9 T.C. 222 (1947)

To claim a war loss deduction under Section 127 of the Internal Revenue Code for property in enemy-controlled territory, a taxpayer must prove the property existed when the U.S. declared war and establish its cost basis, adjusted for depreciation.

Summary

Benjamin Abraham, a resident alien, sought a war loss deduction for property in France occupied by Germany during 1941. The Tax Court addressed whether Abraham proved the existence and value of real and personal property on December 11, 1941, when the U.S. declared war on Germany, as required by Section 127 of the Internal Revenue Code. The Court allowed a deduction for the real property and some personal property, estimating depreciation where precise data was unavailable, but disallowed the deduction for personal property whose existence on the critical date could not be established. The court also addressed the deductibility of unreimbursed business expenses.

Facts

Benjamin Abraham, a resident alien in the U.S., owned real and personal property in Courgent, France. He left France in May 1940, before the German occupation. The property included land, buildings, oil paintings, books, rugs, and furniture. When he returned in 1946, the land and most buildings were intact, but one small house was missing, and some personal property was gone. Abraham sought a war loss deduction on his 1941 tax return for the presumed destruction or seizure of this property.

Procedural History

The Commissioner of Internal Revenue disallowed Abraham’s war loss deduction and a deduction for certain business expenses, resulting in a tax deficiency. Abraham petitioned the Tax Court, contesting these adjustments.

Issue(s)

1. Whether Abraham is entitled to a war loss deduction under Section 127(a)(2) of the Internal Revenue Code for real and personal property located in German-occupied France.

2. Whether Abraham is entitled to a deduction for unreimbursed business expenses incurred for entertaining clients.

Holding

1. Yes, in part, because Abraham demonstrated the existence of the real property and some personal property on December 11, 1941, and provided a basis for

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estimating their value, adjusted for depreciation. No, in part, because Abraham failed to prove that some personal property was in existence on December 11, 1941.

2. Yes, because Abraham substantiated that he incurred and paid for at least $500 in unreimbursed business expenses.

Court's Reasoning

The Court relied on Section 127(a)(2) of the Internal Revenue Code, which deems property in enemy-controlled territory on the date war is declared to have been destroyed or seized. To claim a loss under this section, the taxpayer must prove (1) the property existed on the date war was declared and (2) the cost of the property, adjusted for depreciation. Regarding the real property, the Court found that Abraham's testimony that the property (except one small house) was still there in 1946 was sufficient to prove its existence on December 11, 1941. Lacking precise depreciation data, the court applied the doctrine from *Cohan v. Commissioner*, 39 F.2d 540, and made a reasonable approximation of the loss, bearing heavily against the taxpayer. The Court estimated depreciation at 50% of the cost basis. Regarding the personal property, the Court disallowed the deduction for items Abraham could not prove were in existence on the date war was declared. However, for the personal property that was present when Abraham returned in 1946, the Court again applied the *Cohan* rule and estimated depreciation at 50%. Regarding business expenses, the court allowed a deduction for $500 in unreimbursed entertainment expenses under Section 23(a)(1)(A) of the Code, finding that these expenses were ordinary and necessary business expenses.

Practical Implications

Abraham v. Commissioner illustrates the evidentiary burden for claiming war loss deductions under Section 127 of the Internal Revenue Code. Taxpayers must substantiate the existence and value of property in enemy-controlled territory as of the date war was declared. While precise documentation is ideal, the court may estimate depreciation under the *Cohan* rule when necessary. This case also shows the importance of maintaining records for business expenses, even when unreimbursed, to support deductions under Section 23(a)(1)(A). The case provides a framework for analyzing similar war loss claims, especially where complete records are unavailable due to wartime circumstances. It emphasizes that even in the absence of detailed records, taxpayers can still claim deductions by providing reasonable estimates, although the burden of proof remains with the taxpayer. The ruling highlights the application of the Cohan rule in tax law, allowing for deductions based on reasonable estimates when precise documentation is lacking.

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