BRIEF for the PETITION-ER.

No. 199

In the Supreme Court of the United States

OCTOBER TERM, 1954

COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

GLENSHAW GLASS COMPANY

COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

WILLIAM GOLDMAN THEATRES, INC.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE PETITIONER

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OPINIONS BELOW

The opinion of the Court of Appeals (R. 31-37), which covers two separate cases decided by the Tax Court, is reported at 211 F. 2d 928.[1] The findings of fact and opinion of the Tax Court

[1] The *Glenshaw Glass Co.* case was briefed and set for oral argument in the court below before the *William Goldman Theatres* case was briefed. When counsel in the *William Goldman Theatres* case filed a petition for leave to file an *amicus curiae* brief in the *Glenshaw Glass Co.* case, the court below denied the petition but ordered that the two cases be listed for argument on the same day before the court *en banc*.

in the *Glenshaw Glass Co.* case (R. 7–20) are reported at 18 T. C. 860. The findings of fact and opinion of the Tax Court in the *William Goldman Theatres* case (R. 25–30) are reported at 19 T. C. 637.

JURISDICTION

The judgments of the Court of Appeals were entered on April 9, 1954. (R. 38.) The petition for a writ of certiorari in both cases was filed July 8, 1954, and was granted October 14, 1954 (R. 39). The jurisdiction of this Court rests upon 28 U. S. C., Section 1254.

QUESTION PRESENTED

Each taxpayer received compensatory and punitive damages as the result of litigation in which it claimed injury to its business on the basis of lost profits. The question in each case is whether the amount received as punitive damages constitutes taxable income.

CONSTITUTIONAL AND STATUTORY PROVISIONS AND REGULATIONS

Constitution of the United States:

Art. I, Sec. 2, Clause 3:

> * * * direct Taxes shall be apportioned among the several States * * * according to their respective Numbers * * *

Art. I, Sec. 8, Clause 1:

> The Congress shall have Power To lay and collect Taxes, Duties, Imposts and Excises * * * but all Duties, Imposts and Excises shall be uniform throughout the United States.

Art. I, Sec. 9, Clause 4:

> No Capitation, or other direct, Tax shall be laid, unless in Proportion to the Census Enumeration herein before directed to be taken

Sixteenth Amendment:

> The Congress shall have power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several States, and without regard to any census or enumeration.

Internal Revenue Code of 1939:

> SEC. 22. GROSS INCOME.
>
> (a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service * * * of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *
>
> * * * * *

(26 U. S. C. 1952 ed., Sec. 22.)

Treasury Regulations 111, promulgated under the Internal Revenue Code:

> SEC. 29.21-1. *Meaning of Net Income.*—The tax imposed by chapter 1 is upon in-

come. * * * In the computation of the tax various classes of income must be considered:

(a) Income (in the broad sense), meaning all wealth which flows in to the taxpayer other than as a mere return of capital. It includes the forms of income specifically described as gains and profits, including gains derived from the sale or other disposition of capital assets. * * *

(b) Gross income, meaning income (in the broad sense) less income which is by statutory provision or otherwise exempt from the tax imposed by chapter 1. (See section 22.)

(c) Net income, meaning gross income less statutory deductions. * * *

* * * * *

SEC. 29.22 (a)-1. *What Included in Gross Income.*—Gross income includes in general compensation for personal and professional services, business income, profits from sales of and dealings in property, interest, rent, dividends, and gains, profits, and income derived from any source whatever, unless exempt from tax by law. (See sections 22 (b) and 116.) In general, income is the gain derived from capital, from labor, or from both combined, provided it be understood to include profit gained through a sale or conversion of capital assets. * * *

* * * * *

STATEMENT

In a single opinion the court below affirmed two Tax Court decisions holding that punitive damages do not constitute taxable income. The facts relating to the receipt of the punitive damages by each taxpayer are reflected in findings of fact of the Tax Court (R. 8–16, 25–27) which are largely based upon stipulations of fact and may be summarized as follows:[2]

GLENSHAW GLASS COMPANY

The taxpayer (hereinafter usually referred to as "Glenshaw"), a Pennsylvania corporation having its principal place of business in Glenshaw, Pennsylvania, has been continuously engaged in the manufacture of glass bottles and glass containers. Many years ago it was induced by Hartford-Empire Company (hereinafter referred to as "Hartford") to cancel royalty-free license agreements covering feeder machines in its manufacturing operations and to enter into license agreements with Hartford requiring the payment of royalties. When the license agreements expired, Glenshaw began using the Shawkee feeder, royalty-free, which it had developed through another corporation, the Shaw-

[2] In the *Glenshaw Glass Co.* case the Tax Court's findings of fact are based upon a stipulation of facts (R. 2–7) and oral testimony and exhibits, but the oral testimony had a bearing primarily on an allocation question as to which the Commissioner did not appeal. In the *William Goldman Theatres* case the facts are all stipulated. (R. 22–25.)

kee Manufacturing Company. Hartford thereupon filed an injunction suit against Glenshaw charging infringement of its patents and in 1934 successfully enjoined Glenshaw from using the Shawkee feeder. See *Shawkee Mfg. Co.* v. *Hartford-Empire Co.*, 68 F. 2d 726 (C. A. 3d). As a result, Glenshaw was required to replace the Shawkee feeders with Hartford licensed feeders and, in an accounting which followed, was required to pay Hartford $11,167.85. (R. 8–10.)

Some years later, after the United States instituted a civil suit in which Hartford was ultimately held to have violated the federal antitrust laws (*United States* v. *Hartford-Empire Co.*, 46 F. Supp. 541 (N. D. Ohio), affirmed, 323 U. S. 386, 324 U. S. 570), Glenshaw discontinued all further payments of royalties to Hartford and Hartford filed an action for royalties against Glenshaw (*Hartford-Empire Co.* v. *Glenshaw Glass Co.* (W. D. Pa.), Civil Action No. 1650). Following disclosures made in the Government's antitrust case, Glenshaw filed an answer and counterclaim asking for treble damages for injury to its business by reason of the violation of the federal antitrust laws by Hartford. This proceeding never reached the trial stage. (R. 10.)

In addition, following disclosures in the Government's antitrust case, Glenshaw instituted proceedings to reopen and set aside the perma-

nent injunction entered against it in 1934 on the ground of fraud. This Court ultimately ordered that the fraudulently obtained injunction be annulled and set aside and that Glenshaw be permitted to bring appropriate proceedings for restitution and damages. *Shawkee Mfg. Co.* v. *Hartford Co.*, 322 U. S. 271. Glenshaw thereupon filed a counterclaim in the District Court in the original Hartford injunction proceeding seeking compensatory damages in the amount of $1,500,000 and exemplary damages in a like amount based on the findings of fraud by this Court. (R. 10–11.)

After Glenshaw's damages claims in the fraud action had been substantially sustained on appeal (*Hartford-Empire Co.* v. *Shawkee Mfg. Co.*, 163 F. 2d 474 (C. A. 3d)) and while petitions for rehearing by both sides were pending, the parties began settlement negotiations covering both the fraud suit and the pending but unlitigated antitrust case. The settlement negotiations culminated in a settlement under which Hartford paid $813,358.24 to Glenshaw on December 23, 1947. (R. 11–14.)

Glenshaw allocated $324,529.94 of this settlement sum to punitive damages and did not include it and other portions of the settlement sum as income in its tax return for the year during which it was received. (R. 14–15.) The Commissioner determined a deficiency in the amount of $126,361.06 (R. 8) on the ground that the entire amount of the settlement sum, less deductible legal fees, constituted taxable income.[3]

The Tax Court held that the total amount of the settlement sum received by Glenshaw as compensatory damages was taxable income as consisting of items conceded to constitute taxable income (R. 16) and damages received on the basis of claims for lost profits rather than lost capital (R. 17–19) but that the amount received as punitive damages on the basis of those claims for compensatory damages did not constitute income (R. 16–17). The Tax Court also accepted Glenshaw's allocation of the settlement sum (R. 15, 19–20), with the result that $324,529.94 of that sum was held to be excludible from Glenshaw's taxable income as constituting punitive damages.[4] On appeal by the Commissioner, the Court of Appeals affirmed the Tax Court's holding that

[3] The grounds for the Commissioner's deficiency determination are reflected in the deficiency notice, which was attached as Exhibit A to Glenshaw's petition in the Tax Court but has not been included in the printed record.

[4] With respect to the deductibility of $225,000 in legal fees incurred in the litigation and settlement of the claims against Hartford, the parties agreed in the Tax Court that the fees should be allocated between the various claimed items of damages in the same proportion as the settlement proceeds are allocated, that the amount of fees allocated to the claims that gave rise to taxable income is deductible as an ordinary and necessary business expense, and that the amount of fees allocated to the claims that did not give rise to taxable income is not deductible.

punitive damages do not constitute taxable income.[5] (R. 31–37.)

WILLIAM GOLDMAN THEATRES

The taxpayer (hereinafter usually referred to as "Goldman") is a Delaware corporation having its principal place of business in Philadelphia, Pennsylvania. During 1948 its business consisted of the operation of motion picture houses and the exhibition of motion pictures produced and distributed by other persons and corporations. (R. 25.)

On December 8, 1942, Goldman instituted a civil action in the District Court of the United States for the Eastern District of Pennsylvania (Civil Action No. 2877) against certain motion picture distributors, alleging violation of the federal anti-trust laws and seeking treble damages totaling $1,350,000. The District Court entered judgment for the defendants (*William Goldman Theatres* v. *Loew's, Inc.*, 54 F. Supp. 1011) but on appeal the Court of Appeals held that a violation existed as charged and reversed the judgment (150 F. 2d 738 (C. A. 3d)). Thereafter, the District Court heard evidence directed solely to the question of damages. On September 10, 1946, it made

[5] On appeal we did not question the correctness of the Tax Court's allocation of the settlement sum as between compensatory and punitive damages except to the extent that the allocation is unnecessary under our contention that the punitive damages constituted taxable income.

its findings with respect to damages, finding that Goldman had suffered damages by way of a loss of profits at its Erlanger Theatre in the amount of $125,000 and was entitled to treble damages totalling $375,000 (69 F. Supp. 103). On December 18, 1946, the District Court entered judgment based on its findings. On appeal the judgment was affirmed on January 6, 1948, in a *per curiam* opinion (164 F. 2d 1021 (C. A. 3d)), and certiorari was denied (334 U. S. 811). (R. 25–27.)

On May 28, 1948, the defendants paid Goldman the $375,000 judgment award. Goldman included only $125,000 in its gross income for 1948 (R. 27) and the Commissioner accordingly determined a deficiency against Goldman for 1948 based upon the inclusion of the other two-thirds in Goldman's gross income (R. 25). The Tax Court held that the other two-thirds ($250,000) constituted punitive damages which are not taxable income (R. 27–30), and the Court of Appeals affirmed (R. 31–37).

SUMMARY OF ARGUMENT

Congress by Section 22 (a) of the Internal Revenue Code of 1939 taxed "gains * * * from any source whatever". This language, which has been included in the successive income tax laws since 1913, by its terms taxes all gain except such as may be exempt from tax. It is undisputed that payments of punitive damages constitute gain to the recipients as distinguished from return of

capital and are not within the statutory exemption from tax provided for gifts. It follows that they necessarily fall within the scope of Section 22 (a).

Neither the Constitution nor the decisions of this Court limit gain subject to tax so as to exclude receipts on account of punitive damages. Under Article I, Section 8 of the Constitution, Congress always has had the power to tax receipts not derived from property without apportionment. The power of Congress to tax such receipts existed before the Sixteenth Amendment was adopted and was not affected by that Amendment. The sole purpose of the Amendment was to remove the constitutional requirement of apportionment from a tax on income from property (capital), which this Court had held in *Pollock* v. *Farmers' Loan & Trust Co.*, 157 U. S. 429, 158 U. S. 601, was a direct tax in the constitutional sense, because in substance it imposed a burden on property. The word "gain" in the statute, which is valid under Article I of the Constitution, and not the word "income" in the Sixteenth Amendment, therefore, controls the question whether payments of punitive damages are taxable to the recipient.

The court below, in concluding that gain from punitive damages was not covered by the statute, relied primarily on a definition of income used by this Court to distinguish income from capital in *Eisner* v. *Macomber*, 252 U. S. 189, 207, i. e., that income consists of " 'the gain derived from capital, from labor, or from both combined,' provided it be understood to include profit gained through a sale or conversion of capital assets". While this definition may be helpful in broadly distinguishing income from capital, it was never intended as a precise, restrictive definition modifying the statutory language which declared all gain subject to tax. This Court has repeatedly held subject to tax gain which could not, at least in any usual sense of the words, be said to be derived by the taxpayer from capital or labor or both. Thus this Court has held subject to tax gain resulting from extortion ~~embezzlement~~, the settlement of a law suit, the award of a prize, payments received pursuant to a bequest of income from a trust, etc. Following these cases, and rejecting the contention that the *Eisner* v. *Macomber* definition of income restricts the meaning of gain as that word is used in the statute, the Court of Claims and courts of appeals other than the court below have held receipts from statutory penalties subject to tax, and the Court of Appeals for the Seventh Circuit, in a decision directly contrary to that of the court below, has held payments of punitive damages taxable.

The court below seems to have been of the view that there was a long-standing rule that punitive damages do not constitute taxable income. The only case so holding is a 1940 decision of the Tax Court, with respect to which the Commissioner promptly published his non-acquiescence.

ARGUMENT

THE PUNITIVE DAMAGES RECEIVED BY TAXPAYERS CONSTITUTED TAXABLE INCOME

Section 22 (a) of the Internal Revenue Code of 1939 defines "gross income" to include "gains or profits and income derived from any source whatever." This language, which has been included in the successive income tax laws since 1913, by its terms taxes all gain except such as may be exempt from tax. The court below recognized that the payments of punitive damages constituted gain to the taxpayers concerned, but held that they were not a type of gain which constitutes taxable income.

The court below rested its conclusion primarily on the proposition that taxable income under the Code was limited by a strict reading of the definition of income used by this Court for the purpose of distinguishing income from capital in *Eisner* v. *Macomber*, 252 U. S. 189, 207—that is, that income consists of " 'the gain derived from capital, from labor, or from both combined,' provided it be understood to include profit gained through the sale or conversion of capital assets." It further thought that as "windfalls" the payments should not be regarded as "income" to the taxpayers, although it recognized that to tax punitive damages would put "symmetry into this aspect of the law of income taxation" (R. 37).

Other courts have rejected, in cases involving payments of statutory penalties, the contention that the definition of income used by this Court in *Eisner* v. *Macomber* limited the scope of income subject to tax under the Code. *Park & Tilford Distillers Corp.* v. *United States*, 107 F. Supp. 941 (C. Cls.), certiorari denied, 345 U. S. 917; *General American Inv. Co.* v. *Commissioner*, 211 F. 2d 522 (C. A. 2d), certiorari granted, Oct. 14, 1954, No. 114, this Term. Since the decision of the court below was rendered, the Court of Appeals for the Seventh Circuit in *Commissioner* v. *Obear-Nester Glass Co.*, decided November 15, 1954, now pending on petition for certiorari, No. 478, this Term, held punitive damages like those involved here to constitute taxable income.[6]

Our position is that since payments of punitive damages constitute gain to the recipients which has not been exempted from tax, they constitute taxable income. The statutory language calls for this result and neither the Constitution nor the decisions of this Court warrant any limitation of its plain meaning.

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[6] The decision of the Tax Court in the *Glenshaw case* has been broadly criticized. See *Income Taxation and Treble Damage Antitrust Awards*, 48 Northwestern L. Rev. 85, 90-94 (1953); *The Taxability of Punitive Damages*, 101 U. of Pa. L. Rev. 1052 (1952-1953); *Taxation of Found Property and Other Windfalls*, 20 U. of Chicago L. Rev. 748, 750-753 (1952-1953).

I. SECTION 22 (A) OF THE INTERNAL REVENUE CODE, WHICH DEFINES "GROSS INCOME" TO INCLUDE "GAINS * * * DERIVED FROM ANY SOURCE WHATEVER," MUST BE INTERPRETED IN THE LIGHT OF THE CONGRESSIONAL POLICY TO TAX INCOME COMPREHENSIVELY, AND PLAINLY COVERS RECEIPTS FROM PUNITIVE DAMAGES

We start with the words of the statute which are clear and comprehensive. Since the Revenue Act of 1913, which was enacted a few months after the Sixteenth Amendment became effective, Congress has defined "income" or "gross income" to include "gains, or profits and income derived from any source whatever," and has provided certain exemptions from tax. *E. g.*, Revenue Act of 1913, c. 16, 38 Stat. 114, 167; Internal Revenue Code of 1939, Section 22 (a), 26 U. S. C. 22. The same language has for many years been included in the applicable regulations. Cf. Article 4 of Treasury Regulations 33 (1918 ed.) promulgated under the Revenue Act of 1916 with the current Section 29.22 (a)-1 of Treasury Regulations 111, *supra*, pp. 3, 4. Webster defines gain as "increase in profit, resources, or advantage acquired." The essence of gain is thus increase in resources.

This is the foundation of our position. Congress has plainly imposed a tax on all gain received by the taxpayer (not including return of capital),[7]

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[7] It should be noted that the court below (R. 36) incorrectly stated our position to be that "*any* money or property coming into the hands of any person is taxable as income unless specifically exempted" (italics supplied) and thus to be "a complete negation of the concept of source in relation to taxable income." Source, of course, determines whether money or property constitutes *gain* as distinguished from capital or a return of capital.

except such gain as has been by law specifically exempted from tax.

This Court has many times had occasion to comment on the generality of the statutory language. "The broad sweep of this language indicates the purpose of Congress to use the full measure of its taxing power within those definable categories". *Helvering* v. *Clifford,* 309 U. S. 331, 334. And the Court has cautioned that the construction of the statute "should be consonant with that purpose". *Ibid.* Similarly, in *Commissioner* v. *Jacobson,* 336 U. S. 28, 49, the Court said that "The income taxed is described in sweeping terms and should be broadly construed in accordance with an obvious purpose to tax income comprehensively". See further, e. g., *Irwin* v. *Gavit,* 268 U. S. 161, 166; *Douglas* v. *Willcuts,* 296 U. S. 1, 9; *United States* v. *Safety Car Heating Co.,* 297 U. S. 88; *Rutkin* v. *United States,* 343 U. S. 130.

The payments received by taxpayers as punitive damages constituted gain to them and it is not contended that they constituted return of capital or fall within any of the exemptions provided by Congress.[8] Accordingly, we believe that the payments fall within the plain meaning of Section 22 (a) which covers "gains * * * from any source whatever" and are subject to tax.

[8] Inasmuch as the court below referred by analogy to cases involving the taxability of certain capital contributions and to cases involving the exemption provided by law for gifts, we say more on these subjects in Section III, *infra,* p. 32.

II. NEITHER THE CONSTITUTION NOR THE DECISIONS OF THIS COURT LIMIT GAIN SUBJECT TO TAX SO AS TO EXCLUDE RECEIPTS ON ACCOUNT OF PUNITIVE DAMAGES

A. *Under the Constitution, Congress always has had the power to tax receipts not derived from property without apportionment.*

The basic power "To lay and collect Taxes" is granted to Congress by Article I, Section 8, Clause 1 of the Constitution. The authority so conferred "is exhaustive and embraces every conceivable power of taxation" except as the Constitution expressly imposes its own limitations. *Brushaber* v. *Union Pacific R. R.,* 240 U. S. 1, 12-13; see also, *Steward Machine Co.* v. *Davis,* 301 U. S. 548. The Constitution itself imposed but two restrictions upon the exercise of that power here relevant:[9] (1) "Duties, Imposts, and Excises" must be "uniform throughout the United States" (Art. I, Sec. 8, Cl. 1), which requires only geographical uniformity in application (*Knowlton* v. *Moore,* 178 U. S. 41, 83-109; *Fernandez* v. *Wiener,* 326 U. S. 340, 361), and (2) "direct Taxes" must be "apportioned among the several States" according to population (Art. I, Sec. 2, Cl. 3; Art. I, Sec. 9, Cl. 4). The restrictions "were not so much a limitation upon the complete and all embracing authority to tax" as they were

[9] Article I, Section 9, Clause 5, provides a third restriction on the taxing power—that no tax or duty may be laid on exports.

"regulations concerning the mode in which the plenary power was to be exerted". *Brushaber* v. *Union Pacific R. R.*, 240 U. S. at 13.

As this Court said in upholding the constitutionality of the income tax provisions of the revenue act of 1913, the power of Congress "to lay and collect income taxes" has "never been questioned from the foundation" (*id.* 12–13). The income tax acts of the Civil War period were classed by Congress and the text writers of the day as excises and not as taxes directly on property because of its ownership (*id.* 15). But in *Pollock* v. *Farmers' Loan & Trust Co.*, 157 U. S. 429, 158 U. S. 601, it was held that a tax upon the income (or gain) from real or invested personal property was a direct tax in the constitutional sense because in substance it imposed a burden on property and under the Constitution was required to be apportioned among the states. This decision detracts not at all from the acknowledged plenary power of Congress to levy taxes generally; indeed the Court there expressly recognized the validity of uniform taxes on income from "professions, trades, employments, or vocations" (158 U. S. at 637) and invited attention to the fact that such taxes had been sustained in the past as excises (*id.* at 635). See *Brushaber* v. *Union Pacific R. R.*, 240 U. S. at 16–17.

The constitutional restriction which the *Pollock* case imposed on unapportioned taxes on gain

from property was removed by the Sixteenth Amendment, which provides:

> The Congress shall have power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several States, and without regard to any census or enumeration.

Congress had always had the power to lay and collect taxes on income or gain of any sort. That power was neither conferred nor limited by the Amendment. "It is clear on [its] face * * * that the whole purpose of the Amendment was to relieve all income taxes when imposed from apportionment from a consideration of the source whence the income was derived." *Brushaber* v. *Union Pacific R. R. supra*, pp. 17–18; *Stanton* v. *Baltic Mining Co.*, 240 U. S. 103, 112–113.

The Sixteenth Amendment changed the law *only* with respect to taxes on gain from property: as to such gain it removed the constitutional requirement of apportionment. But with respect to gain from all other sources, including gain or receipts from the payment of punitive damages, Congress always has had and has the power to levy taxes provided only that they are geographically uniform. The question presented here is thus simply one of statutory construction, namely, whether Congress excluded from tax payments of punitive damages, notwithstanding that it comprehensively declared subject to tax "gains * * * from any source whatever."

B. ***The definition of income used by this Court to distinguish income from capital in Eisner v. Macomber has not been regarded by this Court or by courts of appeals other than the court below as limiting gain subject to tax under the Internal Revenue Code.***

The court below, in concluding that the statutory language used by Congress did not cover payments of punitive damages, relied primarily on the definition of income used by this Court in *Eisner* v. *Macomber*, 252 U. S. 189. That case involved the taxability under the Constitution of a stock dividend which did not change the pre-existing proportionate interests of the stockholders. The issue was whether a tax on such a dividend was a tax on property (capital), and hence under the Constitution was subject to apportionment as a direct tax, or whether it was a tax on income, as declared by Congress,[10] and hence under the Sixteenth Amendment was free of the requirement of apportionment.

In approaching this question the Court first looked to the teachings of the economists as to the "fundamental relation of 'capital' to 'income'." Then it looked to the dictionaries and adopted for the purpose of distinguishing income from capital the following definition of income (252 U. S. at 207):

> "Income may be defined as the gain derived from capital, from labor, or from both combined," provided it be understood to include profit gained through a sale or conversion of capital assets.

[10] The Revenue Act of 1916, under which the case arose, provided that a "stock dividend shall be considered income, to the amount of its cash value" (39 Stat. 756, 757).

The Court emphasized that income was *gain* "derived from" not "accruing to" capital, something "severed from" capital and "received by" the taxpayer "for his separate use" (*ibid.*). Returning to an analysis of the character of the stock dividend before it, the Court found that "the essential and controlling fact is that the stockholder has received nothing out of the company's assets for his separate use and benefit" (*id.* at 211). Accordingly the Court held that the tax was a tax on capital and, as such, unconstitutional unless apportioned.

For the purpose of distinguishing income (gain) from capital, the broad definition served the Court adequately and for similar general purposes has frequently been quoted. See *Merchants' L. & T. Co.* v. *Smietanka*, 255 U. S. 509; *Goodrich* v. *Edwards*, 255 U. S. 527; *Bowers* v. *Kerbaugh-Empire Co.*, 271 U. S. 170; *Taft* v. *Bowers*, 278 U. S. 470; *Lucas* v. *Alexander*, 279 U. S. 573; cf. *United States* v. *Phellis*, 257 U. S. 156; see also, *Doyle* v. *Mitchell Brothers Co.*, 247 U. S. 179. In these cases the definition was used, as in *Eisner* v. *Macomber*, to determine that taxes on *gain* from property (which might, because derived from property, be held to be taxes on property and therefore subject to apportionment unless within the scope of the Sixteenth Amendment) were in fact within the scope of that

Amendment. For example, in *Merchants' L. & T. Co.* v. *Smietanka, supra,* the Court considered the taxability of the difference between the 1917 sale price and the March 1, 1913, value of certain trust assets. The Court stated that "very certainly" the gain in question fell within "the comprehensive last clause [of the statute] 'gains or profits and income derived from any source whatever' ". But since the gain in question was derived from property, the Court found it necessary to consider whether the gain was "income" as that term was used in the Sixteenth Amendment. The Court used the *Eisner* v. *Macomber* definition to support its conclusion that the gain in question, which had been produced by and severed from the investment by the sale for cash (255 U. S. at 520):

> * * * thereby became that "realized gain" which has been repeatedly declared to be taxable income within the meaning of the constitutional amendment and the acts of Congress.

But, as we have seen, we are not here concerned with the scope of the Sixteenth Amendment. Taxes on receipts such as those here in issue were taxable without apportionment before the Sixteenth Amendment. Our only question is

[11] We think it clear that the payments of punitive damages were not derived from property of the taxpayer in any sense which would make them direct taxes subject to apportion-

whether a generalization [12] used by the Court to distinguish income from capital is to be taken as restricting or modifying the breadth of the language used by Congress in declaring subject to tax "gains or profits and income derived from any source whatever." At most the *Eisner* v. *Macomber* generalization is but a gloss on the statute, and what is controlling are the words of the statute rather than what was said about one of them, "income", in another context.

This Court, on several occasions, has rejected the notion, adopted by the court below, that the *Eisner* v. *Macomber* definition restricts the scope of the statutory language.[13] The court first did this explicitly in *United States* v. *Kirby Lumber Co.*, 284

ment under *Pollock* v. *Farmers' Loan & Trust Co.*, discussed *supra*, pp. 17–18. But if they should be considered as derived from property (see pp. 26–27, *infra*) and hence of the sort which would have been subject to apportionment under Art. I of the Constitution, then, as realized gain *from property*, they would be "income" within the meaning of the Sixteenth Amendment. *Merchants' L. & T. Co.* v. *Smietanka*, 255 U. S. 509.

[12] *Cf.* Surrey and Warren, *A. L. I. Income Tax Project*, 66 Harv. L. Rev. 761, 770: "Essentially, the *Eisner* v. *Macomber* statement is a generalization rather than a definition."

[13] The *Eisner* v. *Macomber* decision itself has been limited to its particular facts. As the Court stated in *Helvering* v. *Griffiths*, 318 U. S. 371, 375, 393, in *Koshland* v. *Helvering*, 298 U. S. 441, "The Court * * * in effect limited *Eisner* v. *Macomber* to the kind of dividend there dealt with" and in *Helvering* v. *Bruun*, 309 U. S. 461, "rejected the concept that taxable gain could arise only when the taxpayer was able to sever increment from his original capital".

U. S. 1. There the taxpayer, which had issued its bonds and received their par value, later purchased some of the bonds at less than par and the question was whether the difference between the par value and purchase price was income. Accepting the taxpayer's contention that the item in controversy was not income because it was not gain derived from capital or labor or both combined (44 F. 2d 885, 886), the Court of Claims held that it was not "income" though obviously "gain" (44 F. 2d at 887), relying upon this Court's then recent reiteration of the *Eisner* v. *Macomber* definition in *Bowers* v. *Kerbaugh-Empire Co.*, 271 U. S. 170. This Court reversed the Court of Claims, stating (284 U. S. at 3) that under the applicable revenue act gross income includes "gains or profits and income derived from any source whatever", that in the *Kerbaugh-Empire Co.* case the whole transaction resulted in a loss, and that—

> Here there was no shrinkage of assets and the taxpayer made a *clear gain*. As a result of its dealings it made available \$137,521.30 assets previously offset by the obligation of bonds now extinct. *We see nothing to be gained by the discussion of judicial definitions.* The defendant in error has realized within the year an accession to income, if we take words in their plain popular meaning, as they should be taken here. *Burnet* v. *Sanford & Brooks*

Co., 282 U. S. 359, * * *. [Italics supplied.][14]

See also *Helvering* v. *Amer. Chicle Co.*, 291 U. S. 426; *Commissioner* v. *Jacobson*, 336 U. S. 28.

In *Helvering* v. *Bruun*, 309 U. S. 461, this Court again refused to treat the *Eisner* v. *Macomber* definition as if it were a specific blueprint defining the scope of the word "income" for all purposes. In that case a landlord was taxed for the increased value of repossessed land on which the tenant had put a building. Citing *Eisner* v. *Macomber*, the Court said (*id.* at 468–469):

> * * * These expressions, however, were used to clarify the distinction between an ordinary dividend and a stock dividend. They were meant to show that in the case of a stock dividend, the stockholder's interest in the corporate assets after receipt of the dividend was the same as and inseverable from that which he owned before the dividend was declared. We think they are not controlling here.

More recently in *Rutkin* v. *United States*, 343 U. S. 130, the Court held that money obtained by extortion constituted taxable income. The

[14] It has been stated that in the *Kirby Lumber Co.* case this Court "recognized the futility of attempting to capture the concept of income and confine it within a phrase" and "explicitly abandoned the search for a definition." Surrey and Warren, *A. L. I. Income Tax Project*, 66 Harv. L. Rev. 761, 771.

extorted money ($250,000) not only was not derived by the taxpayer-extortionist from capital or labor or both combined, at least in any usual sense of those terms, but was money for which the taxpayer "had no basis for his claim." (*Id.* at 135.) The Court concluded, nevertheless, that Section 22 (a) "reaches these receipts", stating that the power of Congress to tax the receipts is "unquestionable" and that the broad language of Section 22 (a) "supports the declarations of this Court that Congress in enacting that section exercised its full power to tax income". (*Id.* at 138–139.)

Other cases in which the Court has quoted the Section 22 (a) definition of gross income as including "gains or profits and income derived from any source whatever" and held gains subject to tax which do not come within the *Eisner* v. *Macomber* definition include: *Irwin* v. *Gavit*, 268 U. S. 161 (payments received pursuant to bequest of income from a trust); *United States* v. *Safety Car Heating Co.*, 297 U. S. 88 (sum received in settlement of a patent infringement suit for lost profits); and *Robertson* v. *United States*, 343 U. S. 711 (sum received as a prize for a symphony).

Dobson v. *Commissioner*, 320 U. S. 489, rehearing denied, 321 U. S. 231, involved the taxability of the sums received in settlement of litigation which represented partial recoveries of losses on the sale of stock the purchase of which had been induced by fraudulent representations. The

Court there upheld the Tax Court's conclusion that, to the extent that deductions of the losses in prior years had offset gross income for those years, the recoveries must be treated as taxable income (320 U. S. at 507). As taxable income, those recoveries had their direct source in the prior tax benefits for they would otherwise have constituted a return of capital.

Of course most gain has some relation to labor or capital, and, in a loose sense, may be said to be derived therefrom. Thus the activity involved in extortion ~~an embezzlement~~, in repossessing land following default under a lease, in the settlement of a lawsuit, in entering a contest, or in purchasing at a discount one's own promissory obligations, to take the examples of the cases discussed above, could be said to be "labor".

In a similar sense, the punitive damages received by the taxpayers here could be said to derive from "labor" or "capital" or both. Thus the punitive damages were derived from litigation, in which taxpayers employed both capital and labor, based on causes of action (a species of property, 1 Sutherland on *Damages*, Sec. 7 (1916)) which were in turn based upon claims which had their origins in taxpayers' businesses, in which both capital and labor were used. In the case of the antitrust suits, the punitive damages were, in addition, directly dependent upon a showing of actual damages to taxpayers' businesses.[15] 15 U. S. C. 15, *Keogh* v. *C. & N. W. Ry. Co.*, 260 U. S. 156, 164–165. Moreover, inasmuch as punitive damages arise from business or dealings in property in that they can be recovered only if some property or property right has been damaged, they could be said to fall within the language of Section 22 (a) as among the "gains * * * of whatever kind * * * from * * * businesses * * * or * * * growing out of the ownership or use of * * * such property," as well as within the comprehensive last clause of Section 22 (a) which includes "gains * * * from any source whatever". See 101 U. of Pa. L. Rev. 1052, 1065.

But we think little is to be gained from attempting to make the Court's generalization in *Eisner* v. *Macomber* serve, in substitution for the words of Congress in Section 22 (a), as a definition of income. It was plainly not intended by this Court so to be used, and it cannot, consistently with the decisions of this Court, be taken as restricting the plain meaning of the words used by Congress in the Code.

[15] That was not true as to that part of the punitive damages received by Glenshaw in settlement of its fraud action against Hartford. Prior to the settlement agreement between Glenshaw and Hartford (which covered both the fraud action and an antitrust suit), it had been held that punitive damages for fraud were to be awarded Glenshaw in the light of the enormity of Hartford's offense, rather than the actual damages to Glenshaw, because Hartford's fraud was gross and outrageous. *Hartford Empire Co.* v. *Shawkee Mfg. Co.*, 163 F. 2d 474 (C. A. 3d).

The Court of Claims and other courts of appeals, following the decisions of this Court, have rejected the contention that the general definition of income used by this Court in *Eisner* v. *Macomber* restricts the scope of Section 22 (a) in cases involving amounts received as statutory penalties or as punitive damages.

Park & Tilford Distillers Corp. v. *United States*, 107 F. Supp. 941 (C. Cls.), certiorari denied, 345 U. S. 917, involved the taxability of "insider profits" received as a windfall by the taxpayer corporation. In that case an officer-director of the taxpayer-corporation owning more than 10 percent of the stock of the corporation had purchased and sold stock of the corporation on the open market within a six-month period and realized what are called "insider profits." Under Section 16 (b) of the Securities Exchange Act of 1934, c. 404, 48 Stat. 881, he was required to turn over to the corporation his profits from the sales and, upon demand by the corporation, did so. As to the officer-director, the payment to the corporation constituted a penalty. See *Smolowe* v. *Delendo Corp.*, 136 F. 2d 231 (C. A. 2d), certiorari denied, 320 U. S. 751; *Davis* v. *Commissioner*, 17 T. C. 549. The question was whether the payment constituted taxable income to the taxpayer-corporation. In holding that it did, the Court of Claims regarded the payment as a "penalty" to the payor and a "windfall" to the recipient corporation and held that it "could not rationally be suggested that Congress lacks the power to tax windfalls as income" (107 F. Supp. at 943), that the payment was "income derived from any source whatever" under Section 22 (a) of the Code (p. 942), that it saw "no reason for not giving the statutory language its natural meaning" (p. 942), that "If Congress were to select one kind of receipt of money which, above all others, would be a fair mark for taxation, it might well be 'windfalls'" (p. 942), that it was "unwilling to surmise" that by the *Eisner v. Macomber* definition this Court intended to read "income derived from any source whatever" out of Section 22 (a) (p. 943), that the fact that the payment was a penalty to the payor had no bearing on the question of taxability to the recipient (p. 944), and that "Cases such as *Central R. Co. of New Jersey* v. *Commissioner*, 3 Cir., 79 F. 2d 697, and *Highland Farms Corporation*, 42 B. T. A. 1314, 1319, which seem to rest only upon the definition of income given by the Supreme Court in *Eisner* v. *Macomber*, do not seem to us persuasive" (p. 945).

More recently the Tax Court [illegible] and the Court of Appeals for the Second Circuit in *General*

[illegible] In the *General American Inv. Co.* case the Tax Court held (19 T. C. 581), by approving the decision of the Court of Claims in the *Park & Tilford Distillers Corp.* case, that the *Eisner* v. *Macomber* definition of income is not controlling, whereas in the present cases the Tax Court held (R. 16-17, 29) that punitive damages do not constitute taxable income because they do not come within the *Eisner* v. *Ma-*

American Investors Co. v. *Commissioner*, 19 T. C. 581, 211 F. 2d 522, certiorari granted, Oct. 14, 1954, No. 114, this Term, followed the lead taken by the Court of Claims in *Park & Tilford* in another case arising with respect to profits turned over to a corporation pursuant to Section 16 (b) of the Securities Exchange Act of 1934. The taxpayer-corporation there also "relie[d] principally" upon the *Eisner* v. *Macomber* definition of income, which the Court stated did not cover the payments involved "If this definition is to be regarded as all inclusive, and to be applied literally" (211 F. 2d at 523). In answering the taxpayer's argument, the court stated that the *Eisner* v. *Macomber* definition "has met the common fate of generalities" (p. 523), that "it will not help to characterize these payments as a 'windfall' to the corporation or as in the nature of a 'penalty' imposed upon the director and the stockholder" (p. 524), and that "if we consider the words 'gains or profits and income derived from any source,' in their plain popular meaning,' as we think they should be, how can there be any doubt that these Section 16 (b) payments are 'income'?" (p. 524).

comber definition. The Tax Court has therefore placed itself in the inconsistent position of holding both that the *Eisner* v. *Macomber* definition is and is not controlling.

[illegible] The court below regarded the *Park & Tilford Distillers Corp.* and *General American Inv. Co.* decisions as distinguishable from the present cases (R. 36), stating, among other things, that it did not agree with the Court of Claims

The precise question involved here—whether punitive damages received as treble damages under the antitrust laws constitute taxable income—was before the Court of Appeals for the Seventh Circuit in *Commissioner* v. *Obear-Nester Glass Co.*, decided November 15, 1954, pending on petition for certiorari, No. 478, this Term. After reviewing the cases the court concluded that this Court in *Eisner* v. *Macomber* "was merely borrowing a definition of income to support its holding that income attributable to capital must come from it, i. e., be separately expendable, and that it did not consider that definition all encompassing." It did not believe "that the Supreme Court intended to define income exclusively according to its source." It noted that the fundamental principle upon which the income tax is based "is that individuals will be taxed according to their ability to pay." Since windfalls, perhaps above all other sources of income, enhance

in the *Park & Tilford Distillers Corp.* case that the recovery there was purely a windfall (R. 35). The distinction drawn by the court below between those cases and the instant cases seems to be that under the statute involved in those cases the profits were required to be passed on, and inured to the corporation. But as the Court of Appeals for the Second Circuit stated in its *General American Inv. Co.* decision, such reasoning "will not bear analysis," for the "payments were not 'profits' to petitioner, although they represented 'profits' realized by the director and the stockholder." (211 F. 2d at 524.) The Court of Appeals for the Seventh Circuit in *Commissioner v. Obear-Nester Glass Co.*, decided November 15, 1954, quoted and said it agreed with this analysis.

one's ability to pay, it could not conceive that Congress had intended to exclude punitive damages from taxable income.[18] It held accordingly that punitive damages were taxable under Section 22 (a) of the Internal Revenue Code.

III. THERE IS NO LONG STANDING RULE THAT PUNITIVE DAMAGES DO NOT CONSTITUTE TAXABLE INCOME

The court below appears to have been influenced by an assumption, which may have stemmed from statements to that effect in the decisions of the Tax Court in these cases (R. 16, 30), that it was a rule of long standing that punitive damages were not subject to tax.[19] In this too we think the court below was on weak ground.

The notion that there is a long standing rule stems from two decisions—the decision of the court below in *Central R. Co.* v. *Commissioner*, 79 F. 2d 697, decided in 1935, and the Tax Court's

[18] The court seemed to assume that the payments had to qualify as "income" under the Sixteenth Amendment for the tax to be constitutional. For reasons stated *supra*, pp. 16–19, we think that this assumption is based on a mistaken view of the requirements of the Constitution and the nature of the Sixteenth Amendment, but as we also point out, p. 22, n. 11, *supra*, should the payments be considered to be "derived from property" and hence subject to apportionment, they are for that same reason "income" within the meaning of the Sixteenth Amendment.

[19] The court below acknowledged that "The position of the United States would indeed, if adopted, bring symmetry into this aspect of the law of income taxation," and added "But we think if such a result is to be achieved after nearly two decades it should be effected by the Supreme Court and not by this tribunal" (R. 37).

decision in *Highland Farms Corp.* v. *Commissioner,* 42 B. T. A. 1314, 1322, decided in 1940.[20] The *Central R. Co.* case did not involve punitive damages and therefore could not establish any rule specifically as to punitive damages. It was held in that case, however, that gain which is paid as a penalty and received as a windfall is non-taxable to the recipient as not coming within the *Eisner* v. *Macomber* definition of income. Relying upon that holding, the Tax Court held in the *Highland Farms Corp.* case that punitive damages do not constitute taxable income.

One decision of the Tax Court could hardly establish a rule that punitive damages are not sub-

[20] Contrary to an intimation of the court below (R. 33), the pertinent Treasury Regulations have never adopted the *Eisner* v. *Macomber* definition as restricting gain subject to tax or suggested that windfall receipts are not to be taxed. All of the Regulations since 1918 have provided that gross income includes gains or profits and income derived from any source whatever unless exempted from tax by law. See pp. 14-15, *supra.* Following this Court's decision in *Eisner* v. *Macomber*, there was added to the Regulations (Art. 31 of Treasury Regulations 45 (1921 ed.)), the following: "*In general*, income is the gain derived from capital, from labor, or from both combined, provided it be understood to include profit gained through a sale or conversion of capital assets." (Italics supplied.) But these same Regulations (Art. 2l8), also for the first time, defined "income (in the broad sense)" to mean "all wealth which flows in to the taxpayer other than as a mere return of capital" and "Gross income" to mean "income (in the broad sense) less income which is by statutory provision or otherwise exempt from the tax imposed by the statute." These all-inclusive definitions of income and gross income are included in the same terms in current Section 29.21-1 of Treasury Regulations 111, *supra*, pp. 3-4.

ject to tax. In 1940, when the Tax Court applied the *Central R. Co.* decision to punitive damages in the *Highland Farms Corp.* case, the Commissioner published his non-acquiescence in the Tax Court's holding (1941-1 Cum. Bull. 16), thereby showing that he was adhering to his position that punitive damages constitute taxable income and warning everyone that the contrary holding in the *Highland Farms Corp.* case was not being accepted by the Treasury. The Commissioner's position that punitive damages constitute taxable income was not again attacked in the courts until the present *Glenshaw* case.

The premise of the Tax Court's decision in the *Highland Farms Corp.* case—that taxable income is limited by a narrow interpretation of the *Eisner* v. *Macomber* definition of income—has always been questionable. It was based on the *Central R. Co.* decision which, so far as we are aware, has never been followed, except in the *Highland Farms Corp.* case, in respect of its holding that the receipt of a penalty does not constitute taxable income.[21] The *Central R. Co.*

[21] The court below stated that its *Central R. Co.* decision "has been followed frequently" (R. 37) and must have had reference to decisions which Glenshaw cited in the court below in support of an assertion that the other circuits had uniformly accepted the principle of the *Central R. Co.* decision. Not one of the cited cases approved the principle of *Central R. Co.* which the court below applied in the present cases. *Central R. Co.* was cited in *Raytheon Production Corp.* v. *Commissioner*, 144 F. 2d 110, 113 (C. A. 1st), certiorari denied, 323 U. S. 779, and in *White* v. *Thomas*, 116

decision was criticized by the Second Circuit in *Sterling* v. *Commissioner,* 93 F. 2d 304, certiorari denied, 303 U. S. 663, and again in *Lyeth* v. *Hoey,* 96 F. 2d 141, reversed on other grounds, 305 U. S. 188. On its facts the *Central R. Co.* decision was directly contrary to the Fifth Circuit's decision in *Arcadia Refining Co.* v. *Commissioner,* 118 F. 2d 1010. Indeed *Central R. Co.* was decided four years after the *Kirby Lumber Co.* case in which this Court rejected the suggestion that the generalization it used in *Eisner* v. *Macomber* limited or modified the plain meaning of the statutory language.

F. 2d 147 (C. A. 5th), certiorari denied, 313 U. S. 581, along with other cases for the proposition that whether a settlement sum is taxable depends upon the claim settled. In *H. Liebes & Co.* v. *Commissioner,* 90 F. 2d 932, 935 (C. A. 9th), in which it was held that a judgment award constituted income as being a recovery for lost profits rather than a return of capital, *Central R. Co.* was distinguished on the ground that it involved a recovery which was neither for profits nor for an injury to capital. *Crews* v. *Commissioner,* 89 F. 2d 412, 415 (C. A. 10th), cited *Central R. Co.* along with *Eisner* v. *Macomber* for the general proposition that gain from property does not become income until it is realized by the taxpayer. *Mathey* v. *Commissioner,* 177 F. 2d 259 (C. A. 1st), certiorari denied, 339 U. S. 943, was also a case in which it was held that a judgment award constituted income as being a recovery for lost profits rather than a return of capital. In rejecting the taxpayer's contention that the recovery was designed to compensate him for capital losses, the court incidentally stated (p. 264) that the award was received "not as a penalty" but to adequately compensate the taxpayer for lost profits. There was no holding that a penalty does not constitute taxable income and the court did not even cite *Central R. Co.*

Since there is no long standing "rule" that receipts on account of punitive damages are not subject to tax, the decisions of this Court which suggest that such interpretations are to be regarded with respect are inapposite. For example, in *Helvering* v. *Griffiths,* 318 U. S. 371, this Court refused to consider whether it should retroactively overrule the holding in *Eisner* v. *Macomber* as to stock dividends for the reason, among others, that to overrule the decision retroactively would mean that for some seven years a multitude of transactions had been taxable although there was no source of law in any of the three branches of the Government from which the most cautious taxpayer could have learned of the liability. But that is most emphatically not the situation here where the only precedent is a Tax Court decision with respect to which the Commissioner published his non-acquiescence.

IV. PUNITIVE DAMAGES CONSTITUTE GAIN TO THE RECIPIENTS AND ARE NOT EXEMPT AS GIFTS

As we said at the outset (p. 16, n. 8) we feel obliged because of certain analogies drawn by the court below, to discuss further the nature of punitive damages.

There is no question here but that the receipts on account of punitive damages constitute realized gain to the taxpayers concerned. As cash receipts, paid over to taxpayers free of any obligation whatsoever, they were clearly realized.

Similarly they were by definition and in fact gain as distinguished from a return of capital or a contribution to capital. When injury to capital is the basis of a suit which results in an award of damages, the recovery is a return of capital which, since it is not gain, does not constitute taxable income.[22] *United States* v. *Safety Car Heating Co.,* 297 U. S. 88, 98. But taxpayers neither claimed nor sustained a loss of capital; indeed in these cases they concede that the compensatory damages they received constituted gain (rather than a return of capital) and as such were taxable.[23] The punitive damages were received in addition to the actual damages and patently could represent nothing but gain.[24]

[22] This statement assumes a return of capital without a tax benefit. A return of capital as to property which has no cost basis to the taxpayer constitutes taxable income. *Raytheon Production Corp.* v. *Commissioner*, 144 F. 2d 110, 114 (C. A. 1st), certiorari denied, 323 U. S. 779.

[23] Goldman reported the compensatory portion of its judgment in its tax return and paid the tax on that portion (R. 27). Glenshaw conceded that some of the items of compensatory damages were taxable and on the controverted items the Tax Court held that the compensatory damages were for lost profits, rather than a return of capital, and therefore taxable (R. 16, 17-19). Glenshaw did not appeal from this determination.

[24] One writer has suggested that the two-thirds portion of a treble damage award under the antitrust laws should be termed "accumulative damages" and be regarded as liquidated compensation for accumulative, indeterminate, intangible, but actual harm going beyond the ordinarily recoverable actual or legal damages. Vold, *Are Threefold Damages under the Anti-Trust Act Penal or Compensatory?*, 28 Ky. L. J. 117, 134–135, 142–147, 155–159 (1939–1940). If so treated, the two-thirds portion of the treble damages would still constitute gain to the recipients either as compensation for additional lost profits or as return on account of intangibles which have no cost basis. See *Raytheon Production Corp.* v. *Commissioner, supra*, p. 114; cf. *Dobson* v. *Commissioner*, 320 U. S. 489, 507, rehearing denied, 321 U. S. 231.

The decisions relating to governmental subsidies, adverted to by the court below (R. 34, 36), are inapposite to the question whether payments of punitive damages constitute gain to the recipients. In *Edwards* v. *Cuba Railroad*, 268 U. S. 628, it was held that a governmental subsidy payment constituting a *capital contribution* to the railroad did not constitute taxable income, although it was not a mere gratuity. That decision has been criticized for not recognizing that subsidies are gain to the recipients and therefore necessarily either taxable income or gifts,[25] and in *Detroit Edison Co.* v. *Commissioner,* 319 U. S. 98, this Court indicated approval of the latter approach. But cf. *Brown Shoe Co.* v. *Commissioner,* 339 U. S. 583. Moreover the *Cuba Railroad* doctrine has been restricted in its application to the extent that it is well settled that a subsidy or similar payment by a government constitutes taxable income, rather than a nontaxable capital contribution, when its use is not restricted to capi-

[25] Mandell, *Do Subsidies Constitute Taxable Income?*, 26 Taxes 323 (1948); see also, Freeman and Speiller, *Tax Consequences of Subsidies*, 9 Tax. L. Rev. 255, 267–268 (1953-1954); Magill, *Taxable Income* 340–342 (1936).

tal expenditures. *Texas & Pacific Ry Co.* v. *United States,* 286 U. S. 285; *Lykes Bros. S. S. Co.* v. *Commissioner,* 126 F. 2d 725 (C. A. 5th); *Baboquivari Cattle Co.* v. *Commissioner,* 135 F. 2d 114 (C. A. 9th); see also, *United States* v. *Maryland Jockey Club,* 210 F. 2d 367 (C. A. 4th), certiorari denied, 347 U. S. 1014; *Decatur Water Supply Co.* v. *Commissioner,* 88 F. 2d 341 (C. A. 7th). Whatever vitality the *Cuba Railroad* doctrine may still possess as to subsidy payments, it can have no relevance to the taxability of punitive damages not intended as subsidies or capital contributions nor restricted to use for capital expenditures.

It remains only to note that the amounts received by taxpayers as punitive damages are not exempt under Section 22 (b) (3) as gifts. We would not consider this point worth more than passing mention except for the fact that the existence of the statutory exemption for gifts may have influenced the decision of the court below. It noted the exemption and characterized a punitive damage award as "a gift taken from the pocket of the injuring party by virtue of law" adding that "There is no *quid pro quo*" (R. 36).

We think that the receipts here clearly fall outside the statutory exemption. A gift connotes a donative intent on the part of the donor as well as a complete absence of consideration—a transfer of "something for nothing." E. g., *Commissioner* v. *Jacobson,* 336 U. S. 28, 49–51. Payments of punitive damages satisfy neither requirement.

Most assuredly the payments here in question were not made "out of affection, respect, admiration, charity or like impulses," *Robertson* v. *United States,* 343 U. S. 711, 714. The payments were unquestionably involuntary in every sense of the word. Nor did the payments stem from any charitable impulse on the part of the Government. On the contrary, punitive damages, or at least treble damages under the federal antitrust laws,[26] are made available in the interest of better enforcement of the law. Moreover, the recovery of

[26] In *Bruce's Juices* v. *American Can Co.,* 330 U. S. 743, 751–752, the Court stated that:

"It is clear Congress intended to use private self-interest as a means of enforcement and to arm injured persons with private means to retribution when it gave to any injured party a private cause of action in which his damages are to be made good threefold, with costs of suit and reasonable attorney's fee."

See also *Maltz* v. *Sax,* 134 F. 2d 2, 4 (C. A. 7th), certiorari denied, 319 U. S. 772, where it was stated that the grant of the private cause of action for treble damages:

"was for the purpose of multiplying the agencies which would help enforce the Act and therefore make it more effective."

In speaking of the imposition of double, treble and even quadruple damages, this Court long ago stated in *Missouri Pacific Railway Co.* v. *Humes,* 115 U. S. 512, 523, that:

"experience favors this legislation as the most efficient mode of preventing, with the least inconvenience, the commission of injuries. * * * The injury actually received is often so small that in many cases no effort would be made by the sufferer to obtain redress, if the private interest were not supported by the imposition of punitive damages."

punitive damages by taxpayers was dependent upon the institution of suits based upon rights of action which, at least as to the antitrust suits, required taxpayers to prove actual damage to themselves. Thus, so far as the Government is concerned, the punitive damages were made available by law in consideration of taxpayers' enforcement of the law and proof of injury. In that sense they were compensatory. Cf. *Helvering* v. *Mitchell*, 303 U. S. 391; *United States ex rel. Marcus* v. *Hess*, 317 U. S. 537, 549–552.

The fact that punitive damages may be described as windfalls to the recipient does not make them gifts. A windfall which is not a gift is a gain taxable under Section 22 (a). This Court has consistently upheld taxes on receipts or gains which, in a loose sense, might have been characterized as windfalls. E. g., *Robertson* v. *United States*, 343 U. S. 711 (award for prize winning symphony); *Helvering* v. *Bruun*, 309 U. S. 461 (acquisition on forfeiture of lease, of building constructed by lessee on leased premises). In *Commissioner* v. *Jacobson*, 336 U. S. 28, the gain derived by the taxpayer-debtor from the purchase of his own obligations at a discount was in the nature of a windfall but was held to constitute taxable income, rather than a gift by the seller, because the seller did not have a donative intent. Tips can also be labelled windfalls, but they have been held to constitute taxable income for services rendered. *Roberts* v. *Commissioner*, 176 F. 2d 221 (C. A. 9th); *United*

States v. *McCormick*, 67 F. 2d 867 (C. A. 2d), certiorari denied, 291 U. S. 662. A pension received out of retirement deductions by the widow of a city fireman pursuant to state statute is a windfall to the widow but has been held to be taxable income rather than a gift. *Varnedoe* v. *Allen*, 158 F. 2d 467 (C. A. 5th), certiorari denied, 330 U. S. 821; see also *O'Daniel's Estate* v. *Commissioner*, 173 F. 2d 966 (C. A. 2d). "Considering the all-embracing definition of 'gross income' in Section 22", a "windfall" gain accruing to a taxpayer as a result of the devaluation of the pound was held taxable income in *Willard Helburn, Inc.* v. *Commissioner*, 214 F. 2d 815 (C. A. 1st). Windfalls were received by those processors who, upon invalidation of the Agricultural Adjustment Act, c. 25, 48 Stat. 31, were reimbursed for the processing taxes they had paid and passed on to customers under the Act, but such windfalls were held not to constitute gifts and to be subject to the windfall tax imposed by the so-called Unjust Enrichment Act, Section 501 of the Revenue Act of 1936, c. 690, 49 Stat. 1648.[27] *Wilson Milling Co.* v. *Commissioner*, 138 F. 2d 249

[27] A tax of 80 percent was specially imposed on such windfalls by the Unjust Enrichment Act, *supra*, which also prescribed rules to determine liability for the tax. The tax was held to be constitutional in *Wilson Milling Co.* v. *Commissioner*, *supra*. In the absence of that special Act, the windfalls would have been taxable under Section 22 (a) but only at the ordinary rate of tax and there would have been considerable confusion in determining liability for and in collecting the tax.

(C. A. 8th), certiorari denied, 320 U. S. 800; *Sportwear Hosiery Mills v. Commissioner*, 129 F. 2d 376 (C. A. 3d).

This Court has cautioned, in considering whether certain gain to a taxpayer should be excluded from income as a gift, that (*Commissioner v. Jacobson*, 336 U. S. 28, 49):

> The income taxed is described in sweeping terms and should be broadly construed in accordance with an obvious purpose to tax income comprehensively. The exemptions, on the other hand, are specifically stated and should be construed with restraint in the light of the same policy.

These basic policy considerations make it clear that punitive damages cannot be considered exempt from tax as gifts or by any supposed analogy to gifts.

CONCLUSION

For the foregoing reasons, the judgments of the court below should be reversed.

Respectfully submitted,

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