T.C. Memo. 1981-470

A trust established for business purposes, exhibiting corporate characteristics such as continuity of life, centralized management, and limited liability, can be classified as an association taxable as a corporation, even if it has a single beneficiary.

Summary

John B. Hynes Jr. created the Wood Song Village Trust to develop and sell real estate. Hynes, the sole beneficiary, claimed trust losses on his personal income tax returns. The IRS determined the trust was an association taxable as a corporation and disallowed Hynes's deductions, along with other business expense deductions claimed by Hynes. The Tax Court upheld the IRS, finding the trust exhibited enough corporate characteristics to be taxed as a corporation, despite Hynes being the sole beneficiary. The court also disallowed most of Hynes's claimed business expense deductions for lack of substantiation or because they were deemed personal expenses.

Facts

John B. Hynes Jr., a television news writer and announcer, formed the Wood Song Village Trust. Hynes transferred rights to purchase real estate to the trust and was the sole beneficiary. The trust was established to develop and sell real estate for profit. The trust agreement included provisions for continuity of life, centralized management by trustees, and limited liability for trustees and beneficiaries. Hynes personally guaranteed a mortgage for the trust. The trust engaged in real estate development and sales but faced foreclosure. Hynes attempted to deduct trust losses, foreclosure-related losses, interest, and real estate taxes on his personal income tax returns, along with various business expenses related to his TV job.

Procedural History

The Commissioner of the IRS determined deficiencies in John B. Hynes Jr.'s and Marie T. Hynes's federal income taxes for 1973-1976 and in the Wood Song Village Trust's federal income taxes for 1975. The taxpayers petitioned the Tax Court for review of the Commissioner's determinations.

Issue(s)

1. Whether the Wood Song Village Trust is an association taxable as a corporation.
2. Whether Hynes is entitled to a business loss deduction from the trust's mortgage foreclosure.
3. Whether Hynes can deduct interest and real estate taxes owed by the trust.
4. Whether Hynes can deduct various personal expenses (wardrobe, grooming, hotels, meals, auto) as business expenses.
5. Whether Hynes can deduct home office expenses under section 280A.

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6. Whether the Wood Song Trust failed to report income from a property sale.

Holding

1. Yes, because the trust possessed more corporate characteristics than noncorporate characteristics, despite having a single beneficiary.
2. No, because the loss from the guarantee is a bad debt issue, not a business loss, and Hynes had not yet incurred a loss by paying on the guarantee.
3. No, because interest and taxes were the trust's obligations, not Hynes's, and he had not yet paid them.
4. No, for most expenses. Wardrobe, grooming, and hotel expenses were deemed personal. Meal and auto expenses lacked adequate substantiation.
5. No, because the home office was not Hynes's principal place of business and not for his employer's convenience.
6. No, the trust failed to prove the Commissioner's determination of unreported income was incorrect.

Court's Reasoning

The court determined the Wood Song Trust was taxable as a corporation based on Morrissey v. Commissioner, which established criteria for corporate resemblance: associates, business objective, continuity of life, centralized management, limited liability, and transferability of interests. The court found the trust exhibited continuity of life through its defined duration and provisions for trustee succession. Centralized management existed because trustees had broad powers. Limited liability was present due to trust agreement clauses and Massachusetts law allowing trustees and beneficiaries to limit liability. While transferability was modified, the trust still possessed more corporate than non-corporate characteristics. Regarding deductions, the court applied Putnam v. Commissioner, stating guarantor losses are bad debts deductible when the guarantor pays. Hynes hadn't paid, so no deduction was allowed. Interest and tax deductions were denied as they were the trust's obligations (Rushing v. Commissioner). Business expense deductions were largely disallowed as wardrobe, grooming, and hotel costs were personal (Commissioner v. Flowers; Drake v. Commissioner), and meal and auto expenses lacked substantiation under section 274(d). Home office deductions failed under section 280A because Hynes's principal place of business was the TV station (Curphey v. Commissioner). The court emphasized that personal expenses are non-deductible under section 262 and business expenses must be ordinary and necessary under section 162. The court quoted Morrissey v. Commissioner: "The inclusion of associations with corporations implies resemblance; but it is resemblance and not identity."

Practical Implications

This case highlights that the classification of a trust for tax purposes depends on its operational characteristics, not just its legal form or the number of beneficiaries. Even a single-beneficiary trust can be taxed as a corporation if it operates a business

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and possesses corporate traits. Practitioners structuring business trusts must carefully consider these characteristics to avoid corporate tax treatment if pass-through taxation is desired. The case also reinforces the strict substantiation requirements for business expenses, particularly under section 274(d), and the distinction between personal and business expenses, especially for employees claiming home office or wardrobe deductions. It serves as a reminder that personal guarantees of business debts do not create deductible losses until payment is made by the guarantor.

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