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Taxation: Trade or Business—That Is the Question: Whether Full-Time Gambling Should Be Considered a Trade or Business for Purposes of Sections 62 and 162 of the Internal Revenue Code

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TAXATION: TRADE OR BUSINESS? THAT IS THE QUESTION: WHETHER FULL-TIME GAMBLING SHOULD BE CONSIDERED A TRADE OR BUSINESS FOR PURPOSES OF SECTIONS 62 AND 162 OF THE INTERNAL REVENUE CODE—*Groetzinger v. Commissioner*, 771 F.2d 269 (7th Cir. 1985).

I. INTRODUCTION

Taxpayers covet having their income-producing activity classified as a "trade or business" under sections 62 and 162 of the Internal Revenue Code.[1] If a taxpayer's activities gain trade or business status, the taxpayer can deduct from his or her gross income the "ordinary and necessary" business expenses connected with his or her trade or business.[2] The problem which has plagued courts for decades is how to formulate a set of standards for accurately assessing whether an income-producing activity is, by nature, a trade or business.[3] Two criteria have emerged for evaluating trade or business status. The first, the "goods and services" test, focuses on the taxpayers' holding themselves out as providing goods or services or both.[4] The second, the "facts and circumstances" test, focuses on the total circumstances underlying the case to determine if the income-producing activity reaches a sufficient level of "busyness" to warrant trade or business status.[5]

Certain gambling activities have generated particularly difficult

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1. I.R.C. § 62(1) (1982) (all Internal Revenue Code sections are codified in Title 26 of the United States Code). Adjusted gross income equals gross income minus "[t]he deductions allowed by this chapter . . . which are attribut[ed] to a *trade or business* carried on by the taxpayer." *Id.* (emphasis added). I.R.C. § 162(a) (1982). "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* . . . ." *Id.* (emphasis added).

2. I.R.C. § 162 (1982). In contrast, if taxpayer's expenses are held to be personal, then the taxpayer must pay taxes on his or her gross income without subtracting "personal, living, or family expenses." I.R.C. § 262 (1982). A taxpayer's expenses connected with full-time gambling are deductible as "ordinary and necessary expenses . . . for the production or collection of income." I.R.C. § 212 (1982). Section 212 expenses, however, are subtracted from adjusted gross income only to the extent such expenses are in excess of the taxpayer's zero bracket amount. *See* I.R.C. § 211 (1982). Therefore, a taxpayer's taxable income is more greatly reduced if his or her expenses are characterized as business expenses as opposed to income-production expenses.

3. *See infra* notes 8–9 and accompanying text.

4. *See, e.g.*, Estate of Cull v. Commissioner, 746 F.2d 1148 (6th Cir. 1984) (taxpayer did not hold himself out as a gambler; therefore his expenses were not considered trade or business expenses); Gentile v. Commissioner, 65 T.C. 1 (1975) (taxpayer used his own resources for gambling and did not hold himself out as offering a good or service at the betting window).

5. *See, e.g.*, Meredith v. Commissioner, 49 T.C.M. 318 (CCH) (1984) (taxpayer allowed to deduct full-time gambling expenses); Ditunno v. Commissioner, 80 T.C. 362 (1983) (taxpayer in full-time trade or business).

cases for determining the existence of a trade or business status. The difficult cases generally involve taxpayers who devote forty or more hours per week attending races at a track, researching the performance of the various entries, and placing bets.[6] This taxpayer gambles with his or her own money and does not provide others with the results of his or her research. The problem arises when the taxpayer, the Internal Revenue Service, and eventually the courts must decide whether this type of activity constitutes a trade or business. Under the goods and services test, the activity is not considered a trade or business because in placing bets only for themselves, the taxpayers are not providing a service or supplying goods or holding themselves out as doing either. However, when applying the facts and circumstances test, the taxpayer appears to be devoting the time and energy characteristic of a trade or business. It is apparent that the standard which a particular court adopts is determinative of the status which this activity will be granted.[7]

The federal circuits courts of appeals are split as to whether the goods and services test or the facts and circumstances test should be applied when confronting the trade or business issue.[8] In *Groetzinger v. Commissioner*[9] the Court of Appeals for the Seventh Circuit, in a case of first impression, decided to apply the facts and circumstances test. This casenote will examine the *Groetzinger* court's analysis of established precedent in this area[10] and the purpose of section 62 of the Internal Revenue Code.[11] This note will also examine the *Groetzinger* court's analogy of the full-time gambler to the high-volume short-term trader[12] and will consider whether the "facts and circumstances" test is a workable standard.[13] Finally, the merit of other arguments which have influenced other courts when deciding the "trade or business" sta-

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6. *See infra* note 8 for gambling cases which have reached appeals courts.

7. *See supra* notes 4–5.

8. The Courts of Appeals for the Second, Third, and Sixth Circuits have utilized the "goods and services" test. *E.g.*, Estate of Cull v. Commissioner, 746 F.2d 1148 (6th Cir. 1984); Gajewski v. Commissioner, 723 F.2d 1062 (2d Cir. 1983); Noto v. United States, 598 F. Supp. 440 (D.N.J. 1984), *aff'd mem.*, 770 F.2d 440 (3d Cir. 1985). The Court of Appeals for the Eleventh Circuit and the Tax Court have adopted the "facts and circumstances" test. *E.g.*, Groetzinger v. Commissioner, 771 F.2d 269 (7th Cir. 1985); Ditunno v. Commissioner, 80 T.C. 362 (1983); Nipper v. Commissioner, 47 T.C.M. 136 (CCH) (1983), *aff'd mem.*, 746 F.2d 813 (11th Cir. 1984). Each of these cases involved the issue of whether full-time gambling is a trade or business for the purposes of the I.R.C.

9. 771 F.2d 269 (7th Cir. 1984).

10. *See infra* text accompanying notes 31–59.

11. *See infra* text accompanying notes 60–68.

12. *See infra* text accompanying notes 70–74.

13. *See infra* text accompanying notes 76–79.

tus of this type of gambling activity will be weighed.[14]

II. FACTS AND HOLDING

After ending his employment with a private company in January of 1978, the taxpayer dedicated almost all of his working time to betting on dog races.[15] The taxpayer normally spent between sixty and eighty hours per week at the racetrack researching, preparing, and placing bets.[16] The taxpayer applied the results of his labor only for his own profit; he never sold tips nor placed bets for others.[17] Having no other profession or employment, the taxpayer was dependent upon his gambling activities to generate the bulk of his income. His only other source of income—interest, dividends, and sales of investments—amounted to only $6,498 during 1978.[18]

Because of the taxpayer's gambling activities in 1978, the taxpayer sustained a loss of $2,032 resulting from $72,032 wagered offset by $70,000 of winnings.[19] The taxpayer filed a 1978 federal income tax return in which he listed his net gambling losses on schedule E[20] but did not report his $70,000 of winnings as income.[21] The Commissioner of the Internal Revenue Service asserted a deficiency against the taxpayer ruling that the $70,000 of winnings were gross income and that the $70,000 of allowable gambling losses were "below the line" itemized deductions and subject to the minimum tax as in effect in 1978.[22]

The Tax Court ruled that there was no deficiency and held for the taxpayer despite the Commissioner's insistence that the taxpayer's failure to hold himself out as providing goods or services should preclude his activities from being considered a trade or business.[23] The Tax Court decision allowed the taxpayer to deduct his gambling losses as "above the line"[24] deductions in arriving at adjusted gross income.[25]

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14. *See infra* text accompanying notes 80–105.

15. Groetzinger v. Commissioner, 771 F.2d 269, 270 (7th Cir. 1985).

16. *Id.*

17. *Id.*

18. *Id.*

19. *Id.*

20. The taxpayer filed a Supplemental Income Schedule (Schedule E) in which he deducted only $70,000 of his gambling losses because gambling losses are only deductible to the extent of gambling winnings. I.R.C. § 165(d) (1982).

21. *Groetzinger*, 771 F.2d at 270.

22. *Id.* "Below the line" itemized deductions are subtracted from the taxpayer's adjusted gross income to the extent that the deductions exceed the taxpayer's zero bracket amounts. *See* I.R.C. § 211 (1982). The minimum tax on "items of tax preference" was imposed by I.R.C. §§ 56–57 (1976).

23. *Groetzinger*, 771 F.2d at 270.

24. "Above the line" deductions are subtracted from the taxpayer's gross income in arriving at his or her adjusted gross income. I.R.C. § 21 (1982).

25. *Id.* Deductions from gross income are more advantageous to the taxpayer than deduc-

The Commissioner of the Internal Revenue Service appealed this decision and the Court of Appeals for the Seventh Circuit affirmed the Tax Court's holding[26] and upheld the use of the facts and circumstances test over the goods and services test.[27] In examining the facts and circumstances of the case, the court of appeals focused on whether the taxpayer's income-producing activities constituted his livelihood.[28] In finding that the income-producing activities of the taxpayer did constitute his livelihood, the court held that for purposes of sections 62 and 162 of the Internal Revenue Code the taxpayer's gambling activities constituted a trade or business and thus, the taxpayer could deduct his losses and his ordinary and necessary business expenses as "above the line" deductions.[29]

III. BACKGROUND

The goods and services test had its genesis in the United States Supreme Court case of *Deputy v. du Pont*.[30] The taxpayer was the beneficial owner of sixteen percent of the du Pont Company stock.[31] For the purpose of protecting his investment interest, the taxpayer thought that the members of the company's executive committee should be given a financial interest in the company. However, the taxpayer did not have enough shares of stock readily assignable. Through a series of loans from other holders of du Pont stock, the taxpayer was able to secure the shares for the executive committee members.[32] As a result, the taxpayer wanted to deduct the expenses connected with the transactions and loans as ordinary and necessary business expenses.[33]

The majority of the *du Pont* Court ruled against the taxpayer on the narrow ground that the expenses sought to be deducted were not connected with the taxpayer's own income-producing activity but were instead related to the du Pont Company's business.[34] Therefore, the status of the taxpayer's income-producing activity was never determined. In Justice Frankfurter's concurrence[35] he concluded that trade or business status depends on "holding one's self out to others as en-

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tions from adjusted gross income because the latter are reduced by the taxpayer's zero bracket amount. *See id.*

26. *Groetzinger*, 771 F.2d 269, 277 (7th Cir. 1985).
27. *Id.*
28. *Id.* at 274.
29. *Id.* at 272–74.
30. 308 U.S. 488 (1940) (Frankfurter, J., concurring).
31. *Id.* at 490.
32. *Id.* at 490–92.
33. *Id.* at 492.
34. *Id.* at 493–94.
35. *Id.* at 499.

gaged in the selling of goods or services."[36] Even though the majority did not rule on the trade or business issue, Frankfurter's concurrence has spawned a progeny of cases applying the goods and services test.[37]

In 1941, one year after the *du Pont* opinion, the United States Supreme Court in *Higgins v. Commissioner*[38] was again faced with the trade or business issue. In *Higgins* the taxpayer conducted substantial activities directed toward managing his investment affairs.[39] The taxpayer maintained offices and staff for the purpose of coordinating his large and diverse investments.[40] The taxpayer claimed that the "elements of continuity, constant repetition, regularity and extent"[41] which characterized his income-producing activity entitled his income-producing activity to trade or business status.

When deciding the *Higgins* case, the Supreme Court failed to confirm the goods and services test as the standard for trade or business analysis,[42] and merely concluded that trade or business status is dependent upon the facts of each case.[43] Given the opportunity to adopt the goods and services test, the Supreme Court instead relied on the facts and circumstances test to resolve the trade or business issue.[44]

Over thirty years later, in *Snow v. Commissioner*,[45] the Supreme Court was faced with the trade or business issue in the context of section 174 of the Internal Revenue Code[46] which allows research and development deductions. Although the Supreme Court mentioned the goods and services test, the Court concluded that the trade or business language of section 174 should be interpreted broadly by a facts and circumstances analysis.[47] In addition, because section 174 has a broader trade or business provision than section 162, a holding adopting the narrower goods and services test would have suggested an intention to use the more restrictive standard for the section 162 provision.[48]

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36. *Id.*

37. *See, e.g.*, Estate of Cull v. Commissioner, 746 F.2d 1148 (6th Cir. 1984); Gajewski v. Commissioner, 723 F.2d 1062 (2d Cir. 1983); Gentile v. Commissioner, 65 T.C. 1 (1975), *rev'd*, 80 T.C. 362 (1983).

38. 312 U.S. 212 (1941).

39. *Id.* at 213–14.

40. *Id.*

41. *Id.* at 215.

42. *Id.* at 217–18.

43. *Id.*

44. *Id.* "To determine whether the activities of a taxpayer are 'carrying on a business' requires an examination of the facts in each case." *Id.* at 217.

45. 416 U.S. 500 (1974).

46. *Id.* at 501. *See generally* I.R.C. § 174 (1982).

47. *Snow*, 416 U.S. at 503 (the Court also did not decide whether the goods and services standard should be used in conjuction with the facts and circumstances standard).

48. The facts and circumstances test is a broad standard in that it allows the trial court more discretion in finding trade or business status. Since the goods and services test is more re-

However, the Supreme Court did not so hold.[49]

Since *Snow*, the Supreme Court has not had an opportunity to lay to rest the debate over whether the goods and services or the facts and circumstances test should be the only standard used for "trade or business" analysis. On the contrary, during the silence of the Supreme Court, the lower courts have chosen conflicting positions so that a split in the courts' holdings has distinctly arisen.[50] Thus, the trade or business status of many taxpayers, including the taxpayer in *Groetzinger*, is dependent upon the circuit in which the case is heard.[51] The *Groetzinger* case was decided within the framework of this inconsistency, and the reconciliation of the courts in their position on the trade or business issue is a pressing problem in establishing uniform treatment for similarly situated taxpayers.

IV. ANALYSIS

A. *The* Groetzinger *Court's Analysis*

In *Groetzinger v. Commissioner*,[52] the Court of Appeals for the Seventh Circuit analyzed the trade or business issue. In holding for the taxpayer and allowing ordinary and necessary trade or business expense deductions,[53] the court first analyzed precedent dealing with the proper standard for determining the trade or business status of any income-producing activity.[54] The court recognized that the circuits were split as to whether to use the goods and services test or the facts and circumstances test.[55] While noting that Justice Frankfurter's concurring opinion in *Deputy v. du Pont*[56] supported the goods and services test,[57] the *Groetzinger* court concluded that the United States Supreme Court has never adopted, even implicitly, the goods and services test as the required standard[58] for determining trade or business status.

The Court of Appeals for the Seventh Circuit next attempted to determine the congressional purpose behind the enactment of sections

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strictive in that fewer activities will gain trade or business status under it, if a section that has a broader trade or business provision is held to require a goods and services test, then a narrower provision must also require a narrower test than the facts and circumstances test.

49. *Snow*, 416 U.S. at 500.
50. *See* cases cited *supra* note 8.
51. *Id.*
52. 771 F.2d 269 (7th Cir. 1985).
53. *Id* at 274.
54. *Id.* at 271–72.
55. *Id.* at 271.
56. 308 U.S. 488 (1940).
57. *Groetzinger*, 771 F.2d at 272.
58. *Id.*

62[59] and 162[60] of the Internal Revenue Code. After searching the legislative history of these sections, the court found little indication of congressional support for either test and could find no other conclusive standard based upon the legislative history.[61] The court, however, did find a key to solving the problem on the face of the statute itself.

Section 62(1) allows deductions for business or trade expenses only when the "trade or business does not consist of the performance of services by the taxpayer as an employee."[62] The Court of Appeals for the Seventh Circuit reasoned from the language of section 62(1) that the main purpose of the section was to give taxpayers who incur many expenses in the course of their trade or business a deduction.[63] "The most obvious distinction between employees and non-employees earning income is that the latter incur many expenses in earning a living or in their occupation or livelihood that the former do not."[64] The expenses incurred by an employee are usually incidental to his livelihood and resemble personal expenses.[65] Examples of these expenses include traveling expenses to and from work and meal expenses.[66] On the other hand, the expenses of an employer are directly related to producing the income which represents his livelihood and are, by nature, trade or business expenses.[67]

Providing a narrower focus to the facts and circumstances test, the *Groetzinger* court concluded that the key inquiry in determining trade or business status is "whether certain activities of a taxpayer can fairly be characterized as a livelihood, occupation or means of earning a living."[68]

In support of its position, the court of appeals analogized the full-time gambler to the high-volume, short-term trader.[69] The court recognized that long-term investment, like casual gambling, is generally a personal activity designed to preserve the income already gained from the taxpayer's livelihood.[70] High-volume, short-term trading, like full-time gambling, however, is usually a taxpayer's means of earning a

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59. *Id.* at 272–74. *See supra* notes 1–2 and accompanying text for the wording of the section.
60. *Id.* at 272-74. *See supra* notes 1-2 and accompanying text for the wording of the section.
61. *Id.* at 274.
62. *Id.* at 273 (quoting 26 U.S.C. § 62(1) (1976)).
63. *Id.*
64. *Id.*
65. *See id.*
66. I.R.C. § 62(2), (8) (1982).
67. *Groetzinger*, 771 F.2d at 273.
68. *Id.* at 274.
69. *Id.* at 275–76.
70. *Id.* at 273.

living.[71] The expenses incurred both in long-term investment and casual gambling are incidental to the production of income.[72] On the other hand, the expenses incurred in high-volume, short-term trading and full-time gambling are integral to the livelihood of the taxpayer.[73] High-volume, short-term trading has been afforded trade or business status[74] and therefore, due to their key similarities, full-time gambling should also gain trade or business status.[75]

Finally, the Court of Appeals for the Seventh Circuit noted that the goods and services test has not provided "clarity or simplicity" in resolving the trade or business issue.[76] The court of appeals calculated that the livelihood inquiry provides as much simplicity and clarity as the goods and services test[77] and is better designed to fulfill the purpose of section 62.[78] Despite this assertion, however, the goods and services test may provide a more certain standard.[79]

An application of each test to a slight variation of the fact pattern present in *Groetzinger*[80] illustrates that the court of appeal's assertion may not be supportable. The taxpayer might have devoted less time to gambling, thirty to forty hours per week, and had more income from other sources, for example a part-time job in which the taxpayer earned $6,000 per year. Application of the "livelihood" inquiry raises a number of questions. At what point does the taxpayer stop earning a sufficient livelihood from gambling so that his or her gambling activities are no longer considered a "trade or business?" Does the taxpayer's gambling activity have to be his only means of earning a living? Or should the standard be predominant, substantial, or significant in determining the extent the activity must have in providing the taxpayer's livelihood in order to determine trade or business status? The goods and services test eliminates these considerations. Under the goods and services test, the taxpayer's gambling activities do not constitute a holding out to others of goods or services; therefore, the gambling activities would automatically be disqualified from trade or business

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71. *Id.* at 275.

72. *See id.*

73. *Id.*

74. *See* Levin v. United States 597 F.2d 760, (Ct. Cl. 1979) (taxpayer's speculation in the stock market rose to the level of carrying on a trade or business). *But see* Moller v. United States, 721 F.2d 810 (Fed. Cir. 1983) (taxpayer's activities with respect to his investments were held insufficient to be characterized as trading and did not qualify for trade or business status); Purvis v. Commissioner, 530 F.2d 1332 (9th Cir. 1976) (same finding).

75. *Groetzinger*, 771 F.2d at 274–75.

76. *Id.* at 276.

77. *Id.* at 276–77.

78. *Id.*

79. *See infra* text accompanying notes 81–84.

80. 771 F.2d 269 at 270-71.

status.[81]

The goods and services test presents a watershed which appears to simplify trade or business determination. This approach can be effectively illustrated by comparing the full-time gambler, such as the taxpayer in *Groetzinger*,[82] with the gambler who sells tips and places bets for others. Under the facts and circumstances test and the livelihood inquiry, both the independent gambler and the "bookie" could be considered as being involved in a trade or business.[83] The outcome would depend upon the extent to which their activities constituted their livelihood. To decide this issue a court would have to consider many collateral issues such as the totality of the taxpayer's income-producing activities and the use to which the taxpayer put the fruit of these activities. The goods and services test eliminates these collateral issues and provides a more rapid means of resolving the activity's status. A bookie holds himself or herself out as providing a service of selling tips and placing bets; therefore, his or her activities would be considered a trade or business. The independent, full-time gambler does not hold himself out as providing goods or services; therefore, his activities would not be considered a "trade or business." This comparative analysis displays how courts may achieve more rapid dispositions of cases involving the trade or business issue.

However, as the *Groetzinger* court pointed out, there are two essential principles underlying the trade or business issue which make the rapid disposition qualities of the goods and services test less persuasive than the better-reasoned analysis provided by the facts and circumstances test and the "livelihood" inquiry.[84] The first principle is that the taxpayer involved in a trade or business has "the good faith intent . . . to make a profit or produce income."[85] The second principle is that a trade or business is characterized by "continuity, repetition and extensiveness"[86] in its income-producing activities.

B. Good Faith Intent to Make a Profit or Produce Income

The Supreme Court of the United States confronted the first of these principles in *Higgins v. Commissioner*.[87] In *Higgins* the taxpayer devoted extensive time and resources to managing his investments.[88]

81. *See, e.g.*, Gentile v. Commissioner, 65 T.C. 1 (1975).
82. 771 F.2d at 270.
83. *See id.* at 272–74.
84. *Id.* at 274.
85. *Id.*
86. *Id.*
87. 312 U.S. 212 (1941).
88. *Id.* at 214.

The taxpayer rented offices and hired a staff for the sole purpose of coordinating his extensive financial investments.[89] The major expenses of rent and salaries, as well as the active, busy nature of this income-producing activity, gave it the appearance of a "trade or business." Nevertheless, the Court held that no matter how much the taxpayer's investment activities resembled a trade or business, they were still by nature investment, rather than trade or business, activities.[90]

In applying the analysis used by the Supreme Court in *Higgins* to the situation of the full-time gambler, it is again helpful to consider the analogy to the high-volume, short-term trader. While the trader of stocks and securities may appear to be involved in merely an investment activity, the nature of high-volume, short-term trading more closely resembles a trade or business.[91] A trader deals in a large number of stocks and securities and generally only possesses a given stock or security for a very short time.[92] His holding period may be as short as ten minutes and is generally not longer than a few months.[93] This type of activity differs significantly from the long-term investment which involves a profit generated over a period of a year or longer.[94] The long-term investor is much more passive than the short-term investor.[95] The long-term trader invests by using money or property already acquired through prior investments or through the proceeds from his or her trade or business. The short-term trader generates income through original income-producing activities.

Full-time gambling has the same characteristics as high-volume, short-term trading. The gambler makes a large number of bets which have an outcome in a very short time. The period between the placing of a bet and its payoff may be as short as a few minutes and usually is no longer than a few days. In essence, the full-time gambler, like the short-term trader, generates income through his or her own activities.

The focus of the Supreme Court's analysis in *Higgins* is the nature of the income-producing activity.[96] The continuity, regularity, and extent of the taxpayer's efforts in pursuing the income-producing activity are not determinative of trade or business status.[97] An analysis of all the facts to determine if the income-producing activity is business-like in nature is the proper approach to solving the trade or business ques-

89. *See id.*
90. *Id.* at 218.
91. *See supra* text accompanying notes 69–75.
92. *See generally Groetzinger*, 771 F.2d at 274–75.
93. *Id.* at 275.
94. *Id.*
95. *Id.*
96. *Higgins*, 312 U.S. at 212.
97. *See id.* at 217–18.

tion.[98] Since the full-time gambler's activity involves the original creation of wealth, by nature his or her activities should be characterized as "trade or business" activities.

C. The Continuity, Repetition, and Extensiveness of Income-Producing Activity

The United States Supreme Court confronted the second principle in *United States v. Gilmore*.[99] In *Gilmore* the taxpayer was president, principal managing officer, and controlling shareholder of three corporations.[100] During the taxpayer's divorce trial he incurred considerable expenses to protect these assets from his wife's claims and then sought to deduct the expenses because they were connected with his trade or business.[101] The Supreme Court held that the connection with the taxpayer's trade or business did not depend upon the consequences of not incurring the expenses but rather upon the nature of the income-producing activity itself.[102]

In light of the precedent set out by the Supreme Court in *Gilmore*, it would be fruitless for the full-time gambler to argue that if he had not incurred the expenses connected with his gambling activities he would not have been able to support himself and his family.[103] The consequences of not incurring the expenses are clearly not determinative.[104] After examining the Supreme Court's opinion in *Gilmore*, it would seem that the Court would also invalidate the *Groetzinger* livelihood inquiry[105] as the sole standard for analyzing the trade or business issue. The livelihood inquiry focuses upon the consequences of incurring the expenses: earning a living. Under *Gilmore* this is not a permissible inquiry. Nevertheless, the facts and circumstances test and the livelihood inquiry—if used to determine the *nature* of the activity—can provide a well-reasoned basis for determining trade or business status.

V. CONCLUSION

The federal circuit courts of appeals are divided as to whether to use the goods and services test or the facts and circumstances test to resolve the trade or business issue.[106] The analysis of the trade or business issue by the Court of Appeals for the Seventh Circuit in *Groetz-*

98. *Id.*
99. 372 U.S. 39 (1963).
100. *Id.* at 41.
101. *Id.* at 40, 42.
102. *Id.* at 48.
103. *See id.* at 39.
104. *Id.* at 48.
105. *Groetzinger*, 771 F.2d at 274.
106. *See* cases cited *supra* note 8.

inger presents a good precedent for using the facts and circumstances test with a livelihood inquiry. The facts and circumstances test better implements the purpose of sections 62 and 162 than the goods and services test since it allows a court to determine whether the very nature of the activity is that of a trade or business. The key is whether the income-producing activity involves the original creation of wealth or whether it is characteristically an investment.[107] The facts and circumstances test enables a court to make this determination. Although the facts and circumstances test is less precise and involves the resolution of more collateral issues than the goods and services test, it is more readily designed to allow a court to determine if an activity is by nature a trade or business. Therefore, the facts and circumstances test should be adopted as the standard for determining trade or business status.

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107. *See supra* text accompanying note 98.