Reply Brief for the Petitioner

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

REPLY BRIEF FOR THE PETITIONER

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15, 1954, quoted and said it agreed with this analysis.

by this tribunal" (R. 37).

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In our main brief we have shown that the statutory definition of "gross income", which includes "gain * * * derived from any source whatever", is clear and that neither the Constitution nor the decisions of this Court limit gain subject to tax so as to exclude receipts of punitive damages. This reply brief deals with certain additional matters raised by the contentions of the taxpayers in their respective briefs.

the court did not even cite *Central R. Co.*

I

THE STATUTORY DEFINITION OF INCOME IS CONSTITUTIONAL AND ITS MEANING IS CLEAR: THERE IS NO OCCASION FOR RESORT TO ANY OTHER DEFINITION.

Both taxpayers concede that Congress may constitutionally tax punitive damages and state that the question presented is whether Congress has in fact taxed such receipts. (Glenshaw Br. 4; Goldman Br. 4). We agree that that is the question before this Court. Our answer is that by Section 22 (a) of the Internal Revenue Code of 1939, Congress has taxed "gains or profits and income from any source whatever." We stress the word "gain" because the use of that word in the definition of "income" makes it clear that Congress used the word "income" in a comprehensive sense, i. e., to include all gain. Neither taxpayer has suggested that the payments of punitive damages involved here did not constitute gain to the recipients. That in our view disposes of this case.

Taxpayers base their arguments on the premise that the terms of Section 22 (a) have acquired a judicial gloss, and cite the definition of income used by this Court to distinguish income from capital in *Eisner* v. *Macomber,* 252 U. S. 189. (Glenshaw Br. 7–10; Goldman Br. 5, 9–10.) Both the statutory and the *Eisner* v. *Macomber*

definitions define "income" in terms of "gain"—the former as "gains * * * derived from any source whatever" and the latter as the "gain derived from capital, from labor, or from both combined." The source of the gain is thus the only variant. Since the statutory definition specifically covers gain "derived from any source whatever," there is no room for interpreting the definition as covering only gain from particular sources.[1]

Taxpayers urge that the last clause of Section 22 (a) has no independent content; that it "is no more than a generalized reference to the content supplied the term 'income' by the enumeration of items which precede it". (Goldman Br. 9; *cf.*

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[1] A valid statutory definition is of course controlling over any other meaning or definition. See *Walling* v. *Portland Terminal Co.*, 330 U. S. 148, 150–151; *Western Union* v. *Lenroot*, 323 U. S. 490, 502.

It does not aid taxpayers to rely, as they do (Glenshaw Br. 14–15; Goldman Br. 10–11), upon Section 61 of the 1954 Internal Revenue Code, which omits the phrase "gains or profits and income" and provides that "gross income means all income from whatever source derived, including (but not limited to)" certain listed items. In the first place, Section 22 (a) of the 1939 Code, rather than Section 61 of the 1954 Code, is applicable here. Secondly, it is clear that Section 61 of the 1954 Code was not intended to restrict the meaning of income. The House Ways and Means Committee states in its report: "While the language in existing section 22 (a) has been simplified, the *all-inclusive nature* of statutory gross income has not been affected thereby." [Italics supplied.] H. Rep. No. 1337, 83d Cong., 2d Sess., p. A18. See also, S. Rep. No. 1622, 83d Cong., 2d Sess., p. 168.

1934); Magill, *Taxable Income* 340–342 (1936).)

Glenshaw Br. 14.) This suggestion lacks merit. Section 22 (a) describes gross income as including "gains, profits, and income derived from" a number of specific sources such as compensation for services, from business, from the ownership or use of property, etc.—sources which may be described broadly as consisting of labor and capital in the usual sense—and then in addition provides that gross income shall include "gains or profits and income derived from *any* source whatever". [Italics supplied.] Since it will not be presumed that this latter clause has no meaning, it must be understood to provide that income includes "gains or profits and income" from sources other than and in addition to the sources specifically enumerated. This is no novel suggestion. Since 1922 the pertinent Treasury Regulations, as they do today, have defined income to include "*all wealth* which flows in to the taxpayer other than as a mere return of capital". [Emphasis added.] Treas. Reg. 111, Sec. 29.21-1 (main brief, p. 3). See further our main brief, p. 34, n. 20.

That Congress intended the statutory language to have such comprehensive scope is evident from the fact that Congress made its own qualifications to the coverage of the statutory language by providing *expressly* for the exclusion of certain gains from tax under subsection (b) of Section 22. Thus, for example, gains by way of gift, bequest, devise, or inheritance, which are obviously not derived from the capital or labor of

the recipient in any usual sense of those words, are specifically excluded from the coverage of Section 22 (a). And as this Court stated in *Commissioner* v. *Jacobson*, 336 U. S. 28, 49, the income taxed under Section 22 (a) "is described in sweeping terms and should be broadly construed in accordance with an obvious purpose to tax income comprehensively."

II

TAXPAYERS' INTERPRETATION OF THE *EISNER* v. *MACOMBER* DEFINITION OF INCOME DEFEATS THEIR OWN CASE

Both taxpayers assert that decisions of this Court on which we rely are reconcilable with the *Eisner* v. *Macomber* definition of income. (Glenshaw Br. 18–20; Goldman Br. 11–13.) Certainly that is not true if taxpayers are relying upon a narrow, literal interpretation of this definition. On the other hand, if taxpayers are relying upon an interpretation of the definition sufficiently broad to cover all such cases, the conclusion is inescapable that the punitive damages involved here constitute income within the *Eisner* v. *Macomber* definition.

A review of the decisions of this Court will make this clear. Thus in the cases involving a taxpayer's purchase of its own obligations at a discount (*United States* v. *Kirby Lumber Co.*, 284 U. S. 1; *Helvering* v. *American Chicle Co.*, 291 U. S. 426; *Commissioner* v. *Jacobson*, 336 U. S.

not supported by the imposition of punitive damages."

28), capital was involved but taxability was based "on the increase in net assets which resulted" (*Helvering* v. *Amer. Dental Co.*, 318 U. S. 322, 327). In *Helvering* v. *Bruun*, 309 U. S. 461, where the increased value of land repossessed under a lease by the taxpayer-lessor was held to constitute income, a business transaction was involved but the direct source of the gain was in the lessee's voluntary and fortuitous act of erecting a new building on the property. In *Robertson* v. *United States*, 343 U. S. 711, where the taxable income consisted of a prize-winning award for a symphony, labor may have been necessary to receipt of the award but the award had its more immediate source in a third party's selection of the taxpayer as the prizewinner. In *Dobson* v. *Commissioner*, 320 U. S. 489, rehearing denied, 321 U. S. 231, which involved sums received in settlement of litigation representing partial recoveries for losses, the holding that some of the recoveries constituted taxable income (320 U. S., p. 507) was based on the fact that the taxpayers had derived prior tax benefits from deduction of the losses. In *United States* v. *Safety Car Heating Co.*, 297 U. S. 88, where the sum received in settlement of a suit for lost profits for infringement of a patent was held to constitute taxable income, the statute providing for the recovery of damages was one of the sources of the income. In *Rutkin* v. *United States*, 343 U. S. 130, where the

taxable income consisted of extorted money, the threats which were the sole source of the money could hardly be described as "labor" in any familiar sense of the word. In *Irwin* v. *Gavit*, 268 U. S. 161, the taxable income consisted of trust income received pursuant to a bequest which carried no interest in the trust corpus and therefore was not either directly or indirectly derived from capital or labor of the taxapayer.

To assert, as taxpayers do, that the decisions of this Court are reconcilable with the *Eisner* v. *Macomber* definition is merely to recognize that most, if not all, gain can be said to be derived from capital or labor or both. Punitive damages, for example, would appear to be just as much derived from capital and labor as was the income in the foregoing cases. The damages derived from claims which arose in the course of taxpayers' businesses. (See our main brief, p. 27.) Litigation was the means by which the punitive damages were collected, as Goldman states (Goldman Br. 13), but litigation was also the means by which the actual damages in the *Safety Car Heating Co.* case were collected. So far as source is concerned, there is no basis for distinguishing between the recovery of actual damages and punitive damages. It is only the *nature* of the recovery which is different and that can have no relevance so long as punitive damages constitute gain.

v. *Commissioner*, 176 F. 2d 221 (C. A. 9th); *United*

lecting the tax.

III

THE CASES HOLDING CERTAIN OTHER TYPES OF RECEIPTS NOT TAXABLE ARE DISTINGUISHABLE

The decisions holding some categories of receipts not subject to tax, relied on by Glenshaw (Glenshaw Br. 16-17), have no persuasive bearing on this case. In some instances, unlike the present case, difficulty is encountered in determining whether a receipt constitutes *gain*, as in the case of the stock dividends involved in *Eisner* v. *Macomber*. Alimony is a borderline instance. In *Gould* v. *Gould*, 245 U. S. 151, the Court held that alimony did not constitute taxable income under the Income Tax Act of 1913, c. 16, 38 Stat. 114, 166, but Section 22 (k) of the 1939 Code contains express provisions taxing periodic alimony payments and the lower courts have found no constitutional impediment to applying the section. See *Mahana* v. *United States*, 88 F. Supp. 285 (C. Cls.), certiorari denied, 339 U. S. 978; *Fairbanks* v. *Commissioner*, 191 F. 2d 680 (C. A. 9th), certiorari denied, 343 U. S. 915. Recoveries for libel *per se* and for breach of promise to marry have been excluded from income on the ground that the damages are reimbursement for injuries which are personal and merely make the taxpayer whole, as distinguished from giving him a profit or gain. *Hawkins* v. *Commissioner*, 6 B. T. A. 1023; *McDonald* v. *Commissioner*, 9 B. T. A. 1340. As we show in our main brief (pp.

39-40), the governmental subsidy payments involved in *Edwards* v. *Cuba Railroad*, 268 U. S. 628, were excluded from income on the ground that they constituted a *capital contribution* and the doctrine of that case is inapplicable where use of the subsidy payments is not restricted to capital expenditures (*Texas & Pacific Ry. Co.* v. *United States*, 286 U. S. 285).[2] Moreover it is clear that the payments to taxpayers here were not intended as subsidies. *Commissioner* v. *Inland Finance Co.*, 63 F. 2d 886 (C. A. 9th), involving the forfeiture of stock subscriptions upon non-payment of other deferred installments, was apparently decided on the basis of a narrow interpretation of the *Eisner* v. *Macomber* definition and is inconsistent with statements of this Court in *Detroit Edison Co.* v. *Commissioner*, 319 U. S. 98. In *United States* v. *Supplee-Biddle Co.*, 265 U. S. 189, the Court held that a statutory exemption of insurance proceeds as to individuals applied to corporations and did not decide whether Congress could tax them as income.

IV

THE COMMISSIONER HAS CONSISTENTLY MAINTAINED THAT PAYMENTS OF PUNITIVE DAMAGES MUST BE INCLUDED IN THE INCOME OF THE RECIPIENT

Both taxpayers argue that the non-taxability of punitive damages is a rule of long standing which

[2] *Brown Shoe Co.* v. *Commissioner*, 339 U. S. 583, is a related case but did not involve the taxability of subsidies.

should not be changed except by legislative action. (Glenshaw Br. 24–26; Goldman Br. 4–8.) We anticipated and answered that argument in our main brief (pp. 33–37) but taxpayers persist in assuming that punitive damages have not been taxed since the 1940 decision of the Tax Court in *Highland Farms Corp.* v. *Commissioner*, 42 B. T. A. 1314, 1322. As we stated in our main brief, the Commissioner published his non-acquiescence in the Tax Court's holding in that case that punitive damages do not constitute taxable income and thereby served notice that he was going to continue to tax punitive damages. He has done so, as his determination of deficiencies against these very taxpayers attests. To require taxpayers to pay tax on the punitive damages received by them will merely put taxpayers on an equality with other taxpayers who over the years have been taxed, pursuant to the Congressional direction as expressed in Section 22 (a) of the 1939 Code, on "gains or profits and income derived from any source whatever."

Respectfully submitted.

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