***High Plains Agricultural Credit Corp. v. Commissioner, 63 T. C. 118 (1974)***

Section 166(g)(2) of the Internal Revenue Code prohibits non-dealers in property, who are guarantors or endorsers, from deducting additions to a reserve for bad debts for transferred loans.

**Summary**

High Plains Agricultural Credit Corporation sought to deduct additions to its bad debt reserve for loans transferred with recourse to a bank, but the U. S. Tax Court ruled against it. The court held that under Section 166(g)(2), the corporation, as a guarantor and endorser, could not claim such deductions. Additionally, the court upheld the Commissioner's determination that no deductions were reasonable for the corporation's retained loans due to the absence of bad debt experience. This decision clarified that only dealers in property could claim such deductions, impacting how financial institutions and similar entities manage their tax liabilities.

**Facts**

High Plains Agricultural Credit Corporation, a Wyoming-based corporation, rediscounted loans made to farmers and ranchers to the Federal Intermediate Credit Bank (FICB) under a 'General Rediscount, Loan, and Pledge Agreement'. This agreement required High Plains to endorse the notes and guarantee payment if the original borrowers defaulted. The corporation claimed deductions for additions to a bad debt reserve for both the transferred and retained loans. The Commissioner disallowed these deductions for the tax years ending September 30, 1967, 1968, and 1969.

**Procedural History**

The Commissioner determined deficiencies in High Plains' income tax for the years in question and disallowed the claimed deductions. High Plains filed a petition with the U. S. Tax Court, challenging the Commissioner's determination. The Tax Court upheld the Commissioner's decision, ruling that High Plains could not deduct additions to its bad debt reserve under Section 166(g)(2) for the transferred loans and found the Commissioner's disallowance of deductions for the retained loans to be reasonable.

**Issue(s)**

1. Whether Section 166(g) of the Internal Revenue Code allows High Plains to deduct additions to a reserve for bad debts for loans transferred with recourse to a bank?
2. Whether the Commissioner abused his discretion in determining that no deduction for an addition to the reserve was reasonable for the loans retained by High Plains?

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## Holding

1. No, because Section 166(g)(2) prohibits non-dealers in property, who are guarantors or endorsers, from deducting additions to a reserve for bad debts for transferred loans.
2. No, because the Commissioner's determination that no deduction for an addition to the reserve was reasonable for the retained loans was not an abuse of discretion, given High Plains' lack of bad debt experience.

## Court's Reasoning

The court reasoned that under Section 166(g)(2), High Plains, as a guarantor and endorser, was prohibited from deducting additions to a reserve for bad debts related to the transferred loans. The court rejected High Plains' argument that it was primarily liable to the FICB, emphasizing that the statute's language and legislative history intended to treat such entities as guarantors or endorsers, regardless of primary or secondary liability. The court also upheld the Commissioner's determination regarding the retained loans, finding it reasonable given High Plains' lack of prior bad debt experience. The court referenced prior cases like Wilkins Pontiac and Foster Frosty Foods, which established the framework for Section 166(g), and noted that Congress intended this section to be the exclusive provision for such deductions.

## Practical Implications

This decision has significant implications for financial institutions and other entities that transfer loans with recourse. It clarifies that only dealers in property can claim deductions for bad debt reserves under Section 166(g)(1), while non-dealers, classified as guarantors or endorsers, cannot. This ruling may affect how these entities structure their loan agreements and manage their tax liabilities. It also emphasizes the importance of maintaining accurate records of bad debt experience to justify any reserve additions for retained loans. Subsequent cases have referenced this decision to interpret the scope of Section 166(g), influencing tax planning strategies for similar financial arrangements.

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