11 T.C. 1057 (1948)

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For the purposes of calculating whether compensation qualifies for tax benefits under Section 107 of the Internal Revenue Code, all compensation received for the same indivisible services must be combined, regardless of the source of payment.

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Summary

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The Tax Court addressed whether stock received by officers of a corporation qualified for tax benefits under Section 107 of the Internal Revenue Code. The officers received the stock as additional compensation for their services related to a corporate reorganization. The court held that the stock payments did not constitute 80% of the total compensation because the court required the inclusion of their regular salaries when calculating total compensation. This case clarifies that all compensation for the same services must be considered, irrespective of the source, when determining eligibility for Section 107 benefits.

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Facts

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From 1935 to 1943, Hoffmann, Goddin, and LeMaster served as officers and employees of Mortbon Corporation of New York, which was formed following a corporate reorganization. The reorganization plan stipulated that a portion of the new corporation’s stock would be paid to its management upon achieving specific operational success. In 1943, the directors awarded parts of this “management” stock to the petitioners as additional compensation for their services as officers and employees. The corporation had also paid them regular salaries.

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Procedural History

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The Commissioner of Internal Revenue determined income tax deficiencies for the year 1943, including the full value of the stock in the petitioners' gross income. The petitioners contested this determination, claiming entitlement to tax benefits under Section 107 of the Internal Revenue Code. The Tax Court consolidated the cases for hearing.

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Issue(s)

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Whether the petitioners are entitled to the benefits of Section 107(a) of the Internal Revenue Code in computing income tax upon the receipt of the stock.

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Holding

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No, because the stock payments did not constitute at least 80% of the total compensation received for their services, as required by Section 107, when considering their regular salaries along with the value of the stock.

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Court's Reasoning

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The court reasoned that the principal criterion is the divisibility of the personal services rendered, rather than the source of the compensation. The court cited *Civilette v. Commissioner* and *Smart v. Commissioner*, emphasizing that compensation from divisible sources does not automatically make the services divisible. Here, the court found that the petitioners' managerial services as officers and employees of the new corporation were indivisible. The court stated, "Here the compensation received by petitioners, including the management stock, can be considered only as in payment for their managerial services rendered as officers and employees of the new corporation… To hold that these services were divisible, in that a part of them were rendered to the corporation and a part of them were rendered to the bondholders of the old company, would ignore reality." The court concluded that all compensation received for the same, indivisible services must be combined when determining

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