Hines v. Commissioner, 72 T. C. 715 (1979)

Payments under a loss of license plan are taxable if they do not compensate for permanent loss or loss of use of a member or function of the body and are not computed with reference to the nature of the injury.

Summary

In Hines v. Commissioner, a pilot who suffered a heart attack and was disqualified from flying received payments from his airline's Loss of License Plan. The key issue was whether these payments could be excluded from gross income under IRC section 105(c). The Tax Court held that the payments were taxable because the heart attack did not result in a permanent loss of bodily function, and the payments were not calculated based on the nature of the injury. This case underscores the strict interpretation of section 105(c) and its limited application to severe, permanent injuries.

Facts

Oscar J. Hines, a pilot for Pan American World Airways, suffered a heart attack in 1973. Despite a full recovery, FAA regulations permanently disqualified him from flying. As a result, he received payments from Pan Am's Loss of License Plan for Pilots, totaling $37,349. 08 in 1975. The plan provided benefits to pilots unable to hold an FAA medical certificate for 14 continuous months, with payments determined by the number of incapacitated pilots rather than the nature of their injuries.

Procedural History

The Commissioner of Internal Revenue determined a deficiency in Hines's 1975 income tax return, asserting that the payments from the Loss of License Plan should be included in gross income. Hines petitioned the U. S. Tax Court for a redetermination of the deficiency. The case was fully stipulated and submitted under Rule 122 of the Tax Court Rules of Practice and Procedure.

Issue(s)

1. Whether payments received by Oscar Hines under Pan Am's Loss of License Plan for Pilots can be excluded from gross income under IRC section 105(c)(1) as payments for the permanent loss or loss of use of a member or function of the body.
2. Whether these payments can be excluded under IRC section 105(c)(2) as payments computed with reference to the nature of the injury without regard to the period the employee is absent from work.

Holding

1. No, because the damage to Hines's heart did not constitute a permanent loss or

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loss of use of a member or function of the body, as his heart continued to function normally despite the heart attack.
2. No, because the payments were not computed with reference to the nature of the injury, as all incapacitated pilots received the same benefits regardless of their specific condition.

Court's Reasoning

The court interpreted IRC section 105(c) as intended to provide tax relief for severe, permanent injuries that significantly impair the quality of life. The court found that the heart attack did not qualify under section 105(c)(1) because it did not result in a permanent loss of bodily function; the heart continued to function normally despite the loss of some tissue. The court also ruled that the payments did not meet the requirements of section 105(c)(2) because they were not calculated based on the nature of the injury but rather on the number of incapacitated pilots. The court distinguished this case from Rev. Rul. 63-181, which allowed exclusion for payments to a terminally ill cancer patient, emphasizing the permanent nature of the cancer's impact. The court concluded that the termination of Hines's career as a pilot was irrelevant to the tax treatment of the payments under section 105(c).

Practical Implications

This decision clarifies that payments under loss of license plans are generally taxable unless they specifically compensate for severe, permanent physical injuries. Legal practitioners should advise clients that such plans must be structured to meet the strict criteria of section 105(c) for payments to be excludable from gross income. Employers should review their loss of license plans to ensure compliance with tax laws, and employees should be aware that benefits from these plans are likely taxable unless they meet the statutory requirements. Subsequent cases have reinforced this interpretation, emphasizing the limited scope of section 105(c) exclusions.

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