***Slater v. Commissioner, 64 T. C. 571 (1975)***

Losses on stock sales are not deductible as business expenses unless directly related to securing employment or having an ascertainable value when transferred.

## Summary

Bertram Slater, after leaving A. S. Beck Shoe Corp. , transferred rights to 4,000 shares of Beck stock to be released from a non-compete covenant, enabling new employment at Universal Container Corp. The stock, initially purchased at a bargain price, had significantly declined in value. The Tax Court held that the subsequent sale of the stock by Chase Manhattan Bank, which resulted in a loss, was not deductible as a business expense under Section 162(a) because the loss was due to the stock's decline in value, not to securing new employment. Additionally, the court found no ascertainable value in the transferred stock rights at the time of transfer.

## Facts

In 1968, Bertram Slater joined A. S. Beck Shoe Corp. (Beck) under a three-year contract that included a six-month non-compete clause. As part of his compensation, he bought 4,000 restricted shares of Beck stock at a discounted price of $35,000 when their fair market value was $55,000. In 1970, Slater left Beck and sought new employment. To secure a position at Universal Container Corp. , he negotiated a release from his non-compete clause with Beck, transferring certain rights to his Beck stock as payment. By then, the stock's value had dropped to $2. 75 per share from a high of $40 in 1969. Chase Manhattan Bank, holding the stock as collateral for a loan to Slater, sold it in December 1970 for $1. 37 per share. Slater attempted to deduct the resulting loss as a business expense.

## Procedural History

The Commissioner of Internal Revenue disallowed the deduction and issued a deficiency notice for the years 1967 through 1970. Slater and his wife petitioned the U. S. Tax Court, which heard the case and ruled in favor of the Commissioner, denying the deduction.

## Issue(s)

1. Whether the loss on the sale of the Beck stock was a deductible business expense under Section 162(a) of the Internal Revenue Code as an expense incurred in seeking new employment.
2. Whether the loss on the stock sale should be treated as an ordinary loss under the Arrowsmith doctrine due to its integral relation to the bargain purchase of the stock.
3. Whether the transfer of stock rights to Beck in exchange for release from the non-compete covenant constituted a deductible business expense.

## Holding

 

1. No, because the loss resulted from the decline in the stock's value, not from efforts to secure new employment.
2. No, because the sale and the loss were not integrally related to the bargain purchase; they were due to the fortunes of the company.
3. No, because the petitioners failed to prove that the transferred stock rights had an ascertainable market value at the time of transfer.

**Court's Reasoning**

The court applied Section 162(a) to determine if the loss could be considered a business expense. It reasoned that the loss was due to the decline in Beck's stock value, which was unrelated to Slater's efforts to secure new employment. The court distinguished this case from Cremona and Primuth, where expenses were directly related to securing employment. On the Arrowsmith doctrine, the court found no integral relationship between the bargain purchase and the subsequent loss, as the loss was due to external market forces. Finally, the court assessed the value of the transferred stock rights at the time of transfer, concluding that there was no realistic likelihood of the stock recovering to a value that would benefit Beck. The court rejected Slater's valuation testimony due to insufficient evidence of the stock's potential to rise above the loan amount. The court's decision was guided by the principle that deductions must be supported by clear evidence of a business purpose and an ascertainable value.

**Practical Implications**

This decision clarifies that losses on stock sales cannot be deducted as business expenses unless they are directly linked to securing new employment or if the transferred rights have a provable market value. Legal practitioners should advise clients to carefully document any expenses related to employment transitions and to substantiate the value of any assets transferred in such contexts. The ruling affects how similar cases involving stock compensation and non-compete agreements are analyzed, emphasizing the need for a direct causal link between the expense and the business purpose. Businesses should consider these tax implications when structuring employee compensation packages involving stock options or shares. Subsequent cases, such as George Eisler and John E. Turco, have followed this precedent, reinforcing the need for a clear connection between the transaction and the employment-related expense.

 