

### **3 T.C. 131 (1944)**

Interest on bonds issued by the Port of New York Authority is exempt from federal income tax under Section 22(b)(4) of the Revenue Acts of 1936 and 1938 because the Authority is a political subdivision of a state.

#### **Summary**

The Estate of Alexander J. Shamberg petitioned the Tax Court, contesting deficiencies in income tax assessments for 1937 and 1938. These deficiencies stemmed from the decedent's failure to include interest received on bonds issued by the Port of New York Authority in his taxable income. The Tax Court held that the interest was exempt from federal income tax because the Port Authority qualified as a political subdivision of a state, thereby falling under the exemption provided by Section 22(b)(4) of the Revenue Acts of 1936 and 1938. The court emphasized the legislative and administrative history of the exemption provision, indicating a broad interpretation of "political subdivision."

#### **Facts**

The Port of New York Authority was created in 1921 through a compact between New York and New Jersey, with Congressional approval, to develop and operate port facilities on a self-supporting basis. The Authority issued bonds to finance various projects, including the Lincoln and Holland Tunnels. Isidor W. Shamberg's decedent held bonds from these issues, and received interest income in 1937 and 1938. The Commissioner of Internal Revenue sought to tax this interest income, arguing that the Port Authority was not a political subdivision of a state, and therefore, its bonds did not qualify for tax-exempt status.

#### **Procedural History**

The Commissioner of Internal Revenue determined deficiencies in the decedent's income tax for 1937 and 1938. The Estate of Alexander J. Shamberg, through its administrator, Isidor W. Shamberg, petitioned the Tax Court for a redetermination of the deficiencies. The Tax Court reviewed the case based on a stipulated set of facts.

#### **Issue(s)**

Whether interest received on bonds issued by the Port of New York Authority is exempt from federal income tax under Section 22(b)(4) of the Revenue Acts of 1936 and 1938, which excludes from gross income interest on obligations of "a State, Territory, or any political subdivision thereof."

#### **Holding**

Yes, because the Port of New York Authority is a political subdivision of both the

State of New York and the State of New Jersey, and its bonds are thus tax-exempt under Section 22(b)(4) of the Revenue Acts of 1936 and 1938.

### **Court's Reasoning**

The court reasoned that the legislative history of Section 22(b)(4) indicated that Congress intended a broad interpretation of the term “political subdivision.” The court cited opinions from the Attorney General defining “political subdivision” as any division of a state authorized to carry out a portion of the state’s public functions. The court distinguished the Supreme Court’s decision in *Helvering v. Gerhardt*, 304 U.S. 405 (1938), which held that employees of the Port Authority were not state employees for tax purposes, arguing that the *Gerhardt* case dealt with an administrative regulation concerning salaries, not the statutory exemption for interest income. The Tax Court emphasized that the Port Authority was created by the states of New York and New Jersey to perform essential public functions related to transportation and commerce within the Port of New York District. The court noted that the Authority possessed powers such as eminent domain and certain police powers, further supporting its status as a political subdivision. The fact that the Port Authority was an interstate entity did not disqualify it, since it functioned as a political subdivision of each state individually.

### **Practical Implications**

This case clarifies the scope of the tax exemption for obligations issued by state and local government entities. It provides a legal basis for treating bonds issued by public authorities, like the Port Authority, as tax-exempt, thereby reducing borrowing costs for these entities. The decision reinforces the understanding that the term “political subdivision” should be interpreted broadly to include entities created by states to perform public functions, even if they lack taxing power or operate across state lines. Later cases have cited *Shamberg* to support the tax-exempt status of bonds issued by similar public authorities and special districts, affecting municipal finance and infrastructure development. The decision remains relevant for understanding the boundaries of federal taxing power in relation to state and local government instrumentalities.