***Frederick Weisman Co. v. Commissioner, 97 T. C. 563 (1991)***

Expenses incurred in redeeming corporate stock, even when necessary for business survival, are nondeductible capital expenditures.

**Summary**

Frederick Weisman Co. redeemed its stock to secure a Toyota distributorship agreement essential for its survival. The company sought to deduct the redemption costs as ordinary business expenses. The Tax Court held that these costs were nondeductible capital expenditures, rejecting the applicability of the 'Five Star' exception. The decision emphasized the 'origin and nature' of the transaction over the business purpose, aligning with Supreme Court precedents.

**Facts**

Frederick Weisman Co. operated a Toyota distributorship through its subsidiary, Mid-Atlantic Toyota Distributors, Inc. (MAT). To renew its distributorship agreement with Toyota Motor Sales, U. S. A. , Inc. (TMS) in 1982, TMS required Weisman Co. to redeem the shares of all shareholders except Frederick R. Weisman. The company complied, redeeming shares for a total of $12,022,040 and incurring $189,335 in legal expenses. Weisman Co. attempted to deduct these costs over the 5-year term of the new agreement.

**Procedural History**

The Commissioner of Internal Revenue challenged the deductions, leading to a motion for judgment on the pleadings. The Tax Court reviewed the case, considering the precedent set by *Five Star Mfg. Co. v. Commissioner* and subsequent cases. Ultimately, the court declined to follow the Fifth Circuit's *Five Star* opinion and issued a ruling that the costs were nondeductible capital expenditures.

**Issue(s)**

1. Whether the costs incurred by Frederick Weisman Co. in redeeming its stock, necessary for the survival of its business, are deductible as ordinary and necessary business expenses under section 162(a) of the Internal Revenue Code.

**Holding**

1. No, because the costs of stock redemption are capital expenditures under the 'origin and nature' test, and the business purpose or survival necessity does not transform them into deductible expenses.

**Court's Reasoning**

The court applied the 'origin and nature' test established by the Supreme Court in

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cases like *Woodward v. Commissioner* and *Arkansas Best Corp. v. Commissioner*. It rejected the 'Five Star' exception, which allowed deductions for stock redemption costs when necessary for corporate survival, as it focused on the business purpose rather than the nature of the transaction. The court emphasized that stock redemption is a capital transaction, and the costs involved are capital expenditures, not deductible under section 162(a). The court also noted that section 311(a) of the Internal Revenue Code, which precludes recognition of gain or loss on stock redemptions, further supported the nondeductibility of these costs. The legislative history of section 162(k), added in 1986 to disallow deductions for stock redemption expenses, was considered but did not affect the court's interpretation of existing law.

**Practical Implications**

This decision clarifies that costs associated with stock redemptions are capital expenditures, regardless of the business necessity or survival imperative. Practitioners must advise clients that such costs cannot be deducted as ordinary business expenses. This ruling impacts corporate planning, particularly in situations where stock redemptions are required by third parties for business agreements. It also aligns with subsequent legislative changes, like section 162(k), which codified this principle. Future cases involving stock redemption costs will need to consider this precedent, emphasizing the 'origin and nature' of the transaction over any business purpose.

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