***KIRO, Inc. v. Commissioner, 51 T. C. 155 (1968)***

The sliding-scale method for depreciating television film license costs was upheld as a reasonable allowance under IRC § 167(a)(1) for films with limited exposures.

**Summary**

In KIRO, Inc. v. Commissioner, the Tax Court held that the taxpayer’s method of depreciating television film license costs using a sliding-scale approach was a reasonable allowance under IRC § 167(a)(1). KIRO, Inc. , a television broadcaster, had entered into contracts for films to be telecast, and claimed deductions using a sliding-scale method based on the diminishing value of subsequent film showings. The IRS disallowed part of these deductions, advocating for a straight-line method. The court ruled in favor of KIRO for films with limited exposures, finding that the sliding-scale method better reflected the economic realities of the television industry, but upheld the IRS’s method for films with unlimited exposures due to insufficient evidence from the taxpayer.

**Facts**

In 1958, KIRO, Inc. , successor to Queen City Broadcasting Co. , began televising programs in Seattle, Washington. It entered into 41 contracts for films at a total cost of $1,196,319. 90, with varying exposure limits. KIRO claimed a deduction of $424,158. 87 for “Film rentals and purchases” using a sliding-scale depreciation method, which allocated a larger portion of the cost to the first run of each film. The IRS disallowed $245,506. 71 of the deduction, arguing for the use of a straight-line method.

**Procedural History**

The IRS issued a notice of deficiency to Queen City Broadcasting Co. for the disallowed portion of the film rental deduction. KIRO, Inc. , as successor, filed a petition with the U. S. Tax Court. The court heard the case and issued its opinion on October 28, 1968.

**Issue(s)**

1. Whether the IRS erred in disallowing $245,506. 71 of the $424,158. 87 deduction claimed by KIRO for film rentals and purchases in 1958.
2. Whether KIRO claimed excessive net operating loss deductions in prior years based on the carryback of a net operating loss from 1958.

**Holding**

1. Yes, because the sliding-scale method used by KIRO for films with limited exposures was a reasonable allowance under IRC § 167(a)(1), reflecting the diminishing value of subsequent film showings.

 

2. No, because the resolution of the first issue automatically disposed of this issue, as the court upheld the deduction for films with limited exposures.

### Court's Reasoning

The court applied IRC § 167(a)(1), which allows a reasonable allowance for the exhaustion of property used in trade or business. The sliding-scale method was deemed appropriate for films with limited exposures because it matched the economic reality that the first run of a film is most valuable and subsequent runs diminish in value. This method was supported by industry practice and the refund clause in the Paramount contract, which recognized the greater value of earlier runs. The court rejected the IRS's reliance on IRC § 162(a)(3) and related regulations, finding them inapplicable to the license agreements at issue. For films with unlimited exposures, the court upheld the IRS's method due to KIRO's failure to provide sufficient evidence to support its claimed deductions.

### Practical Implications

This decision allows television broadcasters to use a sliding-scale method for depreciating the costs of film licenses with limited exposures, aligning tax deductions more closely with the actual economic benefit derived from the films. It sets a precedent for the industry to tailor depreciation methods to their specific business models and the nature of their assets. However, for films with unlimited exposures, the burden remains on the taxpayer to substantiate their method with clear evidence. Later cases and IRS guidance have continued to refine the application of depreciation methods in the entertainment industry, but this ruling remains significant for its recognition of the unique economic characteristics of television broadcasting.

 