6 T.C. 659 (1946)

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A partnership between spouses is recognized for tax purposes when both contribute capital or vital services to the business, even if one spouse’s capital contribution originated from a gift.

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Summary

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Leo Marks and his wife, Mollie, operated a jewelry and optometry business. Mollie contributed initial capital and years of labor to the business. When their son’s involvement caused friction, Mollie demanded formal recognition for her contributions. A partnership agreement was created, splitting profits equally after Leo’s salary. The IRS challenged the validity of the partnership, arguing that the entire income should be taxed to Leo. The Tax Court held that a valid partnership existed because Mollie contributed both initial capital and substantial, continuous services to the business.

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Facts

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Leo and Mollie Marks married in 1918. Mollie contributed her savings ($400) and wedding gifts ($250) to Leo’s fledgling jewelry and optometry business. Mollie worked alongside Leo from the beginning, managing the jewelry department, handling advertising, and significantly contributing to the business’s growth. She worked long hours, even after having children. In 1941, after a dispute about their son’s role in the business, Leo and Mollie formalized a partnership. Mollie gave Leo a note for half the inventory value, partially offset by a gift from Leo. The partnership agreement stipulated that Leo would receive a $6,000 salary, with the remaining profits split equally.

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Procedural History

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The Commissioner of Internal Revenue assessed deficiencies against Leo Marks, arguing that all business income was taxable to him. Marks petitioned the Tax Court for redetermination. The Tax Court ruled in favor of Marks, finding that a valid partnership existed, allowing income to be split between the partners.

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Issue(s)

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Whether the partnership between Leo and Mollie Marks is a valid partnership for income tax purposes, allowing the business income to be divided between them, or whether the entire income is taxable to Leo alone.

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Holding

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Yes, the partnership between Leo and Mollie Marks is a valid partnership for income tax purposes because Mollie contributed both initial capital and continuous, valuable services to the business over many years.

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Court’s Reasoning

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The court relied on Lusthaus v. Commissioner, 327 U.S. 293, stating that a partnership exists when two or more people contribute property or services to an enterprise and agree to share the proceeds. Referencing Commissioner v. Tower, 327 U.S. 280, the court acknowledged that a husband and wife can be partners if the wife “either invests capital originating with her or substantially contributes to the control and management of the business, or otherwise performs vital additional services, or does all of these things.” Even though some of Mollie’s initial capital was a gift, her decades of continuous and valuable services to the business were undeniable. Her contributions were not

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