35 T.C. 393 (1960)

When a transferee receives assets exceeding the transferor's tax liabilities, federal law, not state law, governs the interest on those liabilities, and interest accrues from the original tax due date.

Summary

Leo Lowy, as transferee of assets from American Rolbal Corporation, contested the start date for interest on the corporation's tax deficiencies. The Tax Court ruled that because the transferred assets significantly exceeded the tax liabilities, federal law (specifically section 292 of the 1939 Internal Revenue Code) dictates the interest accrual. Interest begins from the original due dates of the corporate taxes, not from the date the IRS issued the transferee liability notice to Lowy. The court clarified that state law only becomes relevant for interest on the transferred assets themselves when those assets are insufficient to cover the federal tax liabilities. In this case, with ample assets, federal law exclusively governs the interest on the tax deficiency.

Facts

American Rolbal Corporation had outstanding tax deficiencies for 1942 and 1943, including fraud and failure-to-file penalties. Leo Lowy, the sole stockholder, received corporate assets worth over $1 million on December 31, 1943. The Tax Court had previously adjudicated the corporation's tax liabilities, a decision affirmed by the Second Circuit. On June 2, 1955, the IRS issued a notice to Lowy asserting transferee liability for the corporation's tax deficiencies, including interest. Lowy conceded liability for the taxes and penalties but disputed the date from which interest should be calculated, arguing it should start from the notice date, while the IRS contended it should be from the original tax due dates.

Procedural History

The Commissioner of Internal Revenue assessed deficiencies against American Rolbal Corporation for 1942 and 1943. The Tax Court upheld these deficiencies, and the Second Circuit affirmed. Subsequently, the Commissioner issued a notice of transferee liability to Leo Lowy. Lowy petitioned the Tax Court to contest the interest component of his transferee liability.

Issue(s)

1. Whether, as a transferee of assets, Lowy is liable for interest on the transferor corporation's tax deficiencies.

2. If so, whether the interest on the transferee liability should be calculated from the original due dates of the transferor corporation's taxes under federal law, or from the date of the notice of transferee liability under state law, given that the

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transferred assets exceeded the tax liabilities.

Holding

1. Yes, Lowy, as a transferee, is liable for interest on the transferor corporation's tax deficiencies.

2. Yes, because federal law (section 292 of the 1939 I.R.C.) governs the interest on tax deficiencies, and since the transferred assets were substantially greater than the liabilities, interest accrues from the original tax due dates (March 15, 1943, and March 15, 1944), not the date of the transferee notice. State law does not apply to the determination of interest on the federal tax deficiency in this context.

Court's Reasoning

The Tax Court reasoned that federal statute, specifically section 292 of the 1939 I.R.C., explicitly dictates that interest on tax deficiencies runs from the tax due date. While transferee liability itself is rooted in state law, the nature and extent of the underlying tax debt, including interest, are determined by federal law. The court emphasized that when transferred assets are sufficient to cover the tax liabilities, the federal statute's interest provisions are controlling. The court distinguished situations where transferred assets are insufficient, in which case state law might govern interest on the assets themselves as compensation for their use by the transferee. However, in this case, with ample assets, the court held that federal law exclusively determines the interest on the tax deficiency, stating, "Interest upon the amount determined as a deficiency * * * shall be collected as part of the tax, at the rate of 6 per centum per annum from the date prescribed for the payment of the tax * * *." The court concluded that applying state law to determine the interest accrual on the federal tax deficiency is inappropriate when federal law directly addresses the issue and the assets are sufficient.

Practical Implications

Lowy v. Commissioner establishes that in cases of transferee liability where the transferred assets are sufficient to cover the transferor's federal tax liabilities, the calculation of interest on those liabilities is governed by federal tax law, not state law. This decision clarifies that attorneys should primarily focus on federal statutes, such as section 292 of the I.R.C., to determine the commencement date for interest accrual in such transferee cases. The case highlights a distinction: state law might become relevant only when the transferred assets are insufficient to satisfy the federal tax debt, potentially concerning interest on the assets themselves as a remedy under state law. For practitioners, this means that when advising clients on transferee liability with sufficient assets, the interest calculation on the underlying tax deficiency is a matter of federal tax law, accruing from the original tax due date, regardless of state law considerations.

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