1954 Tax Ct. Memo LEXIS 43

An employer’s contributions to a profit-sharing trust exceeding the amount specified in the pre-approved plan are not deductible under Section 23(p)(1)(C) of the Internal Revenue Code.

Summary

Liberty Machine Works, Inc. sought to deduct contributions to its employee profit-sharing trust that exceeded the 5% of net profits outlined in the trust agreement. The Tax Court disallowed the deduction for the excess contributions, holding that only payments conforming to the pre-approved plan’s formula were deductible under Section 23(p)(1)(C). The court emphasized the unambiguous nature of the trust agreement and that contributions beyond its terms were not part of the approved plan.

Facts

Liberty Machine Works established a profit-sharing trust for its employees. The trust agreement stipulated that contributions would be 5% of the company’s net profits. In certain tax years, Liberty Machine Works contributed amounts exceeding this 5% threshold. The IRS disallowed deductions for these excess contributions.

Procedural History

Liberty Machine Works, Inc. petitioned the Tax Court challenging the Commissioner’s disallowance of deductions for contributions made to its employee profit-sharing trust. The Commissioner argued that the deductions should be limited to the amount called for by the original plan, and the court agreed.

Issue(s)

1. Whether contributions to an employee profit-sharing trust, exceeding the amount called for by the previously approved plan, are deductible under Section 23(p)(1)(C) of the Internal Revenue Code?
2. Whether amounts contributed to organizations engaged in lobbying are deductible?
3. Whether additions to a reserve for bad debts were properly disallowed?

Holding

1. No, because Section 23(p)(1)(C) only allows deductions for contributions made “to or under” the approved plan, and excess contributions are not part of that plan.
2. No, because contributions to organizations substantially engaged in lobbying are not deductible under Regulation 111, Section 29.23(q)-1.
3. No, because the petitioner failed to provide adequate evidence to demonstrate

that the Commissioner's disallowance of additions to a reserve for bad debts was improper.

Court's Reasoning

The court reasoned that the trust agreement clearly defined the contribution formula as 5% of net profits. Contributions exceeding this amount were not made "to or under" the plan as required by Section 23(p)(1)(C). The court distinguished the case from *Commissioner v. Wooster Rubber Co.*, where the Sixth Circuit found ambiguity in the plan's terms. Here, the court found no ambiguity and refused to consider extrinsic evidence. The court emphasized that since the petitioner sought and obtained IRS approval for the plan, it was bound by the plan's express terms. Regarding lobbying expenses, the court cited *Textile Mills Securities Corporation v. Commissioner*, emphasizing that Treasury Regulations have the force of law. Finally, on the issue of bad debt reserve additions, the court emphasized that the taxpayer bears the burden of proof, and the petitioner failed to demonstrate the inadequacy of the existing reserve.

Practical Implications

This case illustrates the importance of adhering strictly to the terms of pre-approved employee benefit plans when claiming deductions for contributions. Employers cannot deduct contributions exceeding the predetermined formula in the plan. The decision emphasizes that unambiguous plan documents will be enforced according to their plain meaning. In practice, this means that employers need to carefully review and, if necessary, amend their plans if they wish to make contributions beyond the originally specified amounts and deduct those contributions. It also reinforces the principle that taxpayers bear the burden of proving the reasonableness of bad debt reserve additions, highlighting the need for thorough documentation and analysis of past experience and future expectations. The holding regarding lobbying expenses serves as a reminder of the stringent rules regarding the deductibility of such expenses, regardless of whether they might otherwise be considered ordinary and necessary business expenses.