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Tax Court & Board of Tax Appeals Reported Decisions

MARJORIE E. HALEY, 54 TC 642

Marjorie E. Haley, Petitioner v. Commissioner of Internal Revenue, Respondent

Case Information:

[pg. 642]

Code Sec(s):	
Docket:	Docket No. 6431-67.
Date Issued:	03/26/1970
Judge:	Opinion by QUEALY, J.
Tax Year(s):	Years 1964, 1965.
Disposition:	Decision for Commissioner.

HEADNOTE


1. INCOME EXCLUSIONS — Scholarship and fellowship grants—employer-employee relationship. Exclusion for scholarship or fellowship grant denied state welfare commission employee for amounts received from commission while on educational leave to attend university school of social work. Grants were bargained-for payments given by state only as compensation for her past or future services. Grantor wasn't U.S. Government with which she

had no employment relationship: funds were distributed by state rather than Department of Health, Education and Welfare.

Reference(s): 1970 P-H Fed. ¶8629(30).

Syllabus

Offical Tax Court Syllabus

Petitioner was an employee of the Jackson County Public Welfare Commission of the State of Oregon. The petitioner was granted educational leave in 1964 and 1965 in order to attend the University of Washington, School of Social Work. *Held*, amounts received by the petitioner from the Oregon State Welfare Commission while on educational leave are not excludable from petitioner's gross income as either scholarships or fellowship grants. Sec. 1.117-4(c); *Bingler v. Johnson*,  394 U.S. 741 (1969).

Counsel

Charles M. Johnson, for the petitioner.

Stephen E. Silver and *Gary C. Randall*, for the respondent.

Quealy, *Judge*:

Respondent determined deficiencies in petitioner's income tax for 1964 and 1965 in the respective amounts of \$375.99 and \$254.55. The issue presented for decision is whether amounts received by petitioner in those years are excludable from gross income as either scholarships or fellowship grants within the meaning of section 117 of the Code.¹

FINDINGS OF FACT

Some of the facts have been stipulated, and those facts are so found.

The petitioner, Marjorie E. Haley, was a legal resident of Salem, Oreg., at the time her petition was filed. She filed her Federal income tax returns for 1964 and 1965 with the district director of internal revenue, Portland, Oreg.

In 1963, and part of 1964, petitioner was employed as a supervisor trainee by the Jackson County Public Welfare Commission in the [\[pg. 643\]](#)State of Oregon. At that time she held a

bachelor's degree. Petitioner applied to the Oregon State Public Welfare Commission (hereinafter State Commission) for educational leave grants in 1963 and 1964 to attend the University of Washington, School of Social Work. Petitioner was given the requested leave and received educational leave grants of \$3,510 in 1964 and \$2,200 in 1965 from the State Commission. Shortly after receiving a master's degree in social work at the University of Washington, petitioner went to work as a supervisor for the Marion County Public Welfare Commission in the State of Oregon.

Under the educational leave grant agreement signed by the petitioner in 1963, she agreed, in accepting the grant from the State Commission, to work at least 1 year in a county welfare department in the State of Oregon or in the State Commission following the period of training. She also agreed to accept employment where the need for work was greatest and to refund training grant payments if she either failed to complete the period of study or failed to carry out the employment agreement.

Under the educational leave grant agreement signed by the petitioner in 1964 she agreed, for and in consideration of the grant, to accept a position assigned by the State Commission in public welfare within the State Commission or a county public welfare department and to discharge the duties of the assigned position for a period of at least twice the length of time of the educational leave. She agreed to reimburse the State Commission for the amount paid on the grant if she failed to accept the position assigned by the State Commission, or if she failed satisfactorily to discharge in its entirety the employment commitment. As petitioner received 9 monthly payments, she was obligated under the 1964 agreement to work for the State Commission or a county department for 18 months. The 1964 reimbursement provision varied from the 1963 contract by providing for a prorata repayment based on actual months of employment.

Prior to the grants, petitioner received compensation of \$500 a month. Petitioner received \$350 monthly from the State Commission under the 1963 agreement and \$440 a month under the 1964 agreement. Upon returning to work, petitioner was paid approximately \$585 per month. Petitioner's salary was not affected (reduced or increased) by reason of the leave grants, except for an increase to reflect her higher education level.

The leave grants were not related to the petitioner's length of service or previous status with the State Commission.

During the period of her educational leave deductions were made for State retirement, and time in school counted for State retirement.[pg. 644] However, petitioner accrued neither sick

nor vacation leave. While petitioner was on leave the State Commission hired a replacement to perform the duties previously assigned petitioner.

The State Commission has encouraged individuals, including its employees and others, to obtain advance degrees and to pursue additional academic work. The administrator of the State Commission, in a letter concerning petitioner that was addressed to the Internal Revenue Service, stated that the purpose of the educational leave grant program was to improve the service and administration of the State Commission by improving the skills of the employees of the agency through graduate work in social work.

Financing of the program through which the petitioner received her grants was provided 75 percent by the Federal Government through the Health, Education, and Welfare Department, and 25 percent by the State of Oregon. Federal funding was authorized under the Public Welfare Amendments of 1962. Pub. L. 87-543 (July 25, 1962). All funds were disbursed from the State of Oregon general funds, as are all other disbursements from other State of Oregon agencies.

The State Commission withheld from the petitioner's 1964 and 1965 grant payments amounts representing Federal withholding. Petitioner excluded the grants from taxable income on her 1964 and 1965 income tax returns and claimed refunds for both years. In his notice of deficiency, respondent included in petitioner's 1964 and 1965 income the amounts of the State Commission payments excluded by the petitioner. However, as the petitioner had not deducted educational costs in her 1964 and 1965 returns the Commissioner made provisions for such deductions allowing a deduction of \$1,461.74 in 1964 and \$937 in 1965 as allowable educational expense deductions. The allowance was made pursuant to a list of deductible items submitted by the petitioner. The respondent also made other adjustments. However, those adjustments are not in issue in this proceeding.

OPINION

Section 117(a)² excludes from gross income any amount received "as a scholarship at an educational institution" or as "a fellowship grant." The statute does not define the terms "scholarship" and "fellowship grant," but the regulations provide that amounts representing [pg. 645]"compensation for past, present, or future employment services," and amounts "paid *** to *** an individual to enable him to pursue studies or research primarily for the benefit of the grantor" are not excludable as scholarships or fellowship grants. Sec. 1.117-4(c)(1),(2), Income Tax Regs.³ These regulations have been held to conform to the statutory purpose and to comport with the ordinary understanding of scholarships and fellowships as relatively

disinterested, no-strings educational grants with no requirement of any substantial quid pro quo from the recipients. *Bingler v. Johnson*, 394 U.S. 741 (1969).

The Supreme Court stated in *Bingler v. Johnson, supra* at 757, that:

The thrust of the provision dealing with compensation [sec. 1.117-4(c)] is that bargained-for payments, given only as a "quo" in return for the *quid* of services rendered—whether past, present, or future—should not be excludable from income as "scholarship" funds. ***

In the *Bingler* case, the Supreme Court cited with approval the cases of *Ussery v. United States*, 296 F. 2d 582 (C.A. 5, 1961), and *Stewart v. United States*, 363 F. 2d 355 (C.A. 6, 1966).

In *Ussery v. United States, supra*, the court held taxable monthly payments received by an employee of the Mississippi Department of Public Welfare who had been given leave to secure a master's degree in social work. The taxpayer in that case retained his rights under a merit system for retirement benefits and workmen's compensation. On completion of his educational work, the taxpayer was obligated to return to service with the grantor for at least 12 months for each school year of educational leave, or reimburse the grantor for that portion of his educational leave not liquidated through service. The taxpayer also received his regular salary, salary advances, retirement benefits, and all other compensation that he would have been entitled to receive had he remained at his regular job. As to the significance of the continuation of the taxpayer's compensation at his regular job level the court stated, *supra* at 586:

By itself this might indicate mere generosity on the part of the employer, but in addition *** [the taxpayer] was obligated to return to work for the [pg. 646] Department for at least a year or to return his employer's investment in his education. The inference is clear that the program was adopted by the [grantor] to train its employees so that they could perform their duties more effectively.

In *Stewart v. United States, supra*, the court held taxable an educational leave grant received by an employee of the Tennessee Department of Public Welfare. In that case there was no indication that the amount of the educational grant was related to the taxpayer's regular salary. However, the taxpayer was an employee of the grantor before and after taking educational leave. Also, during her leave the taxpayer retained her State civil service status and received credit towards retirement. Taking into account the facts that indicated a continuing employment relationship between the grantor and the taxpayer, the court found


sufficient indicia of compensation to hold that the grant was in payment of past and future services.

The petitioner attempts to distinguish prior decisions by dividing the Oregon welfare system into three distinct entities: The Jackson County Public Welfare Commission; the Marion County Public Welfare Commission; and the State Commission. Petitioner contends that when the Oregon welfare system is viewed in this light, it is clear that no employment relationship could exist between the petitioner and the State Commission either before or after the grants, and thus that the grants cannot be considered compensation for past or future services.

Petitioner's argument is inconsistent with the dual responsibility of the State and counties under the Oregon welfare system. The Oregon Revised Statutes establish a State-administered public welfare plan. Ore. Rev. Stat. sec. 411.060 (1967). County public welfare commissions are subject to the regulations made by the State Commission, and can hire only upon the approval of the State Commission and in accordance with the State civil service system. Ore. Rev. Stat. sec. 411.150 (1967). The compensation of county personnel is fixed by the administrator of the State Commission, Ore. Rev. Stat. sec. 411.270 (1967); and the State Commission is the appointing authority of all county personnel for the purposes of the State civil service law. Ore. Rev. Stat. sec. 411.260 (1967). Seventy percent of the funds required for the administration of each county's welfare program are, in general, provided by the State Government and 30 percent of such funds are provided by the county. Ore. Rev. Stat sec. 411.160 (1967).

In the instant case the educational leave grants received by the petitioner in 1964 and 1965 were bargained-for payments given by the State Commission only as compensation in return for past or [pg. 647]future services rendered, or to be rendered, by the practitioner in the office of the State Commission or one of its county affiliates. Such payments are not scholarships or fellowship grants within the meaning of section 117 of the Code. *Bingler v. Johnson, supra*; cf. *Ussery v. United States, supra*; *Stewart v. United states, supra*.

The petitioner also attempts to support an exclusion for 75 percent of her educational grant under the theory that the grantor was the United States, not the State of Oregon. Her argument is that, as she had no employment relationship with the Federal Government, the grant, to the extent funded by Federal moneys under a 75-percent matching program, could not be in consideration of her "past, present, or future services" to the Federal Government. Petitioner's argument must fail as her agreement was not with the Federal Government and as she did not receive funds from the Department of Health, Education, and Welfare or any

other Federal Agency. The Federal government was not the grantor. Cf. *Norman R. Williamsen, Jr.*,  32 T.C. 154 (1959). The grantor of the funds was the State Commission, and the funds were distributed from the general funds of the State of Oregon.

The educational leave grants of \$3,510 in 1964 and \$2,200 in 1965 are not excludable from the petitioner's gross income as either scholarships or fellowship grants within the meaning of section 117 of the Code.

Decision will be entered for the respondent.

¹ All section references are to the Internal Revenue Code of 1954, as amended, unless otherwise noted.

² Sec. 117. SCHOLARSHIPS AND FELLOWSHIP GRANTS.

(a) General Rule.—In the case of an individual, gross income does not include—

(1) any amount received—

(A) as a scholarship at an educational institution (as defined in sec. 151(e)(4)),
or

(B) as a fellowship grant, including the value of contributed services and accommodations; and

³ Sec. 1.117-4 Items not considered as scholarships or fellowship grants.

The following payments or allowances shall not be considered to be amounts received as a scholarship or a fellowship grant for the purpose of sec. 117: ***

(c) *Amounts paid as compensation for services or primarily for the benefit of the grantor.*

(1) Except as provided in paragraph (a) of sec. 1.117-2, any amount paid or allowed to, or on behalf of, an individual to enable him to pursue studies or research, if such amount represents either compensation for past, present, or future employment services or represents payment for services which are subject to the direction or supervision of the grantor.

(2) Any amount paid or allowed to, or on behalf of, an individual to enable him to pursue studies or research primarily for the benefit of the grantor.

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