Wyler v. Commissioner, 14 T.C. 1251 (1950)

A professional's accounting practice, including its goodwill, can be a capital asset, and the sale of that practice results in capital gain, taxable under Section 117 of the Internal Revenue Code.

Summary

The Tax Court addressed whether the transfer of an accounting practice constituted a sale of goodwill, thus qualifying for capital gains treatment under Section 117 of the Internal Revenue Code. Wyler, the petitioner, sold his accounting practice to Peat, Marwick, Mitchell and Company. The Commissioner argued that the $50,000 payment was for personal services, not the sale of goodwill. The court held that the payment was indeed for the sale of Wyler's practice, which included goodwill, and therefore qualified as a capital gain, despite a clause referencing personal service.

Facts

- Wyler, an accountant, entered into an agreement with Peat, Marwick, Mitchell and Company to transfer his accounting practice.
- The agreement included a payment of $50,000 to Wyler upon signing.
- Wyler continued to provide services to Peat, Marwick, Mitchell and Company under a separate compensation arrangement.
- The contract contained a clause stating "this is an agreement for personal service."
- Peat's internal memos indicated the payment was for Wyler's practice and goodwill.

Procedural History

The Commissioner determined that the $50,000 payment was for personal services and thus taxable as ordinary income. Wyler petitioned the Tax Court, arguing that the payment was for the sale of his accounting practice and should be treated as a capital gain.

Issue(s)

1. Whether the goodwill of a professional accounting practice can be considered a capital asset subject to sale.
2. Whether the $50,000 payment was for the sale of Wyler's accounting practice (including goodwill) or for personal services.

Holding

1. Yes, because good will can exist in a professional practice and can be the subject of transfer.
2. Yes, because the court found that the payment was specifically for the

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purchase of Wyler's practice and its associated goodwill, despite contract language to the contrary.

Court's Reasoning

The court first addressed whether a professional practice could possess vendible goodwill, acknowledging conflicting views but adopting the position that goodwill can exist in a professional practice. Citing *Rodney B. Horton, 13 T.C. 143*, the court stated that "good will was a part of the assets transferred in a sale by a certified public accountant of his business." The court then examined the facts, including testimony and internal memos, to determine the true nature of the $50,000 payment. The court noted the testimony of Peat's senior partner, who stated, "It wasn't his terms. It was our terms. We offered him $50,000…to get his practice, to get his good will." The court concluded that "The purchaser certainly thought it was buying good will and agreed to pay for it." The court distinguished *E. C. O'Rear, 28 B. T. A. 698*, because in that case, the agreements were not contracts for the sale of goodwill. The court ruled that the $50,000 was taxable as a capital gain under Section 117 of the Internal Revenue Code.

Practical Implications

Wyler v. Commissioner clarifies that the sale of a professional practice can be treated as a capital gain if the sale includes the transfer of goodwill. This case highlights the importance of properly documenting the intent and substance of the transaction. Specifically, the case demonstrates that the intent of the parties and the surrounding circumstances can outweigh specific language in a contract. Attorneys should advise clients to clearly define the assets being transferred and allocate the purchase price accordingly to ensure proper tax treatment. This case has been followed in subsequent cases involving the sale of professional practices, further solidifying the principle that goodwill can be a capital asset in such transactions.

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