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effect of the provisions can be summed up by saying that they all attempt to put an end to flagrant abuse situations that had arisen when the rate structures and jurisdictional concepts of foreign countries for taxing income did not meet, or overlapped the rate structures and jurisdictional concepts of the United States for taxing income. Of course, taxpayers may not be unanimous in the feeling that all situations covered by the 1962 Act constituted abuses.

Time limitations and the complexity of many of the foreign provisions make it inadvisable to discuss, or even mention, the several provisions.

Other Provisions

The Revenue Act of 1962 also contains several other provisions of lesser importance or of more limited application. The scope of this paper precludes reference to these provisions.

THE DEDUCTIBILITY OF EDUCATIONAL EXPENSES UNDER §162(a) OF THE INTERNAL REVENUE CODE

JOHN J. HARRINGTON

The Internal Revenue Code and the Commissioner's Regulations[1] allow as a deduction from Gross Income[2] educational expenses incurred by a taxpayer, within certain specific limits. The authority for such a deduction being a section of the Code dealing with deductions for the ordinary and necessary expenses of a trade or business, the case law and the Regulations relative to the deductibility of educational expenses have followed closely the developing concepts of "ordinary and necessary" business expenses.

Code § 162(a) provides that "there shall be allowed as a deduction all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business . . ." The Regulations, in general, develop the theory

[1] INT. REV. CODE of 1954, § 162(a); Treas. Reg. § 1.162-5 (1958).

[2] INT. REV. CODE of 1954, § 62(1); Rev. Rul. 97, 1960-1 CUM. BULL. 69, 75.

that in order for an educational expense to be deductible, it must either be (1) incurred to maintain or improve skills required by the taxpayer in his employment or other trade or business, or (2) be an express requirement of the taxpayer's employer or applicable law or regulations, imposed as a condition to the retention of the taxpayer's salary, status or employment.[3] This Regulation was first adopted in 1958[4] and was made retroactive to affect all 1954 Code years.[5]

The detail of the current Regulations is in wide contrast to those prevailing under the 1939 Code, which provided only that "expenses of taking special courses or training" or expenses incurred " . . . in placing oneself in a position to begin rendering personal services for compensation" are not deductible.[6] Prior to the 1954 Code and the promulgation of both the proposed and final Regulations thereunder, a taxpayer who was in doubt as to the deductibility of his educational expenses had to refer mainly to court decisions on the point.

An initial philosophical stumbling-block for those seeking the deduction of educational expenses was set up by Justice Cardozo in oft-quoted dicta from *Welch* v. *Helvering*.[7] The money spent in acquiring learning, declared Justice Cardozo, is not an ordinary expense of business, but is more in the nature of a non-depreciable capital asset. This position was adhered to without exception until 1950.[8]

A precedent-breaking decision was finally handed down in 1950 by the Fourth Circuit Court of Appeals in the *Hill* case.[9] The factual situation involved a Virginia high school teacher who attended a summer session at Columbia University, and sought deductibility of $250 of her expenses under section 162. The Tax Court had denied such deductibility[10] on the ground

[3] Treas. Reg. 1.162-5(a)(1) and (2) (1958).

[4] T. D. 6291, 1958-1 CUM. BULL. 63.

[5] T.I.R. 76, April 11, 1958, 5CCH 1958 STAND. FED. TAX REP. ¶6445.

[6] Treas. Reg. 118, § 39.23(a)-15 (f)(1939).

[7] 290 U. S. 111 (1933).

[8] 58 COL. L. REV. 1097 (1958).

[9] Hill v. Commissioner, 181 F. 2d 906 (4th Cir. 1950).

[10] Nora Payne Hill, 13 T. C. 291 (1949).

that the school teacher had had an option under state law of either reading and being examined on five books, or procuring credits in summer school, under the State Department of Education Regulations, and that there was no showing that the method pursued by the teacher was ordinarily followed by others in similar circumstances. Although attending summer school was an alternative requirement of the taxpayer's employer, it was not the one necessary method of retaining her position and there was no showing that it was ordinary. In reversing, the Court of Appeals held that it would be unreasonable to require the taxpayer to give a statistical showing that is was more usual for other teachers to elect to attend summer school rather than to read five approved books. Instead, the Fourth Circuit promulgated a broader test. "If the particular course adopted by the taxpayer is a response that a reasonable person would normally and naturally make under the specific circumstances,"[11] it would be a sufficient basis for permitting deductibility. Moreover, the Circuit Court found, from all the circumstances, that the taxpayer attended the summer session in order to maintain her present position and not in order to attain a new one. Accordingly, the court had little trouble in holding an ancient Service pronouncement[12] inapplicable to such a situation. Where the ruling cited by the Tax Court had categorically declared that "the expenses incurred by school teachers in attending summer school are in the nature of personal expenses incurred in advancing their education and are not deductible,"[13] the Circuit Court in *Hill* tacitly rewrote the ruling to deny deductibility only *when* the summer school expense *was* of a personal nature. By placing its emphasis on the state requirements relative to the retention of her teaching position by the taxpayer, the appellate court easily found the summer school expense to be of a nonpersonal nature.

The Fourth Circuit cautioned, however, that it was by no means holding that all summer school expenses would be permitted deductibility by all taxpayers; the test of ordinary and necessary would still have to be met. A case which is factually

[11] Hill v. Commissioner, *supra* note 9 at 908.

[12] O.D. 892, 4 CUM. BULL. 209 (1921).

[13] *Ibid.*

distinguishable from *Hill* was not long in coming. An industrial engineer took courses in Administrative Engineering and sought a deduction for his tuition and carfare as an ordinary and necessary educational expense.[14] The Tax Court found, on the basis of the taxpayer's testimony that he received greater earnings as a result of his studies, that the expense was incurred either to improve the taxpayer's professional status or his personal educational attainment level, and were non-deductible even under the *Hill* ruling, since there was no necessity for the taxpayer to incur the expense in order to keep his job. Similar results were attained in other cases in which a taxpayer with a claimed educational expense deduction sought to widen the scope of *Hill*. In *Cardozo*,[15] a college professor voluntarily took a trip to Europe for the purpose of study and research. In denying the deduction for the expenses of the trip, the Tax Court pointed out that there was no requirement of the college that the professor even conduct research in order to maintain his position, although this had a great deal of influence on his subsequent promotion. The *Cardozo* case has been criticized for its failure to look beyond the express written requirements of the university to the frequently unwritten policy of higher educational institutions that the retention of professors, as well as promotions, hinge largely on their published research, and hence, the ordinary and necessary requirements really are present.[16] This criticism, however, seems more properly directed at the refusal of the Tax Court to take judicial notice of the employment policies of universities, in the absence of any showing by the taxpayer as to such policies, than against the legal principle followed in *Cardozo*. A similar result was obtained where a college professor sough to deduct certain expenses connected with his doctor's dissertation, but admitted that this activity was not required of him in order to hold his present position.[17]

The Commissioner expressed his approval of the *Hill* case and those which followed its doctrine by modifying his thirty-

[14] Knut F. Larson, 15 T.C. 956 (1950).

[15] Manoel Cardozo, 17 T.C. 3 (1951).

[16] H. Helmut Loring, *Some Tax Problems of Students and Scholars*, 45 CAL. L. REV. 153, 157 (1957).

[17] Richard Henry Lampkin, 3 P-H 1952 FED. TAX SERV. ¶52,173.

year-old ruling that all summer school expenses were personal,[18] to permit deductions by teachers for educational expenses where they were for the purpose of maintaining an existing position, rather than for obtaining a higher position or qualifying for a permanent status.[19] The initial breach in the wall of non-deductibility having been opened by the decision in *Hill*, others soon appeared in related areas. Again it was a Circuit Court which led the offensive. The case of *Coughlin* v. *Commissioner*[20] was decided by the Second Circuit in 1953 and permitted a deduction as an ordinary and necessary business expense the expenditures made for tuition, travel, board and lodging by a practicing attorney who attended the New York University Institute on Federal Taxation. The Tax Court had disallowed such a deduction on the ground that the attorney was pursuing "an educational and personal" object.[21] The Second Circuit, on the other hand, found that although the knowledge gained by the attorney at the Institute may have "incidentally increased his fund of learning in general, and, in that sense, the cost of acquiring it may have been a personal expense . . . the immediate over-all professional need to incur the expenses in order to perform his work with due regard to the current status of the law so overshadows the personal aspect that it is the decisive factor."[22] In short, the Circuit Court found that it was both ordinary and necessary for a tax lawyer to keep abreast of current developments in the tax field in order to *maintain* his professional position.

With the adoption of the 1954 Code, "proposed" Regulations were promulgated by the Commissioner. These were much less liberal than the present 1962 Regulations. Prior to 1958, the Regulations permitted an educational expense deduction if "the degree of business necessity . . . clearly outweighed any personal aspects of the expenditure" *in addition* to being "ordinary and necessary".[23] The pre-1958 Regulation

[18] O.D. 892, 4 CUM. BULL. 209 (1921).

[19] I.T. 4044, 1951-1 CUM. BULL. 16.

[20] Coughlin v. Commissioner, 203 F. 2d 307 (2d Cir. 1953).

[21] George C. Coughlin, 18 T.C. 528 (1952).

[22] Coughlin v. Commissioner, *supra* note 20, at 309.

[23] Proposed Treas. Reg. 1.162-5(b)(1), 21 Fed. Reg. 5091 (1956).

listed situations in which no deduction would be allowed in any event:

> Expenditures for education which are made primarily for the purpose of, or which have the result of, obtaining a position for the taxpayer; qualifying him to enter an employment or otherwise become established in a trade or business or specialty therein; establishing or enhancing substantially his reputation in his trade or business; substantially advancing him in earning capacity, salary, status or position; or primarily fulfilling the general cultural aspirations or other personal purposes of the taxpayer are personal expenditures and are not deductible.[24]

Although most of this philosophy has found its way into the post-1958 Regulations, it is no longer necessary for the "degree of business necessity to *clearly* outweigh any personal aspects" under the facts of a particular situation; it is now sufficient to show only that the expense was incurred *primarily* as an ordinary and necessary business expense, even though there was a substantial personal benefit to the taxpayer as well. A "dual purpose" of personal and business benefits no longer disqualifies a deduction per se, so long as the primary purpose remains that of an ordinary and necessary business expense. It has been stated by the Tax Court[25] that the principal effect of the liberalized Regulations was to remove the distinction previously made between self-employed individuals, whose educational expenses were generally considered to be personal in nature by the Service and non-deductible, and employees, for whom necessary business reasons for indulging in the educational activity were more easily found.

The current Regulations state specifically that, as a general rule, "a taxpayer's expenditures for travel (including travel while on sabbatical leave) as a form of education shall be considered as primarily personal in nature and therefore not deductible."[26] In court assaults on this position, the taxpayer has generally been unsuccessful. Thus, in *Seibold*,[27] (decided under

[24] Proposed Treas. Reg. 1.162-5(a)(2), 21 Fed. Reg. 5091 (1956).

[25] Cosimo A. Carlucci, 37 T.C. 695 (1962).

[26] Treas. Reg. 1.162-5(c) (1958).

[27] 31 T.C. 1017 (1959).

the 1939 Code but after the promulgation of the "final" Regulations under the 1954 Code) the taxpayer was a music teacher in a public school system who had to secure certain credits in order to validate his teaching certificate to maintain and preserve his present position. He was permitted an election between going to school to obtain the credits, or taking an educational sight-seeing trip of Europe for which he would be granted credit. He elected to follow the latter course. In denying the taxpayer a deduction for the cost of the European jaunt, the Tax Court drew the line at any attempted extension of the *Hill* case[28] which would classify an expense such as this as "ordinary and necessary." The Court agreed that it was necessary for the teacher to secure his credits, but did not think an European sight-seeing tour was the ordinary method of doing so.

A similar result was reached in the later case of *Thomas P. Dennehy*,[29] which involved another summer tour of Europe, this time by a mathematics instructor at a university. In this case, the court refused even to find the tour necessary, let alone ordinary, even though the taxpayer would have been subjected to some type of "sanctions" by the university if he failed to make the trip. The "sanctions" were in the form of a denial of promotion and a pay increase, and hence, there was no compulsion on him to make the trip in order to maintain a presently-held position.

On the other hand, the Tax Court has allowed the expenses of an European trip for educational purposes to be deducted as an ordinary and necessary business expense where the taxpayer was an art and geography teacher in an elementary school.[30] Although the taxpayer visited "common tourist attractions," the Court distinguished the *Siebold* case[31] by finding here a "definite and logical relationship to the teaching of geography" and art.[32]

[28] Hill v. Commissioner, 181 F. 2d 906 (4th Cir. 1950).

[29] 30 P-H Tax Ct. Mem. ¶61,151 (1961).

[30] Evelyn L. Sanders, 29 P-H Tax Ct. Mem. ¶60,061 (1960).

[31] 31 T.C. 1017 (1959)

[32] *Supra* note 30.

A late case[33] presents a troublesome borderline problem in this area. A college professor sought deductibility of his expenses in making a trip to England in order to conduct research on a book he was writing. The majority opinion of the Tax Court, six judges dissenting, disallowed a deduction on a finding that the professor was not required by the college to undertake the research project. Although the majority agreed that the college "expressed an interest in research" and "encouraged it," great stress was laid on the fact that the professor had permanent tenure and hence, his present position was in no danger if he failed to conduct the research. In a vigorous dissent, however, the minority argues that the majority proceeded on a fundamental misunderstanding of the scope of the applicable statute. It is insisted strongly by the dissent that it is quite beside the point whether or not the professor had achieved permanent tenure. The dissenters found the trip to be both ordinary and necessary in spite of the precedent of *Cardozo*, ordinary because of a tradition and commonly recognized expectation of the college "that members of its faculty engage in research and writing in their respective areas of academic interest;"[34] necessary because of indirect pressure by fellow faculty members and administration officials to produce research, although this was not specifically called for in the contract of employment. The case is on appeal as of January 15, 1963, to the Ninth Circuit and whether a further extension of "ordinary and necessary" concepts in the field of educational expense deduction will be forthcoming is of course unpredictable.

Not all the attempts for an educational expense deduction are made by those engaged in the profession of teaching. Especially since the enactment of the liberalized Regulations in 1958, persons engaged in other professions, generally on a self-employment basis, have attempted to avail themselves of this means of cutting their tax bills. Attorneys form a typical professional group for whom such deductions may be permitted. A typical factual situation is that of the *Bistline* case,[35] wherein the taxpayer was an attorney in Idaho who travelled to New

[33] Harold H. Davis, 38 P-H Tax Ct. Rep. ¶38.20 (1962).

[34] *Id.* at 156.

[35] Bistline v. United States, 145 F. Supp. 802 (D. Idaho, 1956).

York for a two-week course in Federal Taxation at the Practicing Law Institute. A District Court, without much discussion of the point, permitted him to deduct his tuition, cost of books, hotel and travel expenses as a business expense. Presumably the Court felt that the tax course enrollment was for the purpose of allowing the attorney to maintain his position in his chosen field. A contrary result was reached and a deduction denied by the Tax Court where the facts showed that the purpose of the attorney in attending New York University tax courses was to enable him to secure a position in a legal partnership prospectively being formed, in which he was to handle the tax work.[36] The Tax Court followed the Regulations in denying a deduction for an expense incurred in obtaining an education for the primary purpose of obtaining a new position.

A deduction is also disallowed by the courts, as well as the Regulations, where the education results in a new skill, one not required of the taxpayer as a condition to the retention of his salary, status or employment. Thus, the costs of a National Labor Relations Board field examiner in pursuing law school courses were non-deductible where he did no legal work for the Board and legal training was not a pre-requisite to the retention of his position.[37] Such an expense is of an inherently personal nature. A similar result was reached in the case of a research chemist who attended law school in order to secure a new position as a patent chemist, rather than merely maintaining his current status.[38]

Psychiatrists were denied educational deductions in two recent cases where the court found the expenses had been essentially incurred to permit the taxpayers to obtain new positions. In *Namrow*,[39] the specific reason two psychiatrists took psychoanalytic courses was to attain the minimum requirements needed in order to practice psychoanalysis. The Court held that psychoanalysis was a new and different skill from psychiatry as a matter of fact, in an opinion devoted mainly to definitions of these terms. In *Gilmore*,[40] the taxpayer sought to distinguish her situation from that in the

[36] Joseph T. Booth, 35 T.C. 1144 (1961).

[37] Louis Aronin, 30 P-H Tax Ct. Mem. ¶61,180 (1961).

[38] Sandt v. Commissioner, 303 F.2d 111 (3rd Cir., 1962).

[39] Namrow v. Commissioner, 288 F.2d 648 (4th Cir., 1961).

[40] 38 P-H Tax Ct. Rep. ¶38.76 (1962).

Namrow case by claiming that since she was already well established in her profession, rather than close to the inception of her career as the psychiatrists in *Namrow* had been, her primary purpose in taking psychoanalysis courses must have been to improve her skill as a teacher and practitioner of psychiatry. The Court concluded that there was no such distinction and that psychiatry and psychoanalysis are essentially different, although not totally unrelated skills. A subsidiary contention that her employer encouraged her study, whereas in *Namrow* the psychiatrists acted on their own, was also rejected as immaterial by the Tax Court, since encouragement is a far cry from a requirement.

A novel question presented for the determination of the courts in 1961 was whether a teacher's expenditures for the acquisition of college credits which admittedly permitted him to continue teaching were disallowable because the credits were also applicable to the awarding of a law degree to the taxpayer.[41] A District Court concluded that a dual purpose on the part of a taxpayer did not preclude the existence of a primary purpose of the taxpayer if at the time he took the courses his purpose was the retention of his job as a school teacher.

The Tax Court has also recently allowed the deduction, as an ordinary and necessary educational expense, of the cost of college courses taken by a Certified Public Accountant and college professor of accountancy, in certain allied fields to his subject, such as management, marketing, and transportation.[42] The Tax Court held these were closely related to the field in which the taxpayer was teaching and his primary purpose in taking such courses was the improvement and maintenance of his skill as a teacher. The fact that such credits could be ultimately applied to a master's degree did not detract from this primary purpose, especially in light of the fact that a master's degree was not a requirement of obtaining a position by the taxpayer, it having been waived by the college authorities.

Two final cases which seem to extend the liberal policy of the courts and the current Regulations even further, with regard to teachers, remain to be considered. Again we find a Circuit Court of Appeals blazing a new trail. In the case of *Devereaux* v.

[41] Michaelson v. United States, 203 F. Supp. 830 (E.D. Wash. 1961).
[42] James E. Lane, P-H Tax Ct. Mem. ¶62,179 (1962).

Commissioner,[43] a deduction was allowed by the Third Circuit for certain costs of an assistant professor in obtaining a Ph.D. degree. The degree was not required by the college in order for the taxpayer to obtain his job; it was required for him to attain permanent tenure in his present position. The Tax Court, in denying the deduction, equated permanent tenure with a new position. In reversing, the Circuit Court of Appeals placed its emphasis on the belief of the taxpayer, in the light of newly promulgated university regulations, that he would not be granted permanent tenure unless he obtained a Ph.D. degree, and that the university would not reappoint him unless he began taking steps toward attaining permanent tenure. Thus, the Tax Court viewed the question of permanent tenure as the granting of a new and different position, while the Circuit Court, in a more liberal frame of mind, found the same position with a different status. The Tax Court seems to have followed the cue. In a case decided one year later,[44] the question of whether the taxpayer was required to incur certain educational expenses to remain in her job was not even in issue. The Tax Court found that the only detriment to the school teacher stemming from a failure to obtain certain credits would be her ineligibility to participate in salary increases. She could remain securely in her job at her present salary despite her failure to get credits. Nevertheless, the Tax Court permitted a deduction, finding that the teacher was only maintaining a presently existing right to future salary advances, which would be lost to her if she did not obtain the credits. If such extensions of the settled principles relating to permissible educational expense deductions as these are allowed to stand by higher court, another major breakthrough in a category of expenditures which were once considered totally non-deductible personal expenses may be in the offing.

In conclusion, it must be emphasized that, although the Regulations were liberalized in 1958, still it is a necessity that any attempted educational expense deduction be able to withstand the scrutiny of "ordinary and necessary business expense" concepts. The taxpayer who ignores these concepts and relies instead on an isolated and non-acquiesced court decision must be prepared for the burdens of litigation in order to sustain his deduction.

[43] Devereaux v. Commissioner, 292 F. 2d 637 (3rd Cir. 1961).
[44] Ruth Donmigan Truxall, P-H Tax Ct. Mem. ¶62,137 (1962).