***James v. United States, 366 U. S. 213 (1961)***

Embezzled funds are taxable as income to the embezzler who exercises dominion and control over them, regardless of whether the funds are used for personal benefit or transferred to another.

**Summary**

Barbara embezzled money from her employer and used the funds to assist her brother Melton, who was aware of the source of the money. The Supreme Court held that the embezzled funds constituted taxable income to Barbara because she had complete control over the funds before transferring them to Melton. This case established that the embezzler’s control over the funds, not their personal use, is the key factor in determining tax liability.

**Facts**

Barbara embezzled $41,165 in 1962 and $5,650 in 1963 from her employer through fictitious deposits into her brother Melton’s bank account. Melton, aware of the embezzlement, used the funds to cover his expenses. Barbara also made fictitious deposits to her own account to cover Melton’s bad checks, which she initially paid with her own money before reimbursing herself through embezzlement.

**Procedural History**

The petitioners conceded the embezzled funds were taxable income in the years they were embezzled but argued they should be taxed to Melton, not Barbara. The case reached the Supreme Court, which affirmed the lower court’s decision that the funds were taxable to Barbara.

**Issue(s)**

1. Whether embezzled funds are taxable as income to the embezzler who exercises dominion and control over them, even if the funds are used to benefit another person.

**Holding**

1. Yes, because the embezzler’s control over the funds constitutes constructive receipt of income, regardless of the ultimate use of the funds.

**Court’s Reasoning**

The Supreme Court relied on the principle established in Helvering v. Horst that income is taxable to the person who has command over its disposition. The Court emphasized that Barbara’s complete dominion and control over the embezzled funds before transferring them to Melton was sufficient to constitute income to her. The

Court distinguished this case from situations where the embezzler might argue the funds flowed directly to the beneficiary without passing through their hands, citing Geiger’s Estate v. Commissioner. The Court found it immaterial that Melton was aware of the source of the funds, focusing instead on Barbara’s control. The Court quoted Geiger’s Estate, stating, “She was the force and the fulcrum which made those benefits possible. She assumed unto herself actual command over the funds. This is enough. “

**Practical Implications**

This decision clarifies that the IRS can tax embezzled funds as income to the embezzler based on their control over the funds, not their personal use. Attorneys should advise clients that transferring embezzled funds to another person does not shield the embezzler from tax liability. This case has been applied in subsequent tax cases involving embezzlement and constructive receipt of income. It also underscores the importance of the “economic benefit” doctrine in tax law, where control over income is the key factor in determining taxability.