29 T.C. 297 (1957)

Litigation expenses, including attorney's fees, assessed against a corporation as a result of a stockholder's derivative suit that benefited the corporation are deductible as ordinary and necessary business expenses under section 23(a)(1)(A) of the Internal Revenue Code of 1939.

Summary

The United States Tax Court addressed the issue of whether a corporation could deduct legal and accounting expenses incurred in a stockholder derivative suit as ordinary and necessary business expenses. Shoe Corporation of America (the corporation) was sued by a shareholder who challenged a plan to issue a new class of stock that would consolidate control within a family. The District Court sided with the shareholder, permanently enjoining the stock issuance and ordering the corporation to pay the shareholder's legal fees. The Tax Court held that the corporation could deduct these expenses because the suit benefited the corporation and was directly related to its business operations.

Facts

Shoe Corporation of America (petitioner) was an Ohio corporation in the business of manufacturing and selling shoes. In 1947, the company's management developed a plan to recapitalize the company's stock, which included issuing a new class of Class B common shares. The primary purpose of this plan was to allow the Schiff family, who already controlled 30% of the company, to maintain control of the corporation. Margaret K. Kahn, a shareholder, filed a derivative suit in the U.S. District Court to prevent the issuance of the Class B stock. The District Court ruled in favor of Kahn, permanently enjoining the stock issuance and ordering Shoe Corporation of America to pay Kahn's legal fees. The corporation then claimed a deduction for these fees on its tax return, which was disallowed by the IRS.

Procedural History

The case began as a shareholder's derivative suit filed in U.S. District Court against Shoe Corporation of America and its officers and directors. The District Court ruled in favor of the shareholder and ordered the corporation to pay the legal fees and expenses. The IRS disallowed the corporation's deduction for these expenses. The corporation appealed to the U.S. Tax Court, which reversed the IRS's decision.

Issue(s)

1. Whether the litigation expenses paid by the petitioner were

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