

UNITED STATES DISTRICT COURT  
WESTERN DISTRICT OF MICHIGAN

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| ABC BEVERAGE CORPORATION &                | ] |                           |
| SUBSIDIARIES, f/k/a Beverage America Inc. | ] | Case No. 1:07-cv-051      |
| & Subsidiaries,                           | ] |                           |
|   | ] |                           |
| Plaintiff,                                | ] |                           |
|   | ] | Honorable Paul L. Maloney |
| v.  | ] |                           |
|   | ] |                           |
| UNITED STATES OF AMERICA,                 | ] |                           |
|   | ] |                           |
| Defendant.                                | ] |                           |

**UNITED STATES’ MOTION IN LIMINE AND SUPPORTING  
MEMORANDUM TO PRECLUDE ALL EVIDENCE OTHER  
THAN EVIDENCE REGARDING THE PAYMENT FOR THE  
MCDONNELL PROPERTY CONCERNING THE ECONOMIC  
PERFORMANCE TEST**

The defendant, United States of America, by its counsel, files this motion in limine to preclude the plaintiff, ABC Beverage Corporation & Subsidiaries (ABC) from introducing certain evidence at the trial that is set for December 9, 2008. Specifically, as a consequence of the Court’s ruling on the plaintiff’s summary judgment motion that a portion of the purchase price that was paid for the McDonnell Property located at 555 McDonnell Boulevard, Hazelwood, Missouri (the “McDonnell Property”) was paid to buy out of an onerous lease, all evidence (both documentary and testimonial) other than evidence concerning when the plaintiff paid the \$11 million for the property is irrelevant with respect to the economic performance test under 26 U.S.C. §461(h) and should be precluded as a matter of law. This motion is limited to evidence relevant to the economic performance test and does not seek to preclude any evidence that relates to the “all events test” under Section

26 U.S.C. §461(h).

In this case, the plaintiff sought to deduct \$6.25 million of the \$11 million purchase price paid for the McDonnell Property as the cost of being relieved of obligations under a purportedly burdensome lease. The United States had argued that plaintiff was prohibited from deducting any portion of the \$11 million purchase price for the McDonnell Property and instead, submitted that the entire purchase price should be used to determine the basis of the property which would be thereafter depreciated over its useful life.<sup>1</sup> On August 27, 2008, this Court granted plaintiff's motion for summary judgment and held that plaintiff was entitled to deduct that portion of the purchase price attributable to buying out an excessive lease.

Alternatively, the United States argued that in the event that the Court found that the plaintiff is permitted to deduct a portion of the purchase price as the cost of getting out of its lease rather than being required to capitalize the entire acquisition cost, the deduction cannot be taken until 1999 and not in 1997 as claimed by ABC. (The tax laws provide that once it has been determined that an expenditure is deductible, rather than capitalizable, it is necessary to determine in what year the deduction is allowed. 26 U.S.C. §461(a) et seq.) Specifically, the government argued that ABC may not take a deduction until the satisfaction

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<sup>1</sup> Specifically, the United States argued ABC was prohibited from deducting any portion of its purchase price because 26 U.S.C. §167(c)(2) precludes allocating any portion of the \$11 million paid for the property to a lease. In addition, the United States argued that plaintiff was also prohibited from taking an expense deduction because 26 U.S.C. §263 prohibits a deduction for the purchase of a capital asset and ABC was bound by the tax consequences of its admitted capital acquisition based upon the Sixth Circuit's holding in *Wolter v. Construction Co., Inc.*, 634 F.2d 1029, 1038 (1980) which stated that “[i]t is axiomatic that a taxpayer must accept the tax consequences of his structural choices, whether contemplated or not.” citing *Commissioner v. National Alfalfa Dehydrating & Miller*, 417 U.S. 1345, 149 (1974). Those arguments did not prevail.

of (a) the “all events test” which requires that both the fact of liability and that the amount of the liability can be determined with reasonable accuracy before a deduction can be taken. (26 U.S.C. §461(h)(4) and, (b) the “economic performance test” which provides that the “all events test” is not met any earlier than when economic performance has occurred with respect to the item that gave rise to the liability. 26 U.S.C. §461(h)(1 and 2); Treas. Reg. §1.461-1(a)(2). This motion is directed at limiting evidence related to the “economic performance” test so as not to permit plaintiff to introduce evidence related to that test which would be inconsistent with the theory on which it succeeded on summary judgment.

In this case, both parties made arguments that involved two different subsections of the economic performance regulations. Specifically, economic performance relating to (1) the providing of property to the taxpayer by another person (Section 461(h)(2)(A)(ii)) or (2) the use of property by the taxpayer (Section 461(h)(2)(A)(iii)). While the Court found issues of material fact regarding the “economic performance” test as well as the “all events test” and denied the motions for summary judgment on the year of deduction arguments, the Court, found that plaintiff’s liability to the seller did not arise due to its use of the property. Thus, under the Court’s ruling Treas Reg. 1.461-4(d)(3)(i) that relates to use of property is now inapplicable. The United States contends that as a natural consequence of the Court’s ruling that part of the purchase price that was paid for the lease termination is that such amount cannot be said to have been paid for the providing of property to the taxpayer.

The Court, in Footnote 16 of its opinion, addressed the government’s alternative argument regarding economic performance where the United States had submitted that ABC was really arguing that its payment was for the termination of the onerous lease and not for

the acquisition of property. Therefore, the payment for the termination of a lease is not for the use of the property, is not for the providing of property to the taxpayer and does not fit within any of the other specified regulations under the economic performance tests. That being the case, the proper regulation is Treas. Reg. Section 1.461-4(g)(7) entitled, Other Liabilities, that states that if a liability cannot be characterized so as to fall under one of the other provisions of the rules, economic performance occurs when the taxpayer makes payments in satisfaction of what is owed. The Court stated “[a]lthough this argument has appeal, plaintiff has not been afforded an opportunity to respond to it” because the government raised the argument for the first time in its reply brief. Slip. op. at 24, n.16.<sup>2</sup> As a result, the Court did not address the argument.

The United States now asserts the above same argument under Treas. Reg. Section 1.461-4(g)(7) entitled, Other Liabilities<sup>3</sup>, to preclude ABC from introducing any evidence on

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<sup>2</sup> The Court summarizes the government’s argument on that issue as follows:

Plaintiff initially wants to characterize the transaction as a business expense for buying out a burdensome lease, rather than as the acquisition of a capital asset. Plaintiff then seeks to characterize the transaction as a provision of property for the purposes of identifying when that deduction can be taken. If the amount paid can be properly characterized as a purchase of property, then Plaintiff is not entitled to a business deduction. If on the other hand, the amount paid was to buy out a burdensome lease, then time of economic performance would not be determined under the regulation for the provision of property, but under the catch all provision, Treas. Reg. § 1.461-4(g)(7). In order to be able to take the deduction as a business expense, the transaction cannot be characterized as a transfer of ownership of property.

<sup>3</sup> Treas. Regulation 1.461-4(g)(7) entitled, Other Liabilities, states as follows:

In case of liabilities for which economic performance rules are not provided elsewhere in this section or in any other Internal Revenue regulation, revenue ruling or revenue procedure, economic performance occurs as the taxpayer makes payments in satisfaction of the liability to the person to which the liability is owed. This paragraph (g)(7) applies only if the liability cannot properly be characterized as a liability covered by rules provided elsewhere in this section. If a liability may properly be characterized as, for example, a liability arising from the provision of services or property, or by a taxpayer, the determination as to when economic performance occurs with respect to that liability is made under paragraph (d) of this section and not under this paragraph (g)(7).

the economic performance issue other than evidence regarding when the \$11 million payment for the McDonnell Property was made.

The Court has now ruled on part of ABC's claim to deduct \$6.25 million of the \$11 million purchase price paid for the McDonnell Property. Specifically, ABC argued and the Court has determined that a portion of ABC's \$11 million payment for the McDonnell Property was a payment for the buy out of a burdensome lease and not for the purchase of a capital asset, and therefore can be deducted rather than depreciated. The second part of ABC's claim is that such amount can be deducted in 1997. Under the law of the case doctrine, findings made at one point in the litigation becomes the law of the case for subsequent stages of that same litigation. *Rouse v. Daimler Chrysler Corp.*, 300 F.3d 711 (6<sup>th</sup> Cir. 2002). Therefore, pursuant to the law of the case doctrine, the Court's ruling that the payment was made to buy out of a bad lease establishes that the only relevant regulatory provision to determine when economic performance was satisfied is the above cited "Other Liabilities" regulation and that only evidence relevant to that regulation is properly admissible on the economic performance test and that the regulatory provision relating to the providing of property under Treas. Reg. Section 1.461-4(d)(6)(iii) and evidence relating to that regulatory provision is irrelevant.

Put another way, ABC has successfully persuaded this Court that it is permitted to deduct a portion of the purchase price paid for acquiring the McDonnell Property as a buy out of a bad lease and is not required to treat the entire purchase price as a capital acquisition

and to depreciate it over its useful life. The next question is when can a deduction for the same transaction be taken. 26 U.S.C. §461(a) *et seq.* It is logically inconsistent to characterize the very same exact transaction as a partial buy out of a bad lease and not as purchase of a capital asset for purposing of determining whether a deduction can be taken and then characterize the same transaction as a purchase of a property and not a partial buyout of a lease for determining when that deduction can be taken. Therefore, having successfully argued that the transaction was partially a buy out of a lease, ABC should now be prevented from arguing just the opposite that the same portion of the purchase price was paid for the acquisition of a capital asset on the related issue of when the deduction can be taken. Therefore, any evidence concerning Treas. Reg. Section 1.461-4(d)(6)(iii) which relates to the providing of property to the taxpayer by another is irrelevant as a matter of law. This is a form of judicial estoppel which is an equitable doctrine that is designed to protect the integrity of the judicial process by preventing a party from taking a position inconsistent with one that was previously successfully asserted. *In re Commonwealth Institutional Sec.*, 394 F.3d 401, 406 (6<sup>th</sup> Cir. 2005); *Browning v. Levy*, 283 F.3d 761, 776 (6<sup>th</sup> Cir. 2002). ABC cannot have it both ways or in other words, have its cake and eat it too). *Reynolds v. Commissioner*, 861 F.2d 469, 472, (6<sup>th</sup> Cir. 1988) *citing*, *Duplan Corp. v. Deering Milliken, Inc.*, 397 F.Supp. 1146, 1177 (D.S.C. 1974).

Accordingly, as discussed above, the payment for the buy out of a lease does not fit within any of the other regulations under Section 461, therefore, the proper regulation is Treas. Reg. 1.461-4(g)(7), which provides that for certain liabilities that are not addressed in the regulations, economic performance occurs when the taxpayer pays the liability.

Therefore, as a matter of law, the only relevant evidence on which economic performance test can be based is when ABC paid the \$11 million for the purchase of the McDonnell Property. Accordingly, any evidence with respect to the economic performance test other than evidence relating to when payment was made should be precluded, as a matter of law.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on November 10, 2008, a copy of the foregoing was filed electronically. Notice of this filing will be sent to all parties by operation of the Court's electronic filing system.

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