16 T.C. 906 (1951)

Losses incurred from the sale of real property used in a trade or business, such as rental property, are fully deductible as ordinary losses, not subject to capital loss limitations.

Summary

John E. Good sold a 20-acre parcel of land he had owned for many years. He originally intended to subdivide the land, but when that plan failed, he rented it out for various uses, including hay and grain farming, pasture, and lumber storage. On his 1944 tax return, Good deducted the loss from the sale as a business loss. The Commissioner of Internal Revenue argued that the loss was from the sale of a capital asset and subject to capital loss limitations. The Tax Court ruled in favor of Good, holding that because the property was used in his trade or business (i.e., renting), the loss was fully deductible under Section 23(e) of the Internal Revenue Code.

Facts

In 1923, Good purchased a 20-acre parcel of land near Clovis, California, intending to subdivide and sell lots. When economic conditions worsened, he abandoned this plan. He refunded the sale price to the few buyers he had. He reclassified the land as acreage to save on taxes. For most of the years between 1923 and 1944, Good rented the property. Uses included hay and grain farming (rented for a quarter share of the profits), pasture ($50/year), and lumber storage ($50/year for a 2-acre portion). The annual rental income sometimes exceeded the property taxes. Good managed the property himself and did not engage real estate brokers. He also owned and rented four other parcels of farm property and occasionally bought and resold houses. He was also a partner in a general merchandising business, spending more than half his time on that venture.

Procedural History

Good deducted the loss from the sale of the 20-acre property on his 1944 tax return as a loss incurred in a transaction entered into for profit. The Commissioner determined that the loss was from the sale of a capital asset and subject to the limitations of Section 117 of the Internal Revenue Code. Good petitioned the Tax Court for a redetermination of the deficiency.

Issue(s)

Whether the loss from the sale of the 20-acre parcel of land constituted a loss from the sale of a capital asset, subject to capital loss limitations, or a fully deductible loss from real property used in the taxpayer’s trade or business.

Holding

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No, because the property was “real property used in the trade or business of the taxpayer” since Good rented the property during substantially all of the period he owned it; therefore, the loss is deductible in full under Section 23(e) of the Internal Revenue Code.

Court’s Reasoning

The court relied heavily on its prior decision in *Leland Hazard, 7 T.C. 372*. In *Hazard*, the taxpayer had converted a former residence into rental property. The Tax Court had held that the loss from the sale of that property was fully deductible, not subject to capital loss limitations. The court in *Good* found no material distinction between the facts in *Good* and those in *Hazard*, noting, “The facts of the case at bar are not distinguishable from the *Hazard* case, *supra*. Petitioner rented the property throughout almost all of the time that he held it.” Because Good rented the property for the majority of the time he owned it, the court concluded the property was used in his trade or business and was therefore not a capital asset under Section 117(a)(1) of the Code. The court also cited *William H. Jamison, 8 T.C. 173*; *Solomon Wright, Jr., 9 T.C. 173*; *Mary E. Crawford, 16 T.C. 678* in support of its holding.

Practical Implications

This case establishes that even if a taxpayer’s primary business is something other than real estate, renting out property can constitute a trade or business for tax purposes. This is a significant benefit, as losses from the sale of such property are fully deductible as ordinary losses. It is important to note that the taxpayer must demonstrate that the property was actually rented out for a substantial period to qualify for this treatment. The decision emphasizes the importance of documenting rental activities. Subsequent cases have distinguished *Good* where the rental activity was minimal or incidental. This ruling remains relevant for taxpayers who own and rent real estate, particularly in determining the tax treatment of gains or losses upon the sale of such property.

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