

## ***Grossman v. Commissioner, 73 T. C. 1155 (1973)***

Demolition expenses are deductible under Section 165 if not required by a lease or agreement resulting in a lease.

### **Summary**

In *Grossman v. Commissioner*, the Tax Court allowed the taxpayer to deduct demolition expenses under Section 165 because the demolition was not required by a lease or agreement. The Grossmans, who owned commercial property, demolished their buildings due to ongoing losses and safety concerns rather than any lease requirement. The court held that for demolition expenses to be non-deductible, there must be a direct link between the demolition and a lease agreement. This case clarifies the conditions under which demolition costs can be treated as deductible losses rather than capital expenditures, impacting how property owners and tax professionals should approach similar situations.

### **Facts**

The Grossmans owned a commercial property in Passaic, New Jersey, which they had used for a dry cleaning business. After the business failed due to road construction and rezoning, they attempted to lease the property but were unsuccessful. The property deteriorated, leading to safety concerns and code violations. In July 1974, the Grossmans decided to demolish the buildings on the property due to these concerns and potential liability. They completed the demolition in December 1974, before entering into a lease agreement with Morrow Restaurants Corp. in January 1975 for a Burger King restaurant. The Grossmans claimed a deduction for the demolition expenses on their 1974 tax return.

### **Procedural History**

The IRS audited the Grossmans' 1974 tax return and initially issued a no-change letter. Subsequently, after auditing Solomon Grossman's return, the IRS proposed adjustments, including disallowing the demolition loss. The Tax Court addressed whether there was a second inspection of the taxpayer's books under Section 7605(b) and the deductibility of the demolition expenses under Section 165.

### **Issue(s)**

1. Whether there was a second inspection of the taxpayer's books and records within the meaning of Section 7605(b).
2. Whether the demolition expenses were deductible under Section 165 as a loss or should be treated as a capital expenditure.

### **Holding**

1. No, because there was no second inspection of the taxpayer's books of account;

the adjustments were based on the inspection of Solomon Grossman's books.

2. Yes, because the demolition was not pursuant to a lease or agreement resulting in a lease, making it a deductible loss under Section 165.

### **Court's Reasoning**

The court determined that there was no second inspection of the taxpayer's books under Section 7605(b), as the adjustments were based on the audit of Solomon Grossman's books. Regarding the demolition expenses, the court relied on Section 165 and the regulations under Section 1.165-3(b). The court emphasized that for demolition expenses to be non-deductible, there must be a direct link between the demolition and a lease agreement. In this case, the demolition occurred before any lease agreement was in place, and the decision to demolish was driven by safety concerns and ongoing financial losses, not a lease requirement. The court cited *Landerman v. Commissioner*, highlighting that demolition must be an essential condition of a lease agreement for it to be non-deductible. The court concluded that the Grossmans' demolition was not linked to the subsequent lease with Morrow, thus allowing the deduction.

### **Practical Implications**

This decision clarifies that demolition expenses can be deducted as losses under Section 165 if they are not required by a lease or agreement resulting in a lease. Property owners facing similar situations should carefully document the reasons for demolition, focusing on factors like safety concerns and financial losses rather than potential future leases. Tax professionals must distinguish between demolitions driven by lease requirements and those undertaken independently. This ruling impacts how property owners and businesses manage their tax liabilities related to property demolition, emphasizing the importance of timing and the absence of a lease agreement in determining deductibility.