16 T.C. 467 (1951)

To deduct a loss under Section 23(e) of the Internal Revenue Code, the taxpayer must demonstrate that the loss was incurred in a trade or business or in a transaction entered into for profit.

Summary

The Estate of Frank D. Waterman sought to deduct a loss incurred when a debt owed to the estate by a British company, L.G. Sloan, Ltd., was repaid in devalued British pounds. The Tax Court denied the deduction, holding that the estate failed to prove the original loan by the decedent was connected to his trade or business or was a transaction entered into for profit. The court emphasized that the estate had the burden of proving the loan's connection to a business or profit-seeking activity to qualify for the loss deduction under Section 23(e) of the Internal Revenue Code.

Facts

Frank D. Waterman (the decedent) loaned 10,000 pounds to L.G. Sloan, Ltd. (Sloan), a British company. The loan was evidenced by a non-interest-bearing bill of exchange due July 27, 1937. Waterman died on May 6, 1938. The 10,000-pound debt was included in Waterman's gross estate for federal estate tax purposes, valued at $46,806.94. On April 18, 1945, Sloan deposited 10,000 pounds in a London bank, which was credited to the estate's account on July 2, 1945, in payment of the debt. The estate's account was a "blocked sterling account," not convertible into dollars during 1945.

Procedural History

The executor of Waterman's estate filed a fiduciary return for 1945, paying the tax due. The executor later claimed an overpayment, asserting a $6,406.94 loss due to the devaluation of the British pound. The Commissioner of Internal Revenue denied the deduction, leading to a petition to the Tax Court. The Tax Court upheld the Commissioner's determination.

Issue(s)

Whether the petitioner is entitled to a loss deduction under Section 23(e) of the Internal Revenue Code as a result of receiving payment on a debt in devalued British pounds, when the estate has not demonstrated the loan was connected to the decedent's trade or business or a transaction entered into for profit?

Holding

No, because the estate failed to demonstrate that the original loan made by the decedent was connected to his trade or business or was a transaction entered into for profit, as required for a loss deduction under Section 23(e) of the Internal

© 2025 SCOTUSreports.com. All rights reserved.

Revenue Code.

Court’s Reasoning

The Tax Court reasoned that under Section 23(e) of the Internal Revenue Code, a loss is deductible only if it is incurred in a trade or business, a transaction entered into for profit, or as a result of a casualty. The court emphasized that the burden of proof lies with the taxpayer (in this case, the estate) to demonstrate that the loss meets one of these criteria. The court noted that the record did not reveal the circumstances surrounding the origin of the loan, only that it was a personal, non-interest-bearing loan. Because the estate failed to prove the loan was connected to the decedent’s trade or business or a transaction entered into for profit, the loss was not deductible. The court distinguished the case from *N. Stuart Campbell, 5 T.C. 272*, where inherited property was immediately listed for sale, thus evidencing a profit-seeking motive by the heir.

Practical Implications

This case underscores the importance of documenting the purpose and nature of financial transactions, especially loans, to ensure potential tax deductions are preserved. For estate planning and administration, it highlights the need to gather evidence showing whether a decedent’s financial activities were related to a trade, business, or profit-seeking venture. Attorneys should advise clients to maintain records that clearly establish the business or investment purpose behind loans and other financial dealings. Subsequent cases will likely distinguish *Waterman* based on the specific facts presented to demonstrate whether the underlying transaction was entered into for profit. Without such proof, losses incurred, even if real, may not be deductible for tax purposes.

© 2025 SCOTUSreports.com. All rights reserved.