Thoms v. Commissioner, 50 T. C. 247 (1968)

An insurance agency's list of expirations is part of its goodwill and cannot be depreciated as it has an indefinite useful life.

Summary

Alfred H. Thoms purchased an insurance agency including its goodwill and customer list for $10,500. He claimed depreciation on the customer list, arguing it had a limited life. The U. S. Tax Court held that the list of expirations was an integral part of the goodwill, which has no determinable useful life and thus cannot be depreciated. The court reasoned that the list's value was tied to the ongoing business and could not be separated from the goodwill transferred in the sale of a going concern.

Facts

Alfred H. Thoms purchased a general insurance agency business from Philip F. Pierce for $10,500 in 1961. The purchase included the goodwill, customer list (list of expirations), and all other intangible assets used in the operation of the business. The customer list detailed approximately 509 policies. Thoms sent letters to the customers and insurance companies to notify them of the change in ownership. He attempted to amortize the purchase price over 14 months, claiming depreciation deductions of $1,500 in 1961 and $9,000 in 1962.

Procedural History

The Commissioner of Internal Revenue disallowed Thoms' depreciation deductions, leading to a deficiency determination. Thoms petitioned the U. S. Tax Court, which heard the case and ultimately decided in favor of the Commissioner, ruling that no depreciation was allowable for the customer list.

Issue(s)

1. Whether the list of insurance expirations purchased by Thoms can be depreciated under section 167(a)(1) of the Internal Revenue Code of 1954.

Holding

1. No, because the list of expirations is an integral part of the goodwill of the insurance agency, which has no determinable useful life and thus cannot be depreciated.

Court's Reasoning

The Tax Court applied the principle that goodwill, and by extension, the list of expirations as part of it, cannot be depreciated because it has no determinable

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useful life. The court emphasized that goodwill continues to serve the business as long as it operates. The list of expirations was deemed essential to the transfer of goodwill, providing the purchaser with the opportunity to secure policy renewals, which is inherent to the goodwill of an insurance agency. The court rejected Thoms' arguments that the list had a definite life tied to policy expiration dates or the end of a five-year covenant not to compete, noting that the list's value persisted beyond these periods. The court cited regulations and case law to support its conclusion that the list was inextricably linked to goodwill and thus non-depreciable.

Practical Implications

This decision clarifies that when purchasing an insurance agency as a going concern, the list of expirations cannot be depreciated separately from the goodwill. Practitioners must allocate the entire purchase price to goodwill, which is not subject to depreciation. This impacts how similar transactions are structured and reported for tax purposes, emphasizing the importance of understanding the nature of goodwill in business acquisitions. The ruling may influence how insurance agencies are valued and sold, as buyers cannot expect to recover their investment through depreciation of the customer list. Subsequent cases have followed this precedent, reinforcing that lists of expirations are treated as goodwill in the context of insurance agency sales.

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