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Simon v. Commissioner: Are Musicians Orchestrating a New Ensemble of Deductions

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Casenotes

SIMON v. COMMISSIONER:
ARE MUSICIANS ORCHESTRATING A NEW
ENSEMBLE OF DEDUCTIONS?

I. INTRODUCTION

Depreciation is one of the most basic concepts inherent in the American income tax system. Generally, it enables a taxpayer to annually deduct from gross income a portion of the cost of an asset used to produce income, so at the end of the asset's useful life the aggregate amount deducted annually equals the original cost.¹ From 1913 to 1981, the basic depreciation provision of the Internal Revenue Code (Code) remained relatively unchanged.² The Internal Revenue Service (IRS) attempted to standardize the application of the depreciation allowance through numerous administrative rules until 1981, when Congress stepped in.³ Congress enacted the Economic Recovery Tax Act (ERTA), I.R.C. § 168 (1981), which introduced the Accelerated Cost Recovery System (ACRS).⁴ The implementation of ACRS abruptly changed the nature of the rules controlling depreciation deductions.⁵

ACRS was enacted to stimulate economic growth and simplify depreciation rules.⁶ The ACRS method for determining the depre-

1. See *United States v. Ludey*, 274 U.S. 295, 300-01 (1927); S. REP. NO. 97-144, at 39 (1981), *reprinted in* 1981 U.S.C.C.A.N. 105, 171 ("Depreciation is based on the concept that the cost of an asset should be allocated over the period it is used to produce income."). For a further discussion of depreciation, see *infra* notes 37-79 and accompanying text.

2. See generally JOHN F. WITTE, *THE POLITICS & DEVELOPMENT OF THE FEDERAL INCOME TAX*. (UNIV. OF WIS. PRESS 1985) (discussing history of income tax).

3. See Henry J. Lischer, Jr., *Depreciation Policy: Whither Thou Goest*, 32 SW. L.J. 545, 550-69 (1978). For a discussion of the history behind the depreciation allowance, see *infra* notes 48-63 and accompanying text.

4. For a further discussion of the Economic Recovery Tax Act (ERTA) and the Accelerated Cost Recovery System (ACRS), see *infra* notes 64-79 and accompanying text.

5. For a discussion of ACRS as a depreciation concept, see *infra* notes 71-79 and accompanying text.

6. See S. REP. NO. 97-144, at 47 (1981), *reprinted in* 1981 U.S.C.C.A.N. 105, 171 (stating that present rules "do not provide the investment stimulus that is essential for economic expansion" and are "unnecessarily complicated."). For a further discussion of the policy objectives behind ACRS, see *infra* notes 64-70 and accompanying text.

ciation deduction allows the taxpayer to recover the cost of tangible property over arbitrary periods of time.⁷ In order to qualify for depreciation, the asset must be a “wasting asset,” one that is subject to exhaustion, wear and tear.⁸

Since its inception in 1981, courts have interpreted the ACRS method inconsistently.⁹ In particular, it is unclear whether ACRS eliminated the “useful life” requirement inherent in the depreciation scheme. In *Simon v. Commissioner*,¹⁰ the Court of Appeals for the Second Circuit held that the useful life requirement was eliminated with the effectuation of ACRS.¹¹ The court reached its conclusion through an analysis of statutory language, legislative history and the nature of the depreciation concept.¹²

This Note examines the Second Circuit’s decision in *Simon*, including the court’s rationale and *Simon*’s future implications. First, section two sets forth *Simon*’s factual background.¹³ Then, section three discusses the concept of depreciation,¹⁴ including the history of depreciation prior to ERTA,¹⁵ the effect ERTA had on depreciation¹⁶ and the judicial interpretations of asset depreciation prior and subsequent to ACRS.¹⁷ Section four summarizes the majority and dissenting opinions in *Simon*.¹⁸ Section five critically analyzes

7. See generally WITTE, *supra* note 2.

8. See I.R.C. § 167(a) (1986). For a further discussion of an asset’s eligibility for depreciation, see *infra* notes 43, 61, 63, 72, 77-79 and accompanying text.

9. Compare *Liddle v. Commissioner*, 65 F.3d 329, 334 (3d Cir. 1995) (holding useful life unnecessary to take deduction), with *Clinger v. Commissioner*, 60 T.C.M. (CCH) 598 (1990) (holding ACRS only de-emphasized useful life, not eliminate it).

10. 68 F.3d 41 (2d Cir. 1995).

11. See *id.* at 46. For a discussion of the *Simon* case, see *infra* notes 106-43 and accompanying text.

12. See *id.* For further discussion of the court’s analysis, see *infra* notes 106-37 and accompanying text.

13. For a discussion of the facts in *Simon*, see *infra* notes 21-36 and accompanying text.

14. For a discussion of the concept of depreciation, see *infra* notes 37-47 and accompanying text.

15. For a discussion of the history of depreciation prior to ERTA, see *infra* notes 48-63 and accompanying text.

16. For a discussion of ERTA and its effect on depreciation, see *infra* notes 64-79 and accompanying text.

17. For a discussion of judicial interpretations of asset depreciation prior and subsequent to ACRS, see *infra* notes 80-105 and accompanying text.

18. For a discussion of the majority opinion, see *infra* notes 106-37 and accompanying text. For a discussion of the dissenting opinion, see *infra* notes 138-43 and accompanying text.

the *Simon* court's decision.¹⁹ Finally, section six examines the future implications of *Simon* on subsequent law.²⁰

II. FACTS

In 1985, Richard Simon and his wife Fiona were professional violinists employed as full-time performers with the New York Philharmonic Orchestra (Philharmonic).²¹ During that year, they purchased two minimally used Tourte violin bows for \$30,000 and \$21,500 respectively.²² The Simons purchased these violin bows for regular use in their employment as professional violinists.²³

In 1989, the Simons used the Tourte bows on a regular basis.²⁴ During this year, the Tourte bows were subject to "substantial" wear and tear from their usage, although not yet becoming "played

19. For a critical analysis of the *Simon* decision, see *infra* notes 144-62 and accompanying text.

20. For a discussion of the future implications of *Simon*, see *infra* notes 163-69 and accompanying text.

21. See *Simon v. Commissioner*, 68 F.3d 41, 42 (2d Cir. 1995). Richard Simon began playing the violin in 1943, when he was seven years old. See *Simon v. Commissioner*, 103 T.C. 247, 249 (1994). In 1956, he earned a bachelor's degree in music from the Manhattan School of Music, which he attended on a full scholarship. See *id.* Thereafter, he earned his master's degree in music from both his alma mater and Columbia University. See *id.* Mr. Simon studied under many renowned musicians during his educational career. See *id.* He joined the first violin section of the Philharmonic in 1965, and additionally was a teacher, chamber music player and a soloist. See *id.*

At four years old, Fiona Simon began to study violin. See *id.* From 1963 to 1971, she studied at the Purcell School in London and, from 1971 to 1973, at the Guildhall School of Music. See *id.* In 1985, Fiona Simon joined the Philharmonic in the first violin section. See *id.* Additionally, she was a chamber music player, soloist and free-lance performer. See *id.*

22. See *Simon*, 68 F.3d at 42-43 (noting that bows were preserved in pristine condition in collections). These particular violin bows were not ordinary in the least: they were made by the premier bow maker Francois Xavier Tourte in the nineteenth century. See *Simon*, 103 T.C. at 250. He was renowned for the technical improvements that he made in bow design. See *Simon*, 68 F.3d at 42-43.

23. See *Simon*, 103 T.C. at 251 ("Petitioners purchased the Tourte bows for their tonal quality, not for their monetary value."); see also Brief for the Appellees at 3, *Simon v. Commissioner*, 68 F.3d 41 (2d Cir. 1995) (No. 94-4237) ("To compete successfully at their professional level, musicians like the Simons require equipment of the highest quality."). The bows were purchased from Moes & Moes, Ltd., a restorer and dealer in violins and violin bows. See *Simon*, 103 T.C. at 250. Prior to this purchase by Moes & Moes, Ltd., the bows belonged to the Hans Weiszar collection in California, which acquired them from a world-famous collection. See *id.* at 279.

24. See *Simon*, 103 T.C. at 252. During that year, the Simons performed with the Philharmonic in the finest concert halls across the nation and around the world. See *id.* at 249. They practiced in numerous rehearsals with the Philharmonic, which were more time consuming and demanding than the concerts themselves. See *id.* The Simons played in four concerts per week, performing over 200 different works. See *id.*

out.”²⁵ Consequently, the Simons believed that they could depreciate the bows under ACRS.²⁶

Central to understanding how Tourte bows suffer wear and tear is an explanation of how a violin bow is constructed. There are four parts to a violin bow: a flexible wooden stick, horsehair, a ferrule (screw) and a frog.²⁷ The bow plays an integral part in the production of sound, through the vibration of the stick.²⁸

Old violins played with old bows produce a superior sound to newer violins played with newer bows.²⁹ When used on a regular basis, violin bows will suffer wear and tear and eventually become

25. *See id.* Richard Simon “admitted that the bows showed a ‘very minuscule amount of wear.’” Lee A. Sheppard, *The Musicians’ Tax Shelter*, 64 TAX NOTES 1259, 1261 (Sept. 5, 1994) [hereinafter Sheppard, *The Musicians*]. Accordingly, substantial testimony by Richard Simon concerning the bow’s wear and tear was attributed to the frog, ferrule and the horsehair. *See Simon*, 103 T.C. at 277. However, the replacement cost for these parts is nominal. *See* Kevin M. Cunningham, Comment, *Which Concept of Depreciation Should Guide Us? Trying To Develop a Consistent Framework for the Federal Income Tax System*, 14 VA. TAX REV. 753, 756 (1995). While the original ferrule and frog had to be replaced when the bows were purchased, the Simons placed the originals “in a vault for safekeeping so . . . they could protect their investment.” *Simon*, 103 T.C. at 277. Wear and tear on a violin bow is created in a few ways. Over time, perspiration from a player’s hands penetrates the wood in the stick, destroying the bow’s performing utility. *See id.* at 251. Wear and tear is also caused by cracks in the wood and using a heavy hand on the bow while playing certain pieces of music. *See id.* Using a heavy hand may cause the bow to curve and warp, since the stick may be pressed against the horsehair. *See id.* at 251-52 (noting that Simons’ use of bows “subjected the bows to substantial wear and tear.”); *see generally* Cunningham, *supra*, at 756 (identifying how stick suffers wear and tear).

26. *See Simon*, 103 T.C. at 251. The Simons wished to depreciate the antique violin bows over a five-year period. *See* Brief for the Appellant at 3, *Simon v. Commissioner*, 68 F.3d 41 (2d Cir. 1995) (No. 94-4237).

27. *See Simon*, 103 T.C. at 250. The Tax Court described the interaction of these four components as follows:

The horsehair is a group of single strands of hair that come from the tails of Siberian horses. A hatchet-shaped head holds one end of the horsehair, and the other end is attached to a frog. The frog, which is inserted into the stick, is a movable hollow piece by which the bow is held. The frog has an eyepiece on the end that catches the screw. The screw is the small knob at the end of the bow that is adjusted to tighten or loosen the horsehair in order to change the tension on the horsehair. The horsehair is the part of the bow that touches the violin strings. Rosin is applied to the horsehair to supply the frictional element that is necessary to make the violin strings vibrate.

Id.

28. *See id.* The stick, which is the working part of the bow, varies in balance, thickness and weight. *See id.*

29. *See id.* Richard Simon plays a Nicolo Amati violin, made in 1660. *See id.* Fiona Simon’s violin was made in 1750. *See id.* (“The combination of these old violins and the Tourte bows results in a magnificent sound that is superior to the sounds produced by newer instruments.”).

“played out,” causing an inferior sound.³⁰ Notwithstanding its diminished utility as a violin bow, the “played out” Tourte violin bow retains its value as a collectible antique.³¹

The Simons claimed depreciation deductions of \$6,300 and \$4,515 on the two bows.³² The Tax Court permitted the deductions, reasoning that such result comports with I.R.C. § 168 (1997) and enables the Simons’ to match the expenditure made on the Tourte bows with the income generated from their use.³³ Additionally, the court found that the violin bows were “tools of a trade,” not “works of art.”³⁴ Two judges wrote separate concurring opinions, while three judges wrote separate dissenting opinions.³⁵ The Com-

30. See *id.* at 252. When a bow becomes “played out,” the wood stick no longer vibrates nor produces a quality sound, due to wear and tear suffered. See *id.* Thus, the violin bow is inferior and of limited use to the musician. See *id.* The bows were meticulously maintained in this case, casting doubt on the actual amount of “wear and tear” suffered. See Sheppard, *The Musicians’*, *supra* note 25, at 1262 (“This maintenance included frequent replacement of parts of the bows that wear out quickly; that is, all parts other than the delicately carved Pernambuco wood stick.”).

31. See *Simon v. Commissioner*, 68 F.3d 41, 43 (2d Cir. 1995). There is an independent market for the purchase and sale of Tourte and other antique violin bows. See *Simon*, 103 T.C. at 252. The value of these bows is partially due to the sticks’ construction, consisting of Pernambuco wood, which is now very scarce. See *id.* at 253. See also Siobhan E. Dupuy, Note, *Works of Art as Depreciable Tools of a Trade Under ACRS: Simon v. Commissioner & Liddle v. Commissioner*, 48 TAX LAW. 629, 635 (1995) (acknowledging scarcity of Pernambuco wood). The wood currently substituted for Pernambuco wood is comparatively inferior. See *Simon*, 103 T.C. at 253.

Furthermore, even though the bows here physically deteriorated since their purchase in late 1985 for \$30,000 and \$21,500, they were appraised five years later at \$45,000 and \$35,000, respectively. See *id.* at 252. Specifically, the sticks of the bows were worn down. See *id.*

32. See *Simon*, 103 T.C. at 251. Both parties agreed that these amounts are the correct amounts to be depreciated if such deduction is permitted. See *id.*

33. See *id.* at 261. The court also stated that a contrary result “would contradict section 168 and vitiate the accounting principle that allows taxpayers to write off income-producing assets against the income produced by those assets.” *Id.* The court found that under § 168, four prerequisites had to be satisfied before an asset could be eligible for a depreciation deduction under ACRS: the asset must be “(1) tangible personal property; (2) placed in service after 1980; (3) used in the taxpayer’s trade or business; and (4) subject to wear and tear from the taxpayer’s use in his trade or business.” Dupuy, *supra* note 31, at 629 (citing *Simon*, 103 T.C. at 258-61) (footnote omitted). The Tax Court found that the only real issue was whether the instruments suffered wear and tear, since ERTA eliminated the useful life concept. See *Simon*, 103 T.C. at 258-61.

34. See Dupuy, *supra* note 31, at 635. “[I]f a work of art is used in a taxpayer’s trade or business and, through such use, is subject to wear and tear, it will not be considered art for tax purposes.” *Id.* In *Simon*, the Tax Court defined a work of art as a “passive object, such as a painting, sculpture, or carving, that is displayed for admiration of its aesthetic qualities.” *Simon*, 103 T.C. at 261 n.11.

35. See *Simon*, 103 T.C. at 247. The first concurring opinion was written by Judge Ruwe, who opined that the less than perfect result here is “the price of tax

missioner subsequently appealed the decision to the Court of Appeals for the Second Circuit.³⁶

III. BACKGROUND

A. What Is Depreciation?

Depreciation is defined as the “amount set aside for each taxable year such that at the end of the asset’s useful life^[37] the sum of those amounts set aside is equivalent to the original cost of the item.”³⁸ By the application of a depreciation deduction, a taxpayer reduces the amount of ordinary income that he must report annually.³⁹ Originally, depreciation deductions were measured by an as-

simplification implicit in section 168.” *Id.* at 267 (Ruwe, J., concurring). In a separate opinion, Judge Beghe also concurred in the result for the same reasons set forth in his opinion in *Liddle v. Commissioner*. *See id.* at 267-68 (Beghe, J., concurring). Judge Hamblen dissented, primarily due to the belief that the Tourte bows were not of a character subject to depreciation. *See id.* at 281 (Hamblen, J., dissenting). Judge Hamblen supported this conclusion by finding that “[t]he Tourte bows are usable and treasured works of art whose physical life and use to petitioners were not lessened by wear and tear that could not be restored by current maintenance.” *Id.* at 281. The second dissenting opinion, written by Judge Gerber, suggested bifurcating the asset into a recoverable value and an intrinsic value. *See id.* at 281 (Gerber, J., dissenting). Under this compromise approach, only the portion of the bows that are subject to wear and tear are depreciable, not the intrinsic value retained after the bows can no longer be used musically. *See id.* at 282. Finally, Judge Halpern’s dissenting opinion criticized the viability of Judge Gerber’s bifurcation approach, due to the lack of a determinable useful life for the bows. *See id.* at 284-85.

36. *See Simon*, 68 F.3d at 43. The Commissioner’s position against permitting the depreciation deductions rested on two arguments. *See Simon*, 103 T.C. at 258. First, the deductions were disallowed since “the useful lives of the Tourte bows are indeterminable because the bows are treasured works of art for which it is impossible to determine useful lives.” *Id.* Second, the Commissioner contended that the bows were depreciable only if they each had a determinable useful life under I.R.C. § 167: since the bows had existed for over 100 years, the remaining useful life was unascertainable. *See id.*

37. Useful life is defined as “the period of time depreciable property [is] expected to be used in the taxpayer’s business or income-producing activities.” BORIS I. BITTKER & LAWRENCE LOKKEN, *FEDERAL TAXATION OF INCOME, ESTATES AND GIFTS* ¶ 23.1.1 (2d ed. 1989).

38. Dupuy, *supra* note 31, at 630 (citing *United States v. Ludey*, 274 U.S. 295, 300-01 (1927)). Stated another way, “[d]epreciation is an annual deduction representing the daily decrease in value of the asset attributable to exhaustion, wear and tear, or obsolescence.” *Id.* at 636. *See also* Douglas A. Kahn, *Accelerated Depreciation-Tax Expenditure or Proper Allowance for Measuring Net Income?*, 78 MICH. L. REV. 1, 14 (1979) (“depreciation is the amortization of the cost of an asset over the period that the owner employs it in a profit-seeking activity.”) (footnote omitted).

39. *See Ludey*, 274 U.S. at 300-01. Permitting depreciation is advantageous to the taxpayer because otherwise, gains and losses are subject to capital gains tax rates. *See Cunningham*, *supra* note 25, at 754-55.

set's declining value over time.⁴⁰ Congress subsequently replaced this method with one that relied on standardized rates, in order to simplify depreciation rules.⁴¹

The concept of depreciation was developed in order to allow taxpayers to accurately match the cost of an asset to the income produced by the asset.⁴² Historically, depreciation was not allowed for assets that were not consumed in the taxpayer's business or over time.⁴³ Instead, the length of time that the asset produced income determined the quantity of depreciation deductions permitted for the asset.⁴⁴ Consequently, the "determinable useful life" concept was needed in order to calculate the yearly depreciation allowance.⁴⁵ An asset's useful life, however, can be shorter than its economic life.⁴⁶ Depreciation considers an asset valueless aside from its income producing capacity.⁴⁷

40. See Cunningham, *supra* note 25, at 759. Both the corporation excise tax of 1909 and the Revenue Act of 1913 utilized the decrease in value depreciation system. See *id.* The policy underlying depreciation deductions, however, is not so related to the asset's decrease in value. See *id.* at 761.

41. See *id.* at 760. By 1939, depreciation included the requirement of a decline in the asset's market value due to wear and tear. See *id.*

42. See Massey Motors, Inc. v. United States, 364 U.S. 92, 96 (1960). Essentially, this results in a "gradual sale" of the asset. See Ludey, 274 U.S. at 301; see also Anthony P. Polito, *Fiddlers on the Tax: Depreciation of Antique Instruments Invites Reexamination of Broader Tax Policy*, 13 AM. J. TAX POL'Y 87 (1996) (noting that "[i]n fact, the depreciation allowance has long tended to be accelerated in some degree relative to economic depreciation.").

43. See Dupuy, *supra* note 31, at 633 (noting that asset must be "wasting" to be depreciated). Examples of undepreciable assets include raw land, antiques and art work because these assets are likely to have a value greater than or equal to their cost to the taxpayer. See *id.* (citing Hawkins v. Commissioner, 713 F.2d 347 (8th Cir. 1993)); see also Cunningham, *supra* note 25, at 758 (concluding that violin bows are not wasting assets and therefore do not cause economic loss).

44. See *Simon*, 68 F.3d at 44. See also Kahn, *supra* note 38, at 35 (noting that depreciation allocates costs incurred in previous years). When determining the amount of the deduction, the accounting concept that depreciation does not consider market fluctuations in the value of the asset governs. See *Fribourg Navigation v. Commissioner*, 383 U.S. 272, 277 (1966). See also Kahn, *supra* note 38, at 31 (reasoning that "such unrealized appreciation or depreciation is not taken into account for tax purposes until realized."). It also does not consider the asset's replacement cost. See Dupuy, *supra* note 31, at 630.

45. See *United States v. Ludey*, 274 U.S. 295, 300-01 (1927). See also Kahn, *supra* note 38, at 15 ("[t]he 'useful life' of an asset is the amount of time that the taxpayer expects to use the asset in his business."). Additionally, the asset's physical life can exceed its useful life. See *id.*

46. See Massey Motors, Inc. v. United States, 364 U.S. 92, 96 (1960). Economic life is defined as "[u]seful or profitable life of property, which may be shorter than the physical life." BLACK'S LAW DICTIONARY 513 (6th ed. 1990).

47. See Dupuy, *supra* note 31, at 630 (citing BORIS J. BITTKER & LAWRENCE LOKKEN, FEDERAL TAXATION OF INCOME, ESTATES & GIFTS ¶ 23.1.2 (2d ed. 1989)). This is so because the asset is valued at the total amount that would be paid for the income it produces. See *id.*

B. The History of Depreciation Prior to ERTA

Prior to 1913, the United States' government lacked a constitutional basis to impose an income tax on its citizens.⁴⁸ Subsequent to ratification of the Sixteenth Amendment, the Tariff Act of 1913 was passed, which permitted a depreciation deduction on corporate income.⁴⁹

Prior to ERTA, the method used to compute depreciation deductions was governed by regulations, not by statute.⁵⁰ In 1920, the Bureau of Internal Revenue issued Bulletin F, which gave the taxpayer the authority to select the appropriate rate of depreciation.⁵¹ The onset of the depression in the 1930's, however, caused the government to tighten its reins over depreciation deductions: this was accomplished through an amendment to Bulletin F that created a "schedule of suggested useful lives for depreciable industrial assets."⁵²

In 1942, Bulletin F was amended once again by revising the existing useful lives and expanding the number of assets included in the bulletin.⁵³ Due to administrative problems concerning disagreement with taxpayers' useful life estimates, coupled with a desire to stimulate economic activity, the Internal Revenue Code of 1954⁵⁴ introduced accelerated depreciation methods.⁵⁵ The administra-

48. See Lischer, Jr., *supra* note 3, at 550. The first federal income tax was adopted in 1861, but without a depreciation deduction. See *id.* It appeared that such a deduction was prohibited by the Act of August 27, 1894. See *id.* However, the Tariff Act of 1909 permitted "a reasonable allowance for depreciation of property, if any," foreshadowing the deduction allowance in 1913. See *id.*

49. See Lischer, Jr., *supra* note 3, at 550.

50. See Brief for the Appellees at 10, *Simon v. Commissioner*, 68 F.3d 41 (2d Cir. 1995) (No. 94-4237).

51. See Lischer, Jr., *supra* note 3, at 551 n.57 ("The taxpayer should in all cases determine as accurately as possible according to his judgment and experience the rate at which his property depreciates.") (quoting U.S. BUREAU OF INTERNAL REVENUE, DEP'T OF THE TREASURY, BULL. "F" (1920)).

52. Lischer, Jr., *supra* note 3, at 551. The schedule served as a standard against which to judge the reasonableness of the depreciation deductions taken by the taxpayer. See *id.* Consequently, the "Bulletin F standardized lives enjoyed a presumption of validity and grew in importance." *Id.* at 552.

53. See *id.* at 552. The revised bulletin provided useful life estimates for approximately 5,000 assets. See *id.*

54. See Pub. L. No. 83-591, 68A Stat. 3 (1954).

55. See Lischer, Jr., *supra* note 3, at 554-55 & n.90 (stating that "[a]ccelerated depreciation was restricted to tangible property with a useful life of three years or more constructed or acquired after 1953."). See also Polito, *supra* note 42, at 96 (observing that "[t]he history of the depreciation allowance is largely one of accelerating tax depreciation relative to economic depreciation and thereby exaggerating the discrepancy between income tax depreciation allowances and the actual consumption of assets."). Through the Internal Revenue Code of 1954, taxpayers were given a choice of two accelerated methods: the sum of the years-digits

tive problems surrounding useful life estimates and the desire to stimulate economic growth, however, would continue to be the stimuli for depreciation policy changes through 1981, with the enactment of ACRS.⁵⁶

Bulletin F was abolished in 1962 for a more general approach to determining useful life.⁵⁷ Its replacement, Revenue Procedure 62-61, classified depreciable property into four groups, each containing numerous classes.⁵⁸ Each class had its own "guideline life" to use in computing depreciation deductions.⁵⁹ This basic group classification approach continued with the Asset Depreciation Range System (ADR), implemented in 1971.⁶⁰ ADR was interpreted as requiring an asset to have a useful life in order to be eligible for depreciation.⁶¹ Under the ADR, guideline lives were established by the IRS for categories of tangible personal prop-

method and the declining balance method. See Alan J. Auerbach, *The New Economics of Accelerated Depreciation*, 23 B.C. L. Rev. 1327, 1329 (1982). Prior to 1954, permissible types of accelerated depreciation were seldom used by taxpayers. See Kahn, *supra* note 38, at 30.

56. See Lischer, Jr., *supra* note 3, at 568-69 (explaining that similar motivations were behind adoption of asset depreciation range system (ADR)); Kahn, *supra* note 38, at 16 (same). For a discussion of how these factors prompted the enactment of ACRS, see *infra* notes 64-70 and accompanying text.

57. See Lischer, Jr., *supra* note 3, at 556-57 ("The Bulletin F useful lives . . . generated animosity in the business community and administrative difficulty for the Service.") (footnote omitted).

58. See *id.* at 556-57. The four groups were general business, manufacturing, nonmanufacturing and transportation, communications and public utilities. See *id.* Each group contained from five to thirty classes of property. See *id.* at 557.

59. See *id.* at 557. See generally Auerbach, *supra* note 55, at 1329-30 (explaining that allowing investors to write off assets over shorter periods of time encourages investment). The use of guideline lives replaced the useful life approach, and were on average 30-40% shorter in duration. See Lischer, Jr., *supra* note 3, at 557.

60. See Lischer, Jr., *supra* note 3, at 567 (describing ADR depreciation and Revenue Act of 1971); Auerbach, *supra* note 55, at 1327 n.4 ("The ADR system created various depreciation write-off periods for various classes of depreciable assets."); Cunningham, *supra* note 25, at 763 (generally describing ADR); Brian R. Bassett, Note, *Simon v. Commissioner and Liddle v. Commissioner: Has the Tax Court Been "Fiddling" Around with Depreciation?*, 75 B.U. L. Rev. 837, 844 (1995) (same). Before ERTA was enacted, depreciation was calculated "by determining the useful life of the property, determining the salvage value, and distributing the excess of the original cost over the salvage value for the years the property would be used." Dupuy, *supra* note 31, at 630. The amount the asset is worth at the end of its useful life connotes its salvage value. See *id.* at 630 n.14.

61. See Cunningham, *supra* note 25, at 763. Ironically, a useful life was a prerequisite for the asset to be assigned to a class to determine its useful life. See *id.*; see also Lischer, Jr., *supra* note 3, at 567 ("The major purpose of ADR depreciation was to provide additional leeway in determining the useful life of depreciable property.").

erty.⁶² Thus, an asset with an indeterminable useful life was not eligible for depreciation deductions under ADR.⁶³

C. The Economic Recovery Tax Act

In 1981, Congress enacted the Economic Recovery Tax Act (ERTA), which altered the depreciation scheme, in an effort to further certain policy objectives.⁶⁴ Congress's primary purpose in changing the depreciation scheme was to stimulate economic growth.⁶⁵ Specifically, higher rates of inflation caused the real value of depreciation deductions to decline.⁶⁶ Consequently, this resulted in the diminished profitability of new investments and discouraged businesses from upgrading their equipment and buildings.⁶⁷ Congress's attempt to solve this problem came through the implementation of ACRS, which it considered to be "an effective way of stimulating capital formation, increasing productivity and improving the nation's competitiveness in international trade."⁶⁸ In addition, by enacting ACRS Congress sought to simplify the de-

62. See Dupuy, *supra* note 31, at 630. See also Cunningham, *supra* note 25, at 763 (stating that "the ADR system grouped the property into broad classes of industry assets, and assigned each class a useful life."). Under the ADR, taxpayers had the option to depreciate the asset over a time period 20% shorter or longer than the guideline period. See Auerbach, *supra* note 55, at 1330; Bassett, *supra* note 60, at 844. This option furthered Congress's goal of minimizing taxpayer disputes with the IRS. See Bassett, *supra* note 60, at 844.

63. See Cunningham, *supra* note 25, at 763.

64. See Economic Recovery Tax Act (ERTA), I.R.C. § 168 (1997); see also BORIS I. BITTKER & MARTIN J. McMAHON, JR., FEDERAL INCOME TAXATION OF INDIVIDUALS ¶ 12.1.2 (1988) (noting that new rules "depart[] dramatically" from old rules); Auerbach, *supra* note 55 at 1327 (stating that ERTA created "several significant changes in the tax law that together represented the most substantial cut in corporate and personal income taxes ever."); Dupuy, *supra* note 31, at 630 (observing that "[t]his statute radically overhauled the rules used to determine depreciation."). In furtherance of these policy objectives, a system was created that has "little to do with measuring economic income." BITTKER & McMAHON, JR., *supra*, at ¶ 12.1.2.

65. See Simon, 68 F.3d at 45. ACRS, however, has been criticized as being "very distortionary in its distribution across different assets and sensitive to the rate of inflation." Auerbach, *supra* note 55, at 1350.

66. See S. REP. NO. 97-144, at 47 (1981), *reprinted in* 1981 U.S.C.C.A.N. 105, 152.

67. See *id.*

68. *Id.* The purpose of ACRS is to allow taxpayers to "recover tax free the cost (or other basis) of property exhausted in the process of generating business income." BITTKER & McMAHON, JR., *supra* note 64, at ¶ 12.1.3. However, since ACRS is merely a method of cost allocation, it does not reflect the asset's actual decline in value. See *id.*; see also Polito, *supra* note 42, at 87 (criticizing ACRS as "vastly exagger[at]ing] th[e] anomalous nature of the depreciation allowance."). Additionally, ACRS is said to inch taxation of businesses closer to a consumption tax. See *id.*

preciation rules.⁶⁹ Through ACRS, Congress endeavored to de-emphasize the concept of useful life because it is “inherently uncertain” and its determination results in frequent disagreements between taxpayers and the IRS.⁷⁰

In order to accomplish these objectives, Congress accelerated the depreciation period of assets through ACRS under ERTA.⁷¹ ACRS permits depreciation deductions for “recovery property,” as defined by I.R.C. § 168.⁷² Once an asset is deemed to be “recovery property,” the taxpayer must assign the asset to the proper table to determine the applicable depreciation deduction.⁷³ Finally, the

69. See *Simon*, 68 F.3d at 45; see also Dupuy, *supra* note 31, at 630-31 (stating that “Congress found that the former system of determining useful life was ‘complex’ and ‘inherently uncertain,’ and led to frequent disagreements between taxpayers and the Service.”); Cunningham, *supra* note 25, at 763 (noting that Congress enacted ERTA to simplify depreciation system).

70. See S. REP. NO. 97-144 (“The committee believes that a new capital cost recovery system should be structured which de-emphasizes the concept of useful life, minimizes the number of elections and exceptions, and so is easier to comply with and administer”); see also Bassett, *supra* note 60, at 843 (noting that “the useful-life issue proved to be a fruitful source of litigation.”). Congress de-emphasized the useful life concept by replacing guideline lives with recovery periods. See Dupuy, *supra* note 31, at 631. The result was a simplification of depreciation rules, since it was now unnecessary to determine an asset’s useful life to determine its recovery period. See *id.* But see Brief for the Appellees at 16, *Simon v. Commissioner*, 68 F.3d 41 (2d Cir. 1995) (No. 94-4237) (stating that “the former need for a determination of ‘useful life’ had been erased.”).

71. See *Simon*, 68 F.3d at 45. ACRS applies only to tangible assets placed in service after 1980. See Auerbach, *supra* note 55, at 1334. In a nutshell, under ACRS “the cost of tangible property is generally recovered over an arbitrary period specified by statute for each of several broad classes of property.” BITTKER & MCMAHON, JR., *supra* note 64, at ¶ 12.1.2. “Anti-churning” rules prevent a taxpayer from taking ACRS deductions on property placed in service prior to 1981. See Auerbach, *supra* note 55, at 1334.

ACRS uses a combination of depreciation methods by “mimic[ing] the use of 150% declining balance with a switch-over to straight-line in the later years.” Auerbach, *supra* note 55, at 1332. Furthermore, taxpayers may opt to elect the straight-line over depreciated method instead of ACRS, but this election is made on a class-by-class basis. See *id.* at 1333 & n.50.

72. See Dupuy, *supra* note 31, at 631. Recovery property is defined as “tangible property of a character subject to the allowance for depreciation- (A) used in a trade or business, or (B) held for the production of income.” I.R.C. § 168(c)(1)(A)-(B) (1997). Section 168 is normally read in conjunction with the applicable provisions of § 167, which provides:

There shall be allowed as a depreciation deduction a reasonable allowance for the exhaustion, wear and tear (including a reasonable allowance for obsolescence)- (1) of property used in the trade or business, or (2) of property held for the production of income. In the case of recovery property (within the meaning of section 168), the deduction allowable under section 168 shall be deemed to constitute the reasonable allowance provided by this section

I.R.C. § 167(a)(1)-(2) (1997).

73. See Cunningham, *supra* note 25, at 764. Assets are classified as either 3, 5, 10 or 15 year property. See *id.* (citing I.R.C. § 168(c)(2) (1981)).

taxpayer takes a depreciation allowance based on the applicable percentage found in the tables.⁷⁴

Under ACRS, the cost of an asset is recovered over a predetermined amount of time, unrelated to the useful life of the asset.⁷⁵ The system inflates depreciation deductions in the asset's early years of life.⁷⁶ Consequently, the determinable useful life requirement is eliminated since the asset is not depreciated over its actual useful life.⁷⁷ Alternatively, the legislative history behind ERTA shows a different intent: the House Conference Report does not permit assets without a determinable useful life to be depreciated.⁷⁸

74. See Cunningham, *supra* note 25, at 764 (citing I.R.C. § 168(b)(1)(A)-(C) (1981)). However, since the time period is arbitrary, the decline in the property's value over its useful life generally is less than the total amount of ACRS deductions taken. See BITTKER & MCMAHON, JR., *supra* note 64, at ¶ 12.1.3.

75. See I.R.C. § 168(b) (1981); see also Polito, *supra* note 42, at 97 (noting that "Congress largely abandoned any attempt clearly to reflect income" under new matching scheme). ACRS replaced the ADR's use of guideline lives. See Dupuy, *supra* note 31, at 631 (noting that recovery periods do not estimate actual useful lives). ACRS substituted a new concept: it established definite recovery periods, each having a statutorily mandated time period to recover depreciation. See *id.*

76. See Dupuy, *supra* note 31, at 631. The front-loading of deductions is like "an interest-free loan from the Treasury to the purchaser of the asset, since it allows the purchaser to defer tax payments to later years with no increase in the amount due." Auerbach, *supra* note 55, at 1329. Furthermore, income realized by the asset once it is fully depreciated is computed as if use of the asset is costless. See BITTKER & MCMAHON, JR., *supra* note 64, at ¶ 12.1.4.

77. See Cunningham, *supra* note 25, at 763; see also Auerbach, *supra* note 55, at 1334 (stating that recovery period is not intended to have any close relationship to "useful life" concept). Additionally, the concept of salvage value becomes irrelevant under ACRS. See S. REP. NO. 97-144, at 47 (1981), reprinted in 1981 U.S.C.C.A.N. 105, 152; see also Sheppard, *The Musicians'*, *supra* note 25, at 1263 (noting that although salvage value is irrelevant for ACRS, it is relevant to deterioration in value); Polito, *supra* note 42, at 101 (noting that ACRS' abandonment of salvage value lifted restriction on depreciation deductions to assets that declined in value only).

78. See H.R. CONF. REP. NO. 97-215, at 206 (1981), reprinted in 1981 U.S.C.C.A.N. 281, 296. Specifically, the House Conference Report states:

Under present law, assets used in a trade or business or for the production of income are depreciable if they are subject to wear and tear, decay or decline from natural causes or obsolescence. Assets that do not decline in value on a predictable basis or that do not have a determinable useful life, such as land, goodwill, and stock, are not depreciable.

Id. Note that the last sentence of this specific excerpt from the House Conference Report has been interpreted differently by both the Commissioner and the Simons. Compare Brief for the Appellees at 18-19, *Simon v. Commissioner*, 68 F.3d 41 (2d Cir. 1995) (No. 94-4237) (pointing to this language as support), with Brief for the Appellant at 17-18, *Simon v. Commissioner*, 68 F.3d 41 (2d Cir. 1995) (No. 94-4237) ("the majority's decision cannot be squared with the Conference Committee Report."). See also Polito, *supra* note 42, at 100 (observing that Conference Report is unclear as to which interpretation it enunciates). The Simons' attempt to "explain away" and distinguish this sentence from the violin bows at issue by construing it in the following manner: "the categories referred to are all things that do not in the relevant sense suffer wear and tear and thus neither wear out

B. Common Law Doctrines Requiring Disclosure

Even if a waiver were held to waive the disclosure requirements of the Act, a duty to disclose might arise from common law. Presumably, Congress designed the Act to benefit future student-athletes and the Act was not intended to be a “one-shot” deal for the year the Act was enacted; there must be compliance in each year subsequent to the Act. Therefore, universities obtaining waivers are still required to continue to compile the data specified by the Act. Once the information is known to the university, there will be a duty to disclose whenever the university is in a confidential relationship with a prospective student-athlete. The duty is owed whenever “one party to a transaction justifiably believes the other is looking out for his interests”¹²⁶ Such a confidential relationship can arise well outside of traditional fiduciary relationships.¹²⁷ In the context of athletic recruiting, it might arise when a religiously-affiliated university recruits a coreligionist.¹²⁸ A court could reasonably find that where an institution of higher learning held itself out as a representative of a prospective student-athlete’s church, a prospective student-athlete could justifiably believe the institution was looking out for his or her interests.

Under some circumstances, even a state university may have an affirmative duty to disclose graduation rates once it has compiled them. As noted above, student-athletes and universities are parties to a contract.¹²⁹ While a state actor is not in a confidential relationship with its contractors merely by virtue of the fact it is a state actor,¹³⁰ it may have a duty to disclose beyond that of private parties. For example, some state courts have held that “[w]here resort to the state is the only reasonable avenue for acquiring the informa-

institution incurs little additional burden by providing the information directly. A court would likely infer that the institution failed to provide the information solely because it did not wish the prospective student-athlete to make a rational decision, based on the best available information. Given this motive, a court would feel some compulsion to grant relief.

126. CALAMARI & PERILLO, *supra* note 42, § 9-20, at 369-70.

127. *See, e.g., Roberts v. Sears, Roebuck & Co.*, 573 F.2d 976, 983 (7th Cir. 1978).

128. Nothing in the First Amendment would prevent a court from finding a confidential relationship under these circumstances. “The clause does not allow purely secular statements of fact to be shielded from legal action merely because they are made by officials of a religious organization.” *In Re The Bible Speaks*, 869 F.2d 628, 645 (1st Cir. 1989). Presumably this analysis would extend with equal force to statements of fact which should have been made but were not.

129. *See supra* note 83 for a further discussion on how a party would seek to void a contract.

130. *See Helene Curtis Indus. v. United States*, 312 F.2d 774, 778 (Ct. Cl. 1963).

tion, the state must disclose it, and may not claim as a defense either the contractor's failure to make an independent request or exculpatory language in the contract documents."¹³¹ Thus, a university would have an affirmative duty to offer the information on graduation rates even if the same information were available through a state Freedom of Information Act, so long as there was no other "reasonable avenue" to obtain the information.¹³²

Finally, any university may have a duty to disclose or more specifically, may be guilty of an affirmative misrepresentation, if its graduation rates are published in a manner calculated to make them difficult to discover.¹³³

VI. STRATEGIES TO AVOID LIABILITY

The Act, if ignored, may expose universities with active athletic programs to significant liability. Even if successfully defended, a court case entails both legal fees and adverse publicity. The following suggestions may help universities limit this exposure: 1) have a formal, written, recruiting policy in compliance with the Act. Punitive damages are the largest single source of exposure. Universities with successful athletics programs and a policy of noncompliance will be tempting targets for their assessment. In addition, the punitive damages carrot will make these institutions a popular target for litigation; 2) train athletic recruiters on acceptable recruiting tactics and document their training. Properly trained recruiters will significantly lower exposure. Should a plaintiff be successful, evidence of proper training will make the assessment of punitive damages less likely; 3) include a merger clause in the financial aid statement.¹³⁴ While this will be valueless in defending against a

131. *Morrison-Knudsen Co., Inc. v. Alaska*, 519 P.2d 834, 841 (Alaska 1974).

132. This might occur, for example, when an athletic association has received a waiver for its members by promising to publish graduation rates, but has not yet done so.

133. "Positive action designed to hide the truth or to stymie the other party's investigation is deemed to constitute misfeasance that can result in liability for misrepresentation." CALAMARI & PERILLO, *supra* note 42, § 9-20, at 367. The graduation rates would not be published by individual schools, but rather by "an athletic association or athletic conference." 20 U.S.C. § 1092(e)(6) (Supp. IV 1992). Thus, the university itself would not undertake the actual concealment. It might, however, be possible to impute the athletic association's action to the university on an agency theory, especially if the university was aware of the athletic association's actions. See HAROLD GILL REUSCHLEIN & WILLIAM A. GREGORY, *THE LAW OF AGENCY AND PARTNERSHIP*, § 201, at 305 (2d ed. 1990).

134. For example, "[t]he University and the Student agree that this financial aid statement represents our entire agreement and that any prior agreements or promises, either written or oral, are void."

As a result of this disparity, the viability of the determinable useful life requirement under ERTA is uncertain.⁷⁹

D. Judicial Analysis of Depreciation Deductions

1. Pre-ACRS

Although ACRS was enacted in 1981, it did not apply to assets placed in service before 1981. Accordingly, in these circumstances courts had to apply the old ADR scheme instead. The first case to address this issue after the enactment of ACRS was *Harrah's Club v. United States*.⁸⁰ The issue faced by the court in *Harrah's* was whether a taxpayer may depreciate the cost of antique automobiles displayed at the taxpayer's place of business in order to attract customers.⁸¹ The court held that since the restored vehicles have an unlimited museum life, they are undepreciable.⁸² The court, therefore, rejected the concept of the depreciability of property lacking a useful life.

Two years later, in *Hawkins v. Commissioner*, the Court of Appeals for the Eighth Circuit was faced with a depreciation deduction taken under the ADR for artwork.⁸³ An attorney contended that he was entitled to claim a depreciation deduction for artwork

nor 'depreciate' in any accustomed usage." Brief for the Appellees at 19, *Simon v. Commissioner*, 68 F.3d 41 (2d Cir. 1995) (No. 94-4237). The error in this construction lies in its failure to read the sentence as a whole, which cites those categories merely as examples of the principle that it sets forth. See Reply Brief for the Appellant at 5, *Simon v. Commissioner*, 68 F.3d 41 (2d Cir. 1995) (No. 94-4237) (stating that "the Conference Committee Report specifically refers to property lacking a determinable useful life."). "It is difficult if not impossible to read [Section 168(c)(1)] in light of the conference agreement and believe that the conferees intended property with an indeterminable useful life to be eligible for ACRS." Liddle v. Commissioner, 103 T.C. 285, 304 (1994) (Halpern, J., dissenting).

79. See Polito, *supra* note 42, at 105 (observing that "[i]n the space of two sentences the Conference Committee states both the determinable useful life standard and the wear and tear standard.").

80. 661 F.2d 203 (Ct. Cl. 1981). Harrah's business consisted of operating hotels and gambling casinos. See *id.* Harrah's Automobile Collection was created in order to lure customers to Harrah's hotels and casinos. See *id.*

81. See *id.* The plaintiff in *Harrah's* exhibited approximately 1,000 antique vehicles in like-new condition. See *id.* at 204.

82. See *id.* at 207-09. The taxpayer argued that the automobiles should be depreciable since they lose their novelty after a few years, ceasing to perform their function of attracting customers. See *id.* at 206. The court rebutted this argument, reasoning that because no limit can be put on the vehicles' use as museum objects, the vehicles are useful to the taxpayer indefinitely. See *id.* at 207. Usually, automobiles used for business purposes will be depreciable because they are subject to wear and tear and have a measurable useful life. See Cunningham, *supra* note 25, at 766.

83. 713 F.2d 347 (8th Cir. 1983). The artwork in this case included mosaics, paintings and statutes, purchased for \$126,453.15. See *id.* at 349.

displayed in his law office.⁸⁴ The Eighth Circuit denied the deduction, ruling that the attorney failed to prove that the artwork had a depreciable useful life or salvage value.⁸⁵

In 1989, the Court of Appeals for the Ninth Circuit decided *Browning v. Commissioner*, a case concerning depreciation deductions taken for violins.⁸⁶ Louis Browning was a professional violinist⁸⁷ who purchased antique violins and used them in the course of his trade.⁸⁸ The Ninth Circuit refused to allow Browning to take depreciation deductions on the violins, since Browning failed to show any real decrease in their value.⁸⁹ The court required a useful life to be established before the violins could be depreciated.⁹⁰ Furthermore, the court concluded that violins are more like works of art than a business asset.⁹¹ The court supported this conclusion by reasoning that violins have an extended useful life that cannot be depreciated.⁹²

84. *See id.*

85. *See id.* at 354. In a footnote, the court implied that it would permit depreciation of artwork if the taxpayer could determine the asset's useful life, contrary to the Commissioner's position. *See id.* at 353 n.11.

Under similar facts, the Sixth Circuit denied depreciation deductions for artwork in a physician's office, holding that the doctor provided insufficient evidence to sustain the 10-year useful life estimate that he attributed to the artwork. *See Associated Obstetricians & Gynecologists v. Commissioner*, 762 F.2d 38 (6th Cir. 1985). The court's application of pre-ERTA rules mandated that a determinable useful life be established for the asset, in order to allow the depreciation deduction. *See Dupuy, supra* note 31, at 634. In this case, the physician purchased over 70 paintings, sculptures, pottery and batik prints, at an aggregate cost of \$75,410.32. *See Associated Obstetricians*, 762 F.2d at 39.

86. 890 F.2d 1084 (9th Cir. 1989).

87. *See id.* at 1085. Louis Browning performed in bars, nightclubs and for private engagements. *See id.*

88. *See id.* Browning bought three antique violins: a Ruggeri for \$24,000 in 1978, a Stradivarius for \$130,000 in 1979 and a Gabrielli for \$27,000 in 1981. *See id.* All three violins were certified as authentic. *See id.* at 1085.

89. *See id.* The court relied in part on expert testimony that placed a value of \$225,000-275,000 on the Stradivarius violin. *See id.* at 1086. In *Browning*, it was debatable whether the violins purchased by Browning had in fact suffered any wear and tear while in his possession. *See Sheppard, The Musicians'*, *supra* note 25, at 1262. It was suspected that Browning's motive lied instead in collecting the violins as an investment. *See id.* *See also Dupuy, supra* note 31, at 634 (noting that "the court suspected that the taxpayer was forming a collection of antique violins.").

90. *See Browning*, 890 F.2d at 1086. The court required the satisfaction of a three-prong test in order to allow depreciation of a business asset: (1) cost of property; (2) salvage value; and (3) useful life. *See id.* at 1086 (citing 26 C.F.R. § 1.167(a)-1).

91. *See id.* at 1086-87 (noting that "the violins have a value independent of their tonal qualities and that value makes the violins more like pieces of art.").

92. *See id.* (explaining that physical condition of artwork usually does not determine its useful life). The court sustained the Tax Court's opinion that the Brownings failed to prove "that violins which had already survived for over two hundred years had only twelve years remaining in their useful lives." *Id.*

As the preceding decisions illustrate, under the ADR courts agreed that in order for an asset to be depreciable, it needed to have a determinable useful life.⁹³ Whether this requirement remained intact after the implementation of ACRS is not quite so clear, as the next section on post-ACRS case law will demonstrate.

2. *Post-ACRS*

Depreciation deductions taken under ACRS present a problem different from those taken under ADR: the determination of a useful life. Under ACRS, there is disagreement as to whether ACRS eliminated ADR's requirement of a useful life as a prerequisite to permitting a depreciation deduction. This dilemma arose in *Clinger v. Commissioner*,⁹⁴ when a professional artist claimed a depreciation deduction for an oil painting. The artist purchased the painting for three reasons: to establish credibility, facilitate marketing and for use as a subject of study, to perfect her artistic abilities.⁹⁵ The court denied Clinger the deduction because she did not meet her burden of proof: she failed to establish the useful life of the oil painting, therefore it was not depreciable recovery property under § 168.⁹⁶ Thus, the court held that ACRS did not eliminate the determinable useful life requirement for an asset to be depreciable, it only de-emphasized it.⁹⁷

The preceding trend of fourteen years, requiring proof of useful life in order to permit a depreciation deduction, was broken in *Liddle v. Commissioner*.⁹⁸ In *Liddle*, the Court of Appeals for the

93. See Polito, *supra* note 42, at 103 (observing that pre-ACRS case law "is unambiguous in predicating depreciability on the taxpayer's ability to prove that its assets have determinable useful lives."). In addition, this section of case law "sought to mitigate the misstatement of income by compelling taxpayers to estimate salvage values for their assets." *Id.* at 94.

94. 60 T.C.M. (CCH) 598, 1990 Tax Ct. Memo LEXIS 504 (1990). The oil painting was created by Alvin Gittins, a former instructor of the taxpayer and a well-known artist in the area. *See id.* at 598. The painting was purchased from Gittins' estate for \$9,000. *See id.*

95. *See id.*

96. *See id.* The burden of proof fell on Clinger because "the Service's determinations are presumptively correct." Dupuy, *supra* note 31, at 632 (citing *Welch v. Helvering*, 290 U.S. 111 (1933)).

97. *See* Dupuy, *supra* note 31, at 632 (citing *Clinger*, 60 T.C.M. (CCH) at 599); Bassett, *supra* note 60, at 850 (citing *Clinger*, 60 T.C.M. (CCH) at 599). *See generally* Joseph M. Dodge & Deborah A. Geier, *Simon Says: A Liddle Night Music with Those Depreciation Deductions, Please*, 69 TAX NOTES 617, 617 (Oct. 30, 1995) (discussing disagreement among courts as to useful life requirement under ACRS).

98. 65 F.3d 329 (3d. Cir. 1995).

Third Circuit was faced with facts similar to those in *Browning*.⁹⁹ Liddle was a professional musician who purchased a valuable bass violin, to be used as a tool in his trade.¹⁰⁰ Liddle sought a depreciation deduction on the bass violin, even though the instrument increased in value during the period of Liddle's ownership.¹⁰¹ The Court of Appeals for the Third Circuit allowed the depreciation deduction, and provided two reasons in support of its decision.¹⁰² First, the court stated that a determinable useful life is not a necessary prerequisite to taking an ACRS deduction.¹⁰³ Instead, the property only has to be subject to "wear and tear."¹⁰⁴ Additionally, the court held that since Liddle used the bass violin as a tool of his trade and not as a work of art, the bass violin is exempt from the rule that a work of art cannot be depreciated.¹⁰⁵

99. See *id.* at 331. For a discussion of the facts surrounding *Browning*, see *supra* notes 88-90 and accompanying text.

Liddle made a similar claim to *Browning*, that the violin's musical quality deteriorated with use. See *Liddle*, 65 F.3d at 331. Oddly enough, there is evidence to the contrary. One commentator noted that "not only do Stradivarius violins not lose value, but also they get better with playing." Lee A. Sheppard, *Would More Expertise Have Helped in the Violin Cases?*, 70 TAX NOTES 1314 (Mar. 4, 1996) [hereinafter Sheppard, *Violin Cases*]. Physicists at the School of Engineering Systems and Design at London's South Bank University found that wood instruments need to be played continuously in order to maintain an enhanced resonance. See *id.*

100. See *Liddle*, 65 F.3d at 330. According to Liddle's counsel, the violin was purchased for its voice quality. See Telephone Interview with David L. Segal, Attorney for Brian P. Liddle (Jan. 30, 1997). Specifically, Liddle purchased a 17th century Ruggeri violin for \$28,000 in 1984. See *Liddle*, 65 F.3d at 330. However, the purchase was subject to at least a 15-year mortgage. See Telephone Interview with David L. Segal, Attorney for Brian P. Liddle (Jan. 30, 1997). Interestingly enough, the Ruggeri violin was subsequently traded in a like-kind exchange, since the audition committee at the Minnesota Symphony no longer liked the violin's voice. See *id.*

101. See *Liddle*, 65 F.3d at 330. The bass violin appreciated \$10,000 in value from 1984 to 1987, and was traded in 1991 for a Domenico Busan violin appraised at \$65,000. See *id.* at 330-31.

102. See Sheppard, *Violin Cases*, *supra* note 99, at 1314. The appellant argued that permitting depreciation of the antique violin created the anomalous result that an antique violin that "has been used for some 300 years will be depreciable over a 5-year period." Brief for the Appellant at 10, *Liddle v. Commissioner*, 65 F.3d 329 (3d Cir. 1995) (No. 94-7733). See also Lee A. Sheppard, *Violins, Ferraris, and the Music of Class Lives*, 69 TAX NOTES 669, 669 (Nov. 6, 1995) [hereinafter Sheppard, *Ferraris*] (criticizing *Liddle* decision for allowing depreciation deductions where there is no wear and tear).

103. See *Liddle*, 65 F.3d at 332-33. "The entire cost or other basis of eligible property is recovered under ACRS, eliminating the salvage value limitation of prior depreciation law." *Id.* at 333.

104. See *id.* at 334. The phrase "wear and tear" also includes obsolescence or exhaustion. See I.R.C. § 168 (1997).

105. See Dupuy, *supra* note 31, at 638 (noting that "but for the viol's use by the taxpayer as a full-time musician, it would be a nondepreciable work of art."). Works of art are not depreciable because they do not have a determinable useful life. See *id.* at 633 (citing *Hawkins v. Commissioner*, 713 F.2d 347 (8th Cir. 1983)).

IV. NARRATIVE ANALYSIS

A. Majority Opinion

The *Simon* majority stylized its opinion by first setting out the issues that both parties agreed upon, and then addressing the arguments made by each on the points of disagreement.¹⁰⁶ The parties' disagreements stemmed from different readings of the text of the Internal Revenue Code.¹⁰⁷ Further, the parties disagreed on the fundamental nature of depreciation.¹⁰⁸ Finally, the Commission pointed to legislative history to support its position.¹⁰⁹ After finding for the Simons on each of these issues, the court defended its holding by: (1) distinguishing precedent, (2) rebutting the implication of favorable treatment of wasteful investments and (3) stressing the limited scope of its holding.¹¹⁰

The Court of Appeals for the Second Circuit began its analysis by directly stating that the essence of the argument "turns on the interpretation of the ACRS provisions of I.R.C. § 168."¹¹¹ The court noted the one point on which both parties agreed: the phrase "of a character subject to depreciation" in § 168 must be read in light of § 167(a), which permits allowances for "exhaustion, wear and tear, and . . . obsolescence."¹¹² The court addressed the textual argument first, which turned on the parties' differing interpretations of §§ 167 and 168 when read together. The Simons contended that when the two sections are read together, the plain language of the provisions requires only that the bows suffer wear and tear in their

See also Rev. Rul. 68-232, 1968-1 C.B. 79 (explaining that while "actual physical condition of the property may influence the value placed on the object, it will not ordinarily limit or determine the useful life. Accordingly, depreciation of works of art generally is not allowable.").

106. For a discussion of the issue agreed upon by both parties, see *infra* note 112 and accompanying text. For a discussion of the issues argued by the parties, see *infra* notes 113-24 and accompanying text.

107. For a discussion of the textual argument, see *infra* notes 113-16 and accompanying text.

108. For a discussion of the nature of depreciation argument, see *infra* notes 117-21 and accompanying text.

109. For a discussion of the legislative history argument, see *infra* notes 122-24 and accompanying text.

110. For a discussion of the Second Circuit's defense of its holding, see *infra* notes 125-37 and accompanying text.

111. *Simon*, 68 F.3d at 43. The court explained § 168 as "provid[ing] a depreciation deduction for 'recovery property' placed into service after 1980." *Id.* For a further discussion of recovery property, see *supra* notes 72-73 and accompanying text.

112. *Id.* (quoting I.R.C. § 167(a)). For a more complete excerpt of §§ 167 and 168, see *supra* note 72 and accompanying text.

trade, in order to qualify as recovery property.¹¹³ Conversely, the Commissioner argued that such a reading would render portions of the provision superfluous because all property used in a trade is necessarily subject to wear and tear.¹¹⁴ Instead, the Commissioner stated that these portions of the section include the “determinable useful life” requirement.¹¹⁵ The court found for the Simons on the textual argument. It rejected the Commissioner’s superfluous language argument, reasoning that there are tangible items not subject to wear and tear.¹¹⁶

Next, the court analyzed the nature of depreciation argument. The Tax Court found that imposing a useful life requirement would resurrect the disagreements that Congress intended to curtail by enacting ERTA.¹¹⁷ The Second Circuit agreed with this reasoning, rejecting the Commissioner’s depreciation argument since the different design of ACRS does not utilize the useful life concept.¹¹⁸ Furthermore, the court rejected the Commissioner’s contention that requiring useful life for a narrow category of property is in accord with the legislative intent of de-emphasizing useful life.¹¹⁹ Instead, the court stressed that useful life is measured by the particular business’s use of the asset, not by the abstract economic life of the asset in any business.¹²⁰ Additionally, the court added that the notion of useful life does not affect the asset’s eligibility under ACRS: thus, the Commissioner’s position of denying the asset eligibility avoids ERTA’s “explicit rejection of ‘salvage value.’”¹²¹

Finally, the court addressed the Commissioner’s argument that §§ 167 and 168 should be interpreted in light of their legislative history. In particular, the Commissioner relied on the House Con-

113. *See id.*

114. *See id.* at 44. Specifically, the Commissioner contends that such a reading of the two sections makes the phrase “of a character subject to the allowance for depreciation” superfluous. *See id.*

115. *See id.* The determinable useful life requirement is found in 26 C.F.R. § 1.167(a)-1 (1997).

116. *See Simon*, 68 F.3d at 44.

117. *See Simon v. Commissioner*, 103 T.C. 247, 258-59 (1994). “ERTA was enacted partially to address and eliminate the issue that we are faced with today, namely, a disagreement between taxpayers and the Commissioner over the useful lives of assets that were used in Taxpayers’ trade or business.” *Id.*

118. *See Simon*, 68 F.3d at 45.

119. *See id.* Such a narrow category of property would include usable antiques and other business property likely to appreciate in real value. *See id.*

120. *See id.* (citing *Massey Motors, Inc. v. United States*, 364 U.S. 92, 97 (1960)).

121. *Id.* at 45. *See also* Brief for Appellee at 18, *Simon v. Commissioner*, 68 F.3d 41 (2d Cir. 1995) (No. 94-4237) (“No trace was left of the notion that depreciation is allowable generally only for assets for which a ‘useful life’ is determined.”).

ference Report.¹²² The court noted a portion of the House Conference Report which states that, “[a]ssets that do not decline in value on a predictable basis or that do not have a determinable useful life . . . are not depreciable.”¹²³ While the court conceded that this legislative history made it pause, the court concluded that two statements found in legislative history are not enough to trump the statutory language and legislative intent.¹²⁴

In reaching its decision, the court defended its position in several ways.¹²⁵ First, the court noted that its decision did not conflict with the Ninth Circuit’s decision in *Browning*.¹²⁶ In *Browning*, the Ninth Circuit disallowed a professional violinist from taking depreciation deductions on an antique violin.¹²⁷ The court explained that the *Browning* court failed to discuss § 168, ERTA or ACRS in its opinion.¹²⁸ In addition, the *Browning* opinion referred to the salvage value of the violin in question.¹²⁹ The court found this reference erroneous, since salvage value is an obsolete concept under ACRS for recovery property.¹³⁰

Next, the court acknowledged that its holding could give favorable treatment to some wasteful investments.¹³¹ Here, the court outlined the scope of its powers. Specifically, the court determined that it is not its function to draw the line between what is wasteful and what is productive, in light of Congress’s intent to stimulate investment in business property.¹³² The court stated that it was in fact obligated to assure that the Commissioner, in his efforts to maximize revenue, does not thwart Congress’s intent to

122. See *Simon*, 68 F.3d at 46 (citing H.R. CONF. REP. NO. 97-215, at 206 (1981), reprinted in 1981 U.S.C.C.A.N. 296).

123. *Id.*

124. See *id.* The *Simon* court reasoned that the overall legislative history of ERTA “definitively repudiates the scheme of complex depreciation rules.” *Id.* The court concluded that the portions of the House Conference Report relied on by the Commissioner sharply conflicted with this overall intent. See *id.*

125. See *id.*

126. *Browning v. Commissioner*, 890 F.2d 1084, 1085 (9th Cir. 1989). For a discussion of the Ninth Circuit’s opinion in *Browning*, see *supra* notes 86-92 and accompanying text.

127. See *id.*

128. See *Simon*, 68 F.3d at 46.

129. See *id.*

130. See *id.* The Tax Court distinguished *Browning* on the ground that the taxpayer failed to supply credible evidence that the violins were depreciable property. See *id.* at 46 n.6. The Second Circuit did not rely on these grounds, however, in the appeal. See *id.*

131. See *Simon*, 68 F.3d at 46.

132. See *id.*

generate economic growth.¹³³ Furthermore, the court concluded that Congress's goals would be frustrated if taxpayers were leery of the viability of these types of investment incentives through the actions of the Commissioner.¹³⁴

Finally, the court emphasized the limited scope of its holding. The court specifically stated that its ruling is not a "license to hoard and depreciate valuable property that a taxpayer expects to appreciate in real economic value."¹³⁵ Instead, the holding is limited to property placed in service between January 1, 1981 and January 1, 1987 and to the concept of "recovery property."¹³⁶ Furthermore, the court reiterated that the test to be applied is whether the asset will suffer wear and tear, exhaustion or obsolescence in its use by a business.¹³⁷

B. Dissenting Opinion

Senior circuit Judge Oakes attacked the majority opinion, citing the statutory language of § 168, its legislative history and rules of statutory construction. Judge Oakes began by pointing out the majority's failure to acknowledge the textual cross-references to §§ 167, 168(c)(2) and 1245(a)(3) in § 168(c), which extensive case law has interpreted to require that the depreciated property has a determinable useful life.¹³⁸

Next, the dissent criticized the majority's handling of the legislative history. The dissent stressed the fact that the majority conceded that the House Conference Report "means what it says," but nevertheless declined to impute any value to the report.¹³⁹ Further-

133. *See id.*

134. *See id.*

135. *Id.* at 46-47.

136. *See Simon*, 68 F.3d at 46 n.1. This time frame is the result of two events: (1) ACRS depreciation deductions began in 1981, and (2) the concept of "recovery property" was deleted in the Tax Reform Act of 1986. *See id.*

137. *See id.* at 46-47. The court gave the following examples: Even without a determinable useful life requirement, a business that displayed antique automobiles, for example, and kept them under near-ideal, humidity-controlled conditions, would still have difficulty demonstrating the requisite exhaustion, wear and tear, or obsolescence necessary to depreciate the automobiles as recovery property. Nor is valuable artwork purchased as office ornamentation apt to suffer anything more damaging than occasional criticism from the tutored or untutored, and it too would probably fail to qualify as recovery property.

Id. (citations omitted).

138. *See id.* at 47.

139. *See id.* For a discussion of the House Conference Report, see *supra* notes 78-79 and accompanying text.

more, Judge Oakes clarified Congress's intent behind enacting ACRS: to de-emphasize, not destroy the useful life concept.¹⁴⁰

The last issue discussed by the dissent involved the statutory construction analysis by the majority. The dissent argued that the majority's reading of the statute renders portions of it superfluous.¹⁴¹ The dissent supported its conclusion with the observation that all tangible property is subject to some degree of wear and tear, so in effect all tangible property would be depreciable.¹⁴² In addition, the dissent pointed out that the majority's reliance on the elimination of the "salvage value" requirement as changing prior law is misplaced, in light of the revised definition of "recovery property," which supports a determinable useful life requirement.¹⁴³

V. CRITICAL ANALYSIS

Although the *Simon* majority limited the scope of its holding to recovery property, it nevertheless opened the floodgates of depreciation deductions to all tangible property.¹⁴⁴ The dissent essentially predicted this result when it opined that all tangible property is subject to some degree of wear and tear.¹⁴⁵ The majority never consid-

140. See *id.* This opinion is in accordance with the holding in *Clinger v. Commissioner*, 60 T.C.M. (CCH) 598 (1990) (holding ACRS only de-emphasized useful life, did not eliminate it).

141. See *Simon*, 68 F.3d at 48 n.1. Specifically, the dissent contended that the majority's application of § 168's provisions to all tangible property subject to "wear and tear" renders the phrase "of a character subject to the allowance for depreciation" in § 168(c)(1) superfluous. See *id.*

142. See *id.* at 48. See also Tom Herman, *Court Rules Professional Musician May Depreciate Cost of Bass Violin*, WALL ST. J. Sept. 14, 1995 at B12 (noting that such rulings could open doors for depreciation of many items).

143. See *id.*

144. See Sheppard, *The Musicians'*, *supra* note 25, at 1263 ("If active, regular, and routine use are to replace determinable useful life as the touchstone of depreciability, then I believe that the majority has opened a loophole that it is inconceivable Congress intended.") (quoting *Liddle v. Commissioner*, 103 T.C. 285, 305 (1994) (Halpern, J., dissenting)); Polito, *supra* note 42, at 101 (noting that "[p]ressed to its logical extreme, this reasoning leads to the conclusion that any tangible personal property used in a trade or business is recovery property, regardless of exhaustion, wear and tear, or obsolescence.") (emphasis added); Cunningham, *supra* note 25, at 777-78 (predicting depreciation deductions for land devoid of useful life but subject to wear and tear). One commentator went so far as to say that the majority did not read the statute in its analysis, resulting in a decision that was "flat wrong, and dangerously so." See Sheppard, *The Musicians'*, *supra* note 25, at 1259.

145. See *Simon*, 68 F.3d at 48 (Oakes, J., dissenting); see also Sheppard, *The Musicians'*, *supra* note 25, at 1263 (noting that "[t]he premise of tax depreciation is that wear and tear or obsolescence is coincident with a loss in value."). For a discussion of the dissenting opinion in *Simon*, see *supra* notes 138-43 and accompanying text.

ered that perhaps the issue at hand was the exception and not the rule, due to the unique role of the tangible property involved.¹⁴⁶ Consequently, the court did not so limit its holding to the facts of that particular case.

The crux of the error in the majority's analysis turns on its assumption that Congress eliminated all prior law interpreting § 167(a) when it enacted ACRS.¹⁴⁷ Clearly, Congress intended to refer to the current method under the law to determine what property was eligible for depreciation under ACRS.¹⁴⁸ Consequently, "[i]t should not be necessary to go to the legislative history to decipher something as seemingly straightforward as the definition of what is depreciable."¹⁴⁹

Essentially, the Simons' contention boils down to interpreting § 168 as making tangible property used in a trade or business that suffers wear and tear depreciable *per se*, regardless of whether the

146. See Brief for the Appellant at 20, *Simon v. Commissioner*, 68 F.3d 41 (2d Cir. 1995) (No. 94-4237) (noting that "[t]he issue in this case affects only a small category of assets such as antiques, works of art or other assets that tend to appreciate in value with the passage of time."); see also Polito, *supra* note 42, at 106 n.73 (indicating that Congress was unconcerned about creating a "few 'mistaken' subsidies" in effectuating goals under ACRS).

147. See Sheppard, *The Musicians'*, *supra* note 25, at 1261; see also Brief for Appellant at 6, *Simon v. Commissioner*, 68 F.3d 41 (2d Cir. 1995) (No. 94-4237) ("[U]nder Section 167, the courts of appeals consistently denied depreciation deductions for property such as antique violins and artworks on the ground that these items lacked determinable useful lives."); Sheppard, *Ferraris*, *supra* note 102, at 671 ("According to the Second and Third Circuits, section 167(a) and its interpretations simply disappeared when Congress enacted ACRS; Congress must have forgotten to repeal it."). In fact, Congress did not change the rules under § 167 pertinent to the eligibility of depreciation for antique musical instruments when it enacted ACRS. See Sheppard, *The Musicians'*, *supra* note 25, at 1261. For the relevant text of § 167(a), see *supra* note 72.

148. See Sheppard, *Ferraris*, *supra* note 102, at 670. It is evident that Congress intended to refer to current law, since the Conference report states that "eligible property includes depreciable property," and then immediately added that "[u]nder the House bill, most tangible depreciable property (real and personal) is covered by the accelerated cost recovery system." *Id.* (quoting S. REP. NO. 97-144, at 48 (1981), and H.R. CONF. REP. NO. 97-215, at 206 (1981)); see also Cunningham, *supra* note 25, at 778 ("Congress has never shifted depreciation policy before without providing clear language indicating the change.") (emphasis added).

Further support for this contention is found in the Blue Book. See Sheppard, *The Musicians'*, *supra* note 25, at 1261 (stating that "[t]he Act does not change any determination under prior law as to whether property is tangible or intangible or depreciable or nondepreciable.") (quoting Joint Committee on Taxation General Explanation of ERTA, 77 (J. Comm. Print 1981)). A recent Seventh Circuit decision lends further credence to this conclusion, through its conclusion that "prior administrative determinations carried over to ACRS." Sheppard, *Ferraris*, *supra* note 147, at 670 (citing *Walgreen Co. v. Commissioner*, 68 F.3d 1006 (7th Cir. 1995)).

149. Sheppard, *The Musicians'*, *supra* note 25, at 1261.

property is depreciable under § 167.¹⁵⁰ This interpretation is inconsistent with the statutory language, which requires the property to be “of a character subject to the allowance for depreciation.”¹⁵¹ In order to ascertain such, it is necessary to look to the requirements imposed by § 167.¹⁵² Therefore, “in enacting Section 168, Congress did not make depreciable any property that previously was nondepreciable under Section 167, but, rather, only shortened the periods for depreciating property otherwise eligible for the reasonable allowance for depreciation provided by Section 167(a).”¹⁵³

Furthermore, the majority’s holding undermines Congress’s intent behind ACRS, to simplify depreciation rules in order to reduce disagreements between taxpayers and the IRS over uncertain concepts.¹⁵⁴ Specifically, the majority held that the assets are depreciable if they are subject to exhaustion, wear and tear or obsolescence.¹⁵⁵ Nowhere in the majority’s opinion, however, did they explain precisely what “wear and tear” is.¹⁵⁶ To what degree does

150. See Brief for the Appellant at 11, *Simon v. Commissioner*, 68 F.3d 41 (2d Cir. 1995) (No. 94-4237).

151. I.R.C. § 168(c)(1) (1997); see also Brief for the Appellant at 15, *Simon v. Commissioner*, 68 F.3d 41 (2d Cir. 1995) (No. 94-4237) (noting that Congress would not have included this phrase in statute if it intended statute to apply to “all tangible property used in a trade or business that is subject to some wear and tear.”); Reply Brief for the Appellant at 3, *Simon v. Commissioner*, 68 F.3d 41 (2d Cir. 1995) (No. 94-4237) (“property that does not have a determinable useful life is not property of a character subject to the allowance for depreciation under Section 167 irrespective of whether it is subject to wear and tear.”). The appellant in *Liddle* criticized the Tax Court’s decision as “allow[ing] what it viewed to be the ‘implicit’ policy of Section 168 to override the *explicit* statutory requirement.” Reply Brief for the Appellant at 8, *Liddle v. Commissioner*, 65 F.3d 329 (3d Cir. 1995) (No. 94-7733).

152. See Brief for the Appellant at 15, *Simon v. Commissioner*, 68 F.3d 41 (2d Cir. 1995) (No. 94-4237) (“Congress *conditioned* eligibility for ACRS on satisfaction of the *threshold* standard for depreciability under Section 167.”).

153. *Id.* at 16. The Tax Court majority conceded that the antique violin bows needed a determinable useful life in order to be depreciable under § 167. See *id.*

154. See *Simon*, 68 F.3d at 45. But see Polito, *supra* note 42, at 106 (opining that continuing requirement of determinable useful life works contrary to ACRS simplification objective). For a further discussion of the purpose of ACRS, see *supra* notes 64-70 and accompanying text.

155. See *Simon*, 68 F.3d at 46-47. But see Brief for the Appellant at 5, *Simon v. Commissioner*, 68 F.3d 41 (2d Cir. 1995) (No. 94-4237) (“the question whether a tangible asset used in a trade or business is subject to wear and tear is merely a starting point and not the final determinant of whether property is depreciable . . .”).

156. See *Simon*, 68 F.3d at 46. Although some examples of wear and tear on a violin bow were discussed in the Tax Court decision, neither the Tax Court nor the Second Circuit created a “floor” of the minimum amount of “wear and tear” required in order for an asset to be eligible for a depreciation deduction. For a discussion of the examples of wear and tear that are evidenced on a violin bow, see *supra* note 25 and accompanying text.

an asset need to be “worn and torn” before it is eligible for a depreciation deduction? Does a mere hairline scratch on the stick suffice?¹⁵⁷ Interpretation of the uncertain concept “wear and tear” will inevitably lead to further disagreements between taxpayers and the IRS, a result that Congress expressly intended to eliminate through the effectuation of ACRS.¹⁵⁸

Property used in a trade or business that is subject to wear and tear may nonetheless be nondepreciable if it does not have a determinable useful life or does not decline in value predictably.¹⁵⁹ The antique Tourte violin bows purchased by the Simons satisfy both criteria for nondepreciability. Their value as collectibles increases over time and their value does not decline predictably,¹⁶⁰ since the amount of care given to the violin bows during their use is the sole factor that effects the length of their playing life.¹⁶¹ Therefore, the Second Circuit’s holding undercuts the basic premise behind depreciation, to compensate the taxpayer for the declining value of an investment, because it endorses depreciating assets with unlimited useful lives.¹⁶²

157. See Brief for the Appellant at 15, *Simon v. Commissioner*, 68 F.3d 41 (2d Cir. 1995) (No. 94-4237) (“all tangible property used in a trade or business necessarily is subject to some wear and tear . . .”).

158. For a discussion of Congress’s policy objectives behind ACRS, see *supra* notes 64-70 and accompanying text.

159. See Kahn, *supra* note 38, at 14 n.53 (“[n]ot all assets have fixed useful lives, and therefore not all assets are depreciable.”). But see Polito, *supra* note 42, at 97 (observing that through ACRS, “Congress abandoned the one measure designed to prevent the depreciation of increasing value assets.”).

160. See Sheppard, *The Musicians’*, *supra* note 25 at 1262. Actually, the bows each appreciated in value by \$10,000 during their ownership. See *id.* But see Brief for the Appellees at 6, *Simon v. Commissioner*, 68 F.3d 41 (2d Cir. 1995) (No. 94-4237) (reiterating Tax Court ruling that “[i]t makes no difference . . . that the bows have appreciated in value and will probably have ‘value as collectibles’ even after they are ‘played out.’”).

161. See Sheppard, *The Musicians’*, *supra* note 25 at 1261. In this case, the Simons could not predict the playing life of their violin bows when used regularly and carefully maintained. See *id.*

162. See Cunningham, *supra* note 25, at 754 (noting that premise behind depreciation is that all machinery is marching toward a junk heap); Kahn, *supra* note 38, at 14 n.53 (“the shareholder’s investment is treated as continuing in perpetuity, and the shareholder can recover his cost only by selling the share or by having it redeemed by the corporation.”); Bittker & McMahon, Jr., *supra* note 64, ¶ 12.4.8 (“Depreciation and ACRS deductions are also denied to assets that are not adversely affected by the passage of time or by use in the taxpayer’s business . . . since their value on retirement from use is likely to equal or exceed the taxpayer’s original cost or other basis.”).

VI. IMPACT

It is likely that the split amongst the circuits on whether an asset needs a useful life in order to be depreciable will not be resolved anytime in the near future.¹⁶³ One path for the resolution of this issue is for the Commissioner to petition for certiorari in order to reconcile the split circuits.¹⁶⁴ Another solution is for Congress to repeal or clarify the statute through a substantive change in the actual wording or by revising the treasury regulations.¹⁶⁵ Or perhaps, the musical instruments could be bifurcated into two components: one practical, the other aesthetic.¹⁶⁶

Although the future implications of the *Simon* decision are unknown at this time, some commentators fear that it will create a "double benefit" to owners of valuable antique instruments.¹⁶⁷ An-

163. See Dodge & Geier, *supra* note 97, at 617 (noting that circuit split exists if current law is unchanged from pre-1981 law on depreciability issue). Furthermore, the IRS has taken a "no acquiescence" stance on this issue. See Telephone Interview with David L. Segal, Attorney for Liddle in *Liddle v. Commissioner*, 65 F.3d 329 (3d. Cir. 1995) (Jan. 30, 1997). Apparently, the union to which the Simons belonged lacks confidence in the stability of these decisions: it refused to pay the Simons' legal fees because in their eyes, the Simons won nothing. See *id.* For a discussion of the circuit split on this issue, see *supra* note 9 and accompanying text.

164. See Sheppard, *Ferraris*, *supra* note 102, at 672 (suggesting argument "that there is a conflict among the circuits as to just how much of section 167(a) and administrative guidance promulgated under it Congress re-enacted when it enacted ACRS," for Supreme Court to grant certiorari).

165. See Polito, *supra* note 42, at 107 n.77 (suggesting that "it would be possible to amend section 168 to limit ACRS recovery to assets with useful lives within some maximum range."). In Judge Ruwe's concurring opinion in the Tax Court's decision in *Simon*, he stated that those who object to the holding should complain to Congress instead of the court, since the anomalous result here is a small price to pay in order to effectuate Congress's greater goal of simplifying the tax code. See Sheppard, *The Musicians'*, *supra* note 25, at 1260; see also Cunningham, *supra* note 25, at 777 (noting that "[b]oth the statutory language and the legislative history are ambiguous."); Polito, *supra* note 42, at 101 (observing that "[t]he *Simon* and *Liddle* cases demonstrate that the courts cannot fully reconcile all of Congress's conflicting statements . . . [and] the statutory language neither justifies nor refutes" either court's interpretation of such language). For a further discussion of the Tax Court's decision in *Simon*, see *supra* notes 33-36 and accompanying text.

166. See *Simon*, 103 T.C. at 281 (Gerber, J., dissenting) (advocating bifurcated approach). Under the bifurcation approach, the only basis eligible for depreciation would be the basis attributable to the practical component. See Sheppard, *The Musicians'*, *supra* note 25, at 1260. The bifurcation solution, opined by Judge Gerber's dissenting opinion in the Tax Court decision, has been subject to much skepticism. See *id.* See also *Simon*, 103 T.C. at 284 (Halpern, J., dissenting) (questioning wisdom of bifurcation approach); *id.* at 168 (Beghe, J., concurring) (criticizing bifurcation approach as inadministrable); Sheppard, *The Musicians'*, *supra* note 25, at 1264 (criticizing bifurcation approach as inadministrable, although perhaps theoretically sound). For further discussion of Judge Gerber's dissent in the Tax Court decision, see *supra* note 35 and accompanying text.

167. See Sheppard, *The Musicians'*, *supra* note 25, at 1261. A "double benefit" would accrue to the owners since the instruments would be depreciated now, cre-

other concern encompasses the scope of the decision. It has been suggested that the IRS is not really concerned with musicians: instead, they are concerned with how far the depreciability of antique objects will go.¹⁶⁸ Until there is a clear basis for the courts to decide the issue, musicians will continue to fiddle around their tax liability by orchestrating a new ensemble of deductions.¹⁶⁹

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ating the initial benefit, and then the value of future depreciation would be capitalized into the selling price, constituting the second benefit, resulting in a "double benefit." *See id.*

168. *See* Herman, *supra* note 142, at B12 (suggesting antique office furniture as example); *see also* Brief for the Appellant at 6-7, *Liddle v. Commissioner*, 65 F.3d 329 (3d Cir. 1995) (No. 94-7733) ("the [Tax Court] majority's decision provided wealthy taxpayers with an incentive to stuff their offices with valuable, antique furniture to take advantage of the accelerated depreciation periods provided by Section 168.").

169. *See* Brief for the Appellees at 7, *Simon v. Commissioner*, 68 F.3d 41 (2d Cir. 1995) (No. 94-4237) (noting Chief Judge Hamblen's dissent in Tax Court decision, opining that "the majority creat[ed] an unsuitable 'tax shelter for musicians.'").