26 T.C. 690 (1956)

For a loss to qualify as a net operating loss under section 122 of the Internal Revenue Code, it must be attributable to a business regularly carried on by the taxpayer; isolated transactions or investments do not qualify.

Summary

The case involved Irving Rothbart, a certified public accountant, and his wife, who invested in an oil venture that turned out to be fraudulent. They sought to deduct their losses as net operating losses, carryable back to a prior year and forward to a subsequent year, under Section 122 of the 1939 Internal Revenue Code. The Tax Court determined that the couple's investments in the oil venture did not constitute a business regularly carried on by them, but rather were isolated transactions. Thus, the loss did not qualify as a net operating loss, and the claimed deductions were denied. The court emphasized the distinction between investment activities and operating a business, underscoring that for a loss to be deductible, it must be connected to a taxpayer's regular business activities.

Facts

Irving Rothbart, a CPA, was persuaded by a client to invest in an oil venture in Mississippi. Between December 1948 and January 1950, the Rothbarts invested $95,500 in interests in the well, mineral leases, and royalty interests. They relied on representations made by the promoters of the venture without conducting thorough investigations. After moving to Mississippi, they discovered that they were victims of fraud. They worked with an attorney, collected evidence, and ultimately settled with the promoter in 1951, conveying their interests back in exchange for $36,048. The Rothbarts claimed a net operating loss deduction for the difference between their investment and the settlement amount. The IRS disallowed the deduction.

Procedural History

The Rothbarts challenged the Commissioner's determination in the United States Tax Court. The Tax Court reviewed the facts and the relevant provisions of the Internal Revenue Code to determine whether the losses qualified as net operating losses under section 122. The Tax Court found that the loss was not attributable to a business regularly carried on by them.

Issue(s)

1. Whether the loss sustained by the taxpayers in 1951 was attributable to a business regularly carried on by them, such that it constituted a net operating loss under section 122 of the Internal Revenue Code.

Holding

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1. No, because the court found that the taxpayers' activities in the oil venture did not constitute a business regularly carried on by them.

Court's Reasoning

The court focused on whether the Rothbarts were engaged in a

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