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COMMENT

EDUCATION AS A TRADE OR BUSINESS EXPENSE UNDER SECTION 162(a)

by Ronald S. Webster

While educational expenses have never enjoyed specific treatment in the Internal Revenue Code of 1954, they may be allowable as trade or business expense deductions under section 162(a).¹ To qualify under section 162(a), expenditures must be incurred as business² and not personal expenses,³ and must be "ordinary and necessary."⁴ Amounts expended for the acquisition of assets having an extended and determinable useful life are not deductible as current expenses under section 162(a), but are capital expenditures,⁵ and are recoverable through depreciation deductions over the useful life of the asset.⁶ The scope of this Comment will be to determine when educational expenses are deductible under section 162(a) as "ordinary and necessary" business expenses.

Early judicial views on the deductibility of educational expenses reflected both the capital and personal nature of acquiring an education, and consequently the inherent difficulty in obtaining the deduction. Dictum in *Welch v. Helvering*⁷ characterized "learning" as a tool "with which to hew a pathway to success," and the cost of acquisition, as with any capital asset, "is not an ordinary expense of the operation of a business."⁸ In *Hill v. Commissioner*⁹ a teacher seeking renewal of her teaching license was permitted to deduct summer school expenses incurred in satisfaction of the renewal re-

¹ INT. REV. CODE of 1954, § 162(a) provides: "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"

² See *United States v. Gilmore*, 372 U.S. 39 (1963). The Court in *Gilmore* recognized that § 162(a) imposed the restriction on a deduction that "the expense item involved must be one that has a business origin." *Id.* at 45. *Gilmore* resolved the conflict of whether an expense is personal or business in nature by viewing "the origin and character of the claim with respect to which an expense was incurred, rather than its potential consequences upon . . . the taxpayer." *Id.* at 49.

³ INT. REV. CODE of 1954, § 262 provides that "no deduction shall be allowed for personal, living, or family expenses."

⁴ The term "necessary" imposes the requirement that the expense be appropriate and helpful for the development of the taxpayer's business. *Commissioner v. Tellier*, 383 U.S. 687, 689 (1966). See also *Welch v. Helvering*, 290 U.S. 111, 113 (1933).

"Ordinary" has been defined as the "usual" or "accepted" practice of the business in which the taxpayer is involved. *Deputy v. DuPont*, 308 U.S. 488, 495 (1940). But this interpretation seems to have been replaced by *Tellier*, in which the Court said: "The principal function of the term 'ordinary' in section 162(a) is to clarify the distinction, often difficult, between those expenses that are currently deductible, and those that are in the nature of capital expenditures, which if deductible at all, must be amortized over the useful life of the asset." 383 U.S. at 689-90.

⁵ INT. REV. CODE of 1954, § 263; see *United States v. Akin*, 248 F.2d 742 (10th Cir. 1957).

⁶ INT. REV. CODE of 1954, § 167; Treas. Reg. § 1.167(a)-1, T.D. 7203, 1972-2 CUM. BULL. 12.

⁷ 290 U.S. 111 (1933).

⁸ *Id.* at 115-16.

⁹ 181 F.2d 906 (4th Cir. 1950).

quirement. The court distinguished between schooling that enabled a taxpayer to maintain a present position, and that which qualified the taxpayer to attain a new position, the former being deductible as an "ordinary and necessary" business expense. The taxpayer in *Coughlin v. Commissioner*¹⁰ was an attorney whose responsibility to his firm required him to maintain a current knowledge of tax law. The court allowed a business expense deduction for the expenses of attending a Federal Tax Institute, including tuition and travel expenses, on the basis that the "trade or business" aspects of fulfilling his professional duty outweighed the personal nature of an incidental increase of the taxpayer's general knowledge.

In an effort to provide statutory guidelines for the deduction of educational expenses, the Treasury Department in 1958 promulgated section 1.162-5¹¹ of the Income Tax Regulations, which was amended in 1967.¹² Both sets of regulations defined the deduction according to the requirements of section 162(a), but the taxpayer's success under the 1967 provisions has proved to be less frequent than under the 1958 regulations.

I. THE 1958 REGULATIONS

Adopting language similar to the *Hill* and *Coughlin* decisions, the 1958 regulations provided that a taxpayer who undertook an education "primarily for the purpose" of maintaining or improving skills required in his employment or meeting the express requirements of his employer, could deduct his expenditures as ordinary and necessary business expenses.¹³ Section 1.162-5(b) denied the deduction if the education was undertaken primarily for the purpose of obtaining a new position, or fulfilling general educational aspirations of a personal nature.¹⁴

The courts, prior to any mention of educational expenses in the regulations, recognized that a taxpayer's education might reflect several motives—personal, business, or capital—none of which were apparent from the nature of the education itself.¹⁵ Therefore, the 1958 regulations required a determination by the courts of the taxpayer's primary purpose in obtaining the educational expense he sought to deduct under section 162(a).¹⁶ The

¹⁰ 203 F.2d 307 (2d Cir. 1953).

¹¹ Treas. Reg. § 1.162-5, T.D. 6291, 1958-1 CUM. BULL. 63.

¹² Treas. Reg. § 1.162-5, T.D. 6918, 1967-1 CUM. BULL. 36.

¹³ Treas. Reg. § 1.162-5(a) (1958) provides:

Expenditures made by a taxpayer for his education are deductible if they are for education (including research activities) undertaken primarily for the purpose of:

- (1) Maintaining or improving skills required by the taxpayer in his employment or other trade or business, or
- (2) Meeting the express requirements of a taxpayer's employer, or the requirements of applicable law or regulations, imposed as a condition to the retention by the taxpayer of his salary, status or employment.

¹⁴ Treas. Reg. § 1.162-5(b), T.D. 6291, 1958-1 CUM. BULL. 63.

¹⁵ See notes 7-10 *supra*, and accompanying text.

¹⁶ See, e.g., Ronald F. Weiszmann, 52 T.C. 1106 (1969), *aff'd*, 443 F.2d 29 (9th Cir. 1971). In attempting to resolve whether the taxpayer (a patent trainee) obtained a law degree in order to improve his job skills, or whether he intended to improve his position by becoming a patent attorney, the court said: "The test is what was his primary purpose, and from the facts of the case, it is demonstrable that the petitioner's primary purpose in undertaking a legal education did not lie in his desire to

question of "primary purpose" was one of fact, the burden resting upon the taxpayer to show that the primary purpose in undertaking the education was to maintain employment skills or to meet employer requirements.¹⁷

Education To Maintain or Improve Skills. Section 1.162-5(a) provided that expenditures for education, undertaken "primarily for the purpose" of maintaining or improving skills required by the taxpayer in his employment, were deductible. The taxpayer could satisfy this requirement by showing that "it is customary for other established members of the taxpayer's trade or business to undertake such education"¹⁸ This test of "customariness" was similar in definition to the "ordinary" requirement of section 162.¹⁹

An important change affecting the deductibility of educational expenses occurred in 1966, just prior to the amendment of the 1958 regulations, with the new interpretation by the courts of "ordinary" expenses under section 162(a).²⁰ In *Campbell v. United States*²¹ the court allowed a forensic pathologist employed with the medical examiner's office to deduct expenses of receiving a law degree. The evidence supported the fact that a law degree would aid the petitioner in his work, as the medical investigations involved many legal considerations.²² Rejecting the Commissioner's contention that it was not customary for a forensic pathologist to acquire a law degree, the court said that "customariness" was by no means controlling, "[o]therwise the person who is a pioneer in his field in attempting to maintain and improve his skills beyond what his fellows have done, would be denied a tax deduction"²³ This apparent abandonment by the courts of looking to the custom of the taxpayer's industry to decide whether

continue working . . . as a patent trainee." *Id.* at 1109. See also Ronald F. Weiszmann, 31 CCH Tax Ct. Mem. 1201 (1972), *aff'd*, 483 F.2d 817 (10th Cir. 1973).

¹⁷ James J. Condit, 21 CCH Tax Ct. Mem. 1306 (1962), *aff'd*, 329 F.2d 153 (6th Cir. 1964). Where the taxpayer had coexistent motives in obtaining an education, the deduction was not denied under the 1958 regulation because all motives did not comply with § 1.162-5 of the regulations. Rather, it was the primary purpose that determined the deductibility. See *United States v. Michaelson*, 313 F.2d 668 (9th Cir. 1963); *Sandt v. Commissioner*, 303 F.2d 111 (3d Cir. 1962). See also Comment, *The Deductibility of Educational Expenses: Administrative Construction of Statute*, 17 BUFFALO L. REV. 182 (1967).

¹⁸ Treas. Reg. § 1.162-5(a)(1) (1958). See William J. Brennan, 22 CCH Tax Ct. Mem. 1222 (1963), in which the petitioner, an estate and gift tax examiner for the Internal Revenue Service, was allowed to deduct tuition costs for law school. The court said that it was the custom, if not the rule, that examiners are attorneys; therefore, the taxpayer's primary purpose in obtaining a law degree was to improve the skills required by his business.

¹⁹ See note 4 *supra*.

²⁰ *Id.*

²¹ 250 F. Supp. 941 (E.D. Pa. 1966).

²² "The pathologist is obviously confronted with crimes and their legal definitions; evidence questions; questions of decedent's estates especially when property is found on the body brought into the office; domestic relations' law; torts; and a number of others." *Id.* at 942.

²³ *Id.* at 945. See also Donald P. Frazee, 22 CCH Tax Ct. Mem. 1086, 1089 (1963), in which the Tax Court stated: "We do not read the regulations as requiring the disallowance of deductions for educational expenses where the deduction is undertaken primarily for the purpose of maintaining or improving skills . . . even though such education is not customarily undertaken by other established members of petitioner's trade or business."

educational expenses were for maintaining skills required in his employment was later reflected in the 1967 regulations.²⁴

Education To Meet Express Requirements. Section 1.162-5(a)(2) of the 1958 Income Tax Regulations allowed a deduction for the costs of an education undertaken "primarily for the purpose" of meeting express requirements of the taxpayer's employer "imposed as a condition to the retention by the taxpayer of his salary, status, or employment."²⁵ The expenditures were deductible only to the extent that they were incurred for the minimum education required by the employer, and then only if such requirement was imposed for a bona fide business purpose of the taxpayer's employer.

Travel as a Form of Education. In a 1951 case, *Manoel Cordozo*,²⁶ a professor sought to deduct the expenses of a European trip undertaken for study and research so that he might "improve his reputation for scholarship and learning."²⁷ The tax court stated that since the trip was not required by his contract of employment or by the authorities of the university, the expenses were not deductible as ordinary and necessary business expenses. Section 1.162-5(c), a part of the 1958 regulation, adopted this approach and provided that a "taxpayer's expenses 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."²⁸

This provision seemed to deny all sabbatical expenses for traveling professors. Therefore, in 1964 the Commissioner in Revenue Ruling 64-176 declared that "the rule in section 1.162-5(c) . . . applies to travel which is undertaken primarily for the broadening, cultural value of travel, as such, and which has no direct relationship to the individual's trade or business."²⁹ According to the ruling, travel which has a direct relationship to the conduct of the taxpayer's trade or business may, under certain undefined circumstances, be considered as the equivalent of education, and therefore would be deductible under section 1.162-5(a) of the regulations. The Commissioner did not clarify under what circumstances the travel would be sufficiently connected with the taxpayer's employment so as to allow the deduction, and it was not until the 1967 amendment to section 1.162-5 that exact guidelines were formulated.³⁰

II. THE 1967 REGULATIONS

The 1958 education expense regulations were amended in 1967³¹ in order to provide a more complete categorization of the deductibility guidelines and to eliminate the difficult factual determinations required by the

²⁴ See notes 37-54 *infra*, and accompanying text.

²⁵ Treas. Reg. § 1.162-5(a)(2) (1958).

²⁶ 17 T.C. 3 (1951).

²⁷ *Id.* at 4.

²⁸ Treas. Reg. § 1.162-5(c) (1958).

²⁹ Rev. Rul. 64-176, 1964-1 CUM. BULL. 89.

³⁰ See notes 94-97 *infra*, and accompanying text.

³¹ Treas. Reg. § 1.162-5, T.D. 6918, 1967-1 CUM. BULL. 36.

1958 regulations, most notably in the area of "primary purpose." Realizing that attempting to ascertain a taxpayer's primary purpose "leads us into 'the mire of the no-man's land of subjective intent,'"³² the new regulations do not require the taxpayer to establish his primary purpose in undertaking the education. The objective categories of deductible expenses include expenditures for an education which (1) maintains or improves skills required by the individual in his employment or other trade or business; or, (2) meets the express requirements of the individual's employer, or the requirements of applicable law or regulations, imposed as a condition to the retention by the individual of an established employment relationship, status, or rate of compensation.³³

The Internal Revenue Service also recognized the earlier case law problems in attempting to define the tax characteristics of obtaining an education,³⁴ and provides that the non-deductible educational expenses "are personal expenditures or constitute an inseparable aggregate of personal and capital expenditures and, therefore, are not deductible as ordinary and necessary business expenses."³⁵ Such expenses, according to the regulations, are those expenditures for an education which is (1) required of him in order to meet the minimum educational requirements for qualification in his employment or other trade or business, or (2) part of a program of study being pursued by him which will lead to qualifying him in a new trade or business. The expense for education, if it falls within either one of the above categories, is automatically denied as a deduction under section 162(a) even though the education may qualify under the deductible categories.

The 1967 regulations were intended to be more liberal in favor of the taxpayer than were the 1958 regulations, by no longer requiring him to establish his primary purpose in incurring the educational expenses.³⁶ But, as will be apparent upon examination of case law, the 1967 regulations have only increased the frequency of factual determinations made by the courts, and have not liberalized the ultimate results in favor of the taxpayer who seeks a deduction under section 162(a).

A. *Maintaining or Improving Skills*

For a taxpayer to establish that an education was incurred to maintain or improve the skills required in his employment, he must have undertaken the education in question while he was engaged in a trade or business, the education gained must bear a direct and proximate relationship to his trade or business, and the skills he seeks to maintain or improve by the education must be "required" by his trade or business. The taxpayer does not have to prove that the primary purpose in receiving the education was to maintain

³² Marshall L. Helms, Jr., 27 CCH Tax Ct. Mem. 1020, 1023 (1968).

³³ Treas. Reg. § 1.162-5, T.D. 6918, 1967-1 CUM. BULL. 36.

³⁴ See notes 7-10 *supra*, and accompanying text.

³⁵ Treas. Reg. § 1.162-5(b) (1967).

³⁶ S. REP. NO. 1983, 85th Cong., 2d Sess. (1958), reprinted in 1958 CUM. BULL. 922, 1032.

or improve his skills, but only that the education in fact does improve or maintain his skills required in his present employment.

Carrying On a Trade or Business. In *John C. Ford*³⁷ the taxpayer was a substitute teacher in a California high school. After four years of teaching, he left his position and traveled to Norway, where he studied anthropology and linguistics at the University of Oslo. During this period the taxpayer was employed as a substitute teacher for a school operated by the Department of the Army, but actually taught for only one day. After one year of schooling in Norway, Ford returned to California and resumed teaching. The Commissioner argued that the one year of education undertaken in Norway was not deductible under section 162(a) because the taxpayer was not engaged in a trade or business when he incurred the expense, claiming that Ford had "voluntarily and indefinitely abandoned any active pursuit of the teaching profession."³⁸ The Tax Court upheld the deduction, stating that "mere membership in a profession is not in itself the 'carrying on' of a trade or business," but since the taxpayer had applied for a teaching job during the period he attended classes and had actually taught, more than "mere membership in the teaching profession" was involved.³⁹

If the taxpayer severs his association with his trade or business completely in order to undertake an education, the courts make a distinction between a "temporary" student and an "indefinite" student in allowing or denying the expense deduction. In dealing with the question of whether the taxpayer was engaged in a trade or business when he attended graduate school in engineering, the court in *Berry Reisine*⁴⁰ concluded that the major issue was whether the education in question "represented a temporary hiatus in an engineering career . . . or was such sojourn of such a character as to categorize his trade or business as that of a student for an indefinite period of time?"⁴¹ The court rejected the taxpayer's argument that *Furner v. Commissioner*⁴² applied, stating that here the petitioner had barely begun his employment as an engineer when he decided to resume his education. "His projected program was for an indefinite rather than a limited period of time,"⁴³ and, therefore, the taxpayer was not engaged in a trade or business at the time he incurred the educational expenses.

³⁷ T.C. 1300 (1971), *aff'd sub nom.* *Ford v. Commissioner*, CCH 1973 STAND. FED. TAX. REP. ¶ 9798 (9th Cir. Nov. 9, 1973).

³⁸ *Id.* at 1304.

³⁹ *Id.* See also *Furner v. Commissioner*, 393 F.2d 292 (7th Cir. 1968), *acquiesced in* 1968-2 CUM. BULL. 73. In this case the taxpayer resigned from her teaching position to pursue graduate courses as her school did not grant leaves of absence. The court upheld the deduction, saying that a year of graduate study under the circumstances disclosed "is as much a normal incident of carrying on the business of teaching as study during vacation periods." *Id.* at 294.

⁴⁰ 29 CCH Tax Ct. Mem. 1429 (1970).

⁴¹ *Id.* at 1429-30.

⁴² 393 F.2d 292 (7th Cir. 1968); see note 39 *supra*.

⁴³ 29 CCH Tax Ct. Mem. at 1430. In Rev. Rul. 591, 1968-2 CUM. BULL. 73, the Commissioner declared that the Service would follow *Furner*, but only as to the same facts presented, *i.e.*, where a taxpayer in order to undertake education or training to maintain or improve skills required in his employment temporarily ceases to engage actively in that employment. The Ruling defines "temporary" as a suspension of a

Proximate Relationship. If the taxpayer establishes that he was engaged in a trade or business when he received the education, he must then establish a direct relationship between the education and the skills of his employment. This is required by section 162(a) rather than any language in regulation section 1.162-5; for an expense to be an ordinary and necessary business expense, and, therefore, deductible under section 162(a), it must bear a proximate and direct relationship to the taxpayer's trade or business.⁴⁴ In *James A. Carroll*⁴⁵ a policeman undertook a general college education, majoring in philosophy, and sought to deduct the expenses under 162(a), claiming the education aided him in his employment. In denying the deduction, the court reiterated the point that before expenses can be considered "ordinary and necessary" under section 162(a), there must be a direct relationship to the taxpayer's trade or business, and "clearly there is only a remote relationship between the study of Shakespeare's plays and the petitioner's work as a policeman."⁴⁶ If the education has the requisite relationship to the taxpayer's trade or business as discussed in *Carroll*, then the education "maintains or improves the skills" as required by regulation section 1.162-5, and the expense is an "ordinary and necessary" business expense under section 162(a).

The expenses of a college education were held deductible under 162(a) for a Baptist minister who claimed he undertook the education to "maintain or improve" his skills as a pastor.⁴⁷ The court stated that there was a direct and proximate relationship between the education and the skills required in his employment, in that psychology courses helped him deal with the problems of adolescents in his congregation; courses in teaching methods aided him in carrying out his teaching duties; and the business-related courses enabled him to execute his financial responsibilities to the church.⁴⁸ In *Ben H. Kim*⁴⁹ a Korean born citizen enrolled in law school and later was dismissed for academic deficiency. Kim sought readmission to the law school but was informed that he needed to take certain preparatory courses in logic, accounting, and advanced composition in order to facilitate his law school studies. While taking these courses Kim was employed as an insurance adjuster. The court allowed Kim to deduct these expenses, saying that although his "primary purpose" in taking those courses was to seek re-

year or less, after which the taxpayer resumes the same employment. See also Walter T. Houston, Jr., 32 CCH Tax Ct. Mem. 686 (1973), in which it was held that the taxpayer had not reached a sufficient level of activity as an engineer to constitute the carrying on of a trade or business of an engineer.

⁴⁴ *Kornhauser v. United States*, 276 U.S. 145 (1928); *James A. Carroll*, 51 T.C. 213 (1968), *aff'd*, 418 F.2d 91 (7th Cir. 1969).

⁴⁵ 51 T.C. 213 (1968).

⁴⁶ *Id.* at 218. See also Daniel J. Coughlin, III, 28 CCH Tax Ct. Mem. 459 (1969), in which the court ruled that the taxpayer's college education was at best "tenuously related" to his job as an insurance controls analyst, and, therefore, the expenses were personal expenditures, and not ordinary and necessary business expenses.

⁴⁷ *John D. Glasgow*, 31 CCH Tax Ct. Mem. 310 (1972).

⁴⁸ *Id.* at 312. The court concluded by saying that "[a.]lthough *James A. Carroll* evinces our belief that there are few situations in which a deduction can be allowed for the cost of an undergraduate college education, we believe that this is one case where a deduction should be allowed." *Id.*

⁴⁹ 28 CCH Tax Ct. Mem. 671 (1969).

admission to law school, the education directly improved his skills as an adjustor by helping him to "express himself orally, and to write in the English language" ⁵⁰ Under the 1958 regulations Kim would have been denied the deduction for being unable to satisfy the "primary purpose" test; but under the objective provisions of the 1967 regulations the education in fact improved his skills required by his employment and was therefore deductible, regardless of his subjective intent in taking the courses.

Skills Required by Employment. If the taxpayer establishes that the education was proximately related to the skills of his employment, the skills improved or maintained must be "those required by the individual in his employment" ⁵¹ In *Paul Katz* the term "required" was said to be a "synonym for the Code section 162(a) term 'necessary,' " ⁵² which has been interpreted to mean appropriate or helpful in a taxpayer's business. ⁵³ The taxpayer in *Katz* was not allowed to deduct the cost of flying lessons, even though he operated an airplane in traveling to meet out-of-town clients for his accounting firm. The court said, notwithstanding the use of the airplane in the taxpayer's business, the skills required by his employment were accounting services for his employer's clients, and the end results of his audits were not affected by his mode of transportation. ⁵⁴

B. *Express Requirements of the Employer*

In *Hill v. Commissioner* ⁵⁵ the taxpayer was allowed to deduct summer school expenses incurred in obtaining a renewal license for teaching, the basis of the decision being that expenses undertaken to meet the requirements of an existing employment status were not capital in nature because the taxpayer was not seeking to qualify for a new position, and were not personal, but were ordinary and necessary business expenses. The 1958 regulations adopted the *Hill* rationale, requiring the taxpayer to show that the education was undertaken primarily for the purpose of meeting the express requirements of a taxpayer's employer before the costs of such education were deductible. ⁵⁶

The 1967 regulations eliminate the requirement of "primary purpose," and in so doing, are more restrictive than the 1958 regulations in allowing deductions for education that meet the express requirements of employers. The provisions are very explicit in describing the deductibility of such educational costs. The taxpayer must undertake the education to meet *express* requirements of his employer, the requirements must be imposed for bona fide business purposes, and the requirements of the employer must be imposed as a condition to the "retention by the [taxpayer] of his established

⁵⁰ *Id.* at 673.

⁵¹ Treas. Reg. § 1.162-5(a)(1) (1967).

⁵² 27 CCH Tax Ct. Mem. 87, 89 (1968).

⁵³ See note 4 *supra*.

⁵⁴ 27 CCH Tax Ct. Mem. at 89.

⁵⁵ 181 F.2d 906 (4th Cir. 1950).

⁵⁶ Treas. Reg. § 1.162-5(a)(2) (1958).

employment relationship, status, or rate of compensation."⁵⁷ Even though the taxpayer satisfies the conditions, no deduction will be allowed if the education falls within one of the non-deductible categories.⁵⁸

Express Requirements. In *Lawrence H. Bakken*⁵⁹ the taxpayer was a full-time engineer whose employment required him to analyze the feasibilities of certain atomic weapons. He enrolled in law school night classes in order to improve his ability to reason and communicate with fellow assistants. Bakken's education was undertaken in response to a performance report which concluded that his job performance was poor and recommended that he undertake some program of self-improvement. Bakken claimed that the expenditures for law school were incurred for the purpose of meeting the express requirements of his employer, imposed as a condition for the retention of his job. The court agreed that the taxpayer's performance report was tantamount to a "shape up or ship out" command, but that the regulations required an "express education requirement."⁶⁰ At no time did his employer expressly require Bakken to undertake any formal program of study in order to retain his present job status.

The Tax Court has followed *Bakken* in applying a strict interpretation of the term "required." An Air Force reserve officer sought to deduct the expenses of a college education, claiming that such degree was a condition for his remaining in the Air Force.⁶¹ The Tax court recognized that the Air Force encouraged officers without degrees to obtain them, and that the Air Force would go to great lengths to implement this policy by allowing extended leaves of absence with pay. However, the court stated that, from the mere fact that additional education was encouraged by his employer, "we cannot conclude that William was pursuing his education to satisfy an express requirement of his employer."⁶²

Business Purpose. The provision in the regulations that the express requirement of the employer be imposed for a "bona fide business purpose of the employer"⁶³ serves the same function as requiring the education to be proximately related to the skills of a taxpayer's employment under section 1.162-5(a)(1); that is, in order to deduct expenses under section 162(a) of the Code, the expenditure must have a business origin and must be directly connected with a business activity of the taxpayer.⁶⁴ There must be a greater connection between the express requirement and the taxpayer's

⁵⁷ *Id.* § 1.162-5(c)(2) (1967).

⁵⁸ *Id.*; see notes 75-93 *infra*, and accompanying text.

⁵⁹ 51 T.C. 603 (1969).

⁶⁰ *Id.* at 611. This result was foreshadowed by the court in *Harold H. Davis*, 38 T.C. 175 (1962), in which the Tax Court denied a deduction for research expenditures even though the professor-taxpayer was subject to the tacit "publish or perish" requirement, saying that there was no express requirement at the university that he do such.

⁶¹ *William Kirch*, 30 CCH Tax Ct. Mem. 502 (1971).

⁶² *Id.* at 504. See also *Richard P. Joyce*, 28 CCH Tax Ct. Mem. 1333 (1969) (a promotion in the taxpayer's employment was more difficult without a degree).

⁶³ Treas. Reg. § 1.162-5(c)(2) (1967).

⁶⁴ *Kornhauser v. United States*, 276 U.S. 145 (1928); *Amend v. Commissioner*, 454 F.2d 399 (7th Cir. 1971).

trade or business than the mere fact such requirement is imposed by the taxpayer's employer. If the courts determine that the requirement is not imposed for the benefit of the taxpayer's employment, but rather it is for the individual benefit of the taxpayer, then there is no business purpose in pursuing that requirement and the educational expenses incurred by the taxpayer will be deemed personal and therefore non-deductible under 162(a).⁶⁵

Retaining an Established Status. The most troublesome area to the taxpayer in establishing a deduction under section 1.162-5(a)(2) is proving that he is meeting the express requirements of his employer in order to retain "an established employment relationship, status, or rate of compensation."⁶⁶ The educational expenses must be incurred in fulfillment of express conditions subsequent which are required to "retain" an existing employment relationship, rather than conditions precedent which are required to "obtain" new employment. In *Arthur M. Jungreis*⁶⁷ the Tax Court found that section 1.162-5(a)(2) actually represented the requirement in section 162(a) of "carrying on a trade or business." The court found that the educational expenses incurred by Jungreis "were clearly for the purpose of 'commencing and increasing,' rather than for 'carrying on' or 'preserving,' and therefore did not constitute allowable deductions under section 162(a) of the Code section 1.162-5(a)(2) of the 1967 regulations"⁶⁸

The status of employment which the taxpayer seeks to retain must be a current status. In *Yaroslav Horodysky*⁶⁹ the taxpayer sought to deduct the expenses of law school. He had immigrated from Poland where he had been a practicing attorney, but was not able to practice law since he had not completed a formal law school curriculum, a prerequisite of admission to the Ohio Bar. The taxpayer claimed that his expenses were incurred to fulfill express requirements for the retention of his status as a lawyer, attained originally in Europe. The court did not agree with the taxpayer and interpreted the term "status" in section 1.162-5(c)(2) as a "status" that existed at the time the educational expense in question was incurred. Therefore, when the taxpayer was in Ohio, he had no status as a lawyer and regaining a status he once enjoyed in Poland was not the same as retaining a current established status of employment.⁷⁰

No "Primary Purpose." The regulations state that "in no event . . . is a deduction allowable for expenditures for education which, even though education required by the employer . . . are within one of the categories of non-deductible expenditures" ⁷¹ By eliminating the need to ascertain the taxpayer's primary purpose in undertaking the education, the

⁶⁵ See, e.g., *Adelson v. United States*, 342 F.2d 332 (9th Cir. 1965). European educational travel expenses were held to be primarily for the benefit of the taxpayer, and, therefore, non-deductible as ordinary and necessary business expenses.

⁶⁶ Treas. Reg. § 1.162-5(a)(2) (1967).

⁶⁷ 55 T.C. 581 (1970).

⁶⁸ *Id.* at 589.

⁶⁹ 54 T.C. 490 (1970).

⁷⁰ *Id.* at 492.

⁷¹ Treas. Reg. § 1.162-5(a)(2) (1967).

1967 provision which requires express requirements of employment is more restrictive than the similar provision in the 1958 regulations. A case decided under the 1958 regulations allowed flight engineers to deduct their expenses in obtaining commercial pilots' licenses, even though as a result of such training they became qualified for a co-pilot's position. The court found that their primary purpose in undertaking the education was to meet express requirements established for their positions as flight engineers and not to advance to the position of co-pilot.⁷² The 1967 regulations, as interpreted in *Fleischer v. Commissioner*,⁷³ would require a different result.

Under these new regulations, even if the course of study taxpayer pursued was required by his employer as a condition of employment and was pursued by him exclusively for the purpose of satisfying his employer's requirements, the expenditures would not be deductible if taxpayer qualified for a new trade or business as a result of the education.⁷⁴

C. *Non-deductible Educational Expenses*

There is actually a two-step process for the taxpayer to comply with before he may deduct the expenses of an education. He must first establish the applicability of one of the deductible expense categories. If the expense so qualifies, it will be deductible under section 162(a) unless a court thereafter determines that the educational expense falls within one of the non-deductible classifications, in which case the deduction is automatically denied.

The regulations attempt to distinguish between those educational expenses which are "ordinary and necessary" expenses of a trade or business, and those which are personal and capital expenditures. This distinction is the basis for denying a deduction for expenses of an education which satisfies minimum requirements in the taxpayer's employment, or qualifies him for a new trade or business. An expense for education which qualifies a taxpayer for his intended trade or business is so inherently personal and capital in nature that it is not a deductible expense even though it maintains or improves the skills required by the individual in his employment, or meets the express requirements of the individual's employer. As discussed in *James A. Carroll*,⁷⁵ the 1967 regulations, by providing two categories of non-deductible educational expenses, recognize the essential balance between section 162 on one hand, and sections 262 and 263⁷⁶ on the other hand, in ascertaining the deductibility of educational expenses.

⁷² Marvin LeRoy Lund, 46 T.C. 321, 331 (1966).

⁷³ 403 F.2d 403 (2d Cir. 1968).

⁷⁴ *Id.* at 407.

⁷⁵ 51 T.C. 213 (1968).

⁷⁶ INT. REV. CODE of 1954, § 262 disallows any deduction for any personal, living, or family expenses, unless elsewhere provided for in subtitle A, ch. 1, subch. A, part IX of the Int. Rev. Code of 1954. *Id.* § 263(a) disallows a deduction for capital expenditures because such expenses may be directly related to an increase in value or permanent improvement of the person's condition or property.

Minimum Educational Requirements. The first category of non-deductible educational expenses in the regulations denies deductibility of expenditures for an education which is required of the taxpayer in order to "meet the minimum educational requirements for qualification in his employment or other trade or business."⁷⁷ The minimum education necessary to qualify for the taxpayer's position is to be determined from such factors as the requirements of the employer, the applicable law and regulations pertaining to the taxpayer's trade or business, and the standards of the profession involved. The sole fact that the taxpayer is already performing similar services in an employment status "does not establish that he has met the minimum educational requirements for qualification in that employment."⁷⁸

The taxpayer in *Arthur M. Jungreis*⁷⁹ was a teaching assistant at a university who sought to deduct the expenses of graduate studies in pursuance of a Doctor of Philosophy degree, an express requirement for promotion to the position of full time faculty member. He argued that his education was not undertaken to meet minimum educational requirements, because he was already qualified at the position of teacher of the university. The court rejected his argument, saying that Jungreis had misinterpreted the meaning of "minimum education necessary to qualify for a position"⁸⁰ as signifying *any* position at his place of employment. A teaching assistantship, while a "position" at the university, was not the same "position" as full professor, which enjoyed greater privileges and advantages and required greater qualifications. Therefore the taxpayer, in seeking to qualify for a professorship, was undertaking education in order to meet the minimum educational requirements for the position of full professor, which he had not met by virtue of his being employed as a teaching assistant.⁸¹

Qualification for a New Trade or Business. The second category of non-deductible educational expenses consists of those expenditures made by the taxpayer for an education which will lead to qualifying him in a new trade or business. The regulations attempt to provide guidelines for determining when the taxpayer is qualified for a new trade or business by virtue of his education. For an employee, a change of duties does not constitute a new trade or business, provided "the new duties involve the same general type of work as is involved in the individual's present employment."⁸²

The cases suggest that taxpayers are most often denied their educational expense deductions under the "new trade or business" category when they attempt to prove their education was undertaken to maintain or improve their present job skills.⁸³ The courts find that, although the education is proxi-

⁷⁷ Treas. Reg. § 1.162-5(b)(2) (1967).

⁷⁸ *Id.*

⁷⁹ 55 T.C. 581 (1970).

⁸⁰ Treas. Reg. § 1.162-5(b)(2) (1967).

⁸¹ See also John C. Ford, 56 T.C. 1300 (1971), in which the taxpayer was held to have met the minimum educational requirements for qualification as a secondary school teacher before undertaking the education in question.

⁸² Treas. Reg. § 1.162-5(b)(3) (1967).

⁸³ See, e.g., James K. Curtin, 31 CCH Tax Ct. Mem. 73 (1972); David N. Bodley, 56 T.C. 1357 (1971).

mately related to the taxpayer's employment, he is qualified for a new job as a result of undertaking the education. Under the objective standards of the 1967 regulations, such a finding by the court leads to an automatic denial of the educational expense deduction, whereas under the "primary purpose" test of the 1958 regulations, the results were not always so harsh.⁸⁴

Under section 1.162-5(b)(3) the sole issue is whether or not the taxpayer is qualified for a new trade or business after receiving the education in question. An inventive argument in this regard was posed by the taxpayer in *Jeffrey L. Weiler*.⁸⁵ The taxpayer relied on the language of the regulations, stating that a change of duties does not constitute a new trade or business where the new duties involve the same general work. Weiler was a certified public accountant employed as an internal revenue agent. He enrolled in law school and sought to deduct his expenses for undertaking an education that maintained or improved his skills in the area of the tax law. The Commissioner contended that the taxpayer's study of law would qualify him as an attorney, and therefore, under the standards of section 1.162-5(b)(3), the taxpayer was not entitled to the deduction since his law school education is a program of study "which will lead to qualifying him in a new trade or business."⁸⁶ Weiler, however, argued to the contrary, saying that his trade or business was that of a "federal income tax professional," within which field were tax attorneys, tax accountants, and internal revenue agents. A lateral shift to a tax attorney status was not the same as entering a new trade or business because the new duties involved the same general work. The Tax Court disagreed, holding that no matter what the taxpayer's present employment was his course of study would qualify him as an attorney, which was "a trade or business separate and distinct from that in which he is now engaged."⁸⁷ The objective standards of section 1.162-5(b)(3) therefore required a denial of his attempted expense deduction.

To determine whether there is a mere change of duties by the taxpayer as a result of the education or whether the education qualifies him for a new trade or business, the courts decide if the education will qualify the taxpayer for a different profession than the one he occupied before the education was undertaken. Criteria used by the courts in determining this issue include comparing the responsibilities of the new job to those of the prior one, examining the tasks to be performed by the taxpayer in his new position, and most importantly, any significant opportunities available to the taxpayer as a result of the education that were not open to him in his prior position.⁸⁸

The effect of new opportunities becoming available to the taxpayer after the education is not dependent upon whether he actually pursues these opportunities. The regulations speak only of a "program of study . . . which

⁸⁴ See notes 18-23 *supra*, and accompanying text.

⁸⁵ 54 T.C. 398 (1970).

⁸⁶ Treas. Reg. § 1.162-5(b)(3) (1967).

⁸⁷ 54 T.C. at 402.

⁸⁸ See Ronald F. Weismann, 52 T.C. 1106, 1110 (1969), *aff'd*, 443 F.2d 29 (9th Cir. 1971), for an example of how the courts determine whether the taxpayer is qualified for a new trade or business as a result of the education in question. See also Ronald F. Weismann, 31 CCH Tax Ct. Mem. 1201 (1972), *aff'd*, 483 F.2d 817 (10th Cir. 1973).

will lead to qualifying him in a new trade or business."⁸⁹ Thus, the argument put forth by the taxpayer, that even though he has a law degree he has not passed the bar exam and does not intend to practice law, is not upheld by the courts.⁹⁰ The denial of the expense deduction under section 1.162-5(b)(3) is not, however, predicated on whether the taxpayer receives a degree, for the regulations provide that the two categories of deductible expenses are ordinary and necessary business expenses "even though the education may lead to a degree."⁹¹ The emphasis is on the "program of study" pursued by the taxpayer; if the education *will lead* to qualifying the taxpayer for a new trade or business, then the expenses of such education are non-deductible, regardless of whether he receives a degree upon completion of his schooling.

Taxpayers had greater success under the 1958 regulations when they sought to deduct the expenses of an education which would qualify them for a new degree. Under the 1958 provision, a deduction was denied only when the expenditures were for an education "undertaken primarily for the purpose of obtaining a new position or substantial advancement in position."⁹² In *Richard M. Baum*⁹³ the expenses of law school for an insurance claims adjuster were held to be ordinary and necessary business expenses even though he was qualified for a new position as a result of the education, because the taxpayer did not intend to leave his present job and seek the position of practicing attorney. The same result would obviously not be reached under the current regulations.

III. APPLICATION OF THE 1967 REGULATIONS

The provisions of the regulations pertaining to educational expenses have been separated and explained by categories according to deductible or non-deductible expenses, with accompanying case law pointing out the difficult problem areas faced by the taxpayers in seeking to deduct their educational expenses under section 162(a). But in order to understand the present status of educational expense deductions, it is necessary to view the regulations in their entirety as they are applied to specific educational endeavors.

Travel as a Form of Education. The 1967 regulations are considerably more liberal than the 1958 provisions in allowing expense deductions for travel taken as a form of education.⁹⁴ Expenses for travel as a form of education, including travel while on sabbatical leave, are deductible only to the extent that the travel expenses are directly related to the taxpayer's trade or business. According to the regulations, only that portion of travel which directly maintains or improves skills required by the taxpayer's employer or

⁸⁹ Treas. Reg. § 1.162-5(b)(3) (1967).

⁹⁰ See 52 T.C. at 1111.

⁹¹ Treas. Reg. § 1.162-5(a) (1967).

⁹² *Id.* § 1.162-5(b) (1958).

⁹³ 23 CCH Tax Ct. Mem. 206 (1964).

⁹⁴ The scope of this discussion is limited to the costs of the trip that qualify as educational. Expenditures for meals and lodging are also deductible under certain circumstances under § 162(a), but are not relevant to this analysis.

trade or business shall be considered "directly related to the duties of the individual in his employment"⁹⁵

The test for the deductibility of travel expenses, claimed as educational expenses, involves the same problem encountered earlier under section 1.162-5(a)(1); namely whether there is a direct and proximate relationship between the educational (travel) and the skills of the taxpayer's trade or business. If the requisite relationship is not found by the courts, then the expenses are personal and not deductible as ordinary and necessary business expenses under section 162(a).⁹⁶ If the taxpayer can prove that the education in the form of travel directly maintained or improved the skills required by his trade or business, then that portion of the travel will be deductible as an ordinary and necessary business expense.⁹⁷

Law School Expenses. Deductions for law school expenses are nonexistent under the 1967 regulations.⁹⁸ The taxpayer may deduct educational expenses only if they qualify under one of the deductible categories, and also avoid the non-deductible classifications. Therefore, if a taxpayer is pursuing a course of education which will qualify him for a new trade or business, his expenditures are not deductible, even though his studies are required by his employer and he does not intend to pursue the new endeavor for which he becomes qualified. Under the objective standards of the 1967 regulations the only criterion for the courts to apply is that the education qualifies, or will qualify, the taxpayer for a trade or business separate and distinct from the one in which he was engaged before undertaking the education,⁹⁹ and this requirement is satisfied by entering law school.

College Expenses. Expenditures for college educations, with rare exceptions,¹⁰⁰ have been held to be personal expenses and therefore not deductible

⁹⁵ Treas. Reg. § 1.162-5(d) (1967).

⁹⁶ In *James L. Denison*, 30 CCH Tax Ct. Mem. 1074 (1971), the Tax Court found that a ten-week trip by the taxpayer-teacher could not be deducted as an educational expense under § 162(a). The taxpayer attempted to prove the business nature of the trip by claiming he took slides for presentation to his classes. The court said that the relationship between the nature of the trip (a 10,000-mile tour to take slides) and the improvement of his skills as a teacher was not sufficiently direct to justify a business expense deduction. See also *Baker v. Commissioner*, 32 CCH Tax Ct. Mem. 962 (1973); 32 CCH Tax Ct. Mem. 466 (1973).

⁹⁷ This involves an apportionment between the deductible and non-deductible portions of the travel claimed as educational. In *Edwin F. Krist*, 31 CCH Tax Ct. Mem. 397 (1972), the court said an allocation of the taxpayer's trip must be made between the portion that involved personal expenditures, and those expenditures that were directly related to her job as a teacher. The taxpayer was able to establish that 80% of her trip contained activities that were directly related to her employment, and that such activities maintained and improved her skills required by such employment. In upholding the 80% expense deduction, the court looked to the information learned by the taxpayer that pertained to her teaching position, and to the travel accommodations of the taxpayer in comparison to the other tourists. *Id.* at 400.

⁹⁸ See, e.g., *Collins v. Commissioner*, 32 CCH Tax Ct. Mem. 890 (1973); *Lundford v. Commissioner*, 32 CCH Tax Ct. Mem. 64 (1973); *Curtin v. Commissioner*, 30 CCH Tax Ct. Mem. 73 (1972); *David N. Bodley*, 56 T.C. 1357 (1971); *Jeffery L. Weiler*, 54 T.C. 398 (1970); *Burke W. Bradley, Jr.*, 54 T.C. 216 (1970); *Ronald F. Weiszmann*, 52 T.C. 1106 (1969), *aff'd*, 443 F.2d (9th Cir. 1971).

⁹⁹ See notes 82-93 *supra*, and accompanying text.

¹⁰⁰ See notes 47-48 *supra*, and accompanying text.

under section 162(a). The difficulty in sustaining the deduction does not lie in avoiding the non-deductible categories, but in qualifying under one of the deductible expense categories. The taxpayer cannot establish either that he is engaged in a trade or business concurrent with his attendance at college,¹⁰¹ or that the education bears a direct and proximate relationship to the skills of his employment.¹⁰² One court indicated that most people "secure a general college education before they commence their life's employment, and it is generally accepted that obtaining such education is a personal responsibility in preparing for one's career. Should the result be any different for the man who goes to college after commencing work?"¹⁰³

Graduate Study for Teachers. There are two major obstacles facing the professor who seeks to deduct the expenses of postgraduate studies under the 1967 regulations. He must be engaged in the "trade or business" of teaching while he is taking the postgraduate studies, and such studies must not be in satisfaction of minimum educational requirements for qualification in a teaching position.

A teacher cannot argue that his postgraduate studies maintain or improve the skill in his employment¹⁰⁴ if he has no "employment" when he incurs the education. The problem of whether the taxpayer is engaged in the trade or business of teaching commonly occurs in three situations: when the graduate studies are completed before the taxpayer actually begins his career in teaching;¹⁰⁵ when the taxpayer is actively engaged in the teaching profession, but leaves temporarily to pursue graduate studies, and returns to the same trade or business of teaching;¹⁰⁶ or when the professor is actively employed, but resigns in order to pursue full-time graduate studies, with or without the intention of returning to the profession of teaching.¹⁰⁷ The

¹⁰¹ Thomas A. Gallery, 57 T.C. 257 (1971). The taxpayer was held not to have been engaged in a trade or business when he incurred the college expenses, and therefore the expenditures were personal and non-deductible.

¹⁰² James A. Carroll, 51 T.C. 213 (1968). See also notes 59-62 *supra* and accompanying text.

¹⁰³ 51 T.C. at 216.

¹⁰⁴ This would allow the teacher to deduct his educational expenses under § 1.162-5(a)(1) of the Regulations, provided the non-deductible categories did not apply to his situation.

¹⁰⁵ In Robert F. Casey, 30 CCH Tax Ct. Mem. 60 (1971), the taxpayer was not allowed to deduct the expenses incurred while attending teacher's college because he did not become actively employed as a teacher until the course work was completed.

The taxpayer in Don E. Wyatt, 56 T.C. 517 (1971), was employed as a teacher before resigning and assuming a secretarial position. After four years of absence from the teaching position, she incurred educational expenses in preparation for returning to a teaching job. The Tax Court held that the expenses were not incurred while carrying on the trade or business of being a teacher but were in preparation for resuming such occupation and, therefore, were not deductible as business expenses under § 1.162-5(a)(1) of the regulations.

¹⁰⁶ This includes the leave-of-absence situation. In Rev. Rul. 591, 1968-2 CUM. BULL. 73, the Commissioner acquiesced in the *Furner* case, which held that if a taxpayer temporarily ceases to engage actively in his employment in order to pursue education that maintains or improves his skills, his educational expenses are deductible.

¹⁰⁷ The "temporariness" distinction which allows a taxpayer to be engaged in carrying on a trade or business for purposes of § 162(a), even though he has technically ceased his active participation, does not apply in this situation. In Peter G. Corbett, 55 T.C. 884 (1971), the teacher terminated all relations with her employer-college to seek a graduate degree. The court held that because the taxpayer did not teach during

teacher or professor must be engaged in the "trade or business" of teaching when he incurs the educational expense, because for an expenditure to be deductible as an ordinary and necessary business expense under section 162(a) it must relate to activities which amount to a present carrying on of a trade or business.¹⁰⁸

If the teacher or professor is engaged in a trade or business and he undertakes an education which relates to his skills as a teacher, he often is denied the expense deduction because the courts determine that the education meets minimum requirements for qualification in the teacher's trade or business. The regulations provide that the minimum level of education, in terms of aggregate hours or degrees, is that required by the institution for employment at that position when the taxpayer is hired. If the institution has no minimum requirements for teaching positions, then the taxpayer is deemed to have met the minimum educational requirements when he becomes a permanent faculty member. This is determined by such factors as the practices of the institution, whether the taxpayer has tenure, or whether he has a vote in faculty affairs.¹⁰⁹

Under the non-deductible category of expenses for an education that qualifies a taxpayer for a new trade or business, the regulations provide that a change in duties does not constitute a new trade or business where the new duties involve the same general type of work as the prior duties. With respect to teaching, the regulations state that "all teaching and related duties shall be considered to involve the same general type of work."¹¹⁰ Thus, for the teacher who incurs an educational expense and then returns to the field of teaching, whether or not the education qualifies him for a new trade or business will never be at issues in denying or sustaining the deduction. However, if the teacher is required to meet minimum educational requirements in order to achieve the "change of duties," his deduction will not be allowed,¹¹¹ regardless of the favorable provisions in section 1.162-5(b)(3).

IV. CONCLUSION

The regulations under section 162(a) were promulgated to establish the circumstances under which educational expenditures satisfy the requirements of trade or business expenses. With the elimination of the "primary purpose" test, the 1967 regulations avoid the litigation problems that plagued the courts under the 1958 regulations with respect to the taxpayer's subjective intent in undertaking the education. Unfortunately, the 1967 regulations also disallow many deductions that were once allowed.

This trend is attributable to denying expenditures for any education which qualifies the taxpayer for a new trade or business, irrespective of the tax-

her graduate studies, was not on a leave of absence from her teaching duties, and was not actively seeking another teaching position, she was not engaged in the trade or business of teaching when she incurred the educational expenses.

¹⁰⁸ See notes 37-43 *supra*, and accompanying text.

¹⁰⁹ Treas. Reg. § 1.162-5(b)(2)(ii) (1967).

¹¹⁰ *Id.* § 1.162-5(b)(3).

¹¹¹ *Id.* § 1.162-5(b)(2).

payer's intended use of the education. The inequities that result from this provision are apparent upon consideration of the rationale set forth by the regulations for denying the deduction—that such expenditures represent personal expenditures, or constitute an inseparable aggregate of personal and capital expenditures. If a taxpayer has met the tests under 162(a), then the educational expense is not personal; yet, the regulations deny the deduction, presumably because the expense is capital in nature. And since the number of years that the education will be used by the taxpayer in his trade or business is indeterminable, he may not recover his expenses through capitalization and amortization. In other words, the 1967 regulations fail to consider situations where an education is a legitimate business expense according to the taxpayer's actual use of the education, and in doing so, overreach the already rigorous tests of section 162(a).