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Volume Author/Editor: Dan Throop Smith and J. Keith Butters

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Chapter Author: Dan Throop Smith, J. Keith Butters

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CHAPTER 6

Interest, Purchase and Retirement of Bonds, Bond Premium and Discount

A INTEREST

THE INTERNAL REVENUE CODE, SECTION 23(b), PROVIDES IN simple terms for a deduction of

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

Though the statement is apparently clear and unambiguous, its application has aroused much litigation and controversy. To a considerable extent the problems have arisen in connection with what, to the uninitiated, must seem rather unusual business relationships. Some transactions, in fact, appear to be in the form they are primarily to gain the tax advantage of the interest deduction. To prevent abuse of the allowance for interest deductions, various rules have been set up that must be met before an interest deduction is allowed; for example, the interest must have been paid on a bona fide debt and the debt must be that of the payer.

None of the special rules is likely to be of any significance to corporations with bonds or debentures outstanding, or in cases involving loans from banks, finance companies, public lending agencies, and other disinterested lenders. Most of the

exceptions and qualifications to interest deductions relate primarily to abnormal conditions in closely held corporations or other situations in which maneuvers to avoid taxes have been undertaken. The arithmetical computation of interest paid or accrued, ignoring bond premium and discount, is simple. However, though tax and accounting practice may agree on the amount, some part may be disallowed in computing taxable income if allowance would permit tax avoidance. But any full discussion of the accounting treatment of these infrequent pathological situations would be unreasonably long.

Whereas one concern of the revenue agent is to make certain that a deduction is not claimed for payments on debts owed by someone other than the taxpayer, the concern of auditors for public reports is to see that all debts of the company and interest on them are included in the accounts. Omission rather than improper inclusion is the danger. Interest paid by a corporation on debts of employees or stockholders to third parties is in the nature of additional compensation or a distribution of profits, if not actually a misuse of corporate funds. There is a real tax advantage in claiming a payment of interest on a stockholder's debt in a family corporation as interest paid by the company, since the stockholder gets the benefit from a distribution of corporation funds of a sort which, contrary to the general rule, would be deductible by the corporation in computing its own income. Although such payments might be included as interest paid in carelessly drawn statements, audited statements would be properly qualified to indicate the exact nature of the payment. The only cases in which a company issuing public reports is likely to have paid interest on debts other than its own are those involving guaranteed debts of subsidiary corporations—a problem of consolidated statements and returns beyond the scope of this study.¹

¹ One special situation, which as a practical matter would arise only in closely held family corporations, is covered by Section 24(c) of the Internal Revenue Code: No deduction will be allowed for ordinary and necessary expenses [covered by Sec. 23(a)] or for interest [covered by Sec. 23(b)] if they are not

Very real possibilities exist for different treatment for tax and book purposes of the interest element in the cost or purchase price of property acquired. Some part of the total payment may be recognized as interest arising because payments are deferred, and treated as such for book purposes, even though the amount is not deductible as interest for tax purposes because it does not meet the technical requirements previously discussed. In this case, book income would be lower than taxable income because of the interest deduction taken when the property was paid for. But though taxable income does not reflect the interest deduction, other factors would operate to make taxable income lower than book income in the same or later periods. The higher original cost of the property would be reflected in the cost of goods sold, through inventory, or in a higher basis for depreciation or for gain or loss calculations. The higher cost as computed for tax purposes could be expected to balance out over a period the immediate interest deduction taken for book purposes.

The two statutory limitations on the deduction of interest paid on indebtedness to purchase or carry securities yielding tax-exempt interest have no counterpart in business accounting. Since all income, whether taxable or tax-exempt, is included in measuring business income, no reason exists for treating interest paid on funds borrowed to purchase tax-

paid within the taxable year or within two and one-half months thereafter, and if the amount is not includible in the gross income of the person to whom the sums are payable, and if the taxpayer and the person to whom the payment is to be made are persons between whom losses would be disallowed under Section 24(b).

Section 24(b) covers transactions between members of a family and in other cases where arms-length dealings are unlikely. The accrued interest payable would be a business expense in measuring the income of a borrower on an accrual basis regardless of the nonpayment of the interest and the nonrecognition of the interest receivable by the creditor on the cash basis. In audited statements the unusual nature of any such continuously growing 'accrued interest payable' item would call for explanation. The disallowance of interest accrued but not paid in certain conditions did not become effective until 1937, and, of course, influences the taxable income figures only since that date.

exempt securities any differently from interest paid on funds borrowed for general purposes. The disallowance of such interest for tax purposes will balance to some extent the non-inclusion of the income from tax-exempt securities. But if tax-exempt securities are held, the net effect of interest paid and received would be the same for taxable and book income only if nonincluded income and nondeductible interest were exactly equal, an unlikely case.

B PURCHASE BY A CORPORATION OF ITS OWN BONDS

Many controversial problems center about the purchase by a corporation of its own bonds. The important question is often whether rather than when an item is income. The Supreme Court has held that when a corporation purchases its own bonds issued at par for less than par, the difference is income.² Various important exceptions have been made to this general rule. In a May 1946 Tax Court case a distinction was made between bonds purchased by direct negotiation with holders and those purchased in the open market.³ For the former, it was held that no income arose, and that the transaction came under the doctrine of the American Dental Company case establishing a rule that in certain situations a purchase at less than face value involved a gratuitous cancellation of debt, i.e., there was no taxable income.⁴ The open market purchases were held to give rise to taxable income under the rule of the Kirby Lumber case. Six members of the Tax Court dissented from the majority opinion, and whether the distinction according to the form of the transaction is sufficiently real to be upheld is questionable. It is altogether unreal as a reason for varying treatment for business purposes.

The Revenue Act of 1939 provided that under certain conditions income arising from the discharge of indebtedness, by the purchase of bonds at less than the issuing price, might be

² U.S. v. Kirby Lumber Company, 284 U.S. 1 (1931).

³ Lewis F. Jacobson v. Commissioner, 6 T.C. 1048 (1946).

⁴ Helvering v. American Dental Company, 318 U.S. 322 (1943).

excluded from gross income. However, any such exclusion must be offset by a reduction in the basis of property held by the corporation.⁵ This provision was designed to facilitate adjustments of capital structures. Without it, corporations found themselves in the anomalous position of incurring large tax liabilities requiring cash payments as the result of events that in no sense gave rise to cash receipts; rather the contrary. Some of the original restrictions were removed by the Revenue Act of 1942, and the expiration date, originally set at December 31, 1945, has been successively extended to December 31, 1949.

In the Revenue Act of 1942 more liberal treatment was accorded railroad companies in case of modification or cancellation of indebtedness pursuant to a court order in bankruptcy or equity receivership proceedings. In such cases the exclusion from gross income was absolute and not associated with an adjustment of basis of property.⁶ This provision too was successively extended to the end of 1949. The general effect of these two exceptions is to bring the taxable income concept more nearly in line with the concept of business income, which in no case would include gains arising from distress recapitalization as income. The first exception is sufficiently broad to cover other than distress activities, but the provision for an adjustment in basis and the phrase 'discharge of indebtedness', which precludes trading in a company's own bonds, are important limitations.

C BOND PREMIUM AND DISCOUNT

Tax Treatment

Two types of question arise in connection with bond discount and premium and with the expenses of issue or redemption: Do certain items enter the computation of income at any time? When should the income or the deduction be reported? The

⁵ Revenue Act of 1939, Sec. 215; now Internal Revenue Code, Sec. 22(b)(9). For effects on basis, see Internal Revenue Code, 113(b)(3).

⁶ Internal Revenue Code, Sec. 22(b)(10); Revenue Act of 1942, Sec. 114(b).

problems are difficult to separate. The legal provisions and court opinions on this subject are presented rather fully as examples of the highly technical nature of the taxable income concept and of the rather arbitrary features that have at times characterized it.

1 *Bond premium*

The Supreme Court has taken the position that bond premium is income and not a loan to the corporation which must be amortized over the life of the bonds in the form of smaller interest deductions. In the leading group of cases, the Old Colony Railroad had issued bonds prior to 1913 at a premium.⁷ The Commissioner contended, in considering the return filed for the tax year 1920, that the income represented by the premium should be amortized over the life of the bonds, in accordance with the then existing regulations. The Board and Circuit Court held, against the Commissioner, that the premiums were income when received, that is, before the adoption of the 16th Amendment.

Later, in connection with the 1921 tax year, the question of the treatment of the premium again came before the Court. This time the Commissioner contended that the deduction for interest expense should be reduced by a pro rata part of the premium, not that a pro rata part of the premium should be included in income. The Circuit Court accepted the theory of the Commissioner. Upon appeal, the Supreme Court held that the premiums were income in the year received and had become capital before the adoption of the 16th Amendment. The Court refused to accept the theory that bond premium is in the nature of capital lent by the bondholder which must be returned over the life of the bond; that each payment of interest is in part interest at the effective rate and in part a pro rata re-

⁷ *Old Colony Railroad Company v. Commissioner*, 6 B.T.A. 1025 (1927), relating to the 1920 taxable year; affirmed 26 F(2d) 408 (CCA 1st, 1928); appeal dismissed, 279 U.S. 876 (1929). *Old Colony Railroad Company v. Commissioner*, 18 B.T.A. 267 (1929), relating to the 1921 taxable year, reversed 50 F (2d) 896 (CCA 1st, 1931), reversed 284 U.S. 552 (1932).

turn of the premium. The decision departs widely from accounting theory in holding that 'interest' in the statute refers to interest as it is popularly understood, not to the accountant's concept of 'effective interest'.

"In the ordinary affairs of life no one stops for a refined analysis of the nature of a premium, or considers that the periodic payment universally called 'interest' is in part something wholly distinct—that is, a return of borrowed capital. It has remained for the theory of accounting to point out the refinement. . . . In short, we think that in the common understanding 'interest' means what is usually called interest by those who pay and those who receive the amount so denominated in bond and coupon, and that the words of the statute permit the deduction of that sum and do not refer to some esoteric concept derived from subtle and theoretic analysis."⁸

The Court's decision on the theory of bond premium has not changed: the premium is considered income, not a factor reducing the coupon rate of interest to the effective rate. But granted that bond premium is income, the second question still remains: when is the income realized?

The Old Colony case involved bond premiums received before March 1, 1913. The Court held that the premiums were income in the year they were received; they had therefore become capital before the Income Tax Amendment was adopted and could not be taxed under any subsequent income tax acts.

The constitutional question concerning the year when the income is taxable, however, is irrelevant for bonds issued at a premium since February 28, 1913. The Board has held that, on the accrual basis, the amortization of the premium over the life of the bonds properly reflects income;⁹ that is, the premium is gain or income which should be amortized over the life of

⁸ *Old Colony Railroad Company v. Commissioner*, 284 U.S. 552 (1932); see discussion of this case in an editorial note, *Harvard Law Review*, Vol. 45, p. 1116 (1931-32).

⁹ *Chicago and Northwestern Railway Company v. Commissioner*, 22 B.T.A. 1407, (1931), reversed on another point 66 F(2d) 61 (CAA-7th, 1933); *Fall River Electric Light Company v. Commissioner*, 23 B.T.A. 168 (1931); Regulations 111, Sec. 29.22(a)-17.

the bonds. On bonds issued at a premium before March 1, 1913 the premium is gain or income for the year the bonds were issued and should not be amortized over the life of the bonds.

2 *Bond discount*

Much of the inconsistency in the tax law between the treatment of income and deduction items arises from the constitutional problem of income realized before March 1, 1913. When income has been realized before the enactment of the 16th Amendment, it cannot later be taxed as income. In the case of deductions, income and capital are not strictly differentiated. The problem of a tax levied on what cannot constitutionally be taxed does not arise in handling deductions. Because of the absence of a constitutional barrier, the tax treatment of deductions may often more closely parallel accepted accounting treatment.

The Supreme Court has held that a taxpayer on the accrual basis may amortize discount and commissions on bonds issued before March 1, 1913 over the life of the bonds.¹⁰ The Old Colony case was specifically distinguished on the ground that it involved the question of income realized prior to the 16th Amendment. The Court seems, however, to have retreated from the theoretical position held in the Old Colony case that a bond premium is not a factor of the effective interest rate. In the Union Pacific case it approached nearer to accounting concepts:

"Both commissions and discount, as the Government concedes, are factors in arriving at the actual amount of interest paid for the use of capital procured by a bond issue. The difference between the capital realized by the issue and the par value, which is to be paid at maturity, must be added to the aggregate coupon payments in order to arrive at the total interest paid."

The regulations, Section 29.22(a)-17, on bond discount do not differentiate between bonds issued before and after March 1, 1913, but state generally: "If bonds are issued by a corpora-

¹⁰ *Helvering v. Union Pacific Railroad Company*, 293 U.S. 282 (1934).

tion at a discount, the net amount of such discount is deductible and should be prorated or amortized over the life of the bonds."

The Court, in the Union Pacific case, treated bond discount and commissions alike. The regulations do not mention the amortization of commissions and expenses; nevertheless, the practice of the Bureau of Internal Revenue is not to differentiate in the treatment of bond discount, expenses, and commissions.

3 *Treatment of unamortized discount and premium when bonds are redeemed*

The law is well established, at least with respect to taxpayers on the accrual basis, that bond discount must be amortized over the life of the bonds. Controversy exists, however, concerning the treatment of unamortized bond discount when bonds are redeemed. Since bonds are frequently retired at a premium, the premium paid upon redemption is an additional factor to be considered. Are these items of unamortized discount and premium paid on retirement deductible in the year of redemption? Are the deductions lost altogether? Or, in case the bonds are retired by exchange for a new issue, are the amounts to be amortized over some future period?

The law is not clearly settled on some of the problems arising in connection with the redemption of bonds; highly technical distinctions have been drawn with the emphasis often upon the form of the transaction. Bonds redeemed for cash are differentiated from bonds retired by exchange for a new issue. When bonds are redeemed for cash, the unamortized discount and the premium paid upon retirement are deductible in the year of retirement.¹¹ Although the cash used for the redemp-

¹¹ Present Treasury rulings are summarized in Cumulative Bulletin XIV-2, p. 58, (1935), revoking an earlier ruling that when the funds used for retirement were acquired from another bond issue, any unamortized discount and redemption premium should be amortized over the life of the new bonds. T.D. 4603 followed a series of cases holding for the taxpayers against the former interpretation.

tion may be obtained by the sale of another bond issue, the discount, premium, and expenses need not be amortized over the life of the new issue.¹² The theory is that the two bond issues are substantially separate transactions.

When bonds are retired by exchange, however, the unamortized discount and the premium are not deductible in the year of redemption but must be amortized over the life of the new issue.¹³ The theory is that the taxpayer merely substitutes a new obligation for the old; both the unamortized discount of the original bonds and the expenses of the exchange are costs of obtaining the new loan.

When bonds are exchanged for stock, unamortized discount and expenses may not be deducted. A new obligation has not been assumed for the old obligation. The unamortized discount and expense are considered capital costs in connection with the issuance of the stock. The conversion of bonds into stock is a readjustment of capital structure that does not result in either a deductible loss or a taxable gain.

4 *Treatment of unamortized discount in the case of reorganized corporations*

When reorganizations, mergers, and consolidations enter the picture, the problem of unamortized discount is further complicated. The general theory is that one corporation cannot deduct a discount on the bonds of another corporation. When there is a continuing corporate entity, the discount on the bonds of the merged or consolidated corporations can be deducted by the successor corporation. But a purchasing corporation, when there is no continuation of the corporate entity, cannot deduct the discount on the bonds of a purchased corporation. When assets are purchased and interest liability assumed, the payment in the form of redemption is a payment of

¹² *Helvering v. California Oregon Power Company*, 75 F(2d) 644 (C.A.-D.C. 1935).

¹³ *Great Western Power Company v. Commissioner*, 297 U.S. 543 (1936); cf. T.D. 4603, paragraph (c).

the purchase price of assets, that is, a capital transaction, not a payment of an interest liability of the payer.

In a case involving (a) several reorganizations accomplished by a transfer of assets and without merger or consolidation, and (b) the merger or consolidation of two other corporations, the amortization of discount was not allowed to be carried over to the reorganized corporations but was allowed to the merged or consolidated company.¹⁴ In reorganization cases, the loss by reason of the discount on the issue of bonds was held to be a loss of the issuing corporation inasmuch as, because of the discount, the transferor received a less valuable consideration upon the transfer of the assets. Under the reorganization section of the statute, however, this loss is not recognized. While the court admitted that it might be more satisfactory to allow the loss to be carried through to the successor corporation, no warrant for such carry-forward was found.¹⁵ In the case of consolidated or merged corporations, the court allowed the deduction for discount to be taken by the successor corporation. The distinction is that in the case of consolidation or merger, the successor corporation succeeds to the rights and liabilities of the constituent companies by operation of law, not by purchase; the successor corporation is treated as identical with the original obligor.

Accounting Treatment

The amortization of bond premium and discount over the life of the bonds is standard accounting practice. R. H. Montgomery states the matter concisely:

“Any use of bond premiums other than to reduce the interest charges of future years will result in the income accounts of the

¹⁴ *American Gas and Electric Company v. Commissioner*, 85 F(2d) 527 (CCA-2d, 1936). See also *Helvering v. Metropolitan Edison Company*, 306 U.S. 522 (1939): deduction allowed to transferee when merger either statutory or de facto.

¹⁵ There is no inequity in denying the deduction to the transferee; the discount is part of the obligation that is assumed, and hence part of the cost. S.S. Surrey, *Assumption of Indebtedness in Tax-Free Exchanges*, *Yale Law Journal*, Vol. 50, No. 1, p. 22 (1940).

future being inaccurate. Conversely, when bonds are sold at a discount, the amount of the discount is treated as a deferred charge and amortized over the life of the bonds."¹⁶

Agreement on the proper method of treating premium and discount should not be taken as evidence that improper methods have not been and may still be used in unaudited statements. Low earnings in one year can be bolstered by showing the entire amount of premium as income in that year, and the income statement can be entirely relieved of the discount and expenses of issue by charging these amounts directly to surplus. The latter move has been especially tempting in the past. The charge to surplus will give a book income in excess of taxable income, and in this case, in excess of any reasonable 'true income' figure.¹⁷

The special tax treatment of premium on bonds issued before February 28, 1913 has no counterpart in business accounting. As with other distinctions arising from the 1913 date, to note the tax rules and the grounds therefore suffices.

The proper treatment of unamortized bond discount and expense at a time of refunding has been a popular subject of controversy among accountants for some time. The arguments in favor of the various methods of accounting for unamortized discount present concisely many of the most fundamental

¹⁶ *Auditing Theory and Practice* (Ronald Press, 5th ed., 1934), p. 365. The simplest and most common practice is to write off premium and discount in equal amounts over the period covered by the bonds. A more complicated procedure has been advocated and used in the accounts of financial institutions whereby discount or premium is amortized on a sinking fund basis to give a constant rate of interest on the actual amount received by the company.

¹⁷ As an extreme example of special treatment, H. R. Hatfield notes the early practice of railroads in charging all bond discount to construction cost, on the theory that the funds were necessary for construction and that accordingly the discount too was attributable to it. This ignores the fact that coupon and discount together make up the full return to the purchaser and that one is dependent upon the other. This procedure was ruled out by the Interstate Commerce Commission, except for the part attributable to the period of construction, which may be conceived of as a make-ready period during which no income could arise and in which, accordingly, expenses are deferred. *Accounting, Its Principles and Problems* (Appleton-Century, 1927), pp. 230-1.

differences of opinion among accountants on the nature of income. The general arguments on the appropriateness of certain items as surplus charges in contrast to current income or deferred charges were discussed briefly in the Introduction. They are now developed more fully.¹⁸

Unamortized discount might be treated in four ways: by a charge to income in the year the securities are retired, by a charge to surplus, by continuation as a deferred charge to be written off over what would have been the normal life of the original securities, or by continuation as a deferred charge to be written off over the life of the new refunding issue, if any. Each method has had its advocate.¹⁹

The write-off, either to income or to surplus, in the year of retirement is justified on the ground that all events have occurred that make it necessary to write completely off the books the deferred charge in the form of bond discount. To carry it beyond the actual life of the bonds would be to burden future periods with an expense altogether unrelated to them and to overstate net worth until the discount was fully written off. To continue to carry the bond discount as an asset in the form of a deferred charge would be as improper, it is contended, as to continue to carry machinery previously disposed of as an asset. Since future income should not be burdened by charges unrelated to the future, and since future balance sheets should not reflect an asset that has no current significance, the write-off should be made at once.

Those favoring the charge to current income prefer it to a charge to surplus on the ground that a real expense is involved and that income must bear the burden to avoid overstating total income over the years even though the income of one year is distorted. It may be contended also that the charge to a single

¹⁸ For a general discussion of alternative methods and the arguments, see *Accounting Research Bulletin No. 2, Unamortized Discount and Redemption Premium on Bonds Refunded* (1939), and its Supplement, No. 18 (1942).

¹⁹ H. R. Hatfield, T. H. Sanders, and N. L. Burton, *Accounting Principles and Practices* (Ginn, 1940), pp. 274-5.

year of the entire balance of unamortized discount really does not distort the current year's income since the decision to retire the bonds was actually made in the current year and all associated gains and losses are accordingly attributed to that year.

The charge to surplus may be preferred for various reasons. It may be claimed that the entire bond discount should have been written off evenly over the actual life of the bonds. Since the income calculations of prior years cannot be revised to give the earlier years the additional charges they should have had, the best solution is to charge this amount to surplus, inasmuch as surplus presumably reflects the accumulated retained net income of all preceding years. In somewhat simpler fashion, the charge to surplus may be favored because the write-off of unamortized discount is considered an unusual, nonrecurring charge, regardless of whether it is properly attributable to the past or the present. To make current reported income reflect only the types of charge and credit that have existed in the past and may be expected to appear in the future, a charge to surplus is considered appropriate. Or the charge to surplus may be justified negatively as a lesser evil instead of positively as an absolutely correct procedure. The distortion of a single year's income by a charge properly attributable to several years may be considered a greater evil than the overstatement of aggregate reported income over the years.

An entirely different point of view is taken by those who hold that even though the original bonds have been retired, part of the bond discount is still attributable to later periods. Since any unamortized discount must ultimately be charged to income or surplus, a continuation of the annual expense over the original planned term of issue is deemed to give the best measure of the total cost of borrowed money.

Though a case can be made for continuing to write off the unamortized discount on retired bonds over the period originally set for them, there seems no reason to extend the period

of write-off over the entire life of the new securities issued in a refinancing. The call or maturity date of the new bonds has no conceivable relation to the life of the old ones, and an extension of the write-off of charges connected with the old bonds far beyond the due date of the old bonds imposes a burden on income of the later years for something entirely unrelated to them.

This discussion of accounting procedures does not require consideration of the complex subject of the relative financial advantages of refinancing or continuing with an old issue until its maturity. Such a consideration would require an entirely different type of analysis and would necessitate assumptions with respect to future as compared with present interest rates, ultimate final repayment or continued refinancing, premium on call prior to maturity, and other matters.

Conclusion

The treatment of bond premium and discount on original issues is substantially the same for both tax and business accounting, except in the case of a premium on bonds issued before March 1, 1913. But the tax rules on unamortized premium and discount on bonds retired before their normal maturity date make arbitrary distinctions according to the form of the transaction. Furthermore, in the case of an exchange of new for retired bonds, the tax requirement that premium or discount be written off over the life of the new bonds is directly contrary to accepted accounting practice. When the differences in tax and business treatment have to do merely with the time of write-off, they will of course eventually balance out. But a charge or credit to surplus for business purposes will make aggregate reported income permanently larger or smaller than taxable income. Likewise, the tax requirement that an unamortized charge or credit be closed to a capital account when bonds are exchanged for stock will also cause a permanent difference between taxable and business income, except in the

rather unlikely case that it is handled in the same way for book purposes.²⁰

The considerable variety of practice on the accounting treatment of bond discount and premium has perhaps justified arbitrary tax rulings. The recent definite and well reasoned statement by the American Institute of Accountants seems to be sufficiently authoritative to provide a standard of good accounting practice for the future.²¹ In general, two methods are approved: amortization over the remainder of the original life of the retired issue or a direct charge to earned surplus. Amortization over the life of the new issue is definitely disapproved. Bonds retired from the proceeds of new issues are not distinguished from those exchanged directly. The tax requirement that amortization be spread over the life of new issues in the case of an exchange is thus in direct contradiction to authoritative accounting doctrine and might well be reviewed under the general provisions of Section 41—that income for tax purposes should accord with the method of accounting regularly used by the taxpayer. If for book purposes the option of a direct charge to surplus is taken, a charge to income for tax purposes seems reasonable, thereby closing out the accounts on the books for both purposes.

²⁰ Cf. Securities and Exchange Commission, *Accounting Series Release 10* (Dec. 23, 1938), for a definite requirement that unamortized discounts and redemption premium be written off either to income or to surplus in the year in which bonds are exchanged for stock.

²¹ Accounting Research Bulletins 2 and 18.