16 T.C. 1157 (1951)

The 1% monthly addition to tax for failure to pay installments of estimated tax continues as long as the estimated tax is unpaid, even after the filing of an income tax return, until the 10% maximum is reached.

Summary

Carl and Evelyn Stephan filed an amended declaration of estimated tax but failed to pay the estimated tax. They subsequently filed timely income tax returns, but remained delinquent in tax payments. The Commissioner assessed a 1% monthly addition to tax under Section 294(d)(1)(B) of the Internal Revenue Code. The Stephans argued that this addition should cease upon filing their income tax returns. The Tax Court held that the penalty continues until the estimated tax is paid, up to the 10% maximum, regardless of filing the income tax return.

Facts

Carl and Evelyn Stephan, husband and wife, were fiscal year taxpayers. On November 15, 1944, they filed a joint declaration of estimated tax showing no tax due. On September 15, 1945, they filed an amended estimate showing $70,000 due. They filed individual income tax returns on November 15, 1945, showing a total tax due of $86,939.10. No payments were made until March 13, 1946, and subsequent payments were made periodically until September 16, 1946.

Procedural History

The Commissioner determined deficiencies in the Stephan's income tax and additions to the tax. The Stephans petitioned the Tax Court, contesting the additions to tax under Section 294(d)(1)(B) of the Internal Revenue Code. The Commissioner conceded error regarding the addition to tax proposed under section 294(d)(2).

Issue(s)

Whether the petitioners are liable under Section 294(d)(1)(B) of the Code for a 6% or 10% addition to tax for failure to pay their declared estimated income tax within the prescribed time, and whether the monthly 1% addition to tax should discontinue after filing the income tax return.

Holding

No, the petitioners are liable for the addition to tax up to the 10% maximum because the statute states there shall be an addition to the tax of 5% of the unpaid amount of such installment, and in addition 1% of such unpaid amount for each month (except the first) or fraction thereof during which such amount remains unpaid.

Court's Reasoning

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The Tax Court examined the legislative history of Section 294(d)(1)(B) and considered committee hearings. The court emphasized the wording of the statute itself, which states that the 1% monthly addition applies while "such amount remains unpaid." The court reasoned that the Code does not explicitly state that the monthly addition stops when the income tax return is filed. The court noted that if the tax due were fully paid upon filing the final return, additions to the tax would cease. However, because the Stephans did not pay the tax due when they filed their returns, the penalty continued to accrue until the 10% maximum was reached. The court cited *Albert T. Felix, 12 T.C. 933*, as precedent, where a 10% addition was sustained for delinquent payment of estimated tax. The court stated: "Section 294 (d) (1) (B) provides an addition to the tax in the case of failure to pay an installment of estimated tax within the time prescribed…That addition is in the amount of 5 per cent of the unpaid part of the installment, plus an addition of 1 per cent for each month…during which the installment remains unpaid, but in no event to exceed 10 per cent of the unpaid part of the installment."

Practical Implications

This decision clarifies that penalties for underpayment of estimated taxes continue to accrue until the tax is paid, regardless of whether an income tax return has been filed. Legal practitioners should advise clients that timely filing of tax returns does not negate the obligation to pay estimated taxes on time. This case emphasizes the importance of paying estimated taxes promptly to avoid penalties and highlights that the penalty accrues monthly, capped at 10% of the unpaid amount. Taxpayers cannot avoid the penalty by simply filing on time; they must also pay their estimated tax liabilities. This ruling remains relevant for interpreting similar provisions in subsequent tax codes, demonstrating the ongoing impact of prompt tax payment.

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