33 T.C. 1038 (1960)

When a company purchases an entire going business, including its customer structure, the cost of acquiring that structure is not amortizable as a depreciable asset if the customer relationships represent a single intangible asset with an indefinite useful life.

Summary

Thrifticheck Service Corporation (Petitioner) purchased a business that provided a checking account system, including its customer contracts. The Petitioner sought to amortize the cost of these contracts over their remaining terms. The IRS disallowed the deduction, arguing that the Petitioner acquired a single intangible asset – the going business – with an indefinite life. The Tax Court agreed, distinguishing the purchase of a customer structure from the purchase of individual contracts. The court held that the cost of acquiring a going business, including its customer base, cannot be amortized because the asset's useful life is not limited and cannot be estimated with reasonable certainty. Therefore, the petitioner could not deduct the cost of the contracts under the Internal Revenue Code.

Facts

Bankers Development Corporation (Bankers) sold and installed the "ThriftiCheck Service Plan" to banks. Bankers entered into 200 contracts with various banks. The contracts had varying terms, but generally, the banks paid fees per account opened and per check processed, and were renewable unless notice was given. Bankers was liquidated, and its assets, including the customer contracts, were purchased by Thrifticheck Service Corporation (Petitioner), a new company formed for this purpose. Petitioner paid a lump sum for the purchase of Bankers' assets, which was allocated among various assets, including an allocated value for the 200 customer contracts. Petitioner sought to deduct the cost of the customer contracts as an amortizable expense. The IRS disallowed the deduction.

Procedural History

The Commissioner of Internal Revenue determined a deficiency in the Petitioner's income tax. The Petitioner challenged this determination in the United States Tax Court, claiming the right to amortize the cost of the customer contracts. The Tax Court sided with the Commissioner, denying the amortization deduction. The court's decision was based on the finding that the Petitioner had purchased the entire going business, not simply individual contracts.

Issue(s)

Whether the Petitioner is entitled to deduct, as amortization, a portion of the cost of the customer contracts it acquired from Bankers under I.R.C. § 23(l) of the 1939 Internal Revenue Code.

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Holding

No, because the Petitioner did not buy individual contracts but a single asset, the customer structure, which did not have a limited useful life, the Petitioner could not amortize and deduct the cost.

Court's Reasoning

The court focused on the substance of the transaction. While the contract listed individual contracts by customer name, the court determined that the Petitioner acquired a single intangible asset consisting of the aggregate of the contracts representing the customer structure of the ongoing business. The court distinguished this from cases involving the purchase of individual contracts. The contracts varied in length and had a renewal term. The court found the key was that the Petitioner acquired the entire customer base as a single asset. "It is clear from the evidence in the instant case that it was the intention of both parties to the transaction that the petitioner should acquire and continue the going business of Bankers and that this was done." The court also noted that, in the contract of sale, the customer contracts were listed but no specific price was set for the individual contracts, but rather the sum of $290,818.61 was paid for the aggregate of such contracts.

The court cited the early case of *Danville Press, Inc.* as an analogy, where the petitioner purchased newspaper subscriptions. The court held that what was purchased was a subscription list, not individual contracts, and that the asset continued to have value, subject to fluctuation, and that the petitioner was not entitled to amortize the cost of such asset. Further support was found in cases involving the acquisition of a customer base for cleaning services, where the purchase was deemed a single intangible asset.

The court determined that the customer structure had no definite life and therefore was not subject to depreciation under the code, as the contracts had a possibility of renewal and provided a continuing source of revenue. The court also noted that an amount had been paid for the "ThriftiCheck" trademark and goodwill; however, the court held that, entirely aside from any goodwill element, the acquisition of the 200 contracts should be treated as the acquisition of a single asset with a continuing useful life precluding an amortization deduction.

Practical Implications

This case underscores the importance of analyzing the substance of a business acquisition to determine whether the acquired assets can be amortized. If a business acquires an entire going concern, including its customer base, the cost of the customer relationships is often treated as part of a single, indefinite-life intangible asset, making it non-amortizable. However, when individual contracts are acquired or when a customer list can be separated from the ongoing business, amortization

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may be permissible. This case is still relevant today in the valuation of businesses for tax purposes. Lawyers and accountants must scrutinize the nature of the acquired assets and the intent of the parties involved in the transaction to determine if the cost of such assets can be amortized. This case highlights the need to distinguish between the purchase of individual contracts and the acquisition of an entire customer structure, particularly in the context of valuing intangible assets and determining tax deductions.

Meta Description

The court determined that the cost of acquiring a going concern and its customer base is not amortizable. Distinguishes between a purchase of individual contracts versus a business acquisition.

Tags

Thrifticheck Service Corp, U.S. Tax Court, 1960, Amortization, Intangible Assets, Going Business, Customer Contracts

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