

Taxation--Deduction of Fines and Penalties Held Not Proper Because Frustrative of State Policies (Tank Truck Rentals, Inc. v. Commissioner, 356 U.S. 30 (1958))

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although seemingly a rejection of the *lex loci delicti* rule, does not actually conflict with it.²⁶

It is felt that the holding in the *Heinemann* case should be limited to the specific fact-situation there involved, and not be considered a leading authority in the general area of the applicability of the *lex loci delicti* rule. It is submitted that the principal case states the correct law on this point and clarifies the New York position. Hence, the *Kaufman* case should be the controlling New York case in situations calling for the application of the *lex loci delicti* rule to cases involving charitable immunity from tort liability.



TAXATION—DEDUCTION OF FINES AND PENALTIES HELD NOT PROPER BECAUSE FRUSTRATIVE OF STATE POLICIES.—Taxpayer sought to deduct as ordinary and necessary expenses¹ fines paid for violations of a Pennsylvania statute² prescribing maximum truck weights. It was commercially impracticable for taxpayer to comply with the statute. The Tax Court disallowed the deduction on the ground that it would frustrate sharply-defined state policy. The Court of Appeals affirmed. On certiorari, the United States Supreme Court held that allowing deduction of fines and penalties would frustrate state policies by mitigating their deterrent effect. *Tank Truck Rentals, Inc. v. Commissioner*, 356 U.S. 30 (1958).

In a companion case, the Court affirmed an order of the Court of Appeals reversing a Tax Court determination that amounts expended by a bookmaker for rent and salaries were not deductible since made in connection with illegal acts. The Court held that since gambling is recognized as a business for federal tax purposes, taxpayer's normal operating expenses are deductible.³ *Commissioner v. Sullivan*, 356 U.S. 27 (1958).

²⁶ See note 18 *supra*.

¹ The former version of § 162 of the Internal Revenue Code of 1954 provided that in computing net income there shall be allowed as deductions "all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; . . . and rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity." 56 STAT. 819 (1942).

² PA. STAT. ANN. tit. 75, § 453 (1953), as amended, PA. STAT. ANN. tit. 75, § 453 (Supp. 1957).

³ The Court distinguishes *Tank Truck Rentals*, stating that a deduction is permitted unless the allowance would avoid the *consequence* of violations of the law. *Commissioner v. Sullivan*, 356 U.S. 27, 29 (1958).

Frustration of public policy as a ground for disallowing an expenditure sought to be deducted as an ordinary and necessary business expense is a judicially-imposed limitation upon the statute.⁴ In one of the first of such cases treated by the Supreme Court, *Textile Mills Sec. Corp. v. Commissioner*,⁵ lobbying expenses were disallowed. It was noted that "contracts to spread such insidious influences . . . have long been condemned"⁶ and asserted that a line may be drawn ". . . between legitimate business expenses and those arising from that family of contracts to which the law has given no sanction. The exclusion of the latter from 'ordinary and necessary' expenses does no violence to statutory language."⁷ Two years later, in 1943, the Court observed that the former version of section 162 had been judicially narrowed in order that the tax deduction might not frustrate national or state policies.⁸ The Court did not consider this particular problem again until 1952. In *Lilly v. Commissioner*,⁹ the deduction of a kickback by an optometrist, disallowed in the lower courts on the ground that payments were contrary to public policy, was allowed as an ordinary and necessary business expense by the Supreme Court.¹⁰ The public policy limitation was thus delimited:

[We assume that] . . . business expenses which are ordinary and necessary in the generally accepted meanings of those words may not be deductible as "ordinary and necessary" expenses under [the former version of section 162] . . . when they "frustrate sharply defined national or state policies proscribing particular types of conduct. . . ." The policies frustrated must be national or state policies evidenced by some governmental declaration of them.¹¹

Many problems arose in the application of the policy expressed by *Lilly*. The Court's statement of the public policy limitation was

⁴ See Note, 51 COLUM. L. REV. 752 (1951); Comment, 41 MARQ. L. REV. 305 (1958). For a criticism of this limitation see Reid, *Disallowance of Tax Deductions on Grounds of Public Policy—A Critique*, 17 FED. B.J. 575 (1957) (hereinafter referred to as Reid, *Disallowance of Deductions*). Mr. Reid considers that "moral turpitude is a very poor criterion for taxability. . . ." *Id.* at 578. He advises adherence to the letter of the Internal Revenue Code. *Id.* at 578-83.

⁵ 314 U.S. 326 (1941).

⁶ *Textile Mills Sec. Corp. v. Commissioner*, 314 U.S. 326, 338 (1941).

⁷ *Id.* at 339.

⁸ *Commissioner v. Heininger*, 320 U.S. 467, 473 (1943) (legal expenses to defend mail fraud order held deductible).

⁹ 343 U.S. 90 (1952).

¹⁰ Under other circumstances, kickbacks were held not "necessary" expenses. *Harden Mortgage Loan Co. v. Commissioner*, 137 F.2d 282 (10th Cir. 1943). In *Lilly*, taxpayer proved the kickbacks essential to his business and ordinary in the locality in which he practiced his profession.

¹¹ *Lilly v. Commissioner*, 343 U.S. 90, 96-97 (1952). See also Reid, *Disallowance of Deductions*, 17 FED. B.J. 575, 576 (1957); Comment, 41 MARQ. L. REV. 305, 309 (1958).

dictum.¹² Likewise, as the Court seemed to be pulling back from its position in *Textile Mills*, doubt was cast upon the extent to which it intended to adhere to this policy in the future.¹³ The Seventh Circuit, in *Doyle v. Commissioner*,¹⁴ disregarded the limitation.¹⁵ It felt that the application of the policy would, in effect, add a separate limitation to the statute.¹⁶ Refusing to thus add to the statute, the court considered only whether the expense was economically integrated with the business and met the "ordinary and necessary" requirements.¹⁷

The principal cases state unequivocally that where a deduction would frustrate national or state policies, the deduction must be disallowed.¹⁸ Thus the Court rejects the rule of the *Doyle* case.¹⁹ The Court indicates that it does not feel that its holding adds a limitation to the statute, but rather that the finding of frustration of public policy precludes a finding of "necessity."²⁰

¹² "Assuming . . . [such expenses] may not be deductible." *Lilly v. Commissioner*, *supra* note 11, at 96. (Emphasis added.) See Reid, *supra* note 11, at 582; Comment, 41 MARQ. L. REV. 305-06 (1958).

¹³ See Reid, *Disallowance of Deductions*, *supra* note 11, at 582.

¹⁴ 231 F.2d 635 (7th Cir. 1956).

¹⁵ The court allowed deduction of a bookmaker's expenses for rent and salaries in face of the Commissioner's contention that the expenses were unlawful. "From [the former version of section 162] . . . we find that an allowable deduction . . . must be ordinary and necessary, nothing more or less. . . . We construe the statutory words 'ordinary and necessary' expenses to mean those expenses which economically are an integral part of a business, whether it be lawful or unlawful." *Doyle v. Commissioner*, 231 F.2d 635, 637 (7th Cir. 1956).

In reversing the Tax Court's disallowance of deductions in *Sullivan v. Commissioner*, the Circuit Court emphasized: "We made it clear, [in the *Doyle* case] . . . that [the former version of section 162], . . . in setting forth what trade or business expenses are to be deducted from gross income in computing net income, makes no distinction between *lawful* and *unlawful* disbursements." *Sullivan v. Commissioner*, 241 F.2d 46, 47 (7th Cir. 1957), *aff'd*, 356 U.S. 27 (1958). See also Comment, 41 MARQ. L. REV. 305, 308 (1958).

¹⁶ "[T]he Commissioner would include the element of lawfulness of expenses . . . as a requirement or [*sic*] their deductibility, in *addition* to the act's requirement that said expenses be 'ordinary and necessary' [He] . . . would have us *add* the word 'lawful' in the guise of judicial construction." *Doyle v. Commissioner*, *supra* note 15, at 636. (Emphasis added.) The court distinguished the bribe, penalty and lobbying cases on the ground that they were not an integral part of the business. *Id.* at 637.

¹⁷ See note 15, *supra*.

¹⁸ "A finding of 'necessity' *cannot* be made, however, if allowance of the deduction would frustrate sharply defined national or state policies. . . ." *Tank Truck Rentals, Inc. v. Commissioner*, 356 U.S. 30, 33 (1958) (emphasis added). The Court cites *Lilly* and *Heininger* for support. In those cases, reference to the frustration "rule" was dicta. See notes 8 and 12, *supra*.

¹⁹ Whereas *Doyle* would ignore lawfulness (see note 15, *supra*), the Court here makes it clear that lawfulness of the disbursement must be considered. *Tank Truck Rentals, Inc. v. Commissioner*, note 18, *supra*.

²⁰ See note 18, *supra*. The question remains, however, what illegality has to do with necessity. In *Deputy v. DuPont*, 308 U.S. 488 (1940), Mr. Justice Douglas stated that ". . . ordinary and necessary is to be construed according to . . . popular or received import of the words. . . . Ordinary has the conno-

The public policy requiring this limitation on the deductibility of expenses must be evidenced by *some* governmental declaration.²¹ Just what type of governmental declaration suffices is unclear. The term certainly denotes federal or state statutes, and has been held to include a local ordinance.²² Court decisions are probably within its scope.²³ In one instance, the determination of an administrator of the Office of Price Administration was effective to define public policy.²⁴ Considerations of professional ethics and general morality were excluded by the *Lilly* case.²⁵ Finding it unnecessary to clarify this question in the principal cases, the Court expressly leaves it open.²⁶

Just when an expense will frustrate public policy is not at all clear from the court decisions.²⁷ Where an expense is itself proscribed by statute, it will be disallowed.²⁸ The principal cases deal

tation of normal, usual or customary." *Id.* at 493. Necessary is defined in *Welch v. Helvering*, 290 U.S. 111, 113 (1933) (cited with approval in *DuPont*), as ". . . appropriate and helpful." The construction in *Lilly* was similarly broad. *Lilly v. Commissioner*, 343 U.S. 90, 93 (1951).

²¹ *Tank Truck Rentals, Inc. v. Commissioner*, *supra* note 18, at 33-34; *Lilly v. Commissioner*, *supra* note 20, at 97.

²² See, e.g., *Automatic Cigarette Sales Corp. v. Commissioner*, 234 F.2d 825 (4th Cir. 1956) (violation of state statute and city ordinance); *William F. Davis, Jr.*, 17 T.C. 549 (1951) (violation of Securities Exchange Act of 1934); *Harry Wiedetz*, 2 T.C. 1262 (1943) (violation of city ordinance).

²³ See *Textile Mills Sec. Corp. v. Commissioner*, 314 U.S. 326, 338 (1941) (cited in *Lilly v. Commissioner*, 343 U.S. 90, 95 (1952)), where lobbying expenses condemned by the courts, *not by statute*, were disallowed. See also Comment, 41 *MARQ. L. REV.* 305, 308 (1958).

²⁴ *Jerry Rossman Corp. v. Commissioner*, 175 F.2d 711 (2d Cir. 1949). In considering whether a deduction of a penalty paid for violation of the Emergency Price Control Act of 1942 would frustrate public policy, the court, holding that it would not, stated: "[W]e have the answer from the best possible source—the Administrator himself." *Id.* at 714.

Prior to 1944, §205 of the act did not distinguish between the willful and non-willful violator. The Administrator, however, construed the statute so as to give him discretion not to sue for treble damages in the case of innocent violators, and in those cases demanded payment of the amount of overcharge only. In 1944, Congress amended the act so as to expressly give the Administrator such power. *Ibid.* "[W]here the Administrator accepted the amount of the overcharge as sufficient, it did not 'frustrate' any 'sharply defined' policies of the Emergency Price Control Act of 1942." *Ibid.*

²⁵ *Lilly v. Commissioner*, 343 U.S. 90, 97 (1952). *But see* *Estate of Joseph Karger*, 23 P-H Tax Ct. Mem. 637 (1954).

²⁶ *Tank Truck Rentals, Inc. v. Commissioner*, 356 U.S. 30, 34 n.6 (1958). "Because state policy in this case was evidenced by specific legislation, it is unnecessary to decide whether the requisite 'governmental declaration' might exist other than in an Act of the Legislature." *Ibid.*

²⁷ See *Reid, Disallowance of Deductions*, 17 *FED. B.J.* 575-79 (1957). ". . . I defy anyone to construct a legal theory . . . which would reconcile the various decisions on the deductibility of costs incurred by illegal enterprises and illegal or immoral payments made by other businesses." *Id.* at 579.

²⁸ See *Boyle, Flagg & Seaman, Inc.*, 25 T.C. 43, 49-50 (1955), disapproving deduction of certain proscribed commissions paid by insurance broker and cited

with expenses not illegal in themselves but, in *Tank Truck Rentals*, incurred as a consequence of an illegal act, and, in *Sullivan*, in the operation of an illegal business.

Expenses incurred in consequence of an illegal act, such as fines imposed for violation of a statute²⁹ or legal fees to defend certain criminal prosecutions,³⁰ are not deductible. Deduction of such expenses would frustrate public policy by mitigating the deterrent effect of the statute. In the *Tank Truck Rentals* case, the Court reaffirms this policy.³¹

In the fine or penalty area, *Jerry Rossman Corp. v. Commissioner*³² allowed deduction of a fine to a non-willful violator of regulations of the Office of Price Administration. In that case, the OPA Administrator demanded payment of the amount of overcharge only and did not sue for treble damages as authorized by statute. The court argued that the fine was not intended as a deterrent, but only to prevent the violator from profiting by the violation. Thus, even assuming that the exaction was a penalty, allowing the deduction would not mitigate the deterrent effect of the statute.³³ In *Tank Truck Rentals*, the Court refuses to differentiate between the willful and non-willful violation, there being no distinction made by the state statute.³⁴ The implication is that the Court will not look behind the statute to discover whether the statutory fine is punitive or remedial.³⁵

Expenses supportive of an illegal business have been variously allowed and disallowed. Generally, normal operating expenses such

with approval in the principal case. *Tank Truck Rentals, Inc. v. Commissioner*, *supra* note 26, at 35. See also Comment, 41 MARQ. L. REV. 305, 307 (1958).

²⁹ See cases cited note 22, *supra*.

³⁰ See, e.g., *Helvering v. Superior Wines & Liquors, Inc.*, 134 F.2d 373 (8th Cir. 1943); *National Outdoor Advertising Bureau, Inc. v. Helvering*, 89 F.2d 878, 880-81 (2d Cir. 1937) (dictum).

³¹ *Tank Truck Rentals, Inc. v. Commissioner*, 356 U.S. 30, 35 (1958).

³² 175 F.2d 711 (2d Cir. 1949).

³³ *Jerry Rossman Corp. v. Commissioner*, 175 F.2d 711, 712-14 (2d Cir. 1949). See discussion note 24, *supra*. But see Note, 51 COLUM. L. REV. 752, 754 (1951). For a discussion of the *Rossman* case and its possible implications, see Gelfand, *Payments to OPA*, 27 TAXES 961 (1949).

³⁴ *Tank Truck Rentals, Inc. v. Commissioner*, *supra* note 31, at 36. "[S]ince . . . statutes make no distinction between innocent and willful violators, state policy is as much thwarted in the one instance as in the other." Referring to the petitioner's reliance on the *Rossman* case, the Court observes that ". . . the Administrator, in applying the Act, had differentiated between willful and innocent violators. No such differentiation exists here. . . ." *Id.* at 37.

³⁵ Although the statute [PA. STAT. ANN. tit. 75, §§ 453-55 (1953) as amended, PA. STAT. ANN. tit. 75, § 453 (Supp. 1957)] authorized a single trip ticket by an overweight trucker, although police never enforced removal of excess weight, and although the fines were devoted to road repairs within the municipality where the trucker was apprehended, the Court considered only the fact that the penalty was imposed by the statute as a penal measure. *Tank Truck Rentals, Inc. v. Commissioner*, 356 U.S. 30, 36 (1958).

as rents and salaries are allowed.³⁶ The Tax Court, however, disallowed expenses of an abortionist in purchasing medical supplies and paying fees to persons who recommended patients to him.³⁷ In allowing deduction of operating expenses to the bookmaker in the *Sullivan* case, the Court states that where a business is a business for federal tax purposes, the otherwise normal expenses it incurs will be allowed.³⁸ The question remains, however, just when a business is

³⁶ See, e.g., *Commissioner v. Doyle*, 231 F.2d 635 (7th Cir. 1956) (salaries and rent of bookmaker); *G. A. Comeaux*, 10 T.C. 201 (1948), *aff'd sub nom.*, *Cohen v. Commissioner*, 176 F.2d 394 (10th Cir. 1949) (expenses of illegal gambling and liquor establishments). In the *Cohen* case, *supra*, the court stated broadly, "legitimate expenses incurred in an illegitimate business are deductible. . . ." *Cohen v. Commissioner, supra*, at 400.

Where the Tax Court found that the salaries and rent of the bookmaker were, by statute, illegal in themselves [ILL. REV. STAT. c. 38, § 336 (1945)] the deduction was disallowed. *Sam Mesi*, 25 T.C. 513 (1955). The same statute was involved in *Commissioner v. Doyle* and *Commissioner v. Sullivan*. In *Doyle*, the Commissioner contended that the taxpayer, in paying rent, was an accessory to the landlord's crime of knowingly permitting his property to be used for gambling. The Seventh Circuit rejected this theory on the ground that the guilt of the landlord could not be determined in an action in which he was not a party. Hence the accessory's guilt must also fail of proof. *Commissioner v. Doyle, supra*, at 638. In *Sullivan*, as in *Mesi, supra*, the Tax Court accepted the Commissioner's contention. The circuit court reversed the Tax Court in *Sullivan* on the basis of the *Doyle* decision. *Sullivan v. Commissioner*, 241 F.2d 46 (7th Cir. 1957), *aff'd*, 356 U.S. 27 (1958). Presumably, *Mesi* is no longer the law.

³⁷ *Estate of Joseph Karger*, 23 P-H Tax Ct. Mem. 637 (1954). The Tax Court's holding here is consistent with its position in *Mesi v. Commissioner* and *Sullivan v. Commissioner, supra* note 36. Query: has the Supreme Court in affirming the reversal in the *Sullivan* case affected the *Karger* case? Perhaps the cases are to be distinguished by the nature of the crime involved. Note the Tax Court's language in *Karger*: "In the long category of crimes, few, if any, are considered more reprehensible or revolting to common decency and good public morals. . . . Decedent's activity was of such a leprous character that it contaminated all who touched it. The fees in question were paid by one participant in a crime to an accomplice. . . . Such deductions cannot be allowed. . . . As to medical supplies, . . . they constituted the tools for decedent's illegal and criminal business. These items cannot be allowed as being contrary to well defined public policy." *Id.* at 640.

In *Textile Mills*, the expense was disallowed as it was consideration for a contract to perform illegal services. *Textile Mills Sec. Corp. v. Commissioner*, 314 U.S. 326, 338-40 (1941). Likewise, a medical deduction is not allowed to the patient of an abortion. U.S. TREAS. REG. § 1.213-1(e)(1)ii. ["Medical care" is, however, specifically defined so as to exclude, apparently, an operation of this type. INT. REV. CODE OF 1954 § 213(e)(1)(A).] A taxpayer was also denied a dependent's deduction for a married undivorced woman with whom he was living in adulterous cohabitation in violation of public morals and the laws of Alabama. *Leon Turnipseed*, 27 T.C. 759 (1957). [The public policy limitation expressed in *Turnipseed* was subsequently codified in U.S. TREAS. REG. § 1.152-1(b).] If the distinction is to be based on the shocking nature of the crime, not only does the problem of line drawing arise, but of line drawing based on the moral sensibilities of a judge. See Reid, *Disallowance of Deductions*, 17 FED. B.J. 575, 578 (1957).

³⁸ *Commissioner v. Sullivan*, 356 U.S. 27 (1958).

“. . . a business for federal tax purposes.”³⁹ The criterion here used, the imposition of a federal excise tax upon gambling, seems not to be exclusive.⁴⁰ Query: what other criteria may be used?⁴¹

In *Sullivan*, the Court seems to disregard the finding of the Tax Court that the bookmaker's expenses were themselves illegal by Illinois statute.⁴² The Court may not overturn a finding of fact without a clear showing that it was erroneous.⁴³ If the Court is holding that, albeit their illegality, the expenses are deductible, it is inconsistent with its own statement of the law in *Tank Truck Rentals*.⁴⁴ It can be argued that the finding of the Tax Court was not of fact but was a statutory construction. Yet it is surprising that the Court neither alludes to this finding in its opinion nor construes the statute itself.

The reluctance of the Court, evidenced by *Tank Truck Rentals*,⁴⁵ to look behind the statute to determine whether a “penalty” is in fact punitive or remedial or whether the allowance of a deduction to a non-willful violator will actually frustrate state policy seems overly strict. A better rule would be to determine in each case whether the statute is intended as an absolute prohibition or merely gives an option to comply or pay damages and, if an absolute proscription, whether allowing deduction of a penalty will actually mitigate its deterrent effect.⁴⁶

³⁹ *Id.* at 29.

⁴⁰ “Regulations . . . make the federal excise tax on wagers deductible as an ordinary and necessary business expense. This seems to us to be a recognition of a gambling enterprise as a business for federal tax purposes.” *Commissioner v. Sullivan*, *supra* note 38, at 28-29. This language does not connote an exclusive rule.

⁴¹ If the mere imposition of a federal income tax is sufficient as a criterion, then, presumably, the abortionist, arsonist, dope smuggler, etc., may deduct their operating expenses. Such a result would be absurd.

⁴² *Commissioner v. Sullivan*, 356 U.S. 27-28 (1958). The statute here involved [ILL. REV. STAT. c. 38, § 336 (1945)] was discussed in note 36, *supra*. In reversing the Tax Court, the Seventh Circuit did *not* reverse its finding of illegality, but held only that the lawfulness of the disbursement made no difference. *Sullivan v. Commissioner*, 241 F.2d 46, 47 (7th Cir. 1957), *aff'd*, 356 U.S. 27 (1958). This argument is, of course, no longer applicable. *Tank Truck Rentals, Inc. v. Commissioner*, 356 U.S. 30 (1958).

⁴³ Review is limited by the Federal Rules of Civil Procedure: “Findings of fact shall not be set aside unless clearly erroneous. . . .” FED. R. CIV. P. 52(a).

⁴⁴ *Tank Truck Rentals, Inc. v. Commissioner*, *supra* note 42, at 35. “[F]rustration of state policy is most complete and direct when the expenditure . . . is itself prohibited by statute.” *Ibid.*

⁴⁵ See discussion in notes 24 and 34 *supra*.

⁴⁶ See *Jerry Rossman Corp. v. Commissioner*, 175 F.2d 711, 714 (2d Cir. 1949): “[T]here are ‘penalties’ and ‘penalties’ . . . some are deductible and some are not. . . . [T]here is no more ground for taking as a ‘rigid criterion’ the imposition of a fine than the incurrence of expenses [referring to the legal expenses in *Commissioner v. Heininger*, 320 U.S. 467 (1943)]. Each may ‘frustrate . . . policies’ . . . ; that will depend on how one views the deterrent effect. We hold therefore that in every case the question must be decided ad hoc.” See also Comment, 41 MARQ. L. REV. 305, 307 (1958).

While the principal cases firmly fix the public policy limitation in the tax law, they do little to clarify its application. This is especially true with regard to the operating expenses of an illegal business: just how far the *Sullivan* rule will be applied to other illegal businesses is unclear.



TAXATION — FEDERAL TAX LIENS — SURETY'S RIGHT HELD INFERIOR TO FEDERAL TAX LIENS.—In return for a surety's execution of a performance bond that guaranteed completion of subcontracting work on a Texas housing project, the subcontractor assigned to the surety all sums due or to become due from the general contractor under the subcontract. These sums were to serve as collateral security not only for losses incurred on the housing project but for any other indebtedness or liability the subcontractor might incur to the surety "whether heretofore or hereafter incurred." Subsequent to this assignment, the surety executed for the subcontractor a second bond covering another job in Kentucky. Then, in sequence, the Texas work was completed and the subcontractor became entitled to the sums held by the general contractor, no payment being actually made; the federal government filed tax liens against the subcontractor; and finally, the surety was forced to perform under the Kentucky bond because of the subcontractor's default. In an interpleader action to determine whether the federal government or the surety had the right to the retained percentages still due on the Texas project, the lower courts¹ held that the surety was a mortgagee under the provisions of section 3672(a) of the Internal Revenue Code of 1954, and therefore its rights took precedence over the government's tax lien. The Supreme Court, per curiam with four justices dissenting, reversed, *holding* that the tax lien took precedence because the instrument creating the surety's right was "inchoate and unperfected." *United States v. R. F. Ball Constr. Co.*, 355 U.S. 587 (1958).

A federal tax lien arises when any person liable to pay any federal tax neglects or refuses to pay the tax after a demand, and it attaches to all property and rights to property owned by the delinquent taxpayer.² In most cases the lien is a secret charge against the property, known only to the taxpayer and the Internal Revenue Service, for it arises at the time the tax assessment is made³ by the District Director of Internal Revenue,⁴ whose records are not open

¹ *United States v. R. F. Ball Constr. Co.*, 140 F. Supp. 60 (W.D. Tex.), *aff'd per curiam*, 239 F.2d 384 (5th Cir. 1956).

² INT. REV. CODE OF 1954, § 6321.

³ INT. REV. CODE OF 1954, § 6322.

⁴ INT. REV. CODE OF 1954, § 6203; Treas. Reg. 301.6201-1 (1954).