17 T.C. 1015 (1951)

Retirement pay received by a police officer due to disability incurred in the line of duty is exempt from federal income tax under Section 22(b)(5) of the Internal Revenue Code.

Summary

The Tax Court held that retirement pay received by a Baltimore police officer, William L. Neill, was exempt from federal income tax under Section 22(b)(5) of the Internal Revenue Code. Neill was retired due to a disability incurred in the line of duty. The court reasoned that although the statute's language might not literally apply, prior precedent and IRS rulings extended the exemption to situations where taxpayers were retired because of injuries sustained while performing their duties. The critical factor was whether the retirement was due to disability or length of service.

Facts

William L. Neill, a Baltimore police officer, was appointed to the police department in 1925, resigned in 1926, and was reinstated in 1927. In June 1945, police department physicians examined him and found him incapacitated for service. As a result, he was retired on July 1, 1945. In 1946, he briefly worked as a bartender but could not continue due to his physical disability. He received $1,355.76 from the Baltimore Police Department as retirement pay in 1946, pursuant to a Baltimore city law that allowed the Police Commissioner to retire officers with at least 16 years of service or those permanently disabled in the line of duty.

Procedural History

The Commissioner of Internal Revenue determined a deficiency in Neill's 1946 income tax. Neill petitioned the Tax Court, arguing that his retirement pay was non-taxable under Section 22(b)(5) of the Internal Revenue Code. The Tax Court ruled in favor of Neill.

Issue(s)

Whether the $1,355.76 received by William L. Neill from the Baltimore Police Department in 1946, as retirement pay, is exempt from tax under the provisions of Section 22(b)(5) of the Internal Revenue Code.

Holding

Yes, because Neill was retired due to a disability incurred in the line of duty, not solely based on his length of service.

Court's Reasoning

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The court relied on Section 22(b)(5) of the Internal Revenue Code, which exempts amounts received through accident or health insurance or under workmen's compensation acts, as compensation for personal injuries or sickness. While acknowledging that the statute's language might not be a perfect fit, the court cited *Frye v. United States* and I.T. 3877, which extended the exemption to situations where a taxpayer was retired due to injuries sustained in the line of duty. The court distinguished cases like *Elmer D. Pangburn*, *Joseph B. Simms*, and *Marshall Sherman Scarce*, where retirement was based on length of service rather than disability. The court reviewed the evidence, finding it somewhat conflicting but ultimately concluding that Neill was retired because of a disability incurred in the line of duty. The court stated: "However, we think that petitioner has placed before us all the evidence that was reasonably at his command, and we are satisfied and so find as a fact, in the light of the testimony and the record as a whole, that petitioner was retired in 1945 by reason of disability incurred in the line of duty, rather than because of service of the prescribed number of years on the police force."

Practical Implications

This case clarifies that retirement pay received due to a disability incurred in the line of duty can be tax-exempt under Section 22(b)(5) (now replaced by subsequent tax code provisions addressing similar exemptions). It highlights the importance of determining the actual basis for retirement – whether it is due to disability or length of service. Legal practitioners should carefully examine the circumstances surrounding a public servant's retirement to determine if the disability was the primary reason. Later cases and IRS guidance would likely build upon this principle, requiring clear documentation and evidence to support a claim for tax exemption based on disability retirement. This decision impacts tax planning for public sector employees, particularly those in high-risk professions like law enforcement and firefighting.

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