problems presented be considered academic after the recent decision *Milwaukee County v. White Co.*[39] holding tax judgments entitled to full faith and credit, and in view of the further possibility that tax assessments made with "due process of law" may be accorded an extraterritorial effect.[40]

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**Income Tax—Distinction between Gift and Compensation—**[Federal].—All the stockholders of *A* Corporation joined in forming *B* Corporation, transferring to it funds of *A* Corporation, which were then used to purchase assets of *C* Corporation. *C* Corporation then acquired the entire stock of *A*. *B* Corporation then distributed $607,500 of the corporate assets to petitioner and other designated former and present employees of *A* "as a bonus. . . . in recognition of the valuable and loyal services" rendered *A*. *B* charged these payments to its surplus account; no attempt was made by the corporations involved to deduct them for federal income tax purposes. The taxpayer treated the payment as a gift deductible from gross income.[1] The Board of Tax Appeals and the Circuit Court of Appeals agreed with the Commissioner of Internal Revenue that the payment to petitioner was not a gift but was compensation. On appeal, *held* (four justices dissenting), reversed. Although the question was a mixed one of law and fact, there was *no evidence* to support a finding that the payment was compensation. *Bogardus v. Helvering*.[2]

If the payment is treated as compensation, it is taxable to the recipient as income[3] and is deductible by the payor as expense in computing his income tax.[4] If the payment is treated as a gift, it is not taxable to the recipient, is not deductible by the payor in computing his income tax, and is taxable to the payor as a gift.[5] Which determination will yield maximum revenue depends upon the particular case.[6]

On payments up to approximately a million dollars the income tax rate is decidedly greater than the gift tax rate.[7] So sharp a difference in treatment suggests a difference

[39] 296 U.S. 268 (1935).

[40] Goodrich, Conflict of Law Since the Restatement, 23 Am. Bar A. J. 119, 121 (1937); Hazelwood, The Full Faith and Credit Clause as Applied to Enforcement of Tax Judgments, 19 Marq. L. Rev. 10 (1934); 22 Marq. L. Rev. 54 (1937); 45 Yale L. J. 339, 350 (1936); *cf.* Moore v. Mitchell, 30 F. (2d) 600 (C.C.A. 2d 1929) aff'd on other grounds, 281 U.S. 18 (1930).

[1] 48 Stat. 686 (1934), 26 U.S.C.A. § 22 (1934). "§ 22. Gross Income. (a) General definition: 'Gross income' includes gains, profits, and income derived from salaries, wages, or compensation for personal services, of whatever kind and in whatever form paid . . . (b) Exclusions from gross income. . . . (3) Gifts, bequests and devises. The value of property acquired by gift, bequest, devise, or inheritance . . . ;"

[2] 302 U.S. 34 (1937), reversing 88 F. (2d) 646 (C.C.A. 2d 1937).

[3] In such a case the recipient may also be subjected to an increased rate if the payment moves him into a higher bracket.

[4] 48 Stat. 687 (1934), 26 U.S.C.A. § 23 (1934); see Lucas v. Ox Fibre Brush Co., 281 U.S. 115 (1930).

[5] 48 Stat. 758–761 (1934), 26 U.S.C.A. §§ 550–551 (1934).

[6] For example, a payment of $100,000 to a single recipient will produce $13,940 more revenue if treated as compensation; but the same payment if made in $5,000 shares to twenty recipients will yield $4,060 more revenue if treated as a gift.

[7] 48 Stat. 684 (1934), 26 U.S.C.A. §§ 11–12 (1934); 48 Stat. 758–761 (1934), 26 U.S.C.A. §§ 550–551 (1934).

in policy. It is clear from its history[8] that the gift tax is primarily a stop-gap for the estate tax, which in turn was directed at the transfer of large accumulations of capital. Payments such as those in the instant case do not fit easily into this picture.

The history of the litigation in these cases[9] indicates that a usable test of compensation is needed. Various criteria have been suggested. The presence of a legal obligation to make the payment is not an adequate test since tipping, for example, seems clearly to be compensation[10] and is frequently substituted for regular wages. Consideration is perhaps[11] useful in determining the enforcibility of promises, but not as a criterion for classifying executed transactions for tax purposes. Again, the probability that the payment will be periodically made, as in the case of tipping, or repeated bonus payments, is useful, but does not cover the case of the single large payment. Nor should the name applied to the transaction by the parties, or their method of bookkeeping,[12] be conclusive, although it is indicative of what they thought they were doing. The same is true of the parties' attempts to distribute the tax burden among themselves.[13] Nor can the nature of the payment be tested by asking whether it constitutes an expense to the payor, for in the difficult cases this is merely a rephrasing of the original question.

The emphasis in the cases has been placed on the above factors taken together as indications of the mental state of the payor,[14] rather than on any one as a conclusive criterion. In his dissent, Brandeis, J., states precisely the contrasting mental attitudes: (1) to make requital for services already fully compensated; (2) to show "good will, kindliness, or esteem to persons who happen to have served but *who are paid without thought to make requital for the services*."[15] Since it is clear that in most cases good will, kindliness, and esteem, coexist with a desire to requite, in ascertaining compensation emphasis is properly placed on the absence of a desire to requite rather than on the presence of good will, etc. Thus, it can almost be said categorically that one does not make a gift to one's employees.

The easiest case short of a straight salary payment, then, is that of a voluntary payment to a group of present or former employees, graduated on a scale similar to the salary scale. But a troublesome case occurs where there is payment to a single employee. Even here it has been held that the voluntary payment of a pension to a

[8] 5 Univ. Chi. L. Rev. 522 n. 10 (1938).

[9] These payments by Unopco Corp. were litigated in three different Circuit Courts of Appeal in addition to the principal decision. These three courts held that the payments were compensation. Walker v. Comm'r., 88 F. (2d) 61 (C.C.A. 1st 1937); Hall v. Comm'r., 89 F. (2d) 441 (C.C.A. 4th 1937); Simpkinson v. Comm'r., 89 F. (2d) 397 (C.C.A. 5th 1937). See also the El Paso R.R. litigation: Barnes v. Comm'r., 17 B.T.A. 1002 (1929); Schumacher v. United States, 55 F. (2d) 1007 (Ct. Cl. 1932); Bass v. Hawley, 62 F. (2d) 721 (C.C.A. 5th 1933). Magill, Taxable Income c. 10 (1936), contains a good collection of cases.

[10] Treas. reg. 45, art. 32. See also Old Colony Trust Co. v. Comm'r., 279 U.S. 716 (1929).

[11] See discussion of enforcing gratuitous promises. 31 Ill. L. Rev. 390 (1936); 5 Univ. Chi. L. Rev. 464 (1938).

[12] Bass v. Hawley, 62 F. (2d) 721 (C.C.A. 5th 1933).

[13] Old Colony Trust Co. v. Comm'r., 279 U.S. 716 (1929); Levey v. Helvering, 68 F. (2d) 411 (App. D.C. 1933).

[14] Magill, Taxable Income c. 10 (1936).

[15] 302 U.S. 34, 45 (1937) (*italics supplied*).

retired employee was compensation;[16] the same result has been reached where the payment is a lump sum.[17] Also somewhat troublesome are cases in which a technical employment relation never existed between payor and recipient. In the case of tips, the person making the payment is certainly not the employer; yet this is clearly compensation. Again where, as here, the services were rendered to the stockholders as *A* corporation and the payment made by the same stockholders as *B* corporation, the fact that the *B* corporation had never employed the recipients is hardly significant.[18] It is clear then that for these purposes, "employer" should mean no more than the person to whom the services are rendered. Conceivably, even where the services are not rendered to the payor, the payment might be regarded as compensation. For example, the payment by a son of the medical expenses of his mother would be compensation to the doctor, although a gift to the mother.[19]

Even where the payment is completely incommensurate with the value of the services rendered it should be treated as compensation for tax purposes. But calling it compensation does not foreclose the possibility that the same payment might be regarded as an unjustified gift when there is a question not of taxation but of protecting the rights of minority stockholders.[20]

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**Income Tax—Stock Dividends—Cost of Zero—Statute Drafted under Mistake—[Federal].**—A corporation having both common and preferred stock outstanding, declared a dividend on its common stock payable in preferred. Later the corporation purchased the dividend shares. The Board of Tax Appeals decided that there had not been such redemption of the shares by the corporation as to constitute a dividend taxable under section 115(g), but that the receipt of the dividend by the stockholder was income. The Circuit Court of Appeals held that the receipt of the dividend was constitutionally income, but was exempt under section 115(f) which provided "a stock dividend shall not be subject to tax";[1] and further that no part of the sale proceeds could be taxed since, applying the rule used for the sale of gifts, the fair market value of the stock at the date of receipt and the date of sale were the same. On *certiorari* to the Supreme Court, *held* reversed. Although the receipt of the dividend was not taxable because of the statutory exemption, the entire proceeds from the sale were taxable since the cost of the dividend was zero. *Helvering v. Gowran.*[2]

This case completes the pattern begun by *Eisner v. Macomber*[3] and left unfinished by the *Koshland* case.[4] In holding a dividend of preferred on common, where both are outstanding, within the Sixteenth Amendment the Court fulfilled the expectation

[16] Beatty v. Comm'r., 7 B.T.A. 726 (1927).

[17] Fisher v. Comm'r., 59 F. (2d) 192 (C.C.A. 2d 1932).

[18] Bass v. Hawley, 62 F. (2d) 721 (C.C.A. 5th 1933).

[19] Consequently, even such payments as the Nobel Prize might seem to be payments for services rendered to the public and their tax exemption attributed to the policy of encouraging such services. C.C.H. Tax Service (1938) Vol. 1, ¶99.05; cf. ¶ 52.36.

[20] See Rogers v. Hill, 289 U.S. 582 (1933); Stevens, Handbook of the Law on Private Corporations 217–22, 628–33 (1936).

[1] 45 Stat. 791, 822 (1928), 26 U.S.C.A. § 115(f) (Supp. 1936).

[2] 58 S. Ct. 154 (1937). [3] 252 U.S. 189 (1920). [4] 298 U.S. 441 (1936).