***8 T.C. 904 (1947)***

Whether a taxpayer's real estate activities constitute a "trade or business" is a factual determination, impacting the characterization of gains and losses as ordinary or capital for tax purposes.

**Summary**

The Tax Court addressed whether Walter Morley's real estate activities qualified as a "trade or business" during 1940-41. Morley sought to deduct losses from property sales as ordinary losses, arguing they were inventory in his real estate business. The court determined Morley was engaged in the trade or business of selling real estate, allowing ordinary loss treatment. It also addressed the deductibility of losses related to property held as tenancy by the entirety, limiting Morley's deduction to one-half of the loss.

**Facts**

Morley was involved in real estate activities for many years, including managing a realty company and personally buying and selling properties. From 1917 to 1931, he purchased lots, built houses, and engaged in sales. His real estate activities decreased after 1931 due to the Depression. In 1940 and 1941, he disposed of several properties, including the Pallister & Churchill Streets property, the West Grand Boulevard property, and an 80-acre tract. Morley also held a real estate broker's license and managed properties. He was also involved in the Steel Plate & Shape Corporation during this time.

**Procedural History**

The Commissioner of Internal Revenue determined a deficiency in Morley's 1941 income tax liability, disallowing a business loss carry-over from 1940 and reducing the deductible loss from the sale of the 80-acre farm. Morley petitioned the Tax Court, contesting these adjustments.

**Issue(s)**

1. Whether the loss sustained on the disposal of an 80-acre tract of land in 1941 is deductible as an ordinary loss or a capital loss.
2. Whether Morley had a net operating loss carry-over from 1940 due to losses on the disposal of real estate properties.
3. Whether Morley can deduct the entire loss from the 80-acre tract, or only one-half because it was held as tenancy by the entirety.

**Holding**

1. The loss on the 80-acre tract is deductible as an ordinary loss; Yes, because Morley was engaged in the trade or business of selling real estate and the property

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was held primarily for sale to customers.
2. Morley had a net operating loss carry-over from 1940; Yes, because the losses were attributable to the operation of a trade or business regularly carried on by Morley.
3. Morley can deduct only one-half of the loss from the 80-acre tract; Yes, because the property was held as tenancy by the entirety, and under Michigan law, only one-half of the loss is deductible.

**Court's Reasoning**

The court reasoned that Morley's activities constituted a "trade or business" based on the frequency, extent, and nature of his real estate dealings. The court considered his long-term involvement, the intent to sell for profit, and the impact of the Depression on his activities. The court noted that while his sales decreased after 1931, this was due to economic circumstances and not a change in intent. The court distinguished this from isolated transactions and emphasized that his activities were extensive, frequent, and regular before the depression. The court emphasized that a taxpayer can be engaged in more than one trade or business simultaneously. Regarding the tenancy by the entirety, the court relied on Michigan law and prior Tax Court decisions, stating that income and losses from such estates are divided equally between the tenants.

**Practical Implications**

This case illustrates the importance of demonstrating continuous and regular real estate activity to qualify for ordinary loss treatment. Taxpayers seeking to deduct real estate losses as ordinary losses must show that their activities constitute a trade or business, considering factors like the frequency and extent of transactions, intent to sell, and the impact of external factors on their business. It also clarifies that even if a business slows down due to economic conditions, the intent to resume operations is a significant factor. Moreover, it reaffirms that state property law significantly impacts the tax treatment of jointly-owned property.

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