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Income-Tax Department

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Income-Tax Department

EDITED BY STEPHEN G. RUSK

The matter of most absorbing interest at present to accountants giving their attention to the subject of federal taxes is the decision of the United States supreme court that stock dividends are not taxable as income.

This interest is accentuated by reading the decision delivered by Justice Pitney and by the lucid definitions contained therein, as, for instance, the definitions of income and of the difference between a true stock dividend and other dividends.

The latter follows:

"A 'stock dividend' shows that the company's accumulated profits have been capitalized, instead of distributed to the stockholders, or retained as surplus available for distribution in money or in kind should opportunity offer. Far from being a realization of profits of the stockholder, it tends rather to postpone such realization, in that the fund represented by the new stock has been transferred from surplus to capital, and is no longer available for actual distribution."

It would seem that if accountancy's terminology were adequate to express, in a word or phrase, precisely the transaction described in the above quotation, and the particular language describing it had become common, much of the confusion of mind, out of which grew the taxing of so-called stock dividends as income, would not have been present.

This is only one of many instances which show the necessity for expansion of the terminology of accountancy.

Accountants generally have found it difficult in many instances to express their thoughts intelligibly to the lay mind. This difficulty is sometimes occasioned by the lack of knowledge upon the part of the one with whom the accountant is dealing, as to the fundamental fact that all transactions in business represent an exchange of values. It is more often occasioned by the fact that the lay mind does not comprehend the technical terms of accountancy, and this lack of knowledge is emphasized by the want of precise language with which to express thoughts related to accounting.

Many a member of the profession has experienced difficulty in making clear to a jury some matter of considerable moment because of the lack of adequate language with which to clothe his thought.

Upon consideration of the matter of terminology, it would seem to be the duty of an accountant first to consult his own vocabulary, purge it of inaccuracy and learn the exact meaning of each word contained therein, and thereby be prepared to define his meaning in clear and non-technical language.

These thoughts as to the limitations of accounting terminology are brought to mind, again, by the language of paragraph 3-a of the regulation

Income-Tax Department

contained in mimeograph 2436, entitled "Further instructions relating to overpayment of taxes of stock dividends."

The above-mentioned paragraph reads as follows:

"Whether the dividend consists of the stock of the corporation distributing the dividend to the taxpayer, or of stock of another corporation acquired by the distributor."

It would seem from a superficial reading of the above paragraph, and without the information contained in the description of a stock dividend, as contemplated by the majority opinion of the United States supreme court, quoted above, that stock dividends include a distribution by a corporation of any stock of another corporation it may have among its assets.

The particularly concise description of a stock dividend contained in the supreme court decision should prevent misunderstanding about this matter, as the application of the above principle to the particular case that may be before the taxpayer or his accountant will remove all doubt as to whether the distribution of stock of another corporation constitutes a taxable stock dividend or not.

It seems to be the duty of the accountancy profession to coin a word or phrase to express the exact meaning of the transaction wherein a distribution of shares of capital to stockholders constitutes simply a transfer of surplus to the capital stock of a corporation.

(Mim. 2436, March 12, 1920)

Further instructions relative to overpayments of taxes on stock dividends

Supplement office telegram of March 9, 1920, and I. T. Mim. 2429, you are advised that a claim for credit on form 47A for payment of tax on stock dividends is to be accepted as a suspension of immediate collection of tax due only—

- (1) Against income or income and excess profits taxes due and unpaid.
- (2) If amount claimed as a credit does not exceed the amount of tax collected on the stock dividend less any additional tax due and unpaid upon the sale of stock received as a dividend or stock upon which the dividend was declared. (The basis of determining the gain or loss upon sale of stock is stated in regulations 45, article 1547, paragraphs 1 and 2. That article provides that the cost of each share of stock is the quotient of the cost of the old stock divided by the number of old and new shares added together.)
- (3) When accompanied by an affidavit of the taxpayer (supported by statements from the corporation which distributed the dividends as to the amount distributed to the taxpayer and years in which the profits distributed were earned) covering the following information:
 - (a) Whether the dividend consists of stock of the corporation distributing the dividend to the taxpayer, or of stock of another corporation acquired by the distributor.
 - (b) The name of each corporation declaring, the declaration of, and the date of receipt by the taxpayer of, the stock dividends, the tax on which was paid and is covered by the claim.
 - (c) The year in which the stock dividend was included in the taxpayer's return of income.
 - (d) The number of shares the taxpayer received and the value placed upon the dividend in the return.
(If no sale of stock was made the taxpayer need not furnish the following information):
 - (e) If any sale has been made of stock of the corporation de-

The Journal of Accountancy

clearing the dividends, whether the stock be that acquired by a dividend, or upon which the dividend was declared, state—

- (1) The number of shares sold.
- (2) The selling price.
- (3) The date or dates of sale.
- (4) The portion, if any, of the selling price included as taxable profit in the return of net income for the year the sale was made and the item in the return under which the amount was reported.

(f) State how many shares of stock the taxpayer owned at the time he received the first stock dividend. How much that stock cost the taxpayer and the date the stock was acquired. (If acquired prior to March 1, 1913, state its value on that date and manner of determining the value.)

(g) State separately the dates from March 1, 1913, upon which you received stock dividends, the number of shares received on each date and the names of the corporations distributing the dividends.

The receipt or cancelled cheque covering the payment of tax involved in the claim should be attached to the claim.

(T. D. 2998, April 10, 1920)

Revenue Act of 1918

Deductions allowed: Charitable contributions, article 251, regulations No. 45 (amended)

Article 251 of regulations No. 45 is hereby amended to read as follows:

ART. 251. *Charitable contributions.*—Contributions or gifts within the taxable year are deductible to an aggregate amount not in excess of 15 per cent of the taxpayer's net income, including such payments, if made (a) to corporations or associations of the kind exempted from tax by subdivision (6) of section 231 of the statute, or (b) to the special fund for vocational rehabilitation under the vocational rehabilitation act of June 27, 1918. For a discussion of what corporations and associations are included within (a) see article 517. A gift to a common agency (as a war chest) for several such corporations or associations is treated like a gift direct to them. In connection with claims for this deduction there shall be stated on returns of income the name and address of each organization to which a gift was made, and the approximate date and the amount of the gift in each case. Where the gift is other than money the basis for calculation of the amount of the gift shall be the cost of the property, if acquired after February 28, 1913, or its fair market value as of March 1, 1913, is acquired prior thereto, after deducting from such cost or value the amount, if any, which has been or which should have been set aside and deducted in the current year and previous years from gross income on account of depreciation, and which has not been paid out in making good the depreciation sustained. A gift of real estate to a city to be maintained perpetually as a public park is not an allowable deduction. The proportionate share of contributions made by a partnership to corporations or associations of the kind included in (a) above and to the special fund for vocational rehabilitation specified in (b) may be claimed as deductions in the personal returns of the partners to an amount which, added to the amount of such contributions made by the partner individually, is not in excess of 15 per cent of the partner's net income computed without the benefit of the deduction for such contributions. However, the contributions made by the partnership shall not be deducted from its gross income in ascertaining the amount of its net income to be reported on form 1065 (revised). See article 321. This article does not apply to gifts by estates and trusts or corporations. See section 219 of the statute and articles 561 and 562.

This decision supersedes T. D. 2966 and T. D. 2977.