Apkin v. Commissioner, 85 T. C. 706 (1985)

Interest accrued on Series E U. S. savings bonds prior to the bondholder's death must be included in the gross income of the person who redeems the bonds after the bondholder's death, as income in respect of a decedent.

Summary

In Apkin v. Commissioner, the Tax Court held that Philip Apkin must include in his gross income the interest accrued on Series E U. S. savings bonds from the time of their purchase by his mother, Dora Apkin, until her death. Dora had purchased the bonds as co-owner with Philip, and upon her death, he became the sole owner. The court ruled that this interest constituted income in respect of a decedent under IRC Section 691, as Dora did not elect to report the interest annually under IRC Section 454. This decision underscores the application of IRC Section 691 to accrued interest on savings bonds, impacting how such income is taxed upon redemption by successors.

Facts

Dora Apkin purchased 49 Series E U. S. savings bonds between 1948 and 1959, co-owned with her son, Philip Apkin. She did not file income tax returns during those years, as her income, including the interest from the bonds, did not require her to do so. Dora held the bonds until her death in 1979, after which Philip became the sole owner. He redeemed the bonds in 1981, receiving the accrued interest from the date of purchase to redemption. Philip reported only the interest accrued after his mother's death on his 1981 tax return, leading to a dispute with the IRS over the taxability of the pre-death accrued interest.

Procedural History

The IRS assessed a deficiency against Philip Apkin for failing to report the full amount of interest received upon redemption of the bonds. Philip conceded the taxability of the interest accrued post-death but contested the inclusion of pre-death interest. The case was submitted to the Tax Court fully stipulated, which then ruled in favor of the Commissioner.

Issue(s)

1. Whether the interest accrued on Series E U. S. savings bonds prior to the bondholder's death must be included in the gross income of the person who redeems the bonds after the bondholder's death.

Holding

1. Yes, because the interest accrued on the bonds prior to Dora Apkin's death constitutes income in respect of a decedent under IRC Section 691, and Dora did not

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elect to include the interest in her income annually under IRC Section 454.

Court’s Reasoning

The court applied IRC Section 691, which mandates that income in respect of a decedent, not properly includable in the decedent’s income at the time of death, must be included in the gross income of the recipient upon receipt. Dora Apkin did not report the interest on the bonds during her lifetime, nor did she elect under IRC Section 454 to include the interest in her income annually. The court rejected Philip’s reliance on Helvering v. Horst, noting that IRC Section 691 specifically addresses the taxation of income in respect of a decedent, which Congress enacted to override prior judicial interpretations. The court emphasized that Dora’s failure to file tax returns did not preclude her from making an election under Section 454, and her inaction resulted in the interest being taxable to Philip upon redemption.

Practical Implications

This decision clarifies that interest accrued on Series E U. S. savings bonds before the bondholder’s death is taxable to the person who redeems the bonds as income in respect of a decedent. Legal practitioners should advise clients who inherit such bonds to report all accrued interest upon redemption, regardless of when it was earned. This ruling impacts estate planning, as it may influence decisions about the timing of bond redemption and the tax implications for heirs. It also serves as a reminder of the importance of making elections under IRC Section 454 if bondholders wish to report interest annually. Subsequent cases have followed this precedent, reinforcing the application of IRC Section 691 to similar situations.

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