Helena Rubinstein, 14 T.C. 752 (1950)

A resident alien is taxable on income credited to their account, even if located abroad and subject to foreign exchange controls, if the funds are freely expendable within the foreign currency area and have a determinable value in the United States.

Summary

Helena Rubinstein, a British citizen, entered the U.S. as a quota immigrant and remained during WWII. The IRS assessed deficiencies, arguing she was a U.S. resident alien and taxable on income credited to her account in England, despite British exchange controls. The Tax Court held that Rubinstein was a U.S. resident alien during the tax years in question. It further held that income credited to her account in England was taxable because she could freely spend it within the sterling area, and it had a determinable value in the U.S. free market. The court ruled that the value should be determined by the free market exchange rate, not the official rate.

Facts

- Rubinstein, a British citizen, came to the United States from Mexico on May 12, 1941, as a quota immigrant.
- She remained in the U.S. during 1942, 1943, and 1944.
- Salaries and dividends were unconditionally credited to her account in England by Helena Rubinstein, Ltd.
- Due to British Exchange Control Regulations, she could not receive these funds in the United States during those years.
- Rubinstein could freely direct the application and expenditure of these funds within the sterling area.
- The British blocked pound was freely selling in the New York free market during the taxable years.
- Rubinstein returned to England in 1945 after the war.

Procedural History

The Commissioner of Internal Revenue determined deficiencies in Rubinstein's income tax for 1942, 1943, and 1944. Rubinstein petitioned the Tax Court for a redetermination of these deficiencies.

Issue(s)

1. Whether Rubinstein was a resident of the United States during 1942, 1943, and 1944.
2. Whether Rubinstein is taxable on dividends and salary unconditionally credited to her account in England in British pounds, which she did not receive in the United States during the taxable years because of British Exchange Control Regulations.

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3. If question No. 2 is answered in the affirmative, then whether her taxable income should be measured by the official exchange rate of the British pound, or by the value of the blocked British pound in the free market of the United States during such period.

Holding

1. Yes, because Rubinstein intended to become a resident of the United States during the duration of the war and, in fact, did so.
2. Yes, because the credits were available to Rubinstein in blocked British pounds and would have been freely expendable anywhere in the sterling area.
3. The taxable income should be measured by the value of the blocked British pound in the free market of the United States, because the official rate of exchange does not apply to blocked pounds.

Court's Reasoning

The court reasoned that residence is a question of fact determined by intent. The regulations state that an alien actually present in the U.S. who is not a mere transient or sojourner is a U.S. resident. The court found Rubinstein intended to reside in the U.S. for the war's duration, making her a resident alien. Regarding the foreign income, the court noted that the funds were freely expendable in the sterling area, making them taxable, citing *Eder, et al. v. Commissioner*, 138 F.2d 27, and *Mar Freudmann*, 10 T.C. 775. Distinguishing *International Mortgage & Investment Corporation*, the court emphasized that, unlike that case, a free market existed for the blocked pounds. Finally, relying on *Morris Marks Landau*, 7 T.C. 12, the court ruled that the free market exchange rate, not the official rate, should determine the pound's value for tax purposes.

Practical Implications

This case clarifies the tax obligations of resident aliens with foreign income, particularly when exchange controls limit the transfer of funds. It establishes that the ability to freely spend funds within a foreign currency area is sufficient for the income to be taxable in the U.S. Further, it emphasizes the importance of using the free market exchange rate to determine the value of blocked currency, rather than relying on official rates. This ruling informs how similar cases involving foreign income and currency restrictions are analyzed, impacting tax planning for individuals with international financial arrangements. It confirms that resident aliens are taxed similarly to citizens, with specific considerations for the nature and accessibility of their foreign income.

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