

## Chapter 3

# Determining Gross Income

---

### Solutions to Develop Research Skills

Note to Instructor: Beginning with this chapter, no research aids or “hints” are provided in the textbook. Before the solution to each problem, however, suggested research aids are provided. This allows you to choose whether or not to provide any hints to your students for a particular problem. For problems that can be solved using free Internet sources, you must provide students with the citations in these hints and refer students to Figure 2.2 of Chapter 2 in the text for the URLs to enable them to solve these problems using free Internet sources. Some of the problems require access to *Checkpoint®* or a similar service. The research process for solving a sample problem is illustrated in Appendix A through screen captures for *Checkpoint®*.

64. *Personal Use of Political Campaign Funds (can be solved using Checkpoint® or a similar service)*

Thomas ran for Congress, raising \$2 million for his campaign. Six months after losing the election, auditors discovered that Thomas kept \$160,000 of the campaign funds using the money to purchase a vacation home. What are the tax consequences of this use of campaign funds?

Hint: Rev. Rul. 71-449, 1971-2 C.B. 77 (clarified by Rev. Rul. 74-22, 1974-1 C.B. 16)

**Issue:** Does Thomas have income as a result of using the campaign funds to purchase a vacation home?

**Conclusion:** Yes, Thomas must recognize \$160,000 income in the year the campaign funds were used to pay for his vacation home.

**Discussion of Reasoning and Authorities:** Code Section 61 states that gross income includes income from all sources unless specifically excluded. Rev. Rul. 71-449, 1971-2 C.B. 77 concluded that political contributions used for personal purposes by a political candidate are included in gross income in the year the funds are diverted to personal use. A candidate is not taxed on campaign funds to the extent they are used for expenses of a political campaign or a similar purpose. Therefore, Thomas must recognize \$160,000 income in the year the campaign funds were used to pay for his vacation home.

65. *Income from Donation of Blood (can be solved using Checkpoint® or a similar service)*

Samantha has been unemployed for some time and is very short of money. She learned that the local blood bank has a severe shortage of her type of blood and, therefore, is willing to pay \$120 for each blood donation. Samantha gives blood twice a week for 12 weeks, receiving \$120 for each donation. Are these funds includable in Samantha's gross income?

Hint: *Green v. Comm.* 74 T.C. 1229 (1980)

**Issue:** Does Samantha have income as a result of the funds she received for donating her blood?

**Conclusion:** Yes, Samantha must recognize as income the payments she received for selling her blood.

**Discussion of Reasoning and Authorities:** Code Section 61 states that gross income includes income from all sources unless specifically excluded. In *Green v. Comm.*, 74 T.C. 1229 (1980), the Court concluded that payments received for “donations” of blood plasma were income received in the trade or business of selling the product of blood plasma.

*Note to instructor:* This case also addresses the deductibility of expenses for transportation to give blood, expenses for special food and drugs, health insurance, and a depletion allowance. Although some expenses were deductible, the taxpayer was not permitted an allowance for depletion.

## 2 Taxation for Decision Makers Research Solutions

### 66. *Payment of Life Insurance Premiums as Alimony (can be solved using free Internet sources)*

Alice and Manny agree to divorce. Alice proposes that Manny purchase and assign to her a life insurance policy on him as part of the divorce agreement. She wants Manny to continue paying the premiums on this policy for the next 10 years. Manny wants to know if the premium payments will be treated as alimony.

Hints: Reg. Section 1.71-1T(b), Q&A 6 and Rev. Rul. 70-218, 1970-1 C.B. 19..

**Issue:** Will Manny's payments of the life insurance premiums qualify as alimony?

**Conclusion:** Yes, the premium payments will qualify as alimony providing that Alice is the irrevocable beneficiary of the life insurance policy assigned to her.

**Discussion of Reasoning and Authorities:** Reg. Section 1.71-1T(b), Q&A 6 states that premiums paid by the payor spouse for term or whole life insurance on the payor's life under the terms of the divorce or separation instrument will qualify as payments on behalf of the payee spouse to the extent that the payee spouse is the owner of the policy. Rev. Rul. 70-218, 1970-1 C.B. determined that when a life insurance policy on the life of the husband is assigned to the wife and she is the irrevocable beneficiary, the premiums are deductible as alimony by the husband and taxable to the wife.

### 67. *Income vs. Gift (can be solved using free Internet sources)*

A minister receives an annual salary of \$16,000 in addition to the use of a church parsonage with an annual rental value of \$6,000. The minister accepted this minimal salary because he felt that was all the church could afford to pay. He plans to report these amounts on his income tax return but he is uncertain how to treat the cash gifts he receives from the members of his congregation. These gifts were made out of love and admiration for him. During the year the congregation developed a regular procedure for making gifts on special occasions. Approximately two weeks before each special occasion when the minister was not present, the associate pastor announced before the service that those who wished to contribute to the special occasion gifts could do so by placing cash in envelopes and giving them to the associate who would give them to the minister. Only cash was accepted to preserve anonymity. The church did not keep a record of the amounts given nor the contributors, but the minister estimates that these gifts amount to about \$10,000 in the current year. How should he treat these gifts?

Hint: *Goodwin, Lloyd L., Reverend v. U.S.*, 76 AFTR 2d 95-6716, 67 F3rd 149, 95-2 USTC ¶150534 (1995, CA8); affirming 74 AFTR 2d 94-6987 (DC IA).

**Issue:** How should the minister treat the \$10,000 in cash gifts?

**Conclusion:** The minister should include the \$10,000 in his gross income as compensation.

**Discussion of Reasoning and Authorities:** Code Section 61(a) provides that gross income includes all income from whatever source derived unless excluded by a specific provision of the Code. According to Section 61(a)(1), compensation for services, in whatever form received, is includable in gross income. Section 102(a) excludes from gross income the value of property acquired by gift. Whether a payment is a gift under Section 102(a) or gross income under section 61(a) is a factual question.

In *Goodwin v. U.S.*, a minister received gifts from members of his congregation who believed he was a good minister and wanted to reward him. The payments were made on a regular basis, were systematically organized and collected by church personnel, were substantial compared to the minister's salary, and were made to retain the minister's services. The court held that these factors showed that the intent was to increase the minister's compensation. The fact that the payments were anonymous and were not coerced did not change the result. Therefore the so-called gifts were part of the minister's taxable compensation.