3 T.C. 712 (1944)

Payment of a judgment on a bond, given to secure payment of taxes, is considered a payment of the underlying tax itself and is therefore not deductible as a loss, even if the statute of limitations for collecting the tax has expired.

Summary

Edwin J. Schoettle Co. sought to deduct a payment made in 1940 pursuant to a judgment on a bond issued in 1923. The bond was given to secure payment of a disputed 1917 tax liability. The Tax Court held that the payment was not deductible. The court reasoned that the bond served as a substitute for the underlying tax obligation, and therefore the payment was effectively a payment of taxes, which are not deductible under the tax code. The fact that the statute of limitations on the tax had expired was irrelevant because the bond created a new contractual obligation.

Facts

In 1918, Edwin J. Schoettle Co. filed its 1917 income and excess profits tax returns. In 1923, the Commissioner of Internal Revenue assessed an additional tax liability for 1917. To avoid immediate collection, Schoettle Co. filed a claim for abatement and provided a bond, with Central Trust & Savings Co. as surety, guaranteeing payment of any tax ultimately found to be due. The Commissioner partially rejected the abatement claim. Schoettle Co. petitioned the Board of Tax Appeals, which ruled in its favor based on the statute of limitations. Despite this ruling, the IRS later sued to enforce the bond. The District Court ruled in favor of the IRS, and Schoettle Co. eventually paid the judgment.

Procedural History

1. 1923: Commissioner assessed additional taxes; Schoettle Co. filed claim for abatement and provided a bond.

2. 1928: Board of Tax Appeals ruled in favor of Schoettle Co. based on the statute of limitations.

3. 1935: IRS sued in District Court to enforce the bond.

4. 1938: District Court dismissed Schoettle Co.'s equity suit to rescind the bond and ruled in favor of the IRS in the suit at law.

5. 1940: Schoettle Co. paid the judgment.

6. 1940: Schoettle Co. claimed a deduction for the payment; the Commissioner disallowed it.

7. Tax Court: Schoettle Co. petitioned the Tax Court, which ruled in favor of the

Commissioner.

Issue(s)

Whether a payment made pursuant to a judgment on a bond, given to secure payment of a tax liability, is deductible as a loss when the statute of limitations on the underlying tax has expired?

Holding

No, because the payment under the bond is considered a payment of the underlying tax itself and is therefore not deductible, even if the statute of limitations for collecting the tax has expired.

Court's Reasoning

The Tax Court reasoned that the bond created a new contractual obligation, distinct from the original tax liability. The court relied on *United States v. John Barth Co.*, 279 U.S. 370 (1929), which held that a bond substitutes the obligation to pay taxes with a contractual obligation. The court emphasized that Schoettle Co. voluntarily provided the bond to prevent immediate collection of taxes and to gain time to contest the assessment. The Court stated that "the making of the bond gives the United States a cause of action separate and distinct from an action to collect taxes which it already had." Because Schoettle Co. received the benefit of delaying tax collection by issuing the bond, it could not now argue that the payment was something other than a tax payment. The court also noted that the expiration of the statute of limitations on the tax did not extinguish the underlying tax liability; it merely barred the remedy. The bond served as a waiver of the statute of limitations. Quoting *Helvering v. Newport Co., 291 U.S. 485 (1934)*, the court pointed out that even if the statute extinguished the liability, the bond obligation remained unaffected.

Practical Implications

This case clarifies that providing a bond to secure payment of taxes creates a distinct contractual obligation that is enforceable even if the statute of limitations on the underlying tax liability has expired. Taxpayers should be aware that issuing a bond essentially waives the statute of limitations defense. Payments made on such bonds are treated as tax payments, which are not deductible. This ruling affects how tax liabilities are managed when disputes arise, especially when statutes of limitations are a factor. Later cases would cite Schoettle for the proposition that a bond creates a new obligation, independent of the underlying tax liability, and that payment on such a bond is the equivalent of paying the tax itself. This affects tax planning and litigation strategies when dealing with disputed tax assessments and bonds.