27 T.C. 372 (1956)

A profit-sharing trust is considered valid and its contributions deductible if a trust corpus, such as a demand promissory note, is provided even if paid within the 60-day period allowed under the statute.

Summary

Tallman Tool & Machine Corporation, an accrual-basis taxpayer, established a profit-sharing plan and trust. On the last day of its fiscal year, it delivered a demand promissory note to the trust. Within the subsequent 60-day period, as allowed by the statute, Tallman paid cash to cover the note and additional amounts. The Commissioner disallowed the deduction claimed for the contribution, arguing the trust lacked a corpus. The Tax Court held that the note provided sufficient corpus under New York law and the payment within the grace period validated the trust's existence, entitling Tallman to the deduction. The court emphasized that a negotiable instrument issued for valuable consideration satisfied the requirement for a trust corpus.

Facts

Tallman Tool & Machine Corporation, a New York corporation, executed a profit-sharing plan and trust with an effective date of September 30, 1952, the last day of its fiscal year. On that same day, the corporation delivered a $20,000 demand promissory note to the trust. The note was unrestricted and negotiable. Tallman had sufficient cash to pay the note at all relevant times. The corporation paid the $20,000 note in full on October 30, 1952, along with an additional $2,520, within the 60-day period allowed by the statute. The Commissioner disallowed the deduction for the contribution, contending the trust lacked a corpus on its creation date.

Procedural History

The Commissioner of Internal Revenue determined a deficiency in Tallman's income tax for its fiscal year ending September 30, 1952, disallowing the deduction for its contribution to the profit-sharing plan. Tallman contested this disallowance, and the case was brought before the United States Tax Court. The Tax Court ruled in favor of Tallman, allowing the deduction.

Issue(s)

1. Whether the profit-sharing trust had a valid corpus on September 30, 1952.

2. Whether the subsequent payment of the note within the 60-day period provided under the statute could cure any defect in the initial corpus.

Holding

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1. Yes, because the demand promissory note delivered by Tallman to the trust constituted a valid trust corpus under New York law, as the note was considered issued for valuable consideration.

2. Yes, because the cash payment within the 60-day grace period, along with the note, provided the trust with a corpus during the fiscal year and was sufficient for the deduction.

Court's Reasoning

The court considered whether the demand note constituted a valid trust corpus under New York law. The court cited Judge Learned Hand's opinion in *Dejay Stores v. Ryan*, which stated, "There was (1) a trustee, (2) a res, (3) a transfer of the res to the trustee, (4) and a complete agreement upon all the terms on which the trustee should hold the res." The court determined that the note, as a negotiable instrument, fulfilled the requirement for a trust corpus because it was issued for valuable consideration. The court reasoned that the subsequent cash payment within the statutory 60-day period further validated the trust. The court found no requirement that the trust instrument must be set up within the fiscal year, provided every element of a trust came into existence before the end of the grace period. The court also noted that the Commissioner's previous rulings indicated that a promise supported by consideration could constitute a trust corpus.

Practical Implications

This case clarifies the requirements for establishing a valid profit-sharing trust and claiming related tax deductions. It underscores the importance of ensuring a trust has a valid corpus, which can include a demand promissory note, especially when the note is issued for valuable consideration. The case also confirms that contributions made within the 60-day grace period can validate the trust. It highlights the interplay between state law (New York in this instance) and federal tax law when determining the validity of trusts. Legal practitioners should ensure that profit-sharing trusts are established with a valid corpus and that contributions are made within the permitted timeframes. This ruling is particularly relevant for businesses employing accrual accounting methods and seeking to establish or maintain qualified retirement plans.

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