Greene v. Commissioner, 81 T. C. 132 (1983)

The income forecast method for depreciation of motion picture films requires the use of net income, not gross receipts, in the calculation.

Summary

In Greene v. Commissioner, the U. S. Tax Court addressed whether a partnership, Alpha Film Co. , could claim a depreciation deduction for a motion picture film using the income forecast method based on gross receipts rather than net income. The partnership had no net income in 1975 due to distribution expenses exceeding gross receipts. The court ruled that under the income forecast method, as prescribed by the Commissioner and upheld in prior cases, depreciation must be calculated using net income. Therefore, Alpha was not entitled to a depreciation deduction for 1975 because it had no net income that year.

Facts

Lorne and Nancy Greene were limited partners in Alpha Film Co. , which purchased the film "Ten Days' Wonder" for distribution. Alpha entered into an agreement with Levitt-Pickman Film Corp. for distribution, where gross receipts were to be deposited into a special account and used first to cover distribution expenses and fees before any funds reached Alpha. From 1972 to 1976, the film's gross receipts totaled $60,778, which was insufficient to cover distribution expenses, resulting in no net income for Alpha in those years. Alpha elected to use the income forecast method for depreciation on its tax returns, calculating depreciation based on gross receipts rather than net income.

Procedural History

The Commissioner of Internal Revenue disallowed the depreciation deduction claimed by Alpha for 1975, leading to a deficiency notice for the Greenes. The Greenes petitioned the Tax Court for a redetermination of this deficiency. Both parties filed cross-motions for partial summary judgment on the issue of whether Alpha could claim a depreciation deduction for 1975 under the income forecast method using gross receipts.

Issue(s)

1. Whether Alpha Film Co. was entitled to a depreciation deduction for 1975 under the income forecast method using gross receipts rather than net income?

Holding

1. No, because under the income forecast method as prescribed by the Commissioner, depreciation must be based on net income, and Alpha had no net income in 1975.

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Court’s Reasoning

The Tax Court, relying on Revenue Rulings 60-358 and 64-273, held that the income forecast method for film depreciation requires the use of net income in the calculation. The court noted that Alpha’s use of gross receipts was inconsistent with prior cases like Siegel v. Commissioner and Wildman v. Commissioner, where the court rejected attempts to vary the method prescribed by the Commissioner. The court emphasized that Alpha elected to use this method and could not unilaterally change it without the Commissioner’s consent. The court found no need to decide if the gross receipts constituted income for Alpha since the lack of net income in 1975 precluded any depreciation deduction under the correct application of the method.

Practical Implications

This decision reinforces that the income forecast method for film depreciation must strictly adhere to the use of net income, impacting how partnerships and film producers calculate depreciation for tax purposes. It underscores the importance of consistent application of chosen depreciation methods and the necessity of seeking the Commissioner’s approval for changes. The ruling affects the tax planning strategies of film industry professionals, requiring careful consideration of distribution agreements and anticipated net income. Subsequent cases, such as Bizub v. Commissioner and Perlman v. Commissioner, have followed this precedent, solidifying the requirement to use net income in the income forecast method for film depreciation.

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