11 T.C. 227 (1948)

A subsequent agreement to refund a portion of partnership income received during a fiscal year does not retroactively reduce the distributed income of the partnership for that year for tax purposes.

Summary

The Simon brothers, partners in Simon Brothers, leased property to their corporation, Simms' Cut Rate Stores, Inc. The IRS challenged the rental payments the corporation deducted. Subsequently, the partners agreed to refund a portion of the rent to the corporation. The Tax Court addressed whether this agreement retroactively reduced the partners' income tax liability for the year the income was initially received. The court held that it did not, emphasizing that income is taxed in the year it is actually received, regardless of later agreements to refund portions of it.

Facts

The Simon brothers formed a partnership, Simon Brothers, which leased property to their corporation, Simms' Cut Rate Stores, Inc. The corporation paid rent to the partnership based on 6% of its gross sales. During an IRS examination, the IRS agent questioned the reasonableness of the rent the corporation deducted. On November 9, 1943, after the close of the partnership's fiscal year, the partners agreed that if the IRS disallowed any of the corporation's rent deduction, they would refund the disallowed amount. On January 31, 1944, the IRS and the corporation agreed to disallow deductions exceeding 4.75% of gross sales. The partners then adjusted their accounts to reflect the reduced rental income.

Procedural History

The Commissioner of Internal Revenue determined deficiencies in the petitioners' income tax liability. The petitioners challenged these determinations, arguing that their agreement to refund a portion of the rental income retroactively reduced their income. The cases were consolidated in the Tax Court.

Issue(s)

1. Whether the execution of a conditional agreement to refund a portion of partnership income, made after the close of the partnership's fiscal year, retroactively reduces the distributed income of the partnership for that year.

Holding

1. No, because the income was actually received by the partnership during its fiscal year without any restrictions; a subsequent agreement cannot retroactively alter the tax liability.

© 2025 SCOTUSreports.com. All rights reserved.

Court’s Reasoning

The Tax Court relied on the principle that income is taxed in the year it is actually received, citing *Burnet v. Sanford & Brooks Co.*, 282 U.S. 359 (1931), and *Security Flour Mills Co. v. Commissioner*, 321 U.S. 281 (1944). The court emphasized that the partnership received the rental income without any conditions or restrictions during its fiscal year. The agreement to refund a portion of the rent was made after the close of the fiscal year, and therefore could not retroactively reduce the partnership’s income for that year. The court stated:

© 2025 SCOTUSreports.com. All rights reserved.