Los Angeles Central Animal Hospital, Inc. v. Commissioner, 73 T. C. 295 (1979)

Medical records can be amortized as a depreciable asset separate from goodwill if they have an ascertainable value and a limited useful life.

Summary

Los Angeles Central Animal Hospital, Inc. , sought to amortize the cost of medical record cards acquired in purchasing a veterinary practice, arguing they were separate from goodwill. The Tax Court held that while the records were separable from goodwill and depreciable, the claimed amount was excessive. The court allowed a portion of the claimed deduction, assigning a 7-year useful life to the records and allocating $85,000 of the purchase price to them, emphasizing their limited utility due to animal mortality and client turnover.

Facts

Los Angeles Central Animal Hospital, Inc. , purchased an animal hospital from Dr. Zaks' Pet Hospital, Inc. , for $245,500. The purchase included various assets, with $120,500 allocated to medical record cards representing 12,000 animal patients treated within the last two years. These cards contained vital information for the treatment and follow-up of animal patients. The hospital claimed a deduction for the amortization of these records over five years, which the IRS disallowed, arguing the records were inseparable from goodwill.

Procedural History

The IRS issued a statutory notice of deficiency in January 1974, disallowing the deduction for amortization of the medical records. The case was then brought before the United States Tax Court, where the petitioner sought a ruling on the deductibility of the amortization expense.

Issue(s)

1. Whether the medical record cards acquired by Los Angeles Central Animal Hospital, Inc. , can be amortized as a depreciable asset separate from goodwill.
2. If so, what is the appropriate amount and useful life for the amortization of these records?

Holding

1. Yes, because the medical record cards have an ascertainable value separate from goodwill and a limited useful life.
2. The court determined that $85,000 of the purchase price should be allocated to the medical records, with a useful life of 7 years for amortization purposes.

Court’s Reasoning

The Tax Court applied Section 167(a) of the Internal Revenue Code, which allows a depreciation deduction for property used in a trade or business, including intangibles with a limited useful life. The court differentiated the medical records from goodwill, noting that goodwill represents the expectation of continued patronage, whereas the records are a tangible asset used for generating income through repeat business and aiding in patient treatment. The court cited cases like Computing & Software, Inc. v. Commissioner, where similar records were deemed depreciable. The court rejected the IRS’s argument that the records were inseparable from goodwill, finding instead that the records had an ascertainable value and a limited life due to animal mortality and client turnover. The court used expert testimony and statistical data to determine that the records should be allocated $85,000 of the purchase price and amortized over 7 years.

Practical Implications

This decision clarifies that medical records can be treated as a depreciable asset distinct from goodwill, provided their value and useful life can be reasonably determined. Practitioners and business owners in similar situations should carefully allocate purchase prices and document the rationale for such allocations, considering the specific utility and obsolescence of acquired records. This ruling may affect how businesses structure asset purchases and report them for tax purposes, potentially influencing tax planning strategies. Subsequent cases like Houston Chronicle Publishing Co. v. United States have referenced this case to distinguish between goodwill and other intangible assets. Legal professionals should use this case to argue for the separate treatment of records in business acquisitions where they have a distinct, limited value.

