Wolfers v. Commissioner, 69 T. C. 975 (1978)

Reimbursement payments received under the Uniform Relocation Assistance Act are not deductible as expenses when used for reimbursed costs, and do not establish a basis for depreciation or investment tax credit for assets purchased with such funds.

Summary

Henry L. Wolfers, Inc. , a subchapter S corporation, was forced to relocate due to the Federal Reserve Bank's acquisition of its premises. The corporation received a lump sum payment under the Uniform Relocation Assistance Act, which was used for moving expenses, new leasehold improvements, and expansion. The court held that expenses reimbursed by these payments, including moving costs and increased rent, were not deductible. Furthermore, the corporation could not claim depreciation or investment tax credits on assets purchased with the funds, as they were considered non-shareholder contributions to capital under section 362(c) of the Internal Revenue Code.

Facts

Henry L. Wolfers, Inc. (HLW) was required to vacate its business premises at 556 Atlantic Avenue, Boston, due to the Federal Reserve Bank's acquisition. HLW negotiated a lump sum payment of $763,900 under the Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970. This payment was intended to cover moving expenses, increased rent for the remaining term of the old lease, and costs of new leasehold improvements. HLW moved to a new, larger location at 39 Sleeper Street, using the funds to expand its operations beyond what was necessary to replace its former premises. HLW claimed deductions for moving costs, increased rent, and depreciation on new assets, as well as investment tax credits.

Procedural History

The Commissioner of Internal Revenue disallowed the deductions and credits claimed by HLW and its shareholders. The case was brought before the United States Tax Court, which consolidated the cases of Henry L. Wolfers and Helen F. Wolfers, and Nancy A. Mazzoni against the Commissioner. The court's decision followed the precedent set in Charles Baloian Co. v. Commissioner, 68 T. C. 620 (1977), and applied section 362(c) of the Internal Revenue Code.

Issue(s)

1. Whether HLW can deduct moving costs, lease rentals, or other expenses reimbursed by the Federal Reserve Bank under the Relocation Act?
2. Whether HLW can claim depreciation deductions for leasehold improvements and assets purchased with funds received under the Relocation Act?
3. Whether HLW's shareholders are entitled to investment tax credits for

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expenditures made by HLW with funds received under the Relocation Act?

Holding

1. No, because the expenses were reimbursed by the Bank under the Relocation Act, making them nondeductible as per Charles Baloian Co. v. Commissioner.
2. No, because the funds received under the Relocation Act constitute contributions to capital by a non-shareholder, to which section 362(c) of the Internal Revenue Code applies, disallowing a basis for depreciation.
3. No, because there was no new qualified investment made with the funds, and thus no basis for investment tax credits.

Court's Reasoning

The court applied the principle from Charles Baloian Co. that expenses reimbursed under the Relocation Act are not deductible. It reasoned that HLW had a fixed right to reimbursement at the time the expenses were incurred, which precluded their deduction. For depreciation and investment tax credits, the court held that the funds received under the Relocation Act were non-shareholder contributions to capital, subject to section 362(c). This section requires that the basis of property acquired with such contributions within 12 months be reduced by the amount of the contribution. The court emphasized that the purpose of the Relocation Act was to make displaced entities whole, not to provide a windfall, and that allowing deductions and credits on reimbursed expenses would contradict this intent. The court also distinguished the case from Revenue Ruling 74-205, which dealt with non-business contexts and did not address section 362(c).

Practical Implications

This decision clarifies that businesses receiving relocation payments under federal programs cannot deduct reimbursed expenses, nor can they claim depreciation or investment tax credits on assets purchased with such funds. Legal practitioners must advise clients to carefully account for and report these funds as contributions to capital, not as income, and to understand the limitations on deductions and credits. This ruling may affect how businesses plan for relocation and expansion when receiving government assistance, and it underscores the need for clear legislative guidance on the tax treatment of such payments. Subsequent cases, such as those involving similar federal or state relocation assistance programs, will likely reference Wolfers for its interpretation of section 362(c) and its impact on tax planning for businesses.

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