T.C. Memo. 1952-202

A teacher who regularly writes and publishes textbooks related to their teaching is considered to be engaged in the trade or business of writing, and income derived from the sale of those manuscripts is considered ordinary income, not capital gains.

Summary

Disney, a mathematics teacher, sought to treat income from the sale of textbook manuscripts as capital gains, arguing that writing was merely a hobby. The Tax Court disagreed, holding that Disney's writing activity constituted a trade or business alongside his teaching. Because the manuscripts were held primarily for sale to customers in the ordinary course of that trade or business, the income derived was ordinary income, not capital gains.

Facts

The petitioner, Disney, was a mathematics teacher who had written and published nine volumes of textbooks from 1923 to 1947. He entered into contracts with publishers to sell his manuscripts. Disney argued that writing was a hobby and that he sold all rights to the manuscripts on an installment basis, entitling him to capital gains treatment. A significant portion of his income, nearly half since 1935 and more than half since 1945, was derived from writing. He maintained an office at home and deducted related expenses on his tax returns.

Procedural History

The Commissioner of Internal Revenue determined that the income from Disney's textbook sales should be taxed as ordinary income rather than capital gains. Disney petitioned the Tax Court for a redetermination.

Issue(s)

Whether the manuscripts held by the petitioner were capital assets within the meaning of the Internal Revenue Code, specifically, whether they were held primarily for sale to customers in the ordinary course of his trade or business.

Holding

No, because the petitioner's writing activity constituted a trade or business alongside his teaching, and the manuscripts were held primarily for sale to customers in the ordinary course of that trade or business.

Court's Reasoning

The court reasoned that Disney's writing activity was not a mere hobby, but a regular part of his profession. The court emphasized that one may have more than

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one trade or business. Despite teaching, his writing was connected to his teaching and was not merely recreation. The court noted the significant income derived from writing, especially after 1935, and the deductions taken for maintaining a home office used for writing. These factors indicated that Disney was in the trade or business of writing textbooks. Since the manuscripts were held primarily for sale in that business, they were not capital assets, and the income was ordinary income. The Court stated, “Under all of these facts we have come to the conclusion that the petitioner had a trade or business including not only teaching but writing the books involved here. His livelihood was clearly from both.”

Practical Implications

This case illustrates that the determination of whether an activity constitutes a trade or business is highly fact-specific. Taxpayers claiming capital gains treatment for the sale of creative works must demonstrate that the creation and sale of those works are not part of their ordinary trade or business. The level of involvement, the regularity of the activity, the proportion of income derived from the activity, and the intent of the taxpayer are all relevant factors. This ruling is often cited in cases involving authors, artists, and inventors who seek capital gains treatment for the sale of their works. Later cases distinguish Disney by focusing on the infrequency or non-commercial nature of the taxpayer’s creative activities.

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