Wilkins v. Commissioner, 54 T. C. 362 (1970)

Distributions from qualified profit-sharing trusts during a strike are taxable as ordinary income, not capital gain, unless they are made on account of a separation from service.

Summary

In Wilkins v. Commissioner, Ford E. Wilkins sought to treat a distribution from his employer's profit-sharing trust as long-term capital gain. The distribution occurred after a strike and subsequent collective bargaining agreement that excluded union members from the trust. The court held that the distribution was taxable as ordinary income because Wilkins' strike participation did not constitute a "separation from service" under Section 402(a)(2) of the Internal Revenue Code. Furthermore, the distribution was made due to the collective bargaining agreement, not any separation. This case clarifies the tax implications of trust distributions related to labor disputes and collective bargaining agreements.

Facts

Ford E. Wilkins was employed by Cupples Products Corp. and participated in the company's profit-sharing trust. In June 1966, Wilkins and other hourly employees went on strike, which lasted until August 4, 1966. During negotiations, the union requested the termination of the profit-sharing plan for its members, leading to an amendment of the trust effective August 31, 1966. On September 22, 1966, Wilkins received a distribution of $837. 40 from the trust. He reported half of this amount as capital gain on his 1966 tax return, but the IRS treated the entire distribution as ordinary income.

Procedural History

Wilkins filed a petition with the U. S. Tax Court challenging the IRS's determination of the deficiency in his 1966 income tax. The Tax Court heard the case and issued its opinion on February 26, 1970, ruling in favor of the Commissioner.

Issue(s)

1. Whether Wilkins' participation in a strike constituted a "separation from the service" under Section 402(a)(2) of the Internal Revenue Code.
2. Whether the distribution from the profit-sharing trust was made "on account of" a separation from service.

Holding

1. No, because a strike does not constitute a "separation from the service" as it is merely a temporary interruption of employment.
2. No, because the distribution was made due to the collective bargaining

agreement that excluded union members from the trust, not due to any separation from service.

Court's Reasoning

The court interpreted "separation from the service" under Section 402(a)(2) to mean a complete severance of the employment relationship, such as death, retirement, or termination. The court cited previous cases like Estate of Frank B. Fry and United States v. Johnson to support this interpretation. It found that Wilkins' participation in the strike did not sever his connection with the employer, as he remained an employee and returned to work after the strike. Additionally, the court determined that the distribution was made pursuant to the collective bargaining agreement and the subsequent amendment to the trust, not due to any separation from service. The court referenced Whiteman Stewart and other cases to support its conclusion that the distribution was not made "on account of" a separation.

Practical Implications

This decision impacts how distributions from qualified profit-sharing trusts are treated during labor disputes. It establishes that a strike does not constitute a separation from service for tax purposes, and distributions made due to collective bargaining agreements rather than separations are taxable as ordinary income. Legal practitioners should advise clients that such distributions cannot be treated as capital gains unless there is a clear separation from service. This ruling may affect negotiations involving profit-sharing plans, as unions and employers must consider the tax implications for employees. Subsequent cases like Estate of George E. Russell have applied this principle, reinforcing the distinction between distributions made due to labor agreements and those due to separations from service.

