12 T.C. 713 (1949)

A taxpayer’s election to deduct a war loss under Section 127 of the Internal Revenue Code is binding and cannot be retroactively rescinded to avoid reporting recovery of the loss in a subsequent year.

Summary

The petitioner, Keeler, sought to amend his 1942 tax return to withdraw a war loss deduction he had previously claimed concerning bonds of the Philippine Railway Co., which were captured by the Japanese. Keeler wanted to avoid reporting the recovery of this loss in a later year, as required by Section 127(c) of the Internal Revenue Code. The Tax Court held that Keeler’s initial election to take the war loss deduction was binding. Allowing taxpayers to change their minds years later would disrupt the orderly administration of tax laws and the strict annual accounting system.

Facts

- In 1942, the petitioner held bonds in the Philippine Railway Co.
- The company’s property was captured by the Japanese in 1942, constituting a war loss.
- The petitioner requested a ruling from the IRS on whether he could deduct the war loss under Section 127 of the Internal Revenue Code.
- He deducted the war loss on his original 1942 tax return and reaffirmed this deduction in two subsequent amended returns.
- Approximately three and a half years after the due date of the 1942 return, the petitioner filed a “third amended return” seeking to withdraw the war loss deduction.
- His motive was to avoid reporting the recovery of the loss in a later year, as required by Section 127(c) of the IRC.

Procedural History

The Commissioner of Internal Revenue denied the petitioner’s attempt to withdraw the war loss deduction. The case was then brought before the Tax Court.

Issue(s)

Whether a taxpayer can retroactively withdraw a war loss deduction claimed under Section 127 of the Internal Revenue Code to avoid reporting the recovery of that loss in a subsequent tax year.

Holding

No, because the taxpayer’s initial election to take the war loss deduction is binding and cannot be retroactively rescinded.

Court's Reasoning

The Tax Court reasoned that allowing the petitioner to withdraw his election would undermine the principle of strict annual accounting and disrupt the orderly administration of tax laws. The court quoted *Security Flour Mills Co. v. Commissioner, 321 U. S. 281*, emphasizing that a tax system must produce revenue ascertainable and payable at regular intervals. Allowing taxpayers to change their minds years later would create unnecessary obstacles and confusion. The court also cited *Champlin v. Commissioner, 78 Fed. (2d) 905*, stating: "To permit taxpayers to change their minds ad libitum for fifteen years would throw the department into inextricable confusion. The general rule is that where a taxpayer has exercised an option conferred by statute he cannot retro-actively and ex parte rescind his action." The court concluded that the petitioner's election to take the war loss deduction in 1942 was binding.

Practical Implications

This case reinforces the principle that taxpayers are bound by elections made on their tax returns, especially when those elections affect the timing of income or deductions. It limits the ability of taxpayers to retroactively amend returns to optimize their tax liability in light of subsequent events. This decision promotes certainty and predictability in tax administration and prevents taxpayers from manipulating the annual accounting system to their advantage. It has implications for elections beyond war loss deductions, influencing how courts view taxpayers' attempts to change accounting methods or other choices made on prior returns. Later cases would distinguish this ruling if the initial election was made based on misinformation from the IRS.