7 T.C. 1469 (1946)

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A taxpayer cannot claim a foreign tax credit under U.S. tax law for taxes paid to a foreign country on an item that is not considered income under U.S. tax law, even if the foreign country treats it as income.

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Summary

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L. Helena Wilson, a Canadian citizen residing in the U.S., sought to claim a credit on her U.S. income tax for taxes paid to Canada on $20,000 received from a testamentary trust. While Canadian authorities considered this amount taxable income, the U.S. considered it a legacy because the will guaranteed the payment from the trust's principal if necessary. The Tax Court denied the credit, holding that U.S. tax law determines what constitutes "income" for purposes of the foreign tax credit, and legacies are not considered income under U.S. law. Further, the court noted the lack of evidence that Canada offered a similar credit to U.S. citizens residing there.

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Facts

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L. Helena Wilson, a Canadian citizen residing in Los Angeles, received income from a trust established by her deceased husband's will in Canada. The will directed the trustees to pay Wilson $20,000 annually, even if it required drawing from the trust's capital. In 1940, Wilson received $33,831.84 (Canadian) from the trust and $808.25 (Canadian) in dividends. Canada taxed these amounts, withholding $1,691.59 (Canadian) and $40.41 (Canadian), respectively. Wilson's U.S. tax return reported the trust income exceeding $20,000 ($13,831.84) and the dividends as taxable income, excluding the $20,000 payment, which she considered a non-taxable legacy.

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Procedural History

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The Commissioner of Internal Revenue determined a deficiency in Wilson's 1940 income tax. This was due to the partial disallowance of the credit she claimed for taxes paid to Canada. Wilson petitioned the Tax Court for a redetermination.

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Issue(s)

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Whether the income tax paid to Canada on the $20,000 received by Wilson, considered a legacy under U.S. law but treated as taxable income by Canada, is creditable against her U.S. Federal income tax under Section 131(a)(3) of the Internal Revenue Code.

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Holding

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No, because the U.S. tax code does not consider the $20,000 a taxable form of income, regardless of how it is treated by Canadian tax authorities. The $20,000 was agreed not to be income as defined by the Internal Revenue statutes of the United States, since it was the equivalent of a legacy.

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Court's Reasoning

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The court relied on *Burnet v. Whitehouse, 283 U.S. 148*, to establish that the $20,000 payment was a legacy, not taxable income, under U.S. law. Citing *Biddle v. Commissioner, 302 U.S. 573*, the court emphasized that the foreign tax must be a tax on income as defined by U.S. tax statutes. The court quoted *Biddle*, stating, "Section 131 does not say that the meaning of its words is to be determined by foreign taxing statutes and decisions… The phrase 'income taxes paid,' as used in our own revenue laws, has for most practical purposes a well-understood meaning… It is that meaning which must be attributed to it as used in section 131." Because the $20,000 was a legacy and not income under U.S. law, the tax paid to Canada on that amount was not creditable. The court also highlighted that there was no

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evidence Canada allowed a similar credit to U.S. citizens residing there, a condition precedent to the allowance of the credit under Section 131(a)(3). The court distinguished *I.B. Dexter, 47 B.T.A. 285*, because that case involved income taxable in both jurisdictions, unlike the legacy in the present case.

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Practical Implications

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Wilson v. Commissioner clarifies that the availability of a foreign tax credit depends on whether the item taxed abroad qualifies as

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