19 T.C. 93 (1952)

The mere offering of a former residence for rent or sale, even with minor rental income from ancillary parts of the property, does not automatically convert it into property used in a trade or business for purposes of deducting a loss upon its sale.

Summary

E.R. Fenimore Johnson and his wife, Janet, sought to deduct a loss on the sale of their former residence (Plot A) and an adjacent lot (Plot B). They had moved out of Plot A in 1940 and listed it for sale or rent. While the main house remained unrented, they received some rental income from the tenant house, garage and barn. Plot B, owned solely by E.R. Fenimore Johnson, was unimproved land. The Tax Court held that the loss on Plot A was not deductible because it was not converted to business use. However, the court allowed a long-term capital loss deduction for Plot B, as it was a capital asset held for speculation.

Facts

In 1921, E.R. Fenimore Johnson purchased a 15-acre property (Plot A) and constructed a large residence and outbuildings. In 1923, he transferred Plot A to his wife, Janet, and in 1937, they held it as tenants by the entirety. The Johnsons resided there until September 9, 1940, when they moved to a new home. In 1930, E.R. Fenimore Johnson purchased a separate 3.6-acre tract for speculation. In 1940, he exchanged this tract for a 15-acre plot (Plot B) adjoining Plot A to enhance the salability of Plot A. After moving out, they listed Plots A and B for sale or rent. From 1940 onward, they received rental income from the tenant house, garage, and later, the barn on Plot A, and starting in 1943, from Plot B.

Procedural History

The Commissioner of Internal Revenue disallowed the taxpayers' claimed deductions for losses on the sale of Plots A and B. The Johnsons petitioned the Tax Court for a redetermination of the deficiencies.

Issue(s)

1. Whether the petitioners sustained a deductible loss under Section 23(e) of the Internal Revenue Code on the sale of their former residence (Plot A)?

2. Whether E.R. Fenimore Johnson sustained a deductible loss under Section 23(e) on the sale of the unimproved real property (Plot B)?

Holding

1. No, because the property was not converted to a trade or business or a transaction entered into for profit.

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2. Yes, because Plot B was a capital asset, and its sale resulted in a long-term capital loss, deductible to the extent provided by Section 117 of the Internal Revenue Code.

Court’s Reasoning

Regarding Plot A, the court emphasized that merely listing property for rent or sale doesn’t constitute appropriation to a business use. While renting portions of a property can, in some cases, indicate conversion to business use (citing *Heiner v. Tindle, 276 U.S. 582*), the court found the rental income from the tenant house, garage, and barn was too trivial to show a real intention to devote the premises to income-producing property. The court distinguished *Heiner*, noting that in that case, the long-term leases put an end to the owner’s possible use of the property as a residence. Here, the Johnsons could have reoccupied the premises at any time. Regarding Plot B, the court determined that its original acquisition for speculation established it as a capital asset, a status not altered by the nominal rental income. The court stated,

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