16 T.C. 1517 (1951)

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A railroad using the retirement method of accounting can deduct the cost of retired property in the year the property is actually retired (i.e., lost, destroyed, or abandoned), not necessarily the year the bookkeeping entries are made.

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Summary

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Boston and Maine Railroad (B&M) used the retirement method of accounting. For 1939-1941, B&M claimed deductions for retired roadway property. The IRS argued B&M's pre-1913 property basis was incorrect and deductions were taken in the wrong years. The Tax Court held that B&M's method for calculating the basis of pre-1913 property was flawed because it did not accurately reflect original cost, but B&M could include engineering costs if they were actually lost upon retirement. Critically, the court determined that deductions should be taken in the year the property was actually retired, regardless of when accounting entries were made.

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Facts

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B&M, subject to Interstate Commerce Commission (ICC) regulations, used the retirement method of accounting where property was carried at original cost. Upon retirement, the cost (undiminished by depreciation) was charged to expense. Pre-1914, B&M didn't track individual item costs. The ICC inventoried and valued B&M's property as of June 30, 1914, determining the reproduction cost new. B&M used this inventory to calculate its deductions for retirements. The IRS challenged the basis and the timing of the deductions.r

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Procedural History

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The IRS determined a deficiency against B&M for 1941, challenging deductions for retired roadway property in 1939, 1940 and 1941, and disallowed some deductions. B&M petitioned the Tax Court, contesting the IRS's adjustments and claiming it was entitled to larger deductions in the relevant tax years based on the retirement method of accounting.r

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Issue(s)

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1. Whether B&M used the proper basis for calculating deductions for roadway property owned at March 1, 1913, under the retirement method of accounting.r
2. Whether the basis of property acquired before March 1, 1913, should include engineering costs upon retirement.r
3. Whether B&M claimed deductions for the proper year or taxable period based on when the property was actually retired.r

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Holding

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1. No, because B&M failed to prove the original costs of the retired properties or that such costs exceeded the inventory cost less estimated depreciation to March 1, 1913.r
2. Yes, because B&M showed that engineering costs in the properties lost by retirement did not survive retirement.r
3. No, because the dates of bookkeeping entries do not determine the dates of deduction; deductions are allowable for the years the properties were actually lost, destroyed, or abandoned.r

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Court's Reasoning

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The court stated that with the retirement method, the original cost is not reduced by depreciation since depreciation is accounted for by charging expenses over time. However, B&M's pre-1914 accounts did not accurately reflect original costs, so the court rejected B&M's calculation method. The court found that B&M's method effectively gave it a double deduction in some instances, and allowed deductions for property that didn't exist anymore in others. However, regarding engineering costs, the court sided with the petitioner noting

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