BJR Corp. v. Commissioner, 67 T. C. 111 (1976)

Advance rental payments must be included in gross income in the year received, regardless of the taxpayer's method of accounting.

Summary

BJR Corp. acquired Jefferson Sales & Distributors, Inc. , which had leased mobile homes to HUD following Hurricane Camille. The IRS challenged Jefferson's tax return, asserting that it had improperly deferred $258,975 of advance rental income received from HUD. The Tax Court held that the entire $795,675 received must be included in Jefferson's gross income for the tax year ending May 31, 1970, as advance rentals are taxable upon receipt. The court also disallowed most of the claimed travel and entertainment expenses due to insufficient substantiation, upheld the reduction of Jefferson's surtax exemption due to its status as a component member of a controlled group, and imposed a penalty for late filing of the tax return.

Facts

Jefferson Sales & Distributors, Inc. , was formed to lease mobile homes to HUD for disaster relief following Hurricane Camille. Jefferson entered into two contracts with HUD in September and November 1969, leasing a total of 301 mobile homes for terms ranging from 9 to 12 months. Jefferson received $795,675 in rental payments from HUD during the tax year ending May 31, 1970, but only reported $536,700 as income, deferring $258,975. Jefferson merged into BJR Corp. on June 1, 1970. Jefferson claimed deductions for travel and entertainment expenses totaling $13,237, and a $25,000 surtax exemption. The IRS issued a deficiency notice to BJR as Jefferson's successor on January 17, 1975, asserting that the entire $795,675 should have been included in income, disallowing most of the travel and entertainment deductions, reducing the surtax exemption, and imposing a penalty for late filing.

Procedural History

The IRS issued a deficiency notice to BJR Corp. on January 17, 1975. BJR filed a petition with the U. S. Tax Court challenging the IRS's determinations. The Tax Court held that the notice of deficiency was timely, the entire $795,675 received from HUD was includable in income for the tax year ending May 31, 1970, most of the claimed travel and entertainment expenses were disallowed, the surtax exemption was correctly reduced, and the penalty for late filing was upheld.

Issue(s)

1. Whether the issuance of the statutory notice of deficiency was barred by the 3-year period of limitations under I. R. C. § 6501(a)?
2. Whether the entire $795,675 received from HUD was includable in Jefferson's gross income for the tax year ending May 31, 1970?

© 2025 SCOTUSreports.com. All rights reserved.

3. Whether deductions claimed for travel and entertainment expenses were properly allowable?
4. Whether Jefferson was a "component member" of a "controlled group" of corporations and thus entitled to only one-third of a $25,000 surtax exemption?
5. Whether BJR was liable for the penalty under I. R. C. § 6651(a) for failure to file a timely return?

Holding

1. No, because the taxpayer failed to prove that the return was filed more than 3 years prior to the issuance of the deficiency notice.
2. Yes, because the payments constituted advance rentals, which must be included in gross income upon receipt regardless of the taxpayer's accounting method.
3. No, because the taxpayer failed to substantiate most of the claimed expenses as required by I. R. C. § 274, except for $293. 68 in legal fees and $155. 80 for a truck rental.
4. Yes, because Jefferson was a "component member" of a controlled group on December 31, 1969, and thus entitled to only one-third of the surtax exemption.
5. Yes, because the taxpayer failed to show that the late filing was due to reasonable cause.

Court's Reasoning

The Tax Court reasoned that advance rentals must be included in gross income in the year received, as established by I. R. C. § 61 and Treasury Regulation § 1. 61-8(b). The court rejected Jefferson's arguments that the payments were capital advances or that they could be deferred under Revenue Procedure 71-21 or I. R. C. § 83. For the travel and entertainment deductions, the court applied the strict substantiation requirements of I. R. C. § 274, disallowing most of the claimed expenses due to lack of adequate records or corroborating evidence. Regarding the surtax exemption, the court applied I. R. C. §§ 1561 and 1563, finding Jefferson to be a "component member" of a controlled group on December 31, 1969. Finally, the court upheld the penalty for late filing under I. R. C. § 6651(a), as the taxpayer failed to demonstrate reasonable cause for the delay.

Practical Implications

This decision reinforces the rule that advance rental income must be included in gross income in the year of receipt, regardless of the taxpayer's accounting method. Taxpayers leasing property should be aware that they cannot defer such income by treating it as capital advances or applying Revenue Procedure 71-21 or I. R. C. § 83. The case also underscores the importance of maintaining adequate records to substantiate travel and entertainment expenses under I. R. C. § 274. For corporate taxpayers, the decision serves as a reminder to consider the impact of controlled group status on surtax exemptions. Finally, the case emphasizes the need for timely filing of tax returns to avoid penalties, even if the taxpayer believes a return was

© 2025 SCOTUSreports.com. All rights reserved.

previously filed.

© 2025 SCOTUSreports.com. All rights reserved.