1 T.C. 656 (1943)

Gains received upon the retirement of an investment certificate issued by a corporation in registered form are considered amounts received in exchange for the certificate and are taxable as capital gains, not ordinary income.

Summary

George Peck Caulkins acquired an "Accumulative Investment Certificate" in 1928, promising a significantly larger payment after ten years if required payments were made. The certificate was in registered form. Upon its retirement in 1939, Caulkins received $20,000, exceeding his total payments of $15,043.33. The Commissioner of Internal Revenue argued the $4,956.67 difference was ordinary income, akin to interest. The Tax Court held that the gain was taxable as a capital gain under Section 117(f) of the Revenue Act of 1938, as the certificate qualified as an evidence of indebtedness issued by a corporation in registered form.

Facts

On December 19, 1928, Investors Syndicate delivered to George Peck Caulkins an "Accumulative Installment Certificate." The certificate promised to pay Caulkins $20,000 after ten years, contingent on annual payments of $1,512. The certificate was in registered form and assignable with the company's consent. Caulkins made payments totaling $15,043.33 by November 7, 1938. He surrendered the certificate on April 11, 1939, receiving $20,000 from Investors Syndicate.

Procedural History

Caulkins reported the $4,956.67 gain as a long-term capital gain on his 1939 tax return, including only 50% in his taxable income. The Commissioner determined the entire amount was ordinary income, resulting in a deficiency assessment. Caulkins petitioned the Tax Court for a redetermination of the deficiency.

Issue(s)

Whether the excess amount received by Caulkins upon the retirement of the Accumulative Investment Certificate over his aggregate payments constitutes ordinary income or capital gain under the Revenue Act of 1938.

Holding

Yes, the excess amount is taxable as a capital gain because the certificate qualifies as "…certificates or other evidences of indebtedness issued by any corporation…in registered form" under Section 117(f) of the Revenue Act of 1938.

Court's Reasoning

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The Tax Court reasoned that Section 117(f) specifically addresses the retirement of corporate indebtedness. While the Commissioner argued the gain was either interest or income from a transaction entered into for profit taxable under Section 22, the court emphasized that Section 117(f) carves out specific transactions for capital gain treatment. The court relied on *Willcuts v. Investors Syndicate, 57 F.2d 811*, which held similar certificates were corporate securities subject to stamp tax. It also noted the similarity to U.S. Savings Bonds, whose increment is treated as interest only due to explicit Congressional action. The court distinguished cases like *Frank J. Cobbs, 39 B.T.A. 642*, which excluded insurance and annuity contracts from Section 117(f), because the certificate here was an evidence of indebtedness issued by a corporation in registered form, therefore meeting the requirements of 117(f). "For the purposes of this chapter, amounts received by the holder upon the retirement of bonds, debentures, notes, or certificates or other evidences of indebtedness issued by any corporation (including those issued by a government or political subdivision thereof), with interest coupons or in registered form, shall be considered as amounts received in exchange therefor."

Practical Implications

This decision clarifies that certain investment certificates issued by corporations fall under the capital gains provisions of the tax code when retired. Legal practitioners should analyze the specific terms of such certificates to determine if they qualify as evidences of indebtedness issued in registered form. The ruling highlights that absent specific Congressional exclusion, gains from the retirement of such instruments are treated as capital gains, not ordinary income. This can significantly impact the tax liabilities of investors holding similar instruments. Subsequent cases would need to consider the specific characteristics of the financial instrument in question, focusing on whether it represents a corporate indebtedness and whether it is in registered form.

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