Langer v. Commissioner, 16 T.C. 41 (1951)

Financial difficulties that induce a corporation’s officers to voluntarily restrain from paying themselves salaries are not an event similar in nature to a receivership, and thus do not qualify payments as ‘back pay’ eligible for special tax treatment under Section 107(d) of the Internal Revenue Code.

Summary

The petitioners, Langer and Lindsey, argued that payments received in 1944 and 1945 were back salary eligible for tax benefits under Section 107(d) because the corporation’s financial difficulties prevented earlier payment. The Tax Court disagreed, holding that voluntary restraint due to financial distress is not equivalent to the legally enforceable restrictions imposed by a bankruptcy or receivership. The court emphasized that the officers’ decision was voluntary, unlike a receivership where a receiver has legally enforceable control over such decisions.

Facts

Langer and Lindsey were officer-shareholders of a corporation operating a hotel. Pacific advanced funds to the corporation and kept close oversight of the corporation’s operations. The corporation experienced financial difficulties. Langer and Lindsey did not receive authorized salaries after 1937. Payments were made to Langer and Lindsey in 1944 and 1945, which they claimed were back salaries attributable to prior years’ services. There was no legal restriction on the payment of salaries.

Procedural History

The Commissioner of Internal Revenue determined deficiencies in the petitioners’ income tax. The petitioners appealed to the Tax Court, arguing that the payments qualified as back pay under Section 107(d) of the Internal Revenue Code. The Tax Court reviewed the case.

Issue(s)

Whether the financial difficulties and factual necessity restricting a corporation’s freedom of action can be deemed an event similar in nature to a receivership under regulations prescribed by the Commissioner, thus qualifying payments as “back pay” under Section 107(d)(2) of the Internal Revenue Code.

Holding

No, because the voluntary restraint of corporate officers due to financial difficulties is not similar in nature to the legally enforceable restrictions imposed by a receivership under Section 107(d)(2).

Court's Reasoning

The court reasoned that while cogent circumstances deterred the corporation from paying salaries, this voluntary restraint was not the same as a restriction imposed by a receivership. The court emphasized the distinction between a voluntary decision made by corporate officers and the legally enforceable control exercised by a receiver. The court stated,