

**MEMO# 11929**

June 6, 2000

## **APPEALS COURT REVERSES TAX COURT DECISION THAT BANK LOAN ORIGINATION COSTS MUST BE CAPITALIZED**

1 PNC Bancorp, Inc. v. Commissioner, 2000 U.S. App. LEXIS 11084 (3d Cir. 2000). 2 PNC Bancorp, Inc. v. Commissioner, 110 T.C. 349 (1998). 3 INDOPCO, Inc. v. Commissioner, 503 U.S. 79 (1992). 4 Commissioner v. Lincoln Savings & Loan Ass'n, 403 U.S. 345 (1971). 5 FMR Corp. v. Commissioner, 110 T.C. 402 (1998). See ICI Memorandum to Tax Members No. 17-98, dated June 25, 1998. [11929] June 6, 2000 TO: TAX COMMITTEE No. 26-00 RE: APPEALS COURT REVERSES TAX COURT DECISION THAT BANK LOAN ORIGINATION COSTS MUST BE CAPITALIZED

The Court of Appeals for the Third Circuit recently held<sup>1</sup> that certain costs incurred by banks for marketing, researching and originating loans are deductible as “ordinary and necessary expenses” under section 162 of the Internal Revenue Code (the “Code”), reversing the Tax Court’s opinion in PNC Bancorp<sup>2</sup> that such costs must be capitalized under section 263 of the Code and amortized over the life of the loans. The Appeals Court decision is the latest in an important series of cases interpreting the scope of the Supreme Court’s decision in INDOPCO,<sup>3</sup> which has been understood by some courts to limit the types of expenses that may be deducted as ordinary and necessary expenses under section 162 of the Code. In its decision, the Appeals Court emphasized that any capitalization analysis must “keep the facts firmly in view”; it criticized the Tax Court for what it considered to be an overbroad reading of Lincoln Savings,<sup>4</sup> stating that “[w]e will not mechanistically apply phrases from those precedents in ignorance of the realities of the facts before us.” It is worth noting that Judge Ruwe of the Tax Court filed, within 10 days of each other, both the PNC Bancorp opinion and the opinion in FMR,<sup>5</sup> which held that costs related to developing and launching new mutual funds must be capitalized under section 263 of the Code. Naomi Gendler Camper Assistant Counsel