# Advantages of new Tax Court decision allow use of LIFO with completed contract method

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*A Tax Court holding that LIFO may be used with the completed contract method greatly enhances that method's use where there are numerous contracts. The authors analyze this decision and its ramifications for taxpayers in construction and manufacturing who either use or contemplate using the completed contract method.*

TAXPAYERS ENGAGED in long-term construction have long contemplated the use of the completed contract method in combination with the LIFO method of inventory valuation. In particular, since the adoption of a liberalized eligibility standard for the use of the completed contract method in 1976, large numbers of manufacturers have switched from the traditional accrual method to the completed contract method, a move which, until now, was thought to preclude such manufacturers from using a LIFO method with respect to the costs incurred in the long-term contract activities of such taxpayers.

For these taxpayers, the use of the completed contract method has provided significant income deferral on multi-unit contracts.[1] However, while the completed contract method permits contract revenues to be deferred until the completion of the contract, it also requires that contract costs be comparably deferred. In this regard, the completed contract method possesses marked similarities to the accrual method where inventories are maintained. Notwithstanding these similarities, the IRS has long taken the position that the adoption of the LIFO method (or other special inventory valuation rules) is incompatible with the use of the completed contract method.[2] With the recent enactment of the Tax Equity and Fiscal Responsibility Act of 1982, Congress has restricted considerably the liberal treatment accorded to costs incurred in performing long-term contracts.

As a result, taxpayers using the completed contract method will be especially vigilant in searching for ways to accelerate the deduction of long-term contract costs. With this in mind, it is particularly significant that in *Peninsula Steel Products and Equipment Co., Inc.*, 78 TC No. 74, the Tax Court ruled that a taxpayer may use the LIFO inventory method in conjunction with the completed contract method.

### *Analysis of decision*

The taxpayer, Peninsula Steel Products and Equipment Co., and its wholly-owned subsidiary, Monotech Corporation, were principally engaged in the manufacture and sale of air pollution control equipment. The equipment was manufactured in the taxpayer's plants or those of its subsidiary in component form and then shipped in kit form to the premises of customers for assembly by the taxpayer or its subsidiary. Peninsula's and Monotech's performance under typical contracts spanned two taxable years. Accordingly, both companies elected to use the completed contract method of accounting.[3]

Under the completed contract method of accounting, Peninsula and Monotech were required by Reg. 1.451-3(d)(1) to defer the inclusion of revenues in income and the deduction of costs associated with any particular contract until such contract was finally completed and accepted. Such treatment applies irrespective of the receipt of progress payments (often in excess of accumulated costs) prior to completion of the contract. The completed contract method, thus, afforded Peninsula and Monotech the ability to defer recognizing income on profitable contracts until such time as these contracts were completed and accepted. However, the recognition of losses on loss contracts would likewise have been deferred until completion of any such loss contracts.

In utilizing the completed contract method, an issue arises as to the method to be used to identify which costs are allocable to particular contracts and thus offset against contract revenues when a contract is finally completed and accepted.[4] Where a taxpayer performs relatively few contracts during the year, it may be possible specifically to identify the costs which are allocable to particular contracts. However, where a taxpayer undertakes work on many long-term contracts at the same time and has numerous items of cost incurred throughout the year, it may be impossible for specific costs to be identified with particular contracts. Furthermore, this identification problem is exacerbated when the same type of cost (*e.g.*, raw material) incurred with respect to long-term contracts is also incurred during the year in a standard inventory transaction without regard to the taxpayer's long-term contract business. In such cases, it is necessary to make an assumption not only as to how costs are shared between contracts completed during the year and contracts still in progress at year end, but also between long-term contracts and a taxpayer's general inventory accounts.

It is precisely this issue of identifying the costs to be attributed to long-term contracts completed and accepted during any given year which was presented to the Tax Court in the *Peninsula Steel* case. The Government argued that costs must be allocated to particular contracts-in-progress in the order in which such costs are incurred (*i.e.*, a FIFO basis). In contrast, the taxpayer contended that all of the costs of production, including the costs of raw materials purchased, would not be allocated to particular long-term contracts until such contracts were completed. Prior to completion, the taxpayer contended that the maintenance of a single inventory account, which included the cost of raw materials (both for specific contracts and as a general source of supply) and the costs of work-in-process, was appropriate. Furthermore, the taxpayer argued that the value of this single inventory account could be determined on a LIFO basis. Thus, under the taxpayer's method, the most recent purchase and production costs were allocated each year to contracts completed during such year and the historical costs were attributed to the raw materials and work-in-process remaining on hand. Only when the level of the ending inventory in equivalent dollars was less than the opening inventory level, would historical costs (in reverse chronological order) be allocated to contracts completed during the year.

The Tax Court in *Peninsula Steel* basically sided with the taxpayer. It held that the allocation of costs to specific long-term contracts need be done

only at the time that such contracts are completed and that the costs so allocated could be determined on a LIFO basis.

The Tax Court's conclusion that the LIFO method could be used in conjunction with the completed contract method was based on several grounds. First, the court concluded that the taxpayer's method of accumulating and allocating such costs amounted to a method of accounting which could not be disturbed unless such method failed to clearly reflect income.[5] Because, in the court's view, such method clearly reflected income, it concluded that the Commissioner could not change Peninsula's method of accounting under Section 446(b). Second, the Tax Court placed great weight on the taxpayer's consistent accounting practice. Consistency, as the court stated, "is a factor weighing heavily in petitioner's favor." The court also noted that the taxpayer's practice of inventorying raw steel and raw material costs allocable to work-in-process was a practical expedient given the large number of jobs and large quantities of steel on hand at any given time. Finally, the court concluded that the use of LIFO in this case was not inconsistent with either the Regulations or underlying concepts of the completed contract method.[6]

### *Who may rely on decision*

While the *Peninsula Steel* decision might be said to apply broadly to all taxpayers who employ the completed contract method, it seems apparent that the right to use the LIFO method in valuing deferred contract costs must be limited to those taxpayers whose deferred costs could be considered to be inventories within the meaning of Section 471.

One category of taxpayers who might be precluded from using the LIFO method are taxpayers engaged in a variety of real estate construction activities. As to these types of taxpayers, the Service has followed a long-standing position that taxpayers holding real property for *sale* in the ordinary course of their business do not possess inventories in the Section 471 sense.[7] This position has been upheld directly in one court decision and has been alluded to in dicta in several others.[8] The Service has also extended this interpretation in private rulings to accrual-basis taxpayers engaged in real estate construction.[9] However, this issue is now pending before the Tax Court.[10] If the Tax Court reverses the Service's position, long-term contractors engaged in the construction of apartment, office, and factory buildings, bridges, and roads would be able to take advantage of the *Peninsula Steel* decision.

Another major segment of the construction industry whose eligibility to use the LIFO method is unclear is the government contracting industry. It is now a standard practice in government contracts, and in some non-government commercial contracts, to provide that title to work-in-process is at all times vested in the government (or in the non-government customer). In *Ltr. Rul.* 8122001, the Service held that a contractor engaged in a construction project for the Federal Government under a contract which provided that title to the work-in-process was at all times vested in the government did not have inventories within the meaning of Section 471 and was, therefore, ineligible to value its deferred costs pursuant to the LIFO inventory method. The letter ruling relies on several court decisions which appear to hold that if a taxpayer lacks title to its work product, it does not have inventories in the conventional sense.[11]

There is, however, at least one decision which holds that the title passage clause in a government contract is merely security for the performance of the work and that any progress payments are in the nature of a loan to the contractor.[12] This latter notion is also closely tied in with the timing rules for revenue recognition of long-term contract progress payments. Under Regs. 1.446-1(c)(1)(ii) and 1.451-5(b)(1)(ii), an accrual basis contractor need not include progress payments under a contract in gross income until the subject matter of the contract is shipped, delivered or accepted. The presence of a government title passage clause apparently did not change this result according to *Ltr. Rul.* 8122001. Accordingly, it could be argued that the accounting treatment of progress payments under Sections 446 and 451 override the strict title notion in Section 471 to confer inventory treatment on deferred contract costs until the related progress payments are includable in gross income.

Recently, in *Rockwell International Corp.*, 77 TC 780 (1981), the Tax Court was afforded an opportunity to resolve the conflicting decisions in this area when faced with the question of whether a title passage clause in a government contract precluded the contractor from having inventories. The court was asked to determine the propriety of an accrual-method taxpayer's market writedowns (which writedowns could only occur if inventories were proper) on government contracts which were not yet completed. The Tax Court avoided having to decide this issue of the effect of title on inventories by rejecting the taxpayer's writedown methodology as being inconsistent with the rules of Reg. 1.471-2(c) and 1.471-4. Thus, the title passage issue remains a lingering uncertainty to government contractors seeking to follow the *Peninsula Steel* decision.

A third category of taxpayers for whom the *Peninsula Steel* decision has uncertain applicability is those taxpayers that employ the percentage of completion method for financial reporting purposes. Sections 472(c) and 472(e)(2) provide that as a prerequisite to the use of the LIFO method for tax purposes, a taxpayer may not use a method other than the LIFO method in valuing its inventories for financial reporting purposes. In T.D. 7756, 1/16/81, the Service substantially liberalized the Regulations dealing with the so-called "LIFO conformity requirement" in order to permit a wide variety of LIFO book/tax differences. However, these Regulations continue to require that a taxpayer's primary financial statements be maintained on a LIFO basis.

Many taxpayers that use the completed contract method for tax purposes employ the percentage of completion method for financial reporting purposes.[13] If a taxpayer uses the percentage of completion method for financial reporting purposes, it is possible that all of the costs of performing long-term contracts will have been expensed as they are incurred. Thus, there is a real question as to whether such a taxpayer has reported income for financial re-

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porting purposes under a LIFO method.

There appear to be two possible legal bases for justifying such methodology as not being inconsistent with the LIFO conformity requirement. The first contention is premised on the fact that the immediate expensing of contract costs under the percentage of completion method is tantamount to the use of no inventories at all. Since Sections 472(c) and 472(e)(2) merely require that no method of inventorying goods other than the LIFO method be used in a taxpayer's financial reports, the immediate expensing of contract costs does not appear to violate such requirement since it does not involve an inconsistent *inventory* method. There are, however, no administrative or judicial precedents on this point.

The other basis for defending the treatment of contract costs under the percentage of completion method is the contention that it represents a permissible timing difference under Reg. 1.472-2(e)(8). However, it is unclear whether such provision is intended to reach this type of disparity in book/tax reporting. There is at least one Service consent letter where the use of the percentage of completion method for financial reporting purposes was approved in a LIFO context where the taxpayer used the accrual shipment method for tax purposes. It is uncertain whether the Service would continue to follow this position after the *Peninsula Steel* decision.

Some taxpayers using the completed contract method for tax purposes and the percentage of completion method for financial reporting purposes have attempted to avoid this problem by maintaining inventories of raw materials and, in some cases, inventories of deferred progress expenditures under their financial reporting method, and have utilized the LIFO method in valuing such costs. If this approach is feasible for financial reporting purposes, it should eliminate the uncertainties in the LIFO conformity area.

### *How to elect*

How can taxpayers currently reporting income under the completed contract method adopt the LIFO method approved by the Tax Court in *Peninsula Steel*? One approach would be to employ the change in accounting method procedures set forth in *Rev. Proc.* 80-51, 1980-2 CB 818. However, it is unlikely that the Service would grant such taxpayers permission to change to the LIFO method under these circumstances. Accordingly, the question that arises is whether the LIFO method can be validly adopted by taxpayers employing the completed contract method without securing the prior consent of the Commissioner.

Reg. 1.446-1(e)(2)(i) provides:

"Except as otherwise expressly provided in Chapter 1 of the Code and the regulations thereunder, a taxpayer who changes the method of accounting employed in keeping his books shall, before computing his income upon such new method for purposes of taxation, secure the consent of the Commissioner. Consent must be secured whether such method is proper or is permitted under the Internal Revenue Code or the regulations thereunder."

Pursuant to the rule in the first sentence of this Regulation, Reg. 1.472-3 provides that any taxpayer permitted or required to take inventories under Section 471 may elect to compute its inventories in accordance with the LIFO method under Section 472 without securing the advance consent of the Commissioner. Reg. 1.472-3 merely requires that the taxpayer file with its income tax return for the taxable year as of the close of which the method is first to be used a statement of its election to use such inventory method.[14]

On the basis of these rules, taxpayers currently employing the completed contract method of accounting could validly adopt the LIFO method for the costs incurred in performing such long-term contracts to the extent that the previous treatment of such costs amounted to an inventory method of accounting. Where, however, the taxpayer's treatment of such costs does not constitute an inventory method, it would appear that such taxpayer must first secure the consent of the Commissioner in order to change to an inventory method of accounting with respect to such costs prior to adopting the LIFO method.

It may be possible for most, if not all, taxpayers who presently use the completed contract method to claim that they are using an inventory method in accounting for their deferred contract costs.[15] The treatment of costs under the completed contract method of accounting rules directly parallel the rules provided for taxpayers using the nonconforming method of accounting for tax and financial reporting purposes under the full absorption inventory costing requirements of Reg. 1.471-11 (c)(3). Thus, there appears to be considerable support for the proposition that taxpayers accumulating costs for completed contract purposes in accordance with Reg. 1.451-3(d)(5) are using an inventory method, since such methodology is comparable to that which would apply under the inventory Regulations. Furthermore, the Tax Court itself in *Peninsula Steel* recognized that the deferral of costs under the completed contract method was not inconsistent with, and could amount to, an inventory method of accounting.

The above discussion addresses certain problems for existing taxpayers who attempt to change to the method of accounting approved in the *Peninsula Steel* decision without securing the

[1] See Schneider, *Tax planning for contractors and manufacturers under new final Regs.*, 44 JTAX 210 (April 1976).

[2] See *Rev. Rul.* 59-329, 1959-2 CB 138.

[3] While the taxpayer vigorously argued that it reported income from its manufacturing activities under the "accrual shipment" method, the court dismissed this argument after it found that it was not "shipment" but rather "completion and acceptance" that precipitated income recognition by the taxpayer.

[4] This problem of allocating costs among various long-term contracts is distinct from the requirement that taxpayers using the completed contract method treat certain expenses incurred during the year as expenses directly attributable to long-term contracts which are deductible only when the specific contract is finally completed and accepted.

[5] See *Bay State Gas Co.*, 75 TC 410 (1980), cited by the court.

[6] See, however, Reg. 1.451-3(d)(6) which was not discussed by the court.

[7] See *O.D.* 848, 4 CB 47 (1921), *superseded by Rev. Rul.* 69-536, 1969-2 CB 109.

[8] *Atlantic Coast Realty Co.*, 11 BTA 416 (1928); *Keeney*, 17 BTA 560 (1929), *acq. in part; Loughborough Development Corporation*, 29 BTA 95 (1933), *acq.*

[9] See, *e.g.*, *Ltr. Rul.* 7907003.

[10] *Homes by Ayres*, Docket No. 1160-81; *Classic Development Corp.*, Docket No. 1389-81.

[11] *Gunderson Bros. Engineering Corp.*, 16 TC 118 (1951); *Boeing Co.*, 338 F.2d 342 (Ct. Cls., 1964).

[12] *Consolidated-Hammer Dry Plate & Film Co.*, 317 F.2d 829 (CA-7, 1963).

[13] In fact, from 1970 to 1972, when the Treasury attempted to condition the use of the completed contract method for tax purposes on its use in the taxpayer's financial reports, such attempt was viewed as an effective ban on the use of the completed contract method.

[14] Ordinarily the statement is made on Form 970. See also *Rev. Proc.* 74-2, 1974-1 CB 412.

[15] As discussed previously, certain long-term contractors may not be entitled to use inventories in cases involving sales of real estate and real estate construction, as well as cases where title is not vested in such contractors. For other long-term contractors who could have inventories, it must be further decided, as discussed in this portion of the article, whether inventories are maintained.

[16] See Reg. 1.472-8(e)(1).

[17] See *Rev. Rul.* 80-190, 1980-2 CB 161; Reg. 1.472-8(g)(1).

advance consent of the Commissioner. In contrast, a new taxpayer (*i.e.,* one filing its first return with respect to a trade or business), may adopt any permissible method of accounting in computing taxable income for the taxable year covered by such return. Thus, if the long-term contract business of an existing taxpayer can be transferred to a new subsidiary or affiliate, such new corporation can validly elect any proper method of accounting for its first taxable year. Where all of the assets of an existing corporation are transferred to a new affiliate, the Service could attack such a transfer as a reorganization, with the result that the methods of accounting employed by the transferor would carry over to the transferee under Section 381. However, it may be possible to achieve the desired result by forming a new subsidiary or affiliate to handle all new long-term contracts and arrange for this new corporation to adopt both the completed contract method and the LIFO method. As in all business changes, a valid business purpose must exist for shifting the long-term contract operations to a separate taxable entity in order for the separateness of such new entity to be respected.

***LIFO procedures***

One final significant problem that is likely to be faced by completed contract taxpayers seeking to follow the *Peninsula Steel* decision is the selection of a practical method of computing dollar-value LIFO. Under the traditional form of dollar-value LIFO, a taxpayer would double-extend the costs of its ending inventory of finished goods, work-in-process, and raw materials, at their current-year cost and at their base-year (or prior-year) cost, depending upon the particular form of indexing which is used.[16] However, such methodology is generally practical only in cases where the taxpayer is manufacturing standardized products with some degree of repetitiveness. In contrast, many taxpayers utilizing the completed contract method are constructing unique products. For such taxpayers, the use of a cost-component indexing technique may be the only feasible approach in making annual LIFO calculations. Under the cost-component method, a taxpayer would separately index the raw material, labor, and overhead cost of a product, rather than the aggregate cost of the product. Unfortunately, in *Ltr. Rul.* 7920008, the Service has challenged the validity of such approach.

Another significant technical problem might involve the pooling of the long-term contract deferred costs. To the extent that the long-term contract operations were conducted as a separate trade or business, they would probably be treated as a separate natural business unit pool under Reg. 1.472-8(b)(1). In contrast, if such operations were conducted as part of an existing manufacturing division which was already utilizing the LIFO method, the incorporation of the long-term contract costs into the existing LIFO pool would probably constitute an accounting method change which would require the Commissioner's advance consent.[17] Whatever pooling method is ultimately adopted, the Service could probably not successfully treat each separate contract as a separate LIFO pool under the natural business unit concept.

There may also be a variety of other technical problems confronting completed contract method taxpayers who seek to adopt the LIFO method. All of these problems will require careful consideration. However, in the final analysis, since the benefits which accrue under the LIFO method are potentially so significant, it will be difficult for completed contract taxpayers not to follow the *Peninsula Steel* decision. ☆

## Optional mileage rate liberalized a bit by IRS

ALTHOUGH THE MAXIMUM deduction for business use of an auto under the IRS standard mileage rate remains 20 cents a mile, a change in the rules, made by *Rev. Proc.* 82-61, IRB 1982-46, 28, may make it more beneficial.

Instead of itemizing deductions for operating expenses of an automobile used for business purposes, *Rev. Proc.* 80-7, 1980-1 CB 590, as modified by *Rev. Proc.* 80-32, 1980-2 CB 767, allows a deduction of 20 cents a mile for the first 15,000 business miles traveled during the year. For miles in excess of 15,000, the rate is 11 cents a mile. If however, the automobile is considered fully depreciated (see below), the deduction for all business miles is computed at the 11 cent rate.

There is yet another standard mileage rate for use of a car for charitable, medical, or moving purposes. There, the deduction is nine cents a mile.

The deduction is in lieu of all operating expenses of the car, such as depreciation, maintenance, repairs, gasoline, insurance, registration fees, etc. However, parking fees and tolls may be deducted in addition to the mileage rate. There's nothing new on this point.

For cars placed in service after 1980, use of the optional method constitutes an election not to take deductions for depreciation under ACRS. (For cars placed in service before then, depreciation is assumed to be on a straight-line basis using a five-year life.)

In *Rev. Proc.* 81-54, 1981-2 CB 649, the Service stated that depreciation under ACRS when the mileage allowance is used is based on 60,000 miles. That is, once a taxpayer has used a car for business purposes for a total of 60,000 miles, it is considered fully depreciated and the 11 cent rate applies to future business mileage.

This rule has been modified by *Rev. Proc.* 82-61, which states that for this purpose a car will be considered as being driven for a maximum of 15,000 business miles a year even if the actual mileage is higher. Thus, if a car is used 20,000 miles per year for each of three years, rather than using the 11 cents per mile rate for the fourth year, the 15 cents per mile rate can be used for the first 15,000 miles of the fourth year.

In determining the basis of a car that is used for business purposes, the car is considered depreciated at the rate of seven cents a mile for each business mile in 1980 and 1981. For 1982, the rate is seven and a half cents per business mile.

Under *Rev. Proc.* 80-7, if a taxpayer used more than one car for business purposes during the year, the rate was computed on the total mileage, *i.e.,* for this purpose the two cars were combined. However, if one of those cars is, or is considered to be, fully depreciated, *Rev. Proc.* 82-61 requires the mileage to be computed separately for each vehicle. This only applies if the taxpayer used one vehicle at a time. If two or more vehicles were in service simultaneously, the optional mileage allowance procedure cannot be applied. ☆

## *New decisions*

### WHOSE INCOME IS IT?

***Purchaser of obligations was the owner despite a simultaneous purchase of puts.*** *(Rev. Rul.)*

Taxpayer, a regulated investment

company, purchased municipal obligations at fair market value and simultaneously purchased puts from the seller with respect to those obligations for a period substantially less than their lives. The taxpayer was the owner of the obligations for tax purposes. Taxpayer was not holding the obligations as a security for a loan, was entitled to the full benefit of any appreciation in value and was free to dispose of them at any time. The fact that the risk of loss shifted to the seller was immaterial because an arm's-length price was paid for the puts, the primary purpose of the puts was to insure liquidity and the risk of loss was not transferred for the entire life of the obligations. *Rev. Rul.* 82-144, IRB 1982-31.

***Corporation's existence disregarded in determining the correct taxpayer. (TCM)***

Taxpayer was the sole shareholder of a corporation. Taxpayer conducted real estate business activities in his personal capacity, believing that the existence of the corporation was sufficient to cause the income to be taxable to it.

*Held:* For the Commissioner. The corporation may be disegarded and the income is taxable to taxpayer. *Harris,* TCM 1982-410.

## TAX-FREE EXCHANGES

***Election under gain-deferral provision for FCC-ordered sales may be made on amended return. (DC)***

Taxpayers sold their interest in a cable TV corporation after the Federal Communications Commission ordered divestiture because taxpayers also owned an interest in a TV station. Taxpayers claimed nonrecognition treatment under Section 1071 (which allows election of Section 1033 involuntary conversion treatment) on an amended return, since the required FCC certification arrived after they filed their original returns. The Service argued that a Section 1071 election is invalid unless made on the original return.

*Held:* For taxpayers. The IRS position is overly technical and unrealistic due to the lengthy process of obtaining FCC certification. *Cloutier,* DC Ind., 5/28/82; *Metzger,* DC Ind., 5/28/82.

***Cash and collectible coins not like-kind property. (CA)***

Taxpayer received U.S. gold coins in exchange for Swiss francs. Taxpayer argued that its amount realized was the coins' face amount of $20 each, although their numismatic value was much higher. Taxpayer alternatively contended that the exchange was nontaxable under Section 1031. The Tax Court rejected both arguments.

*Held:* Affirmed. The coins are not "money" under Section 1031, but "property" valued at their fair market value. The exchange of old coins used today only as collectors' items for presently used currency (the Swiss francs) is not a like-kind exchange. *California Federal Life Insurance Co.,* CA-9, 6/25/82.

## DEPRECIATION

***Depreciation recapture on liquidation of utility company sold to a city. (CA)***

Taxpayer, a city, purchased the stock of a privately-owned water company from its shareholders. The city, on the same day as the purchase, amended the corporate charter to make it a public utility, and liquidated the company. The IRS assessed against the city as transferee depreciation recapture arising from the liquidation. The city argued it was not subject to recapture under Section 115, which exempts income derived from a public utility that accrues to a municipality. The district court held for the Government.

*Held:* Affirmed. Depreciation recapture is taxable because the company was taxable when the depreciation was deducted. The company's brief status as a city-owned public utility was irrelevant. *City of Woodway,* CA-5, 8/4/82.

***Raised roof on processing plant not eligible for investment credit. (CA)***

The lower court held that taxpayer was entitled to an investment credit for a raised roof on a tobacco processing-and-storage plant and with regard to a railroad dock.

*Held:* Reversed. Taxpayer failed to demonstrate that the roof could not be used for anything other than housing its machinery. Also the railroad dock is found to be part of the building. The lower court is upheld in its determination that taxpayer was not entitled to a credit on a storage building. Finally, the issue of whether the plant's electrical systems are structural components of the building is remanded to the lower court. *Monk & Co., Inc.,* CA-4, 8/27/82.

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***Other accounting decisions.***

A taxpayer was denied the ITC on equipment that he had recieved upon liquidaton of his corporation, *Keene, Jr.,* TCM 1982-585. No depreciation is allowable under the income forecast method where no income exists. *Curcio,* TCM 1982-609. ITC was denied on a cattle herd where taxpayer never received any benefits or burdens of ownership. *Ramirez,* TCM 1982-608. Taxpayer-railroad was allowed to expense railroad ties. *Florida East Coast Railway Co.,* Ct. Cls., 9/30/82. The Service will seek a technical correction to TEFRA's Section 208 transitional rules involving leases of turbines and boilers to cooperative organizations. *Ann.* 82-134, IRB 1982-42. A "loan" was treated as a payment in the year of sale in a pre-1980 installment sale. *Greenfield,* TCM 1982-617. A taxpayer is liable for estimated tax even where the only tax is ITC recapture. *A. O. Smith Co.,* CA-7, 10/25/82. A cash basis taxpayer cannot deduct nonrefundable prepaid interest. *Zidanic,* 79 TC No. 40. Taxpayer allowed a business expense deduction for allowing employees to drive company cars to and from work. Value of this use is taxable to employees. *N.W.D. Investment Co.,* TCM 1982-564. Expenses incurred in investigating a corporation in preparation of its purchase are capital expenses. *Ellis Banking Corp.,* CA-11, 10/15/82. Corporation denied bond discount deduction when it exchanged cash and debentures in return for preferred stock, because there is no proof that a discount existed. *Texstar Corp.,* CA-5, 10/7/82. A loan origination fee charged in obtaining a VA loan is not deductible as interest, but the 3% rate charged to the seller to bridge the gap between the market rate and the VA rate is deductible as interest. *Dozier,* TCM 1982-569. The Service has issued Temporary Regs, in question and answer form, on the transitional rules on safe harbor leasing. Temp. Reg. 5f.168(f)(8)-1. A bad debt deduction was disallowed where taxpayer never had any reasonable expectation of repayment. *Estate of Rappaport,* TCM 1982-584. Bad debt deduction disallowed for failure to show that the debt became worthless. *Meissler,* TCM 1982-588; *Hines,* TCM 1982-589. Nonbusiness bad debt deduction only allowed where loans were made for investment purposes and not to protect employment. *Miller,* TCM 1982-629. A case was remanded to the Tax Court to determine character of payments made to a gas company. *City Gas Co. of Florida,* CA-11, 10/21/82.