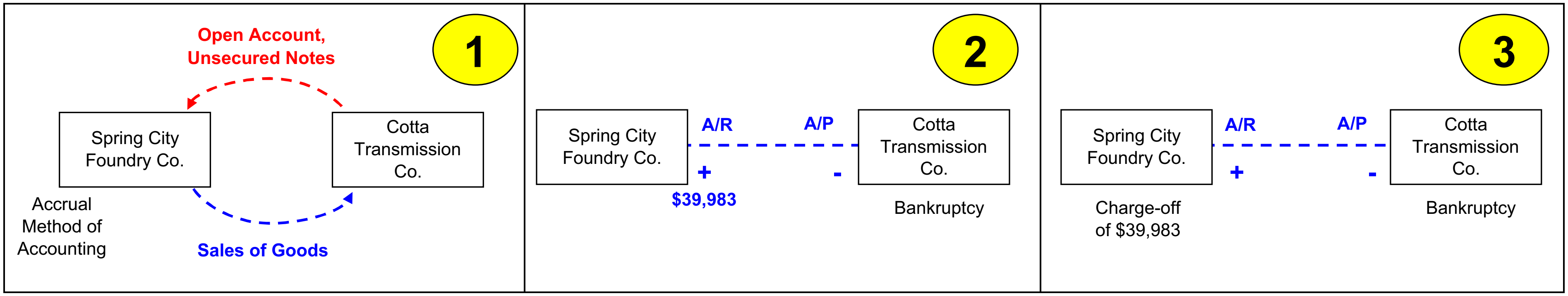
Spring City Foundry Co. v. Comm'r
292 U.S. 182 (1934)

No Partial Deduction for Bad Debt of Accrual Basis Taxpayer

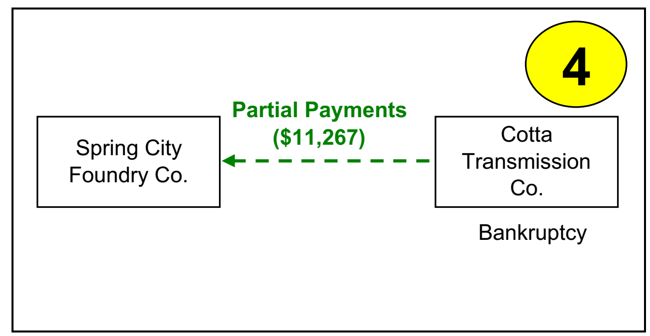
Initial Structure | **Cotta Bankruptcy (Dec. 23, 1920)** | **Debt Charge-off (1920)**



Spring City Foundry Co. ("Spring City") kept its books and filed its income tax return on the accrual basis. From March, 1920, to September, 1920, Spring City sold goods to the Cotta Transmission Company for which the latter became indebted in the amount of $39,983, represented by open account and unsecured notes. The Cotta Transmission Company filed for bankruptcy in 1920. In 1922 the receiver paid to creditors, including Spring City a dividend of 15% and, in 1923, a second and final dividend of 12.5%.

Spring City charged off on its books the entire debt in 1920, and claimed this amount as a deduction in its income tax return for that year. It included as income in its returns for 1922 and 1923 the dividends received in those years. The Commissioner disallowed the amount claimed as a deduction in 1920 but allowed a deduction in 1923 of $28,715, the difference between the full amount of the debt and the two dividends. The Board of Tax Appeals found that the debt was not entirely worthless at the time it was charged off.

Partial Recovery (1922 & 1923)



The statute authorized only the deduction of a debt ascertained to be worthless and charged off within the taxable year. It did not authorize the deduction of a debt which was ascertained to be partially worthless but was recoverable in part, the amount that was not recoverable being still uncertain. In 1923, on the winding up, the debt that then remained unpaid, after deducting the dividends received, was ascertained to be worthless and the deduction is allowed in that year. Spring City contended that "good business practice" forbade the inclusion in its assets of the account receivable in question or at least the part of it which was subsequently found to be uncollectible. However, questions relating to allowable deductions under the income tax act are quite distinct from matters which pertain to an appropriate showing upon which credit is sought.