Catron v. Commissioner, 50 T. C. 306 (1968)

A specialized cold storage facility qualifies for the investment tax credit as a storage facility under Section 38 property, even if part of a larger structure that does not qualify.

Summary

The Catron brothers, operating an apple farming partnership, sought investment tax credits for a Quonset structure used for apple processing and storage. The Tax Court held that the nonrefrigerated two-thirds of the structure, used for sorting and packing apples, did not qualify as Section 38 property because it provided general working space. However, the court found that the refrigerated one-third, used solely for cold storage of apples, qualified as a storage facility under Section 48(a)(1)(B)(ii) and was eligible for the credit. The decision hinged on the functional use of the space, allowing an allocation of costs for the qualifying cold storage area.

Facts

In 1962, Robert and Eugene Catron, operating as partners in an apple farming business near Nebraska City, Nebraska, purchased and erected a prefabricated Quonset-type structure. The structure was 120 feet long and 40 feet wide, with the southernmost one-third (40 feet) insulated and refrigerated for cold storage of apples. The remaining two-thirds of the structure was used for sorting, grading, and packing apples. The cold storage area was separated from the rest by a partition with a single refrigerator door and was insulated with 2-inch-thick spray insulation. The nonrefrigerated area had 1-inch-thick insulation and was used for various apple processing activities, including sorting and packing.

Procedural History

The Commissioner of Internal Revenue determined deficiencies against Robert and Eugene Catron for the taxable year 1962, disallowing their claimed investment tax credits based on the cost of the entire Quonset structure. The cases were consolidated and heard by the United States Tax Court, which rendered its decision on May 16, 1968.

Issue(s)

1. Whether the nonrefrigerated portion of the Quonset structure qualifies as Section 38 property under the Internal Revenue Code of 1954.
2. Whether the refrigerated portion of the Quonset structure qualifies as Section 38 property under the Internal Revenue Code of 1954.

Holding

1. No, because the nonrefrigerated portion provided general working space and was

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considered a building, which is excluded from Section 38 property.
2. Yes, because the refrigerated portion was used solely for cold storage of apples and thus qualified as a storage facility under Section 48(a)(1)(B)(ii), making it eligible for the investment tax credit.

Court's Reasoning

The court applied the statutory and regulatory definitions of "building" and "Section 38 property. " Buildings and their structural components are explicitly excluded from Section 38 property. The court determined that the nonrefrigerated portion of the structure was a building because it provided general working space for sorting, grading, and packing apples. However, the refrigerated portion was deemed a storage facility because it was used exclusively for storing apples and did not provide working space. The court allowed for an allocation of costs to the qualifying refrigerated portion, rejecting the Commissioner's argument against such allocation. The court emphasized the functional use of the space, citing examples from the regulations and revenue rulings to support its conclusion. The court also noted that incidental human activity within the refrigerated area, such as using forklifts to store and remove apples, did not disqualify it as a storage facility.

Practical Implications

This decision clarifies that specialized storage facilities within larger structures can qualify for the investment tax credit if they serve a specific storage function and do not provide general working space. Practitioners should carefully analyze the use of space within a structure to determine eligibility for the credit, especially in cases where a structure serves multiple functions. The ruling also underscores the importance of cost allocation in such cases, allowing taxpayers to claim credits for qualifying portions of their property. Subsequent cases and IRS guidance have built upon this decision, further refining the criteria for qualifying storage facilities. Businesses in agriculture and other industries that rely on storage facilities should consider the potential tax benefits of structuring their storage operations to meet the criteria established in this case.

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