Estate of Platt W. Davis, Deceased, Janet H. Davis, Executrix, and Janet H. Davis, Surviving Spouse, Petitioners v. Commissioner of Internal Revenue, Respondent, 79 T. C. 503 (1982)

Legal fees incurred to establish a right to an estate or to protect personal assets from estate litigation are not deductible under IRC section 212(2).

Summary

Janet H. Davis, a cousin of Howard R. Hughes, Jr. , sought to deduct legal fees incurred to establish her claim to Hughes' estate and to protect her own assets from potential estate litigation. The U. S. Tax Court held that these fees were not deductible under IRC section 212(2) because they were not for the management, conservation, or maintenance of income-producing property. Instead, they were capital expenditures for establishing a right to property or personal expenses for protecting personal assets, neither of which are deductible.

Facts

Janet H. Davis was adjudged a legal heir of Howard R. Hughes, Jr. , but numerous uncertainties remained regarding her right to share in his estate, including his domicile at death, applicable state law on intestacy, and the validity of multiple wills. Davis paid legal fees to various law firms to work out a settlement agreement among Hughes' heirs and to prosecute claims against purported wills. She also paid legal fees to explore creating a revocable trust to protect her and her husband's assets from entanglement with the Hughes estate litigation.

Procedural History

Davis and her husband claimed a deduction for these legal fees on their 1977 joint federal income tax return. The Commissioner of Internal Revenue disallowed the deduction, leading to a deficiency determination. Davis petitioned the U. S. Tax Court, which upheld the Commissioner's determination and ruled in favor of the respondent.

Issue(s)

1. Whether legal fees incurred to establish a right to share in the Hughes estate are deductible under IRC section 212(2)?
2. Whether legal fees incurred to protect personal assets from potential Hughes estate litigation are deductible under IRC section 212(2)?

Holding

1. No, because these fees were capital expenditures for the acquisition of property, not for its management, conservation, or maintenance.
2. No, because these fees were either capital expenditures or personal expenses,

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depending on the nature of the anticipated claims, and thus not deductible under IRC section 212(2).

Court's Reasoning

The court applied the "origin and character" test from *United States v. Gilmore* and *Woodward v. Commissioner* to determine the deductibility of the legal fees. For the fees related to the Hughes estate, the court reasoned that Davis did not "hold" any part of the estate at the time the fees were incurred; she was merely attempting to establish a right to it. Such fees are capital in nature and must be added to the basis of any property ultimately acquired from the estate.

For the fees related to the potential trust, the court found that the origin of the claim Davis sought to protect against was her connection to the Hughes estate, not the management of her existing income-producing property. Therefore, these fees were either capital expenditures (if the claim arose from her efforts to establish a right to the estate) or personal expenses (if the claim stemmed from her family relationship to Hughes). The court emphasized that the nature of the measures taken to avoid a claim (e. g. , creating a trust) does not change the nondeductible nature of the underlying claim.

The court also cited relevant regulations and case law, including *Grabien v. Commissioner* and *United States v. Patrick*, to support its conclusions. It rejected Davis' argument that the primary purpose of the expenditures (i. e. , to protect income-producing property) should control their deductibility, adhering instead to the "origin and character" test.

Practical Implications

This decision clarifies that legal fees incurred to establish a right to an estate or to protect personal assets from estate litigation are not deductible under IRC section 212(2). Taxpayers in similar situations must capitalize such fees as part of their basis in any property ultimately acquired or treat them as nondeductible personal expenses. This ruling may affect estate planning and tax strategies, particularly for heirs involved in complex estate litigation.

Attorneys advising clients on estate matters should be aware that legal fees related to establishing or defending a right to an estate are not currently deductible. Instead, clients may be able to recover these fees through a capital loss deduction if they ultimately receive nothing from the estate. Similarly, fees incurred to protect personal assets from estate-related claims are likely nondeductible, regardless of the method used to achieve such protection (e. g. , trusts, asset transfers).

This case has been cited in subsequent decisions involving the deductibility of legal fees, such as *Epp v. Commissioner*, reinforcing the principle that the origin and character of a claim, rather than its purpose, determine the deductibility of related

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expenses.

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