

What is Income and What is Compensation?

*"There is a clear distinction between 'profit' and 'wages' and **compensation for labor CANNOT be regarded as profit within the meaning of the law.** The word 'profit', as ordinarily used, means the **gain made upon any business or investment--a different thing altogether from mere compensation for labor.**"*

[Oliver v. Halstead, 86 S.E.2d. 859]

*"Income within the meaning of the Sixteenth Amendment and the Revenue Act, means 'gain'... and in such connection **'Gain' means profit**...proceeding from property, severed from capital, **however invested** or employed, and coming in, received, or drawn by the taxpayer, for his separate use, benefit and disposal... **Income is not a wage or compensation for any type of labor.**"*

[Stapler v. U.S., 21 F.Supp. 737 at 739]

"...Congress has taxed income [profits and gains] not compensation"

[Connor v. U.S., 303 F. Supp., 1187 (1969)]

*"The phraseology of form 1040 is somewhat obscure...But it matters little [what the form says]; the statute and **the statute alone determines what is income to be taxed.** It taxes income 'derived' from many different sources; **ONE DOES NOT 'DERIVE INCOME' [gains and profits] BY RENDERING SERVICES AND CHARGING FOR THEM.**"*

[Edwards v. Keith, 231 F.. 1. (Emphasis added)]

"The labor of a human being is not a commodity or article of commerce..."

[15 U.S.C. §17]

*"There would seem to be no room to doubt that the word [income] must be given the meaning **in all Income Tax Acts** of Congress that was given to it in the **Corporation Excise Tax Act** and what that meaning is has now become **definitely settled** by decisions of the court." (Emphasis added)*

[Merchant's Loan & Trust Company vs. Smietanka, 255 U.S., pp 518, 519 (1921)]

"Income" has been taken to mean the same thing as used in the Corporation Excise Tax Act of 1909, in the Sixteenth Amendment and in the various revenue acts subsequently passed"

[Bowers v. Kerbaugh-Empire Co., 271 U.S. 174]

*"Decided cases have made the **distinction between wages and income** and have refused to equate the two."*

[Central Illinois Publishing Service v. U.S., 435 U.S. 31]

"Constitutionally the only thing that can be taxed by Congress is 'income.'" And the tax actually imposed by Congress has been on net income as distinct from gross income. THE TAX IS NOT, NEVER HAS BEEN, AND COULD NOT CONSTITUTIONALLY BE UPON "GROSS RECEIPTS" ..."

[Anderson Oldsmobile, Inc. v. Hofferbert, 102 F.Supp. 902]

*"Among these **unalienable rights**, as proclaimed in the Declaration of **Independence is the right of men to pursue their happiness, by which is meant, the right any lawful business or vocation, in any manner not inconsistent with the equal rights of others,*** which may increase their prosperity or develop their faculties, so as to give them their highest enjoyment...It has been well said that, **THE PROPERTY WHICH EVERY MAN HAS IS HIS OWN LABOR, AS IT IS THE ORIGINAL FOUNDATION OF ALL OTHER PROPERTY SO IT IS THE MOST SACRED AND INVIOABLE...**"

[Butchers' Union Co. v. Crescent City Co., 111 U.S. 746. 1883]

That definition of income was clearly given in 1918 in the Supreme Court:

*"Whatever difficulty there may be about a precise and scientific definition of 'income,' it imports, as used here [in the Internal Revenue Code] the idea of **gain or increase** arising from **corporate activities**... We must **reject** in this case...**the broad contention submitted in behalf of the Government that all receipts, everything that comes in -- are income within the proper definition of the term 'gross income'...**"*

[Doyle v. Mitchell, 247 U.S. 179, 330]

That definition has been consistent in other cases:

"Certainly the term "income" has no broader meaning in the 1913 Act than in that of 1909 (see [Stratton's Independence v. Howbert, 231 U.S. 399, 416, 417](#)), and for the present purpose we assume that there is no difference in its' meaning as used in the two acts."

[Southern Pacific C. v. John Z. Lowe, United States Collector of Internal Revenue, 247 U.S. 330, 335 (1918)]

"Property acquired by gift is excluded from gross income."

[Commissioner of IRS v. Duberstein, 80 S.Ct. 1190]

"An income tax is neither a property tax nor a tax on occupations of common right, but is an EXCISE tax...The legislature may declare as 'privileged' and tax as such for state revenue, those pursuits not matters of common right, but it has no power to declare as a 'privilege' and tax for revenue purposes, occupations that are of common right."

[Simms v. Ahrens, 271 S.W. 720]

*"...the definition of 'income' approved by this court is: The gain derived from capital, from labor, or from both combined, provided it be understood to include **profits gained through sale or conversion of capital assets.**"*

[Eisner v. Macomber, 252 US 189]

"Reasonable compensation for labor or services rendered is not profit"

[Laureldale Cemetery Assoc. vs Matthews, 345 Pa. 239]

Further, the Supreme Court ruled in that:

*"...it becomes essential to distinguish between what is and what is not "income," according to **truth and substance**, without regard to form. **Congress cannot, by any definition it may adopt, conclude the matter, since it cannot by legislation, alter the***

Constitution, from which it derives its power to legislate, and within whose limitations, alone, that power can be lawfully exercised..." [income is] **Derived-from-capital -- the gain-derived-from-capital, etc.** Here we have the essential matter -- not gain **accruing** to capital, not a growth or increment of value in the investment; but a gain, a **profit**, something of exchanged value...**severed from the capital** however invested or employed, and coming in, being "derived," that is received or drawn by the recipient for his separate use, benefit and disposal -- **that is the income derived from property. Nothing else answers the description ...**"

[Eisner vs. Macomber, 252 U.S. 189]

Congress has not taxed Compensation:

"Income is realized gain."

[Schuster v. Helvering, 121 F.2d. 643]

"..whatever may constitute income, therefore, must have the essential feature of gain to the recipient. This was true at the time of Eisner v. Mcomber, it was true under section 22(a) of the Internal Revenue Code of 1938, and it is likewise true under Section 61(a) of the IRS code of 1954. **If there is not gain, there is not income. CONGRESS HAS TAXED INCOME, NOT COMPENSATION"**!

[Conner v. U.S. 303 F.Supp. 1187]

"The Treasury cannot by interpretive regulations, make income of that which is not income within the meaning of the revenue acts of Congress, nor can Congress, without apportionment, tax as income that which is not income within the meaning of the 16th Amendment."

[Helvering v. Edison Bros. Stores, 133 F.2d. 575]

"... the government can collect the tax from a district court suitor by exercising it's power of distraint... but we cannot believe that compelling resort to this extraordinary procedure is either wise or in accord with congressional intent. **Our system of taxation is based upon VOLUNTARY ASSESSMENT AND PAYMENT , NOT UPON DISTRAINT"** [Footnote 43] If the government is forced to use these remedies(distraint) on a large scale, it will affect adversely the taxpayers willingness to perform under our VOLUNTARY assessment system.

[Flora v. U.S., 362 U.S. 145]

"Treasury regulations can add nothing to income as defined by Congress."

[Blatt Co. v. U.S., 59 S.Ct. 186]

The following rulings are quoted from **Conner v. United States**, 303 F. Sup. 1187 (1969) pg. 1191.

"...The meaning of income in its everyday sense is a gain recovered by an individual in a given period of time." Webster's Seventy New Collegiate Dictionary, p. 425 "**Income is nothing more or less than realized gain.**" Shuster v. Helvering, 121 F. 2d 643 (2nd Cir. 1941) "**It [Income] is not synonymous with receipts.**" 47 C J S Internal Revenue 98, p. 226."

Issues relative to the 16th Amendment and other cases:

*“After further consideration, we adhere to that view and accordingly hold that **the Sixteenth Amendment does not authorize or support the tax in question.**”*
[Evens v. Gore, 253 U.S. 245, (A tax on salary of federal judges)]

“The 16th Amendment does not authorize laying of an income tax upon one person for the income derived solely from another.”[wages]
[McCutchin v. Commissioner of IRS, 159 F.2d. 472]

“Income” has been taken to mean the same thing as used in the Corporation Excise Tax Act of 1909, in the Sixteenth Amendment and in the various revenue acts subsequently passed”
[Bowers v. Kerbaugh-Empire Co., 271 U.S. 174]

*“The conclusion reached in the Pollock Case did not in any degree involve holding that income taxes generically and necessarily came within the class of direct taxes on property, but on the contrary recognized the fact that **taxation on income was in its nature an excise entitled to be enforced as such...**”*
[Brushaber v. Union Pacific R.R. Co., 240 U.S. 1]

Claim of right doctrine. As contemplated under doctrine of adverse possession is simply that claimant is in possession as owner, with intent to claim the land as his or her own, and not in recognition of or subordination to record title owner. *Sisson v. Koelle*, 10 Wash.App. 746, 520 P.2d 1380, 1384. In taxation, a judicially imposed doctrine applicable to both cash and accrual basis taxpayers which holds that an amount is includible in income upon actual or constructive receipt if the taxpayer has an unrestricted claim to such amounts. A payment received under a claim of right is includible in income even though there is a possibility that all or part of it may have to be returned. *North American Oil Consolidated v. Burnet*, 286 U.S. 417, 52 S.Ct. 613, 76 L.Ed. 1197.



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Sec. 1341. - Computation of tax where taxpayer restores substantial amount held under claim of right

(a) General rule

If -

- (1) an item was included in gross income for a prior taxable year (or years) because it appeared that the taxpayer had an unrestricted right to such item;

- (2) a deduction is allowable for the taxable year because it was established after the close of such prior taxable year (or years) that the taxpayer did not have an unrestricted right to such item or to a portion of such item; and
- (3) the amount of such deduction exceeds \$3,000, then the tax imposed by this chapter for the taxable year shall be the lesser of the following:
- (4) the tax for the taxable year computed with such deduction; or
- (5) an amount equal to -
 - (A)

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the tax for the taxable year computed without such deduction, minus

(B)

the decrease in tax under this chapter (or the corresponding provisions of prior revenue laws) for the prior taxable year (or years) which would result solely from the exclusion of such item (or portion thereof) from gross income for such prior taxable year (or years).

For purposes of paragraph (5)(B), the corresponding provisions of the Internal Revenue Code of 1939 shall be chapter 1 of such code (other than subchapter E, relating to self-employment income) and subchapter E of chapter 2 of such code.

(b) Special rules

(1)

If the decrease in tax ascertained under subsection (a)(5)(B) exceeds the tax imposed by this chapter for the taxable year (computed without the deduction) such excess shall be considered to be a payment of tax on the last day prescribed by law for the payment of tax for the taxable year, and shall be refunded or credited in the same manner as if it were an overpayment for such taxable year.

(2)

Subsection (a) does not apply to any deduction allowable with respect to an item which was included in gross income by reason of the sale or other disposition of stock in trade of the taxpayer (or other property of a kind which would properly have been included in the inventory of the taxpayer if on hand at the close of the prior taxable year) or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business. This paragraph shall not apply if the deduction arises out of refunds or repayments with respect to rates made by a regulated public utility (as defined in section 7701(a)(33) without regard to the limitation contained in the last two sentences thereof) if such refunds or repayments are required to be made by the Government, political subdivision, agency, or instrumentality referred to in such section, or by an order of a court, or are made in settlement of litigation or under threat or imminence of litigation.

in the principal business of the taxpayer, unless with the approval of the Commissioner change to a different method is authorized, and then upon such terms and conditions and in accordance with such regulations as the Commissioner, with the approval of the Secretary, may prescribe.

(e) **DISTRIBUTIONS BY CORPORATIONS.**—Distributions by corporations shall be taxable to the shareholders as provided in section 115.

(f) **DETERMINATION OF GAIN OR LOSS.**—In the case of a sale or other disposition of property, the gain or loss shall be computed as provided in section 111.

(g) **GROSS INCOME FROM SOURCES WITHIN AND WITHOUT UNITED STATES.**—

For computation of gross income from sources within and without the United States, see section 119.

(h) **FOREIGN PERSONAL HOLDING COMPANIES.**—

For provisions relating to gross income of foreign personal holding companies and of their shareholders, see section 334.

(i) **CONSENT DIVIDENDS.**—

For inclusion in gross income of amounts specified in shareholders' consents, see section 28.

(j) **INCOME FROM MORTGAGES MADE OR OBLIGATIONS ISSUED BY JOINT STOCK LAND BANKS.**—

For taxable status of income derived from mortgages made or obligations issued by joint stock land banks, see section 3799.

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

(a) **EXPENSES.**—

(1) **IN GENERAL.**—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; traveling expenses (including the entire amount expended for meals and lodging) while away from home in the pursuit of a trade or business; 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.

(2) **CORPORATE CHARITABLE CONTRIBUTIONS.**—No deduction shall be allowable under paragraph (1) to a corporation for any contribution or gift which would be allowable as a deduction under subsection (q) were it not for the 5 per centum limitation therein contained and for the requirement therein that payment must be made within the taxable year.

(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.

(c) **TAXES GENERALLY.**—Taxes paid or accrued within the taxable year, except—

(1) Federal income, war-profits, and excess-profits taxes (other than the excess-profits tax imposed by section 106 of the Revenue Act of 1935, 49 Stat. 1019, or by section 600 of this title);

(2) income, war-profits, and excess-profits taxes imposed by the authority of any foreign country or possession of the United States; but this deduction shall be allowed in the case of a taxpayer who does not signify in his return his desire to have to any extent the benefits of section 131 (relating to credit for taxes of foreign countries and possessions of the United States);

(3) estate, inheritance, legacy, succession, and gift taxes; and

(4) taxes assessed against local benefits of a kind tending to increase the value of the property assessed; but this paragraph