18 T.C. 742 (1952)

A payment to an employee for past services does not qualify as "back pay" eligible for special tax treatment under Section 107(d) of the Internal Revenue Code unless the failure to pay in prior years was due to bankruptcy, receivership, or a dispute determined after the commencement of court proceedings or similar formal intervention.

Summary

Thomas Thompson received a $60,000 settlement from his former employer, Virginia Shoe Company, for alleged unpaid commissions. Thompson argued this payment should be taxed as "back pay" under Section 107(d) of the Internal Revenue Code, which provides beneficial tax treatment. The Tax Court disagreed, holding that the settlement did not qualify because the dispute was resolved through negotiation without any formal proceedings like a lawsuit or arbitration. The court emphasized that the "intervention of one of the following events" as specified in the statute was a prerequisite for back pay treatment and a simple negotiated settlement did not meet that requirement.

Facts

Thomas Thompson was employed by Virginia Shoe Company from 1939 to 1946, primarily selling shoes on commission. In 1942, Thompson secured significant new accounts for the company. A dispute arose regarding commissions on these sales. Thompson claimed he was owed a substantial amount. After being discharged in 1946, Thompson, with legal representation, demanded $125,000 in alleged past due commissions. To avoid a lawsuit and potential negative publicity, the company paid Thompson $60,000 in a compromise settlement. The company never conceded it owed Thompson any commissions and did not accrue any such expenses on its books.

Procedural History

The Commissioner of Internal Revenue determined a deficiency in Thompson's 1946 income tax based on the $60,000 payment. Thompson petitioned the Tax Court, arguing the payment qualified as "back pay" under Section 107(d) of the Internal Revenue Code. The Tax Court ruled against Thompson.

Issue(s)

1. Whether the $60,000 payment Thomas received from Virginia Shoe Company in 1946 qualifies as "back pay" under Section 107(d)(1) of the Internal Revenue Code.

Holding

© 2025 SCOTUSreports.com. All rights reserved.

1. No, because the failure to pay the remuneration in prior years was not due to the intervention of bankruptcy, receivership, or a dispute determined after the commencement of court proceedings or an event similar to those.

Court’s Reasoning

The court analyzed Section 107(d)(2)(A) of the Internal Revenue Code, which defines “back pay.” It noted that back pay includes remuneration that would have been paid prior to the taxable year but for specific events, including bankruptcy, receivership, or a dispute determined after the commencement of court proceedings. The court emphasized that the regulations require unusual circumstances similar to those listed in the statute that defer payment of remuneration. In this case, the court found that the settlement was reached through negotiation between Thompson and the company, without any formal proceedings. The court stated, “Congress must have intended to exclude the settlement of a dispute by the parties through a mere discussion between themselves without the commencement of any court proceeding or without the intervention of any event which might be considered similar in nature to a court proceeding, even though in the discussion between the parties threats of suit might be mentioned.” The court also noted that

© 2025 SCOTUSreports.com. All rights reserved.