Lavery v. Commissioner, 158 F.2d 859 (7th Cir. 1946)

A cash-basis taxpayer must include a check in gross income for the year it is received, even if the check is not cashed until the following year, provided the check is available for the taxpayer's unrestricted use.

Summary

Urban A. Lavery, a cash-basis taxpayer, received a check from the American Bar Association on December 30, 1941, for services rendered. He deposited the check on January 2, 1942, and argued that the funds should be included in his 1942 income. The Tax Court ruled against Lavery, holding that because he received the check in 1941 and had unrestricted access to the funds, it constituted income for 1941, irrespective of when he physically cashed it. This case illustrates the principle that receipt, not necessarily physical possession of cash, determines income recognition for cash-basis taxpayers.

Facts

- Urban A. Lavery received a check for $2,666.67 from the American Bar Association on December 30, 1941.
- The check represented payment for services rendered as managing editor of the American Bar Association Journal.
- Lavery provided a written statement accepting the payment in full satisfaction of his claims against the Association.
- Lavery did not deposit the check until January 2, 1942.
- Lavery was a cash-basis taxpayer.

Procedural History

The Commissioner of Internal Revenue determined that the $2,666.67 should be included in Lavery's 1941 income. Lavery appealed to the Tax Court, arguing that the income was not realized until 1942 when the check was deposited. The Tax Court ruled in favor of the Commissioner. Lavery then appealed to the Seventh Circuit Court, which affirmed the Tax Court's decision.

Issue(s)

Whether a cash-basis taxpayer must include a check in gross income for the year it is received, even if the check is not cashed until the following year.

Holding

Yes, because the taxpayer received the check in 1941, had unrestricted access to the funds, and provided a written statement accepting the check in full settlement of his claims; therefore, it constituted income for 1941, irrespective of when he physically cashed it.

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Court’s Reasoning

The court relied on the established principle that a cash-basis taxpayer recognizes income when it is actually or constructively received. The court emphasized that Lavery received the check on December 30, 1941, and could have cashed it that day or the next. The court distinguished this case from *Avery v. Commissioner*, 292 U.S. 210 (1934), stating that in *Avery*, the Supreme Court observed that “The checks did not constitute payments prior to their actual receipt.” The court found that Lavery’s control over the check in 1941 was unrestricted, and his decision to delay depositing it was irrelevant for tax purposes. The court cited Treasury Regulations 103, which state that income credited to or set apart for a taxpayer without restriction is taxable in the year it is credited or set apart. Even if the payment was intended for future services (which the court found it was not), the court noted the principle that “payments of compensation are income to a taxpayer on a cash basis in the year of receipt, as distinguished from the year in which the compensation is earned.”

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