22 T.C. 1236 (1954)

A partner's share of a partnership's long-term capital gains from non-capital assets, as defined under Section 117(j) of the Internal Revenue Code of 1939, does not offset the partner's individual long-term losses from individually owned non-capital assets when computing their distributable shares of partnership income.

Summary

The case involved a husband and wife (the Paleys) who filed joint tax returns. The husband was a member of a partnership that realized gains from the sale of non-capital assets. Simultaneously, the husband sustained losses of a similar nature from his individually owned assets. The Commissioner of Internal Revenue determined that the husband's individual losses should offset his share of the partnership's gains, effectively reducing the taxable income. The Tax Court held that the partnership's gains and the individual's losses were to be treated separately, allowing the Paleys to report the partnership gains as long-term capital gains without offsetting them by the individual losses.

Facts

Jacob Paley was a partner in a partnership that had gains from the sale of non-capital assets, which were considered long-term capital gains under Section 117(j) of the Internal Revenue Code of 1939. Jacob's share of these gains was reported as long-term capital gains on the joint tax returns with his wife. Simultaneously, Jacob individually sustained losses of a similar nature from his own non-capital assets. The Commissioner of Internal Revenue, in calculating tax deficiencies, determined that these individual losses should offset Jacob's share of the partnership's gains.

Procedural History

The Commissioner determined deficiencies in the Paleys' income tax for 1948 and 1949. The Paleys disputed this assessment, contending that the individual losses should not offset the partnership gains. The case was brought before the United States Tax Court, where the issue was the sole focus of the proceedings, as the facts were agreed upon by both parties.

Issue(s)

Whether Jacob's individual Section 117(j) losses could be offset by his share of the partnership's Section 117(j) gains in the calculation of the Paleys' taxable income.

Holding

No, because the court held that the individual's losses and the partnership gains should be treated separately for tax purposes, and the individual losses could not be used to offset the partnership gains.

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Court’s Reasoning

The Tax Court’s ruling was based on the interpretation of Section 117(j) of the Internal Revenue Code of 1939 and its prior decision in the similar case of *Jack Jordan Ammann*, 22 T.C. 1106. The court emphasized that the partnership’s Section 117(j) gains or losses should be computed at the partnership level and should not be merged with the individual partner’s Section 117(j) losses or gains. The court reasoned that the individual’s share of partnership income is calculated separately and then added to their personal income. The court cited the *Ammann* case to support its conclusion. The court explicitly stated, “…the principle is the same, the section 117(j)(2) losses or gains of the partnership do not enter into the section 117(j)(2) computation for the partner, and upon authority of that case the issue is decided for the petitioners.”

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