6 T.C. 782 (1946)

Selling expenses related to securities and legal fees for tax advice are generally not deductible as ordinary and necessary expenses under Section 23(a)(2) of the Internal Revenue Code for individuals not engaged in the trade or business of dealing in securities, unless directly related to the production or collection of income or the management, conservation, or maintenance of property held for income production.

Summary

This case addresses whether an individual can deduct selling commissions for securities and legal fees for tax advice as ordinary and necessary expenses under Section 23(a)(2) of the Internal Revenue Code. The Tax Court held that selling commissions must be treated as offsets against the sale price, not as deductible expenses. The Court further held that legal fees connected with the preparation of income tax returns are personal expenses and are not deductible unless the taxpayer can show a direct connection to income production or property management.

Facts

The petitioner, the Estate of Marcellus L. Joslyn, sought to deduct $6,923.70 in selling commissions paid to brokers for the sale of securities and $5,000 for registration of securities with the Securities and Exchange Commission. Additionally, the petitioner sought to deduct $1,275 paid to an attorney for legal services, including $150 for preparing income tax returns and the remainder for general legal and auditing services.

Procedural History

The Commissioner of Internal Revenue disallowed the deductions claimed by the Estate. The Estate then petitioned the Tax Court for a redetermination of the tax deficiency.

Issue(s)

1. Whether selling commissions paid in connection with the disposition of securities by an individual not a dealer in securities are deductible as ordinary and necessary expenses under Section 23(a)(2) of the Internal Revenue Code.

2. Whether expenses for registration of securities with the Securities and Exchange Commission are deductible as ordinary and necessary expenses under Section 23(a)(2) of the Internal Revenue Code.

3. Whether legal fees paid for tax advice and preparation of income tax returns are deductible as ordinary and necessary expenses under Section 23(a)(2) of the

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Internal Revenue Code.

Holding

1. No, because selling commissions are treated as offsets against the sale price in determining gain or loss, consistent with established precedent and the intent of Congress.

2. No, because expenses for registering securities with the SEC are in the nature of selling costs and receive the same treatment as selling commissions.

3. No, because the costs of tax advice and preparation of income tax returns are considered personal expenses and are not deductible unless the taxpayer can prove a proximate relationship to the production or collection of income, or the management, conservation, or maintenance of property held for the production of income.

Court's Reasoning

The court reasoned that the Supreme Court in *Spreckles v. Helvering* established that selling commissions are offsets against the sale price. Section 23(a)(2) was designed to alleviate the harshness of *Higgins v. Commissioner*, allowing deductions for non-business expenses, but was not intended to overturn existing rules regarding selling commissions. The court cited congressional reports stating that deductions under 23(a)(2) are subject to the same restrictions as 23(a)(1), except for the trade or business requirement. The court stated: "A deduction under this section is subject, except for the requirement of being incurred in connection with a trade or business, to all the restrictions and limitations that apply in the case of the deduction under section 23(a) (1) (A) of an expense paid or incurred in carrying on any trade or business." Regarding legal fees, the court followed precedent that such costs are personal expenses unless a direct connection to income-producing activities is demonstrated, which the petitioner failed to do. The court emphasized that the taxpayer bears the burden of proving that claimed deductions fall within the statutory provisions, citing *New Colonial Ice Co. v. Helvering*.

Practical Implications

This case reinforces the principle that taxpayers cannot deduct selling expenses for securities unless they are in the business of dealing in securities. This means that individual investors must reduce the proceeds from sales by the amount of any commissions paid to brokers, impacting the calculation of capital gains or losses. The decision also clarifies that legal fees for tax advice are generally considered personal expenses and are not deductible unless a clear and direct link to income-producing activities or property management can be established. Attorneys and tax advisors must inform clients of this limitation and advise them to maintain detailed records demonstrating the connection between legal services and income-producing

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activities if they intend to claim a deduction. This case is often cited when determining the deductibility of expenses related to investment activities and tax planning.

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