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### Federal Income Tax—26 U.S.C. § 280A(c)(1)(A)—The Self-Employed Taxpayer's Dashed Hopes of a Home Office Deduction. *Commissioner v. Soliman*, 113 S. Ct. 701 (1993).

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FEDERAL INCOME TAX—26 U.S.C. § 280A(c)(1)(A)—THE SELF-EMPLOYED TAXPAYER'S DASHED HOPES OF A HOME OFFICE DEDUCTION. *Commissioner v. Soliman*, 113 S. Ct. 701 (1993).

I. INTRODUCTION

Self-employment is a growing phenomenon in America's business sector, due in part to advances in technology. Today, it is not uncommon to find a personal computer in the average American home. The array of available software and lower costs in photocopiers and facsimile machines have contributed to the increase in home businesses. Furthermore, a freelance worker can reduce the cost of overhead that might necessarily doom a small business by turning an extra bedroom into an office, a seemingly sensible decision.

*Commissioner v. Soliman*<sup>1</sup> has effectively dashed the hopes of self-employed taxpayers seeking to deduct any expenses incurred in the furnishing or use of an office at home which are connected with a trade or business. The Supreme Court held that a taxpayer may be entitled to a home office deduction only if the taxpayer spends the majority of his time in his office or actually meets clients in a home office.<sup>2</sup>

II. FACTS

In 1983, the tax year in question, Nader E. Soliman ("taxpayer") was a self-employed anesthesiologist who lived in Virginia and worked in hospitals in both Virginia and Maryland.<sup>3</sup> He had privileges to work in three hospitals, two in Maryland and one in Virginia,<sup>4</sup> none of which provided an office for him.<sup>5</sup> The taxpayer turned a spare bedroom of his Virginia condominium into an office, which he furnished with "a chair, desk, telephone, answering machine, sofa, copier, and filing cabinet"<sup>6</sup> and used exclusively for his medical practice.<sup>7</sup> In this office he kept his medical library, patient records

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1. 113 S. Ct. 701 (1993).

2. *Id.* at 708.

3. *Id.* at 704. For further discussion of the *Soliman* decision, see James A. Fellows, *Current Status of Home Office Deductions Needs Clarification*, 72 J. TAX'N 332, 334 (1990).

4. *Soliman v. Commissioner*, 935 F.2d 52, 53 (4th Cir. 1991).

5. *Id.*

6. *Id.*

7. *Soliman v. Commissioner*, 94 T.C. 20, 24 (1990). One of the requirements of 26 U.S.C. § 280A(c)(1) is that the portion of the dwelling unit that is allocated as an office for a trade or business must be "exclusively used on a regular basis." 26 U.S.C. § 280A(c)(1) (1988). The Commissioner conceded that Dr. Soliman met this requirement. 94 T.C. at 24.

and correspondence, billing records, and information on surgeons, collections, and insurance.<sup>8</sup> He spent two to three hours per day in his home office performing such necessary tasks as telephoning surgeons, hospitals, and patients; maintaining billing records and patient charts; researching and preparing for specific patient treatments; preparing for monthly presentations to post-anesthesia care nurses (required by one of the hospitals); and performing work required to satisfy the profession's continuing medical education requirements.<sup>9</sup> The taxpayer spent thirty to thirty-five hours per week in the three hospitals administering anesthesia, caring for patients following surgery, and treating patients for pain.<sup>10</sup>

On his 1983 tax return, the taxpayer claimed deductions for his home office, including a portion of his utilities, condominium fees, and depreciation on the condominium.<sup>11</sup> Following an audit, the Commissioner of Internal Revenue ("Commissioner") disallowed these deductions, ruling that the home office was not the taxpayer's principal place of business.<sup>12</sup> The Commissioner assessed a deficiency, and the taxpayer sought review of the assessment by filing a petition in the Tax Court.<sup>13</sup>

The Tax Court reversed the Commissioner,<sup>14</sup> finding specifically that the taxpayer's home office was his principal place of business.<sup>15</sup> The Tax Court abandoned the "focal point" test, which identified the principal place of business as that "where services are performed and income is generated," citing criticism of the test by two courts of appeals.<sup>16</sup> The Tax Court formulated a new "facts and circumstances" test, which provided "that where management or administrative activities are essential to the taxpayer's trade or business and the only available office space is in the taxpayer's home, the 'home office' can be his 'principal place of business.'"<sup>17</sup>

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8. 935 F.2d at 53.

9. 113 S. Ct. at 704.

10. *Id.*

11. *Id.*

12. *Id.*

13. *Id.*

14. 94 T.C. at 29. This was an eleven to six decision. *Id.* at 31-34, 41.

15. *Id.* at 29.

16. *Id.* at 24-25. Criticism of the focal point test is found specifically in *Meiers v. Commissioner*, 782 F.2d 75 (7th Cir. 1986), *Weissman v. Commissioner*, 751 F.2d 512 (2nd Cir. 1984), and *Drucker v. Commissioner*, 715 F.2d 67 (2nd Cir. 1983). These courts generally advocated a "comparative analysis of the functions performed at each location." 113 S. Ct. at 705.

17. 935 F.2d at 54. The tax court listed three factors that weighed heavily in finding that the taxpayer's home office was his principal place of business: "[The] home office is essential to [the taxpayer's] business, he spends substantial time there, and there is no other location available to perform the office functions of the business." 94 T.C. at 29.

The Commissioner appealed to the Fourth Circuit Court of Appeals.<sup>18</sup> The court of appeals affirmed the Tax Court's decision and approved the new facts and circumstances test.<sup>19</sup> The court supported its decision by citing a proposed Treasury regulation allowing salespersons who spend "a substantial amount of time on paperwork at home" to deduct expenses for home offices.<sup>20</sup> Although the court acknowledged that the proposed regulation was not binding, it declared that the regulation reflected a policy of permitting home office deductions for taxpayers who legitimately maintain home offices, even if a majority of the taxpayer's time is not spent in the office.<sup>21</sup>

The Supreme Court granted certiorari<sup>22</sup> to resolve the conflict of the various tests advocated by the different circuits in determining the principal place of business with the presence of a home office.<sup>23</sup> The Supreme Court reversed the Fourth Circuit Court of Appeals and reinstated the focal point test with a few modifications, declaring that the hospital was the taxpayer's principal place of business, thereby disallowing any deductions for a home office.<sup>24</sup>

### III. HISTORICAL DEVELOPMENT

#### A. The "Appropriate and Helpful" Test

Section 162(a) of the Internal Revenue Code<sup>25</sup> allows "as a deduction all the ordinary and necessary expenses paid or incurred

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18. *Soliman v. Commissioner*, 935 F.2d 52 (4th Cir. 1991).

19. *Id.* at 53, 55. This was a two to one decision. *Id.*

20. *Id.* at 54 (citing Prop. Income Tax Reg. § 1.280A-2(b)(3), 45 Fed. Reg. 52,399 (1980) (proposed Aug. 7, 1980), as amended, 48 Fed. Reg. 33,320 (1983) (proposed July 21, 1983)). This regulation was proposed in 1980 but has not yet been approved by the Commissioner. *Id.* at 54 n.3. "Under the Commissioner's regulation promulgation procedures, a proposed regulation can lay dormant indefinitely until the Commissioner either withdraws the proposal or adopts a final draft of a proposal as a regulation." *Id.*

21. *Id.* at 54-55.

22. *Commissioner v. Soliman*, 112 S. Ct. 1472 (1991).

23. 113 S. Ct. at 705-06 (citing *Meiers*, 782 F.2d at 79; *Weissman*, 751 F.2d at 514). The Seventh Circuit Court of Appeals in *Meiers* held that the principal place of business was "where work is predominately performed." 782 F.2d at 79. The court reached this decision by examining the amount of time spent in the home office along with the importance of the business functions performed there, the business necessity of having a home office and the expenses required to establish the home office. *Id.*

The Second Circuit Court of Appeals in *Weissman* found that the taxpayer's principal place of business was "where the dominant portion of his work is accomplished." 751 F.2d at 514. This conclusion was reached by comparing the amount of time spent at each location and the importance of the activities performed at each location. *Id.* at 515.

24. 113 S. Ct. at 708.

25. 26 U.S.C. § 162(a) (1988).

during the taxable year in carrying on any trade or business.”<sup>26</sup> Prior to the Tax Reform Act of 1976, there was no statutory provision to guide courts in determining ordinary and necessary expenses for a home office, and the case law regarding deductions for an office in a personal residence was unsettled.<sup>27</sup> Thus, whether the deduction was granted varied from court to court.<sup>28</sup> Generally, the courts permitted taxpayers to deduct a pro rata share of proper expenses allocated to a home office under § 162(a) if the expenses were found to be “appropriate and helpful” to the taxpayer’s business.<sup>29</sup> This allowed many taxpayers to deduct otherwise nondeductible family and living expenses as business expenses.<sup>30</sup>

To eliminate this “loophole,” Congress passed § 280A as part of the Tax Reform Act of 1976.<sup>31</sup> Section 280A provides that “no deduction otherwise allowable under this chapter shall be allowed with respect to the use of a dwelling unit which is used . . . as a residence.”<sup>32</sup> The restrictions of § 280A serve as an exception to the deductions allowed by § 162(a).<sup>33</sup> There are three exceptions to § 280A, found in § 280A(c), two of which are relevant here:

Subsection (a) shall not apply to any item to the extent that such item is allocable to a portion of the dwelling unit which is exclusively used on a regular basis—(A) the principal place of business for any trade or business of the taxpayer. (B) [A]s a place of business which is used by patients, clients, or customers in meeting or dealing with the taxpayer in the normal course of his trade or business . . . .<sup>34</sup>

This statute was Congress’ answer to what it saw as a need for explicit rules establishing the proper standard for determining the

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26. *Id.*

27. Fellows, *supra* note 3, at 332.

28. Fellows, *supra* note 3, at 332.

29. 113 S. Ct. at 705. *See Newi v. Commissioner*, 432 F.2d 998 (2d Cir. 1970) (allowing deduction for a television executive who watched television advertisements of competitors in “home office”).

30. 113 S. Ct. at 705. *See also* H.R. REP. NO. 658, 94th Cong., 2nd Sess. 160, *reprinted in* 1976 U.S.C.C.A.N. 3050, 3053-54.

31. 935 F.2d at 54 (referring to The Tax Reform Act of 1976, Pub. L. No. 94-455, 90 Stat. 1520 (codified in scattered sections of 26 U.S.C.)).

32. 26 U.S.C. § 280A(a) (1988).

33. 113 S. Ct. at 705.

34. 26 U.S.C. § 280A(c)(1)(A) and (B) (1988). There is a third exception in § 280A(c)(1)(C) which allows for a deduction “in the case of a separate structure which is not attached to the dwelling unit, in connection with the taxpayer’s trade or business.” For a short discussion of the deduction allowed under this particular section, see Henri C. Pusker, *Home Office Deductions: Some Good News*, 18 J. REAL EST. TAX’N 24, 31 (1990).

deductibility of expenses of a home office.<sup>35</sup> Congress was concerned that expenses, which were otherwise considered nondeductible because they were personal, living, and family expenses, might become deductible business expenses because the expenses were “appropriate and helpful” in performing a portion of the taxpayer’s business in his home.<sup>36</sup> Congress hoped to eliminate the “subjective determination” inherent in the “appropriate and helpful” standard by providing “definitive rules” in § 280A.<sup>37</sup>

### B. The “Focal Point” Test

Congress never defined “principal place of business” in § 280A, and the tax courts responded by developing the “focal point” test.<sup>38</sup> In the case of a self-employed taxpayer, the focal point was that place where goods or services generated by the taxpayer were provided to customers.<sup>39</sup> One of the leading cases in developing the focal point test was *Baie v. Commissioner*.<sup>40</sup> In *Baie*, the taxpayer owned a hot dog stand and sold food to the public.<sup>41</sup> Because of the cramped quarters of the stand, she prepared the food to be sold in her kitchen and used a spare bedroom to keep records of the business.<sup>42</sup> Prior to the passage of § 280A, the Tax Court no doubt would have allowed deductions for use of the rooms in her home because such usage was “appropriate and helpful” for her sales from the hot dog stand.<sup>43</sup> However, the Tax Court held that the principal place of business, the focal point for a sole proprietor, was where the sales were actually made to the consuming public, not where any preparation or essential record-keeping took place.<sup>44</sup> Thus, the taxpayer was denied any deductions for the use of her home.<sup>45</sup>

### C. Criticism of the Focal Point Test

It was not long before criticism of the focal point test emerged in several of the circuit courts of appeals. In *Drucker v.*

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35. H.R. REP. No. 658, 94th Cong., 2nd Sess. 160, *reprinted in* 1976 U.S.C.C.A.N. 3050, 3053.

36. *Id.* at 3053-54.

37. *Id.* at 3054.

38. 935 F.2d at 54.

39. *Id.* In the case of an employee, the focal point was where the taxpayer’s income was generated, i.e., his employer’s place of business. Fellows, *supra* note 3, at 332.

40. 74 T.C. 105 (1980).

41. *Id.* at 106.

42. *Id.* at 106-07.

43. *Id.* at 108.

44. *Id.* at 109.

45. *Id.*

*Commissioner*,<sup>46</sup> the Second Circuit Court of Appeals reversed the Tax Court's decision that deductions for expenses incurred in a "home office" were disallowed.<sup>47</sup> The taxpayers were employed as concert musicians by the Metropolitan Opera.<sup>48</sup> The taxpayers had practice rooms set up in their homes where they spent thirty to thirty-two hours per week studying or practicing, many more hours than were spent in actual rehearsal or performance.<sup>49</sup> The Tax Court applied the focal point test and held that the taxpayers, as employees, had the same principal place of business as their employer, Lincoln Center.<sup>50</sup> The court of appeals rejected this and declared that the home practice studios of the musicians were their principal places of business.<sup>51</sup> Although the court acknowledged that the taxpayers were employees, the court held that this was a "rare situation in which an employee's principal place of business is not that of his employer."<sup>52</sup> The court further stated that this finding was in harmony with the legislative history of § 280A.<sup>53</sup> The failure of their employer to provide practice facilities to the musicians and the requirement of private practice for their profession were considered to be overriding factors.<sup>54</sup>

The following year the Second Circuit Court of Appeals followed its decision in *Drucker*, again reversing the Tax Court, in *Weissman v. Commissioner*.<sup>55</sup> The taxpayer, a college professor, spent approximately twenty percent of his working time on the college campus and eighty percent in his home office.<sup>56</sup> Although the school did provide office space on the campus, it had to be shared with other professors, and even the Tax Court found that it was not safe for the taxpayer to leave his teaching, research, or writing notes and equipment in that office.<sup>57</sup> Nevertheless, the Tax Court sought to determine the focal point of the taxpayer's business activities and found that, for those who teach, it is the educational institution.<sup>58</sup> The court of appeals declared that the Tax Court had "focused too much on Professor Weissman's title and too little on his activities,"

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46. 715 F.2d 67 (2nd Cir. 1983).

47. *Id.* at 68.

48. *Id.*

49. *Id.* at 68-69.

50. *Id.* at 69.

51. *Id.*

52. *Id.*

53. *Id.*

54. *Id.* at 70.

55. 751 F.2d 512 (2nd Cir. 1984).

56. *Id.* at 513.

57. *Id.*

58. *Id.* at 514.

and that as a matter of law it erred by failing to contemplate all aspects of the taxpayer's activities.<sup>59</sup> The court specifically criticized the use of the focal point test because it is centered on the place where the work of the taxpayer is more visible, instead of where the primary portion of the work is performed.<sup>60</sup> The court saw a similarity between the practice room required for a musician in *Drucker* and a suitable office for a college professor.<sup>61</sup> Both were viewed as a "practical necessity" that justified the deductions.<sup>62</sup>

The focal point test was criticized once more, this time by the Seventh Circuit Court of Appeals in *Meiers v. Commissioner*.<sup>63</sup> This case represents the first challenge to the focal point test involving self-employed taxpayers. The taxpayers owned a self-service laundromat. One of the taxpayers, functioning as manager, spent twice as much time with record-keeping activities in the taxpayers' home office as in the laundromat itself.<sup>64</sup> It was undisputed that these taxpayers had made a logical business decision to locate their office in their home instead of the laundromat.<sup>65</sup> Applying the focal point test, the Tax Court disallowed any deductions for the home office, concluding that the laundromat itself was the focal point of the taxpayers' laundry business.<sup>66</sup> Citing *Drucker* and *Weissman*, the Seventh Circuit Court of Appeals questioned the practicality of the focal point test<sup>67</sup> and agreed with the Second Circuit Court of Appeals that the focus was mistakenly placed on more visible business activities.<sup>68</sup> The court conceded that the focal point test was an easier standard to implement, but it did not believe that the test was fair to taxpayers or appropriately carried out the intent of Congress.<sup>69</sup> The Seventh Circuit Court of Appeals declared that the

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59. *Id.*

60. *Id.*

61. *Id.* at 514-15.

62. *Id.* The court stated "in each case the determination of a taxpayer's principal place of business depends on the nature of his business activities, the attributes of the space in which such activities can be conducted, and the practical necessity of using a home office to carry out such activities." *Id.* The court noted that not only did the taxpayer spend the majority of his time in the home office, but the home office was required because of the lack of suitable office space on the campus. *Id.* at 515. In addition, because the taxpayer was an employee of the college, he had to satisfy the convenience-of-the-employer test, which the court found was met. *Id.* at 516-17.

63. 782 F.2d 75 (7th Cir. 1986).

64. *Id.* at 76.

65. *Id.*

66. *Id.*

67. *Id.* at 78-79.

68. *Id.* at 79.

69. *Id.*



taxpayers' principal place of business was their home office and suggested several factors to be considered in such a determination, including the relative amount of time spent in the home office, the importance of the tasks performed in the home office, the business necessity of a home office, and the expense in establishing and maintaining the office in the taxpayer's home.<sup>70</sup> After applying these factors, and in light of the Commissioner's concession that there was no attempt by the taxpayers to "convert non-deductible personal living expenses into deductible business expenses," the Seventh Circuit allowed the home office deduction.<sup>71</sup>

In 1988, the Ninth Circuit Court of Appeals decided a case which presented a fact situation very similar to *Soliman*. In *Pomarantz v. Commissioner*,<sup>72</sup> the taxpayer was an emergency room physician who worked as an independent contractor at a local hospital.<sup>73</sup> Although he was not provided with private office space at the hospital, he did have access to a work area in the hospital that was furnished with a desk, chair, telephone, and medical texts.<sup>74</sup> The taxpayer maintained an office in his home, where he kept patient records, business records, and his medical library.<sup>75</sup> During the tax years in question, the taxpayer spent thirty-three to thirty-six hours per week at the hospital and usually even fewer hours per week working in his home office.<sup>76</sup> The Ninth Circuit declared that a taxpayer can only have one principal place of business for each trade or business.<sup>77</sup> The court of appeals upheld the Tax Court's use of the focal point test in finding that the taxpayer's principal place of business was the hospital where he performed his professional services.<sup>78</sup> Although the court of appeals did not endorse any standard to determine whether home office deductions should be allowed, the court did declare that, under any of the tests used by the Tax Court, the Second Circuit Court of Appeals, or the Seventh Circuit Court of Appeals, the hospital was the taxpayer's principal place of business.<sup>79</sup>

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70. *Id.*

71. *Id.*

72. 867 F.2d 495 (9th Cir. 1988).

73. *Id.* at 495.

74. *Id.*

75. *Id.*

76. *Id.* at 495-96.

77. *Id.* at 496 (citing *Curphey v. Commissioner*, 73 T.C. 766, 776 (1980)).

78. *Id.* at 497.

79. *Id.* The Tax Court advocated the "focal point" test (*Baie v. Commissioner*, 74 T.C. 105, 109 (1980)), the Second Circuit Court of Appeals urged a comparison of time spent and importance of the activities between the various locations (*Weissman v. Commissioner*, 751 F.2d 512, 514 (2nd Cir. 1984)), and the Seventh Circuit

#### D. The "Facts and Circumstances" Test

In 1990, the Tax Court in *Soliman v. Commissioner*<sup>80</sup> acknowledged criticism of the focal point test by the Second and Seventh Circuit Courts of Appeals and declared that "[i]n light of this response, we believe we need to revisit the 'focal point' test and our interpretation of § 280A . . . ."<sup>81</sup> The Tax Court admitted that application of the focal point test in the taxpayer's situation would have resulted in a conclusion that the home office was not the principal place of business.<sup>82</sup> The court then criticized the test as practically eliminating "the principal place of business exception" provided to taxpayers in § 280A.<sup>83</sup> Subsection (A) permits deductions for home offices if it is the taxpayer's principal place of business; subsection (B) allows a deduction if the home office is used for meeting clients or customers.<sup>84</sup> The Tax Court reasoned that by treating the principal place of business as the place where the taxpayer meets clients or customers, the focal point test effectively eliminates the principal place of business exception.<sup>85</sup> The court then declared that determining the "principal place of business" requires a review of the "facts and circumstances" of each case and concluded that the principal place of business may be the administrative headquarters of the business, even though the taxpayer meets customers and clients elsewhere.<sup>86</sup>

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Court of Appeals examined the relative amount of time spent in the home office, considered with the importance of the functions performed in the home office, the business necessity of the office, and the expenses required to establish the home office (*Meiers v. Commissioner*, 782 F.2d 75, 79 (7th Cir. 1986)).

80. 94 T.C. 20 (1990). This Tax Court decision was appealed to the Fourth Circuit Court of Appeals and then to the United States Supreme Court. It is the Supreme Court decision that is the subject of this casenote.

81. *Id.* at 25.

82. *Id.*

83. *Id.*

84. 26 U.S.C. § 280A(c)(1)(A) and (B) (1988).

85. 94 T.C. at 25. See *Drucker v. Commissioner*, 79 T.C. at 623 (Wilbur, J., dissenting).

Congress provided exceptions to the restrictions of section 280A by allowing deductions for a home office if either the home office is the taxpayer's principal place of business, section 280A(c)(1)(A), or it is used for meeting with the taxpayer's patients, clients, or customers in the taxpayer's business, section 280A(c)(1)(B). Goods and services could be transferred to customers and clients in the taxpayer's home, the "focal point," only if the taxpayer meets clients or customers in his home. The "focal point" test, therefore, merges the "principal place of business" exception with the "meeting clients" exception and practically eliminates the principal place of business exception from section 280A.

94 T.C. at 25.

86. 94 T.C. at 25-26. Optimism that the focal point test had been abandoned

The Tax Court acknowledged that the circuit courts' criticisms of the focal point test had suggested a comparison of the amount of time spent at various locations to determine the principal place of business.<sup>87</sup> The Tax Court rejected such a comparison in *Soliman* as misleading, because the diversity of the activities performed at each location would not lend itself to proper comparison.<sup>88</sup> The court declared that a taxpayer could qualify for deduction for a home office if the amount of time spent in the home office was "substantial."<sup>89</sup> The Tax Court further justified its decision by citing a proposed regulation directed at home office use by salespeople, where the standard of allowing a deduction was a "substantial amount of time."<sup>90</sup> The court reasoned that the proposed regulation recognized that taxpayers like *Soliman* may qualify for legitimate deductions for an office in the residence if there is no other space available and the taxpayer spends a substantial amount of time in the office.<sup>91</sup> *Pomarantz*<sup>92</sup> was distinguished as a case in which "the taxpayer . . . spent an insubstantial amount of time in his home office."<sup>93</sup> In addition to the amount of time spent in the home office, the court listed other considerations. These included whether

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was reflected in articles that appeared shortly after the Tax Court decision was announced. See, e.g., *Wisdom of Soliman Opens Door to Home Office Deductions*, 68 TAXES 403 (1990) (reprinted from CCH STANDARD FEDERAL TAX REPORTS No. 7, (Tax Focus), February 21, 1990); John C. Zimmerman, *Abandonment of the Focal Point Test for Office-in-Home Deductions*, 68 TAXES 434 (1990); Mark Levine, Note, *Home Office Deductions: Deserving Taxpayers Finally Get a Break*, 45 TAX LAWYER 247 (1991).

87. 94 T.C. at 24-25 (citing *Meiers v. Commissioner*, 782 F.2d 75 (7th Cir. 1986); *Weissman v. Commissioner*, 751 F.2d 512 (2d Cir. 1984); and *Drucker v. Commissioner*, 715 F.2d 67 (2d Cir. 1983)).

88. *Id.* at 26.

89. *Id.* at 27.

90. Prop. Income Tax Reg., 45 Fed. Reg. 52,399 (Aug. 7, 1980), as amended 48 Fed. Reg. 33,320 (July 21, 1983). This regulation proposed that if an outside salesperson had no other office available except his home office and he spent a "substantial amount of time" in this office, the home office could qualify as the principal place of business for the salesperson. The court pointed out that the regulation did not require the salesperson to spend more time in his office than on the road to qualify for the deductions, thus eliminating any comparison test. 94 T.C. at 27. However, this regulation has never been enacted by the Commissioner. See *supra* note 21.

91. 94 T.C. at 27. One of the criticisms by Justice Ruwe in his dissent in *Soliman* was the weight placed on a proposed regulation because "[p]roposed regulations are not entitled to judicial deference." *Id.* at 37 (Ruwe, J., dissenting).

92. *Pomarantz v. Commissioner*, 867 F.2d 495 (9th Cir. 1988).

93. 94 T.C. at 27. Another criticism Justice Ruwe expressed in his dissent of the *Soliman* decision was that no such finding was made by the court in *Pomarantz*. The Ninth Circuit simply found that Dr. Pomarantz "spent *more* time on duty at the hospital rather than at home." *Id.* at 39 (Ruwe, J., dissenting) (quoting *Pomarantz v. Commissioner*, 867 F.2d at 497) (emphasis added).

the home office was necessary, whether the activities of the home office were essential to the business, whether the home office was suitable for the business activities, and whether the furnishings of the home office were appropriate for an office.<sup>94</sup> The court declared that § 280A was not intended to force a taxpayer to rent commercial office space instead of working out of a home office and that Dr. Soliman's deductions were the type that Congress intended to allow.<sup>95</sup> The Tax Court concluded that the taxpayer's home office was his principal place of business and listed three factors that, if present, would give other taxpayers the same favorable holding: 1) the office is essential to the taxpayer's business; 2) a substantial amount of time is spent in the office; and 3) no other office is available to the taxpayer.<sup>96</sup>

The dissenting opinion by Judge Nims advocated continued use of the focal point test, modified somewhat to allow taxpayers the desired deductions if they spend the majority of their time in the home office.<sup>97</sup> This would maintain the test already established by the courts and also take into consideration unusual situations like musicians and college professors, who spend more time at home than anywhere else.<sup>98</sup> Justice Ruwe, in his dissent, acknowledged that the focal point test in some situations may unduly emphasize the location where the activities of the taxpayer are more visible.<sup>99</sup> However, he declared that deductions are a "legislative grace" and should be construed strictly.<sup>100</sup> He ultimately urged adoption of the standard of "where the dominant portion of the taxpayer's work is accomplished."<sup>101</sup>

The Fourth Circuit Court of Appeals affirmed the Tax Court's decision and endorsed the new facts and circumstances test.<sup>102</sup> After reviewing the history of the home office deductions, the court of appeals cited the proposed regulation regarding deductions for

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94. *Id.* at 28.

95. *Id.* at 29.

96. *Id.* at 28.

97. *Id.* at 32 (Nims, J., dissenting).

98. *Id.* Both Judge Nims and Judge Ruwe, in each respective dissent, felt that the new "facts and circumstances" test was a return to the old "appropriate and helpful" test, a test used by the courts prior to the passage of section 280A and resulting in abuses by taxpayers. *Id.* at 33 (Nims, J., dissenting) and 39 (Ruwe, J., dissenting). It was these very abuses that Congress was targeting when it passed § 280A. H.R. REP. NO. 658, 94th Cong., 2nd Sess. 160, *reprinted in* 1976 U.S.C.C.A.N. 3050 at 3053-3054.

99. 94 T.C. at 34 (Ruwe, J., dissenting).

100. *Id.* at 40.

101. *Id.* at 41.

102. *Soliman v. Commissioner*, 935 F.2d 52, 55 (4th Cir. 1991).

home offices of outside salespersons as a reflection of the same policy embodied in the new facts and circumstances test.<sup>103</sup> The court held that the regulation "evinced a policy to allow 'home office' deductions for taxpayers who maintain 'legitimate' home offices, even if the taxpayer does not spend a majority of his time in the office."<sup>104</sup>

Judge Phillips dissented,<sup>105</sup> agreeing with the dissent in the Tax Court opinion. He urged a continuation of the focal point test with some modifications.<sup>106</sup> Judge Phillips believed that the deduction should be granted for a home office only if the taxpayer spent the majority of his time in the office or if the most important work of the business was conducted in this office.<sup>107</sup>

#### IV. REASONING OF THE SUPREME COURT

The Supreme Court rejected the new facts and circumstances test and reinstated, for the most part, the focal point test.<sup>108</sup> Writing for the majority, Justice Kennedy declared that when interpreting the meaning of the words of the statute, the Court looks to the " 'ordinary, everyday senses' of the words."<sup>109</sup> The dictionary definition of "principal" is "most important, consequential, or influential."<sup>110</sup> To determine the principal place of business, that location which is the "most important, consequential, or influential," courts must compare all the places where business is conducted.<sup>111</sup>

The majority criticized the new test advocated by the Tax Court and upheld by the Fourth Circuit Court of Appeals as a return to the old "appropriate and helpful" test that Congress sought to eliminate with the passage of § 280A.<sup>112</sup> By allowing

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103. *Id.* at 54.

104. *Id.* at 55.

105. *Id.* at 55 (Phillips, J., dissenting).

106. *Id.* at 56.

107. *Id.* Judge Phillips further stated that a fair application of § 280A compelled a comparison of the various business locations to determine which was the principal place of business. *Id.*

108. 113 S. Ct. at 707. The Court stated, "In determining the proper test for deciding whether a home office is the principal place of business, we cannot develop an objective formula that yields a clear answer in every case." *Id.* at 706. But the Court later concluded that "the point where services are rendered or goods delivered is a principal consideration in most cases." *Id.* at 707. This is the essence of the "focal point" test.

109. *Id.* at 705-06 (quoting *Malat v. Riddell*, 383 U.S. 569, 571 (1966) (per curiam) (quoting *Crane v. Commissioner*, 331 U.S. 1, 6 (1947))).

110. *Id.* at 706 (quoting WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY 1802 (1971)).

111. *Id.*

112. *Id.*

deductions that are “essential” to a taxpayer’s business, the test failed to discern “whether the home office is more significant in the taxpayer’s business than every other place of business.”<sup>113</sup> Since § 280A permits deductions only for the principal place of business, the majority stated there must be a determination of what is the most important place of business.<sup>114</sup>

Acknowledging that a hard and fast rule would be impossible, the majority listed two primary considerations that should be used to determine if a home office is the principal place of business: “[T]he relative importance of the activities performed at each business location and the time spent at each place.”<sup>115</sup> To ascertain the level of importance at the various business locations, the trier of fact must first develop an “objective description of the business in question.”<sup>116</sup> With this “objective description” in hand, the judge can classify the activities at each location in light of the unique characteristics of a particular business or trade.<sup>117</sup> The majority acknowledged the usefulness of the focal point test and concluded that “the point where goods and services are delivered must be given great weight in determining the place where the most important functions are performed.”<sup>118</sup> The Court strengthened the focal point inquiry by declaring that “the point where services are rendered or goods delivered is a principal consideration in most cases.”<sup>119</sup> A “further and weighty consideration” is whether the goods or services are delivered at a facility that has unusual or special features, such as a hospital.<sup>120</sup>

Believing that all parts of a business are integrated and essential, the Court refused to give much weight to the “essential” nature of the business conducted in the taxpayer’s home office as the court of appeals had.<sup>121</sup> The Court was equally unswayed by the absence of alternative office space for the taxpayer, a factor that the court of appeals found important.<sup>122</sup> The Court saw this

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113. *Id.*

114. *Id.*

115. *Id.*

116. *Id.*

117. *Id.*

118. *Id.* The Court went on to point out that as long as a taxpayer meets with clients or patients in his home office or delivers goods or services in his home office, he will be allowed the deduction, even though it is not determined to be the principal place of business. The reasoning for this allowance is because Congress has granted this deduction for such visits or deliveries when conducted in the normal course of business. *Id.* at 706-07.

119. *Id.* at 707.

120. *Id.*

121. *Id.*

122. *Id.*

as a significant factor in the case of an employee using a home office for the convenience of the employer, but saw no relevance in terms of a self-employed taxpayer.<sup>123</sup>

The majority further stated that if an evaluation of the importance of the different locations of the business did not yield a clear answer as to the principal place of business, the trier of fact should then examine the amount of time spent at each location.<sup>124</sup> Concluding that, in the medical profession, the treatment given to patients was the most important event, that the delivery of such treatment was in a facility with special characteristics and that more time was spent in the special facility than in the home office, the majority held that the home office deductions sought by the taxpayer were not allowed.<sup>125</sup>

Justice Blackmun, in his concurring opinion, declared that, in addition to the arguments espoused by the majority, deductions from gross income are a matter of congressional grace, not a matter of right.<sup>126</sup> He viewed the starting point as a presumption against deductibility to which is applied any precise exceptions explicitly supplied by the Tax Code.<sup>127</sup>

In a concurring opinion joined by Justice Scalia, Justice Thomas advocated an unqualified return to the focal point test.<sup>128</sup> Justice Thomas argued that the test espoused by the majority would require the factfinder to engage in full evidentiary hearings to determine the principal place of business.<sup>129</sup> Additionally, he contended that the majority provided no guidance as to how the "two-factor inquiry" should work.<sup>130</sup> He reasoned that where the income is generated, that place where the goods or services are delivered to the client or customer, determines the principal place of business.<sup>131</sup> Justice Thomas strongly believed that the Court erred by not

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123. *Id.*

124. *Id.* The Court indicated that there may be cases where a principal place of business may not be found. In such cases, the home office expenses are not deductible simply by default, but are deductible only because they satisfy the requirements of the statute. *Id.* at 707-08.

125. *Id.* at 708. The Court reiterated its point that whether or not the functions performed in the home office were essential to the delivery of services to the patients in the hospital was not controlling. *Id.*

126. *Id.* at 708 (Blackmun, J., concurring) (citing *Commissioner v. Sullivan*, 356 U.S. 27, 28 (1958) and *Commissioner v. Tellier*, 383 U.S. 687, 693 (1966)).

127. *Id.*

128. *Id.* at 709 (Thomas, J., concurring).

129. *Id.*

130. *Id.*

131. *Id.* Justice Thomas further interpreted the focal point test to include a "totality of the circumstances" approach in cases where there were multiple points of sale. *Id.*

adopting the focal point test outright and, by not so doing, failed not only to clarify a question of law, but made the question more obscure.<sup>132</sup>

The sole dissenter in *Soliman* was Justice Stevens. Justice Stevens argued that denying the taxpayer deductions for his home office “deviates from Congress’ purpose in enacting [§ 280A], and unfairly denies an intended benefit to the growing number of self-employed taxpayers who manage their businesses from a home office.”<sup>133</sup> Justice Stevens pointed out that the expenses in *Soliman* fell within the general rule of deductibility.<sup>134</sup> The expenses were questioned, however, because the taxpayer’s residence was the site of the office.<sup>135</sup> If the office had been located in someone else’s house or in a separate structure located on the same property as the taxpayer’s home, these deductions would have been allowed.<sup>136</sup>

While acknowledging that deductions are a matter of congressional grace, Justice Stevens felt that the majority’s reading of the statute was too restrictive and resulted in “unequal treatment of similarly situated taxpayers.”<sup>137</sup> Justice Stevens observed that the major abuse which Congress sought to eliminate was the deduction of a home office by employees who were working at home on evenings and weekends and using the home as a “second office” for their own convenience and not for the convenience of the employer.<sup>138</sup> Section 280A requires a self-employed taxpayer to satisfy three conditions in order to qualify for a home office deduction. These three conditions, observed Justice Stevens, are more stringent than the “appropriate and helpful” standard that Congress was trying to eliminate.<sup>139</sup> First, the taxpayer must set aside a room or a portion of his residence for exclusive use in the business.<sup>140</sup> Justice Stevens stated that this requirement alone eliminates many of the employee abuses associated with home

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132. *Id.* at 710-11.

133. *Id.* at 711 (Stevens, J., dissenting).

134. *Id.*

135. *Id.*

136. *Id.*

137. *Id.* at 712. Justice Stevens further argues that such unfair treatment could have been required by the statute itself if such result was intended by Congress, but there was no reason to believe that this was Congress’ intent. *Id.* Justice Stevens agreed with the Tax Court’s statement that “Section 280A was not enacted to compel a taxpayer to rent office space rather than work out of his own home.” *Id.* at 712 n.3 (citing *Soliman v. Commissioner*, 94 T.C. 20, 29 (1990)).

138. *Id.* at 713 and n.8. Justice Stevens opines that “Congress may have been particularly offended by the home office deductions claimed by employees of the Internal Revenue Service.” *Id.* at 712 n.6.

139. *Id.* at 713.

140. *Id.*



office deductions.<sup>141</sup> Second, the taxpayer must use this designated space "on a regular basis."<sup>142</sup> Although there is no definition of what constitutes a regular basis,<sup>143</sup> it appeared clear to Justice Stevens that § 280A requires the use of the space to be substantial. Third, the taxpayer must meet one of the exceptions listed in § 280A(c)(1).<sup>144</sup>

Justice Stevens acknowledged that the taxpayer did not meet the conditions of § 280A(c)(1)(B), that the home office be used to meet clients or customers, or of § 280A(c)(1)(C), that the home office be contained in a separate structure.<sup>145</sup> It seemed clear to Justice Stevens that § 280A(c)(1)(A) was designed to cover those "places where the taxpayer does not normally meet with patients, clients, or customers."<sup>146</sup> Justice Stevens criticized the majority for its focus on the word "principal" and its neglect of the phrase "place of business."<sup>147</sup> He pointed out that in issues of jurisdiction and venue, "place of business" for a corporate defendant often is the administrative headquarters of a company.<sup>148</sup> He reiterated this point by stating, "The only place where a business is managed is fairly described as its 'principal' place of business."<sup>149</sup>

The majority insisted that Congress could have used the words "principal office" in § 280A to cover situations like that of the taxpayer but chose not to do so.<sup>150</sup> Justice Stevens responded by arguing that, in choosing those words, Congress would have further narrowed the deduction and would have excluded business uses, such as storage, that would qualify under the present statute.<sup>151</sup> Justice Stevens reasoned that the test advocated by the Tax Court

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141. *Id.* There was no assertion by the Commissioner that this condition was not met by Dr. Soliman.

142. *Id.*

143. *Id.* This condition was never in contention by the Commissioner.

144. *Id.* To qualify, the space must be used as

(A) the principal place of business for any trade or business of the taxpayer[;] (B) as a place of business which is used by patients, clients, or customers in meeting or dealing with the taxpayer in the normal course of his trade or business, or (C) in the case of a separate structure which is not attached to the dwelling unit, in connection with the taxpayer's trade or business.

*Id.* (quoting 26 U.S.C. 280A(c)(1) (1988)).

145. *Id.*

146. *Id.* at 714. Justice Stevens, like the Tax Court, argues that by requiring the principal place of business to be the location where the taxpayer meets with clients and customers, the Court merges Sections (A) and (B) and renders Subsection (A) meaningless. *Id.* See *supra* note 72 and accompanying text.

147. 113 S. Ct. at 714.

148. *Id.*

149. *Id.* at 714-15.

150. *Id.* at 706.

151. *Id.* at 715. Justice Stevens gives examples of an artist's studio or a cabinet-

and upheld by the Fourth Circuit Court of Appeals was "both true to the statute and practically incapable of abuse."<sup>152</sup> Justice Stevens concluded:

A self-employed person's efficient use of his or her resources should be encouraged by sound tax policy. When it is clear that no risk of the kind of abuse that led to the enactment of § 280A is present, and when the taxpayer has satisfied a reasonable, even a strict, construction of each of the conditions set forth in § 280A, a deduction should be allowed for the ordinary cost of maintaining his home office.<sup>153</sup>

#### V. IMPLICATIONS OF THE *SOLIMAN* DECISION

The significance of the *Soliman* decision is two-fold. First, the return to the focal point test, even with its modifications, denies the Tax Court the opportunity to fashion a liberal test that would allow certain taxpayers to receive the deductions of a home office, even when there is clearly no taxpayer abuse. Unless a taxpayer can meet the narrow definitions of § 280A, no deductions will be allowed for a home office, no matter how essential or important its existence is to the self-employed taxpayer.

Second, rather than clarify the law as the Court hoped to do, the *Soliman* decision seems to have muddied the waters more than before. The majority returned to the focal point test to define the "principal place of business," but injected "two primary considerations" to further assist in that determination: a comparison of the functions performed at each location and, if that does not produce a clear answer, a comparison of the amount of time spent at each location. But how does a factfinder weigh two completely different functions conducted at two different locations? Is the court not forced to interject its own value system upon various activities performed by a taxpayer to determine which is the most important?

Other issues were left unanswered by the opinion. What if the taxpayer had spent equal time between the hospitals and his home office? It would seem that the majority in *Soliman* would still deny the deductions, since the taxpayer would be performing services in a specialized facility and would be unable to meet patients in his home office. What if the taxpayer had spent more time in his home office than he did in the hospitals?<sup>154</sup> Because

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maker's workshop that might be excluded from allowable home-use deductions if Congress had chosen the words "principal office." *Id.*

152. *Id.*

153. *Id.*

154. Justice Thomas asks this question in his concurrence. *Id.* at 711.

of the professional need to use a facility with unique and special characteristics, it appears that, even in the face of spending less time in the hospital than in the home office, the majority would still hold that the hospital would be the taxpayer's principal place of business. What if the taxpayer hired employees to administer most of the anesthesia, supervised them from his home office, but still made daily trips to the hospital to check on patients, while occasionally administering anesthesia himself? Because the taxpayer's income would be derived from services performed at the hospital, it would still be within the reasoning of the *Soliman* decision to deny the taxpayer the deductions for the home office.

Assume that a taxpayer is in commercial construction and maintains a home office. Is the principal place of business for such a taxpayer the construction site? It is doubtful that Congress envisioned that such a principal place of business would change every few months or every year as one job was completed and a new one begun. However, under *Soliman*, the Court might find that a construction site is such a facility, with unique and special characteristics that mark it as the principal place of business. What if the construction manager succeeded in having his home office declared as his principal place of business by the IRS and then hired a secretary to work in his home office in order to allow him to spend more time on the construction sites? Does he then lose any chance of a deduction because he is spending more time at the site than in his office?<sup>155</sup> The focal point test, even with the Supreme Court's new modifications, seems to hurt taxpayers who have legitimate home offices and forces these taxpayers to rent commercial space.

## VI. CONCLUSION

If a taxpayer freelances outside of his home, it will now be difficult to meet the standards announced in the *Soliman* decision for § 280A deductions. The Supreme Court will continue to narrowly construe the language of § 280A to disallow all but the obviously-permitted deductions. The self-employed taxpayer's only hope is congressional relief. As Justice Blackmun observed, "Con-

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155. See J. Martin Burke and Michael K. Friel, *Recent Developments in the Income Taxation of Individuals*, 14 THE REV. OF TAX'N OF INDIVIDUALS 373 (1990).

gress must change the statute's words if a different result is desired as a matter of tax policy."<sup>156</sup>

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156. 113 S. Ct. at 709 (Blackmun, J., concurring).

