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Income Taxation--Contribution to Employees' Savings Trust

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(1962) (contract cancelable upon thirty days notice by either party), and *Desrosiers v. Commissioner*, 21 CCH TAX CT. MEM. 264 (1962) (contract terminable by either party on thirty days notice after the first one hundred twenty days). In *Utah Alloy Ores, Inc. v. Commissioner*, 33 T.C. 917 (1960), the contracts were for terms of one year unless the operator failed to work the claim but depletion was disallowed since a term of one year was not sufficient to mine the claims to exhaustion. Thus, it would appear that there must be a reasonable probability that coal will be mined to exhaustion under the contract before the courts will allow a depletion allowance to taxpayer mining under the contract.

The *Parsons* case, *supra*, laid down seven guide-lines for aid in interperting an "economic interest". Subsequent decisions have interpreted the *Parsons* case to mean that stripping rights terminable on minimal notice are not a sufficient interest to support depletion, and that the factor of terminability should be given top priority in the court's determination of an "economic interest". In accord with this interpretation, the court held in the principal case that a contract conferring the right to terminate the contract only on grounds of default by the strip miner or lack of profitability to the lessee was not an agreement terminable at will or on short notice. The court based its decision almost entirely on terminability as the *Parsons* case was similar in every instance except for the limited right of termination. In the future, the courts will look to the terminability of the contract to determine if the strip miner has an "economic interest". It would appear that the test of terminability of a contract to depletion cases may eliminate much of the vagueness and uncertainty that has previously existed.

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Income Taxation—Contribution to Employees' Savings Trust

Action for refund of income tax. *P* sought deduction from gross income as a business expense money contributed by transfer to employee savings trust fund. The three year trust, established in 1950, permitted employees to join through wage withholdings with *P* matching all contributions equally. Under no circumstance was *P* to receive back sums contributed. If his employment was terminated because of death, retirement, disability, or layoff, the employee received the amount set aside from wages plus the matched amount of *P*. If terminated voluntarily or discharged for cause, the employee would receive only his contribution. Contributions and earnings were distributed January 2, 1953, two days after termination of the trust. Tax Commissioner disallowed deduction. *Held,* reversed. Statute allows as deduction money paid to certain trust funds during the taxable year when paid to employees if nonforfeitable by employees at that time. *Mississippi River Fuel Corp. v. United States,* 314 F.2d 953 (Ct. Cl. No. 180-60, 1963).

The principal case was decided upon the same reasoning and under a substantially similar factual situation as *Russell Mfg. Co. v. United States,* 146 Ct. Cl. 833, 175 F.Supp. 159 (1959). The ruling in both cases turned upon the interpretation of INT. REV. CODE of 1939, § 23 (p) (1) (D) (now INT. REV. CODE of 1954, § 404 (a) (5)). The result in both instances is contra to earlier rulings by the Commissioner of Internal Revenue. In order to understand the problems involved, it is necessary to investigate the position taken by the Commissioner in both cases.

In 1942, § 23 (p) (now INT. REV. CODE of 1954, § 404) became the exclusive section for deductions of this nature. The 1942 amendment was designed to grant tax advantages to encourage pension, profit-sharing, and stock bonus plans which could qualify under certain non-discriminatory requirements set forth in § 165 (a) (now INT. REV. CODE of 1954, § 401). If an employer could qualify under these requirements, he was given favorable treatment in § 23 (p) (1) (A), (B), or (C). Otherwise, it was necessary to "qualify" under § 23 (p) (1) (D) or no deduction would be allowed. *Russell Mfg. Co. v. United States, supra.*

INT. REV. CODE of 1939, § 23 (p) (1) (D) provided:

> "If contributions are paid by an employer to or under a stock bonus, pension, profit-sharing, or annuity plan, or if compensation is paid or accrued on account of any employee under a plan deferring the receipt of such compensation, such contributions or compensation shall not be deductible under subsection (a) but shall be deductible, if deductible under subsection (a) without regard to this subsection, under this subsection but only to the following extent:
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> "(D) In the taxable year when paid, if the plan is not one included in paragraphs (A), (B), or (C): if the employees'

rights to or derived from such employer's contribution or such compensation are nonforfeitable at the time the contribution or compensation is paid."

The Treasury Department interpreted § 23 (p) (1) (D) to mean "if an amount is paid during the taxable year but the rights of the employee therein are forfeitable at the time the amount is paid, no deduction is allowed for such amount for any taxable year." Treas. Reg. 111, § 29.23(p)-11 (1943), as amended, T.D. 5666, 1948-2 CUM. BULL. 46 (now Treas. Reg. § 1.404(a)-12 (1956)). The Commissioner construed the words of § 23 (p) (1) (D) "in the taxable year" to mean "in the taxable year when paid by the employer." In the principal case at the time the contributions were paid by the employer, the employees' rights were clearly forfeitable; therefore, the Commissioner argued the plan did not "qualify" under § 23 (p) (1) (D). The court in overruling this interpretation said that while it is clear that Congress intended to give certain tax advantages to plans qualifying under § 165 (a) (now INT. REV. CODE of 1954, § 401) it did not intend to disallow deductions as ordinary and necessary business expenses compensation paid under plans that "qualify" under § 23 (p) (1) (D). That this plan did "qualify" under § 23 (p) (1) (D) was clear to the court, the rights being nonforfeitable in the taxable year when paid to the employees. In *Russell Mfg. Co. v. United States, supra,* the court construed the statute to mean that compensation paid to employees shall be deductible in the year of distribution if nonforfeitable in that year. The statute provided that *compensation paid to the employee* shall be deductible; whereas the Commissioner relied upon the wording which said that *contributions paid by the employer* shall be deductible.

The Commissioner further argued that there could be no deduction under the plan in the principal case if the statute meant "in the taxable year when paid by the employer," becauce payment was made by the trustee. The court felt, however, that payment by a trustee had been anticipated. The statute refers to "contributions paid by the employer," but in using the term compensation, it fails to say "paid by the employer."

In 1954 Congress failed to enact a provision which would have changed § 23 (p) (1) (D) to read "in the taxable year when the amount is actually distributed or made available to a distributee."

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Upon arguing legislative intent, the Commissioner said that apparently Congress was satisfied with the section as it existed and with the treasury regulation. As to the rejection of this revision, the court found that the change would not only have specifically allowed deductions as in this situation; it would also have allowed deductions in the year in which it was set aside by the employer, even though nonforfeitable at that time. It was not possible to determine what Congress was approving or disapproving by rejecting such a revision. *Russell Mfg. Co. v. United States, supra.*

In the principal case, the court placed heavy emphasis upon public policy. It felt that to deny such a deduction would be to penalize the employer with progressive plans and to encourage the use of less favorable ones. If the employer, for example, merely agreed to pay the money, but did not set it aside, his contributions when made would be clearly deductible. Rev. Rul. 525, 1955–2 CUM. BULL. 543 would permit a deduction for just such a plan. Thus to follow the treasury regulation and disallow a deduction in the principal case would have created the anomolous situation where under the regulations the employer who gives the employees the lesser protection is afforded the greater tax benefit.

It appears that if such a case again reaches the Commissioner, the same conflict will arise. The Commissioner is not bound by the Court of Claims, and there is no apparent evidence that the former has any intention of altering the regulation. This is certainly needless litigation with which the taxpayer should not be burdened. The decision of the court does not weaken the advantages legislatively granted to qualifying funds. Nor is there any apparent reason why allowance of these deductions would work to give a taxpayer undue advantage. The court's reasoning appears to be the better interpretation, and leaves two alternatives: The Commissioner should acquiesce; or Congress should be encouraged to enact a more clearly worded statute.

Charles Ellsworth Heilmann

Legislation—Admission of Extrinsic Evidence to Show Irregularities in Passage of Bill

Relators, both corporations, were indicted under a 1963 West Virginia statute which barred certain business activities on Sunday. By writ of prohibition brought against the county judge and