Charles Baloian Company, Inc. , Petitioner v. Commissioner of Internal Revenue, Respondent, 68 T. C. 620 (1977)

An accrual basis taxpayer cannot deduct expenses for which it has a fixed right to reimbursement, even if the reimbursement occurs in a subsequent tax year.

Summary

Charles Baloian Company was forced to relocate due to urban redevelopment and incurred moving expenses. The company received written authorization to incur moving expenses up to a specified amount before the end of its fiscal year, but was reimbursed in the following year. The Tax Court held that because the company's right to reimbursement was fixed and matured without substantial contingency before the expense was accrued, it could not deduct the reimbursed portion of the moving expenses. Additionally, the court ruled that Charles Baloian Company and another related corporation, Pam-Pak, did not form a "brother-sister controlled group" for tax purposes due to differing stock ownership structures.

Facts

On February 25, 1971, Charles Baloian Company (the petitioner) was notified by the Redevelopment Agency of the City of Fresno that the building it was leasing was scheduled for demolition, giving the petitioner at least 90 days to vacate. On May 20, 1971, the agency authorized the petitioner to incur moving expenses up to $16,967. The petitioner moved by June 30, 1971, and incurred moving expenses of $18,008. 80, which it deducted on its tax return for the fiscal year ending on that date. The agency reimbursed $17,120 of these expenses on January 17, 1972. The petitioner's stock was equally owned by Charles, Edward, and James Baloian, who also owned 78% of Pam-Pak, with Milton Torigian owning the remaining 22%.

Procedural History

The Commissioner of Internal Revenue (respondent) determined deficiencies in the petitioner's Federal income tax for the fiscal years ending June 30, 1971, and June 30, 1972. The petitioner contested the disallowance of the moving expense deduction and the treatment as a "brother-sister controlled group" with Pam-Pak. The case was heard by the United States Tax Court, which ruled in favor of the respondent on the moving expense issue but in favor of the petitioner regarding the controlled group status.

Issue(s)

1. Whether the petitioner is entitled to deduct moving expenses incurred and accrued in its fiscal year ended June 30, 1971, and whether the amount of subsequent reimbursement for such expenses is includable in its gross income?
2. Whether the petitioner and Pam-Pak Distributors, Inc. , constitute a "brother-sister controlled group" within the meaning of section 1563(a)(2) of the Internal

Revenue Code?

Holding

1. No, because the petitioner’s right to reimbursement matured without substantial contingency on May 20, 1971, when the agency issued its written authorization to incur moving expenses in a specified amount.
2. No, because Milton Torigian’s ownership in Pam-Pak cannot be taken into account for the purposes of section 1563(a)(2) since he did not own stock in both Pam-Pak and the petitioner.

Court’s Reasoning

The court reasoned that under the “fixed right to reimbursement” rule, an accrual basis taxpayer cannot deduct expenses for which it has a right to reimbursement that has matured without substantial contingency. The court determined that the petitioner’s right to reimbursement was fixed when it received the written authorization to incur moving expenses, as this document specified the maximum reimbursable amount and outlined the process for reimbursement. The court rejected the petitioner’s argument that the right to reimbursement was contingent upon submitting a claim form post-move, viewing this as a ministerial act rather than a substantive contingency. Regarding the second issue, the court followed its precedent in Fairfax Auto Parts of No. Va. , Inc. v. Commissioner, holding that for the purposes of the 80% test in section 1563(a)(2), only common ownership can be considered, thus excluding Torigian’s ownership in Pam-Pak.

Practical Implications

This decision impacts how businesses account for expenses when reimbursement is anticipated. Accrual basis taxpayers must be aware that expenses reimbursed in a subsequent year are not deductible if the right to reimbursement was fixed before the expense was accrued. This ruling necessitates careful timing and documentation of expenses and reimbursements. For tax practitioners, it underscores the importance of understanding when a right to reimbursement becomes fixed. In terms of controlled groups, the decision clarifies that for the 80% test, only common ownership is considered, affecting how related corporations are assessed for tax purposes. Subsequent cases like Fairfax Auto Parts have been influenced by this ruling, with courts continuing to apply the principle of common ownership for the 80% test.