The Deductibility of Educational Costs: Why Does Congress Allow the IRS to Take Your Education So Personally?

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THE DEDUCTIBILITY OF EDUCATIONAL COSTS: WHY DOES CONGRESS ALLOW THE IRS TO TAKE YOUR EDUCATION SO PERSONALLY?

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TABLE OF CONTENTS

I. INTRODUCTION 3
   A. Prelude to Inequitable Tax Treatment of Educational Costs 4
   B. Position and Structure of the Article 7
   C. The Current Regulations Treat Most Educational Costs as Nondeductible Personal Expenses 9
   D. An Example of How the Current Regulations Treat Educational Costs Differently Than All Other Business Expenses 15

II. HISTORY OF "PERSONAL" EDUCATIONAL COSTS 16
   A. 1921-1940 – Are Educational Costs Business or Personal? – The Early Years 16

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The author dedicates this article to the memory and the spirit of Dr. David Katz. Every time I hear a joke, I think of him. Every time I tell a joke, I think of him.
B. 1940-1950 – Teachers Get Involved and Contend that the Service Took Their Continuing Education Too Personally

C. 1950-1958 – The Hill Period – Two Appellate Courts Direct the Tax Court and the Service not to Take Education So Personally


III. ISSUES CONCERNING THE DEDUCTIBILITY OF EDUCATIONAL COSTS UNDER THE CURRENT REGULATIONS

A. The Current Regulations Replace the 1958 Regulations

B. What is Education?

C. Potentially Deductible Educational Costs

D. How Otherwise Deductible Educational Costs Are Converted Into Nondeductible Personal Expenses

IV. EDUCATIONAL COSTS SHOULD BE TREATED LIKE ANY OTHER BUSINESS EXPENSES

A. Educational Costs Are Not Inherently Personal Expenses

B. The Current Regulations Deny a Deduction for Educational Costs Based Upon the Same Standard Which Allows a Deduction for Other Business Expenses

C. Deductibility of Educational Costs As Business Expenses

V. ONLY PIECEMEAL AND LIMITED CHANGES TO THE DEDUCTIBILITY OF EDUCATIONAL COSTS WILL OCCUR THROUGH NEW LEGISLATION

A. Judicial Declaration of Current Regulations as Void is Unlikely
The Deductibility of Educational Costs

B. Congressional Overhaul of the Current Regulations is Unlikely

C. Recent Legislation Provides Limited Tax Relief for Educational Costs

VI. CONCLUSION

I. INTRODUCTION

In the past year, the 105th Congress has made the improvement of education a national priority. To make higher education more affordable to Americans, Congress has recently added provisions to the Internal Revenue Code of 1986 (the "Code") providing some limited tax relief for educational costs.\(^1\) In support of this tax relief, President Clinton stated:

As I told the American people, we should make the 13th and 14th years of education as universal as a high school diploma is today. So I will work to see to it that this balanced budget includes the education tax cuts I outlined during the campaign, which had very broad and overwhelming support among the American people.\(^2\)

Ironically, Congress would not need to amend the Code if the Internal Revenue Service (the "Service") applied the same standard to the deductibility of educational costs as is applied to the deductibility of all other business costs. There is no language in the Code, with the exception of one section,\(^3\) to justify the treatment of the deductibility of educational costs by a different standard. Nonetheless, since 1921, when the Service proclaimed that educational costs were nondeductible personal expenses,\(^4\) Congress

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\(^1\) See discussion infra part V.C.


\(^3\) See I.R.C. § 274(m)(2) (disallowing a deduction for the expenses of travel as a form of education).

\(^4\) See O.D. 892, 4 C.B. 209 (1921) (ruling that summer courses taken by a teacher are nondeductible); O.D. 984, 5 C.B. 171 (1921) (ruling that post-graduate courses taken by a
has given the Service free rein in promulgating the rules which apply a different standard. These rules wrongfully deny the taxpayer a deduction for the cost of education which qualifies the taxpayer for her chosen trade or business or for a new trade or business.

In spite of the inequitable treatment of the deductibility of educational costs, the Tax Court has consistently upheld the Service's position. In addition, it is evident from the recent legislation providing only limited tax relief for educational costs that Congress continues to acquiesce to the Service’s rules.

In light of the approval of Congress and the Tax Court, and in the absence of authority from the Code, the Service’s position that most educational costs are nondeductible is the de facto law. If the controversy were to be resolved solely on the basis of tax principles, the author would advocate the immediate repeal of the Service's position. Yet, if Congress or the courts ever repealed this position, it would result in tax deductions for educational costs in a magnitude never before available to taxpayers. Such a solution would cost the government billions of dollars in lost tax revenues and would have a corresponding negative effect on the current budget deficit. Thus, the only practical alternatives are to (1) accept the limited educational tax relief provided by the recently enacted legislation; or (2) eliminate some currently deductible expenses or other tax benefits so as to offset the lost tax revenues caused by the more liberal deductibility of educational costs. Although the author advocates the second alternative, a discussion of which deductions or other tax benefits should be eliminated in favor of deductible educational costs is beyond the scope of this article.

A. Prelude to Inequitable Tax Treatment of Educational Costs

Because the Service treats educational costs differently than other business expenses, very few educational costs are deductible.

\[^5\] See infra note 23 and accompanying text.

\[^6\] For example, the Senate Report accompanying the Taxpayer Relief Act of 1997, Pub. L. No. 105-34, makes the following assessment of “present law”: “Taxpayers generally may not deduct education and training expenses.” S. Rep. No. 33, 105th Cong., 1st Sess. 6 (1997).
Generally, business expenses are deductible if there is a direct and proximate relationship between the benefit or use of the expense and the taxpayer's trade or business. However, the Service does not apply this business standard to most educational costs; instead, they are characterized as nondeductible "personal" expenses. 

Ironically, as compared to other business expenses, educational costs characterized by the Service as "personal" are often the most significant business-related expense a taxpayer is likely to incur in her entire career and, therefore, present the most compelling argument for deductibility. For example, an aspiring physician must attend medical school to obtain the necessary license and training to practice medicine. Yet, the Service treats the cost of medical school as a nondeductible personal expense for that very reason—it qualifies the taxpayer to practice medicine. This result is illogical because without a medical degree, the taxpayer could not practice medicine. Without a medical practice, the taxpayer would not have a business in which to incur such deductible expenses as office rent and utilities. In spite of the compelling significance of a medical degree to the taxpayer's practice, the cost of medical school is the only business-related expense that the taxpayer may never deduct.

Another instance of the Service's improper treatment of educational costs occurs when a taxpayer established in a profession decides to pursue education to maintain or improve her work skills. Regardless of the extent to which this education enhances the taxpayer's work skills, the Service treats its cost as a nondeductible personal expense if it also qualifies her for a new trade or business (even if the taxpayer never enters into such trade or business). For example, many non-legal professionals, such as accountants, corporate administrators, and doctors who testify as expert witnesses, may routinely deal with legal matters. Suppose that such a professional decides to attend law school to improve her legal skills. If she attends an accredited law school because it provides a better legal education, the Service would deny her a deduction for its cost, on the theory that as a graduate of an

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7 See Kornhauser v. Commissioner, 276 U.S. 145, 153 (1928).
8 See Reg. § 1.162-5(b)(2) (as amended in 1967).
9 See Reg. § 1.162-5(b)(3) (as amended in 1967).
accredited law school she could potentially become a licensed attorney. On the other hand, if the professional attends non-accredited law school of lesser quality, the Service would allow a deduction for its cost, because a graduate of a non-accredited law school cannot qualify to become a lawyer.

Finally, in the midst of nonsensical rules which deny a deduction for most educational costs, there are special rules that, for no apparent reason, allow teachers to deduct certain educational costs that other taxpayers may not deduct. For example, a certified teacher in one state may deduct the cost of college courses necessary to become a certified teacher in a second state. This is because under the Service's rules all teaching is considered to be one trade or business. Therefore, the cost of the education necessary to become certified to teach in a second state is deductible because it does not qualify the taxpayer for a new trade or business.

In contrast, any other professional licensed to render services in one state may not deduct the cost of education necessary or helpful to become licensed to render those same services in another state. This is because the Service considers professionals (other than teachers) of the same discipline licensed in different states to be separate trades or business. Thus a lawyer licensed in one state may not deduct the cost of a bar review course taken to prepare for the bar examination of a second state.

In the final analysis, without any authority from the underlying Code sections, the Service inappropriately departs from basic tax principles to wrongfully deny a deduction for most educational costs. Specifically, a taxpayer may not deduct the cost of education necessary to enter into a trade or business or to maintain or improve skills in an existing one (if the underlying education also

10 See Reg. § 1.162-5(b)(3).
12 See Reg. § 1.162-5(b)(3)(i) and following examples. For a discussion of the deductibility of educational costs to teachers, see infra parts III.D.1.b, III.D.2.d; Laurano v. Commissioner, 69 T.C. 723 (1978) discussed infra notes 381, 385-86 and accompanying text.
13 See Reg. § 1.162-5(b)(3).
The Deductibility of Educational Costs

qualifies the taxpayer for a new trade or business). In addition, for no apparent reason, the Service discriminates in favor of teachers, allowing a deduction for certain educational costs that non-teachers cannot deduct.

B. Position and Structure of the Article

Based upon the premise that tax law should apply the same standard to determine the deductibility of similar expenses, this article takes exception to the Service applying a different standard for educational costs. Educational costs related to a taxpayer's trade or business are no different than any other business expense and their deductibility should be judged on the same principles. Absent any authority from the underlying Code sections, the Service's rules concerning the deductibility of educational costs set forth in Treasury Regulation section 1.162-5 (the "Current Regulations") inappropriately characterize educational costs as nondeductible personal expenses. In the final analysis, the Current Regulations wrongfully deny the taxpayer a deduction for one of the most significant expenses related to his work.

Part I of the article explains how the Current Regulations treat most educational costs as nondeductible personal expenses. Specific examples illustrate how the Current Regulations treat educational costs differently than all other business expenses.

Part II tracks the history of the treatment of educational costs as nondeductible "personal" expenses from 1921 until the promulgation, in 1967, of the Current Regulations. Part III focuses on the various issues pertinent to the limited deductibility of educational costs under the Current Regulations. As part of this discussion, part III explores the impact of the special guidelines and rules in the Current Regulations which apply exclusively to teachers.

Part IV criticizes the treatment of educational costs by the Current Regulations and challenges the premise that educational

15 See Reg. §§ 1.162-5(b)(2), (3).
17 Reg. § 1.162-5 (as amended in 1967). All references to the regulations refer to the Treasury Regulations promulgated under the Internal Revenue Code.
costs are inherently personal expenses. Then, part IV illustrates how the Current Regulations cause most educational costs to be nondeductible in situations in which other business expenses are deductible. Finally, part IV.C explains how educational costs, like other business expenses, which have a business nexus to the taxpayer's trade or business and meet all other applicable deductibility requirements should be (1) deductible in the year paid or incurred,\(^\text{18}\) (2) amortizable over a sixty month period,\(^\text{19}\) or (3) amortizable over a period spanning the taxpayer's career or lifetime.\(^\text{20}\)

Part V explores the realistic prospects for judicial or legislative repeal of the Current Regulations to allow for the equitable treatment of the deductibility of educational costs. Part V discusses the unlikely possibility that a court would nullify the Current Regulations. Although the author contends that the Current Regulations should be declared void because they are "unreasonable and plainly inconsistent with the revenue statutes,"\(^\text{21}\) such regulations could be validated under the legislative reenactment doctrine.\(^\text{22}\) Moreover, whenever a taxpayer has challenged the validity of the Current Regulations, the Tax Court has always found them to be consistent with the underlying revenue statutes.\(^\text{23}\) Next, part V discusses the unlikelihood of congressional repeal of the Current Regulations due to a prohibitive cost of billions of dollars in lost tax revenues. Finally, part V

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\(^{18}\) For a discussion of the current deductibility of educational costs in a variety of contexts, see infra notes 451-52 and accompanying text (educational costs paid or incurred prior to entering a trade or business); notes 471-80 and accompanying text (educational expenses paid or incurred while carrying on an established trade or business).

\(^{19}\) For a discussion of the amortization of educational costs as start-up expenditures, see infra part IV.C.1.b.

\(^{20}\) For a discussion of the amortization of educational costs spanning a period of the taxpayer's career or lifetime, see infra parts IV.C.1.c, IV.C.2.b.


The Deductibility of Educational Costs outlines the limited tax relief for educational costs provided by recently enacted legislation.

Finally, the article concludes that the repeal of the Current Regulations would not be economically feasible in today's deficit budget environment without eliminating some currently allowable deductions. Thus, unless Congress is willing to make some hard choices and eliminate some currently allowable deductions or other tax benefits, any tax relief for educational costs is likely to be limited and piecemeal.

C. The Current Regulations Treat Most Educational Costs as Nondeductible Personal Expenses

An understanding of how the Current Regulations deal with educational costs begins with the premise that education is inherently personal. In general, section 262(a) denies a deduction for "personal, living, or family expenses." Occasionally, the Code and the regulations do allow a deduction for some personal expenses if they also meet the requirements for a trade or business deduction under section 162(a). However, for many deductible personal expenses, the Code and regulations impose more restrictive rules than those usually applied to other business deductions. The effect of these restrictive rules is often to limit or, in some cases, eliminate the deduction for such otherwise deductible expenses. Although section 262 does not enumerate educational costs as a nondeductible personal expense, the underlying regulations do. Yet, these regulations do authorize a deduction for educational costs which meet the requirements of section 162(a) and the Current Regulations. Under section 162(a), any deductible item must be an ordinary and necessary expense

24 See, e.g., I.R.C. § 162(a)(2) (allowing a deduction for traveling expenses, including amounts expended for meals and lodging while away from home in the pursuit of a trade or business).

25 See, e.g., I.R.C. §§ 274(n)(1)(A) (limiting the deduction for otherwise deductible meals to 50% of their cost), 274(a)(1)(A) (eliminating a deduction for business entertainment unless such entertainment is directly related to or associated with a substantial and bona fide business discussion).

26 See Reg. § 1.262-1(b)(9).

27 Id.
paid or incurred in carrying on a trade or business. In addition, a direct and proximate relationship must exist between the benefit and use of the expense and the taxpayer's trade or business. The Current Regulations provide that educational costs have the requisite business relationship and meet the requirements of section 162(a) if the underlying education: (1) maintains or improves the taxpayer's work skills; or (2) meets the express requirement(s) imposed by the taxpayer's employer or by law or regulation as a condition of retaining the taxpayer's employment relationship, status, or rate of compensation.

The Current Regulations then impose additional restrictive rules which often eliminate the deductibility of most other deductible educational costs. This is accomplished by testing all educational costs against two "personal" categories of education. If a particular type of education falls within either personal category, the Current Regulations treat its cost as no longer deductible. Specifically, educational costs are treated as nondeductible personal expenses if the underlying education: (1) qualifies a taxpayer to enter her chosen trade or business; or (2) qualifies a taxpayer already established in a trade or business to enter a new trade or business.

1. Educational Costs Which Qualify the Taxpayer for Her Chosen Profession Are Treated as Nondeductible Personal Expenses

One effect of the Current Regulations on education costs is the denial of a deduction for the cost of all pre-employment education (such as college, graduate and professional school) pursued by the taxpayer to qualify for her chosen profession. Arguably, the cost of the education which launches a taxpayer's career is the most significant expense that a professional incurs in her entire career.

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28 See Kornhauser v. Commissioner, 276 U.S. at 153.
29 Reg. § 1.162-5(a)(1).
30 Reg. § 1.162-5(a)(2).
31 Reg. §§ 1.162-5(b)(2), (3).
32 Reg. § 1.162-5(b)(2).
33 Reg. § 1.162-5(b)(3).
34 See Reg. § 1.162-5(b)(2).
Yet, under the Current Regulations, it is the only business expense that the taxpayer may never deduct.

In many cases, a strong business nexus exists between the required education and the taxpayer's trade or business for the following reason(s): (1) the education satisfies the applicable licensing requirements in the taxpayer's chosen trade or business; and/or (2) the education provides the training necessary to perform in the taxpayer's chosen trade or business.

Enrollment in a professional school is an example of education which satisfies a licensing requirement and provides essential training in a taxpayer's chosen profession. For example, an aspiring dentist must first attend dental school. Other professions, such as public school teaching, may require a degree and a particular course of study in a college or graduate program (rather than in a professional school) to obtain the necessary credentials or certification.35

Some non-licensed professions, such as college level teaching, may require a course of study in a college or graduate program which provides the essential training necessary to enter such profession. For example, a college may require an aspiring professor to have a Ph.D. in her subject area as a condition of employment. By pursuing this degree, the taxpayer acquires the skills and training required to teach in her chosen subject area.36

In contrast, for other positions, some employers may either formally or informally require a degree (in no particular subject area) from a college or graduate school as a condition of employment. Unlike education which satisfies a licensing requirement or provides essential training for the taxpayer's trade or business, this type of education is not directly related to the taxpayer's specific work skills. However, higher education, in

35 See Orr v. Commissioner, 64 T.C.M. (CCH) 882 (1992). Orr involved the following educational requirements necessary to obtain a teaching credential in California:

California Education Code section 44259... provides that the minimum requirements for a teaching credential, except for designated subjects, are:

(a) A baccalaureate degree or higher degree, except in professional education, from an approved institution.
(b) A fifth year of study to be completed within five years from the date of issuance of the preliminary credential.

Id. at 884 n.6.

36 This example is based on the facts of P.L.R. 93-16-005 (Apr. 23, 1993).
general, makes a person a more productive and competent worker by improving his ability to think and reason. In many cases, employers value the general competence any form of higher education provides its potential employees.

For example, suppose that a taxpayer aspires to become a hotel manager. Some hotel chains may expressly require a bachelor's degree as a condition of employment. Other hotel chains may not formally require such a degree as a condition of employment but usually hire college graduates. In either case, most hotel chains value employees with the general competence provided by a college education.

In the above hotel example, to present herself as an attractive candidate for employment, the taxpayer pursues a bachelor's degree in philosophy. After receiving her degree, a hotel chain hires the taxpayer as a manager. Although the degree meets the formal or informal requirements of the employer, the underlying education does not bear any particular relationship with the taxpayer's skills as a hotel manager. Moreover, even though the taxpayer's general college education does not satisfy a licensing requirement or provide essential training, her employer may not have hired her without the degree.

In the final analysis, whether pre-employment education is beneficial, essential or necessary to a taxpayer's employment, the Current Regulations treat the cost of all such education as a nondeductible personal expense. Yet if the Service applied the same standard to educational costs as is applied to other business expenses, the former costs would be deductible in some form. For example, a taxpayer who aspires to become a lawyer must attend law school to acquire the necessary license and the training. Once qualified to practice law, the taxpayer begins to earn business-related income. Then, her gross business income, less allowable deductions, results in taxable income. Certain business expenses are deductible in the year in which they are paid or incurred. These expenses include items specifically deductible under the Code and

37 See Reg. § 1.162-5(b)(1).
38 See I.R.C. § 61(a)(2).
40 See, e.g., I.R.C. § 163(h)(2) (allowing a deduction for business-related interest).
all other ordinary and necessary business expenses. Some business expenses not currently deductible may be deductible over a period of years as start-up expenditures or depreciable capital expenditures. Ultimately, every type of business expense, with the significant exception of educational costs, is deductible in one of these forms. However, rather than treat educational costs like other deductible business expenses, the Current Regulations rationalize that educational costs are "personal expenditures or ... an inseparable aggregate of personal and capital expenditures ...".

2. Educational Costs Which Qualify the Taxpayer for a New Profession Are Treated as Nondeductible Personal Expenses

Post-employment educational costs are potentially deductible if the education maintains or improves the taxpayer's job skills or satisfies a condition of retention of employment. Some taxpayers already established in a profession pursue education in a different profession for these reasons, never intending to enter the new profession. Nonetheless, if the education also qualifies or potentially qualifies the taxpayer for a new trade or business, the Current Regulations treat the educational costs as nondeductible personal expenses.

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41 See I.R.C. § 162(a). Ordinary and necessary expenses under this section are deductible, in full, in the taxable year in which they were paid or incurred. For a discussion of section 162(a), see infra notes 459-66 and accompanying text.

42 I.R.C. § 195. Generally, start-up expenditures are items which would be deductible under section 162(a) but for the fact that the taxpayer has not yet begun to operate her business. I.R.C. § 195(c)(1). Such expenditures are deducted by amortizing the cost of the expenditures over a period of not less than sixty months beginning with the month in which the taxpayer actually began the business. I.R.C. § 195(b)(1). For a further discussion of section 195, see infra notes 453-66 and accompanying text.

43 I.R.C. §§ 167, 168. Generally, a depreciation deduction is allowed for an expenditure which would be deductible under section 162(a) but for the fact that the benefit derived from such expenditure continues beyond the taxable year in which the expenditure was made. Thus, the taxpayer must deduct the cost over the useful life of the expenditure. For a further discussion of section 167, see infra notes 467-68 and accompanying text.

44 Reg. § 1.162-5(b)(1). See also Gallery v. Commissioner, 57 T.C. 257 (1971); Reg. § 1.262-1(b)(9).

45 See Reg. § 1.162-5(a)(1).

46 See Reg. § 1.162-5(a)(2).

47 See Reg. § 1.162-5(b)(3).
To illustrate, suppose that a person employed by the Criminal Investigation Division of the Internal Revenue Service decides to attend law school because a law school education (as compared with other educational programs) would enhance his work skills as a special agent. Although a legal education would improve his current job skills, it would also potentially qualify the taxpayer to enter into the new trade or business of practicing law. Thus, despite the nexus between the education and the taxpayer's work skills, the taxpayer may not deduct its cost.

In another context, some employers may require their employees pursue some form of higher education (in no particular subject area) as a condition of retaining employment. Note that an employee who seeks a general degree may then also qualify for many different new trades or businesses. This would bar a deduction for the education costs under the Current Regulations even if the employee would lose her job if she did not pursue the education.

For example, suppose that a taxpayer was employed as an office manager of a consulting firm. Several years after her initial hire, the taxpayer complied with her employer's demand that she obtain a college degree to retain her position. In a similar situation, the Tax Court concluded that the taxpayer's education qualified her for many new trades or businesses. The Tax Court consulted a publication issued by the Department of Labor which listed at least eight different trades or businesses the taxpayer's college degree qualified her to enter. The Tax Court noted that:

it may be all but impossible for a taxpayer to carry his or her burden of proving ... that a bachelor of arts degree program, or

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48 This example is based on the facts of Welsh v. United States, 210 F.Supp. 597 (N.D. Ohio 1962), aff'd per curiam, 329 F.2d 145 (6th Cir. 1964). See also Gore v. Commissioner, 62 T.C.M. (CCH) 426 (1991) (person employed at an engineering company attended law school because his duties included coordinating work on a variety of legal matters with his employer's outside counsel).

49 See Reg. § 1.162-5(b)(3).

50 This example is based on the facts of Malek v. Commissioner, 50 T.C.M. (CCH) 792 (1985). For a discussion of Malek, see infra notes 316-22 and accompanying text.

51 Malek, 50 T.C.M. (CCH) 792.
a liberal arts bachelor of science degree program, does not qualify the taxpayer in a new trade or business.\textsuperscript{52}

Thus, whether education pursued by a taxpayer already established in a profession is beneficial to her work or necessary to retain it, the Current Regulations treat the cost as a nondeductible personal expense. This is the result even though the taxpayer never enters nor intends to enter the new trade or business.\textsuperscript{53} Similar to educational costs which qualify the taxpayer for her chosen profession, the Current Regulations rationalize that the costs of education which qualify the taxpayer to enter into a new profession are "personal expenditures or constitute an inseparable aggregate of personal and capital expenditures . . . "\textsuperscript{54} Educational costs characterized as nondeductible personal expenses are not deductible in any form.\textsuperscript{55}

D. An Example of How the Current Regulations Treat Educational Costs Differently Than All Other Business Expenses

The effect of the Current Regulations is to deny a deduction for educational costs in situations in which other analogous business expenses would be deductible. The following illustration highlights this disparity:

Suppose that a taxpayer rents space in a commercial office building. If, at the time of rental, the taxpayer is carrying on a trade or business, she may deduct the rental payments under section 162(a)(3). If, instead, at the time of rental, the taxpayer is preparing the space for eventual opening, she may not deduct the pre-opening rental payments because she has not yet started her business.\textsuperscript{56} However, as a "start-up expenditure" made in preparation of carrying on a trade or business,\textsuperscript{57} the taxpayer may

\textsuperscript{52} Id. at 796.
\textsuperscript{53} See Reg. § 1.162-5(b)(3)(i), Example (2).
\textsuperscript{54} Reg. § 1.162-5(b)(1).
\textsuperscript{55} See infra part IV.B.
\textsuperscript{56} See Gulick v. Commissioner, 43. T.C.M. (CCH) 490, 492 (1982) (stating that "[p]reparation for entering into a trade or business is not the carrying on of a trade or business within the meaning of section 162").
\textsuperscript{57} I.R.C. § 195(c)(1). For a discussion of start-up expenditures, see infra part IV.C.1.b.
elect to amortize the rental payments over a period of not less than sixty months beginning with the month in which she actually begins operating her business.\footnote{I.R.C. § 195(b)(1).}

Compare this situation with that of a taxpayer who attends medical school to become a physician. While in medical school, the educational costs (like the rental payments) should not be deductible, because the student has not yet begun her practice. However, instead of denying a deduction for the taxpayer's educational costs on that basis, the Current Regulations treat such costs as nondeductible personal expenses.\footnote{See Reg. § 1.162-5(b)(2).} As a result, even though medical school is a necessary prerequisite to begin a practice as a licensed physician, the taxpayer may not amortize her medical school costs (unlike the rental payments) as "start-up expenditures."\footnote{See infra part IV.B.2.} Thus, unlike other business costs essential to creating or carrying on a trade or business, educational costs necessary to enter a trade or business may not be currently deducted nor amortized as start-up expenditures.

II. HISTORY OF "PERSONAL" EDUCATIONAL COSTS

A. 1921-1940 – Are Educational Costs Business or Personal? – The Early Years

The Service's treatment of educational costs dates back to 1921 when the Service, without explanation, declared in two separate rulings that the costs of courses taken by teachers and doctors were nondeductible personal expenses.\footnote{See O.D. 892, 4 C.B. 209 (1921) (summer courses taken by a teacher); O.D. 984, 5 C.B. 171 (1921) (post-graduate courses taken by a doctor).} Not until 1942 did the Service again issue a ruling or regulation dealing with the deductibility of the cost of educational courses.\footnote{In 1942, the Service issued Regulation 103, section 19.23(a)-15(b), treating the "expenses of taking special courses or training" as nondeductible expenses. T.D. 5196, 1942-2 C.B. 96.} The lack of activity during this period is probably attributable to the fact that a large class of people likely to challenge the Service's position, i.e., public school teachers, had no incentive to do so. Until 1938, the Supreme Court
consistently held that it was unconstitutional for Congress to tax the compensation of state employees (including public school teachers). Since public school teachers were not taxed on their compensation, the deductibility of the cost of educational courses was a non-issue.

In the interim, between 1921 (after the two 1921 pronouncements) and 1940, the Service did address the deductibility of other costs related to education. For example, one ruling involved expenses incurred by a physician to attend a medical convention. Here, without labeling the physician's expenses as "educational" or "personal," the Service ruled that such expenses were not deductible. Another ruling involved a college professor who did research to achieve professional recognition and standing. Again, without discussion or labeling the taxpayer's activities as "educational," the Service ruled that the taxpayer's research and traveling expenses were nondeductible personal expenses.

64 See I.T. 2677, XII-1 C.B. 141 (1933). That ruling involved the issue of whether a certain portion of the compensation earned by an agricultural teacher employed by the Virginia public school system was subject to tax. Id. In the ruling, the Service cited Regulation 74, Article 643 which provided that "compensation paid to its officers and employees by a State or a political subdivision thereof for services rendered in connection with the exercise of an essential governmental function is not subject to tax." Id. at 142. The Service concluded that a teacher in a state public school performed an essential governmental function. Id. As a result, the Service ruled that none of the taxpayer's compensation was subject to tax. Id. Cf. G.C.M. 12137, XII-2 C.B. 81 (1933) (stating that the government could tax the compensation of teachers not employed by a state government).
65 I.T. 1369, I-1 C.B. 123 (1922). Although not cited in the ruling, Income Tax Ruling 1369 overruled an earlier ruling in which the Service stated:

A physician may claim as deductions ... the expenses of attending medical conventions ... This in a general way outlines the ordinary and usual expenses incurred by a ... professional man, which may be claimed as deductions, and the principles underlying these allowances are equally applicable in the case of anyone engaged in a ... profession. In short, all expenses connected directly and solely with the conduct of an income-producing business, trade, profession or vocation are allowable.

Income Tax Primer, question 59, (1918), quoted in Robert H. Montgomery, Income Tax Procedure 406 (1919). In the early years of federal income tax law, the Secretary of the Treasury issued "primers" dealing by the 'question and answer' method with the same material as is covered by the regulations. These primers [did] not carry the same force as regulations." Id. at 37. See also Appeal of Lain, 3 B.T.A. 1157 (1926).
66 I.T. 1369 at 123.
68 Id. at 146.
In the judicial arena, between 1926 and 1931, a common issue litigated before the Board of Tax Appeals (the “Board”) was whether a professional could deduct the costs incurred in attending professional conventions. In these cases, the Board, unlike the Service, allowed the taxpayer to deduct such costs if they were related to an active trade or business. For example, Darling v. Commissioner involved a cartoonist employed by a Des Moines newspaper who traveled to New York City to attend conventions and gatherings to obtain information for his work. Unrelated to his cartoon work, the taxpayer did sculptural work on his own time to prepare for a new profession after his career as a cartoonist ended.

Without discussion, the Board determined that the traveling expenses related to the taxpayer’s cartoonist work were deductible. However, the Board characterized the taxpayer’s sculpturing expenses as “purely educational” to prepare him for a new career. Because the taxpayer was not engaged at that time in sculpturing for profit, the Board disallowed a deduction for these expenses.

Another case, Appeal of Driscoll, did involve the “purely” educational costs of a taxpayer who took voice lessons to prepare for potential vocal engagements. However, poor health caused the taxpayer to abandon her plans to pursue her career. The Board denied the taxpayer a deduction for her educational costs, “upon the ground that the expenditure at the time made was for educational purposes and of a personal character, and not a proper deduction from gross income as a loss in 1922.”

Although the Board referred to the taxpayers’ education as personal, a close reading of the Darling and Driscoll cases suggests that the Board did not differentiate the deductibility of educational

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70 Id.
71 Id. at 502-03 (assuming that if such expenses were reimbursed the taxpayer included the reimbursements in gross income).
72 Id. at 503.
73 Id.
74 4 B.T.A. 1008 (1926).
75 Id.
76 Id. at 1009.
costs from the deductibility of any other business expense. In both *Darling* and *Driscoll*, the Board denied the taxpayers a deduction for educational costs for a business not yet started (sculpturing) or a business abandoned (singing). However, in *Darling*, the Board did allow a deduction for expenses related to the taxpayer’s active business as a cartoonist, expenses which seemed educational in nature. Reading the two cases together suggests that the Board characterized educational costs not related to an active trade or business as nondeductible “personal” expenses. However, educational expenses related to an active trade or business were deductible.

On the legislative front, on several occasions during this period, Congress considered legislation expressly allowing a deduction for the cost of educational courses. As part of the Revenue Act of 1926, Congress considered legislation allowing physicians and other professionals to deduct the “expenses incurred in taking special courses . . . for the development of their professional ability.” In support of that legislation, Senator Moses noted:

> I can not see why a distinction should be made as between a trade or business and a profession, especially when a physician, for example, wishes to take a short course, let us say to be specific, at Rochester, Minn., at the Mayo Hospital, and has to separate himself wholly from his source of income from his practice at home, and subject himself to a very considerable

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77 4 B.T.A. at 502-03.

78 See, e.g., *Silverman v. Commissioner*, 6 B.T.A. 1328 (1927). In that case, the Board allowed a university chemistry professor to deduct expenses related to attending conventions to keep current in his field. *Id.* at 1328-29. Although his employer expected the taxpayer to attend such conventions, the taxpayer's contract did not specifically mention such activities or provide reimbursement for such expenses. *Id.* at 1329. Citing *Darling*, the Board stated: “We have also held that expenditures made by a professional cartoonist for periodicals and other current literature and in attending political conventions, when properly proved, were proper deductions as ordinary and necessary business expense.” *Id.* Various cases following *Silverman* allowed taxpayers who were doctors or lawyers to deduct the cost of attending conventions of their respective professional societies. See *Coffey v. Commissioner*, 21 B.T.A. 1242 (1931); *Ellis v. Commissioner*, 15 B.T.A. 1075 (1929); *Upham v. Commissioner*, 16 B.T.A. 950 (1929); *Jack v. Commissioner*, 13 B.T.A. 726 (1928); *Squier v. Commissioner*, 13 B.T.A. 1223 (1928).

79 Revenue Act of 1926, ch. 27, 44 Stat. 9 (1926).

expense of travel and maintenance, to say nothing whatever of fees he may have to pay, all for the benefit of his profession.81

Ultimately, a divided Senate rejected the legislation.82 Two years later, as part of the Revenue Act of 1928,83 Congress again considered legislation expressly allowing physicians and other professionals to deduct the costs of attending their respective conventions.84 Again, Congress failed to enact the proposed legislation.85

Even though Congress failed to enact any specific legislation, numerous Board decisions allowing taxpayers to deduct their convention-related expenses prompted the Service to retract its prior position and accept these holdings.86 In a General Counsel Memorandum, the Service ruled that traveling expenses incurred while attending scientific conventions, previously cast as nondeductible expenses, were now deductible.87 However, the ruling did not address the deductibility of the cost of educational courses treated as personal expenses by Office Decision 892 and Office Decision 984.

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81 Id. at 3023.
82 Id. at 3789.
84 69 Cong. Rec. 9053 (1928). Interestingly, the legislative history reveals uncertainty among Senators concerning the deductibility of the costs of educational courses under then-current law. Id. at 9055.
85 Id. at 10133. Explaining the decision not to include the amendment in the Revenue Act of 1928, Representative Hawley stated:

The conferees on both sides, having examined the question, found that the deduction asked for would extend so far that we could not compute how much it would decrease the revenue or how it would operate, and we thought that for the present the existing law should stand as it is.

Id.
86 G.C.M. 11654, XII-1 C.B. 250 (1933). For a sampling of the Board cases allowing the taxpayer to deduct convention-related expenses, see supra note 78.
87 G.C.M. 11654, 11-1 C.B. at 251.
In 1938, the Supreme Court overruled its earlier decisions and held the taxation of the compensation of state employees to be constitutional.\textsuperscript{88} Shortly thereafter, Congress enacted the Public Salary Tax Act of 1939 which imposed federal income tax on the compensation of state employees, including public school teachers, for taxable years beginning after December 31, 1938.\textsuperscript{89} Then, in 1940 and 1941, perhaps as a result of its new taxing authority over public school teachers,\textsuperscript{90} the Service issued two rulings dealing with the travel expenses of teachers. Although neither ruling involved deductions for educational courses, both appeared to be more liberal than the Service’s position in Office Decision 892 and Office Decision 984.\textsuperscript{91} First, Income Tax Ruling 3380 involved travel expenses incurred by teachers on a sabbatical leave with pay.\textsuperscript{92} Although the sabbatical leave was apparently voluntary, the board of education required a teacher to submit a monthly report of the sabbatical travel and limited a teacher’s travel in any one state to no more than thirty days.\textsuperscript{93} The Service ruled that a teacher could deduct these travel expenses as incurred in pursuit of her trade or business.\textsuperscript{94} Similarly, in Income Tax Ruling 3448, the Service ruled that a teacher could deduct unreimbursed expenses related to attending teachers’ conventions.\textsuperscript{95}

In 1942, the Service issued its first regulations dealing specifically with “special courses or training.”\textsuperscript{96} Consistent with Office Decision 892\textsuperscript{97} and Office Decision 984,\textsuperscript{98} the new regulations

\textsuperscript{88} See Commissioner \textit{v. Gerhardt}, 304 U.S. 405 (1938).
\textsuperscript{89} 53 Stat. 59 (1939).
\textsuperscript{90} For a discussion of the period in which public school teachers were not subject to federal income taxation, see supra notes 61-64.
\textsuperscript{91} See supra note 61 and accompanying text.
\textsuperscript{92} I.T. 3380, 1940-1 C.B. 29.
\textsuperscript{93} \textit{Id}.
\textsuperscript{94} \textit{Id}.
\textsuperscript{95} I.T. 3448, 1941-1 C.B. 206.
\textsuperscript{96} T.D. 5196, 1942-2 C.B. 96, 98.
\textsuperscript{97} O.D. 892, 4 C.B. 209 (1921). For a discussion of Office Decision 892, see supra note 61.
denied a deduction for the cost of any type of educational course.\textsuperscript{99} However, the Service accomplished this result not by labeling education as personal, but by placing the regulation in a section captioned “Nontrade or Nonbusiness Expenses.”\textsuperscript{100} Significantly, labeling the cost of special courses and training as a “nontrade or nonbusiness expense” meant that such cost could not be a deductible trade or business expense.\textsuperscript{101}

The National Education Association (the “NEA”) opposed the new regulations but failed to persuade the Service to allow teachers to deduct their continuing education expenses.\textsuperscript{102} In addition, the NEA Research Division lobbied Congress to enact legislation allowing teachers to deduct the cost of educational courses.\textsuperscript{103} In 1947, legislation was introduced which would allow teachers to deduct all educational expenses required to continue employment or advance in grade or salary.\textsuperscript{104} However, the full Senate defeated the legislation by a vote of 47 to 37.\textsuperscript{105} In the following year, similar legislation was proposed which would allow a teacher to deduct the costs of attending summer school to qualify for continued...
employment or salary advancements. \footnote{Reduction of Individual Income Taxes: Hearings on H.R. 4790 Before Senate Finance Comm., 80th Cong., 2d Sess. 176 (1948) (statement of Sen. Kem).} Likewise, this legislation was never enacted by Congress.

At the end of the decade, a Virginia school teacher, supported by the NEA and the Virginia Education Association, challenged the Service's position of disallowing teachers deductions for the cost of summer courses. \footnote{See Goal of Equitable Tax Treatment, supra note 103.} The case, \textit{Hill v. Commissioner}, involved a teacher who was required by state law to renew her teaching certificate by either (1) passing an examination, or (2) earning three college credits in professional or academic subjects. \footnote{\textit{Hill v. Commissioner}, 13 T.C. 291, 292 (1949).} The taxpayer chose the second alternative and attended summer school, where she earned the credits necessary to renew her teaching certificate. \footnote{Id. at 292.}

The Service treated the summer school costs as nondeductible personal expenses. In response, the taxpayer argued that the costs were deductible as ordinary and necessary business expenses because the courses sharpened her teaching skills and enabled her to renew her teaching certificate. \footnote{Id. at 293.} The Tax Court rejected this argument because she failed to show that summer school attendance was an "ordinary" expense for renewing a teaching certificate when alternative methods were available. \footnote{Id. at 294.} In addition, the Tax Court found to be significant that the taxpayer's re-employment as a teacher depended on the renewal of her expiring teaching certificate. \footnote{Id. at 294.} The Tax Court inferred that as an unemployed teacher she was not carrying on a trade or business when she attended summer school. \footnote{Id.}

In further support of its holding against the taxpayer, the Tax Court relied on two different provisions of Regulation 111, section 29.23(a)-15(b). \footnote{Id.} First, consistent with the Service's position in Office Decision 892, one provision of the regulation specifically
denied a deduction for the expenses of taking special courses or training. The other provision denied a deduction for expenses incurred from seeking employment or in preparation to render personal services for compensation. Here, the taxpayer incurred the cost of her summer school courses to qualify her for re-employment. As a result, the Tax Court characterized the cost of the summer school courses as a nondeductible personal expense.

C. 1950-1958 – The Hill Period – Two Appellate Courts Direct the Tax Court and the Service not to Take Education So Personally

On appeal, the Fourth Circuit reversed the Tax Court’s Hill decision, rejecting the holding that the taxpayer’s educational costs were not deductible as ordinary and necessary business expenses. Significantly, the Fourth Circuit’s opinion established what was to become a new standard for the deductibility of educational costs. In essence, the Fourth Circuit characterized educational costs incurred by a teacher “to maintain her present position, not to attain a new position; to preserve not to expand or increase; to carry on, not to commence” as ordinary and necessary business expenses.

In reaching its decision, the Fourth Circuit did not discuss or even cite the regulation relied upon by the Tax Court. Instead, the Court focused on the Service’s position in Office Decision 892 and determined that it did not apply where “attendance at summer school was undertaken essentially to enable a teacher to continue her (or his) career in her (or his) existing position.” In addition, the Fourth Circuit compared the cost of educational courses with the expenses related to attendance at teacher’s conferences that the Service ruled deductible as ordinary and necessary business

115 Id.
116 Id.
117 Id.
118 Id. at 295.
119 Hill, 181 F.2d at 908.
120 Id. at 909.
121 Id. at 908-09.
The Deductibility of Educational Costs

expenses. The Fourth Circuit concluded that the cost of attending summer school was analogous to those expenses and should be similarly deductible.

Although the Fourth Circuit held that the cost of certain educational courses were deductible as ordinary and necessary business expenses, its failure to reject, rather than to distinguish, Office Decision 892 was significant. As a result, the Tax Court distinguished the facts in Hill from the facts of every subsequent case and applied Office Decision 892 to disallow a deduction for educational expenses.

For example, in Larson v. Commissioner, the Tax Court disallowed a deduction for the educational costs of a mechanic who attended engineering school to become an industrial engineer with the same employer. The Tax Court distinguished Larson from Hill by noting that in Hill the education maintained the taxpayer's present position, but in Larson the education led the taxpayer into a new position with an increased earning capacity. Therefore, in characterizing the taxpayer's educational costs as nondeductible personal expenses, the Tax Court followed Office Decision 892 and Office Decision 984, rather than Hill.

Even as the Tax Court was narrowing the scope of the Hill decision, however, the Service expanded the deductibility of educational costs by modifying Office Decision 892. In doing so, the Service allowed a taxpayer to deduct as ordinary and necessary business expenses educational costs incurred for purposes similar
to those presented in *Hill*. At the same time, the Service also declared that educational expenses incurred "for the purpose of obtaining a teaching position, or qualifying for permanent status, a higher position, an advance in the salary schedule, or to fulfill the general cultural aspirations of the teacher, are deemed to be personal expenses which are not deductible in determining taxable net income."\(^1\)

Next, *Coughlin v. Commissioner*,\(^2\) pitted the *Hill* decision against the Service's ruling in Office Decision 984.\(^3\) In *Coughlin*, an attorney whose practice included matters of federal taxation attended the Fifth Annual Institute on Federal Taxation sponsored by New York University.\(^4\) The institute spanned approximately five days and provided an opportunity for practitioners to keep abreast of trends and developments in federal taxation.\(^5\) The taxpayer attended the institute because he and his partners believed that keeping abreast of current developments in federal taxation was vital to his practice.\(^6\)

Relying on *Hill*, the taxpayer argued that his educational costs were deductible as ordinary and necessary expenses related to his practice of law.\(^7\) In contrast, the Service analogized the taxpayer's educational costs to the cost of postgraduate courses taken by a doctor in Office Decision 984 where the Service treated such cost as a nondeductible personal expense.\(^8\) Holding for the Service, the Tax Court again distinguished the facts of the case from *Hill*. First, the Tax Court noted that in *Hill*, unlike in *Coughlin*, the taxpayer was compelled to pursue education as required to continue in her teaching position.\(^9\) Second, the Tax Court stated that the Fourth Circuit expressly limited the *Hill* decision to its facts.\(^10\) Thus, the

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\(^1\) I.T. 4044, 1951-1 C.B. at 17.
\(^2\) Id.
\(^3\) *Coughlin v. Commissioner*, 18 T.C. 528 (1952).
\(^4\) See supra note 61 and accompanying text.
\(^5\) 18 T.C. at 528.
\(^6\) Id. at 528-29.
\(^7\) Id. at 528.
\(^8\) Id. at 529-30.
\(^9\) Id. at 529.
\(^10\) Id. at 530.
\(^11\) Id. at 529-30.
The Deductibility of Educational Costs

Tax Court characterized the cost of education to improve the taxpayer's existing work skill as nondeductible personal expenses.\(^{140}\)

On appeal, the Second Circuit reversed the Tax Court but did not address the validity of Office Decision 984.\(^{141}\) Instead, the court focused on whether Regulation 103, section 19.23(a)-15(b) applied to disallow the taxpayer's deduction for the costs of attending the institute.\(^{142}\) First, the Second Circuit acknowledged that the regulation denied a deduction for the cost of taking special courses or training.\(^{143}\) However, since that regulation pertained to the deductibility of non-trade or non-business expenses, it did not apply here because the taxpayer attended the tax institute while carrying on the trade or business of being a lawyer.\(^{144}\) Next, the Second Circuit considered Regulation 111, section 29.23-5, which deals with the ordinary and necessary business expenses of a professional, to be relevant.\(^{145}\) Comparing the cost of the tax institute with the types of deductible expenses listed in that regulation (i.e., dues to professional societies, subscriptions to professional journals), the Second Circuit determined that the former cost was an analogous expense also deductible as an ordinary and necessary business expense.\(^{146}\)

Finally, addressing the "personal" aspect of education, the Second Circuit stated:

It may be that the knowledge he thus gained incidentally increased his fund of learning in general and; in that sense, the cost of acquiring it may have been a personal expense; but we think that the immediate, over-all professional need to incur the expenses in order to perform his work with due regard to the

\(^{140}\) Id. at 530.

\(^{141}\) Coughlin v. Commissioner, 203 F.2d 307 (2d Cir. 1953).

\(^{142}\) Id. at 309. Ironically, the Second Circuit focused solely on the regulation and did not discuss nor even cite Office Decision 984. In contrast, the Tax Court focused solely on Office Decision 984 and did not discuss nor cite the regulation. For a further discussion of Regulation 103, see supra notes 99-103 and accompanying text.

\(^{143}\) Coughlin, 203 F.2d at 309.

\(^{144}\) Id.

\(^{145}\) Id.

\(^{146}\) Id.
current status of the law so overshadows the personal aspect that it is the decisive feature.\footnote{Id.}

Thus, in \textit{Coughlin}, the Second Circuit clearly rejected the view that educational costs are inherently personal expenses and instead treated them as any other business expense. Not surprisingly, various professional groups that advocated the deductibility of educational costs incurred by established professionals were interested in the outcome of \textit{Coughlin}.\footnote{See \textit{General Revenue Revision: Hearings Before the Comm. on Ways and Means}, 83d Cong., 1st Sess. 177, 198 (1953) (statement of Dr. Walter B. Martin, President-Elect, American Medical Association). In addition, the American Medical Association filed an amicus curiae brief in the case. \textit{Id.}} However, despite the result in \textit{Coughlin}, these groups feared its holding would be limited and not extended to postgraduate courses taken by established professionals.\footnote{Id.} Thus, these groups supported a congressional bill (never passed) which would have allowed school teachers and other professionals to deduct certain educational expenditures.\footnote{See \textit{99 Cong. Rec. 2661 (1953) (H.R. 4393 introduced by Rep. Davis)}.}

The reversal in \textit{Coughlin} did not deter the Tax Court and the Service from continuing to treat any educational expense incurred to enhance (rather than to retain or preserve) a taxpayer's position as a nondeductible personal expense. For example, in \textit{Marshall v. Commissioner}, the taxpayer took music lessons to qualify to become a music teacher.\footnote{\textit{Marshall v. Commissioner}, 14 T.C.M. (CCH) 955, 956 (1955).} Without discussion, the Tax Court characterized the cost of the music lessons as a nondeductible personal expense.\footnote{\textit{Id.} at 957. See also \textit{Rev. Rul. 55-412, 1955-1 C.B. 318} (treating the costs of a teacher's voluntary sabbatical travel and study as nondeductible personal expenses, reasoning that they were incurred not to retain a current teaching position but to increase prestige and reputation).}

Subsequently, two cases involving similar facts, \textit{Kamins v. Commissioner}\footnotetext{Kamins v. Commissioner, 25 T.C. 1238 (1956).} and \textit{Marlor v. Commissioner},\footnote{\textit{Marlor v. Commissioner}, 27 T.C. 624 (1956).} indicated that the Tax Court and the Second Circuit disagreed as to whether the \textit{Hill} rationale should apply where a taxpayer was hired on the condition
that he obtain an educational degree. In Kamins, a university hired the taxpayer as a research associate on the condition that he pursue and complete a doctorate degree. The taxpayer argued that the Hill rationale supported a deduction for his educational costs because his continued employment depended on his obtaining a doctorate degree. In contrast, the Tax Court distinguished the case from Hill noting that in this case, the taxpayer's position remained temporary and terminable unless he completed his doctorate degree. The Tax Court concluded that the taxpayer pursued the education to begin a permanent position rather than to preserve an existing temporary position. As a result, the Tax Court treated the taxpayer's educational costs as nondeductible personal expenses.

Shortly after Kamins, the Second Circuit reversed the Tax Court's decision in Marlor v. Commissioner.

In Marlor, a college hired the taxpayer as a tutor, a temporary position subject to yearly renewal. To qualify for yearly renewals, the college required a tutor to make substantial progress toward obtaining a doctoral degree, with mandatory termination if the tutor failed to qualify as an instructor (a position requiring a doctorate) within five years of his initial appointment.

As in Kamins, the taxpayer contended that he pursued a doctorate to retain his position as a tutor. In response, the Tax Court characterized a “tutor” as a temporary position leading to the permanent position of instructor. The Tax Court therefore reasoned (as it did in Kamins) that the taxpayer did not pursue a doctoral degree to preserve his temporary tutor position but to attain the higher permanent rank of instructor. Consistent with

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155 Kamins, 25 T.C. at 1239.
156 Id. at 1240.
157 Id.
158 Id.
159 Id. at 1241.
160 Marlor v. Commissioner, 251 F.2d 615 (2d Cir. 1958).
162 Id. at 625.
163 Id.
164 Id. at 625-26.
165 Id. at 626.
Kamins, the Tax Court treated the taxpayer's educational costs as nondeductible personal expenses.\textsuperscript{166}

In a dissenting opinion, Judge Raum found the taxpayer's education as serving two purposes.\textsuperscript{167} For the long term, the taxpayer pursued the education to qualify for the permanent position of instructor. Yet, for a more immediate purpose, the taxpayer pursued the education to retain his position as a tutor. Thus, Judge Raum reasoned, a taxpayer who incurred educational expenses to retain even a temporary position should be able to deduct those expenses against the income earned from that position. In support, Judge Raum found the Hill case consistent with this outcome.\textsuperscript{168} In a \textit{per curiam} decision, the Second Circuit agreed with Judge Raum's dissent and reversed the Tax Court.\textsuperscript{169}


As discussed above, after the Fourth Circuit's reversal of Hill, taxpayers enjoyed modest success in chipping away at the Service's restrictive position concerning the deductibility of educational costs. However, the litigated cases also produced inconsistent results. Hence, there grew increasing momentum for regulatory and legislative liberalization and clarification of the deductibility of educational costs. Finally, in 1956, the Treasury Department issued its first set of comprehensive proposed regulations dealing exclusively with the deductibility of educational expenses.\textsuperscript{170} Unfortunately, these proposed regulations were extremely restrictive and ambiguous.

Specifically, the proposed regulations continued to treat educational costs as inherently personal expenses. Proposed Treasury Regulation section 1.162-5(a)(1) stated the general rule: "[A] taxpayer's expenditures for his education are personal and are

\textsuperscript{166} Id.

\textsuperscript{167} Id.

\textsuperscript{168} Id.

\textsuperscript{169} \textit{Marlor v. Commissioner}, 251 F.2d 615.

The deductibility of educational costs is not deductible. Next, Proposed Treasury Regulation section 1.162-5(a)(2) explained that a taxpayer incurred educational expenditures for personal purposes when incurred primarily for, or having the result of, the following:

- Obtaining a position for the taxpayer; qualifying him to enter an employment or otherwise become established in a trade or business or a 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.

However, in limited situations, Proposed Treasury Regulation section 1.162-5(b) allowed a deduction for certain educational expenses. Under this provision, educational expenses were deductible if (1) they were ordinary and necessary expenses directly related to maintaining the taxpayer's employment or other trade or business, and (2) the business needs and relationship of the expenses clearly outweighed any personal aspects of the expenses. Yet, any such educational expenses were nondeductible if the underlying education was also of the type described in Proposed Treasury Regulation section 1.162-5(a)(2).

In addition, if the education carried academic credit, it could not in "more than an incidental and relatively minor manner" have the result described in Proposed Treasury Regulation section 1.162-5(a)(1).

The NEA responded negatively to the proposed regulations because they were even more restrictive than the Service's earlier position. As a result, the NEA and several state education...
associations formally protested the proposed regulations. In addition, the NEA Research Division and NEA Legislative Commission sought congressional relief. In 1957, Representative King introduced a bill, H.R. 4662, specifically allowing teachers to deduct the costs of further education.

Meanwhile, as the Treasury Department pondered revisions to the proposed regulations, congressional momentum for legislative action grew. In early 1958, Senator Flanders introduced legislation similar to H.R. 4662. By the time the Treasury Department issued its final regulations, the two sessions of the 85th Congress produced fifty-eight educational expense bills introduced by more than sixty Senators and Representatives.

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178 Id.
180 H.R. 4662, 85th Cong., 1st Sess. (1957). H.R. 4662 would have added a new section 217 to the Code. Section 217 provided in pertinent part:

(a) ALLOWANCE OF DEDUCTION.—In the case of a taxpayer who is an established teacher (as defined in subsection (b)(1)), there shall be allowed as a deduction the expenses paid during the taxable year by such teacher for his further education (as defined in subsection (b)(2)).

(b) DEFINITIONS.—For purposes of this section—

(1) the term 'established teacher' means an individual who is employed on the educational staff of a public or private school accredited by the accrediting agency of a State or Territory or by a regional accrediting agency; and

(2) the term 'expenses paid during the taxable year by such teacher for his further education' includes all expenses which are incurred by an established teacher (as defined in paragraph (1)) for tuition, books, and other equipment, travel, and living expenses while away from home (to the extent that they exceed his normal living expenses), and which are paid by him during the taxable year in connection with his enrollment in a course or courses of education at an institution of higher education accredited by the accrediting agency of a State or Territory or by a regional accrediting agency.

(c) LIMITATIONS.—The deduction allowed a taxpayer under subsection (a) shall not exceed $600 for any taxable year; and no expense shall be allowed as a part of such deduction if such expense is allowable as a deduction under section 162 (relating to trade or business expenses).

183 See Teachers Get Tax Break, supra note 179.
The Deductibility of Educational Costs


1. Positive Response to the 1958 Regulations

Heading off congressional action, on April 5, 1958, the Treasury Department issued the final educational expense regulations (the "1958 Regulations"). The 1958 Regulations allowed more liberal deductibility of educational costs than did the previously proposed regulations. The NEA and Representative King, the sponsor of H.R. 4662, hailed the promulgation of the 1958 Regulations as a major victory for teachers. In fact, the NEA estimated that the educational expense deductions allowed by the 1958 Regulations would save U.S. teachers as much as $20 million in taxes per year. Congress also responded favorably by enacting special legislation allowing taxpayers to apply the 1958 Regulations retroactively to all taxable years beginning on or after January 1, 1954.

2. Explanation of the 1958 Regulations

Although the 1958 Regulations liberalized the deductibility of educational costs, they did not completely abandon the premise that educational costs were inherently personal expenses. Instead, the 1958 Regulations made the taxpayer's primary purpose for pursuing education as the factor used to determine whether educational costs would be treated as nondeductible personal expenses or as ordinary and necessary business expenses. Thus,

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184 Reg. § 1.162-5.

185 See Teachers Get Tax Break, supra note 179, at 1. In this special issue of NEA News, the NEA hailed the new regulations as providing long-needed relief to all educators and administrative staffs. See Teachers Get Tax Break, supra note 179, at 1. Representative Cecil R. King, the sponsor of H.R. 4662, expressed his satisfaction with the new regulations as they eliminated the need for H.R. 4662. Id. at 4.

186 See Teachers Get Tax Break, supra note 179, at 1.


188 Reg. § 1.162-5.
a taxpayer could deduct his educational costs if he incurred them primarily for the following purpose(s): (1) maintaining or improving skills required by the taxpayer in his employment or other trade or business,\textsuperscript{189} 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 of his salary, status or employment.\textsuperscript{190}

However, the 1958 Regulations did not allow a taxpayer to deduct his educational costs if he incurred them primarily for purposes of “obtaining a new position or substantial advancement in position, or primarily for the purpose of fulfilling the general educational aspirations or other personal purposes of the taxpayer.”\textsuperscript{191} Finally, the 1958 Regulations treated the cost of education needed by the taxpayer to meet the minimum educational requirements of his chosen trade or business or specialty therein as a nondeductible personal expense.\textsuperscript{192}

\textsuperscript{189} Reg. § 1.162-5(a)(1). Under paragraph (a) of the regulations, to determine whether education pursued by the taxpayer maintained or improved his work skills was a question of fact. However, the regulations presumed this requirement to be met if other established members of the taxpayer’s trade or business customarily pursued such education. Reg. § 1.162-5(a) (flush language). The “deductible” purpose of Regulation § 1.162-5(a)(1) appeared to track the holding in Coughlin v. Commissioner, 203 F.2d 307, where the Second Circuit allowed the taxpayer to deduct the cost of education which directly improved the taxpayer’s ability to perform his trade or business.

\textsuperscript{190} Reg. § 1.162-5(a)(2). Paragraph (a) states that education pursued by the taxpayer would meet the express requirements of his employer “if the requirement is imposed primarily for a bona fide business purpose of the taxpayer’s employer and not primarily for the taxpayer’s benefit.” In the case of a teacher, the regulations presumed this requirement to be met by a “written statement from an authorized official or school officer to the effect that education was required as a condition of retention of the taxpayer’s salary, status, or employment.” Reg. § 1.162-5(a) (flush language). The “deductible” purpose of Treasury Regulation § 1.162-5(a)(2) appeared to track the holding in Hill v. Commissioner, 181 F.2d 906, where the Fourth Circuit allowed the taxpayer to deduct the cost of education which directed improved the taxpayer’s ability to perform his trade or business.

\textsuperscript{191} Reg. § 1.162-5(b). To determine whether the taxpayer pursued education primarily for the purpose of a new position or substantial advancement, the regulations considered important the fact that the education actually met the express requirements for a new position or substantial advancement. However, the regulations deemed such fact not important if the education was “required as a condition to the retention by the taxpayer of his present employment.” Id.

\textsuperscript{192} Reg. § 1.162-5(b). The educational costs nondeductible under the 1958 regulations appeared to track the limits of the Fourth Circuit’s decision in Hill. Hill allowed the taxpayer to deduct the cost of education required to preserve her teaching position. 181 F.2d 906. By inference, Hill would not allow the taxpayer to deduct education which attained, expanded,
3. The Deductibility of the Cost of Law School Under the 1958 Regulations

Perhaps the most significant consequence of the liberalization of the deductibility of educational costs by the 1958 Regulations involved the cost of law school. During the tenure of the 1958 Regulations, there were a number of cases in which taxpayers sought to deduct the cost of law school. Interestingly, only under the 1958 Regulations was a taxpayer ever allowed to deduct the cost of an accredited law school. In those cases, taxpayers who proved that their primary purpose in pursuing such education was to maintain and improve their skills in an established trade or business were allowed to deduct its cost.
III. Issues Concerning the Deductibility of Educational Costs under the Current Regulations

A. The Current Regulations Replace the 1958 Regulations

Under the 1958 Regulations, determining the taxpayer's primary purpose in pursuing an education was a question of fact. However, difficult proof problems arose when the taxpayer pursued education for multiple purposes. As a result, the 1958 Regulations were eventually amended "to provide more specific rules with respect to the treatment for federal income tax purposes, of expenditures for education.

The overall effect of the "more specific rules" promulgated by the Current Regulations was to significantly limit the deductibility of educational costs by retracting many of the liberal aspects of the 1958 Regulations. Moreover, the Current Regulations resurrected in full strength the irrebuttable premise that certain educational costs are inherently personal expenses. By amending the 1958 Regulations in 1967, the Current Regulations made the following substantive changes:

1. Eliminated the subjective primary purpose test so that the taxpayer must only show that the education improves his skills in

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196 Id. See also United States v. Michaelson, 313 F.2d 668, 671-72 (9th Cir. 1963), aff'd 20 T.C.M. (CCH) 582 (1961); Furner v. Commissioner, 47 T.C. 165, 177 (1966), rev'd, 393 F.2d 292 (7th Cir. 1968). Judge Simpson's dissent in Furner commented on a taxpayer who pursued education for multiple purposes:

It may very probably be said, then, that petitioner wished to undertake further study for more than one reason. Such a situation is not unusual, and it is my opinion that these other reasons do not nullify petitioner's desire to improve her teaching skills. That a taxpayer has more than one purpose in undertaking education does not necessarily deny him the privilege of a deduction. ... I believe that since the graduate program undertaken by the petitioner substantially aided her in her trade or business as a teacher, the expenses of such a program should be deductible even though she derived some other benefit from the additional education.

Furner, 47 T.C. at 177.
198 Reg. § 1.162-5.
his present employment, regardless of the taxpayer's primary purpose in pursuing such education; 199

2. Implemented an objective standard to bar a deduction for the cost of any education which qualifies a taxpayer for a new trade or business, regardless of his primary motivation in seeking it; 200

3. Allowed a deduction for education which qualifies the taxpayer for a new position, raise, or specialty within an established trade or business provided the education does not also qualify the taxpayer for a new trade or business; 201 and

4. Provided special rules and guidelines to determine how the provisions of the Current Regulations apply to teachers. 202

To this day, the Current Regulations set forth the rules governing the deductibility of educational costs. The remainder of part III explores the issues relevant to the deductibility of educational costs under the Current Regulations.

B. What is Education?

Although the Current Regulations refer to several examples of education, 203 they do not provide an explicit definition of the term "education." However, the Tax Court has interpreted "education" by applying a "broad commonsense meaning." 204

For example, Lage v. Commissioner 205 involved a taxpayer who was a vice-president and general superintendent of a construction company. Because the taxpayer lacked knowledge in certain areas

201 See Reg. § 1.162-5(b)(3); Furner, 393 F.2d at 293.
202 See Reg. §§ 1.162-5(b)(2)(ii) and (iii), Examples (1) and (2); Reg. §§ 1.162-5(b)(3)(i)(a)-(d).
203 See Reg. § 1.162-5(a) (providing that education includes "research undertaken as part of [an individual's] educational program" and also making reference to education which may lead to a degree). Also, Reg. § 1.162-5(c)(1) includes "refresher courses or courses dealing with current developments as well as academic or vocational courses" as the types of education which maintain or improve a taxpayer's work skills. See also Sharon v. Commissioner, 66 T.C. 515, 528 (1976) (bar review course treated as education within the meaning of the Current Regulations); Glenn v. Commissioner, 62 T.C. 270, 273-74 (1974) (C.P.A. review course treated as education).
of corporate management, he hired a business management consultant and psychologist to educate and train him in those areas. Arguing that such informal training was not "education" within the meaning of the Current Regulations, the Service denied the taxpayer's deduction. Holding for the taxpayer, the Tax Court refused to limit the meaning of "education" to a formal program. Instead, the Tax Court defined "education" as including "not merely instruction in a school, college, university, or a formally conducted training program, but embrac[ing] the acquiring of information and knowledge from a tutor." 

Similarly, Boser v. Commissioner involved a second officer employed by an airline who purchased an airplane to practice his flying skills. The taxpayer deducted the airplane expenses related to his flying practice as educational costs. The Service argued that flying was not education because it was not part of a formal education program. As in Lage, the Tax Court refused to apply such a restrictive definition of "education" and rejected the Service's argument.

C. Potentially Deductible Educational Costs

Even though the I.R.C. section 262 regulations treat educational costs as inherently personal expenses, they do allow a deduction if such costs meet the requirements of section 162(a) and the Current Regulations. Section 162(a) allows a deduction for an ordinary and necessary expense paid or incurred in carrying on a trade or business. In addition, a direct and proximate relationship must exist between the expense and the taxpayer's trade or business.

206 Id. at 131.
207 Id. at 133.
205 Id. at 134.
209 Id.
210 Boser v. Commissioner, 77 T.C. at 1126-27.
211 Id. at 1127.
212 Id. at 1129-30.
213 Id. at 1130.
214 See Reg. § 1.262-1(b)(9).
215 See Kornhauser v. United States, 276 U.S. at 153.
The Current Regulations treat the cost of education as being potentially deductible, if the underlying education:

1. maintains or improves the taxpayer's work skills;\(^{216}\) or
2. is expressly required either by the taxpayer's employer or by law or regulation as a condition to retaining an established employment relationship, status, or rate of compensation;\(^{217}\) and, is not,
3. a minimum educational requirement to qualify for the taxpayer's chosen employment or trade or business;\(^{218}\) or
4. part of a program of study which will lead the taxpayer to qualify for a trade or business.\(^{219}\)

1. Educational Costs Meeting the Requirements of Deductibility Under Section 162(a)

a. Education Which Maintains or Improves the Taxpayer's Work Skills

Under the Current Regulations, education maintains or improves the taxpayer's work skills only if it is directly and proximately related to the taxpayer's specific work skills. For example, *Galbreath v. Commissioner*\(^ {220}\) involved an air traffic controller who took flight training courses not required by his employer. Comparing the flight training to the skills required of an air traffic controller, the Tax Court found a direct and proximate relationship between the education and the taxpayer's actual work skills.\(^ {221}\) Explaining the requisite relationship between education and a taxpayer's work skills, the Tax Court stated:

> Whether education maintains or improves skills required by the taxpayer in his employment must be determined from all the facts and circumstances involved . . . Petitioner has the burden

\(^{216}\) Reg. § 1.162-5(a)(1).
\(^{217}\) Reg. § 1.162-5(a)(2).
\(^{218}\) Reg. § 1.162-5(b)(2).
\(^{219}\) Reg. § 1.162-5(b)(3).
\(^{220}\) *Galbreath v. Commissioner*, 44 T.C.M. (CCH) 1163 (1982).
\(^{221}\) Id. at 1165.
Virginia Tax Review

of proof to establish that he is entitled to such deductions . . . . In order to satisfy this burden, petitioner must show that there was a direct and proximate relationship between the flight training courses taken by him and the skills required in his employment as an air traffic controller . . . . A precise correlation is not necessary, and the educational expenditure need not be for training which is identical to petitioner's prior training so long as it enhances existing employment skills.\(^{222}\)

In contrast, education which merely enhances a taxpayer's general competence is not deemed to maintain or improve the taxpayer's work skills because such education is not directly and proximately related to the taxpayer's specific work skills.\(^ {223}\) For example, *McAuliffe v. Commissioner* involved an appellate defense attorney in the United States Army who argued cases before military courts, wrote briefs and did other legal work.\(^ {224}\) While employed, the taxpayer voluntarily pursued an English Masters program at a university.\(^ {225}\) Arguably, the education enhanced the taxpayer's general competence and job performance by making him more articulate and improving his writing ability. However, the Tax Court found that the education only remotely related to the taxpayer's specific work skills and did not maintain or improve the taxpayer's work skills within the meaning of the Current Regulations.\(^ {226}\)

Finally, not all education in the taxpayer's general field of employment is necessarily treated as directly and proximately

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\(^{222}\) *Id.* See also *Kosmal v. Commissioner*, 39 T.C.M. (CCH) 651 (1979), aff'd, 670 F.2d 842 (9th Cir. 1982) (holding that Spanish lessons taken by deputy district attorney who frequently dealt with witnesses and victims who spoke Spanish bore a direct and proximate relationship with his work duties).

\(^{223}\) See *Bradley v. Commissioner*, 54 T.C. at 220; *Carroll v. Commissioner*, 51 T.C. 213, 216 (1968), aff'd, 418 F.2d 91 (7th Cir. 1969); *McEneaney v. Commissioner*, 46 T.C.M. (CCH) 453, 455 (1983); *Betz v. Commissioner*, 30 T.C.M. (CCH) 119 (1971). For a further discussion of *Carroll*, see infra notes 405-17. But see *Kim v. Commissioner*, 28 T.C.M. (CCH) 671 (1969) (courses taken by Korean-born insurance claims adjuster which improved his English, as well as his understanding of American finance and governmental operations, were found to maintain or improve the taxpayer's work skills within the meaning of the regulations).

\(^{224}\) *McAuliffe v. Commissioner*, 40 T.C.M. (CCH) 420 (1980).

\(^{225}\) *Id.* at 421.

\(^{226}\) *Id.* at 421-22.
related to his specific work skills. For example, *Heffernan v. Commissioner* involved a general accounting specialist in the Air Force who voluntarily pursued an MBA. Because the Tax Court found that the courses taken by the taxpayer in the graduate program were far more complex than his simple accounting duties, it held that the education did not maintain or improve the taxpayer's specific work skills within the meaning of the Current Regulations.

b. Education Required by the Taxpayer's Employer or by Law or Regulation as a Condition to Retaining an Established Employment Relationship, Status or Rate of Compensation

The Current Regulations also treat educational costs as potentially deductible if the underlying education is the minimum education necessary to meet the express requirements of the taxpayer's employer or applicable law or regulation as a condition to retain an established employment relationship, status or rate of compensation. For this purpose, the "express requirements" must be more than rules or guidelines encouraging the taxpayer to pursue some type of education. In addition, the education must be a requirement at the time the taxpayer pursues such education.

For example, *Kinch v. Commissioner* involved a navigator on career reserve status with the Air Force. Such status entitled the taxpayer to a 20-year active duty career with mandatory retirement in 1973. The only way the taxpayer could continue to serve

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229 *Id.* at 87. See also *Lee v. Commissioner*, 723 F.2d 1424, 1427 (9th Cir. 1984) (finding that helicopter lessons taken by commercial pilot were not sufficiently related to his employment skills).
230 See Reg. § 1.162-5(c)(2).
231 See Reg. § 1.162-5(a)(2).
232 *See Kinch v. Commissioner*, 30 T.C.M. (CCH) 502, 504 (1971); Rev. Rul. 61-133, 1961-2 C.B. 35 (ruling that college courses taken by an Army Captain in subject areas of functional importance to the military profession reflected a goal of his employer and not a requirement).
235 *Id.*
beyond 1973 was to attain a permanent appointment as an officer. Although the Air Force did not formally require its officers to obtain a college degree, it did encourage them to do so. The taxpayer believed that the Air Force would award him a permanent appointment only if he obtained a college degree. In fact, after the taxpayer obtained a baccalaureate degree, the Air Force appointed him to the permanent rank of captain.

The taxpayer argued that his educational costs were deductible under the Current Regulations because the underlying education was essential to retain his employment beyond 1973. Rejecting this argument, the Tax Court stated:

As the regulation states, a requirement that one achieve certain educational goals to retain employment must be an express one . . . . The facts only indicate that . . . the Air Force had a policy of encouraging officers without degrees to obtain them, and the Air Force would go to great lengths to implement this policy including the granting of extended leaves of absence with pay . . . . From the mere fact that additional education was encouraged by his employer or that such education would be helpful to him, we cannot conclude that [the taxpayer] was pursuing his education to satisfy an express requirement of his employer.

Similarly, an educational requirement imposed by applicable law or regulation must be current, enforceable law. Raines v. Commissioner involved a taxpayer who was certified as a respiratory therapist at a time when local law did not impose an educational requirement. Later, the California legislature

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236 Id. at 503.
237 Id.
238 Id.
239 Id.
240 Id. at 504.
241 Id. See also Baker v. Commissioner, 30 T.C.M. (CCH) 1192 (1971) (holding that education considered by the Air Force as one of the criteria for promotion was not a "requirement" within the meaning of the regulation in the absence of an express or implied requirement).
243 Id. at 220.
considered the mandatory licensing of respiratory therapists that would require an established respiratory therapist with three years of experience to obtain a bachelor's degree.\textsuperscript{244} Based on the possibility of enactment, the taxpayer enrolled in college.\textsuperscript{245} The Tax Court held that the education requirement was merely proposed legislation and not yet the law, and therefore not within the meaning of the Current Regulations.\textsuperscript{246}

Finally, under the Current Regulations, the education must be the \textit{minimum} education necessary to meet the express requirements for retention of the taxpayer's established employment arrangement, status or rate of compensation.\textsuperscript{247} For example, \textit{Fleischer v. Commissioner}\textsuperscript{248} involved a taxpayer employed at a hotel to demonstrate hypnosis to the guests. Due to potential liability, the taxpayer's employer subsequently required him to qualify as a hypnotist.\textsuperscript{249} In response, the taxpayer pursued education leading to a doctoral degree in general psychology.\textsuperscript{250} Eventually, the taxpayer became a trainee in psychology and hypnosis at a university medical center.\textsuperscript{251}

The taxpayer argued that the education qualified him to become a hypnotist as required by his employer to retain his job.\textsuperscript{252} The Tax Court disagreed, stating that "the cost, intensity, scope and duration of [the taxpayer's] education far exceeded that required by either the demands of his job or those of his employer."\textsuperscript{253}

\textsuperscript{244} Id.
\textsuperscript{245} Id.
\textsuperscript{246} Id. at 221.
\textsuperscript{247} Reg. § 1.162-5(c)(2).
\textsuperscript{248} \textit{Fleischer v. Commissioner}, 30 T.C.M. (CCH) 699 (1971).
\textsuperscript{249} Id. at 700.
\textsuperscript{250} Id.
\textsuperscript{251} Id.
\textsuperscript{252} Id. at 703.
\textsuperscript{253} Id.
c. Deductible Educational Costs Must be Paid or Incurred While Carrying on a Trade or Business

As required of any deductible expense, otherwise deductible educational costs must relate to "the present 'carrying on' of an existing trade or business."254 A "trade or business" is "all means of gaining a livelihood by work."255 Therefore, to deduct educational costs, a taxpayer must be carrying on a trade or business while she pursues her education.256 Determining whether a taxpayer is carrying on a trade or business is a question of fact.257

On occasion, a taxpayer may pursue education prior to entering a trade or business. Obviously, a taxpayer preparing to enter a trade or business cannot be carrying on that trade or business. Therefore, the taxpayer may not deduct those educational costs.258 This is true even if the taxpayer is a member in good standing in her profession before actually starting her trade or business.259

In another situation, a taxpayer may pursue education during a transition period between employment positions. Here, the issue

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255 Trent v. Commissioner, 291 F.2d 669, 671 (2d Cir. 1961). But see Wassenaar v. Commissioner, 72 T.C. 1195 (1979). In that case, the taxpayer attended law school after being employed in numerous positions. The taxpayer argued that when he attended law school he was in the trade or business of "rendering services to employers for compensation." Id. at 1201. The Tax Court rejected this characterization of a trade or business. Id.
256 See Cannon v. Commissioner, 40 T.C.M. (CCH) 541 (1980) (whether being a member in good standing in a profession establishes that a person is carrying on a trade or business); Sherman v. Commissioner, 36 T.C.M. (CCH) 1191 (1977) (whether a person is carrying on a trade or business during a transition period between positions).
258 See Gulick v. Commissioner, 43 T.C.M. (CCH) 490 (1982) (Marine Corps retiree pursued an engineering degree as a full-time student); Casey v. Commissioner, 30 T.C.M. (CCH) 60 (1971) (taxpayer enrolled in a teachers' college the summer prior to becoming a teacher). See also Kohen v. Commissioner, 44 T.C.M. (CCH) 1518, 1520 (1982). In Kohen, the taxpayer began to practice law immediately after completing an LL.M program. The taxpayer argued that he was entitled to deduct the cost of the program because he was carrying out a trade or business in the same year as the education. Id. at 1520. The Tax Court disagreed, stating that "... the statute has consistently been construed to require activity prior to the outlay for education." Id.
259 See Goldenberg v. Commissioner, 65 T.C.M. (CCH) 2338 (1993); Kohen v. Commissioner, 44 T.C.M. (CCH) 1518 (1982); Randick v. Commissioner, 35 T.C.M. (CCH) 195 (1976). In each case, the taxpayer was admitted to at least one state bar but had not actually practiced law prior to attending an LL.M program. The Tax Court in each case held that being a member in good standing was not the same as being in a trade or business.
is whether a taxpayer is carrying on a trade or business during this transition period. According to the Service, a taxpayer continues to carry on a trade or business during a transition period if such period is "temporary." Generally, the Service considers an absence from active employment for a year or less as temporary. However, the Tax Court has refused to apply the Service's one year guideline as an absolute rule of law. Instead, the Tax Court has treated each case as a question of fact determined on its own merits.

d. Deductible Educational Cost Must be an Expense Not a Capital Expenditure

Finally, as is required of any deductible expense, potentially deductible educational costs must be an "expense" rather than a "capital expenditure." An expense is an item of short duration

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261 Id. See also P.L.R. 91-12-003 (Dec. 18, 1990) (attorney who temporarily suspended his practice for less than a year to attend a graduate tax program treated as carrying on a trade or business during such year).
262 See Hitt v. Commissioner, 37 T.C.M. (CCH) 333 (1978) (holding that a taxpayer continued to be in the trade or business as a nurse educator during the three year period in which she pursued a doctoral degree); Picknally v. Commissioner, 36 T.C.M. (CCH) 1292 (1977) (holding that taxpayer who resigned his position as an elementary school principal to pursue a Ph.D. degree over a three year period continued to be in the trade or business of being a teacher or educational administrator even though he held no teaching position during that period).
263 See Goldstein v. Commissioner, 41 T.C.M. (CCH) 1016 (1981). In Goldstein, the Tax Court applied the following factors to determine that a taxpayer who left teaching for thirteen years was not carrying on the trade or business of being a "teacher" when she pursued a Master of Science degree in education:
   (1) she left teaching for non-business reasons;
   (2) she did not intend to return promptly to teaching;
   (3) she did not return to teaching for a long time; and
   (4) she did not seek a teaching position for a long time.
   41 T.C.M. (CCH) at 1019. See also Hitt, 37 T.C.M. (CCH) at 334; Lenihan v. Commissioner, 36 T.C.M. (CCH) 1540, 1541 (1977) (holding that "[w]hen a taxpayer leaves his trade or business for a prolonged period of study with no apparent continuing connection with his former job or any clear indication of an intention to actively carry on the same trade or business upon completion of study, the taxpayer is not 'carrying on' his trade of [sic] business while attending school").
264 See I.R.C. § 162(a). For a further discussion of section 162(a), see infra notes 572-84 and accompanying text.
which relates to the gross receipts generated in the current year. Capital expenditures are items of longer duration which relate to gross receipts generated over several years. Under Code section 162(a), a taxpayer may not currently deduct the cost of a capital expenditure. Instead, a taxpayer must depreciate or amortize such cost over the useful life of the expenditure.

Arguably, education which maintains or improves a taxpayer's work skills or meets a requirement of continued employment provides a benefit extending beyond one taxable year. Indeed, such benefit should extend over the taxpayer's entire career or lifetime. However, as case law has interpreted the Current Regulations, educational costs are either currently deductible or not deductible at all. Therefore, under current law, whether deductible educational costs should be currently deducted under I.R.C. section 162(a) or amortized as a capital expenditure appears to be a non-issue.

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265 See Reg. § 1.162-3 (1958) relating to the current deductibility under I.R.C. § 162(a) of the cost of materials ("Taxpayers . . . should include in expenses the charges for materials and supplies only in the amount they are actually consumed and used in operation during the taxable year . . . "); Reg. § 1.162-6 (1958) relating to the current deductibility of professional expenses ("Amounts currently paid or accrued for books, furniture, and professional instruments and equipment, useful life of which is short, may be deducted.").


267 See I.R.C. §§ 167, 168. For further discussion of section 167, see infra notes 467-68 and accompanying text.


269 See Damm v. Commissioner, 41 T.C.M. (CCH) 1359, 1363 n.9 (1981). Commenting on the all-or-nothing nature of deductible educational costs, the Tax Court observed that the taxpayer's education "clearly may be expected to be useful in his career as teacher for many years after the expenses were made. Nevertheless, neither side disputes the now-or-never status of the educational expenses deduction." Id. But see Reg. § 1.162-5(b)(1) (nondeductible educational costs characterized as "an inseparable aggregate of personal and capital expenditures." (emphasis added). The characterization of educational costs as "capital" suggests that they are not "expenses.").
D. How Otherwise Deductible Educational Costs Are Converted Into Nondeductible Personal Expenses

1. The Minimum Educational Requirement of the Taxpayer's Chosen Trade or Business

a. What is a Minimum Educational Requirement of a Trade or Business?

According to the Current Regulations, otherwise deductible educational costs are converted into nondeductible personal expenses if the education pursued by the taxpayer is the minimum educational requirement of her chosen trade or business. In this regard, the Current Regulations characterize any education required or helpful to the taxpayer in entering her chosen trade or business as a minimum educational requirement of such trade or business. For example, suppose that a taxpayer decides to become a realtor. Since the potential realtor must first pass a real estate examination, courses taken to prepare for such examination are a minimum educational requirement of that profession. As a result, the cost of real estate courses is a nondeductible personal expense.

The scope of the minimum educational requirement is broad. Under the Current Regulations, any education imposed as a condition of initial employment is a minimum educational requirement even if other employers in the same profession do not impose such a requirement. For example, Antuna v. Commissioner involved a taxpayer hired by a hospital as a pediatric social worker. Although her employer required her to obtain a master's degree in social work (M.S.W.), other employers of pediatric social workers did not require an M.S.W. Moreover, the taxpayer also

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270 See Reg. § 1.162-5(b)(2).
271 Id.
272 Id.
274 Id.
worked part-time as a social worker for a different employer who did not require the degree.\textsuperscript{275} 

The Tax Court held that any educational requirement imposed as a prerequisite for employment by a particular employer for a particular job is a minimum educational requirement even if other employers in the same field did not impose such a requirement.\textsuperscript{276} Hence, the Tax Court determined that obtaining an M.S.W. was the minimum educational requirement for the taxpayer's position with the hospital.\textsuperscript{277}

\textit{i. A Taxpayer Hired to a Position Has Not Necessarily Met the Minimum Educational Requirements to Qualify for that Position}

As discussed above, the Current Regulations treat the cost of education which meets the minimum educational requirements for the taxpayer's chosen employment position as a nondeductible personal expense.\textsuperscript{278} However, in some cases, a taxpayer may work in her chosen employment while simultaneously pursuing her education. To illustrate, suppose an employer hires the taxpayer and, as a condition of her employment, the taxpayer agrees to pursue a certain type of education. Thus, once hired to the position, the taxpayer must pursue her education to retain her position. In this case, perhaps, the taxpayer could argue that being hired prior to pursuing the education means that (1) there is no minimum educational requirement for the position; or (2) if there is a minimum educational requirement, her hiring means that she already met this requirement and that the additional education required is necessary to retain her position and not as a minimum educational requirement.

The Current Regulations address this situation by stating that being hired and working in an employment position does not necessarily establish that the taxpayer has met the minimum

\textsuperscript{275} Id.
\textsuperscript{276} Id. at 1780.
\textsuperscript{277} Id.
\textsuperscript{278} See Reg. \textsection 1.162-5(b)(2).
The Deductibility of Educational Costs

educational requirements for that position. Thus, any education pursued as a condition of initial employment is a minimum educational requirement of such employment. For example, Davidson v. Commissioner involved a taxpayer employed as an accountant, a position that required a college degree or two years of experience. Although the taxpayer did not initially meet these requirements, he was hired and worked as an accountant as he pursued the required degree. Holding that the education pursued by the taxpayer was the minimum educational requirement for his position, the Tax Court reasoned:

The fact that an individual . . . is already performing service in an employment status does not establish that he has met the minimum educational requirement for qualification in that employment. The minimum education necessary to qualify for a position must be determined from a consideration of such factors as the requirements of the employer, the applicable law and regulations, and the standards of the profession, trade or business involved.

ii. Educational Requirement Imposed on the Taxpayer After She is Hired

A taxpayer who met the minimum educational requirements of her chosen position when initially hired may be required to pursue additional education because her employer later changed the minimum educational requirements for that position. Under these circumstances, the Current Regulations treat a taxpayer who initially met the minimum educational requirements of her position as continuing to meet those requirements in spite of the subsequent changes. As a result, the taxpayer may deduct the cost of the

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279 See Reg. § 1.162-5(b)(2)(i).
280 Davidson v. Commissioner, 43 T.C.M. (CCH) 743, 743-44 (1982).
281 Id. at 743.
282 Id. at 745. See also Browne v. Commissioner, 73 T.C. 723 (1980); Kuh v. Commissioner, 46 T.C.M. (CCH) 1405 (1983); Antuna v. Commissioner, 36 T.C.M. (CCH) 1778 (1977); Hering v. Commissioner, 33 T.C.M. (CCH) 1329 (1974).
283 See Reg. § 1.162-5(b)(2).
required education because it is an express condition of continued employment.\textsuperscript{284}

For example, \textit{Sumner v. Commissioner} involved a taxpayer who initially met the minimum educational requirements of a welder.\textsuperscript{285} Later, new state regulations required welders to become certified.\textsuperscript{286} To comply with these regulations, the taxpayer pursued the education necessary for certification.\textsuperscript{287} The Tax Court determined that the taxpayer pursued the education as required by state regulation to retain his position.\textsuperscript{288} Since the taxpayer met the minimum educational requirements of his position prior to the change in regulations, he was treated as continuing to meet them in spite of the subsequent change.\textsuperscript{289}

\textit{b. The Current Regulations Do Not Favor Teachers Over Other Taxpayers in Determining Whether Education is a Minimum Educational Requirement}\textit{ }

As previously discussed, the Current Regulations treat the cost of education necessary to qualify a taxpayer in her chosen trade or business as a nondeductible personal expense. However, exclusively for taxpayers in the field of education, the Current Regulations provide specific guidelines for determining "[t]he minimum educational requirements for qualification of a particular individual in a position in an educational institution."\textsuperscript{290} As discussed below, these special guidelines do not favor teachers over other taxpayers.

Although the Current Regulations provide rules regarding the deductibility of educational costs which apply to all taxpayers,\textsuperscript{291} they inexplicitly set forth detailed guidelines and examples of how the rules apply to determine the minimum educational

\textsuperscript{284} See \textit{Sumner v. Commissioner}, 44 T.C.M. (CCH) 1233, 1236 (1982).
\textsuperscript{285} Id. at 1234.
\textsuperscript{286} Id.
\textsuperscript{287} Id.
\textsuperscript{288} Id. at 1236.
\textsuperscript{289} Id. See also Rev. Rul. 68-580, 1968-2 C.B. 72.
\textsuperscript{290} Reg. § 1.162-5(b)(2)(ii).
\textsuperscript{291} See Reg. § 1.162-5.
requirements of an educational position.\footnote{See Reg. §§ 1.162-5(b)(2)(ii), (iii).} In contrast, for all non-educational professions, the Current Regulations provide only general guidelines.\footnote{See Reg. § 1.162-5(b)(2)(i). For example, for any non-teaching trade or business, the Current Regulations state that whether education meets the minimum educational requirements “must be determined from a consideration of such factors as the requirements of the employer, the applicable law and regulations, and the standards of the profession, trade, or business involved.” Id. However, the Current Regulations do provide one example illustrating that law school courses and bar review courses are minimum educational requirements for qualification as a lawyer. Reg. § 1.162-5(b)(2)(iii).}

Several cases have raised the issue as to whether these specific guidelines are intended to favor educators over other taxpayers. For example, \textit{Jungreis v. Commissioner} involved a taxpayer who was hired as a graduate teaching assistant while he pursued a Ph.D.\footnote{55 T.C. 581 (1970).} Graduate teaching assistants did not vote at or attend faculty meetings\footnote{Id. at 583.} or have other benefits of regular faculty members.\footnote{Id. at 585.} The only education required of a graduate teaching assistant was a bachelor’s degree, whereas the education required of a regular faculty member was a Ph.D.\footnote{Id. at 584.}

At issue in \textit{Jungreis} was the meaning of the following sentence from the Current Regulations: “The minimum educational requirements for qualification of a particular individual in a position in an educational institution is the minimum level of education . . . which . . . is normally required of an individual initially employed in such a position.”\footnote{Id. at 587 (quoting Reg. § 1.162(b)(2)(ii)).} Relying on this sentence, the taxpayer argued that the costs of attaining his Ph.D. were deductible. Since the taxpayer met the minimum educational requirements of a graduate research assistant when he was first hired by the university, the taxpayer reasoned that he then met the minimum educational requirements for a position at an educational institution.\footnote{Id. at 589.} The Current Regulations state that once an individual meets the minimum educational requirements for a position at an educational institution, those requirements are
always considered met by him. The taxpayer concluded that since he met the minimum educational requirements of a graduate research assistant when he was hired, the Ph.D. he pursued was not a minimum educational requirement.

The Tax Court rejected the taxpayer's interpretation of the Current Regulations. According to the Tax Court, meeting the minimum requirements for a position at an educational institution means a "permanent position." Therefore, this provision of the regulation did not apply to the present case because the taxpayer's graduate assistant position was only a temporary position.

In support of its interpretation, the Tax Court noted that the same subsection of Current Regulations cited by the taxpayer provides that one is a member of the faculty if (a) he has tenure, (b) the institution makes contributions for him in a retirement plan, or (c) he has a faculty vote. In this case, because none of these criteria applied to the taxpayer's graduate teaching assistant position, the taxpayer had not yet attained a permanent position in an educational institution within the meaning of the Current Regulations. Therefore, the Tax Court treated the Ph.D. pursued by the taxpayer as the minimum educational requirement to become a permanent faculty member and denied him a deduction for his educational costs.

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300 Id.
301 Id.
302 Id.
303 Id.
304 Id. at 590 (quoting Reg. § 1.162(b)(2)(ii)).
305 Id.
306 Id. at 590-91. In support of its holding, the Tax Court also cited Treasury Regulation section 1.162-5(b)(2)(iii), which provides a factually similar example: where a temporary instructor at a university takes graduate courses required to obtain a graduate degree to become a faculty member, such courses are the minimum educational requirements for that position. Id. at 590. See also Davis v. Commissioner, 65 T.C. 1014 (1976); Hering v. Commissioner, 33 T.C.M. (CCH) 1329 (1974) (holding that education qualifying an individual with a provisional teaching certificate for a standard teaching certificate was a minimum educational requirement for qualification as a "teacher").

But see Damm v. Commissioner, 41 T.C.M. (CCH) 1359 (1981). In that case, the taxpayer, who had been employed as a university lecturer for 2½ years, pursued a doctoral degree as a full-time student. Id. at 1360. Thereafter, he resumed his position as lecturer and was eventually appointed to the position of associate professor. Id. at 1361. Distinguishing this case from Jungreis, the Tax Court held that the doctoral degree was not a minimum education requirement of an associate professor because the taxpayer's years as
Another case, *Diaz v. Commissioner*, 70 T.C. 1067 (1978), raised the issue of whether a taxpayer who met the minimum educational requirements of a permanent position in an educational institution at a level below a certified teacher could deduct the cost of education necessary to become a certified teacher. In *Diaz*, the taxpayer held the permanent position of an educational associate (a position similar to a teaching assistant) in a public school system. The taxpayer aspired to become a certified teacher, and pursued a baccalaureate degree to meet the local law requirements.

Denying a deduction for the taxpayer's educational costs, the Tax Court found that holding a permanent position as an educational associate did not mean that she met the minimum educational requirements of a teacher. Although the taxpayer performed many tasks and activities performed by teachers, local law prohibited an individual without a teacher's certificate to perform duties "essential to the teaching function." Under these circumstances, the Tax Court would not allow the taxpayer to deduct the cost of the education necessary to become a teacher, even though she had already met the minimum educational requirements for a permanent position at an educational institution.

In the final analysis, the specific guidelines for determining whether taxpayers in the field of education have met the minimum educational requirements for a position in an educational institution do not favor such taxpayers over other taxpayers in different fields. As the case law indicates, these guidelines do not allow a taxpayer who has met an educational requirement at an educational institution for a temporary position or a permanent

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a lecturer counted toward tenure and in all other ways the taxpayer was treated like a regular faculty member. *Id.* at 1364-66.


*Id.* at 1069.

*Id.* at 1071.

*Id.*

*Id.* at 1075.

*Id.* at 1076. See also *Baist v. Commissioner*, 56 T.C.M. (CCH) 778 (1988); *Kuh v. Commissioner*, 46 T.C.M. (CCH) 1405.
position below a teacher to deduct the cost of education necessary to achieve a permanent position or the higher position of teacher.

2. Education Which Potentially Qualifies the Taxpayer to Enter Into a New Trade or Business

The Current Regulations also treat otherwise deductible educational costs as nondeductible personal expenses if the education pursued by the taxpayer qualifies her for a new trade or business.\textsuperscript{313} For example, suppose that a taxpayer is a C.P.A. with a substantial part her practice involving Tax Court litigation. To improve her legal skills, the taxpayer decides to attend law school. Although the legal education is directly and proximately related to this taxpayer's work skills, the Current Regulations treat its cost as a nondeductible personal expense, because law school could lead to qualification as a lawyer.\textsuperscript{314} This is the result even if the possibility of the taxpayer actually becoming a lawyer is remote.\textsuperscript{315}

In another context, an employee may be required to pursue an educational program to retain her employment. If such education also qualifies the taxpayer for a new trade or business, then the Current Regulations characterize its cost as a nondeductible personal expense. For example,\textit{Malek v. Commissioner} involved a taxpayer who performed a myriad of duties for her employer, a psychology-based consulting firm.\textsuperscript{316} Approximately five years after her initial hire, the taxpayer was required by her employer to obtain a college degree in order to retain her position.\textsuperscript{317} Subsequently, the taxpayer attended college and obtained a bachelor of arts degree, with a major in professional communications/management.\textsuperscript{318}

Although the Tax Court acknowledged that the taxpayer's employer required her to pursue the additional education to retain her job, the Tax Court determined that her degree qualified her to

\begin{footnotesize}
313 See Reg. § 1.162-5(b)(3).
314 See Reg. § 1.162-5(b)(3)(i),(ii), Example 2.
316 50 T.C.M. (CCH) 792, 793 (1985).
317 \textit{Id}.
318 \textit{Id}. at 794.
\end{footnotesize}
enter many new trades or businesses. The Tax Court based its finding on an extract from Occupational Outlook for College Graduates, a publication issued by the Bureau of Labor Statistics. The Tax Court reasoned:

A cursory examination of the entire publication reveals that Malek's bachelor of science degree... would lead to qualifying her in many trades or businesses, among them the following: advertising workers, bank officers, college student personnel workers, credit managers, marketing research workers, purchasing agents, insurance claim representatives, and insurance underwriters, as well as a variety of counseling occupations.

Since the taxpayer's degree potentially qualified her for numerous trades or businesses, the Tax Court treated the taxpayer's educational costs as nondeductible personal expenses.

a. Education Which, Combined with Other Educational or Non-Educational Requirements, Potentially Qualifies the Taxpayer For a New Trade or Business

Under the Current Regulations, the disallowance for educational costs extends beyond the cost of education which directly qualifies the taxpayer to enter into a new trade or business. This is because the Current Regulations define education which qualifies the taxpayer to enter into a new trade or business as any education which is "part of a program of study... which will lead to qualifying him in a new trade or business." The courts interpret the phrase "part of a program of study" to include each part of an educational program even if the taxpayer never completes the

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319 Id. at 795-96.
320 Id. at 796.
321 Id. See also Zeidler v. Commissioner, 71 T.C.M. (CCH) 2603 (1996); Meredith v. Commissioner, 65 T.C.M. (CCH) 2876 (1993).
322 Malek, 50 T.C.M. at 797.
323 Reg. § 1.162-5(b)(3).
324 See Vetrick v. Commissioner, 628 F.2d 885 (5th Cir. 1980), affg 37 T.C.M. (CCH) 392 (1978); Rance v. Commissioner, 45 T.C.M. (CCH) 956 (1983) (considering each separate year of law school education as part of the course of study and rejecting the taxpayer's argument
program.\textsuperscript{325} In addition, the phrase "lead to qualifying" includes any education which, if combined with additional educational or non-educational requirements, could potentially qualify the taxpayer for a new trade or business.\textsuperscript{326}

In each of the following situations, the Tax Court found the education to be "part of a program of study . . . which will lead to qualifying him for a new trade or business" regardless of whether the taxpayer actually pursued the additional requirements necessary to enter into a new trade or business:

1. A claims representative for an insurance company, who worked with the in-house legal department, attended law school. After receiving a law degree and passing the bar, he became legal counsel of record for the company.\textsuperscript{327} Here, the taxpayer became a lawyer after satisfying all of the requirements necessary to become one.

2. A C.P.A. who worked in the tax department of an accounting firm attended law school to improve his accounting and tax skills. Although he passed the state bar, he never intended to practice law.\textsuperscript{328} Here, the taxpayer never became nor intended to become a lawyer even though he completed all of the steps necessary to become one.

3. An air traffic controller took a limited amount of flight training courses to improve his work skills. If the taxpayer had taken some additional flight training, he could have qualified to become a commercial pilot. However, the taxpayer never took the additional flight training and there was only a remote possibility

\textsuperscript{325} See Wu v. Commissioner, 61 T.C.M. (CCH) 2088 (1991) (two years of law school treated as "part of a program of study" even though (1) it was questionable whether the taxpayer would receive credit for those years, and (2) the taxpayer dropped out of the law school without receiving a degree).

\textsuperscript{326} For example, a person who attains a J.D. is not qualified to practice law. As additional educational and non-educational steps, she might take a bar review course and then sit for a state bar examination to qualify as a lawyer. See Rehe v. Commissioner, 40 T.C.M. (CCH) 975 (1980).

\textsuperscript{327} McDermott v. Commissioner, 36 T.C.M. (CCH) 144, 145 (1977); see also Stuart v. Commissioner, 42 T.C.M. (CCH) 405 (1981).

\textsuperscript{328} O'Donnell v. Commissioner, 62 T.C. 781, 782 (1974); see also Connelly v. Commissioner, 30 T.C.M. (CCH) 376 (1971).
that the taxpayer would ever do so to become a commercial pilot.\textsuperscript{329} Here, the taxpayer did not complete all of the steps necessary to become a commercial pilot and never became one.

\textit{b. What is a New Trade or Business?}

As stated above, the Current Regulations treat the cost of education which is "part of a program of study . . . which will lead to qualifying him in a new trade or business" as a nondeductible personal expense.\textsuperscript{330} However, the Current Regulations do not define the term "new trade or business." To provide a guideline for determining whether the taxpayer has qualified for a new trade or business, the Tax Court developed a "commonsense" approach.\textsuperscript{331}

In application, the commonsense approach compares the types of tasks and activities the taxpayer's educational level qualified her to do before pursuing the education with the tasks and activities the taxpayer is qualified to do after pursuing the education.\textsuperscript{332} If there is a significant difference between the tasks and activities the taxpayer can perform before and after she pursued the education, the education qualifies her for a new trade or business.\textsuperscript{333} This is true even if the taxpayer never actually performs any of those new tasks and activities.\textsuperscript{334}

The simplest illustration of the commonsense approach involves two obviously different trades or businesses. Suppose that a practicing doctor also acts as an expert witness in medical

\textsuperscript{329} Hinton \textit{v. Commissioner}, 44 T.C.M. (CCH) 1160 (1982). The Tax Court articulated its holding as follows:

We sympathize with [the taxpayer's] position in this case since we do not question the fact that the flight training courses in question helped him become a better air traffic controller. We also recognize that in today's job market it is highly unlikely that [the taxpayer], without additional flight hours, could embark on a career as a commercial pilot. The situations in which [the taxpayer] could earn a livelihood are limited, and becoming a commercial pilot may be a detrimental career move for him to make. Nevertheless, his commercial pilot certificate enables him to earn compensation and engage in a trade or business for which he was previously unqualified. \textit{Id.} at 1163. \textit{See also Rehe \textit{v. Commissioner}}, 40 T.C.M. (CCH) 975 (1980).

\textsuperscript{330} Reg. § 1.162-5(b)(3).

\textsuperscript{331} \textit{See Glenn \textit{v. Commissioner}}, 62 T.C. 270 (1974).

\textsuperscript{332} \textit{Id.} at 275.

\textsuperscript{333} \textit{Id.}

\textsuperscript{334} \textit{Id.} at 276-77. \textit{See also Rehe \textit{v. Commissioner}}, 40 T.C.M. (CCH) 975.
malpractice cases. The doctor attends law school to improve his skills as an expert witness by learning the substantive and procedural aspects of law. Prior to attending law school, the taxpayer, as a licensed doctor, could practice medicine but not law. After law school, the taxpayer could potentially qualify (if he successfully passed the bar examination) to practice law. Under the commonsense approach, a doctor and a lawyer are clearly separate trades or businesses. Therefore, the taxpayer would not be entitled to deduct the cost of law school.\textsuperscript{335}

The Tax Court has also applied the commonsense approach to find separate trades or businesses within the same general field.\textsuperscript{336} For example, \textit{Glenn v. Commissioner} involved a licensed public accountant who took a certified public accountant review course to prepare for a C.P.A. examination.\textsuperscript{337} At issue was whether the review course was part of a course of study leading the taxpayer to qualify for a new trade and business. Addressing this issue, the Tax Court applied the commonsense approach to determine whether a licensed public accountant and a C.P.A. were two different trades or businesses. In so doing, the Tax Court compared the tasks and activities that state law allowed a licensed public accountant to do with those it allowed a C.P.A. to do.\textsuperscript{338} For example, the applicable state law allowed a C.P.A., but not a licensed public accountant, to advise taxpayers on federal and state tax statutes and to represent taxpayers before taxing authorities.\textsuperscript{339} According to the Tax Court, these differences made the practice of a C.P.A. much broader than the practice of a licensed public accountant.\textsuperscript{340} The Tax Court also noted that a C.P.A. held a higher public status and represented a higher level of professional competence.\textsuperscript{341} As a result, a C.P.A.'s opinion and certification

\textsuperscript{335} Reg. § 1.162-5(b)(3)(ii), Example (2).
\textsuperscript{336} See \textit{Dierker v. Commissioner}, 68 T.C.M. (CCH) 535 (1994) (holding that because the work of a registered landscape architect differs from that of an unregistered landscape architect, educational expenses were not deductible).
\textsuperscript{338} \textit{Id.} at 275.
\textsuperscript{339} \textit{Id.} at 275-76.
\textsuperscript{340} \textit{Id.} at 276.
\textsuperscript{341} \textit{Id.}
carried more value than that of a licensed public accountant.\textsuperscript{342} These significant differences in tasks and activities led the Tax Court to find a C.P.A. to be a different (and, thus, new) trade or business from a licensed public accountant.\textsuperscript{343} Accordingly, the Tax Court treated the taxpayer’s educational costs as nondeductible personal expenses.\textsuperscript{344}

In the most extreme application of the commonsense approach, courts have found the same profession practiced in different states to be separate trades or businesses. For example, \textit{Sharon v. Commissioner}\textsuperscript{345} involved a taxpayer licensed to practice law in New York. After accepting a position with the Internal Revenue Service in California, the taxpayer decided that membership in the California bar would be helpful in his employment.\textsuperscript{346} The taxpayer incurred expenses, including the cost of a bar review course, to gain admission to the California bar.\textsuperscript{347}

Applying the commonsense approach, the Tax Court found that a lawyer licensed to practice in California was a different trade or business than a lawyer licensed to practice in New York.\textsuperscript{348} Although the Tax Court acknowledged that the taxpayer was engaged in the “business of practicing law,” it also noted that before the taxpayer was admitted to the California bar “he could not appear either in the State courts of California, the Federal District Courts located there, nor otherwise act as an attorney outside the scope of his employment with the IRS.”\textsuperscript{349} Therefore, the Tax Court

\textsuperscript{342} \textit{Id.}

\textsuperscript{343} \textit{Id.} at 277. For additional examples of courts finding different trades or businesses in the same general field, see \textit{Siewert v. United States}, 500 F.Supp. 1076 (N.D. Texas 1980) (chiropractor held as a different trade or business than a medical doctor); \textit{Reisinger v. Commissioner}, 71 T.C. 568 (1979) (physician’s assistant held as a different trade or business than a licensed practical nurse); \textit{Hewett v. Commissioner}, 71 T.C.M. (CCH) 2350 (1996) (music therapist held as a separate trade or business than a professional pianist and piano teacher); \textit{Mason v. Commissioner}, 44 T.C.M. (CCH) 365 (1982) (flight engineer held as a different trade or business than a pilot); \textit{Antzoulatos v. Commissioner}, 34 T.C.M (CCH) 1426 (1975) (registered pharmacist held as a different trade or business than an intern pharmacist).

\textsuperscript{344} \textit{Glenn v. Commissioner}, 62 T.C. at 278.

\textsuperscript{345} \textit{Sharon v. Commissioner}, 66 T.C. 515 (1976), aff’d, 591 F.2d 1273 (9th Cir. 1978).

\textsuperscript{346} \textit{Sharon}, 66 T.C. at 519.

\textsuperscript{347} \textit{Id.}

\textsuperscript{348} \textit{Id.}

\textsuperscript{349} \textit{Id.} at 529.
found the tasks and activities that a licensed California lawyer could do in California to be significantly different from the tasks and activities that a lawyer without a California license could do in California. As a result, the Tax Court held that the taxpayer's bar review course was part of a course of study leading to his qualification for a new trade or business, and treated its cost as a nondeductible personal expense.

c. A Change in Duties or Pursuing a Specialty Within a Trade or Business Not Treated as a New Trade or Business

Within the scope of qualifying for a new trade or business, the Current Regulations do not treat a change of duties in an existing trade or business as a new trade or business. A change of duties is characterized by the Current Regulations as the same general type of work as is performed by the taxpayer in her present employment. As such, the Current Regulations allow a deduction for the cost of education which qualifies the taxpayer to perform new duties in the same general type of work.

For example, *Granger v. Commissioner* involved a taxpayer who worked at the lower management level of a retail food store. The taxpayer attended a food marketing management program at a university and received a Certificate in Food Marketing.

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350 Id. at 529-30.

351 Id. See also Vetrick v. Commissioner, 37 T.C.M. (CCH) 392 (1978), aff'd, 628 F.2d 885 (5th Cir. 1980). In that case, the taxpayer passed the Montana bar examination after two years of law school. The taxpayer established a law practice in Ohio limited to federal practice. Although the taxpayer regularly appeared in federal district court, Ohio state law barred a lawyer without a J.D. to practice in state courts. Id. at 393. Later, the taxpayer completed a third year of law school and received a J.D. Applying the commonsense approach, the Tax Court found that a lawyer qualified to practice law in state court was a different trade or business than a lawyer qualified to practice only in federal court. Id. at 394.

352 Reg. § 1.162-5(b)(3).

353 Id. The Current Regulations then state that all teaching and related duties are considered the same type of work.

354 See Granger v. Commissioner, 39 T.C.M. (CCH) 1158 (1980).

355 Id.
Management. The taxpayer was later promoted to the position of store manager.

The Tax Court determined that the courses taken by the taxpayer maintained or improved his current work skills, and did not qualify him for a new trade or business. The Tax Court noted that before the education and promotion, the taxpayer performed managerial duties on a substitute basis. After completing his education, the taxpayer became a manager and performed similar duties at a higher level of responsibility. As a result, the Tax Court allowed the taxpayer to deduct his educational costs.

Similar to a change in duties, the Current Regulations do not treat a specialty within a trade or business as a new trade or business. For example, Revenue Ruling 74-78 involved a dentist engaged in general practice. To specialize his practice, he pursued a postgraduate program in orthodontics. After completing the program, the taxpayer limited his practice to orthodontics. Ruling that a change of specialities within the same trade or business was not a new trade or business, the Service allowed the taxpayer to deduct his educational costs.

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356 Id.
357 Id. at 1159.
358 Id. at 1159-60. The Tax Court found that the taxpayer's education "bore a substantial and direct relationship to the skills he needed in his ascension in the field of retail food management." Id. at 1160.
359 Id.
360 Id.
361 Id. See also Gilliam v. Commissioner, 51 T.C.M. (CCH) 567, 571 (1986) (holding that college courses taken by a computer programmer to improve his chances for promotion did not qualify the taxpayer for a new trade or business; rather, the added management duties were merely a change of duties).
362 See Rev. Rul. 74-78, 1974-1 C.B. 44.
363 Id.
364 Id.
365 Id. See also Ruehmann v. Commissioner, 30 T.C.M. (CCH) 675, 679 (1971) (practicing lawyer pursued an LL.M. to develop a specialty); Reg. § 1.162-5(b)(3)(ii), Examples (3) and (4) (a refresher course of new developments in specialized fields of medicine does not qualify a general practitioner for a new trade or business and a psychiatrist who studies psychoanalysis does not qualify as a new trade or business).
d. Determining Whether Education Pursued by a Teacher Qualifies her to Enter into a New Trade or Business

i. Non-Application of Commonsense Approach to Teachers Allows Teachers to Deduct Certain Educational Costs Not Deductible by Non-Teachers

In certain situations, the courts do not apply the commonsense approach to determine whether education pursued by a teacher qualifies her for a new trade or business. In these instances, the Current Regulations favor teachers over non-teachers by allowing the latter group to deduct certain educational costs which non-teachers may not deduct.

This preferential treatment is the result of a more favorable standard used by the Current Regulations to determine whether education pursued by a teacher qualifies him for a new trade or business or simply a change of duties. Specifically, the Current Regulations state that "all teaching and related duties shall be considered to involve the same general type of work." The Current Regulations provide the following four examples of a teacher changing positions within the general educational field: (1) elementary to secondary school classroom teacher; (2) classroom teacher in one subject to classroom teacher in another subject; (3) classroom teacher to guidance counselor; and (4) classroom teacher to principal. These new positions are depicted by the Current Regulations as changes of duties rather than as new trades or businesses.

Because the Current Regulations treat all forms of teaching as within the same general field, the courts have not applied the commonsense approach in the following circumstances: (1) where the teacher has already met the minimum educational requirements of a permanent teaching position or a teaching-

367 Id.
368 Id.
369 Id.
related position of equal stature, and (2) where the education qualifies her for a new position within the general field of teaching, but does not also qualify her for a trade or business outside of teaching.

On the other hand, the courts have always applied the commonsense approach to non-teachers. Two cases which illustrate this difference in approach are *Glenn v. Commissioner*, in which a licensed accountant took a review course to prepare for a C.P.A. examination, and *Toner v. Commissioner*, in which a parochial school teacher pursued education which qualified her to teach in public school. Each case raised the issue of whether the new qualification amounted to a new trade or business.

In *Glenn*, the Tax Court applied the commonsense approach and found that a licensed public accountant was a different trade or business than a C.P.A. In so-holding, the Tax Court reasoned that a C.P.A. performs significantly different tasks and activities than does a licensed public accountant. However, in *Toner*, the Third Circuit held that a parochial school teacher and a public school teacher are in the same trade or business. Here, instead of applying the commonsense approach, the Third Circuit followed the Current Regulations' assertion that all teaching is the same.

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372 See *Toner v. Commissioner*, 623 F.2d 315; *Schwerm v. Commissioner*, 51 T.C.M. (CCH) 270. Contra P.L.R. 93-16-005 (Apr. 23, 1993) (ruling that elementary school teacher and assistant professor at a university were not the same trade or business).

373 See *Dreher v. Commissioner*, 46 T.C.M. (CCH) 1144 (1983), aff'd, 738 F.2d 421 (3d Cir. 1984) (holding that law school education qualified assistant principal for new trade or business outside of teaching even though the education could advance him in an administrative position or lead him to teach law in the future); *Ardavany v. Commissioner*, 38 T.C.M. (CCH) 569 (1979) (holding that law school courses pursued by community college teacher to fill position as business law teacher at the same college qualified her for a new trade or business); *Bouchard v. Commissioner*, 36 T.C.M. (CCH) 1098 (1977) (holding that law school education pursued by a college mathematics professor to meet his employer's requirement for tenure and to be qualified to teach law at the college qualified him for a new trade or business); *Wright v. Commissioner*, 32 T.C.M. (CCH) 31 (1973).


375 623 F.2d at 315.

376 62 T.C. at 270.

377 Id.

378 623 F.2d at 315.
type of work. In both Toner and Glenn, the taxpayer appeared to pursue a position within the same field of employment. However, because the Current Regulations apply a different standard to these seemingly similar transactions, a different result is obtained. In this manner, the Current Regulations favor teachers over non-teachers.

The disparity between these approaches can also be seen in cases where taxpayers pursue education to obtain a license to perform the same trade or business in another state or country. The issue raised is whether a taxpayer licensed in a trade or business in one state or country is in the same trade or business as a taxpayer similarly licensed in another state or country. In cases involving non-teachers, the courts held that practicing the same profession in a second state is a new trade or business. Yet, in cases involving teachers, the courts held that all teaching is the same profession by conclusively relying on the Current Regulations instead of applying the commonsense approach.

The following two cases illustrate this disparity: Sharon v. Commissioner involved a licensed New York lawyer who pursued education to become a licensed California lawyer. In Laurano v. Commissioner, a certified Canadian teacher pursued the education required by state law to become a certified teacher in the New Jersey public school system.

In Sharon, the Tax Court applied the commonsense approach and held that a lawyer licensed in one state was in a different trade or business than a lawyer licensed in another state. In so holding, the Tax Court found the tasks and activities that a licensed California lawyer could do in California were significantly different from those that a non-licensed lawyer could do in

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379 Id. In Toner, the taxpayer met the minimum educational requirements to be a parochial elementary teacher but not those to be certified to teach in the state public schools. Id. at 316. However, when she was hired, her employer required her to obtain additional college credits until she earned a degree. Id. When she obtained her degree, she also became certified to teach in the state public schools. Id. at 320.

380 66 T.C. 515, 528 (1976), aff'd, 591 F.2d 1273 (9th Cir. 1978). For further discussion of Sharon, see infra notes 421-31.

381 69 T.C. 723, 725 (1978).

382 66 T.C. at 528-29.
California. Therefore, because the California bar review course was a program of study leading the taxpayer to qualify for a new trade or business, the Tax Court treated its cost as a nondeductible personal expense. In contrast, in Laurano, the Tax Court held that a teacher certified to teach in Canada was in the same trade or business as one certified to teach in New Jersey, reasoning that "both Canadian and New Jersey teachers involve the same general type of work." The only way the Tax Court distinguished Laurano from Sharon was to note that the Current Regulations treat all teaching and related duties as the same general type of work.

In both cases, a licensed or certified professional lacked the license or certification to perform in the same trade or business in another jurisdiction. Despite their factual similarities, the respective Tax Courts came to different conclusions, yielding different tax treatments for educational expenses. The only factor distinguishing these cases is the Current Regulations' unsupported assertion that "all teaching and related duties shall be considered to involve the same general type of work." The Current Regulations thus favor teachers over non-teachers by allowing a teacher to deduct educational costs which qualify her for certain career moves that a non-teacher can not deduct for similar career moves.

383 Id. See also Walker v. Commissioner, 54 T.C.M. (CCH) 169 (1987); Vetrick v. Commissioner, 37 T.C.M. (CCH) 392 (1978), aff'd, 628 F.2d 885 (5th Cir. 1980).

384 Sharon, 66 T.C. at 529-30.

385 Laurano, 69 T.C. at 728.

386 Id. at 728-29.


388 In spite of the Current Regulations favoring teachers over other taxpayers, easier deductibility of educational costs does not necessarily lead to corresponding tax benefits. Most teachers are likely to be employees of educational institutions who are not reimbursed for educational costs. For deduction purposes, the Code treats unreimbursed employee business expenses as miscellaneous itemized deductions. I.R.C. § 67(b).

Miscellaneous itemized deductions must pass through two hurdles to provide any tax benefit to a taxpayer. First, they are deductible only to the extent that they exceed 2% of the taxpayer's adjusted gross income. I.R.C. § 67(a). Second, the taxpayer must itemize her deductions to receive any benefit beyond the applicable standard deduction. See I.R.C. § 63. Therefore, unless a teacher has sufficient miscellaneous itemized deductions (including educational costs) and can itemize, she would realize no tax benefit for her otherwise deductible educational costs.
ii. Application of Commonsense Approach to Teachers Provides Similar Treatment to Teachers and Non-Teachers

The courts do apply the commonsense approach to teachers when the issue is whether education qualifies a teacher for a trade or business in a field outside of teaching. In these situations, the Current Regulations do not favor teachers over other taxpayers. For example, in *Bouchard v. Commissioner*, a college mathematics professor enrolled in law school to meet the college's tenure requirements and to switch from teaching mathematics to teaching law. The Service treated the law school costs as a nondeductible personal expense because law school qualified the taxpayer to become a lawyer. The taxpayer countered by asserting that the Current Regulations treat all teaching and related duties as within the same trade or business and, as such, the legal education which qualified him to teach a different subject should not be treated as qualifying him for a new trade or business.

The Tax Court rejected the taxpayer's interpretation of the Current Regulations, noting that the words "all teaching and related duties shall be considered the same general type of work" were preceded by a basic principle which treats all educational costs qualifying the taxpayer for a new trade or business as nondeductible personal expenses. Additionally, the Tax Court found the words of the teachers' examples in the Current Regulations to embrace this basic principle:

The examples are worded precisely and they are particularly informative. Example (a) is, "Elementary to secondary school classroom teacher." It is not kindergarten teacher to college professor, for example. Example (b) is, "Classroom teacher in one subject (such as mathematics) to classroom teacher in another subject (such as science)." It is not classroom teacher in one subject (such as home economics) to classroom teacher in another subject (such as neurosurgery).
Because the law school education also qualified the taxpayer to become a lawyer, the Tax Court treated its cost as a nondeductible personal expense. By so holding, the Tax Court refused to extend the provisions in the Current Regulations relating to teachers so as to allow teachers to deduct any type of educational cost. Thus, the Tax Court would treat educational costs which qualify a teacher for a new trade or business outside of teaching as nondeductible personal expenses.

IV. EDUCATIONAL COSTS SHOULD BE TREATED LIKE ANY OTHER BUSINESS EXPENSES

A. Educational Costs Are Not Inherently Personal Expenses

1. Education Which Qualifies the Taxpayer for Her Chosen Profession or Qualifies Her for a New Profession

Contrary to the Service's longstanding position, education which qualifies the taxpayer for her chosen profession or qualifies her for a new profession is not inherently personal. To explain why the Current Regulations treat such educational costs as nondeductible personal expenses, the Tax Court provided the following unenlightening observation:

For a discussion of the Service's position from a historical perspective, see supra part II.
[The regulations] recognize that the expense for education which qualifies an individual for his intended trade or business or profession is so inherently personal and capital in nature that is not a deductible expense even though it maintains or improves the skills required by the individual in his employment and even though it meets the express requirements of the individual's employer. In other words, such an educational expense is nondeductible even though there exists a legitimate business purpose for incurring such expense.\textsuperscript{397}

In contrast, in a dissenting opinion, Tax Court Judge Murdock once criticized the Tax Court's characterization of a law school education as personal:

The headnote on the majority opinion indicates that the decision is against the petitioner because his study of law was undertaken "for personal purposes." How could any individual's education be for any other purpose? Naturally he was trying to educate himself rather than any other person but his purpose was within the law allowing a deduction.\textsuperscript{398}

Perhaps the Tax Court and the Current Regulations treat educational costs as personal expenses because of the personal-

\textsuperscript{397} Jungreis \textit{v. Commissioner}, 55 T.C. 581, 591 (1970). In another context, the Tax Court and the Ninth Circuit have taken opposite positions on whether interest on a deficiency in federal income tax arising out of adjustments relating to business income and deductions is nondeductible personal interest under section 163(h). Validating Temporary Regulation § 1.163-9T(b)(2)(i)(A), which treats such interest as nondeductible personal interest, the Eighth Circuit stated:

The regulation adopts the reasonable rule that an individual's income tax liability, regardless of the nature of the income giving rise to the liability, is a personal obligation and that, consequently, interest owed by such individual because of a failure to pay his tax obligation on time necessarily is also a personal obligation.\textit{Miller v. United States}, 65 F.3d 687, 691 (8th Cir. 1995).

On the other hand, invalidating the same regulation, the Tax Court disputed the characterization as "personal" interest: "[W]e do not think that the Secretary of the Treasury should be entitled to use the authority conferred by section 7805(a) to construct a formula which excludes an entire category of interest expense in disregard of a business connection such as exists herein." \textit{Redlark v. Commissioner}, 106 T.C. 31, 40 (1996).

Ironically, if the Tax Court applied its rationale for treating interest on a tax deficiency related to carrying on a trade or business as business interest to the deductibility of educational expenses, it would likely find most educational costs to be deductible.

interaction involved in the educational experience. To paraphrase Judge Murdock's words, an individual educates himself.

However, if a personal connection makes an expense personal, then the cost of education necessary to qualify for a chosen profession or to improve work skills in an existing profession is no more personal than any number of expenses that involve personal interaction. For example, rental office space often includes substantial personal amenities. Tenants decorate and furnish rental office space to suit their personal taste. Family photographs often adorn credenzas and desks. Air conditioning and heat provide a comfortable environment. Many offices have small kitchens or dining areas for meals and snacks. Office space may also include a lounge with a television, sofas and magazines.

Yet, in spite of the many personal amenities found in rental office space, rental costs are not treated as inherently personal expenses. Instead, the cost of office rental space essential to conducting a taxpayer's trade or business is unconditionally deductible. Unlike educational costs, there are no regulations which impose any additional rules and restrictions to limit the deductibility of office rental costs.

Education which qualifies the taxpayer to enter into her chosen trade or business or maintains or improves her skills in an existing trade or business has a compelling business purpose. And, similar to the personal amenities found in rental office space, education may also have some elements of personal benefit. For example, an aspiring physician must attend medical school to obtain the necessary license and training to practice medicine. While at medical school the taxpayer may find some courses in the curriculum to be intellectually stimulating apart from their professional utility. Nonetheless, the presence of such personal benefit in an educational expense essential to the taxpayer's trade or business does not convert it into an inherently personal expense.

Similarly, suppose that a practicing physician also serves as an expert witness in medical malpractice cases. Subsequently, the physician attends law school to improve his skills as an expert

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399 See Carter v. Commissioner, 39 T.C.M. (CCH) 350, 351 (1979) ("Education as a general rule, however, is beneficial to an individual in a variety of ways and for a long period of time . . . .").
witness by learning the substantive and procedural aspects of law. If law school improves his skills as an expert witness, the fact that the education could also potentially qualify him to become a lawyer should not convert it into an inherently personal expense.

With regard to the personal elements of business-related education, the Second Circuit observed:

It may be that the knowledge he thus gained incidentally increased his fund of learning in general and, in that sense, the cost of acquiring it may have been a personal expense; but we think that 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 feature.\(^{400}\)

In the final analysis, educational costs which prepare a taxpayer for her chosen profession or improve her work skills in an established profession are no more personal than office rental costs. Therefore, these costs should be treated like rent or any other business expense without imposing additional rules and regulations which wrongfully deny a deduction for most educational costs.

2. Voluntarily Pursued Higher Education Which Improves General Competence and Makes the Taxpayer a Better Worker

In many instances, higher education voluntarily pursued by many taxpayers either before or after obtaining employment is not inherently personal. Although it may not meet training or licensing requirements or directly improve a taxpayer’s specific work skills, a general higher education enhances a taxpayer’s competence, which in turn improves his overall productivity.

For example, suppose that a taxpayer is employed as a chief engineer in charge of managing all engineering projects. To improve his general communication skills and to help him distinguish assumptions from facts when interpreting experiments, the taxpayer voluntarily pursues a graduate degree in philosophy.

\(^{400}\) Coughlin v. Commissioner, 203 F.2d at 309.
Although the education improves his work performance by enhancing his communication and thinking skills, such education does not directly relate to the specialized skills required of a chief engineer.\textsuperscript{401} The Tax Court has consistently treated education which improves a taxpayer's general competence as a nondeductible educational cost.\textsuperscript{402} The underlying reason for denying a deduction appears to be a bias that improving general competence is \textit{per se} a personal aspect of education.\textsuperscript{403} The Tax Court has rationalized this view by asserting that education which improves general competence is only remotely related to the taxpayer's work skills.\textsuperscript{404} In reality, the Tax Court has not given more than token consideration to the value or benefit that education which enhances general competence provides to a taxpayer's trade or business.

\textit{Carroll v. Commissioner} is illustrative of this point.\textsuperscript{405} \textit{Carroll} involved a police officer who voluntarily attended a university to pursue a degree with a major in philosophy.\textsuperscript{406} Police department policy encouraged, but did not require, its officers to attend college.\textsuperscript{407} Also, special work shifts were provided to accommodate any officer who pursued education deemed by the department to increase his value to the police department.\textsuperscript{408} Here, the taxpayer's education qualified under the police department's general order.\textsuperscript{409}

Focusing on the "personal" elements of education, the Tax Court characterized the cost of a general college education as an

\begin{footnotes}
\item[401] See \textit{Mullen v. Commissioner}, 29 T.C.M. (CCH) 925 (1970).
\item[402] Id. at 927.
\item[403] See \textit{McElhany v. Commissioner}, 42 T.C.M. (CCH) 1206, 1208 (1981). In that case, the Tax Court noted:
  There have been numerous cases discussing the question of whether the education for which an expenditure is made is so proximately and directly related to the individual's employment as to constitute a business expense. If such a proximate and direct relationship does not exist, the educational expenditure is a nondeductible personal expense.
  \textit{Id.} at 1208.
\item[404] Id. See also \textit{Carroll v. Commissioner}, 51 T.C. 213.
\item[405] 51 T.C. 213 (1968).
\item[406] \textit{Id.}
\item[407] \textit{Id.} at 214.
\item[408] \textit{Id.} at 214-15.
\item[409] \textit{Id.} at 215.
\end{footnotes}
inherently personal expense. On this basis, the court denied the taxpayer's deduction, stating:

A general college education . . . may not be as clearly a personal expense as an elementary education, but it seems to us that both are essentially the same type of expense. Millions of people must 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 . . . . Furthermore, a general college education has more than economic utility. It broadens one's understanding and increases his appreciation of his social and cultural environment.

In an alternative holding, the court superficially analyzed the benefits of the taxpayer's education to his job performance. Although the court acknowledged that the education made the taxpayer a better policeman, it concluded that the relationship between the taxpayer's education and his job skills as a police officer was too remote to be deductible. In this regard, the majority opinion noted:

A further bar to the petitioner's deduction of his educational expenses lies in the requirement that before expenses will be considered ordinary and necessary under section 162, it must be established that they bear a proximate and direct relationship to the taxpayer's trade or business . . . . Neither the petitioner's major field of philosophy nor the specific courses taken by him in 1964 indicates the sort of proximate relationship required for deduction. The regulations allow a deduction for education that maintains or improves skills, but what we have in this case is an education designed to increase the petitioner's general understanding and competency. Clearly, there is only a remote relationship between the study of Shakespeare's plays and the petitioner's work as a policeman. If we look at his ultimate goal, rather than at particular courses, there is still lacking the direct and substantial relationship to his skills that justifies a business

\[410\] Id. at 215-16.

\[411\] Id. at 216. See also Houston v. Commissioner, 32 T.C.M. (CCH) at 688 ("Unfortunately the obtaining of a broad education is not a deductible activity, but merely, at least hopefully, part of the admission price to entering that stage where deductions become meaningful.").
The Deductibility of Educational Costs

deduction. What he will secure as a result of his general college education will be of great value to him, socially, aesthetically, and otherwise. No doubt, it will help him be a better policeman. However, we think that for a business deduction to be allowed, there must be a showing of a more direct and substantial relationship to his skills in his employment.412

Clearly, because the court had conclusively characterized the taxpayer's educational cost as an inherently personal expense, it considered any actual value or benefit the education provided as only remotely connected to the taxpayer's work skills. However, a closer examination of the facts indicates a much stronger connection between the taxpayer's education and his work skills. Specifically, the police department encouraged its officers to pursue higher education.413 Then, only if it determined that the education would increase the officer's value to the department would the department accommodate the employee's school schedule by assigning him special work shifts.414 Despite the department's determination that the education would improve the taxpayer's work performance,415 the court's alternative holding did not consider this indicative of a sufficient business relationship between the education and the taxpayer's work as to merit a deduction.416

Without the presumption that voluntarily pursued higher education which improves general competence is inherently personal, as illustrated in Carroll, a fair analysis would simply consider all benefits and uses of the education to the taxpayer's work skills. Then, if the fact finder determines that the education enhanced the taxpayer's work performance, its cost should be a deductible business expense.417 On the other hand, if the fact finder

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412 Carroll, 51 T.C. at 218 (citations omitted).
413 Id. at 223-24.
414 Id. at 224.
415 Id.
416 Id. at 225 (Mulroney, J., dissenting).
417 In his dissent, Judge Mulroney criticized the majority for not considering whether there was a requisite business relationship with the taxpayer's job duties. In his view, there was such a business relationship:

To me it seems obvious that petitioner's college education in philosophy would help him maintain and improve the skills required in his employment as a police officer. Included
determines that the education did not enhance the taxpayer's work skills, its cost should be a nondeductible expense. In the final analysis, the deductibility of voluntarily pursued higher educational costs should be determined on the facts of each case without the presumption that all such costs are inherently personal.

B. The Current Regulations Deny a Deduction for Educational Costs Based Upon the Same Standard Which Allows a Deduction for Other Business Expenses

Ironically, the Current Regulations apply the same standard to deny a deduction for many educational costs which allows a deduction for all other business expenses. Consequently, by departing from basic tax principles, the Current Regulations wrongfully deny a deduction for most educational costs.

Under basic tax principles, business expenses are potentially deductible if a business relationship exists between the benefit or use of the expense and the taxpayer's trade or business. If a business relationship exists, the inquiry continues to determine whether the expense meets the other applicable deductibility requirements. On the other hand, if a business relationship does not exist, the inquiry ends and the expense is not deductible. Ultimately, business expenses which bear the requisite business relationship to the taxpayer's trade or business and meet the other applicable deductibility requirements are deductible.

In contrast, if educational costs qualify the taxpayer for her chosen profession (a strong business relationship to the taxpayer's trade or business), the Current Regulations treat them as nondeductible personal expenses. Similarly, even educational costs which directly relate to the taxpayer's work skills in an established profession are treated as nondeductible personal expenses if they also qualify her for a new trade or business.

in the usual definition of "philosophy" is the explanation that it means a science which comprises logic, ethics, and an investigation of human nature and human conduct.

Id. at 226 (Mulroney, J., dissenting).

418 See Kornhauser v. United States, 276 U.S. at 153.

419 See Reg. § 1.162-5(b)(2).

420 See Reg. § 1.162-5(b)(3).
To illustrate this point, parts IV.B.1 and 2 contrast specific situations in which other business expenses are amortizable because a business relationship exists between the expense and the taxpayer's trade or business yet educational costs are not amortizable because an identical or analogous business relationship exists between the education and the taxpayer's trade or business.

1. Taxpayer Allowed to Amortize All Expenses Related to Becoming a Licensed Attorney in a Second State Except His Educational Costs

The Current Regulations effectively deny the taxpayer the ability to amortize certain educational costs even if they serve the identical business purpose which allows the taxpayer to amortize all other business expenses. For example, recall the facts of Sharon v. Commissioner, in which a licensed New York lawyer accepted a position as a lawyer with the Internal Revenue Service in California. To prepare for the bar examination, the taxpayer took a bar review course to study California law that the taxpayer also found helpful in performing his ongoing work duties. The taxpayer's other costs included (1) registration as a law student; (2) a general bar examination fee; (3) an attorney's bar examination fee; (4) the California bar admittance fee; (5) an admittance fee into U.S. District Court for the Northern District of California; (6) an admittance fee into U.S. Court of Appeals for the Ninth Circuit; and (7) expenses related to admittance into the U.S. Supreme Court.

The Tax Court allowed the taxpayer to amortize these costs except the cost of the bar review course. The Tax Court treated the cost of the bar review course as a nondeductible personal expense, because passing the bar examination would lead the taxpayer to qualify for the new trade or business of being a lawyer.

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421 66 T.C. 515 (1976). For a discussion of a different aspect of Sharon, see supra notes 380-88 and accompanying text.
422 Id. at 515
423 Id. at 520.
424 Id. at 528, 530. However, the Tax Court required the amortization period to be over the taxpayer's life expectancy rather than his career expectancy. Id. at 530, 532.
Yet, as to the taxpayer's non-educational costs, the Tax Court did allow the taxpayer to amortize them because they did relate to the taxpayer becoming a lawyer licensed to practice in California.\textsuperscript{425} Thus, the Tax Court applied the same rationale to disallow the taxpayer to amortize the cost of his bar review course as it did to allow him to amortize his other costs.

The Tax Court analyzed the deductibility of the taxpayer's non-educational costs as it would any other business expense, evaluating their business utility to the taxpayer's potential career as a lawyer licensed to practice in California.\textsuperscript{427} The Tax Court found these costs sufficiently related to the taxpayer's future career possibilities as to be amortizable over his lifetime.\textsuperscript{428} Explaining its rationale for allowing the taxpayer to amortize his state bar licensing fees and the court admittance fees, the Tax Court asserted:

Once [an attorney] launches into the practice of law, he must decide what bars to join, and so long as there is some rational connection between his present or prospective work and those that he joins, we think that the expenses of joining them should be accepted as an appropriate cost of acquiring the necessary licenses to practice his profession. Since . . . the petitioner was working in California, he had reason to anticipate that he might eventually leave the Government and enter into private practice of law in that State, thus, when that possibility is considered together with the immediate benefit to be derived from membership in the California bar, there was ample reason for him to join such bar at that time. For these reasons, we are satisfied that . . . the petitioner did make use of the tangible asset constituting the privilege of practicing law in California . . . . Furthermore, it is altogether appropriate for any attorney-at-law to become a member of the bar of the Supreme Court . . . . No one can know when the membership in such bar may be useful to him in the practice of law—it may bring tangible benefits today, tomorrow, or never; yet, if one holds himself out to

\textsuperscript{425} \textit{Id.} at 528-29. For further discussion of this aspect of \textit{Sharon}, see \textit{supra} notes 380-88.

\textsuperscript{426} \textit{Id.} at 527-31.

\textsuperscript{427} \textit{Id.} at 530-32.

\textsuperscript{428} \textit{Id.}
practice law, there is ample reason for him to acquire membership in the bar of the Supreme Court. Under these circumstances, we find that the intangible asset acquired by becoming a member of such bar was used by the petitioner... and hold that he may amortize the costs of acquiring such asset over his life expectancy. 429

The Tax Court's rationale for allowing the taxpayer to amortize his state licensing and court admittance fees presents an even more compelling reason to allow the taxpayer to amortize the cost of his bar review course. Specifically, the Tax Court allowed the taxpayer to amortize his state licensing and court admittance fees based upon the possibility that he might enter private law practice.430 Yet, there was also the possibility that he might never enter private practice. In contrast, the taxpayer found the bar review course to be immediately useful to him on an ongoing basis in his current position with the IRS. 431 Compared with the immediate and continuous benefit of the bar review course, the other costs provided the taxpayer with an unrealized potential benefit which might or might not mature at some undetermined time in the future.

In Sharon, the Tax Court never engaged in the above analysis because the Current Regulations characterize the cost of any education which qualifies the taxpayer for a new trade or business as a nondeductible personal expense. Moreover, Sharon showcases the absurdity of the Current Regulations because their restrictive rules deny the taxpayer the ability to amortize the cost most worthy of such treatment.

2. Educational Costs Necessary to Enter Into a Trade or Business Are the Only Business Costs Not Amortizable as Start-Up Expenditures

Educational costs serve an analogous business purpose in creating the taxpayer's trade or business to other amortizable pre-employment business expenses. Yet the former may not be

429 Id. at 530-32.
430 Id. at 530-31.
431 Id. at 519.
amortized as start-up expenditures. Generally, a taxpayer may amortize business costs incurred as start-up expenditures over a period of sixty months, beginning with the month in which the taxpayer actually begins to carry on her active trade or business.\textsuperscript{432} Thus, a licensed professional, such as a dentist, may amortize all of the costs necessary to open a practice except the cost of the education required to obtain the license and essential training to practice.

For example, suppose that a person who aspires to become a lawyer attends law school. On January 1, 1997, after the taxpayer graduates from law school, the taxpayer rents office space and hires clerical staff to prepare for the opening of her practice on July 1, 1997. During the pre-opening period, she acquires necessary computer equipment and remodels the office space. Additionally, her clerical staff sets up her financial accounting books and file system. The pre-opening rental and clerical costs are essential to her active practice because she could not perform legal services without an appropriately prepared office. However, she may not deduct these costs under section 162(a) because during the pre-opening period, she is not carrying on a trade or business.\textsuperscript{433} Instead of a current deduction, however, the taxpayer may elect to amortize the pre-opening expenses as start-up expenditures.\textsuperscript{434}

The cost of her legal education is also essential to the taxpayer’s practice because without a law degree, the taxpayer could not legally or competently practice law. Similar to the start-up rental and clerical costs, the cost of law school should not be deductible under section 162(a) because a law student is not yet in practice.\textsuperscript{435} However, instead of disallowing a current deduction for this reason, the Current Regulations characterize this type of educational cost as a nondeductible personal expense.\textsuperscript{436} Yet, of all of the taxpayer’s

\textsuperscript{432} See I.R.C. § 195. For further discussion of section 195, see infra notes 519-32 and accompanying text.

\textsuperscript{433} See Gulick v. Commissioner, 43 T.C.M. (CCH) 490.

\textsuperscript{434} See I.R.C. § 195(b)(1).

\textsuperscript{435} See Gulick, 43 T.C.M. 490.

\textsuperscript{436} See Reg. § 1.162-5(b)(1). See also Duecaster v. Commissioner, 60 T.C.M. (CCH) 917, 920 (1990). In Duecaster, the Tax Court held that the cost of the taxpayer’s legal education did not qualify as a section 195 start-up expenditure. To hold otherwise, the Tax Court reasoned, would allow a taxpayer to convert a nondeductible personal expense into an amortizable
pre-opening expenses, the most important is the cost of her legal education, without which the taxpayer could not conduct her business. Consequently, she would have no need for office space, financial accounting books, or client files.

Unlike other pre-opening expenses, only the cost of the education necessary to begin a trade or business may not be amortized as a start-up expenditure. If, instead, educational costs were treated like any other business expense, the taxpayer would be able to amortize one of the most substantial costs of her career.

3. Quality of Education or its Benefit to the Taxpayer's Trade or Business is not the Determinative Factor for the Deductibility of Educational Costs

Another significant deficiency of the Current Regulations is that, to be entitled to a deduction, a taxpayer who pursues education to maintain or improve his skills in an existing trade or business may be compelled to choose an education of inferior quality over a superior quality education if the latter would also qualify him to enter into a new trade or business. This is the result even if the superior education would better improve the taxpayer's work skills. The following discussion of a Tax Court case and private letter ruling illustrates this illogical result.

_Carter v. Commissioner_ involved a taxpayer appointed to the position of county judge. The only educational requirement of this position was a high school diploma. To improve his legal skills, the taxpayer attended law school. However, because law school also qualified the taxpayer to become a lawyer, the Tax Court treated his educational costs as nondeductible personal expenses. In the Tax Court's analysis, the fact that a legal education was directly related to his duties as a judge was irrelevant. In this regard, the Tax Court stated: "We do not
question petitioner’s thesis that the study of law was helpful to him in handling certain aspects of his work as a county judge. But that is not the test.441

In contrast, a private letter ruling involved a taxpayer who for thirteen years held an elected position as a business representative and financial secretary.442 Because most of his work responsibilities involved law-related matters, the taxpayer attended a non-accredited law school. As a graduate of a non-accredited law school, the taxpayer was not eligible to take the bar exam in any state.443

Ruling that the taxpayer could deduct his educational costs, the Service acknowledged that the law school education maintained and improved the taxpayer’s work skills.444 However, the determinative factor was that as a graduate of a non-accredited law school, the taxpayer could not become a licensed lawyer.445 Hence, the education did not prepare the taxpayer for a new trade or business and the deduction was therefore not prohibited under the Current Regulations.

Both Carter and the private letter ruling involved taxpayers pursuing a law school education to improve their work skills. The deductibility of the cost depended not on the quality of the education nor its benefit to the taxpayer’s work skills but on whether the legal education could qualify the taxpayer to become a lawyer. Thus, if the taxpayer chooses to attend an accredited law school based upon the quality of the education, he may not deduct his costs. However, if he chooses to attend a non-accredited law school in order to deduct his costs, he must forego a better education. If educational costs were treated like any other business expense, their deductibility would be determined solely by evaluating the benefit that the underlying education provides to the taxpayer’s trade or business.

441 Id. at 351.
443 Id.
444 Id.
445 Id.
C. Deductibility of Educational Costs As Business Expenses

This article contends that the most compelling reason to treat educational costs like other business expenses is that tax law should apply the same standard to determine the deductibility of similar expenses.\footnote{There are also numerous social policy reasons justifying a more liberal treatment of the deductibility of educational costs. Some commentators attribute the different and less favorable treatment of educational costs, an investment in human capital, to tax law favoring investments in physical capital, such as in productive machinery, over investments in human capital. They argue that tax law should provide the same treatment to human capital investments as it does to physical capital investments because both are necessary to generate the income Congress seeks to tax. See, e.g., Louis Kaplow, Human Capital Under an Ideal Income Tax, 80 Va. L. Rev. 1477, 1478 (1994) ("A tax scheme's treatment of human capital is immensely important. The value of human capital, most individuals' primary asset, is substantially larger than that of nonhuman capital. Moreover, human capital is the underlying source of a considerable majority of revenue collected by income, consumption, and sales taxes."); Loretta Collins Argrett, Tax Treatment of Higher Education Expenses: an Unfair Investment Disincentive, 41 Syracuse L. Rev. 621, 622 (1990) ("[T]he Treasury Department's interpretation of present law for certain of these educational expenditures is inequitable and unjustified because it prohibits cost recovery of capital expenditures which are a significant factor in the production of trade or business income over a determinable period.").} In spite of the restrictions placed on the deductibility of educational costs by the Current Regulations, nothing in current "statutory" tax law directly or indirectly indicates that such costs should be treated differently than other business expenses. For example, section 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."\footnote{I.R.C. § 162(a) (emphasis added).}

The language of section 162(a) is clear—"all" expenses which meet its requirements are currently deductible. In addition, section 262(a), which denies a deduction for personal, living and family expenses, does not expressly include educational costs among these types of expenses. There is no authority within the Code to justify the application of a different standard to determine the
deductibility of educational costs. Accordingly, educational costs which bear a business relationship to the taxpayer's trade or business and meet other applicable deductibility requirements should be (1) deductible in the year paid or incurred,\textsuperscript{448} (2) amortizable over a period of at least sixty months,\textsuperscript{449} or (3) amortizable over the taxpayer's career or lifetime.\textsuperscript{450}

1. Deductibility of Educational Costs Which Qualify the Taxpayer for Her Chosen Trade or Business

a. Should Not Be Currently Deductible Under Section 162(a)

Consistent with the treatment of any other type of business expense, the educational costs of a student preparing to enter into a trade or business should not be deductible at that time under section 162(a). To currently deduct a cost, the taxpayer must be carrying on a trade or business at the time the cost is paid or incurred.\textsuperscript{451}

For example, to become a licensed professional (such as a physician, lawyer, dentist, etc.), the taxpayer must attend the appropriate professional school, satisfying the licensing requirements and learning the skills necessary to practice effectively in her chosen profession. After graduating from professional school, the taxpayer must pass the applicable examination to become licensed in the state in which she intends to practice. Only after the taxpayer completes these requirements may she engage in her chosen profession. Therefore, as a student, the taxpayer should not be entitled to take a current section 162(a)

\textsuperscript{448} For a discussion of the current deductibility of educational costs in a variety of contexts, see \textit{infra} notes 517-18 and accompanying text (educational costs paid or incurred prior to entering a trade or business); notes 538-47 and accompanying text (educational expenses paid or incurred while carrying on an established trade or business).

\textsuperscript{449} For a discussion of the amortization of educational costs as start-up expenditures, see \textit{infra} notes 454-66 and accompanying text.

\textsuperscript{450} For a discussion of the amortization of educational costs spanning a period of the taxpayer's career or lifetime, see \textit{infra} notes 466-70 and 481 and accompanying text.

\textsuperscript{451} I.R.C. § 162(a). \textit{See also} \textit{Gulick v. Commissioner}, 43 T.C.M. (CCH) 490.
deduction for her professional school educational costs because during those years she is not yet carrying on a trade or business.\textsuperscript{452}

b. Potentially Amortizable Over a Sixty Month Period as a Start-Up Expenditure

Although a student may not currently deduct the cost of her education, she may be able to amortize such cost as a “start-up expenditure” when she actually begins to carry on her trade or business. To qualify as an amortizable start-up expenditure,\textsuperscript{453} the taxpayer’s educational costs must meet the two requirements of section 195(c).\textsuperscript{454}

To satisfy the first requirement, the taxpayer must pay or incur the educational costs to create a trade or business.\textsuperscript{455} The cost of the taxpayer’s professional education clearly meets this requirement because it is a prerequisite to beginning her professional trade or business.\textsuperscript{456}

To satisfy the second requirement, the educational cost must be deductible if it was paid or incurred while the taxpayer was actually carrying on her trade or business.\textsuperscript{457} Generally, section 162(a) allows a deduction for business expenses. However, a business relationship must exist between the benefit or use of the expense and the taxpayer’s trade or business.\textsuperscript{458} In the case where education is required or essential to entering into a particular trade or business, such a business relationship does exist.

Section 162(a) also requires that a cost be “ordinary,” “necessary” and an “expense” rather than a capital expenditure. “Ordinary” is

\textsuperscript{452} See also Gulick, 43 T.C.M. (CCH) 490.

\textsuperscript{453} See I.R.C. § 195.

\textsuperscript{454} Another relevant section 195 issue is whether that section applies to the start-up expenditures of an employee. In James J. Freeland, et al., Fundamentals of Federal Income Taxation 343 (9th ed. 1996), the authors state that section 195 “has no application to an individual having employee status with respect to the deduction of expenses incurred in seeking new employment.” However, the authors cite no authority for their statement. If they are correct, section 195 would apply only if the taxpayer engaged in the practice of her chosen profession as a sole proprietor.

\textsuperscript{455} I.R.C. § 195(c)(1)(A)(ii).

\textsuperscript{456} See Duecaster v. Commissioner, 60 T.C.M. (CCH) 917, 919 (1990).

\textsuperscript{457} I.R.C. § 195(c)(1)(B).

\textsuperscript{458} See Kornhauser v. United States, 276 U.S. at 153.
“a course of conduct which constitutes a normal and natural response under the specific circumstances in which the taxpayer finds himself.”

Here, the pursuit by a professional of the type of courses offered in a professional school curriculum would be a “normal and natural response” by a taxpayer who practices in that profession.

Section 162(a) also requires that an expense be necessary. In McCulloch v. Commissioner, the Tax Court described a “necessary” expense as an expense reasonable in amount that is appropriate or helpful even if it is not indispensable or required. Clearly, a practicing professional would find her professional education to be “necessary.”

Finally, section 162(a) requires a cost to be an “expense” rather than a capital expenditure. An expense is an item that has a relatively short life span. A capital expenditure is an item “having a useful life substantially beyond the taxable year.”

Arguably, the cost of an education is a capital expenditure because the taxpayer will derive the benefit from such education for her entire career. Therefore, if the taxpayer could not currently deduct the cost of her professional education as a practicing professional, she may not amortize its cost under section 195.

Yet, under current law, whenever the courts have allowed a deduction for educational costs, it has always been as a currently deductible expense rather than as a capital expenditure. Thus, if in this example, the cost of professional school is treated as an

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460 55 T.C.M. (CCH) 259 (1988).
461 See Reg. § 1.162-3 relating to the current deductibility under I.R.C. § 162(a) of the cost of materials (“Taxpayers . . . should include in expenses the charges for materials and supplies only in the amount that they are actually consumed and used in operation during the taxable year . . . .”); Reg. § 1.162-6 relating to the current deductibility of professional expenses (“Amounts currently paid or accrued for books, furniture, and professional instruments and equipment, useful life of which is short, may be deducted.”).
462 Reg. § 1.263(a)-2(a) (as amended in 1987).
463 See Reg. § 1.162-5(b)(1) which provides that educational costs which qualify the taxpayer for her chosen trade or business are treated as nondeductible personal expenses because they “are personal expenditures or constitute an inseparable aggregate of personal and capital expenditures.” (emphasis added). If such educational costs are “capital” expenditures, they would not be deductible under section 162(a).
465 See discussion supra note 269.
expense, such cost would meet the requirement of section 195(c)(1)(B). Then, when the taxpayer actually began her practice, she could elect to amortize the cost of professional school over a period of not less than sixty months.\textsuperscript{466}

c. Potentially Amortizable Over the Taxpayer's Career or Lifetime

Assuming that the cost of education is a capital expenditure rather than amortizable as a start-up expenditure, the taxpayer should nonetheless be able to amortize the cost over a period spanning the taxpayer's career or lifetime. Section 167(a) allows an amortization deduction for a cost otherwise deductible under section 162(a), but for the fact that the cost was a capital expenditure rather than an expense.\textsuperscript{467} If education is an expenditure which creates an intangible asset or benefit extending over time, the taxpayer should be able to amortize the cost over the useful life of the asset if it "is known from experience or other factors to be of use in the business or in the production of income for only a limited period, the length of which can be estimated with reasonable accuracy . . . ."\textsuperscript{468}

The cost of education pursued prior to beginning the taxpayer's trade or business could be characterized as an intangible asset which will last her entire career or lifetime. Thus, a dentist, for example, should be able to amortize the cost of dental school over a period spanning her projected career or lifetime.\textsuperscript{469} Interestingly, the Tax Court articulated a rationale supportive of this result in \textit{Sharon}, where it allowed the taxpayer to amortize, over his lifetime, all costs related to becoming a licensed California attorney with the significant exception of the cost of his bar review course.\textsuperscript{470}

\textsuperscript{466} I.R.C. § 195(b)(1).
\textsuperscript{467} See supra notes 463-64 and accompanying text.
\textsuperscript{468} Reg. § 1.167(a)-3 (as amended in 1960); See also Reg. § 1.461-1(a)(1) (as amended in 1994).
\textsuperscript{469} See \textit{Sharon}, 66 T.C. 515; supra notes 421-31 and accompanying discussion; see also Rev. Rul. 70-171, 1970-1 C.B. 55. That revenue ruling involved fees paid by a doctor to a hospital, entitling him to a nontransferable lifetime privilege to practice in such hospital. \textit{Id.} The Service reasoned that the useful life of a lifetime privilege was the taxpayer's life expectancy, and as such required the taxpayer to amortize the fee over his life expectancy. \textit{Id.} at 56. However, the Service acknowledged that a taxpayer who established the merits of a shorter useful life could amortize the fees over such shorter useful life. \textit{Id.}
\textsuperscript{470} See \textit{Sharon}, 66 T.C. 515, supra notes 421-31 and accompanying text.
2. Deductibility of Educational Costs Which Improve a Taxpayer's Work Skills in an Established Trade or Business

a. Potentially Currently Deductible Under Section 162(a)

Unlike education pursued prior to beginning a career, the cost of education incurred by a taxpayer already established in a trade or business which meets the requirements of section 162(a) may be potentially currently deductible. For example, suppose an established physician who also testifies in medical malpractice cases attends law school to become a better expert witness. To be currently deductible under section 162(a), a business relationship must exist between the benefits of a law school education and the taxpayer's skills as an expert witness. Arguably, in this case, such a business relationship exists if the legal education would enhance the taxpayer's skills as an expert witness.

In addition, to qualify as a deduction under section 162(a), the cost of law school must be an "ordinary" cost. Since "ordinary" means "a course of conduct which constitutes a normal and natural response under the specific circumstances in which a taxpayer finds himself," an "extraordinary" cost is not deductible in spite of its usefulness to a trade or business.

Here, the issue is whether the cost of law school would be an "ordinary" or "extraordinary" expense to a physician who attends law school to improve her skills as an expert witness in medical


473 For an example of an extraordinary expense, see Goedel v. Commissioner, 39 B.T.A. 1 (1939), in which the Board denied a deduction to a stock broker for the cost of an insurance policy on the life of the President of the United States. Although it reasoned that the President's death would disrupt the stock market and adversely affect the taxpayer's business, the Board found the taxpayer's premium payments to be an "extraordinary" expense. Id. at 8-9.
The Deductibility of Educational Costs

malpractice cases. One possible indicium of "ordinary" is whether other physicians who testify in medical malpractice cases customarily attend law school. If so, the educational cost should be treated as an ordinary expense.

Next, the cost of law school must be a "necessary" expense. Arguably, a physician who testifies as an expert witness would find law school appropriate or helpful. However, another element of a necessary expense is its reasonableness. In this regard, in *McCulloch v. Commissioner*, the Tax Court observed:

[A] requirement inherent in the concept of "necessary" is that any payment asserted to be allowable as a deduction must be reasonable in relation to its purpose . . . . To the extent that an expense is unreasonable, it is not necessary, in such a case, only the portion which was reasonable is deductible under section 162.

Thus, regardless of whether law school is "helpful" to the physician, its cost in relation to a business purpose must be reasonable. For example, if the income generated from the taxpayer's work as an expert witness is only a small amount of her total income, the cost of a law school education may not be reasonable. Ultimately, determined on a case by case basis, the taxpayer's potential deduction may be limited or eliminated.

The final issue under section 162(a) is whether the cost of law school to a physician who testifies as an expert witness is an "expense" rather than a capital expenditure. Arguably, any education which provides a benefit over the taxpayer's entire career or lifetime is a capital expenditure. Therefore, the physician should not be entitled to currently deduct the cost of law school

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477 See *McCulloch*, 55 T.C.M. at 263.
478 See Reg. § 1.162-5(b)(1) which provides that educational costs which qualify the taxpayer for a new trade or business are treated as nondeductible personal expenses because they "are personal expenditures or constitute an inseparable aggregate of personal and capital expenditures." (emphasis added). If such educational costs are "capital" expenditures, they would not be deductible under section 162(a).
under section 162(a). However, as previously discussed, all decided cases which allowed a deduction for educational costs treated such costs as a currently deductible expense rather than as a capital expenditure. Under this view, if treated as an expense and assuming all of the other requirements of section 162(a) are met, the cost of law school should be currently deductible.

b. Potentially Amortizable Over the Taxpayer's Career or Lifetime

If in the above example, the physician’s law school costs were treated as a capital expenditure so that the taxpayer may not currently deduct such costs, for the reasons discussed above (concerning education which qualifies the taxpayer to enter into her chosen profession), the taxpayer should be able to amortize such costs over a period spanning her projected career or lifetime.

3. Issues Raised Concerning Deductibility of General Higher Educational Costs

As previously discussed, a taxpayer aspiring to become a professional should be able to deduct, in some form, the cost of the education which provides the taxpayer with the licensing and training required in her chosen profession. However, should a taxpayer who does not become a professional also be able to deduct the cost of a general higher education? Whereas a professional education provides specialized skills and training, a general higher education provides a rich and varied curriculum which improves the taxpayer's ability to reason and broadens her general understanding and appreciation of the social, economic, political and cultural environment. Arguably, this training instills a general competence in the taxpayer to enter the work force as a more productive worker.

479 See I.R.C. § 263(a).
480 See Damm v. Commissioner, 41 T.C.M. (CCH) 1359, supra note 269.
481 See supra part IV.C.1.c.
482 See Carroll v. Commissioner, 51 T.C. at 216. For further discussion of Carroll, see supra notes 405-17.
The deductibility of the cost of a general higher education should depend on its importance to the taxpayer in obtaining and performing in a job. A view of the job market should determine whether employers seek and value employees with the general competence provided by some form of higher education.

For example, suppose that prior to entering the work force, to make herself an attractive candidate for a variety of employment opportunities, a taxpayer pursues a general college education with a major in liberal arts. After receiving a bachelor's degree, the taxpayer obtains the position of claims adjuster with an insurance company. Because of her college education, the taxpayer is able to easily learn the nuances of her position and to demonstrate the communication and writing skills necessary to make her a competent adjuster. In spite of these benefits, none of the taxpayer's college courses specifically trained her to become a claims adjuster. In theory, even a person without a college education could be a competent claims adjuster. Yet, in practice, without a college degree, her employer may not have hired her.

Contrast this with a taxpayer who attends dental school to become a licensed dentist. In dental school, the taxpayer learns the basic skills that she will directly use in her practice. Without a dental school education, the taxpayer could not practice dentistry regardless of her other abilities. Absent a clear relationship between her college education and her work skills, should the claims adjuster be allowed to deduct or amortize her educational costs? Perhaps the answer is yes, if today's economic reality is relevant in determining the existence of the requisite business relationship between a general college education and the taxpayer's employment.

Under basic tax principles, the existence of a business relationship between any educational cost and the taxpayer's work skills is a question of fact.\textsuperscript{483} By analogy, in \textit{Welch v. Helvering},\textsuperscript{484} the Supreme Court considered whether a certain payment made by a taxpayer was an "ordinary" business expense. Deciding the issue as a question of fact, the Supreme Court observed:

\textsuperscript{483} See \textit{Stoddard v. Commissioner}, 45 T.C.M. (CCH) 323, 325 (1982).
\textsuperscript{484} 290 U.S. 111 (1933).
Here, indeed, as so often in other branches of the law, the decisive distinctions are those of degree and not of kind. One struggles in vain for any verbal formula that will supply a ready touchstone. The standard set up by the statute is not a rule of law; it is rather a way of life. Life in all of its fullness must supply the answer to the riddle.\textsuperscript{485}

The message from the Supreme Court's observation is that life itself provides the answers to questions of fact, such as what is an ordinary expense or what constitutes a business relationship between an expense and the taxpayer's trade or business. In a work environment experiencing constant technological advancement and global competition, an employee in the workforce must have some form of higher education. By imposing such an educational requirement, today's employers must believe that the benefits provided by a college education directly impacts the competence of their employees.

Finally, the recent legislation providing some tax relief for educational costs indicates that Congress recognizes the importance of pursuing higher education and securing quality employment.\textsuperscript{486} Commenting on the relationship between higher education and securing a quality job, a House Report states:

The Committee believes that the exclusion for employer-provided education should be targeted to those most in need of educational assistance—low- and middle-income employees who seek to obtain education which improves their skills and qualifies them for better jobs.\textsuperscript{487}

Today's employers recognize that some form of higher education is directly related to their employees' general competence. Moreover, recent legislation has designated much of the limited tax relief to the cost of general higher education (as opposed to

\textsuperscript{485} Id. at 114-15.

\textsuperscript{486} For example, in 1996, Congress reenacted I.R.C. section 127 to allow a taxpayer to exclude employer-provided educational assistance. Small Business Job Protection Act of 1996, Pub. L. No. 104-188, sec. 1202. § 127(d), 110 Stat. 1755, 1772-73 (1996). For a more comprehensive discussion of recent legislation providing tax relief for educational costs, see \textit{infra} part V.C.

graduate and professional school education). As a result, taxpayers are wise to assume that without at least a college education, job opportunities may be nonexistent or severely limited. Because of this reality, the cost of a general higher education necessary to obtain employment is analogous to the professional school education necessary to become licensed and trained in a particular profession. Although professional education may provide specialized training not provided by a general college education, both forms of education are a prerequisite to obtaining employment. As such, there is no reason to treat the deductibility of a general higher education required to obtain employment any differently than a professional school education required to enter a profession.

V. ONLY PIECENAL AND LIMITED CHANGES TO THE DEDUCTIBILITY OF EDUCATIONAL COSTS WILL OCCUR THROUGH NEW LEGISLATION

A. Judicial Declaration of Current Regulations as Void is Unlikely

In the thirty year history of the Current Regulations, the Tax Court has consistently upheld the validity of these regulations, making it unlikely that any court will declare them void. This

See infra part V.C.


On occasion, several Tax Court judges have criticized the inequitable treatment of educational costs as compared to other business expenses. In Greenberg v. Commissioner, 45 T.C. 480 (1966) (Dawson, J., dissenting), Judge Dawson commented:

If expenses are "ordinary and necessary" within the meaning of section 162 and proximately related to a taxpayer's work, then they are deductible. Educational expenses are not special items requiring special rules. In my opinion they should be treated like any other basic expense item and should be judged by the same standards . . . . Since other businesses deduct the expenses of carrying on their operations, should professional people such as doctors, lawyers, accountants, engineers, and teachers be denied their "ordinary and necessary" business expenses incurred in maintaining and improving their skills? If the majority of this Court thinks so, it seems to me that they are swimming against the tide of educational, scientific, and medical advancement in America today.

Id. at 486-87. See also, Hartrick v. Commissioner, 22 T.C.M. (CCH) 145, 149 (1963) ("Educational expenses stand on no different footing than any other deduction allowable
is true even though interpretative regulations, such as the Current Regulations, may be judicially declared void if they are "unreasonable and plainly inconsistent with the revenue statutes." 

In a 1982 article, Professor Schoenfeld argued that the Current Regulations are an unreasonable interpretation of the underlying statute because (1) "the disallowance of education expenses is based upon mere 'qualification' for any new trade or business, even if there is no real possibility that the taxpayer will ever actually enter the hypothetical new trade or business" and (2) the Current Regulations fail to define the concept of a new trade or business. However, Professor Schoenfeld's criticisms of specific provisions of the Current Regulations are only symptomatic of the underlying unreasonableness of the Current Regulations. The Current Regulations are an unreasonable interpretation of the underlying statutes because the deductibility of all business expenses governed by a common statutory scheme should be determined by the same standard. By applying a standard that establishes a deduction for business expenses generally and then applying that same standard to deny a deduction for educational costs, the Current Regulations wrongfully deny a deduction for most educational costs.

under section 162.

See I.R.C. § 7805(a) (granting the Secretary of the Treasury general authority to "prescribe all needful rules and regulations for the enforcement of [the Code]").

Commissioner v. South Texas Lumber Co., 333 U.S. 496, 501 (1948). Ironically, in a recent case, Redlark v. Commissioner, 106 T.C. 31 (1996), the Tax Court took the opposite stance with regard to a regulation classifying all interest paid on income tax deficiencies as personal interest. Because the regulation also treats interest paid on an income tax deficiency allocable to the taxpayer's trade or business as nondeductible personal interest, the Tax Court invalidated the regulation, stating "[W]e do not think that the Secretary of the Treasury should be entitled to use the authority conferred by section 7805(a) to construct a formula which excludes an entire category of interest expense in disregard of a business connection such as exists herein." Id. at 39-40.


Id. at 311.

As a standard for an unreasonable regulation, the Tax Court once stated: [J]udicial deference is not a substitute for judicial scrutiny and analysis. A regulation which contradicts the unambiguous language of the statute it purports to interpret cannot stand. Moreover, where the statute is unambiguous, and there is no valid reason for adding a requirement to those the statute already provides, the Commissioner may not usurp congressional authority by adding a requirement by regulation. Finally,
Even if the Current Regulations were challenged as unreasonable, the doctrine of legislative reenactment could be invoked to validate them. Under this doctrine, Congress is deemed to approve of existing regulations when it reenacts the underlying Code section(s) without substantial change. Since the promulgation of the Current Regulations in 1967, neither section 162(a) nor section 262(a) has been amended. In his article, Professor Schoenfeld argues that unless Congress actually considers amending the underlying Code sections but fails to make changes overruling the Service's regulations, the legislative reenactment doctrine should not be applied to validate the Current Regulations. However, his argument fails to take into account several factors.

First, since 1921, Congress has allowed the Service free rein in setting the guidelines for the deductibility of educational costs. Second, in 1986, the one occasion in which Congress did affirmatively act, it enacted a Code section disallowing travel as a deductible educational expense. In so doing, Congress specifically overruled a provision of the Current Regulations. By failing to overrule any other objectionable provisions, however, Congress arguably expressed its approval of the Current Regulations.

In addition, in 1978, Congress enacted section 127, allowing employees to exclude from gross income a certain amount of

although a regulation does not clearly contradict or limit the provisions of the statute it purports to interpret, it is nonetheless invalid if it is inconsistent with the statute's origin and purpose.


See Schoenfeld, supra note 492, at 312.


The Conference Report stated:

No deduction is allowed for costs of travel that would be deductible only on the ground that the travel itself constitutes a form of education . . . . This provision overrules Treas. Reg. § 1.162-5(d) to the extent that such regulation allows deductions for travel as a form of education.

educational assistance provided by employers.\textsuperscript{499} Prior to this enactment, an employee would include employer-provided educational assistance in his gross income and then attempt to offset this income with a deduction for his educational costs.\textsuperscript{500} However, an employee could take the offsetting deduction only if the cost of such education was deductible under the Current Regulations.\textsuperscript{501} Since some education funded with educational assistance might not be deductible under the Current Regulations, Congress was compelled to take legislative action to assure the tax-free treatment of educational assistance payments.\textsuperscript{502} Otherwise, the educational assistance would be included in gross income and the corresponding educational costs may or may not have been deductible. As an alternative to enacting an exclusion from gross income, Congress could have overruled the Current Regulations by liberalizing the deductibility of educational costs. Instead, by enacting section 127, Congress appeared to validate the Current Regulations.\textsuperscript{503}

Thus, even if the Current Regulations are potentially void, the doctrine of legislative reenactment could be invoked to validate them. Moreover, a judicial overruling of the Current Regulations is unlikely in view of the long history of congressional deference to the Service’s position on the deductibility of educational costs and the Tax Court’s consistent validation of the Current Regulations as a reasonable interpretation of the underlying revenue statutes.

\section*{B. Congressional Overhaul of the Current Regulations is Unlikely}

In spite of the inequitable treatment of educational costs, the \textit{de facto} current state of the law is that most educational costs are


\textsuperscript{501} \textit{Id.} at 6862.

\textsuperscript{502} \textit{Id.} at 6863.

\textsuperscript{503} For additional evidence of congressional approval of the Current Regulations, see I.R.C. § 127(c)(6) ("This section shall not be construed to affect the deduction . . . of amounts . . . which are paid or incurred, or received as reimbursement, for educational expenses under section . . . 162 . . . ").
nondeductible. If Congress were to repeal the Current Regulations, such repeal would generate substantial deductions never before available to taxpayers. In view of the nation’s large current deficit, Congress is unlikely to overhaul the Current Regulations at a cost of billions of dollars in lost tax revenues.

Recent legislation illustrates how even limited tax relief for educational costs can generate a substantial loss in tax revenues. For example, the Congressional Budget Office estimates a tax revenue loss (for years 1997 through 2002) from the education tax incentives provided by the Taxpayer Relief Act of 1997 to be in excess of $39 billion. Moreover, of the total $151.6 billion in lost revenues generated by the Act, the education tax incentives is the largest single category, representing approximately 26% of the total tax revenue loss.

In addition, the reenactment of section 127 by Congress as part of the Small Business Job Protection Act of 1996 suggests that lost tax revenue is a major concern in providing tax relief for educational costs. Specifically, section 127 (as reenacted) allows employees to exclude from gross income a certain amount of educational assistance provided by employers. However, the section as reenacted makes the exclusion inapplicable (with respect to expenses related to courses beginning after June 30, 1996) to any “graduate level course of a kind normally taken by an individual pursuing a program leading to a law, business, medical, or other advanced academic or professional degree.” Thus, this “tax break” for educational expenses applies only to education below the graduate level. According to the House Report, budget concerns

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504 Pub. L. No. 105-34. For a discussion of the education tax incentives provided by the Taxpayer Relief Act of 1997, see infra part V.C.


508 For tax years beginning before May 31, 1997, I.R.C. section 127, as reenacted, allows an employee to exclude from gross income up to a maximum amount of $5,250 of educational assistance provided by her employer. The Taxpayer Relief Act of 1997 extended section 127 an additional three years until May 31, 2000. Pub. L. No. 105-34, § 221(a).

509 I.R.C. § 127(c)(1).
were the reason that the Committee did not include educational assistance for graduate school within the exclusion:

The need to balance the Federal budget necessitates some modification of the exclusion . . . . [T]he exclusion for employer-provided education should be targeted to those most in need of educational assistance—low- and middle-income employees who seek to obtain education which improves their skills and qualifies them for better jobs. Accordingly, the Committee believes it appropriate to reinstate the restriction on graduate-level education.\(^{510}\)

In light of the high cost of the recently enacted education tax incentives and congressional sensitivity to the budget deficit, it is unlikely that Congress will enact legislation overhauling the Current Regulations at a cost of many more billions of dollars in additional lost tax revenues.

C. Recent Legislation Provides Limited Tax Relief for Educational Costs

Although repeal of the Current Regulations is not likely to occur, Congress has recently enacted legislation providing some tax relief for educational costs.\(^{511}\) The specific provisions are summarized as follows:

1. The HOPE scholarship credit:\(^{512}\) This is a non-refundable tax credit of up to $1,500 per year\(^{513}\) per student\(^{514}\) (for no more than two years of post secondary education)\(^{515}\) for qualified higher education expenses (tuition and fees)\(^{516}\) paid during the taxable year for the education of the taxpayer, the taxpayer's spouse, or the


\(^{514}\) I.R.C. § 25A(b)(1).

\(^{515}\) I.R.C. §§ 25A(b)(2)(A), (C).

taxpayer’s dependents.\textsuperscript{517} To qualify for the credit, the student must be at least a half-time student for one academic period during the year.\textsuperscript{518} However, the tax credit is phased out ratably for taxpayers with modified adjusted gross income within specified ranges.\textsuperscript{519} Also, taxpayers convicted of a federal or state drug related felony are not eligible for the credit.\textsuperscript{520}

2. The Learning Lifetime Credit.\textsuperscript{521} This is also a nonrefundable per taxpayer tax credit equal to 20 percent\textsuperscript{522} of the qualified higher education expenses (tuition and fees)\textsuperscript{523} paid during the taxable year for the education of the taxpayer, the taxpayer’s spouse, or the taxpayer’s dependents.\textsuperscript{524} Unlike the HOPE scholarship credit, the Lifetime Learning Credit is (1) not limited to the first two years of post secondary education;\textsuperscript{525} and(2) applies to any course, including graduate level courses, taken at an eligible educational institution to acquire or improve the student’s job skills.\textsuperscript{526} Similar to the HOPE scholarship credit, this tax credit is phased out ratably for taxpayers with modified adjusted gross income within specified ranges.\textsuperscript{527}

3. Exclusion from gross income for certain student loan cancellations:\textsuperscript{528} The new law allows a taxpayer to exclude from gross income the forgiveness of a student loan (or refinanced loan) made by a tax-exempt educational organization to the taxpayer to be used to pay for tuition and fees as a student at a tax-exempt

\textsuperscript{518} I.R.C. § 25A(b)(2)(B).
\textsuperscript{519} I.R.C. § 25A(d)(2)(A) (the phase-out range is modified adjusted gross income between $40,000 and $50,000 for individual taxpayers, and between $80,000 and $100,000 in the case of a joint return). The phase-out ranges are to be indexed for inflation beginning in tax years after 2001. I.R.C. § 25A(h)(1).
\textsuperscript{520} I.R.C. § 25A(b)(2)(D).
\textsuperscript{522} I.R.C. § 25A(c)(1) (the dollar amount of the tax credit is capped at $1,000 for all tax years before January 1, 2003 and at $2,000 for all tax years after December 31, 2002).
\textsuperscript{523} I.R.C. §§ 25A(b)(1), (f)(1).
\textsuperscript{524} I.R.C. § 25A(f)(1)(A).
\textsuperscript{525} I.R.C. § 25A(c).
\textsuperscript{526} I.R.C. § 25A(c)(2)(B).
\textsuperscript{527} See supra note 519.
\textsuperscript{528} I.R.C. § 108(f)(2)(D), amended by the Taxpayer Relief Act, § 225(a)(1).
educational organization.\textsuperscript{529} To qualify for the exclusion, as a condition of the loan cancellation, the student must agree to work in certain occupations providing a public service (for any of a broad class of employers) for a certain period of time.\textsuperscript{530}

4. Extension of exclusion for employer-provided educational assistance: This exclusion from gross income of up to $5,250 for employer-provided educational assistance for undergraduate level courses only is extended through May 31, 2000.\textsuperscript{531}

5. Expansion of tax benefits for qualified state tuition programs with regard to beneficiaries,\textsuperscript{532} qualified higher education expenses\textsuperscript{533} and eligible educational institutions.\textsuperscript{534} Prior to its amendment, section 529 provided tax-exempt status to qualified state tuition programs\textsuperscript{535} as well as the deferral of tax to the beneficiaries on the earnings of such programs.\textsuperscript{536} To participate in a qualified state tuition program, individuals contribute funds to prepay for the qualified educational expenses of a designated beneficiary.\textsuperscript{537} The new legislation extends the definition of qualified educational expenses to include the beneficiary's future room and board expenses.\textsuperscript{538} In addition, the new legislation expands the definition of "member of family" for purposes of tax-free rollovers (of unused funds from one beneficiary account to another) and beneficiary changes to include children, siblings, nieces, nephews, in-laws and spouses of such individuals.\textsuperscript{539} Finally, the new legislation expands the definition of an eligible educational institution to include proprietary and post-secondary vocational institutions.\textsuperscript{540}

\textsuperscript{529} Id.
\textsuperscript{530} Id.
\textsuperscript{531} I.R.C. § 127(d), amended by the Taxpayer Relief Act, § 221(a).
\textsuperscript{532} I.R.C. § 529(e)(2), amended by the Taxpayer Relief Act of 1997, § 211(b)(1).
\textsuperscript{533} I.R.C. § 529(e)(3), amended by the Taxpayer Relief Act of 1997, § 211(a).
\textsuperscript{534} I.R.C. § 529(e)(5), amended by the Taxpayer Relief Act of 1997, § 211(b)(2).
\textsuperscript{535} I.R.C. § 529(a).
\textsuperscript{536} I.R.C. § 529(c)(1).
\textsuperscript{537} I.R.C. § 529(b)(1)(A).
\textsuperscript{538} I.R.C. § 529(e)(2), amended by the Taxpayer Relief Act of 1997, § 211(b)(1). Effective for tax years ending after August 20, 1996. Taxpayer Relief Act, § 211(a).
\textsuperscript{539} I.R.C. § 127(d), amended by the Taxpayer Relief Act, § 221(b).
\textsuperscript{540} I.R.C. § 529(e)(3), amended by the Taxpayer Relief Act, § 211(a). Effective after
6. Education Individual Retirement Accounts ("Education IRA"). An Education IRA is a trust or a custodial account established exclusively to pay the qualified educational costs (as defined in section 529(e)(3)) of a designated beneficiary. Annual contributions are limited to no more that $500, payable in cash, and may not be made after the designated beneficiary attains age eighteen. Earnings on the contributions accumulate tax-free. Distributions are also tax-free to the extent that they do not exceed the beneficiary's qualified higher educational expenses during the taxable year of distribution. Distributions in excess of these expenses are taxable and subject to an additional ten percent penalty tax. However, beneficiary redesignations, or rollovers from one Education IRA into the Education IRA of another beneficiary, are allowed tax-free, provided that the new beneficiary is a member of the family of the old beneficiary. Finally, an educational IRA must terminate when the beneficiary reaches age thirty. At that time, the remaining funds must be distributed and taxed to the beneficiary, subject to an additional 10 percent penalty tax.

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Paragraph numbers and references are indicated as follows:

542 I.R.C. § 530(b)(1).
543 I.R.C. § 530(g).
544 I.R.C. § 530(b)(2).
545 I.R.C. §§ 530(a), (b).
546 I.R.C. § 530(b)(1)(A)(iii). The contribution limit is phased out for single taxpayers with a modified adjusted gross income between $95,000 and $110,000 and for married taxpayers with a modified adjusted gross income between $150,000 and $160,000. I.R.C. §§ 530(c)(1)(A), (B).
549 I.R.C. § 530(a).
552 I.R.C. §§ 530(d)(5), (6).
7. Deduction for Interest on Education Loans: The new law allows an above the line deduction for interest paid on a qualified education loan. Beginning in 1998, this deduction is limited to $1,000, increasing by $500 each year until it is capped at $2,500 in the year 2001. The deduction is available only with respect to interest paid on a qualified education loan within the first sixty months in which interest payments are required. A qualified education loan means any indebtedness incurred to pay the qualified education expenses of the taxpayer, the taxpayer's spouse or any dependent of the taxpayer. Qualified education expenses include tuition, fees, room and board and related expenses less amounts excludable from gross income, such as amounts excluded under section 135, tax-free distributions from Education IRAs and excluded employer-provided educational assistance. Finally, the expenses must be paid or incurred within a reasonable time before or after the loan was incurred and attributable to a time when the student was at least a half-time student.

8. Penalty Tax-Free Withdrawal of Funds from Individual Retirement Accounts to Pay for Qualified Education Expenses: The new law allows the penalty tax-free withdrawal of funds from a regular IRA or a Roth IRA to pay for the qualified higher education expenses of the taxpayer, the taxpayer's spouse, or any child or grandchild of the taxpayer or the taxpayer's spouse.

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556 I.R.C. § 221(a).
557 I.R.C. § 221(b)(1). The deduction limit is phased out for single taxpayers with modified adjusted gross income between $40,000 and $50,000 and for married taxpayers filing jointly with modified adjusted gross income between $60,000 and $70,000. I.R.C. §§ 221(b)(2)(A), (B).
558 I.R.C. § 221(d).
559 I.R.C. § 221(e).
560 I.R.C. § 221(e)(2).
561 I.R.C. §§ 221(e)(1)(B), (C).
562 Effective for distributions made after December 31, 1997. The Taxpayer Relief Act, § 203(c).
564 I.R.C. § 72(t)(7).
In the aftermath of the new legislation, two propositions remain clear: First, although well intended, the new education tax incentives are limited and fail to put the deductibility of educational costs on the same footing as other business expenses. Second, considering the high cost of the new education tax incentives, the cost of overruling the Current Regulations would be billions of dollars greater. Ultimately, this means that any additional tax relief for educational costs must include the elimination of tax benefits in other areas. To balance tax effectiveness and fairness with budget concerns, Congress should evaluate and prioritize the merits of current allowable deductions and other tax benefits. Then, Congress should decide whether treating the deductibility of educational costs like any other business expense justifies the elimination of some other current deductions or tax benefits.

VI. CONCLUSION

Under current statutory tax law, there is no justification to treat educational costs differently from any other business expense. Section 162(a) is worded in broad terms: “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 word “all” in section 162(a) suggests that any expense which meets the requirements of that section is currently deductible. In addition, section 262(a), which denies a deduction for personal expenses, does not expressly include educational costs as such an expense. Therefore, under current statutory law, any educational cost which bears the requisite business relationship with the taxpayer’s trade or business and meets the requirements of section 162(a) (or the requirements of any other deduction section) should be deductible.

In the final analysis, “regulatory” tax law discriminates against investments in education. By treating educational costs as inherently personal expenses, the section 262 regulations set the stage for the Current Regulations to impose an additional layer of

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565 I.R.C. § 162(a) (emphasis added).
restrictive rules, eliminating the deductibility of most educational costs, regardless of their connection with the taxpayer's trade or business. These additional restrictive rules go beyond those applied to other business expenses. Ultimately, the Current Regulations deny a deduction for those educational costs which often bear the most compelling business relationship to the taxpayer's trade or business than do any other business expense.

The most direct way to correct the inequitable treatment of educational costs is to treat them like any other business expense. The courts could accomplish this by declaring the Current Regulations void. Since the underlying statutes do not discriminate against the deductibility of educational costs, the courts could declare the Current Regulations invalid because they are "unreasonable and plainly inconsistent with the revenue statutes."666 Unfortunately, such judicial interpretation is unlikely to occur because the courts have consistently upheld the validity of the Current Regulations.

Finally, because the Service and the courts inappropriately continue to treat educational costs as personal expenses, any change would require legislative intervention. However, in spite of recent legislation providing limited tax relief, the nation's large current budget deficit makes the more ambitious repeal of the Current Regulations prohibitive. Thus, the only practical alternatives are to (1) accept the limited educational tax relief provided by the recent legislation; or (2) eliminate some currently deductible expenses and/or other tax benefits so as to allow the more liberal deductibility of educational costs. The author advocates that a debate should now begin on the second alternative.