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Federal Taxation: Contest Prizes—Taxable Income or Gift?

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CASE COMMENTS

FEDERAL TAXATION: CONTEST PRIZES — TAXABLE INCOME OR GIFT?

United States v. Robertson, 190 F.2d 680 (10th Cir. 1951)

Petitioner, while a professor of music, had composed a symphony during a three-year period ending in 1939. The Detroit Symphony Orchestra, in 1945, offered a prize for the best musical composition by a native composer of the Americas. Petitioner took the score from his files and submitted it along with an official entry blank. The symphony did not become the property of the Detroit Symphony Orchestra nor did the petitioner perform any additional work on the score. In 1947 the petitioner received \$25,000 as first prize. HELD, the prize was taxable income and not a gift.

Fellowship awards have already been held by administrative ruling to fall under the holding of the instant case. Grants from the M Foundation to (1) a professor for research in structural chemistry, (2) a writer for finishing a novel, (3) a professor for research in botany, and (4) a researcher for study of economics and political science were all held taxable to the recipients. In each instance the recipient selected his own program, retained all rights to his work, and was in no way controlled by the M Foundation.¹ The present attitude of the Bureau appears to be that a grant for research or other scholarly work is taxable unless it is made for the purpose of furthering the recipient's own education.

If an award is determined not to be a gift, it is automatically placed in the category of taxable income, on the ground that the sweeping terms in Section 22 (a) of the Internal Revenue Code require a broad construction. On the other hand, the provision for exclusion of gifts from gross income² should be construed strictly as being a limitation on Section 22 (a).³

General standards for distinguishing taxable income from gifts are apparently based on relationships between the payor and recipient with respect to motive, intent, and consideration, and different weight is given to these elements in various combinations.

¹1951 INT. REV. BULL. No. 17 at 2 (1951).

²INT. REV. CODE §22 (b) (3).

³Commissioner v. Jacobson, 336 U.S. 28 (1949).

When a payor is motivated by some commercial purpose such as publicity or business promotion, the contest award is very likely to be placed in the category of income.⁴ On the other hand, the motive may be to achieve a public purpose completely apart from any private objective, and weight is given to that factor in holding the payment a gift.⁵ If the award winner has been motivated by a desire to get the award money rather than by a pure compulsion to achieve distinction in a noncommercial endeavor, that motivation tends to a finding of taxable income.⁶ As pointed out in *Helvering v. American Dental Co.*,⁷ motive is not usually regarded as a significant element.

Donative intent of the payor in particular has been considered a basic element of gifts,⁸ and that intent is determined by reference to all the facts and circumstances surrounding the transaction.⁹ Presumptions against the transfer being intended as a gift sometimes arise from the relation of parties, for example, employer-employee.¹⁰ Particular facts also give rise to a presumption of intent, for example, a donor treating payment as a deduction in arriving at taxable net income.¹¹ A directly expressed intent on the part of the payor does not necessarily determine whether the payment is a gift or is taxable income.¹²

Consideration is often held to be the essential and controlling element in deciding whether or not a payment is a gift.¹³ Just what amounts to consideration has given the courts some difficulty, and the extremes are especially apparent in the contest award or prize cases. The act of receiving information on the telephone that a prize has been awarded does not constitute consideration,¹⁴ but compliance

⁴Herbert Stein, 14 T.C. 494 (1950). *But cf.* *Helvering v. American Dental Co.*, 318 U.S. 322 (1943).

⁵McDermott v. Commissioner, 150 F.2d 585 (D.C. Cir. 1945). *But cf.* Frederick v. Waugh, P-H 1950 TC MEM. DEC. ¶ 50,095 (1950).

⁶McDermott v. Commissioner, 150 F.2d 585 (D.C. Cir. 1945).
7318 U.S. 322 (1943).

⁸Bogardus v. Commissioner, 302 U.S. 34 (1937).

⁹Botchford v. Commissioner, 81 F.2d 914 (9th Cir. 1936); Estate of McAdow, 12 T.C. 311 (1949).

¹⁰Van Dusen v. Commissioner, 166 F.2d 647 (9th Cir. 1948).

¹¹Willkie v. Commissioner, 127 F.2d 953 (6th Cir. 1942); Herbert Stein, 14 T.C. 494 (1950).

¹²Schall v. Commissioner, 174 F.2d 893 (5th Cir. 1949).

¹³Roberts v. Commissioner, 176 F.2d 221 (9th Cir. 1949).

¹⁴Pauline C. Washburn, 5 T.C. 1333 (1945).

with rules of a contest,¹⁵ such as answering questions or working puzzles, amounts to sufficient consideration to make the payment of the prize taxable income to the recipient. Until the instant case there appeared to be some distinction based on (1) time of consideration, whether already given as in *Bogardus v. Commissioner*,¹⁶ or to be given in the future as in *Van Dusen v. Commissioner*,¹⁷ and (2) type of work involved, whether scholarly or charitable as in *McDermott v. Commissioner*¹⁸ and *Schall v. Commissioner*,¹⁹ or manual as in a case where a laborer receives money from payor for mowing the lawn of payor's neighbor.²⁰

The distinctions between gifts and taxable income are obviously in a state of confusion. It is very important to separate the decisions according to the level at which they are made — namely, administrative tribunals, circuit courts, and the Supreme Court. According to the *Bogardus* and *Jacobson*²¹ decisions in the Supreme Court, donative intent is still an important factor. In view of the *McDermott* case and the instant case there is a pronounced conflict in the circuits as to the controlling standards. By administrative rulings of the commissioner, consideration of the most meager type takes payments from the category of gifts and renders them taxable income. Whether the award winner has to pay a tax or not would appear to be determined to a considerable extent by which litigation ladder he climbs and how high he climbs it.

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¹⁵E.T. 13267, 1950-1 CUM. BULL. 9.

¹⁶302 U.S. 34 (1937).

¹⁷166 F.2d 647 (9th Cir. 1948).

¹⁸150 F.2d 585 (D.C. Cir. 1945).

¹⁹174 F.2d 893 (5th Cir. 1949).

²⁰Herbert Stein, 14 T.C. 494 (1950).

²¹*Commissioner v. Jacobson*, 336 U.S. 28 (1949).