

## ***Nordberg v. Commissioner, 79 T. C. 664 (1982)***

Money received under a claim of right without restriction as to its disposition is taxable income, even if there is a contingent obligation to repay it.

### **Summary**

In *Nordberg v. Commissioner*, the Tax Court ruled that a \$100,000 distribution received by Paul Nordberg was taxable income under the claim of right doctrine. Nordberg received the funds as a partial payment on subordinated notes he held in Scarburgh Co. , Inc. , which was involved in the salad oil scandal. Despite a conditional repayment obligation, Nordberg spent the money freely without setting aside funds for repayment. The court held that the funds were taxable in the year received because they were received under a claim of right and Nordberg made no provisions for repayment, emphasizing the annual accounting principle of income tax.

### **Facts**

Paul Nordberg received \$100,000 in 1978 from Scarburgh Co. , Inc. , a company involved in the salad oil scandal. The payment was a distribution related to subordinated notes Nordberg had purchased. The distribution agreement required noteholders to repay the funds upon demand if certain claims were asserted against Scarburgh or its officers. Despite this contingency, Nordberg spent the money on personal expenses, including student loan repayment, home improvements, and a vacation. He did not segregate the funds or make arrangements to repay them if demanded.

### **Procedural History**

The Commissioner of Internal Revenue determined a tax deficiency against Nordberg for 1978, treating the \$100,000 as taxable income. Nordberg filed an amended return claiming the payment was a loan, not income, and sought a refund. The Tax Court upheld the Commissioner's determination, applying the claim of right doctrine.

### **Issue(s)**

1. Whether the \$100,000 received by Paul Nordberg in 1978 was taxable income under the claim of right doctrine.
2. Whether the conditional repayment obligation negated the application of the claim of right doctrine.

### **Holding**

1. Yes, because the funds were received under a claim of right without restriction as to their disposition, and Nordberg made no provisions for repayment.

2. No, because the obligation to repay was contingent, not fixed, and did not alter the taxability of the funds in the year received.

### **Court's Reasoning**

The court applied the claim of right doctrine, established in *North American Oil Consolidated v. Burnet*, which holds that money received under a claim of right, without restriction as to its disposition, is taxable income in the year received, even if there is a contingent obligation to repay it. The court noted that Nordberg did not recognize a fixed obligation to repay or make provisions for repayment, as required to avoid the doctrine's application. Nordberg's rapid expenditure of the funds and lack of specific plans to repay them if demanded supported the court's conclusion that the funds were received under a claim of right. The court also rejected Nordberg's argument that the distribution was a loan, citing the absence of typical loan characteristics such as a fixed maturity date and interest obligation. The court emphasized the annual accounting principle of income tax, stating that the mere possibility of future repayment does not negate the taxability of funds in the year received.

### **Practical Implications**

This decision reinforces the application of the claim of right doctrine in cases involving contingent repayment obligations. Taxpayers receiving funds under similar circumstances should be aware that such funds are likely taxable in the year received, even if there is a possibility of future repayment. This ruling may affect how taxpayers report and plan for such distributions, particularly in complex financial arrangements. Practitioners should advise clients to carefully document any fixed repayment obligations and make provisions for repayment if they wish to avoid the immediate taxability of received funds. The decision also highlights the importance of the annual accounting principle in income tax law, reminding taxpayers and practitioners of the need to report income in the year it is received.