12 T.C. 232 (1949)

A cash-basis taxpayer can deduct state income taxes in the year they are paid, even if paid before the taxes are legally due, provided the state tax authorities accept the payment as taxes.

Summary

The Tax Court addressed whether taxpayers using the cash receipts and disbursements method could deduct state income taxes paid in 1944, even though the taxes weren't legally due until 1945. The taxpayers submitted checks to Louisiana state tax authorities in December 1944, covering their estimated state income tax liabilities, and the state accepted these payments as taxes for 1944, issuing receipts accordingly. The court held that because the taxpayers used the cash method and the state accepted the payments as taxes, the deductions were permissible in 1944.

Facts

The Glassells, residents of Louisiana, used the cash receipts and disbursements method for their books and tax returns.
In December 1944, they computed estimated state income tax liabilities and sent checks to the state collector before the end of the year.
The state collector accepted the checks as payments for 1944 income taxes and provided receipts noting "For 1944 Income Tax."
The checks cleared the bank in January 1945.
In May 1945, the Glassells filed their official Louisiana income tax returns for 1944.

Procedural History

The Commissioner of Internal Revenue disallowed the deductions claimed by the Glassells for state income taxes paid in 1944.
The Glassells petitioned the Tax Court for a redetermination of the deficiencies.
The Tax Court consolidated the cases.

Issue(s)

Whether taxpayers who use the cash receipts and disbursement method of accounting can deduct state income taxes in the year they paid them, even if payment occurred before the taxes were legally due under state law.

Holding

Yes, because the taxpayers used the cash method of accounting, and the state taxing authority accepted their payments as tax payments in 1944, providing receipts accordingly.

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Court’s Reasoning

The court relied on Section 23(c) of the Internal Revenue Code, which allows deductions for “Taxes paid or accrued within the taxable year.”
The key determination was whether the taxpayers’ actions constituted a ‘payment’ of taxes in 1944, which required interpreting Louisiana tax law.
Louisiana law allowed taxpayers to pay their taxes, or installments thereof, before the prescribed due date. According to the court, “(d) A tax imposed by this act, or any instalment thereof, may be paid at the election of the taxpayer, prior to the date prescribed for its payment.”
Since Louisiana tax officials accepted the checks as payments and issued receipts, the court concluded that the payments were deductible in 1944 because the taxpayers used the cash method.
The court distinguished cases cited by the Commissioner, noting they involved either the constitutionality of a state tax law or deposits with a third party, not direct payments to the state tax authority.
The court also cited Section 41 of the Internal Revenue Code and Regulations 111, sec. 29.41-1, which mandate following the taxpayer’s accounting method if it clearly reflects income.

Practical Implications

This case clarifies that cash-basis taxpayers can accelerate deductions by paying state income taxes before the legal due date, provided the state accepts the payment as taxes.
Tax professionals can advise clients on the benefits of early tax payments for managing taxable income in specific years.
This ruling emphasizes the importance of proper documentation, such as receipts from the state tax authority, to support the deduction.
The decision highlights the interplay between federal tax law and state tax laws in determining deductibility.
Subsequent cases may distinguish this ruling based on differences in state tax laws or facts indicating the payment was not truly accepted as a tax payment by the state.

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