Bottome v. Commissioner, 58 T. C. 212 (1972)

A U. S. citizen residing in a community property country may exclude the full amount of foreign-earned income under section 911, even if half of the income is attributed to a nonresident alien spouse.

Summary

Robert Bottome, a U. S. citizen residing in Venezuela, sought to exclude $35,000 in 1964 and $25,000 in 1965 and 1966 of his foreign-earned income under IRC section 911. The Commissioner limited his exclusion to half these amounts, arguing that since his wife, a nonresident alien, owned half the income under Venezuelan community property laws, the exclusion should be split. The Tax Court, however, ruled that Bottome could claim the full exclusion, invalidating the Treasury regulation that supported the Commissioner's position. This decision was based on the interpretation that the statute intended to allow one full exclusion per year for income earned abroad, regardless of community property laws.

Facts

Robert R. Bottome, a U. S. citizen, was a bona fide resident of Venezuela from 1939 and received compensation for services performed there in 1964, 1965, and 1966. His wife, a Venezuelan citizen and nonresident alien, lived with him and, under Venezuelan community property law, owned half of his earnings. The Commissioner determined deficiencies in Bottome's income tax, limiting his foreign-earned income exclusion under section 911 to half the statutory limits, due to his wife's nonresident alien status and her share of the community income.

Procedural History

The case was heard by the U. S. Tax Court after the Commissioner issued a notice of deficiency for Bottome's 1964, 1965, and 1966 tax years. The Tax Court's decision was based on fully stipulated facts under Rule 30 of the Tax Court Rules of Practice.

Issue(s)

1. Whether a U. S. citizen residing in a community property country can exclude the full amount of foreign-earned income under section 911, when half of the income is attributable to a nonresident alien spouse.

Holding

1. Yes, because the Tax Court held that the full statutory exclusion under section 911 applies to the taxpayer's foreign-earned income, regardless of the community property laws that attribute half the income to a nonresident alien spouse, invalidating the Treasury regulation that attempted to split the exclusion.

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Court’s Reasoning

The Tax Court’s decision was grounded in the interpretation of section 911 and its legislative history. The court noted that the statute and committee reports emphasized that the exclusion amount should not be altered by community property laws. The court found no statutory basis for the Commissioner’s position, which was supported by a Treasury regulation (section 1. 911-2(d)(4)(ii), Example 5). The court invalidated this regulation as inconsistent with the statute, which intended one exclusion per taxable year for income earned abroad. The court also referenced the *Renoir* case to support its interpretation that the exclusion should not be divided between spouses. The dissent argued that the regulation should be upheld to prevent discrimination in favor of community property residents, but the majority opinion prevailed, highlighting the statutory language and legislative intent.

Practical Implications

This ruling clarifies that U. S. citizens in community property jurisdictions can claim the full foreign-earned income exclusion under section 911, even when their spouse is a nonresident alien. This has significant implications for expatriates in such jurisdictions, allowing them greater tax benefits than if the exclusion were halved. Legal practitioners should advise clients accordingly, ensuring they maximize their exclusions based on this precedent. The decision also underscores the judiciary’s willingness to invalidate Treasury regulations that conflict with statutory language and legislative intent. Subsequent cases and IRS guidance should reflect this interpretation, potentially influencing future regulatory adjustments to align with the court’s ruling.

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