12 T.C. 311 (1949)

The controlling test for determining whether a transfer of property is a gift or compensation for services is the intent of the transferors, gathered from all facts and circumstances.

Summary

Richard C. McAdow, a long-time employee of William E. Benjamin, received securities from Benjamin's son and daughter. The IRS claimed these securities were taxable compensation, while McAdow's estate argued they were a gift. The Tax Court held that the securities were a gift, based on the expressed intent of the transferors (Benjamin's children), their treatment of the transfer as a gift on their tax returns, and the lack of evidence suggesting the transfer was intended as compensation for services rendered to them personally. This case illustrates the importance of establishing donative intent in determining whether a transfer is a tax-free gift or taxable income.

Facts

Richard C. McAdow was a long-time employee of William E. Benjamin, managing his investments and those of his companies. He also served as a trustee for Benjamin family trusts. After William E. Benjamin removed McAdow as an executor-trustee in his will, Benjamin's children, Henry R. Benjamin and Beatrice B. McEvoy, transferred securities valued at $75,981.25 to McAdow in 1941.

A note delivered with the securities stated the transfer was a "gift" expressing "love and affection," and that "no services were rendered or required." Henry and Beatrice each filed gift tax returns, reporting the securities as gifts to McAdow. McAdow also filed donee's information returns of gifts.

Procedural History

The Commissioner of Internal Revenue determined deficiencies in the income tax of Richard C. McAdow and his wife, Grace G. McAdow, for the taxable year 1941. The deficiencies were attributed to the inclusion of the value of the securities received from Henry R. Benjamin and Beatrice B. McEvoy as income. The Tax Court consolidated the proceedings related to the estates of Richard and Grace McAdow. The Tax Court ruled in favor of the McAdow estates, finding the securities were a gift and not taxable income.

Issue(s)

1. Whether the securities transferred to McAdow by Henry R. Benjamin and Beatrice B. McEvoy in 1941 were payments for services rendered and, therefore, includible in income, or whether they constituted gifts and, as such, were excludable from income.

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Holding

1. No, the securities were a gift because the transferors intended to make a gift, as evidenced by their contemporaneous statements and actions.

Court's Reasoning

The court emphasized that determining whether the securities were a gift or compensation required examining the intent of the transferors. The court relied on the Supreme Court's decision in *Bogardus v. Commissioner, 302 U.S. 34 (1937)*, stating, "If the sum of money under consideration was a gift and not compensation it is exempt from taxation and cannot be made taxable by resort to any form of subclassification. If it be in fact a gift, that is an end of the matter."

The Tax Court found compelling evidence of donative intent: the note describing the transfer as a gift, the ledger entries classifying the transfer as a gift, the gift tax returns filed by Henry and Beatrice, and Henry's testimony. The court found unpersuasive the IRS's argument that the securities were compensation for services McAdow rendered to the Benjamin family, noting McAdow was already compensated for his services to William E. Benjamin and Henry. The court stated, "These two undoubtedly felt deeply grateful to McAdow for what he had done, and that was the moving cause for their gifts to him…"

Practical Implications

This case reinforces the importance of documenting donative intent when making a gift, particularly when there's a pre-existing relationship, such as employer-employee, that could suggest the transfer is compensation. Contemporaneous documentation, such as a written gift letter, and consistent treatment of the transfer on tax returns are crucial. The case highlights that the IRS will scrutinize transfers that could be construed as compensation, and taxpayers bear the burden of proving donative intent. Subsequent cases cite *McAdow* for the principle that the transferor's intent is paramount in distinguishing a gift from taxable income.

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