Precision Industries, Inc. v. Commissioner, 64 T. C. 901 (1975)

For a contribution to a profit-sharing plan to be deductible in a given year, the liability must be fixed and accruable by the end of that year.

Summary

Precision Industries, Inc. , an accrual basis taxpayer, sought to deduct a $16,200 contribution to its profit-sharing plan for the fiscal year ending March 31, 1970. The plan, adopted mid-year, allowed the company's board to determine annual contributions without a set formula. The court held that the liability for the contribution was not fixed by the fiscal year-end because the board did not formally decide on the amount until after the year closed. As a result, the contribution was not deductible in the fiscal year 1970, emphasizing the necessity for a clear, fixed liability for tax deductions under accrual accounting.

Facts

Precision Industries, Inc. , an Ohio corporation using the accrual method of accounting, adopted a profit-sharing plan on March 10, 1970, during its fiscal year ending March 31, 1970. The plan did not prescribe a contribution formula, instead allowing the board of directors to determine the contribution amount annually. Precision contributed $100 to the plan at adoption and later added $16,200 on July 27, 1970, which was the maximum deductible amount for that year. The company claimed a deduction for the full $16,300 on its tax return for the fiscal year ending March 31, 1970.

Procedural History

The Commissioner of Internal Revenue disallowed the deduction of $16,200, asserting that Precision had not incurred a fixed liability by the end of the fiscal year. Precision petitioned the U. S. Tax Court to challenge this disallowance.

Issue(s)

1. Whether Precision Industries, Inc. , incurred a fixed liability to contribute $16,200 to its profit-sharing plan by the end of its fiscal year ending March 31, 1970, such that the amount was accruable and deductible in that year.

Holding

1. No, because Precision's liability to contribute the $16,200 was not fixed by the end of its fiscal year ending March 31, 1970, as there was no formal board resolution or action taken to establish the amount before that date.

Court's Reasoning

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The court applied the rule that for an accrual basis taxpayer to deduct a contribution to a profit-sharing plan in a particular year, the liability must be fixed and accruable by the end of that year. The court noted that under section 404(a)(6) of the Internal Revenue Code, a taxpayer on the accrual basis can deduct contributions made within the time prescribed for filing the return if the liability was incurred during the taxable year. However, the court found that Precision did not meet this requirement. The profit-sharing plan required the board to determine the contribution amount before the end of each year and accrue it on the company's books. No such determination or accrual occurred before March 31, 1970. The court rejected the company's argument that oral representations to employees about potential contributions could establish a fixed liability, especially since the plan lacked a fixed contribution formula. The court emphasized the need for clear evidence of a fixed liability, which was absent in this case.

Practical Implications

This decision underscores the importance of formal action by a company's board of directors to establish a fixed liability for contributions to a profit-sharing plan before the end of the fiscal year for those contributions to be deductible. It affects how companies on an accrual basis should manage their profit-sharing contributions to ensure tax deductibility. The ruling suggests that informal or oral commitments are insufficient to establish a fixed liability under the tax code. Companies should implement formal procedures and document board decisions regarding contributions well before the fiscal year-end to secure deductions. Subsequent cases have reinforced this principle, requiring clear documentation of liability fixation for deductions under similar circumstances.

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