1 T.C. 286 (1942)

A corporation’s contributions to a pension trust benefiting its employees, including its controlling shareholder, are deductible as ordinary and necessary business expenses if the total compensation, including the pension contribution, is reasonable and the trust meets the requirements of Section 165 of the Revenue Act.

Summary

Phillips H. Lord, Inc. created a pension trust for its employees, including Phillips H. Lord, the company’s president, treasurer, and sole shareholder. The company contributed $14,769 to the trust, which the trustees used to purchase annuity contracts. The Commissioner argued that the portion of the contribution benefiting Lord was not deductible because the trust was primarily for his benefit, not for the exclusive benefit of the employees. The Tax Court held that the entire contribution was deductible because Lord was also an employee, his total compensation was reasonable, and the trust met the requirements of Section 165 of the Revenue Act of 1936.

Facts

Phillips H. Lord was the president, treasurer, and sole shareholder of Phillips H. Lord, Inc., a company that produced radio programs. In 1937, the corporation established a pension trust for all permanent employees. The trust agreement stipulated that the corporation would contribute 15% of each employee’s annual salary to the trust. These funds were used to purchase retirement annuity contracts from an insurance company that would mature when the employee reached 65. In 1937, the corporation contributed $14,769 to the trust, including $9,750 for an annuity contract for Phillips H. Lord himself. The corporation deducted the full amount of the contribution on its tax return.

Procedural History

The Commissioner of Internal Revenue disallowed the deduction for the $14,769 contribution, arguing it was not deductible under any provision of the Revenue Act of 1936. The Commissioner asserted that because Lord was the president, treasurer, sole director, and shareholder, and was also a beneficiary of the trust, it was not created for the exclusive benefit of the corporation’s employees within the meaning of Section 165. The Tax Court consolidated the cases of Phillips H. Lord (regarding his personal income tax liability) and Phillips H. Lord, Inc. and both were before the court.

Issue(s)

1. Whether Phillips H. Lord, Inc. was entitled to deduct the $14,769 paid to the pension trust in 1937.
2. Whether the $14,769 should be included in the undistributed adjusted net income

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of Phillips H. Lord, Inc., for computing its personal holding company surtax liability.
3. Whether Phillips H. Lord was taxable on the $9,750 used to purchase his annuity contract.

Holding

1. Yes, because the contribution was an ordinary and necessary business expense, Lord's total compensation was reasonable, and the trust met the requirements of Section 165 of the Revenue Act of 1936.
2. No, because the $14,769 was a legal deduction from the corporation's gross income.
3. No, because the amount was not distributed to Lord or made available to him in 1937.

Court's Reasoning

The court reasoned that Phillips H. Lord, Inc., was a separate taxable entity from Phillips H. Lord. Lord was an employee of the corporation and received a salary. The court found that the $9,750 paid for Lord's annuity contract, when added to his salary, constituted reasonable compensation for his services. Section 23(a) of the Revenue Act of 1936 allowed a deduction for ordinary and necessary business expenses, including reasonable compensation for personal services. The court distinguished this case from *W.F. Parker, 38 B.T.A. 989*, where the trust was primarily for the benefit of the controlling stockholder. Here, Lord was compensated on the same basis as other permanent employees. The court also cited *Raymond J. Moore, 45 B.T.A. 1073*, which held that a pension trust providing benefits to officer-stockholders could be a true pension trust under Section 165.

The court emphasized that Section 165 specifies that only amounts

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