Guren v. Commissioner, 66 T. C. 118 (1976)

A demand promissory note does not constitute "payment" for purposes of claiming a charitable contribution deduction under section 170(a)(1) of the Internal Revenue Code.

Summary

In Guren v. Commissioner, the Tax Court ruled that Sheldon Guren could not claim a charitable contribution deduction for a $25,000 demand promissory note given to the United Jewish Appeal in 1971, as it did not constitute "payment" under section 170(a)(1). Guren, using the cash method of accounting, argued the note should be deductible in the year issued, despite actual payment occurring in 1972. The court held that for cash method taxpayers, actual payment in cash or its equivalent is required for a deduction, not merely the issuance of a promissory note, regardless of the note's enforceability or the maker's ability to pay.

Facts

On December 1, 1971, Sheldon Guren made a conditional pledge of $25,000 to the 1972 Jewish Welfare Fund Appeal, with $15,000 firm and $10,000 contingent. On December 30, 1971, he executed a non-interest-bearing cognovit demand promissory note for the full $25,000 in favor of United Jewish Appeal, Inc. Guren had substantial net worth and the financial ability to pay the note on demand. The note was paid in installments in 1972, totaling $25,000 by October 2, 1972. Guren claimed the note as a charitable deduction on his 1971 tax return.

Procedural History

The Commissioner of Internal Revenue disallowed the deduction, asserting the contribution was not paid in 1971. Guren petitioned the U. S. Tax Court, which heard the case and issued its opinion on April 19, 1976, ruling in favor of the Commissioner.

Issue(s)

1. Whether the delivery of a demand promissory note to a charity constitutes "payment" within the meaning of section 170(a)(1) of the Internal Revenue Code, thereby entitling the taxpayer to a charitable contribution deduction in the year the note was delivered.

Holding

1. No, because the term "payment" under section 170(a)(1) requires actual payment in cash or its equivalent, not merely the issuance of a promissory note, even if the note is enforceable and the maker has the ability to pay it on demand.

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Court’s Reasoning

The Tax Court relied on established precedent that under the cash method of accounting, actual payment is required for a deduction. The court cited *Norman Petty* (40 T. C. 521 (1963)), where it was held that a promissory note does not constitute actual payment. The court emphasized that Congress intended for both cash and accrual method taxpayers to have the same requirement of actual payment for charitable deductions. The court also noted that while a promissory note may be considered property once transferred, it does not constitute payment between the maker and the payee. This interpretation was upheld by the Seventh Circuit in *Don E. Williams Co. v. Commissioner* (527 F. 2d 649 (7th Cir. 1975)). The court concluded that Guren’s financial ability to pay the note did not change the requirement for actual payment to claim a deduction.

Practical Implications

This decision clarifies that for cash method taxpayers, a charitable contribution deduction cannot be claimed in the year a demand promissory note is issued; actual payment must occur within the taxable year. This ruling impacts how taxpayers plan their charitable giving, as they must ensure payments are made by the end of the tax year to claim deductions. It also affects charities, which may need to adjust their fundraising strategies to encourage timely payments. Subsequent cases have generally followed this precedent, reinforcing the requirement for actual payment in cash or its equivalent for charitable deductions.

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