Tutor-Saliba Corp. v. Commissioner, 115 T. C. 1 (2000)

Disputed claims must be included in the estimated contract price for long-term contracts under the percentage of completion method when it is reasonably estimated that they will be received.

Summary

Tutor-Saliba Corp. challenged the validity of an IRS regulation requiring the inclusion of disputed claims in the estimated contract price for long-term contracts reported under the percentage of completion method. The Tax Court upheld the regulation, finding it consistent with the statutory language and purpose of section 460. The court reasoned that the regulation's requirement to include disputed claims when reasonably expected to be received aligns with the statute's goal of reducing income deferral and is supported by the legislative history's use of terms like 'expected' and 'anticipated'. This decision has significant implications for how long-term contract income is reported and the potential interest obligations under the look-back method.

Facts

Tutor-Saliba Corp. , a California-based general contractor, entered into fixed-price long-term contracts for construction projects. These contracts often led to disputes over additional work required due to changes or delays. Tutor-Saliba reported income from these contracts using the percentage of completion method but did not include income from disputed claims until they were resolved, in accordance with the all events test. The IRS, however, required the inclusion of disputed claims in the estimated contract price as soon as it was reasonably estimated that they would be received, as per section 1. 460-6(c)(2)(vi) of the Income Tax Regulations.

Procedural History

Tutor-Saliba filed a motion for partial summary judgment in the U. S. Tax Court, challenging the validity of the IRS regulation requiring the inclusion of disputed claims in the estimated contract price. The Tax Court denied the motion, upholding the regulation as a valid interpretation of section 460.

Issue(s)

1. Whether section 1. 460-6(c)(2)(vi) of the Income Tax Regulations, which requires the inclusion of disputed claims in the estimated contract price when it is reasonably estimated that they will be received, is a valid interpretation of section 460 of the Internal Revenue Code?

Holding

1. Yes, because the regulation harmonizes with the plain language, origin, and

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purpose of section 460, and is a reasonable interpretation of the statute.

Court’s Reasoning

The court applied the Chevron standard of review, focusing on whether the regulation was a reasonable interpretation of the statute. The court found that the term ‘estimated’ in section 460 did not preclude the inclusion of disputed claims and that the regulation did not contradict the statute’s plain language. The court also considered the legislative history, noting that Congress intended to limit income deferral by mandating the percentage of completion method and providing for a look-back method. The regulation’s requirement to include disputed claims when reasonably expected to be received was seen as consistent with this intent, as it would reduce the likelihood of look-back interest due to income deferral. The court rejected Tutor-Saliba’s argument that the all events test should apply, stating that section 460 created a self-contained accounting method that did not necessarily incorporate the all events test. The court also found that the regulation’s ‘reasonable expectancy’ standard, while potentially difficult to apply, was not a reason to invalidate it.

Practical Implications

This decision requires taxpayers to include disputed claims in the estimated contract price as soon as they can reasonably expect to receive them, rather than waiting until the claims are resolved. This may lead to earlier income recognition and potentially reduce the amount of look-back interest owed. Taxpayers and practitioners must now assess when it is reasonably foreseeable that disputed claims will be received, which may involve case-by-case determinations. The decision also reaffirms the IRS’s authority to issue interpretive regulations that reasonably implement the statutory intent, even if they depart from traditional accrual accounting principles like the all events test. Subsequent cases have applied this ruling in determining the timing of income recognition for long-term contracts, and it has influenced how taxpayers approach their accounting and tax planning for such contracts.

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