*22 T.C. 1276 (1954)*

A lump-sum payment received by a federal employee for accumulated leave upon separation from service does not constitute “back pay” under Section 107(d) of the Internal Revenue Code of 1939 unless the remuneration would have been paid before the taxable year absent specific, qualifying circumstances.

**Summary**

The case of Donahoe v. Commissioner addresses the tax treatment of a lump-sum payment received by a federal employee for accumulated annual leave upon retirement. The court held that this payment did not qualify as “back pay” under Section 107(d) of the Internal Revenue Code of 1939. The court reasoned that the employee had no right to the compensation for accumulated leave until separation from service and that the payment was made according to the custom and practice of the employer at the time of separation. Therefore, the payment did not meet the requirements for back pay, which necessitates that the remuneration would have been paid prior to the taxable year but for certain specified events.

**Facts**

Francis T. Donahoe was a federal employee who accumulated 90 days of annual leave from 1933 to 1942. Upon his retirement in 1951, he received a lump-sum payment for this accumulated leave, calculated based on his salary at the time of retirement. Donahoe reported a portion of this payment as “back pay” under Section 107(d) of the Internal Revenue Code of 1939, attempting to take advantage of favorable tax treatment. The Commissioner of Internal Revenue disagreed, asserting the entire lump-sum payment was taxable at the current rates.

**Procedural History**

The case was heard by the United States Tax Court. The petitioners, Francis T. Donahoe and his wife, contested a deficiency in their 1951 income tax. The Tax Court reviewed the stipulated facts and the applicable law, ultimately ruling in favor of the Commissioner. The court’s decision resulted in a tax liability for the Donahoes.

**Issue(s)**

1. Whether the lump-sum payment received by petitioner for accumulated annual leave upon separation from federal service constituted “back pay” within the meaning of Section 107(d) of the Internal Revenue Code of 1939.

**Holding**

1. No, because the payment did not meet the criteria for “back pay” under the statute as the employee had no right to the payment until separation from service.

© 2025 SCOTUSreports.com. All rights reserved. 

## Court’s Reasoning

The court analyzed Section 107(d) of the Internal Revenue Code of 1939, which defines “back pay.” The court emphasized that for remuneration to qualify as back pay, it “would have been paid prior to the taxable year” but for specific intervening events, such as lack of funds. The court found that no agreement or legal obligation existed during the years the leave was accumulated for the government to pay the petitioner for the leave at that time. Instead, the opportunity to use the accumulated leave existed or it could be lost due to death or other factors. The court noted that the lump-sum payment was only authorized by Public Law 525, enacted in 1944. This law provided a new method for compensating separated employees for accumulated leave. The court determined that the lump-sum payment was not remuneration “which would have been paid prior to the taxable year” but for a qualifying event. The court also noted that the payment was made according to the usual custom and practice of the employer.

## Practical Implications

This case clarifies the tax treatment of lump-sum payments for accumulated leave for federal employees. The decision is a reminder that such payments are not automatically classified as “back pay” and do not receive special tax treatment. It underscores the importance of determining whether the remuneration would have been paid in a prior year but for specific circumstances. Legal professionals should advise clients who receive lump-sum payments for accumulated leave to carefully review the facts and circumstances of their situation to assess if they are eligible for special tax treatment. Tax attorneys should also consider the relevant Treasury regulations and any subsequent case law. If the payment is made in accordance with the employer’s usual practice, as indicated by this decision, it is unlikely to be considered back pay. This case also highlights the significance of statutory interpretations, and the application of legal principles to specific factual situations.

© 2025 SCOTUSreports.com. All rights reserved. 