APPENDIX A

Opinion of the United States Court of Appeals for the Ninth Circuit

United States Court of Appeals for the Ninth Circuit Karl F. Knetsch and Eva Fay Knetsch, Appellants, vs. United States of America, Appellee. No. 16,356, November 16, 1959.

Appeal from the United States District Court Southern District of California, Central Division.

Before: Stephens and Hamlin, Circuit Judges and Lindberg, District Judge, Stephens, Circuit Judge.

On December 11, 1953, the taxpayers purchased ten single premium annuity bonds from the Sam Houston Life Insurance Company. The purchase price of $4,004,000 was paid by a note for $4,000,000 and $4,000 in cash. The note was without recourse, and was secured by the annuity bonds. Interest on the note at three and one-half percent per annum, amounting to $140,000 was paid in cash. On December 16, $99,000 was sent to the taxpayers by Sam Houston as an additional loan, and the taxpayers paid the company $3,465 in interest. The bonds bore interest at the rate of two and one-half percent per annum, compounded annually. They matured in thirty years, and at that time would pay the taxpayers a monthly income of $43.00. Maturity could be accelerated or the bonds cashed in, at any time at the taxpayers' option. Mr. Knetsch was sixty when he made the purchase in 1953.

A similar transaction involving an interest payment of $147,105 was entered into for 1954, prior to March 1, when the provisions of the 1954 Internal Revenue Code affecting interest deductions for annuities went into effect.

These interest payments to Sam Houston were claimed as deductions in the taxpayers' 1953 and 1954 tax returns. When the deductions were disallowed, the deficiencies were paid under protest, and suit was brought in the District Court for refund. The District Court found, with ample support in the record, that the annuity bonds provided neither profit nor insurance; that they had been purchased solely to obtain a tax benefit; and that the alleged interest was not interest in fact, but the purchase price of a tax deduction. From that adverse judgment, the taxpayers have appealed.

This case arises under the Internal Revenue Code of 1939, which allows interest[1] as a deduction from gross income. The issue is whether such payments were payments of interest.

The problem has been carefully considered in United States v. Bond, 5th Cir., 258 F. 2d 577, which adopted the viewpoint of the taxpayer; and in Weller v. Commissioner, 3rd Cir., ... F. 2d ......, which agreed with the arguments of the government. We find ourselves in agreement with the opinion expressed by the judges of the Third Circuit.

The judgment of the District Court is affirmed.

(Endorsed:) Opinion. Filed Nov. 16, 1959.

Paul P. O'Brien, Clerk.

[1]Section 23(b).

APPENDIX B

United States Court of Appeals for the Ninth Circuit.

Karl F. Knetsch and Eva Fay Knetsch, Appellants, vs. United States of America, Appellee. No. 16,356.

Judgment

Appeal from the United States District Court for the Southern District of California, Central Division.

This cause came on to be heard on the Transcript of the Record from the United States District Court for the Southern District of California, Central Division, and was duly submitted.

On consideration whereof, it is now here ordered and adjudged by this Court, that the Judgment of the said District Court in this cause be, and hereby is affirmed.

(Endorsed) Judgment

Filed and entered: November 16, 1959

Paul P. O'Brien, Clerk

APPENDIX C

Pertinent Statutes Involved

(Internal Revenue Code of 1939)

"SEC. 23. DEDUCTIONS FROM GROSS INCOME

In computing net income there shall be allowed as deductions:

* * * * * * * *

(b) Interest. — All interest paid or accrued within the taxable year on indebtedness, except on indebtedness incurred or continued to purchase or carry obligations (other than obligations of the United States issued after September 24, 1917, and originally subscribed for by the taxpayer) the interest upon which is wholly exempt from the taxes imposed by this chapter."

"SEC. 24. ITEMS NOT DEDUCTIBLE

(a) General rule. — In computing net income no deduction shall in any case be allowed in respect of—

* * * * * * * *

(6) Any amount paid or accrued on indebtedness incurred or continued to purchase a single premium life insurance or endowment contract. For the purposes of this paragraph, if substantially all the premiums on a life insurance or endowment contract are paid within a period of four years from the date on which such contract is purchased, such contract shall be considered a single premium life insurance or endowment contract."

(Internal Revenue Code of 1954)

"SEC. 163. INTEREST

(a) General Rule. — There shall be allowed as a deduction all interest paid or accrued within the taxable year on indebtedness."

"SEC. 264. CERTAIN AMOUNTS PAID IN CONNECTION WITH INSURANCE CONTRACTS.

(a) General Rule.—No deduction shall be allowed for—

* * * * * * * *

(2) Any amount paid or accrued on indebtedness incurred or continued to purchase or carry a single premium life insurance, endowment, or annuity contract.

Paragraph (2) shall apply in respect of annuity contracts only as to contracts purchased after March 1, 1954."

APPENDIX D

Revenue Ruling 54-94

"Section 23 (b).—Deductions From Gross Income: Interest Regulations 118, Section 39.23 (b)-1: Interest. Rev. Rul. 54-94

Amounts claimed as "interest" in connection with certain so-called tax savings plans the purpose of which is to obtain an interest deduction for Federal income tax purposes are not deductible under section 23(b) of the Internal Revenue Code.

The attention of the Internal Revenue Service has been called to several situations where taxpayers are attempting to derive supposed tax benefits in connection with transactions designed to obtain interest deductions, for Federal income tax purposes. The question is whether the amounts designated as "interest" are deductible under section 23(b) of the Internal Revenue Code. The following two examples are illustrative:

Example 1. M Insurance Company has sold to the taxpayer an "annuity savings bond" (herein called the "bond") under the following conditions: Taxpayer "pays" to M a single cash premium of $100,000. To finance the premium, taxpayer pays $100 to M in cash and "borrows" $99,900 from M on a note that bears "interest" at the rate of 5 percent the first year and 3 percent thereafter. Taxpayer is not personally liable on the note, M's sole recourse being against the bond.

The bond has a maturity of 30 years. The "cash value" of the bond is $100,000 at the time the bond is issued and the "cash value" increases at the rate of 2½ percent a year compounded annually. At maturity taxpayer will be entitled to an annuity based on the "net cash value" of the bond at that time, *i.e.*, the excess of the "cash value" over the unpaid balance on taxpayer's

note to M. Taxpayer has the election at maturity to receive in cash the "net cash value" of the bond, and if taxpayer dies before maturity a beneficiary named by him is entitled to the then "net cash value".

(In some cases of this type it is provided that the taxpayer may surrender the bond at any time after 1 year and receive the "net cash value" thereof at such time. In some cases it is provided that the taxpayer may at any time borrow the "net cash value" on the bond on a nonrecourse note without surrendering the bond. In such cases there may be no "net cash value" at maturity and if so no annuity will be paid. In some cases it is provided that the taxpayer may at any time suspend payment of "interest" except to the extent of one-sixteenth of 1 percent without surrendering the bond, and the "cash value" of the bond will cease to increase during such suspension.)

Taxpayer claims that for Federal income tax purposes he may deduct the "interest" that he "pays" on the amount that he has "borrowed" on the bond, but that he realizes capital gain if he sells the bond. If this is so, and if taxpayer's surtax rate is sufficiently high, he will make a "profit" on the transaction notwithstanding that he pays 3 percent "interest" for a 2½ percent investment.

Example 2. In July 1952 taxpayer, an individual who is not a dealer in securities, purported to "purchase" $5,000,000 United States Treasury 1⅜ percent notes due March 15, 1954, at $99. Taxpayer financed the "purchase" by making a small down payment and purported to "borrow" the balance from the N Company, a dealer in securities, on a 2¼ percent nonrecourse note maturing March 15, 1954, depositing the Treasury notes as sole security for the principal and interest on the note. N thereupon sold short the same amount of Treasury notes of the same series, and with taxpayer's consent N covered the short sale with the deposited Treasury notes, thereby receiving the funds which it had "loaned" to the taxpayer. Taxpayer may direct the sale of his Treasury notes at any time. It is contemplated that at or before maturity taxpayer will direct the sale of his Treasury notes, and N will purchase $5,000,000 of such notes at the then market price to cover its short sale.

(In some cases of this type the taxpayer "pays" part of the "interest" on the note to N with money "borrowed" from N on an additional nonrecourse note.)

Since the taxpayer will "pay" more "interest" on the note to N than the total of the interest and appreciation that he will realize on the Treasury notes, taxpayer will realize no profit on the transaction apart from the effect of the transaction on his Federal income tax. However, taxpayer, whose surtax rate is sufficiently high, seeks to make a "profit" by deducting the "interest" that he pays from ordinary income and reporting the gain on the sale of the Treasury notes as capital gain.

It is the view of the Internal Revenue Service that amounts paid by taxpayer and designated as "interest" in the above examples are not interest within the meaning of section 23(b) of the Code, and are not deductible for Federal income tax purposes. Cf. Old Colony Railroad Co. v. Commissioner, 284 U. S. 552, Ct. D. 456, C. B. XI-1, 274 (1932), where the Supreme Court indicated that interest is "the amount which one has contracted to pay for the use of borrowed money."

In the above examples the amounts paid by the taxpayer are not in substance payments for the use of borrowed money. As a matter of substance the taxpayer does not borrow any money, hence there is no "debt" on which he pays "interest". An instrument that is called a "note" will not be treated as an indebtedness where it does not in fact represent an indebtedness. See Talbot

Mills v. Commissioner, 326 U. S. 521, Ct. D. 1660. C. B. 1946-1, 191; Matthiessen, et al. v. Commissioner, 194 Fed. 2d 659. In example 1, part of the "interest" paid by the taxpayer will be returned to him through the increase in the value of the bond and the remainder represents a payment to M for arranging the transaction so that taxpayer may derive a supposed tax benefit. If it is possible to regard the transaction as an annuity transaction at all, the "interest" payments in reality represent the premiums paid for the annuity. If the transaction is regarded as an endowment contract, the "interest" deduction is to be disallowed under section 24(a)(6) of the Code. In example 2, taxpayer in substance pays a sum of money to the N Company for arranging a transaction lacking commercial substance so that taxpayer may derive a supposed tax benefit; taxpayer does not expect to make a cash profit on the transaction independent of Federal income tax consequences, nor does taxpayer risk the money that he "borrows". Cf. Commissioner v. Transport Trading & Terminal Corp., 176 Fed. 2d 570, 572, where the Court of Appeals for the Second Circuit emphasized that "in construing words of a tax statute which describe commercial or industrial transactions we are to understand them to refer to transactions entered upon for commercial or industrial purposes and not to include transactions entered upon for no other motive but to escape taxation."

APPENDIX E

Schedule 1

KARL F. KNETSCH

Loss On Annuity And Loan Transactions

Loss on Transactions with Insurance Company		
Payments to Company		
For loan interest		$441,315.00
For part of annuity consideration		4,000.00
Total payments		$445,315.00
Receipts from company		
Proceeds of loans	$307,000.00	
Net cash surrender value	1,000.00	
Total receipts		308,000.00
Loss on Transaction with Insurance Company		$137,315.00
Federal Income Tax Benefits		
Reduction of tax by deduction of annuity loan interest		
1953 (see Notice of Deficiency)	$113,684.48	
1954 (see Notice of Deficiency)	119,613.20	
1955 (see Schedule 2)	123,236.17	
Total	356,533.85	
Tax upon surrender of annuities in 1956 (see Schedule 3)	269,869.21	
Federal Income Tax Benefit		$ 86,664.64
Net Loss on Annuity and Loan Transaction		$ 50,650.36

Note: The above statement does not give effect to state income tax consequences, if any.

Schedule 2

KARL F. KNETSCH

Federal Income Tax Benefit Attributable To Deduction Of Annuity Loan Interest In Return For Tax Year 1955

Net income per line 5 of 1955 return	$ 92,174.39
Add: Annuity Loan Interest Deducted	150,745.00
Adjusted net income	$242,919.39
50% of Net Long Term Capital Gain	8,608.79
Ordinary Income	$234,310.60
Tax on Ordinary Income	$165,176.43
Tax on Capital Gain	4,304.40
Total Tax	$169,480.83
Tax Per Return	46,244.66
Tax Attributable to Interest Deduction	$123,236.17

Schedule 3

KARL F. KNETSCH

Recomputation Of Federal Income Taxes
1956

		Without Annuity Transaction	With Annuity Transaction
Net taxable income per return		$ 6,074.58	$ 6,074.58
Add back deduction for surrender loss erroneously claimed in return if interest a proper deduction		138,315.00	138,315.00
Income upon Annuity Surrender			
Loan cancelled upon surrender			
December 11, 1953	$4,000,000		
December 16, 1953	99,000		
December 30, 1954	104,000		
December, 1955	104,000		
Total	$4,307,000		
Cash received upon surrender	1,000		
Total Received	$4,308,000		
Cost basis of annuity contract	4,004,000		
Gain on surrender			$304,000.00
Adjusted net taxable income		$144,389.58	$448,389.58
50% of long term capital gain		97.50	97.50
Ordinary income		144,292.08	448,292.08
Federal Income Tax			
On ordinary income		$ 47,716.58	$357,585.79
On capital gain		48.75	48.75
Total		$ 87,765.33	$357,634.54
			87,765.33
Federal Income Tax upon Surrender of Annuities			$269,869.21

APPENDIX F

Opinion of the United States Court of Appeals for the Third Circuit.

United States Court of Appeals for the Third Circuit.

Carl E. Weller, and Emily I. Weller, Petitioners, vs. Commissioner of Internal Revenue, Respondent. No. 12,-844.

W. Stuart Emmons, Petitioner, vs. Commissioner of Internal Revenue, Respondent. No. 12,854.

Filed September 9, 1959.

On Petitions for Review of Decisions of the Tax Court of the United States. Argued June 9, 1959.

Before Biggs, Chief Judge, and McLaughlin and Stanley, Circuit Judges.

By Staley, Circuit Judge.

These cases present identical questions of law,[1] namely, whether the Tax Court erred in holding that certain transactions involving prepayment of interest on annuity contract loans lacked substance so as not to be deductible as interest payments under Section 23(b) of the Internal Revenue Code of 1939.

The essential facts in the Emmons case, as found by the Tax Court, may be summarized as follows: Emmons, a cash basis taxpayer, purchased an annual premum annuity policy from Standard Life Insurance Company of Indiana in 1951. The policy required forty-one annual payments of $2,500 each, and the initial premium

[1]The cases were tried separately in the Tax Court and argued separately in this court; however, inasmuch as the Tax Court relied on the reasoning in the Emmons case as dispositive of both and as the facts differ in no material particulars, we will consider them together. Cases reported below: W. Stuart Emmons v. Commissioner of Internal Revenue, 31 T.C. No. 4 (1958), reviewed by full court (Tietjens, J., dissenting without opinion); Carl E. Weller v. Commissioner of Internal Revenue, 31 T.C. No. 5 (1958).

was paid on December 20, 1951, the date of issuance of the policy. The next day Emmons borrowed on his personal note $59,213.75 from the Girard Trust Corn Exchange Bank, pledging the annuity policy as collateral. This sum was credited to the account of the insurance company as a prepayment, at a discount, of all future premiums on the annuity policy.

On December 24, 1951, Emmons paid an additional $13,627.30 to Standard purportedly as interest to December 20, 1956, on an anticipated loan and received in return a receipt designating the payment as "Interest on Annuity Loan Contract No. AN-53651 to December 20, 1956." Following this payment the "cash or loan" value of the annuity contract had increased to $68,364. The petitioner received exactly that amount on December 27, 1951, and executed an agreement designated "Annuity Loan Agreement," providing for interest at 4 per cent per annum. That same day Emmons repaid the bank the earlier loan, utilizing part of the proceeds of the annuity loan.

One year later, on December 31, 1952, Emmons paid Standard the additional amount of $9,699.64 and received a receipt indicating the payment was for "Annuity Loan interest to December 20, 1959." The discount rate for prepayment of interest was 2.85 per cent. Thus, the second prepayment of interest increased the cash or loan value of the annuity contract to $73,728 and the increase of $5,364 was received by the taxpayer on the same day. Upon receipt, Emmons executed a second "Annuity Loan Agreement." At the date of the proceeding in the Tax Court the "loans" had not been repaid.

Emmons deducted the $13,627.30 payment as interest in his income tax return filed for 1951 and the $9,699.64 payment in his 1952 tax return. The Commissioner disallowed both deductions, insisting that (1) no indebtedness arose upon which payments of interest may be predicated, and (2) the payments constituted premiums rather than interest.

In arriving at its decision, which was reviewed by the full court, the Tax Court concluded that, despite the fact that the payments in question were in form interest within the meaning of Section 23(b) of the Internal Revenue Code of 1939, the entire transaction lacked substance and therefore was to be ignored for tax purposes.

The facts in the Weller case, except for dates and amounts, are practically the same.

Petitioners' attack on the judgments is essentially twofold. They assert that the payments clearly constituted interest within the meaning of Section 23(b) and were therefore deductible under that section. Additionally, they contend that the Commissioner may not, under the circumstances of these cases, retroactively reverse his prior rulings which allowed similar deductions.

Section 23 of the Internal Revenue Code of 1939, "Deductions from gross income," provides for deductions of "All interest paid or accrued within the taxable year on indebtedness * * * ." The Supreme Court has defined the term interest as used in the Internal Revenue Code on several occasions. In Old Colony Railroad Co. v. Commissioner of Internal Revenue, 284 U. S. 552, 560 (1932), it was held to be "the amount which one has contracted to pay for the use of borrowed money." Again, in Deputy v. duPont, 308 U. S. 488, 497-498 (1940), the Court stated that "* * * although an indebtedness is an obligation, an obligation is not necessarily an 'indebtedness' within the meaning of §23(b). Nor are all carrying charges 'interest.' * * * We are dealing with the context of a revenue act and words which have today a well-known meaning. In the business world 'interest on indebtedness' means compensation for the use or forbearance of money. In absence of clear evidence to the contrary, we assume that Congress has used these words in that sense." Applying these definitions to the instant cases, we come to the crux of the government's case. It contends that since interest for tax purposes is confined to payments for the use of money and since no money or other economic benefit was ever in effect advanced to the taxpayers by the insurance company, the payments were not interest.

The Tax Court, and the government on appeal, rely quite heavily on the pattern of conduct evidenced by the taxpayer and Standard. This pattern, as summarized above, involved prepayments of interest which accelerated the cash or loan value of the policy, concurrent borrowing of the accelerated increase in the cash or loan value, thus immediately recouping a major portion of the purported prepayments of interest. The cycle was completed when the taxpayer claimed deductions on his 1951 and 1952 returns of the entire amounts of each prepayment of interest, although his actual outlay was much less. We agree with the conclusion of the Tax Court that, although in form the payments appear to constitute interest within the meaning of Section 23(b) of the Internal Revenue Code of 1939, the entire transaction lacks substance.

Gregory v. Helvering, 293 U. S. 465 (1935), relied upon by the Tax Court, involved the creation of a corporate entity for the purpose of transferring shares of stock to the taxpayer. While recognizing that a real, valid corporate entity was created and that the transaction was within the terms of the statute, the Supreme Court concluded that it was "an elaborate and devious form of conveyance masquerading as a corporate reorganization." The activities were described as "an operation having no business or corporate purpose—a mere device which put on the form of a corporate reorganization as a disguise

for concealing its real character, and the sole object and accomplishment of which was the consummation of a preconceived plan, not to reorganize a business * * * but to transfer a parcel of corporate shares to the petitioner." The Court there also referred to the rule which excludes from consideration the motive of tax avoidance but determined that it was not pertinent to the situation "because the transaction upon its face lies outside the plain intent of the statute." The question of form versus substance as regards the incidence of taxation has been before the courts on a number of occasions involving numerous differing factual situations. In Higgins v. Smith, 308 U. S. 473, 476 (1940), it was stated that "If * * * the Gregory case is viewed as a precedent for the disregard of a transfer of assets without a business purpose but solely to reduce tax liability, it gives support to the natural conclusion that transactions, which do not vary control or change the flow of economic benefits, are to be dismissed from consideration." See Griffiths v. Commissioner of Internal Revenue, 308 U. S. 355 (1939). In like vein the Supreme Court stated in Commissioner of Internal Revenue v. Court Holding Co., 324 U. S. 331, 334 (1945), "The incidence of taxation depends upon the substance of a transaction. The tax consequences which arise from gains from a sale of property are not finally to be determined solely by the means employed to transfer legal title. Rather, the transaction must be viewed as a whole, and each step, from the commencement of negotiations to the consummation of the sale, is relevant. * * * To permit the true nature of a transaction to be disguised by mere formalisms, which exist solely to alter tax liabilities, would seriously impair the effective administration of the tax policies of Congress."

Any case of this nature is beset with difficulties, for in viewing the substance of the entire transaction one is faced with the rule alluded to above that enjoins us to disregard the motive of tax avoidance. That is not to say that we are confronted with a dilemma. Far from it. The proper resolution of the problem has succinctly been set forth by Judge Learned Hand in Gilbert v. Commissioner of Internal Revenue, 248 F. 2d 399, 411-412 (C. A. 2, 1957), (dissenting on a procedural matter unrelated to this case),

> "* * * If, however, the taxpayer enters upon a transaction that does not appreciably affect his beneficial interest except to reduce his tax, the law will disregard it; for we cannot suppose that it was part of the purpose of the act to provide an escape from the liabilities that it sought to impose. * * * [The Gregory doctrine] covers only those transactions that do not appreciably change the taxpayer's financial position, either beneficially or detrimentally."

Thus, the principle laid down in the Gregory case is not limited to corporate reorganizations, but rather applies to the federal taxing statutes generally. The words of these statutes which describe commercial transactions are to be understood to ~~refer to~~ transactions entered upon for commercial purposes and "not to include transactions entered upon for no other motive but to escape taxation." Commissioner of Internal Revenue v. Transport Trading & Terminal Corp., 176 F. 2d 570, 572 (C. A. 2, 1949), cert. denied, 338 U. S. 955 (1950).

The Tax Court could find no independent economic purpose present in the instant cases and thus concluded that the sole purpose was the creation of a tax deduction. The petitioners have gone to great lengths to demonstrate that there was commercial substance to the transactions, over and above the tax benefits, but we are far from convinced. If one ignores the practice of concurrently borrowing the increased cash or loan value of the contracts built up by prepayments of interest one might

find some economic sense in the transactions, other than the hoped for tax deductions. However, given the practice, which is borne out by the records, the fact that there was a 4 per cent interest rate on the loans and a mere 2.85 per cent discount rate on the pre-paid interest, and the fact that the loans were non-recourse in nature and were never repaid, the conclusion of the Tax Court is a reasonable one.

Petitioners, on the other hand, point out that the insurance company, which was regularly organized and authorized to issue annuity contracts, and to make loans such as those made here, treated the payments on its books as interest received. The government does not challenge the validity of the labels employed by the insurance company nor does it contest the validity of the transactions under the Indiana insurance law. Rather, it points to the well-settled principle that for the purpose of the federal tax laws the substance of transactions is to be determined uniformly in relation to the meaning and intendment of the federal laws. United States v. Gilbert Associates, Inc., 345 U. S. 361 (1953). A denial of these claimed deductions would represent no attack in any way upon the insurance laws of Indiana or any other state in which Standard operates nor would it characterize it a "sham corporation" issuing "sham policies." That there may be an obligation which is valid under local law is not determinative of whether there is a true indebtedness within the meaning of Section 23(b). See Haffenreffer Brewing Co. v. Commissioner of Internal Revenue, 116 F. 2d 465 (C. A. 1, 1940), cert. denied, 313 U. S. 567 (1941).

Petitioners also place considerable emphasis upon the provisions and legislative history of Section 24(a)(6) which prohibits deductions for certain specified forms of interest, that is, "any amount paid or accrued on indebtedness incurred or continued to purchase a single premium life insurance or endowment contract * * *." The fact that annuity contracts are not covered by this prohibition is clear beyond peradventure of a doubt. However, such a showing is far from determinative of the issue in the case, for Section 24(a) applies to specific items that are *not* deductible. The section does not even purport to indicate what items are deductible and, therefore, legislative history indicating that annuity contracts were specifically not included therein fails to conclude the issue. Regardless of Section 24(a)(6), the taxpayers' payments must still qualify as interest under Section 23(b) to be deductible.

In disallowing the interest in these cases, the department relied upon Revenue Ruling 54-94, 1954-1 Cum. Bull. 53, which, of course, was issued after the taxable years in question. The petitioners contend that the Commissioner may not retroactively reverse his prior rulings which allowed similar deductions. The prior rulings had not been issued to the petitioners, for they had never requested any but were individual rulings in other cases. These individual rulings had been shown to petitioners by insurance company salesmen prior to the time of the purchase of the annuity contracts. Recognizing that they may not rely on these rulings directly, petitioners maintain that all taxpayers have the right to be treated equally and fairly and since they undoubtedly would have received similar rulings had they applied for them, they are entitled to their benefits. They argue further that the very number of individual rulings made by the Commissioner[2] established a practice, a course of conduct, and that a retroactive change would be an arbitrary exercise of the authority committed to the Commissioner by Congress.[3]

[2]Although there is no evidence in the record as to the number of such rulings made by the Commissioner, Emmons testified he had been shown seven and Weller six or seven such individualized rulings.

The first contention has little substance or reason to support it, for it is just another way of stating that anyone who sees a ruling should be allowed to rely on it. Even with respect to rulings *published* in the Internal Revenue Bulletin, the Supreme Court said in Helvering v. New York Trust Co., 292 U. S. 455, 468 (1934):

> "* * * The rulings * * * 'have none of the force or effect of Treasury Decisions and do not commit the Department to any interpretation of the law.' See cautionary notice published in the bulletins containing these rulings."

Certainly *unpublished* rulings can be given no greater effect.

In support of their second contention that it would be an abuse of discretion for the Commissioner to retroactively change his practice established by a series of individual rulings, taxpayers rely upon Automobile Club of Michigan v. Commissioner of Internal Revenue, 353 U. S. 180 (1957), and our case of Lesavoy Foundation v. Commissioner of Internal Revenue, 238 F. 2d 589 (C. A. 3, 1956). Reliance upon the Lesavoy case is misplaced, for it merely determined that the Commissioner had exceeded his permissible discretion in retroactively withdrawing a ruling issued to a particular taxpayer who had not estopped himself. The Supreme Court in Automobile Club of Michigan v. Commissioner of Internal Revenue,

[3]Section 3791(b) provides:

"Retroactivity of Regulations or Rulings—The Secretary, or the Commissioner with the approval of the Secretary, may prescribe the extent, if any, to which any ruling, regulation, or Treasury Decision, relating to the internal revenue laws, shall be applied without retroactive effect." 53 Stat. 467 (1939), 26 U.S.C.A. I.R.C. 1939, § 3791(b).

supra, sets forth the standard which we must apply in questions of this nature. In that case, the petitioner-automobile club had received a ruling of exemption from the Commissioner in 1934 which was re-confirmed in 1938. In 1945, applying a new interpretation of the revenue laws rendered by the General Counsel, the Commissioner revoked this individual ruling and applied his re ocation retroactively to tax years 1943 and 1944. The revocations applied to exemptions issued to all automobile clubs and the Supreme Court stated, at page 186, "that the Commissioner, having dealt with petitioner upon the same basis as other automobile clubs, did not abuse his discretion." Similarly in the instant cases, the petitioners have been treated in the same manner as all other taxpayers.

Petitioners contend, however, that although the revenue ruling fails to indicate any limitation on its application, agents of the Treasury have stated to Congress that it does not intend to apply the revenue ruling retroactively to individuals who have previously been issued rulings. We need not determine whether such action if carried out would be an abuse of discretion, for petitioners are not in the same position as those parties who have been issued rulings. They are entitled to the same treatment as all other taxpayers similarly situated, i.e., without rulings, no more and no less. This the Commissioner has afforded them.

Petitioners' further arguments are adequately disposed of by Automobile Club of Michigan v. Commissioner of Internal Revenue, supra.

We are not unmindful of the decision recently rendered by the Court of Appeals for the Fifth Circuit in a similar case, United States v. Bond, 258 F. 2d 577 (1958), which holds contrary to this opinion. We agree, however, with the dissenting opinion of Judge Wisdom

in that case. In accord with our opinion are Haggard v. United States, 59-1 U. S. T. C. 9299 (D. C. Ariz. 1959); and Knetsch v. United States, 58-2 U. S. T. C. 9935 (S. D. Calif. 1958). And see Goodstein v. Commissioner of Internal Revenue, 267 F. 2d 127 (C. A. 1, 1959); Sonnabend v. Commissioner of Internal Revenue, 267 F. 2d 319 (C. A. 1, 1959).

The judgments will be affirmed.

A True Copy:

Teste:

Clerk of the United States Court of Appeals for the Third Circuit.