18 T.C. 892 (1952)

Income derived from the sale of foreign publication rights to an article, by a nonresident U.S. citizen, is not considered ‘earned income’ from sources outside the U.S. if the rights were sold within the U.S. after the article was written.

Summary

Frank Kluckhohn, a nonresident U.S. citizen residing in Argentina, wrote an article and later sold the foreign publication rights to Reader’s Digest while in the United States. He sought to exclude the income from his U.S. taxes under Section 116 of the Internal Revenue Code, arguing it was earned income from foreign sources. The Tax Court held that the income was not exempt because it didn’t meet the definition of ‘earned income’ under the statute, relying on the precedent set in *E. Phillips Oppenheim*.

Facts

Frank Kluckhohn, a U.S. citizen, lived in Argentina from 1945 to early 1947 and worked as a newspaper correspondent and writer.
While in Argentina in 1946, he wrote an article about Peron and retained the rights to sell the article outside the United States.
In early 1947, while in the United States, he received an offer from Reader’s Digest to reprint the article in foreign countries.
He accepted the offer and received $1,200 in 1947 for the foreign rights, which he did not report as gross income.

Procedural History

The Commissioner of Internal Revenue determined a deficiency in the Kluckhohns’ income tax for 1947.
The Commissioner included the $1,200 in gross income, which the Kluckhohns contested in the Tax Court.

Issue(s)

Whether the $1,200 received by Frank Kluckhohn from Reader’s Digest for foreign rights to his article constitutes ‘earned income’ from sources without the United States under Section 116 of the Internal Revenue Code.

Holding

No, because the income was not considered ‘earned income’ within the meaning of Section 116, as it was not received as compensation for personal services rendered as an employee or at the request of Reader’s Digest.

Court’s Reasoning

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The court relied on *E. Phillips Oppenheim, 31 B.T.A. 563*, which held that royalties received by a writer for granting publication rights do not constitute ‘earned income’ as defined by the statute.
The court distinguished between wages received as an employee and royalties or payments received for granting rights to intellectual property.
The court noted that Kluckhohn wrote the article independently and not as an employee or at the request of Reader’s Digest. Therefore, the payment was not considered compensation for personal services actually rendered.
Section 116(a)(3) defines earned income as “wages, salaries, professional fees, and other amounts received as compensation for personal services actually rendered.”

Practical Implications

This case clarifies the definition of ‘earned income’ for U.S. citizens living abroad, particularly regarding income from intellectual property.
It highlights that income from the sale of rights to an article is treated differently from wages or fees for services rendered.
Attorneys should consider the source and nature of the income when advising clients on the applicability of Section 116 exclusions.
This ruling is relevant for self-employed individuals and those who receive income from royalties or licensing agreements while residing outside the United States.
Later cases would likely distinguish this case based on the specific facts, such as whether the writer was commissioned to write the article or was an employee of the publisher.

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