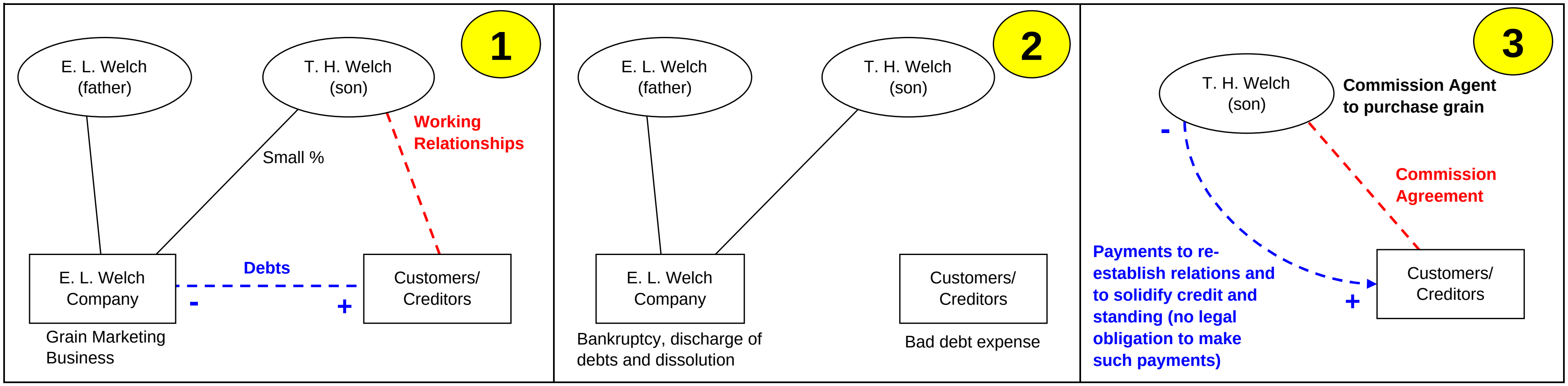
Welch v. Helvering
290 U.S. 111 (1933)

Deductibility of Reputation Payments

Initial Structure | **Bankruptcy** | **Reputation Payments**



In Welch, the taxpayer, a former secretary of a bankrupt grain business, later became a commission agent for another grain company. The taxpayer agreed to pay the debts of the bankrupt business in order to solidify his credit and standing and to reestablish his relations with customers. The Supreme Court upheld the Commissioner's disallowance of a deduction, and stressed the factual nature of section 162(a) issues. In considering whether the expenditures in issue were "ordinary" under section 162, Justice Cardozo stated:

> Now, what is ordinary, though there must always be a strain of constancy within it, is none the less a variable affected by time and place and circumstance. Ordinary in this context does not mean that the payments must be habitual or normal in the sense that the same taxpayer will have to make them often. A lawsuit affecting the safety of a business may happen once in a lifetime. The counsel fees may be so heavy that repetition is unlikely. None the less, the expense is an ordinary one because we know from experience that payments for such a purpose, whether the amount is large or small, are the common and accepted means of defense against attack. . . . The situation is unique in the life of the individual affected, but not in the life of the group, the community, of which he is a part.
> . . . .
> 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 its fullness must supply the answer to the riddle.

Later cases and rulings have interpreted Welch v. Helvering as standing for the proposition that expenditures for the purpose of **acquiring** goodwill (i.e., a new or acquired business) are not deductible. However, expenditures for the purpose of retaining, protecting, and promoting the goodwill of an established business are deductible as ordinary and necessary expenses. See e.g., Rev. Rul. 56-359, Rev. Rul. 79-283, Scruggs-Vandervoort Barney, Inc. v. Commissioner, 7 T.C. 779 (1946).

Welch v. Helvering is most often cited for the proposition that the burden of proof generally is on taxpayer to show that the Commissioner's determinations set forth in notices of deficiency are incorrect ("[The Commissioner's] ruling has the support of a presumption of correctness, and the [taxpayer] has the burden of proving it to be wrong."). This is now embodied in Tax Court rule 142(a).