which it held. It arranged that the Morrisdale Coal Co. should pay for certain repairs to the buildings and apparatus on the lands, while the plaintiff paid for the greater part of the capital improvements and also taxes on the land, the bookkeeping and distribution of work in each case being arranged, of course, by Wigton, the owner of both companies. The officers of the two companies were the same and were paid as officers of the Morrisdale Coal Co. The plaintiff did not maintain separate offices, but conducted its business, held its meetings, and kept its accounts in the offices of the Morrisdale Coal Co.

The plaintiff owned a store building on the premises, and it leased this to another company, the Morrisdale Supply Co., the stock of which was also all owned by Wigton. Advances were made in 1925 and 1926 to the Morrisdale Coal Co. by the plaintiff, together with certain insurance money, to enable the Morrisdale Coal Co. to rebuild the store building, which had been burned down, and the Morrisdale Coal Co. on several occasions prior to July, 1921, advanced money to plaintiff in order to enable it to pay off its bonds.

The plaintiff paid no dividends during its existence, but paid off its bonds (\$200,000) and built up by 1923 a profit and loss account of over \$61,000, which included over \$52,000 in bonds. Plaintiff's capital account showed an average real estate account of \$35,000 and coal lands of an estimated value of from \$350,000 to \$500,000 in 1914, and the only liability on the capital side of the account was the capital stock of \$5,000 and \$126,738.10 carried as paid-in surplus.

On several occasions the plaintiff sold at a profit some of the bonds which it held for investment and maintained a working capital of from \$1,000 to \$9,000, and paid taxes each year on its real estate amounting to about \$800. It paid its capital stock taxes of \$659 for the years stated above, namely, June 30, 1922, 1923, 1924, and 1925. Plaintiff for these years tendered to the Government its capital stock returns, and the tax was assessed according to the returns, and paid. The last payment was made for the year ending June 30, 1925. On or about July 29, 1925, plaintiff filed with the collector at Philadelphia a claim demanding the refund of \$659, the total tax paid for these years, on the ground that it was not doing business within the meaning of the statute and therefore not subject to a capital stock tax.

It will be seen from the foregoing that the plaintiff and the Morrisdale Coal Co., when their corporate garments are pulled aside, reveal Wigton as the person doing business in each case. He owned both companies; their offices were in the same place; they transferred money from one to the other as might be necessary, and were undoubtedly two parts which made up one operation and one concern. It is perfectly clear that the plaintiff was doing business and assisting in the coal operations of the Morrisdale Coal Co. But, aside from that, were it standing alone and not intimately connected with the operation of the Morrisdale Coal Co., it would be within the meaning of the statute. We hold that it was carrying on and doing business within the meaning of the statute, and was right originally when it rendered its returns each year for capital stock taxes and paid them.

It is clear that under the provisions of the statute each case must rest upon its own bottom and its own facts. There can be no rule of general application laid down to cover the language of the statute "carrying on and doing business," except that no particular amount of business is required in order to bring a party within the terms of the statute. (See *Von Baumbach v. Sargent Land Co.*, 242 U. S., 503, 517 [T. D. 2436].) Compare the following cases: *Chevrolet Motor Co. v. United States* (64 C. Cls., 211 (certiorari denied) [T. D. 4123, C. B. VII-1, 329]); *Edgar States Corporation v. United States* (65 C. Cls., 415 [T. D. 4180, C. B. VII-2, 381]); *Conhaim Holding Co. v. Willcuts* (21 Fed. (2d), 91 [T. D. 4090, C. B. VI-2, 374]); *Flint v. Stone-Tracy Co.* (220 U. S., 107); *Edwards v. Chile Copper Co.* (270 U. S., 452 [T. D. 3857, C. B. V-1, 410]); and *Harmar Coal Co. v. Heiner* (26 Fed. (2d), 729).

Plaintiff is not entitled to recover and its petition should be dismissed. It is so ordered.

TAX ON DOMESTIC CORPORATIONS.

REGULATIONS 64, ARTICLE 15: Fair average value of capital stock.

VIII-37-4357
Ct. D. 109

CAPITAL STOCK TAX—REVENUE ACT OF 1924—DECISION OF COURT.

FAIR AVERAGE VALUE OF CAPITAL STOCK—EXISTENCE OF ONE MONTH.

For the purpose of determining the amount of the capital stock tax on a corporation in existence only for the month of June preceding the taxable year commencing July 1, during which month there was no change in the value of the stock, "the fair average value of its capital stock for the preceding year ending June 30," the measure of the tax provided by section 700(a)1 of the Revenue Act of 1924, is the value of the shares during the month of its existence and not one-twelfth of such value.

COURT OF CLAIMS OF THE UNITED STATES.

Alaska Consolidated Canneries, Inc., v. The United States.

[February 4, 1929.]

OPINION.

Moss, Judge, delivered the opinion of the court.

The facts in this case are stipulated by the parties, and may briefly be stated as follows:

Plaintiff was incorporated in March, 1925, with an authorized capital stock of \$2,000,000. It had no assets, and was not engaged in business prior to June 1, 1925. On that date plaintiff acquired certain salmon-canning plants of the value of \$2,000,000, in payment of the total authorized issue of 20,000 shares of the stock in plaintiff company. On July 24, 1925, plaintiff filed its capital stock tax return for the taxable period July 1, 1925, to June 30, 1926, showing, among other facts, the fair value of the capital stock of plaintiff on June 30, 1925, to be \$2,000,000, and paid the tax shown to be due by said return, amounting to \$1,995. Plaintiff thereafter filed a claim for the refund of \$1,864 of this amount, on the ground that inasmuch as plaintiff was engaged in business only for the month of June in the year 1925 the fair value of the stock should have been computed by taking one-twelfth of the value of same, which method would result in a tax liability of only \$131. The claim was rejected, and this action is brought for the recovery of said sum, \$1,864.

The tax in question, known as the capital stock tax, is imposed by section 700(a) of the Revenue Act of 1924 (43 Stat., 325), which reads as follows:

"On and after July 1, 1924, in lieu of the tax imposed by section 1000 of the Revenue Act of 1921—

"(1) Every domestic corporation shall pay annually a special excise tax with respect to carrying on or doing business, equivalent to \$1 for each \$1,000 of so much of the fair average value of its capital stock for the preceding year ending June 30 as is in excess of \$5,000. In estimating the value of capital stock the surplus and undivided profits shall be included;

"(2) * * *

"(b) The taxes imposed by this section shall not apply in any year to any corporation which was not engaged in business * * * during the preceding year ending June 30, * * *."

The capital stock tax is an excise tax imposed on a corporation for the privilege of doing business. It is assessed and collected *annually* for the privilege of doing business in the following year, and the tax is measured by values relating to the preceding year. Regulations 64 (1924 edition), article 14, as amended by Treasury Decision 3771 [C. B. IV-2, 272, 273], contains the clear and pertinent statement: "The tax is measured by the fair average value of the capital stock of the corporation for the year ending June 30 preceding the taxable period. A corporation *in existence less than a year on July 1 of the taxable period* will be permitted to consider values only *during that portion*

of the year it was in existence." [Our italics.] In the present case the corporation was in existence only for the month of June in the year preceding the taxable period. There was no change whatever in the value of the stock from June 1 to June 30, 1925. Where there is no change in value, there is no occasion for determining the "fair average value." It is only in case of an increase or a decrease in value that the term used in the statute, "fair average value," has any importance. The regulation above cited contains the statement: "A corporation in existence less than a full year will *average* the shares outstanding from the date of its incorporation to June 30, following." [Our italics.] Again, it is suggested that it is not possible to apply the rule of the *average* mentioned in this regulation to a value which has neither been increased nor decreased during the period under consideration, to wit, during the month of June, 1925. It must be borne in mind that the sole purpose of ascertaining the value for the preceding year is to obtain a measure for the computation of the tax for the coming year. The case relied on by plaintiff, *One Liberty Street Realty and Securities Corporation v. Bowers* (8 Fed. (2d), 278), has no application to the question involved here. In that case the value of the capital stock was enhanced by substantial increases. The court held, in substance, that the fair value of the capital stock was not the same throughout the year, and that the Commissioner should have considered that fact in ascertaining the *fair average value* of the stock for the preceding year. Plaintiff is not entitled to recover, and the petition will be dismissed.

TITLE X.—SPECIAL TAXES. (1918 AND 1921)

REGULATIONS 50 (REVISED), ARTICLE 3; REGULATIONS 64 (1922), ARTICLE 4: Associations and joint-stock companies.

VIII-31-4298
Ct. D. 88

CAPITAL STOCK TAX—REVENUE ACTS OF 1918 AND 1921—DECISION OF COURT.

1. ASSOCIATION—STATE AGENCY ENGAGED IN BANKING.

The Bank of North Dakota, an agency of that State, which is engaged in the business of banking under the management, like that of a board of directors, of the industrial commission of the State, is an "association" within the meaning of section 1 of the Revenue Acts of 1918 and 1921.

2. EXEMPTION—INSTRUMENTALITY OF A STATE.

The exemption of State agencies and instrumentalities from taxation by the United States is limited to those of a strictly governmental character and does not extend to those which are used by a State in the carrying on of an ordinary private business.

3. SAME.

The Bank of North Dakota, whose capital stock is owned by that State and which is engaged in the business of banking, is not exempt as an instrumentality of the State from the capital stock tax imposed by the Revenue Acts of 1918 and 1921.

UNITED STATES CIRCUIT COURT OF APPEALS, EIGHTH CIRCUIT.

The State of North Dakota doing business as the Bank of North Dakota, appellant, v. Gunder Olson, as Collector of Internal Revenue of the United States for the District of North Dakota, appellee.

Appeal from the District Court of the United States for the District of North Dakota.

[June 24, 1929.]

OPINION.

PHILLIPS, Circuit Judge, delivered the opinion of the court.

This is an action brought by the Bank of North Dakota against Gunder Olson, as collector of internal revenue for the district of North Dakota, to

recover the sum of \$6,085 assessed and collected from the Bank of North Dakota under the capital stock tax provision of the United States Revenue Acts of 1918 and 1921.

From a decree in favor of the collector the bank has appealed.

In 1918, the constitution of North Dakota was amended by the adoption of article 32 of amendments, which reads as follows:

"The State, any county or city, may make internal improvements, and may engage in any industry, enterprise or business not prohibited by article 20 of the constitution."

Article 20 relates to the manufacture and sale of intoxicating liquors.

The bank of North Dakota was created by chapter 147 of the Session Laws of North Dakota for 1919. Section 1 of that act reads as follows:

"For the purpose of encouraging and promoting agriculture, commerce and industry, the State of North Dakota shall engage in the business of banking, and for that purpose shall, and does hereby, establish a system of banking owned, controlled and operated by it, under the name of the Bank of North Dakota."

Section 2 of such act provides that it shall be operated, managed, and controlled by the industrial commission. The industrial commission was created by chapter 151 of the Session Laws of North Dakota for 1919, and is composed of the governor, the attorney general, and the commissioner of agriculture and labor.

Section 5 of chapter 151, supra, provides that the commissioner is empowered to manage, operate, control, and govern all utilities, industries, enterprises, and business projects now or hereafter established, owned, undertaken, administered, or operated, by the State of North Dakota, except penal, charitable, and educational institutions.

Section 3 of chapter 147, supra, authorizes the commission to acquire all requisite property and property rights for the bank.

Section 4 of chapter 147, supra, authorizes the commission to employ a manager and necessary subordinate officers and employees.

Section 6 of chapter 147, supra, provides for the issuance by the State of \$2,000,000 in bonds to provide the capital for the bank.

Section 7 of chapter 147, supra, provides that public funds shall be deposited in the bank.

Section 9 of chapter 147, supra, provides that the bank may receive deposits from any source.

Section 14 of chapter 147, supra, provides that the bank may deposit funds in any other bank or banking association.

Section 15 of chapter 147, supra, provides that the bank may make loans to political subdivisions of the State, to State and National banks, and when secured by first mortgages on real estate in the State of North Dakota to private persons or corporations.

Section 22 of chapter 147, supra, provides that the bank may be sued on account of causes of action claimed to have arisen out of transactions connected with the operation of the bank.

Counsel for the bank rely upon two principal propositions:

First. That the bank is neither a corporation, an association, nor a joint stock company, and therefore does not come within the purview of the capital stock tax provision of the Federal Revenue Acts of 1918 and 1921.

Second. That the Federal Government has no power, under the Constitution of the United States, to levy a capital stock tax upon the Bank of North Dakota, because such bank is a governmental agency of the State of North Dakota and exempt from Federal taxation.

Taking up the first contention of counsel for the bank, we find that section 1000(a) of the Revenue Act of 1918, in part, provides:

"(1) Every domestic corporation shall pay annually a special excise tax with respect to carrying on or doing business, equivalent to \$1 for each \$1,000 of so much of the fair average value of its capital stock for the preceding year ending June 30, as is in excess of \$5,000."

and that section 1 of such Act, in part, provides:

"The term 'corporation' includes associations, joint-stock companies, and insurance companies."

These provisions were reenacted by sections 1 and 1000(a) of the Revenue Act of 1921.

In construing these provisions, in *Hecht v. Malley* (265 U. S., 144, at 154 [T. D. 3595, C. B. III-1, 489]) the Supreme Court said:

"Reading together the defining and enacting sections of the Act it is as if section 1000(a) provided in terms that: Every corporation, association, joint-stock company, and insurance company, 'created or organized in the United States,' shall pay a special excise tax, as prescribed, with respect to the carrying on or doing business. And it must be given effect as thus read."

We are of the opinion that the broad language employed by Congress in the provisions of the Act above quoted manifested an intent on the part of Congress to levy an excise tax on every kind of business association.

The Bank of North Dakota is an artificial being created by statute to engage in the banking business. It is endowed with certain powers and capable of subjecting itself to liabilities. It may sue and be sued. It has a capital stock owned by the State. It is managed by the industrial commission, which corresponds to a board of directors. It possesses the attribute of a corporation sole and, unless exempt because it is an instrumentality of the State, is subject to the tax.

The second contention made by counsel for the bank presents a more difficult problem. The general principles which must be adhered to in determining whether the bank, as an instrumentality of the State, is exempt from Federal taxation were stated by the Supreme Court in *Metcalf & Eddy v. Mitchell* (269 U. S., 514, at 522 and 523 [T. D. 3824, C. B. V-1, 218]), as follows:

"Just what instrumentalities of either a State or the Federal Government are exempt from taxation by the other can not be stated in terms of universal application. But this court has repeatedly held that those agencies through which either government immediately and directly exercises its sovereign powers are immune from the taxing power of the other.

* * * * *

"But neither government may destroy the other nor curtail in any substantial manner the exercise of its powers. Hence the limitation upon the taxing power of each, so far as it affects the other, must receive a practical construction which permits both to function with the minimum of interference each with the other; and that limitation can not be so varied or extended as seriously to impair either the taxing power of the government imposing the tax * * * or the appropriate exercise of the functions of the government affected by it. * * *

"While it is evident that in one aspect the extent of the exemption must finally depend upon the effect of the tax upon the functions of the government alleged to be affected by it, still the nature of the governmental agencies or the mode of their constitution may not be disregarded in passing on the question of tax exemption; for it is obvious that an agency may be of such a character or so intimately connected with the exercise of a power or the performance of a duty by the one government, that any taxation of it by the other would be such a direct interference with the functions of government itself as to be plainly beyond the taxing power.

"It is on this principle that, as we have seen, any taxation by one government of the salary of an officer of the other, or the public securities of the other, or an agency created and controlled by the other, exclusively to enable it to perform a governmental function, * * * is prohibited."

Of the adjudicated cases, the one most nearly in point is *South Carolina v. United States* (199 U. S., 437). In that case, the State of South Carolina, under the provisions of several statutes adopted by the State, had established dispensaries for the wholesale and retail sale of intoxicating liquor, and had prohibited the sale thereof by other than such dispensaries. The State was the principal, and the dispensaries acted as the agents of such principal in selling such liquor. The dispensaries had no interest in the sales and received no profits therefrom. The entire profits were appropriated by the State, one half being divided equally between the municipality and the county in which the dispensaries were located and the other half paid into the State treasury. The State protested payment of certain internal revenue license taxes and brought three actions in the Court of Claims to recover the amounts paid. These actions were consolidated, judgment in the Court of Claims went in favor of the United States, and the case came before the Supreme Court of the United States on appeal.

The dispensaries were established by the State in the exercise of its police power to regulate the liquor traffic. The argument was made that if Congress

could tax the agents of the State charged with the duty of selling intoxicating liquors, it could in effect assume control over the police power of the State to regulate the liquor traffic within its borders and could thus embarrass and thwart the attempt of the State to carry on its adopted mode of regulation. In disposing of this argument, the Supreme Court said:

"We are not insensible to the force of this argument, and appreciate the difficulties which it presents, but let us see to what it leads. Each State is subject only to the limitations prescribed by the Constitution and within its own territory is otherwise supreme. Its internal affairs are matters of its own discretion. The Constitution provides that 'the United States shall guarantee to every State in this Union a republican form of government' (Article IV, section 4.) That expresses the full limit of national control over the internal affairs of a State.

"The right of South Carolina to control the sale of liquor by the dispensary system has been sustained. (*Vance v. W. A. Vandercook Co.*, No. 1, 170 U. S., 438.) The profits from the business in the year 1901, as appears from the findings of fact, were over half a million of dollars. Mingling the thought of profit with the necessity of regulation may induce the State to take possession, in like manner, of tobacco, oleomargarine, and all other objects of internal revenue tax. If one State finds it thus profitable other States may follow, and the whole body of internal revenue tax be thus stricken down.

"More than this. There is a large and growing movement in the country in favor of the acquisition and management by the public of what are termed public utilities, including not merely therein the supply of gas and water, but also the entire railroad system. Would the State by taking into possession these public utilities lose its republican form of government?

"We may go even a step further. There are some insisting that the State shall become the owner of all property and the manager of all business. Of course, this is an extreme view, but its advocates are earnestly contending that thereby the best interests of all citizens will be subserved. If this change should be made in any State, how much would that State contribute to the revenue of the Nation? If this extreme action is not to be counted among the probabilities, consider the result of one much less so. Suppose a State assumes under its police power the control of all those matters subject to the internal revenue tax and also engages in the business of importing all foreign goods. The same argument which would exempt the sale by a State of liquor, tobacco, etc., from a license tax would exempt the importation of merchandise by a State from import duty. While the State might not prohibit importations, as it can the sale of liquor, by private individuals, yet paying no import duty it could undersell all individuals and so monopolize the importation and sale of foreign goods.

"Obviously if the power of the State is carried to the extent suggested, and with it is relief from all Federal taxation, the National Government would be largely crippled in its revenues. Indeed, if all the States should concur in exercising their powers to the full extent, it would be almost impossible for the Nation to collect any revenues. In other words, in this indirect way it would be within the competency of the States to practically destroy the efficiency of the National Government."

The court then proceeds to review the authorities bearing upon the question of when an instrumentality of the State is subject to Federal taxation, and at page 461 further says:

"These decisions, while not controlling the question before us, indicate that the thought has been that the exemption of State agencies and instrumentalities from national taxation is limited to those which are of a strictly governmental character, and does not extend to those which are used by the State in the carrying on of an ordinary private business."

The court then takes up the distinction between the governmental powers exercised by a municipal corporation and the private powers exercised by such corporation and shows how, when a municipality engages in the latter, it is clothed with none of the immunities of sovereignty and is liable for negligent acts, and at page 463 further says:

"Now, if it be well established, as these authorities say, that there is a clear distinction as respects responsibility for negligence between the powers granted to a corporation for governmental purposes and those in aid of private business, a like distinction may be recognized when we are asked to limit the full power

of imposing excises granted to the National Government by an implied inability to impede or embarrass a State in the discharge of its functions. It is reasonable to hold that while the former may do nothing by taxation in any form to prevent the full discharge by the latter of its governmental functions, yet whenever a State engages in a business which is of a private nature that business is not withdrawn from the taxing power of the Nation.

"For these reasons we think that the license taxes charged by the Federal Government upon persons selling liquor is not invalidated by the fact that they are the agents of the State which has itself engaged in that business."

In the case of *Flint v. Stone Tracy Co.* (220 U. S., 107, at 157) the Supreme Court adverted to its former opinion in *South Carolina v. U. S.*, and said:

"In the opinion previous cases in this court here were reviewed, and the rule to be deduced therefrom stated to be that the exemption of State agencies and instrumentalities from national taxation was limited to those of a strictly governmental character, and did not extend to those used by the State in carrying on business of a private character."

It therefore becomes necessary to determine whether the Bank of North Dakota is an instrumentality of the State of a strictly governmental character or is an instrumentality of the State used to carry on a business of a private character.

It is well settled that when a State creates a corporation for the purpose of engaging in private business and acquires either a part or the whole of the capital thereof, it divests itself, so far as it concerns the transactions of such corporation, of its sovereign character and takes that of a private citizen. Instead of communicating to the corporation its privileges and prerogatives, it descends to the level of a private citizen. As to the transactions of such corporation, it can not claim the privileges or immunities of a sovereign. (*U. S. v. Planters Bank*, 9 Wheat., 904; *Curran v. The Bank of the State of Arkansas*, 15 How., 304, 308; *Georgia v. Chattanooga*, 264 U. S., 472, 481; *Metropolitan Savings Bank & T. Co. v. Farmers State Bank*, 20 Fed. (2d), 775, 779; *Briscoe v. Bank of Kentucky*, 11 Pet., 257, 323, 324; *Darrington v. Bank of Alabama*, 13 How., 12; *Western Railway v. Carlton*, 28 Ga., 180; *Gross v. Managers of World Columbian Expedition*, 105 Ky., 840, 49 S. W., 458.)

The Supreme Court of North Dakota, in the case of *Sargent County v. State, doing business as Bank of North Dakota* (47 N. Dak., 561, 182 N. W., 270, 272, 273, 274), expressly approved the doctrine of the cases last above cited. The question before the North Dakota court was whether the bank could be sued by a proceeding in garnishment. The court quoted from the opinion of Chief Justice Marshall in the *Planters Bank* case, as follows:

"It is, we think, a sound principle, that when a government becomes a partner in any trading company, it divests itself, so far as concerns the transactions of that company, of its sovereign character, and takes that of a private citizen. Instead of communicating to the company its privileges and its prerogatives, it descends to a level with those with whom it associates itself, and takes the character which belongs to its associates, and to the business which is to be transacted."

Reviewing the case of *Curran v. The Bank of the State of Arkansas*, supra, the North Dakota court said:

"It appeared that the Bank of the State of Arkansas was incorporated by legislative act with the usual banking powers of discount, deposit, and circulation; that the State was its sole stockholder; that the capital stock of the bank consisted of \$1,146,000 raised by the sale of State bonds and certain other sums. It was again held that a bank was a distinct trading corporation having a complete separate existence; enabled to enter into valid contracts by itself alone and having specific capital stock, provided and held out to the public, as a means to pay its debts; that the obligations of its contracts, the funds provided for their performance, and the equitable rights of its creditors, were in no way affected by the fact that a sovereign State paid in its capital and consequently became entitled to its property. It further reaffirmed the principle that a State by owning all of the capital stock does not impart to that corporation any of its privileges or prerogatives; that it lays down its sovereignty so far as respects the transactions of the corporation and exercises no power or privilege in respect to those transactions not derived from the charter."

We think it a fair deduction from this opinion that the North Dakota court is of the opinion that the Bank of North Dakota is engaged in a private business.

Counsel for the bank urge that a contrary conclusion must be drawn from the opinions in *Green v. Fraser, Governor, et al.* (44 N. Dak., 395, 176 N. W., 11, and 253 U. S., 233). In that case, the purposes for which the bank was created were considered in relation to the taxing power and it was held that the bank was created for a public purpose, which would authorize the levy of taxes to pay the principal and interest on the bonds issued to provide capital for the bank. However, there is a distinction between public purpose and governmental function. The distinction is recognized in cases involving the exemption of property from taxes where property devoted to a public use is exempted. The authorities hold that "public purpose" is not synonymous with "governmental purpose." (See *Cooley on Taxation*, 4th ed., vol. 2, sec. 639; *San Felipe de Austin v. State*, 111 Tex., 108, 229 S. W., 845, 847.) This distinction is frequently noticed in cases involving the liability of municipal corporations for tort. In the case of *Eastern Illinois State Normal School v. City of Charleston* (271 Ill., 602, 111 N. E., 573) the court said:

"* * * In the creation of a system of waterworks and the operation of the same for the purpose of protection against fire, flushing sewers, or other uses pertaining to the public health and safety, the city is in the exercise of the police power and is therefore exercising a governmental function. * * * In supplying the water for the use of the inhabitants for domestic and commercial purposes, a municipality is not in the exercise of a governmental power, but acts in the same capacity as a private corporation, although the business is carried on for the public advantage, and, being public in its nature, is impressed with a public use. * * *

It will be observed that the Supreme Court in the case of *So. Carolina v. U. S.*, supra, noted the analogy between the two kinds of power exercised by a municipal corporation and the two kinds of function performed by instrumentalities of a State.

Is the Bank of North Dakota an instrumentality of the State used by such State in carrying on a business of a private character? The Bank of North Dakota has a capital. It has what amounts to a board of directors. It makes loans to privately owned banks and to individuals on real estate security. It receives deposits from the public generally. It may sue and be sued with reference to all its banking transactions.

"It possesses a status distinct and separate from that of the State itself, a status of a State enterprise circumscribed by and dependent upon the rights, powers, and liabilities created by a specific statutory enactment." Its profits accrue to it as a bank and "are not public funds of the State for disbursement in governmental operations." (*Sargent County v. State*, supra, 182 N. W., 269, 274, 275.) While it is a depository of public funds, in this respect it merely succeeds to the functions formerly performed by privately owned depository banks. (*State v. Waters*, 45 N. Dak., 115, 176 N. W., 913, 914.) While it was created to promote the general welfare of the State, the people of the State, by an amendment to its constitution, recognized that such public welfare might be promoted by the State engaging in private business. We think these facts compel an affirmative answer to the question.

Furthermore, there is no limitation on the power of the State of North Dakota to engage in private business, and if the bank is exempt from Federal taxation the way is open for the State of North Dakota to relieve its citizens from all Federal excise taxes. It was such a dangerous consequence which the Supreme Court sensed in *South Carolina v. U. S.*, and which no doubt had a controlling influence upon the decision of the court in that case.

It is our conclusion that the Bank of North Dakota, while an instrumentality of the State, is one created by the State to engage in carrying on business of a private character and that as such it is subject to the excise tax imposed by section 1000(a) of the Revenue Acts of 1918 and 1921.

The decree is affirmed with costs.

MISCELLANEOUS TAX RULINGS.

TITLE VIII.—STAMP TAXES. (1926)

SCHEDULE A-5. PASSAGE TICKETS.

REGULATIONS 71, ARTICLE 58: Passage tickets to ports not in the United States, Canada, Mexico, or Cuba. VIII-49-4456
G. C. M. 7152

Seaplanes, hydroplanes, and amphibian airplanes are "vessels" within the meaning of subdivision 5 of Schedule A of Title VIII of the Revenue Act of 1926. Passage tickets on such planes to the Canal Zone, Porto Rico, Panama, and the Bahama Islands are subject to the stamp tax imposed by that subdivision. Landplanes are not "vessels."

Inquiry is made relative to the application of the stamp tax on tickets covering passage by seaplanes, hydroplanes, amphibian airplanes, and landplanes.

Schedule A-5, Title VIII, Revenue Act of 1926, as amended by section 442 of the Revenue Act of 1928, imposes a stamp tax on—

5. Passage ticket, one way or round trip, for each passenger, sold or issued in the United States for passage by any vessel to a port or place not in the United States, Canada, Mexico, or Cuba, if costing not exceeding \$30, \$1; costing more than \$30 and not exceeding \$60, \$3; costing more than \$60, \$5. This subdivision shall not apply to passage tickets costing \$10 or less.

A ruling is requested specifically as to whether tickets sold in the United States for passage over air lines to places outside of the United States, Cuba, and Mexico are subject to the stamp tax imposed by Schedule A-5, *supra*, and also as to whether tickets for passage on planes to the Canal Zone are exempt from the tax.

The first question to be decided is whether seaplanes, hydroplanes, amphibian airplanes, or landplanes, constitute "vessels" within the meaning of Schedule A-5. Section 3 of the United States Revised Statutes (U. S. C. A., Title 1, sec. 3) defines a vessel as follows:

SEC. 3. "*Vessel*" as including all means of water transportation.—The word "vessel" includes every description of water craft or other artificial contrivance used, or capable of being used, as a means of transportation on water. (R. S., sec. 3.)

In the case of *The Crawford Bros.*, No. 2 (215 Fed., 269), the United States District Court for the Western District of Washington had occasion to decide whether an admiralty court had jurisdiction of a suit to establish and enforce a lien for repairs against an aeroplane not adapted for use on water. The court concluded its opinion as follows:

The action of the Juridic Committee on Aviation manifests a recognition of the fact that legislation is necessary for the regulation of aircraft. They are

neither of the land nor sea, and, not being of the sea or restricted in their activities to navigable waters, they are not maritime.

In the case of *Reinhardt v. Newport Flying Service Corporation et al.* (232 N. Y., 115, 133 N. E., 371), the Court of Appeals of New York was called upon to decide whether a hydroaeroplane, while on the water, is a "vessel." The court went into the matter very carefully and in the course of its opinion made the following statements, viz:

We think the craft, though new, is subject, while afloat, to the tribunals of the sea. Vessels in navigable waters are within the jurisdiction of the admiralty. Any structure used, or capable of being used, for transportation upon water, is a vessel. (U. S. Compiled Statutes, Title 1, ch. 1, sec. 3; *Chas. Barnes Co. v. One Dredgeboat* [D. C.], 169 Fed., 895.) All that remains is to ascertain the uses and capacities of the structure to be classified. The conclusion might be more dubious if the word "vessel" had been interpreted grudgingly and narrowly. The fact is that it has been interpreted liberally and broadly. It includes a canal boat drawn by horses (*The Robert W. Parsons*, 191 U. S., 17, 30, 24 Sup. Ct., 8, 48 L. Ed., 73); a bathhouse upon floats (*The Public Bath* [D. C.] No. 13, 61 Fed., 692); a raft (*The Mary* [D. C.], 123 Fed., 609); a scow (*The Sunbeam*, 195 Fed., 468, 115 C. C. A., 370; *Geo. Leary Const. Co. v. Matson* [C. C. A.], 272 Fed., 461); a dredge (*Chas. Barnes Co. v. One Dredgeboat*, supra; *Saylor v. Taylor*, 77 Fed., 476, 23 C. C. A., 343; *Ellis v. United States*, 206 U. S., 246, 259, 27 Sup. Ct., 600, 51 L. Ed., 1047, 11 Ann. Cas., 589); a temporarily sunken drillboat (*Eastern S. S. Corp. v. Great Lakes D. & D. Co.*, 256 Fed., 497, 168 C. C. A., 13); anything upon the water where movement is predominant rather than fixity or permanence (*Cope v. Vallette Dry Dock Co.*, 119 U. S., 625, 7 Sup. Ct., 336, 30 L. Ed., 501); *Berton v. Tietjen & Lang Dry Dock Co.* [D. C.], 219 Fed., 763, 774; *The Mac*, 7 P. D., 126; *The Mudlark* [1911], p. 116; *The Whitton* [1896], p. 42, 57, affirmed [1897], A. C., 337). A hydroaeroplane, while in the air, is not subject to the admiralty (*Crawford Bros.*, No. 2 [D. C.], 215 Fed., 269), or so at least we may assume, because it is not then in navigable waters, and navigability is the test of admiralty jurisdiction.

A hydroaeroplane, while afloat upon waters capable of navigation, is subject to the admiralty, because location and function stamp it as a means of water transportation. Such a plane is, indeed, two things—a seaplane and an aeroplane. To the extent that it is the latter, it is not a vessel, for the medium through which it travels is the air. (*Crawford Bros.*, No. 2, supra.) To the extent that it is the former, it is a vessel, for the medium through which it travels is the water. If a seaplane, incapable of flight, breaks its moorings and causes injury to man or ship, there will be a remedy against the offending res. If, moving upon the water, it becomes disabled, and is rescued on the high seas by a ship, it will be subject to a lien for salvage. We think the jurisdiction of the admiralty is not less where the structure found afloat is seaplane and aeroplane combined. It is true that the primary function is then movement in the air, and that the function of movement in the water is auxiliary and secondary. That is, indeed, a reason why the jurisdiction of the admiralty should be excluded when the activities proper to the primary function are the occasion of the mischief. It is no reason for the exclusion of jurisdiction when the mischief is traceable to the function that is auxiliary and secondary. Collision does not cease to be collision and a peril of the sea because the structure is amphibious. We can not even say that the chance that the peril will be encountered is so remote as to be negligible. The records of the Navy Department show that there have been times, in transatlantic flights, when planes, abandoning the air, moved for days upon the water. The cause might be lack of fuel or other disability. Even in the absence of such causes, there must always, for at least some space, be movement upon the water before there is ascent into the air. Jurisdiction can not vary as the distance is short or longer. That would require us to say that the plane, by keeping to the water, could transform itself into a vessel, but would leave us helpless to define the point at which transformation would be suffered. From such embarrassments of definition there is but one avenue of escape. It is found in the conclusion that the plane is a vessel, and hence within the jurisdiction of the admiralty, when it is in the fulfillment of its function as a traveler through water, and has put aside its functions and capacities as a traveler through air.

The conclusion to which we are thus led is in accordance with the practice of the Government, so far as practice has developed. The Treasury Department of the United States requires seaplanes or hydroplanes to be registered as vessels. The same Department has held that in navigating the water they are subject to the rules of the road. It has also held them to be vessels within the meaning of the tariff law (Act Oct. 3, 1913, sec. 4-J, subds. 5 and 6 [U. S. Comp. St., secs. 5309, 5310]; Treasury Decision No. 36156). Rulings not dissimilar have been made by the Department of Commerce. * * *

Upon a careful consideration of the foregoing authorities, it is clear that seaplanes and hydroplanes are vessels. A so-called amphibian, being an airplane constructed to arise from or alight on either land or water, also belongs to this same general class. All three types come within the definition of a vessel embodied in the United States Statute, *supra*, because all of them are artificial contrivances used, or capable of being used, as a means of transportation on water. A landplane, even though used for passage over (i. e. above) water, does not come within the definition of a vessel, because it is not used, or capable of being used, as a means of transportation on water. Thus there is a clear distinction in this respect between a seaplane and a landplane. It is therefore the opinion of this office that the stamp tax in question is not applicable to tickets for passage by landplanes, but that it is applicable to tickets for passage on seaplanes, hydroplanes, or amphibian airplanes to places coming within the terms of Schedule A-5.

Section 2(a)5 of Title I, Revenue Act of 1926, provides that the term "United States," when used in that law in a geographical sense, includes only the States, the Territories of Alaska and Hawaii, and the District of Columbia. As the term "United States" is undoubtedly used in a geographical sense in Schedule A-5, it follows that tickets sold or issued in the United States for passage on seaplanes, hydroplanes, or amphibian airplanes to the Canal Zone, Porto Rico, Panama, and the Bahama Islands are subject to the stamp tax in question, provided the amount paid for passage is in excess of \$10.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

EXPORTATION WITHOUT PAYMENT OF TAX.

REGULATIONS 73, ARTICLE 5: Shipping cases.

VIII-44-4417
T. D. 4273

EXPORT SHIPPING CASE LEGEND.

Change in legend on export shipping case authorized. Article 5(a)3, Regulations 73, amended.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, D. C.

To Collectors of Internal Revenue and Others Concerned:

Article 5(a)3 of Export Regulations 73 (1928 edition) is amended by inserting after the first sentence therein two new sentences to read as follows:

A manufacturer who exports goods in behalf of another person or firm may, if desired, substitute on the second line of the legend, in lieu of his own name, the

name of the person or firm for whom the exportation is made. In case of such substitution the first two lines of the legend should be separated from the matter below by a conspicuous black horizontal line.

H. F. MIRES,

Acting Commissioner of Internal Revenue.

Approved October 30, 1929.

A. W. MELLON,

Secretary of the Treasury.

OLEOMARGARINE.

REGULATIONS 9(1923), ARTICLE 40: Substances,
etc., taxable as oleomargarine, etc.

VIII-37-4359

Ct. D. 111

OLEOMARGARINE TAX—ACT OF AUGUST 2, 1886, AS AMENDED—DECISION OF COURT.

OLEOMARGARINE—VEGETABLE OIL—NO ANIMAL FATS.

A compound, designated "Rich Nut Shortening," consisting of vegetable oils, artificial coloring matter, and other ingredients, excluding animal fats, not only "made in imitation or semblance of butter" but "calculated or intended to be sold as butter or for butter," is oleomargarine, and properly taxable as such under the Act of August 2, 1886, as amended.

DISTRICT COURT OF THE UNITED STATES FOR THE WESTERN DIVISION OF THE
WESTERN DISTRICT OF MISSOURI.

The Harrow-Taylor Butter Co., a Missouri Corporation, plaintiff, v. Noah Crooks, United States Collector of Internal Revenue for the Sixth District of Missouri, defendant.

[August 5, 1929.]

OPINION.

REEVES, District Judge: This is an action at law to recover certain taxes which, it is alleged, were paid under protest. A jury was waived by stipulation of the parties and the cause tried to the court.

Said tax was collected under an Act approved August 2, 1886. That Act, with subsequent amendments, imposes a stipulated tax upon manufactured substances classed as oleomargarine. In defining what substances should be so classed, the following pertinent definitions were given in the Act:

"All mixtures and compounds of tallow, beef-fat, suet, lard, lard-oil, *vegetable-oil annatto*, and other coloring matter," etc.

It was further provided by said Act that all substances falling within the above definition should be taxable if "made in imitation or semblance of butter, or when so made, calculated or intended to be sold as butter or for butter."

The plaintiff has a product which it designates "Rich Nut Shortening." Admittedly it contains no animal fat but is wholly composed of mixtures or compounds of vegetable oils, salt, benzoate of soda, water, and artificial coloring matter.

The Commissioner of Internal Revenue determined that such manufactured substance should be classed as oleomargarine and moreover that it was made in imitation or semblance of butter and that it became taxable under said Act.

The plaintiff makes the manifold contention (a) that such substance is not within the purview of the Act; (b) that, if so, said act is unconstitutional; (c) that the questions here involved have been previously adjudicated; and (d) that the evidence shows that such substance was neither made in imitation or semblance of butter nor was it calculated or intended to be sold as butter or for butter.

1. Adverting to the first proposition, that said substance is not within the purview of the Act, it is to be noted that the Act contains the language—
 "All mixtures and compounds of * * * vegetable-oil annotto, and other coloring matter," etc.

Plaintiff says that vegetable-oil was not employed at the date of the enactment in the manufacture of substances such as the substance in question. However, it is insisted that the words vegetable-oil were used to describe the word annotto and that said substance was a mere coloring matter. In other words, it is the contention of the plaintiff that only mixtures and compounds containing animal fat were defined and classed as oleomargarine.

The defendant, on its part, says that the words vegetable-oil should have been followed by a comma so as to separate said words from the word "annotto" following.

The plaintiff has presented for the inspection of the court original and authentic records of the Act as same was passed and signed by the presiding officers of the House of Representatives and the Senate of the United States. Such record fails to disclose a comma between the words "vegetable-oil" and the word "annotto." Plaintiff offered testimony that a substance known as vegetable-oil annotto as a coloring matter was actually in use at the time of the enactment of said law. On this question, however, there was opposing evidence.

The court is called upon in the first instance to interpret the meaning of said section and to determine whether or not it should be construed as if a comma were in fact inserted. The original records of the bill do not particularly aid in such interpretation. Such records do prove conclusively the enactment of the law.

It is well settled "that punctuation is a fallable standard of the meaning of a statute, and the last resort as an aid in its interpretation, though it may be resorted to as such aid when the meaning of the statute is doubtful." (25 R. C. L., 965, section 220; *Northern Pacific Railway Co. v. United States*, 227 U. S., 355, 1 c. 360; 36 Cyc., 1117; Words and Phrases judicially defined.)

Contrary to the evidence offered by plaintiff, the defendant proved that vegetable-oil was not only known but used in the manufacture of similar substance at the time of the enactment of said law. Moreover, the evidence was not satisfactory that such a substance as "vegetable-oil annotto" was ever used extensively for coloring matter.

There was evidence that the printed bill taken from congressional files showed that a comma was inserted after the word vegetable-oil. Moreover, no reason seemed to exist for designating any single coloring matter as "vegetable-oil annotto." Annotto, according to the evidence, was a coloring matter wholly independent of vegetable-oil.

In the case of *Higgins Mfg. Co. v. Page* (297 Fed., 644, 1 c., 651 [T. D. 3590, C. B. III-1, 507]), Judge Brown, of the district of Rhode Island, granted a request for findings of law as follows:

"That the phrase 'vegetable-oil annotto, and other coloring matter' contained in section 2 of the Act of August 2, 1886 (24 Stats., 209), should be read as though there were a comma after the word 'oil.'"

Apparently Judge Brown was of the opinion that the Act should be interpreted as if the comma had been inserted. The decision of Judge Brown did not rest on this point, however, but was based upon his view that the product there under inquiry was "not made in imitation or semblance of butter or when so made calculated or intended to be sold as butter or for butter."

With respect to the substance there under inquiry, the Commissioner of Internal Revenue had previously ruled that it was not made in imitation or semblance of butter. The court simply followed the ruling of the Commissioner. Said opinion must be considered, however, as holding that there was such a mixture or compound as could be made up of vegetable-oil and other ingredients excluding animal fats and that in a proper case such substances might be classed for the purposes of taxation as oleomargarine.

A reasonable interpretation of said statute would require the insertion of the comma after the word oil and before the word annotto.

2. There is nothing in the language of the Act as contended by the plaintiff to indicate a purpose on the part of Congress to regulate rather than tax. The Act itself is a pure Revenue Act and has no regulatory features, unless it be in the language that exempts from the tax if not made in imitation and semblance of butter. The right and power of Congress to impose such a tax, even though burdensome, can not be questioned.

3. There has been no adjudication of the questions here involved. Rulings have been promulgated from time to time by the Commissioner of Internal Revenue and such rulings have had the force of law. However, in no case has such a ruling been made and promulgated by the Commissioner of Internal Revenue that might become applicable to the facts here presented. In each ruling certain conditions were named. Such conditions are not present in the instant case. It can not be said that the Commissioner had previously ruled favorably to the plaintiff with respect to the product under inquiry for the reason that the plaintiff did not submit to the Commissioner its product as sold to the public. The samples submitted were without coloring matter.

4. There remains the final inquiry as to whether plaintiff's product is "made in imitation or semblance of butter or when so made calculated or intended to be sold as butter or for butter."

With commendable frankness plaintiff offered testimony as to the nature and character of its product and the demand of the public therefore. Plaintiff did not by its advertisements, nor by its containers or printed matter, offer its product as butter or a substitute for butter, yet the evidence was overwhelming that retail merchants, restaurant keepers, and others carried and used plaintiff's product "as butter and for butter."

Retail merchants kept said product with their butter and recognized oleo-margarine substances and proffered same to their customers as a suitable substitute for butter. Restaurant keepers regularly served said product as butter and for butter.

The evidence was overwhelming that said substance not only looked like butter but that it had the taste of butter. It was put up in cartons similar in size and shape as butter. It was not used except very moderately for "shortening," as indicated on plaintiff's cartons. Plaintiff acknowledged that sharp competition had forced the use of this substance. Such competition was for butter substitutes. Plaintiff undoubtedly knew that the demand for its product was not alone for "shortening" in baking, but as butter substitute.

It would be idle to say that the plaintiff did not know that its customers, the retail dealers, were selling said substance as a butter substitute. Said substance was not only "made in imitation or semblance of butter" but it was "calculated" and "intended to be sold as butter or for butter."

In view of the foregoing, the judgment of the court will be for the defendant.

MISCELLANEOUS RULINGS.

OLEOMARGARINE.

VIII-28-4272
MS. 92

Schedule of oleomargarine produced and materials used during the month of May, 1929, as compared with May, 1928.

	May, 1929.	May, 1928.
	<i>Pounds.</i>	<i>Pounds.</i>
Total production of uncolored oleomargarine	26,954,237	22,441,087
Ingredient schedule for uncolored oleomargarine:		
Butter.....	239,103	321,228
Cocconut oil.....	14,163,306	11,165,044
Cottonseed oil.....	2,360,665	1,918,360
Edible tallow.....	1,950	7,763
Milk.....	7,066,230	6,881,586
Mustard oil.....	1,070	4,040
Neutral lard.....	1,754,968	1,878,322
Oleo oil.....	3,916,270	3,229,023
Oleo stearine.....	560,469	436,923
Oleo stock.....	122,302	131,592
Palm oil.....	93,971	68,805
Palm-kernel oil.....		1,298
Peanut oil.....	445,434	372,257
Salt.....	2,258,845	1,887,414
Sesame oil.....		3,975
Soda.....	9,129	7,844
Vanilla extract.....		19
Total	32,993,712	28,305,491
Total production of colored oleomargarine	1,402,273	1,303,383
Ingredient schedule for colored oleomargarine:		
Butter.....	1,168	115
Cocconut oil.....	440,045	457,886
Color.....	1,610	1,656
Cottonseed oil.....	157,502	216,415
Milk.....	447,903	573,047
Neutral lard.....	172,929	249,242
Oleo oil.....	369,247	441,248
Oleo stearine.....	14,518	16,758
Oleo stock.....	16,205	10,265
Palm oil.....	37,341	21,803
Peanut oil.....	20,118	23,259
Salt.....	111,745	130,960
Soda.....	166	168
Total	1,790,497	2,142,822

VIII-31-4294
MS. 93*Schedule of oleomargarine produced and materials used during the month of June, 1929, as compared with June, 1928.*

	June, 1929.	June, 1928.
	<i>Pounds.</i>	<i>Pounds.</i>
Total production of uncolored oleomargarine.....	23,064,734	22,499,418
Ingredient schedule for uncolored oleomargarine:		
Butter.....	192,775	186,770
Cocoanut oil.....	11,674,104	11,345,862
Cottonseed oil.....	1,993,477	1,899,977
Edible tallow.....	1,600	6,297
Milk.....	6,118,116	6,466,680
Mustard oil.....	630	3,520
Neutral lard.....	1,462,912	1,889,108
Oleo oil.....	3,437,207	3,162,067
Oleo stearine.....	505,734	429,081
Oleo stock.....	70,518	119,229
Palm oil.....	75,742	59,431
Palm-kernel oil.....		3,993
Peanut oil.....	366,636	360,306
Salt.....	1,870,503	1,887,607
Soda.....	7,403	7,566
Vanilla extract.....		18
Total.....	27,717,357	27,771,512
Total production of colored oleomargarine.....	1,210,847	1,238,414
Ingredient schedule for colored oleomargarine:		
Butter.....	2,236	224
Cocoanut oil.....	354,616	445,283
Color.....	1,679	1,428
Cottonseed oil.....	130,430	205,967
Milk.....	368,491	567,665
Neutral lard.....	153,111	240,280
Oleo oil.....	335,979	427,128
Oleo stearine.....	18,398	16,452
Oleo stock.....	18,650	11,098
Palm oil.....	17,999	22,400
Peanut oil.....	15,802	19,895
Salt.....	98,150	124,200
Soda.....	137	223
Total.....	1,515,678	2,082,243

VIII-37-4351
MS. 94*Schedule of oleomargarine produced and materials used during the month of
July, 1929, as compared with July, 1928.*

	July, 1929.	July, 1928.
	Pounds.	Pounds.
Total production of uncolored oleomargarine.....	23,644,494	20,434,798
Ingredient schedule for uncolored oleomargarine:		
Butter.....	184,277	156,862
Cocconut oil.....	12,344,054	10,299,075
Cottonseed oil.....	1,940,982	1,705,358
Edible tallow.....	1,600	1,900
Egg yolks (fresh).....	640	
Milk.....	6,671,843	6,192,382
Mustard oil.....	810	1,435
Neutral lard.....	1,496,197	1,557,187
Oleo oil.....	3,257,460	2,918,306
Oleo stearine.....	453,446	444,186
Oleo stock.....	71,346	112,555
Palm oil.....	86,238	58,315
Palm-kernel oil.....		2,104
Peanut oil.....	372,996	429,438
Salt.....	1,954,277	1,686,380
Soda.....	8,892	7,070
Vanilla extract.....		18
Total.....	28,845,058	25,572,571
Total production of colored oleomargarine.....	1,228,507	1,009,135
Ingredient schedule for colored oleomargarine:		
Butter.....	180	124
Cocconut oil.....	314,191	343,413
Color.....	1,651	1,307
Cottonseed oil.....	110,476	161,523
Milk.....	373,125	459,355
Neutral lard.....	166,260	198,020
Oleo oil.....	376,529	367,885
Oleo stearine.....	13,075	11,360
Oleo stock.....	22,045	15,438
Palm oil.....	27,860	16,217
Peanut oil.....	15,681	19,720
Salt.....	96,714	99,997
Soda.....	167	107
Total.....	1,517,954	1,695,371

VIII-41-4385

MS. 95

Schedule of oleomargarine produced and materials used during the month of August, 1929, as compared with August, 1928.

	August, 1929.	August, 1928.
	Pounds. 27, 006, 714	Pounds. 22, 436, 765
Total production of uncolored oleomargarine.....		
Ingredient schedule for uncolored oleomargarine:		
Butter.....	225, 482	173, 730
Cocoanut oil.....	14, 269, 639	11, 474, 250
Cottonseed oil.....	2, 255, 770	1, 887, 910
Edible tallow.....	1, 000	2, 235
Egg yolks.....	660	
Milk.....	7, 738, 652	6, 483, 955
Mustard oil.....	1, 535	1, 265
Neutral lard.....	1, 548, 604	1, 595, 056
Oleo oil.....	3, 548, 849	3, 167, 019
Oleo stearine.....	582, 389	424, 599
Oleo stock.....	76, 735	101, 778
Palm oil.....	95, 028	62, 716
Palm-kernel oil.....		1, 711
Peanut oil.....	405, 116	416, 394
Salt.....	2, 207, 793	1, 895, 059
Soda.....	16, 440	10, 465
Soya-bean oil.....	32	
Vanilla.....		18
Total.....	32, 973, 504	27, 698, 160
Total production of colored oleomargarine.....	1, 393, 343	1, 173, 484
Ingredient schedule for colored oleomargarine:		
Butter.....	3, 439	210
Cocoanut oil.....	445, 510	435, 633
Color.....	1, 662	1, 303
Cottonseed oil.....	131, 063	173, 708
Edible tallow.....	420	
Milk.....	404, 981	530, 326
Neutral lard.....	167, 062	224, 791
Oleo oil.....	373, 868	417, 310
Oleo stearine.....	13, 055	12, 030
Oleo stock.....	18, 284	13, 605
Palm oil.....	35, 883	22, 546
Palm-kernel oil.....		339
Peanut oil.....	17, 053	23, 538
Salt.....	109, 205	115, 567
Soda.....	156	194
Total.....	1, 721, 641	1, 971, 300

VIII-45-4422
MS. 96

Schedule of oleomargarine produced and materials used during the month of September, 1929, as compared with September, 1928.

	September, 1929.	September, 1928.
	<i>Pounds.</i>	<i>Pounds.</i>
Total production of uncolored oleomargarine.....	28, 978, 926	27, 210, 628
Ingredient schedule for uncolored oleomargarine:		
Butter.....	254, 309	218, 948
Cocoanut oil.....	15, 521, 114	14, 028, 353
Cottonseed oil.....	2, 203, 264	2, 240, 064
Edible tallow.....	1, 735	3, 170
Egg yolks.....	540	
Milk.....	8, 388, 563	7, 999, 276
Mustard oil.....	4, 225	1, 070
Neutral lard.....	1, 574, 343	1, 926, 979
Oleo oil.....	3, 769, 055	3, 890, 377
Oleo stearine.....	512, 092	498, 348
Oleo stock.....	100, 781	122, 594
Palm oil.....	94, 341	70, 329
Palm-kernel oil.....		1, 056
Peanut oil.....	565, 632	495, 260
Salt.....	2, 337, 537	2, 262, 331
Soda.....	10, 280	9, 439
Soyabean oil.....	36	
Vanilla extract.....		24
Total.....	35, 337, 847	33, 768, 218
Total production of colored oleomargarine.....	1, 582, 667	1, 235, 061
Ingredient schedule for colored oleomargarine:		
Butter.....	5, 670	378
Cocoanut oil.....	554, 005	424, 020
Color.....	1, 958	1, 536
Cottonseed oil.....	158, 097	195, 951
Milk.....	435, 981	530, 419
Neutral lard.....	176, 740	218, 740
Oleo oil.....	413, 188	445, 516
Oleo stearine.....	13, 571	16, 585
Oleo stock.....	11, 365	13, 800
Palm oil.....	6, 400	4, 450
Peanut oil.....	20, 128	22, 120
Salt.....	121, 312	116, 590
Soda.....	205	116
Total.....	1, 919, 470	1, 990, 221

VIII-50-4466
MS. 97

Schedule of oleomargarine produced and materials used during the month of October, 1929, as compared with October, 1928.

	October, 1929.	October, 1928.
	<i>Pounds.</i>	<i>Pounds.</i>
Total production of uncolored oleomargarine.....	34, 751, 964	29, 181, 242
Ingredient schedule for uncolored oleomargarine:		
Butter.....	295, 321	225, 986
Cocoanut oil.....	18, 802, 207	15, 177, 219
Cottonseed oil.....	2, 834, 965	2, 436, 933
Edible tallow.....	1, 870	2, 905
Egg yolk.....	400	
Milk.....	9, 805, 039	8, 515, 204
Mustard oil.....	6, 987	935
Neutral oil.....	1, 873, 094	2, 032, 119
Oleo oil.....	4, 214, 873	3, 877, 869
Oleo stearine.....	621, 292	523, 535
Oleo stock.....	96, 045	108, 247
Palm oil.....	116, 279	88, 896
Palm-kernel oil.....		6, 300
Peanut oil.....	555, 391	589, 428
Salt.....	2, 829, 496	2, 351, 689
Soda.....	9, 466	8, 374
Total.....	42, 062, 725	35, 945, 639
Total production of colored oleomargarine.....	1, 872, 294	1, 449, 975
Ingredient schedule for colored oleomargarine:		
Butter.....	5, 240	2, 851
Cocoanut oil.....	708, 343	537, 602
Color.....	2, 007	1, 768
Cottonseed oil.....	186, 963	241, 414
Milk.....	515, 891	685, 808
Neutral lard.....	201, 706	259, 838
Oleo oil.....	469, 533	485, 896
Oleo stearine.....	10, 425	16, 885
Oleo stock.....	6, 748	6, 820
Palm oil.....	9, 100	24, 630
Peanut oil.....	33, 714	31, 291
Salt.....	149, 431	139, 817
Soda.....	161	123
Total.....	2, 299, 262	2, 384, 143

MISCELLANEOUS.

VIII-26-4254

[H. J. RES. 82, PUBLIC, NO. 7, SEVENTY-FIRST CONGRESS.]

Joint resolution making appropriations for additional compensation for transportation of the mail by railroad routes in accordance with the increased rates fixed by the Interstate Commerce Commission.

Resolved by the Senate and the House of Representatives of the United States of America in Congress assembled, That to enable the Postmaster General to provide for the additional compensation due various railroad companies for inland transportation of mails in accordance with the increased rates fixed by the Interstate Commerce Commission in case 9200, under orders dated December 8,

1925; January 5 and March 2, 1927; July 10, 1928; and February 9, 1929, the same being retroactive, the following sums are appropriated, out of any money in the Treasury not otherwise appropriated:

For the inland transportation of mails by railroad routes for the fiscal years 1924 to 1929, inclusive, \$39,000,000; and in addition to such sum there is hereby made available so much as may be necessary of the unexpended balances of the appropriations for inland transportation of mails by railroad routes for the fiscal years 1927 and 1928.

For payment of the judgments rendered by the Court of Claims and reported to the Seventy-first Congress in House Document No. 18, as follows: Under the Post Office Department, exclusive of interest as and where specified in any of such judgments, \$3,997,089.50

Provided, That any sums paid to a railroad company from the amounts made available by this joint resolution shall be considered for income-tax purposes as income for the taxable year in which such payment is actually received by such company: *Provided further*, That no part of the appropriations made available by this joint resolution shall be paid to any such company which does not waive all interest and claims for interest upon the principal amounts found to be due such company.

Approved June 6, 1929.

VIII-32-4307

AUGUST 1, 1929.

Changes in Bureau Personnel.

Collectors of Internal Revenue, Internal Revenue Agents in Charge, Officials and Employees of the Bureau of Internal Revenue, and Others Concerned:

Effective as of August 1, 1929, Mr. David Burnet has been appointed Deputy Commissioner in charge of the Income Tax Unit.

Effective as of August 1, 1929, Mr. George J. Schoeneman has been appointed Deputy Commissioner in charge of the Accounts and Collections Unit.

H. F. MIREs,
Acting Commissioner.

VIII-32-4308

T. D. 4270

Record of daily collections and deposits.—Regulations 2 amended.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, D. C.

To Collectors of Internal Revenue:

Record 9, a loose-leaf sheet 17 by 13 inches in size and designed for use by division chiefs and stamp deputy collectors in charge of branch offices of collectors of internal revenue in making a daily

record of collections and deposits on account of internal revenue taxes collected and deposited direct by such officers, referred to in articles 4 and 10, Regulations No. 2, is hereby abolished. This record is no longer essential to the proper functioning of the system of accounting for internal revenue collections now in use in collectors' offices.

Regulations No. 2 are amended accordingly.

H. F. MIREs,

Acting Commissioner of Internal Revenue.

Approved August 3, 1929.

HENRY HERRICK BOND,

Acting Secretary of the Treasury.

VIII-35-4330

AUGUST 22, 1929.

Change in Bureau personnel.

Collectors of Internal Revenue, Internal Revenue Agents in Charge, Officials and Employees of the Bureau of Internal Revenue, and Others Concerned:

Effective as of August 16, 1929, Mr. Victor H. Self has been appointed Assistant Deputy Commissioner of the Accounts and Collections Unit.

ROBT. H. LUCAS, *Commissioner.*

VIII-43-4409

Mim. 3761

Symbols for use in correspondence.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, D. C., October 18, 1929.

Collectors of Internal Revenue, Internal Revenue Agents in Charge, Deputy Commissioners, and Other Officers and Employees concerned:

The following directions supersede those contained in Commissioner's Mimeograph, * * * Collectors' No. 3633 [C. B. VII-1, 361] * * * and all other instructions in conflict therewith. Also section 66, Part I, of the Internal Revenue Manual is amended to conform to the following:

Every letter prepared in the Bureau in Washington will bear in the upper left-hand corner of the first page, and immediately below the instructions "Address reply to," etc., a symbol that will indicate the office of origin: *Provided*, That this practice will not apply to congressional correspondence, nor to letters prepared for signature by other than officials of this Bureau.

Every letter addressed to the Bureau by a field office, if it be in reply to a communication from the Bureau, will bear, immediately above the body of the letter and near the center of the sheet, the symbol that appears in the communication that is being answered;

thus: "Attention: IT:AR:B3:STK." If the letter be not in reply to a Bureau communication, the symbol of the unit, division, or section in the Bureau concerned will be indicated in the same manner, provided there is no question as to the proper symbol; *if any doubt exists, no symbol whatever will be used.*

Where a field office uses a system of symbols in conducting its correspondence, the symbol used in this connection will be placed in the upper left-hand corner of the first sheet of each letter addressed to the Bureau just below the instructions "In reply refer to." The Bureau letter, if any, replying to such communication will show the field office symbol above the body of the letter in the same manner as is prescribed in the next preceding paragraph.

Envelopes with printed or typewritten address will be used by field offices in transmitting mail to the Bureau, rather than window envelopes. Also, every such envelope or wrapper will bear, in the lower left-hand corner of the face thereof, the same symbol that is quoted in the communication which it incloses. There is no objection to forwarding in one envelope a number of communications intended for the same unit or division of the Bureau; in fact this is desirable. Under no circumstances, however, should correspondence pertaining to the work of one unit be inclosed in an envelope addressed to another unit.

Information which will assist the field officer to determine the destination of correspondence that is not in reply to Bureau letters may be obtained by directing an inquiry to the Administrative Division, Communication Section.

Only one subject will be treated in any one letter.

The following represents the organization and symbols used:

OFFICE OF THE COMMISSIONER.

Ad—Administrative Division.
 Ad-C—Communication Section.
 Ad-PB—Printing and Binding Section.
 Ad-SL—Space and Lease Section.
 Ad-SE—Supplies and Equipment Section.
 AP—Appointment Division.
 SA—Special Advisory Committee.
 SD—Special Deputy Commissioner.

ACCOUNTS AND COLLECTIONS UNIT.

A&C:DC—Deputy Commissioner.
 A&C:D—Disbursement Accounting Division.
 A&C:Col—Collection Accounting Division.
 A&C:PES—Personnel, Equipment, and Space Division.

OFFICE OF THE GENERAL COUNSEL.

GC:I—Interpretative Division.
 GC:P—Penal Division.
 GC:Ap—Appeals Division.
 GC:R—Review Division.
 GC:C—Civil Division.
 GC:CC—Compromise Section.
 GC:Adm—Administrative Division.
 Mail and Record Section.
 Library and Manuscript Section.

INCOME TAX UNIT.

IT: E—Deputy Commissioner.
 Assistant Deputy Commissioner.
 IT: E: P—Personnel Section.
 IT: E: RR—Rules and Regulations Section.
 IT: E: Sr—Service Section.
 IT: E: Aj—Special Adjustment Section.
 IT: E: F—Field Procedure Division.

AUDIT REVIEW DIVISION.

IT: AR—Head of Division.
 IT: AR: B—Section B.
 IT: AR: C—Section C.
 IT: AR: D—Section D.
 IT: AR: G—Section G.
 IT: AR: RR—Railroad Section.
 IT: AR: En—Engineering Section.

CLEARING DIVISION.

IT: C—Head of Division.
 IT: C: CC—Claims Control Section.
 IT: C: PrA—Preliminary Audit Section.
 IT: C: P—Proving Section.
 IT: C: St—Statistical Section.

RECORDS DIVISION.

IT: R—Head of Division.
 IT: R: F—Files Section.
 IT: R: S—Sorting Section.

INTELLIGENCE UNIT.

SI—Chief, Intelligence Unit.

MISCELLANEOUS TAX UNIT.

MT: DC—Deputy Commissioner.
 MT: ET—Estate Tax Division.
 MT: ET: GT—Gift Tax Section.
 MT: M—Miscellaneous Division.
 MT: T—Tobacco Division.

ROBT. H. LUCAS, *Commissioner.*

VIII-49-4458
 Mim. 3769

Bureau training division created.

TREASURY DEPARTMENT,
 OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, D. C., November 29, 1929.

*Collectors of Internal Revenue, Internal Revenue Agents in Charge,
 and Other Officials and Employees of the Bureau Concerned:*

Effective at the close of business November 30, 1929, the training section, Office of the Commissioner of Internal Revenue, is abolished as such.

Effective December 1, 1929, there is created in the Office of the Commissioner of Internal Revenue, a training division, under the immediate supervision of Special Deputy Commissioner Pressly R. Baldrige. Mr. William M. Vastine, now chief of the training section, is transferred to and designated head of the training division.

The new training division will take over all duties formerly performed by the training section, together with such additional educational work as may be assigned to it by the Commissioner. All employees of the training section, together with all files, furniture, etc., now utilized by that section, are, effective December 1, 1929, transferred to the training division.

Collectors of internal revenue, internal revenue agents in charge, and others concerned will hereafter address all communications with reference to correspondence study course and other educational and training matters to "Commissioner of Internal Revenue, Training Division, Washington, D. C."

Correspondence in regard to the procedure outlined herein should refer to the number of this mimeograph and to the symbol SD.

ROBT. H. LUCAS, *Commissioner*.

VIII-49-4459
Mim. 3770

Furnishing addresses of attorneys or agents named in powers of attorney.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, D. C., November 30, 1929.

*Collectors of Internal Revenue, Internal Revenue Agents in Charge,
and Other Officials and Employees of the Bureau Concerned:*

In order that a more accurate record may be maintained of the addresses of agents and attorneys who are authorized to represent taxpayers before the Bureau of Internal Revenue, it is requested, whenever possible, that the addresses of the representatives named in powers of attorney filed in your office and subsequently forwarded to the Bureau under the provisions of Mimeograph 3730 [C. B. VIII-1, 333], be either placed on the power of attorney or stated in the letters of transmittal.

Queries regarding this order should be marked for the attention of IT:E:DB.

ROBT. H. LUCAS, *Commissioner*.

Disbarments and suspensions from practice before Treasury Department of attorneys and agents.²

DISBARMENTS.

The Secretary of the Treasury, after due notice and opportunity for hearing, has ordered the disbarment from further practice before the Treasury Department of the following-named attorneys and agents:

Name.	Address.	Date of disbarment.	Cause.
Abbott, Leslie.....	New York, N. Y..	Nov. 25, 1929	Charged with failure to pay the Federal income taxes assessed against respondent for the years 1920, 1923, 1925, and 1926. Charges found proven.
Cleveland, Thomas J..	Oklahoma City, Okla.	Sept. 19, 1928	Charged with misappropriation of funds of his employer, obtaining money by false pretenses, and drunkenness. Charges found proven.
Cordin, Cephas W....	Formerly Sawtelle, Calif., now Los Angeles, Calif.	Sept. 19, 1928	Charged with having been disbarred from practice before the Interior Department for disreputable conduct. Charges found proven.
Drabble, R. King....	Newark, N. J.....	Mar. 21, 1929	Charged with being interested in and profiting by a fraud perpetrated upon a taxpayer client by a partner of said respondent. Charges found proven.
Frost, Charles.....	New York, N. Y..	July 2, 1928	Charged with having been accused and convicted of the crime of arson in the State of Connecticut and sentenced to serve a term of from one to three years in jail. Charges found proven.
Gibson, Wm. Patrick.	New York, N. Y..	Jan. 12, 1929	Charged with soliciting employment from taxpayers with whom he had no previous contact, and with preparing false return for a taxpayer, receiving and keeping fees for such work, which was abandoned by taxpayer, who employed another practitioner to prepare a correct return. Charges found proven.
Kaderly, May E....	Chattanooga, Tenn.	Aug. 30, 1928	Charged with preparing and filing false income-tax returns. Charges found proven.
Kalbach, H. Earl....	Reading, Pa.....	Oct. 10, 1929	Charged with misappropriating \$1,000 of partnership funds and with making false representation to his partners that such \$1,000 had been paid to Government officials. Charges found proven.
Lindsay, Brent A....	Los Angeles, Calif.	Apr. 26, 1929	Charged with having presented false and misleading evidence in a tax case. Charges found proven.
McGrath, James J....	Formerly Savannah, Ga., now Easthampton, Mass.	Oct. 10, 1929	Charged with having obtained \$500 from client in tax case upon false representation that such \$500 was to be paid to Government official. Charges found proven.
McNamara, Charles L.	Chicago, Ill.....	Dec. 21, 1928	Charged with writing threatening letters to a client in a tax case, demanding an extortionate fee, and falsely stating in such letters that a representative of the Government had to be paid out of such fee, and that such taxpayer would go to jail if such fee were not paid. Charges found proven.
Meakim, John F....	Formerly Newark, N. J., now Linden, N. J.	Oct. 16, 1929	Charged with having been convicted on an indictment for bribery. Charges found proven.

¹ This ruling (4487) includes also rulings Nos. 4256, 4264, 4273, 4280, 4288, 4296, 4303, 4313, 4320, 4331, 4344, 4352, 4363, 4372, 4378, 4386, 4396, 4407, 4415, 4423, 4429, 4436, 4443, 4457, 4467, and 4477. These rulings have been thus consolidated because publication of each one separately would be largely duplication.

² This list includes all attorneys and agents disbarred from practice during the 12-month period January 1-December 31, 1929, inclusive, and all suspensions in effect during the 6-month period July 1-December 31, 1929, inclusive. It does not include those barred from practice by reason of disapproval of their application for enrollment.

Name.	Address.	Date of disbarment.	Cause.
Neu, Edmund H.	Kansas City, Mo.	Apr. 26, 1929	Charged with writing and mailing an anonymous letter to an officer of the Internal Revenue Service which contained false statements that certain taxpayers had failed to make proper returns of their income taxes, thereby causing useless examination of records of such taxpayers; also charged with soliciting employment in Federal tax matters from persons with whom he had no previous contact. Charges found proven.
Overmyer, Charles G.	Wichita, Kans.	Apr. 13, 1929	Charged with preparing and filing false Federal income tax returns for taxpayers. Charges found proven.
Showen, Frank G.	Formerly Kansas City, Mo., now Ottawa, Kans.	July 2, 1928	Charged with having been convicted in the United States District Court for the Western Division of the Western District of Missouri for the violation of section 145, United States Criminal Code, and sentenced to a term of 10 months in jail. Charges found proven.
Stern, Isador.	Newark, N. J.	Apr. 26, 1929	Charged with having been indicted for embezzlement of funds of a client and convicted and sentenced to serve a term in prison on such conviction. Charges found proven.
Sullivan, F. J.	Formerly Wilmington, N. C., now Sumter, S. C.	Apr. 29, 1929	Charged with preparing false income tax returns for a client, and mailing letters soliciting employment in tax matters to taxpayers with whom respondent had no previous contact. Charges found proven.
Swanwick, John T.	Toledo, Ohio.	Sept. 18, 1929	Charged with making false income tax returns in his own tax matters. Charges found proven.
Walton, E. M.	Detroit, Mich.	Apr. 26, 1929	Charged with misappropriation of clients' money in tax cases. Charges found proven.
Watts, Charles J.	Milwaukee, Wis.	Aug. 4, 1928	Charged with making false income tax returns for taxpayers; also charged with making false and misleading statements of facts in briefs filed with the Bureau of Internal Revenue in tax cases; also charged with advising the taxpayer to make a false income tax return, who followed such advice and filed a false income tax return. Charges found proven by the committee.

SUSPENSIONS.

The Secretary of the Treasury, after due notice and opportunity for hearing, has ordered the suspension from practice before the Treasury Department for the period stated in each case of the following-named attorneys and agents:

Name.	Address.	Period of suspension.	Cause.
Cathrae, William Morrison.	Eustis, Fla.	1 year, from Oct. 4, 1929.	Charged with making false income tax returns for taxpayers. Charges found proven.
Berenter, Philip H.	Washington, D. C.	6 months, from Mar. 21, 1929.	Charged with addressing and mailing letters soliciting employment in tax matters to taxpayers with whom respondent had no previous contact. Charges found proven.
Maguire, John B.	Shreveport, La.	6 months, from Mar. 11, 1929.	Charged with making false income tax returns for a taxpayer; also with making false statements of facts in a brief of protest in a tax case. Charges found proven.
Mease, H. Warren.	Philadelphia, Pa.	90 days, from June 22, 1929.	Charged with failure to produce books of taxpayer when requested by revenue agent, and with obstructing the administration of the Revenue Acts by Internal Revenue Bureau. Charges found proven.
Winston, Gus V.	Wichita, Kans.	6 months, from Nov. 25, 1929.	Charged with failure to return balance of money received from client after paying client's income taxes. Charges found proven.

Resignations from enrollment to practice before the Treasury Department.

The following-named persons have tendered their resignations from enrollment to practice before the Treasury Department. The Secretary of the Treasury has accepted the resignations and ordered their names stricken from the roll of attorneys and agents enrolled to practice before the Treasury Department. They are therefore no longer entitled to practice before the Treasury Department.

Name.	Address.	Designation.	Date of acceptance.	Remarks.
Frey, Oscar H.	Daytona Beach, Fla.	Agent.	Dec. 12, 1929	Without prejudice.
Higgins, W. Stock- ton.	New York, N. Y.	do.....	June 20, 1929	
Zimmerman, James Roy.	Dallas, Tex.	do.....	Sept. 6, 1929	

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