6 T.C. 1183 (1946)

A taxpayer can deduct a loss on an investment in a trust in the year the loss is sustained, evidenced by a closed and completed transaction fixed by an identifiable event, when the amount of the loss becomes reasonably certain.

Summary

Arthur Webster, a shareholder in Bankers Trust Co., invested $17,000 in a trust created by 30 shareholders to purchase real properties from the trust company. The properties were subject to mortgages. After two properties were foreclosed and one was sold, the remaining assets were distributed, except for funds impounded in a closed bank. In 1940, Webster received $213.15, his share of the impounded funds, and assigned his remaining interest in the trust. The Tax Court held that Webster sustained a deductible loss in 1940 because the amount of the potential loss was not reasonably determinable until the final distribution and assignment occurred in that year, marking a closed and completed transaction.

Facts

In 1931, 30 shareholders of Bankers Trust Co. created a $126,325 fund to purchase three mortgaged apartment buildings from the company. Arthur Webster contributed $17,000 to this fund. The properties were conveyed to a trustee, John C. Bills, to manage and distribute any net profits. Due to mortgage foreclosures and a sale, by April 1, 1936, the trust's assets dwindled. Most of the remaining cash was distributed in June 1936, but a portion remained impounded in a closed bank. While further distributions were expected, their amount was uncertain.

Procedural History

Webster claimed a long-term capital loss on his 1940 tax return related to his investment in the trust. The Commissioner of Internal Revenue disallowed the deduction, arguing the loss was not sustained in 1940. Webster petitioned the Tax Court, contesting the Commissioner's determination.

Issue(s)

Whether Webster sustained a deductible long-term capital loss on his investment in the trust in the tax year 1940.

Holding

Yes, because the loss was sustained in 1940, evidenced by the final distribution of remaining trust assets and Webster's assignment of his interest in the trust, constituting a closed and completed transaction and making the amount of the loss reasonably certain.

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Court’s Reasoning

The court emphasized that a deductible loss must be evidenced by a closed and completed transaction, fixed by an identifiable event. The court cited prior precedent including *United States v. S.S. White Dental Mfg. Co.* and *Lucas v. American Code Co.*, and noted that the determination of when a loss is sustained is a practical, not a legal, test. While most trust assets were distributed in 1936, the amount of future distributions from the closed bank was uncertain. Only in 1940, with the final dividend and Webster’s subsequent assignment of his interest, did the loss become reasonably certain. The court distinguished this case from *Bickerstaff v. Commissioner*, where the amount of loss was determinable with reasonable certainty in an earlier year. The court stated, “Partial losses are not allowable as deductions from gross income so long as the stock has a value and has not been disposed of.” Herein the amount of further distributions could not be determined with reasonable certainty.

Practical Implications

This case provides a practical application of the “identifiable event” standard for deducting losses. It clarifies that a loss on an investment is deductible when the amount of the loss becomes reasonably certain and the transaction is closed, not necessarily when the underlying asset declines in value. Legal professionals should consider Webster when advising clients on the timing of loss deductions related to trusts, partnerships, or other investments where the ultimate value is uncertain. Taxpayers can’t claim deductions for partial losses on assets that still have value unless they dispose of those assets. This ruling highlights the importance of assessing the facts to determine the year in which the loss is definitively sustained, considering both objective events and the taxpayer’s actions.

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