12 T.C. 246 (1949)

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A taxpayer cannot deduct a loss for tax purposes if the cost basis of the asset related to the loss has already been recovered through prior deductions.

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Summary

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R.G. and Martha Robinson claimed a $10,000 loss deduction in 1942 related to timber rights, arguing that bombing activities and subsequent settlement of damage claims rendered the remaining timber valueless. The Commissioner disallowed the deduction, asserting that the cost basis of the timber rights had already been recovered through cost of goods sold deductions in prior years (1939 and 1940). The Tax Court upheld the Commissioner's determination, finding that the taxpayers' prior returns demonstrated complete cost recovery, and they failed to prove those returns were erroneous. The court denied the deduction because the taxpayers had already benefitted from deducting the cost of the timber in previous years.

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Facts

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In 1939, R.G. Robinson purchased timber rights near Destin, Florida, for $29,000, financed by a bank loan secured by a mortgage on the timber. The purchase agreement allowed five years to remove the timber. Robinson contracted with Perry, a sawmill owner, to log and convert the timber into lumber under the name Destin Saw Mill Co., with Perry receiving a fixed price per thousand feet and 50% of the net profits. Operations continued until 1941 when Army bombing activities in the area forced Perry to cease operations. In 1942, former owners of the timber land claimed Perry had cut timber outside the permitted area and damaged roads. Robinson relinquished his remaining timber rights in exchange for a release from damage claims and later claimed a $10,000 loss related to the timber rights in his 1942 tax return.

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Procedural History

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The Commissioner of Internal Revenue disallowed the $10,000 loss deduction claimed by R.G. and Martha Robinson on their 1942 tax return. The Robinsons petitioned the Tax Court, contesting the Commissioner's determination, claiming the deduction was a valid loss under Section 23(e) of the Internal Revenue Code and also arguing the statute of limitations barred the deficiency assessment. The Tax Court ruled in favor of the Commissioner, upholding the disallowance of the loss deduction.

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Issue(s)

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1. Whether the assessment of a deficiency was barred by the statute of limitations.

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2. Whether the taxpayers were entitled to deduct $10,000 as a loss under Section 23(e) of the Internal Revenue Code for the year 1942, arising from relinquishing timber rights.

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Holding

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1. No, because the statute of limitations defense was not properly raised in the original or amended petitions.

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2. No, because the cost basis of the timber rights had already been recovered through cost of goods sold deductions in prior years (1939 and 1940).

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Court's Reasoning

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The court first addressed the statute of limitations argument, finding that it was not properly raised in the pleadings and therefore was not a valid defense. Even if it had been properly raised, the court stated that it would still rule against the taxpayers based on precedent. As to the loss deduction, the court relied on the tax returns filed by the petitioner, which clearly showed that the $29,000 cost of the timber purchased in 1939 was recovered through cost of sales deductions in 1939 and 1940. The court stated that the taxpayers had failed to overcome the presumption of correctness of the Commissioner's determination that the cost basis of the timber rights was previously recovered. Even though the taxpayer argued that the returns

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