Income from Illicit Transactions.—In *United States v. Sullivan*,[44] the Court held that gains derived from illicit traffic were taxable income under the act of 1921.[45] Justice Holmes wrote, for the unanimous Court: "We see no reason . . . why the fact that a business is unlawful should exempt it from paying the taxes that if lawful it would have to pay."[46] Consistent with that decision, although not without dissent, the Court ruled that Congress has the power to tax as income moneys received by an extortioner,[47] and, more recently, that embezzled money is taxable income of an embezzler in the year of embezzlement. "When a taxpayer acquires earnings,

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gain to the person whose income is under consideration became such subsequent to the date at which the amendment went into effect, namely, March 1, 1913, and is a real, and not merely an apparent, gain, said gain is taxable. Thus, one who purchased stock in 1912 for $500 could not limit his taxable gain to the difference, $695, the value of the stock on March 1, 1913 and $13,931, the price obtained on the sale thereof, in 1916; but was obliged to pay tax on the entire gain, that is the difference between the original purchase price and the proceeds of the sale, Goodrich v. Edwards, 255 U.S. 527 (1921). Conversely, one who acquired stock in 1912 for $291,600 and who sold the same in 1916 for only $269,346, incurred a loss and could not be taxed at all, notwithstanding the fact that on March 1, 1913, his stock had depreciated to $148,635. Walsh v. Brewster, 255 U.S. 536 (1921). On the other hand, although the difference between the amount of life insurance premiums paid as of 1908, and the amount distributed in 1919, when the insured received the amount of his policy plus cash dividends apportioned thereto since 1908, constituted a gain, that portion of the latter that accrued between 1908 and 1913 was deemed to be an accretion of capital and hence not taxable. Lucas v. Alexander, 279 U.S. 473 (1929).

However, a litigant who, in 1915, reduced to judgment a suit pending on February 26, 1913, for an accounting under a patent infringement, was unable to have treated as capital, and excluded from the taxable income produced by such settlement, that portion of his claim that had accrued prior to March 1, 1913. Income within the meaning of the Amendment was interpreted to be the fruit that is born of capital, not the potency of fruition. All that the taxpayer possessed in 1913 was a contingent chose in action that was inchoate, uncertain, and contested. United States v. Safety Car Heating Co., 297 U.S. 88 (1936).

Similarly, purchasers of coal lands subject to mining leases executed before adoption of the Amendment could not successfully contend that royalties received during 1920–1926 were payments for capital assets sold before March 1, 1913, and hence not taxable. Such an exemption, these purchasers argued, would have been in harmony with applicable local law under which title to coal passes immediately to the lessee on execution of such leases. To the Court, however, such leases were not to be viewed "as a 'sale' of the mineral content of the soil," as minerals "may or may not be present in the leased premises, and may or may not be found [therein]. . . . If found, their abstraction . . . is a time-consuming operation and the payments made by the lessee to the lessor do not normally become payable as the result of a single transaction. . . ." The result for tax purposes would have been the same even had the lease provided that title to the minerals would pass only "on severance by the lessee." Burnet v. Harmel, 287 U.S. 103, 107, 106, 111 (1932).

[44] 274 U.S. 259 (1927).

[45] 42 Stat. 227, 250, 268.

[46] 274 U.S. at 263. Profits from illegal undertakings being taxable as income, expenses in the form of salaries and rentals incurred by bookmakers are deductible. Commissioner v. Sullivan, 356 U.S. 27 (1958).

[47] Rutkin v. United States, 343 U.S. 130 (1952). Four Justices—Black, Reed, Frankfurter, and Douglas—dissented.