Lincoln Electric Co. Employees' Profit-Sharing Trust v. Commissioner, 17 T.C. 160 (1951)

A taxpayer on the accrual basis cannot deduct a contribution to a pension trust in a prior year unless the liability for the payment actually accrued in that prior year, even if the payment is made within 60 days after the close of that year.

Summary

Lincoln Electric Company sought to deduct a $23,500 payment made in February 1945 to a pension trust from its 1944 income tax return, arguing that Section 23(p)(1)(E) of the Internal Revenue Code allowed the deduction because the payment was made within 60 days of the close of the 1944 tax year. The Tax Court disallowed the deduction, holding that the liability for the payment did not accrue in 1944 because the pension trust was not actually created until January 1945. The court clarified that Section 23(p)(1)(E) only applies if the liability was properly accruable in the prior year.

Facts

On December 28, 1944, the board of directors of Lincoln Electric Company resolved to create a pension trust and authorized a contribution of up to $25,000. The pension trust was formally created on January 26, 1945. The trustees were named on January 25, 1945. Employees were notified of the trust after January 30, 1945. The company paid $23,500 to the trust in February 1945. The company then attempted to deduct this amount from its 1944 income tax return.

Procedural History

The Commissioner of Internal Revenue disallowed Lincoln Electric Company's deduction for the 1944 tax year. The Lincoln Electric Co. Employees' Profit-Sharing Trust then petitioned the Tax Court for review. The Tax Court upheld the Commissioner's determination.

Issue(s)

Whether a taxpayer on the accrual basis can deduct a payment to a pension trust in a prior year, pursuant to Section 23(p)(1)(E) of the Internal Revenue Code, when the trust was not established and the liability for the payment did not accrue until after the close of that prior year, even though the payment was made within 60 days after the close of that prior year.

Holding

No, because Section 23(p)(1)(E) only applies when the liability was properly accruable in the prior year, and in this case, the liability to make the payment to the pension trust did not accrue in 1944, as the trust was not created until 1945.

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Court’s Reasoning

The court reasoned that Section 23(p)(1)(E) provides a limited exception to the general rule that pension trust contributions are deductible only in the year they are paid. This exception allows accrual basis taxpayers to deduct payments made within 60 days after the close of the taxable year, but only if the liability for the payment actually accrued in that prior year. The court found that the liability did not accrue in 1944 because the pension trust was not created until January 1945. Prior to the creation of the trust, the company’s board of directors could have decided not to proceed with the plan without incurring any liability. The court distinguished the present case from *555, Inc.* and *Crow-Burlingame Co.*, where tentative trust agreements had been executed in the earlier year, establishing that the amounts in question had accrued in that year. Here, no such agreement existed, and the liability was not properly accruable in 1944. The court emphasized that section 23(p)(1)(E) does not make an otherwise non-accruable item deductible simply because payment was made within 60 days after year end. As the court stated, “Section 23 (p) (1) (E) merely allows the deduction to an accrual basis taxpayer in the earlier year, where the payment, otherwise accruable in the earlier year, is in fact made within 60 days after the close of the earlier year.”

Practical Implications

This case clarifies the requirements for deducting pension trust contributions under Section 23(p)(1)(E) of the Internal Revenue Code. It emphasizes that accrual basis taxpayers must ensure that the liability for the contribution has actually accrued in the prior year to take advantage of the 60-day payment rule. This means that all necessary steps to establish the trust and create a binding obligation to make the contribution must be completed before the end of the tax year for which the deduction is sought. Subsequent cases would cite this ruling when determining whether an accrual-basis taxpayer could deduct certain payments in a prior year.

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