

**MEMO# 3555**

March 2, 1992

## **SUPREME COURT DENIES DEDUCTION FOR EXPENSES INCURRED IN TAKEOVER**

March 2, 1992 TO: TAX MEMBERS NO. 11-92 ACCOUNTING/TREASURERS MEMBERS NO. 7-92 12b-1 AD HOC COMMITTEE RE: SUPREME COURT DENIES DEDUCTION FOR EXPENSES INCURRED IN TAKEOVER \_\_\_\_\_ In

Indopco, Inc. v. Commissioner, No. 90-1278, February 26, 1992, the Supreme Court held that the investment banking and legal expenses arising as a result of the acquisition of National Starch and Chemical Corporation by Unilever United States, Inc., were not deductible under Internal Revenue Code section 162(a) as ordinary and necessary business expenses. The Tax Court had ruled that because long-term benefits accrued to National Starch as a result of the acquisition, the expenditures were capital in nature and non-deductible. The Court of Appeals affirmed. National Starch argued that in Commissioner v. Lincoln Savings and Loan Assn. the Supreme Court had set forth the exclusive test for identifying capital expenditures, in which creation or enhancement of a separate and distinct additional asset is a prerequisite for capitalization, and deductibility is the norm. The Supreme Court, in a sweeping opinion, stated that deductions are exceptions to the norm of capitalization, and are allowed only if there is a clear provision for them in the Code and the taxpayer demonstrates its right to the deduction. The Court further stated that Lincoln Savings holds only that creation of a separate asset may be sufficient reason for classification as a capital expenditure, not that it is a prerequisite to that finding. National Starch also had argued that Lincoln Savings prohibited relying on the existence of a future benefit to distinguish an ordinary expense from a capital expenditure. The Supreme Court found that while it might not be proper to capitalize an expenditure merely because of an incidental future benefit, the existence of a future benefit is important in deciding whether the proper treatment is expensing or capitalization. We will keep you informed of further developments. David J. Mangefrida Jr. Assistant Counsel - Tax Attachment

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