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## Federal Taxation -- Deductibility of Attorney's Fees in Contesting Gift Tax Deficiency Determination

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manner of excuses to remove a case from the docket. Judges deserve sympathy for the excessive amount of work to which they have been subjected, however, we cannot bring ourselves to believe that allowing a judge to be persuaded of his court's unsuitability less by the circumstances of the case than by his own overcrowded calendar would be a suitable remedy or a correct solution.<sup>34</sup> Under the revised Judicial Code<sup>35</sup> it would seem to be the intent of the Congress to limit the remedy to transfer only, there being no other indication in the Code of allowing dismissal of action, or refusal to exercise jurisdiction where other requirements therefor are met. It would seem to be a rather serious matter for a federal court to refuse jurisdiction to a litigant with an unadjudicated cause which is definitely within the statutory authority of the court. The right, or privilege, to litigate is not something which the court may grant or withhold simply for the sake of its convenience.

### FEDERAL TAXATION—DEDUCTIBILITY OF ATTORNEY'S FEES IN CONTESTING GIFT TAX DEFICIENCY DETERMINATION

Petitioner made gifts of stock. Commissioner of Internal Revenue notified him of a deficiency in his gift tax return. A redetermination of liability was filed and an out of court settlement was reached. In filing his income tax return petitioner deducted attorney fees expended in defending said assessment. Commissioner refused deduction. On appeal, *held*, that said deduction was allowable under § 23(a)(2) of the Internal Revenue Code<sup>1</sup> as constituting expenses ". . . for the management, *conservation*, or maintenance of property held for the production of income."<sup>2</sup> *Lykes v. Commissioner*, 84 F. Supp. 537 (S.D. Fla. 1949).

Prior to 1944 one could deduct from gross income only those expenses incurred in the operation of a trade or business.<sup>3</sup> Since that time, Congress

34. *Forum Non Conveniens, a New Federal Doctrine*, 56 YALE L.J. 1234, 1247 (1947). See Justice Clark's dissent in *Hammett v. Warner Bros.*, 176 F.2d 145, 152 (2d Cir. 1949).

35. 28 U.S.C. § 1404(a) (1948). "For convenience of parties and witnesses, in the interest of justice, a district court may transfer any civil action to any other district or division where it might have been brought." The Reviser in his note on this section states that it was drafted in accordance with the doctrine of *forum non conveniens*, permitting transfer to a more convenient forum, even though the venue is proper and cites *Baltimore & Ohio R.R. v. Kepner*, 314 U.S. 44 (1941) as an example of the need of such a provision.

1. 56 STAT. 819, 26 U.S.C. § 23(a)(2) (1942). "Deductions from gross income. In computing net income there shall be allowed as deductions: . . . (2) non-trade or non-business expenses. In the case of an individual, all the ordinary and necessary expenses paid or incurred during the taxable year for the production or collection of income, or for the management, conservation, or maintenance of property held for the production of income."

2. The court found Treasury Regulation 111 § 29.23(a)-15(b) as amended by T.D. 5513 in conflict with the Internal Revenue Code and therefore invalid.

3. *Williams v. Burnett*, 59 F.2d 357 (D.C. Cir. 1932) (expenses incurred in prosecution of claim for compensation against city property condemned by city were not deduct-

has liberalized the allowances for such expenses with the enactment of § 23(a)(2).<sup>4</sup> Interpreting this statute the court held that attorney's fees resulting from litigation involving income-producing property were deductible only when directly connected with or proximately resulting from taxpayer's business.<sup>5</sup> However, the holding in *Bingham v. Commissioner*<sup>6</sup> reversed this trend toward strict application and liberally construed the section so as to widen the scope of allowable deductions thereunder. In the *Bingham* case, fees paid an attorney by trustees for attacking an income tax deficiency judgment were deductible expenses incurred in the management of property, even though not a trade or business expense.

Cases involving the deductibility of attorney's fees uniformly followed the doctrine of the *Bingham* case<sup>7</sup> until the holding in *Cobb v. Commissioner*.<sup>8</sup> In the latter case, it was held that attorney's fees paid by petitioner for advice and services rendered in a controversy concerning the amount of petitioner's liability for gift taxes were not deductible. The plaintiff contended that expenses incurred in defending a tax assessment were related to the conservation of income-producing property because judgment against him would result in a lien upon said property. The court rejected this contention holding it was not sufficiently related to *conservation* to be a deductible expense. The *Bingham* case was distinguished<sup>9</sup> on the ground that under the terms of the trust instrument involved, the trustees had a legal obligation to distribute the property to the heirs, and consequently, the expense was related to the management of that property. But in the *Cobb* case, the court held that since the transfer was voluntary it was not related to the *conservation* of property.

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ible from income tax); *Hall v. Helvering*, 70 F.2d 284 (D.C. Cir. 1934) (fees paid by decedent's devisees to attorney for services in collecting estate tax were not deductible); *Crawley v. Commissioner*, 89 F.2d 715 (6th Cir. 1937) (expenditure made for purpose of acquiring property or gaining control of business—not deductible).

4. See *Higgins v. Commissioner*, 143 F.2d 654 (1st Cir. 1944), *cert. denied*, 325 U.S. 868 (1944) (reference to taxes on property held for production of income were deductible); *Heller v. Commissioner*, 147 F.2d 376 (9th Cir. 1944) (court held deductible attorney's fees paid in litigating the cash value of certain shares of stock); *Commack v. Commissioner*, 5 T.C. 467 (1945) (Plaintiff bought stock to produce income. Stock became worthless and Plaintiff deducted cost from income for that year. Legal fees incurred in that tax litigation were deductible); *Tyler v. Commissioner*, 6 T.C. 135 (1946) [attorney's fee paid in connection with a will contest which determined amount of annual income payable to Plaintiff as a life tenant was held deductible under § 23 (a) (2)].

5. *Spear v. Gane*, 49 F. Supp. (E.D.N.Y. 1943) (allowances for services of guardians, commissions paid, attorney's fees, and court fees were deductible); *Edmunds v. United States*, 71 F. Supp. 29 (E.D. Mo. 1947) (attorney fees paid by taxpayer for recovery of principle sum overpaid on estate of taxpayer's dead mother were not deductible); *cf. Helvering v. Stormfultz*, 142 F.2d 982 (8th Cir. 1944) (ward sued guardians for recovery of embezzled funds. Attorney's fees were deductible for that portion of legal expenses allocable to recovery of interest, but not to that part pertaining to recovery of capital).

6. 325 U.S. 365 (1945).

7. *E.g., Stoddard v. Commissioner*, 152 F.2d 445 (2d Cir. 1945); *Williams v. McGowan*, 152 F.2d 570 (2d Cir. 1945); *Dunitz v. Commissioner*, 167 F.2d 223 (6th Cir. 1948).

8. 173 F.2d 711 (6th Cir. 1949).

9. 325 U.S. 365, 367 (1945).

The instant case refutes the distinction between the *Bingham* and *Cobb* cases, stating that the former had correctly stated the law when it held that expenses must be proximately related to the *conservation* of property. It holds that if a lien upon any of petitioner's income-producing property would result from a tax assessment, attorney's fees paid out in defending such a claim are proximately related to the *conservation* of income-producing property and, consequently, are deductible under § 23(a)(2) of the Internal Revenue Code.

To logically follow this reasoning would be to conclude that the expense of defending any type of litigation, for example, a tort action, would be deductible because a judgment rendered against taxpayer would become a lien on his income-producing property.<sup>10</sup> However, the law is still clear that where the transaction which gave rise to the tax assessment was not proximately related to the production or collection of income, any expense arising from such litigation would not be deductible.<sup>11</sup> The *Lykes* case does not change this rule. It merely broadens the scope of expenses considered proximately related to include attorney's fees paid for defending a tax assessment where the assessment might result in a lien on any of petitioner's income-producing property, even though such property was not the subject of the transaction which gave rise to the original tax assessment.

#### INSURANCE—SUBROGATION—REQUIREMENT TO DEFEND—ATTORNEY'S FEES IN DECLARATORY JUDGMENTS

Plaintiff, insurance company, brought suit for a declaratory judgment against its insured under a public liability policy to determine whether it was required to defend an action against the insured by a third party. Judgment was rendered for the insured and attorney's fees were adjudged against insurer under a Florida statute<sup>1</sup> which provides that attorney's fees be assessed against insurer where insured successfully prosecutes suit against the company. On appeal, *held*, that attorney's fees were properly awarded insured since the statute is applicable to situations where suit is brought by insurer as well as insured, *Phoenix Indemnity Co. v. Anderson's Groves, Inc.*, 176 F.2d 246 (5th Cir. 1949).

Where attorney's fees are permitted by statute, cases arising thereunder

10. See *John W. Willmot*, 2 T.C. 321, 326 (1943).

11. *Kohnstamm v. Pedrick*, 66 F. Supp. 410 (S.D.N.Y. 1946); *Joseph v. Commissioner*, 8 T.C. 583 (1947).

1. FLA. STAT. § 625.08 (1941). "Upon the rendition of a judgment or decree by any of the courts of this state against any insurer in favor of the beneficiary under any policy or contract of insurance executed by such insurer, there shall be adjudged or decreed against such insurer and in favor of the beneficiary named in said policy or contract of insurance, a reasonable sum as fees or compensation for his attorneys or solicitors prosecuting the suit in which recovery is had."