

Landfill Closure Costs: U.S. Tax Court Addresses Section 468 Internal Revenue Code Deduction Issue



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07/17/2017

The United States Tax Court (“TC”) in a July 11th opinion addressed whether the owners of a landfill could deduct clean-up costs (i.e., closure costs) under Internal Revenue Code (“IRC”) Section 468. See *Gregory v. Commissioner of Internal Revenue*, 149 T.C. No. 2.

The key question was whether a cash-method taxpayer is included within the term “taxpayer” in Section 468.

Bob and Kay Gregory (collectively “Petitioners”) incorporated a waste management business in Texas in 1988 (Texas Disposal Systems Landfill, Inc. [“TDSL”). The TDSL operation included a solid waste disposal facility (i.e., a “landfill”).

The landfill is described as including 730 acres outside of Creedmoor, Texas (cited as the State of Texas “first fully integrated-service landfill”). The activities included recovery of resources from its solid waste disposal, compost production and recycling. Between two and three thousand tons of solid waste was processed daily.

The aspect of the landfill’s operation which triggered the IRC issue involves the closure requirements imposed by the Texas Commission of Environmental Quality.

Landfills, incinerators and other facilities that manage various types of wastes are often required to demonstrate their ability to finance and/or ensure proper closure of the facility at the end of its life. In other words, has the facility operator planned for and maintained the ability to incur certain costs to ensure the operation as permanently closed imposes no threat to human health and environment? Various federal and state environmental regulations impose such requirements on specific types of facilities. The Texas closure requirements imposed upon the TDSL are an example of such requirements.

Section 468(a)(1) of the IRC provides:

[I]f a taxpayer elects the application of this section with respect to any mining or solid-waste disposal property, the amount of any deduction for qualified reclamation or closing costs for any taxable years in which such election applies shall equal a current reclamation of closing costs allocable to that year.

Upon the advice of an accountant, TDSL in 1996 first deducted closure costs under Section 468. Various amounts were deducted on its 2008 and 2009 tax returns. As the TC opinion notes:

. . . TDSL hadn’t actually paid those clean-up costs yet – it simply estimated the costs; and it also hadn’t charged the estimated costs against its letter of credit yet either. TDSL also did not just make the numbers up – it hired a professional engineering service to estimate the correct amount.

The Internal Revenue Service Commissioner sent the petitioners Notice of Deficiencies for their 2008 and 2009 tax years disallowing the Section 468 deductions. The basis for the disallowance was that TDSL is a cash-method taxpayer. The Commissioner concluded that a taxpayer in regards to Section 468(a) was a taxpayer using the accrual method (as opposed to the cash method).

TDSL had always utilized the cash method for tax-accounting purposes. The Petitioners argued on appeal that the term “taxpayer” in Section 468 includes all taxpayers (regardless of what method of accounting they utilize).

The TC characterized this question as “novel.” It undertook a detailed review of the text of Section 468, along with its legislative history and policy. After concluding its review, it stated:

Taxpayers like TDSL must comply with numerous environmental-protection laws at the federal, state, and local levels. These costs can be large, and they continue after a landfill, mine, or nuclear-power plant stops earning income. Section 468 lessens the burden of compliance by helping to match income and expenses better in an era where businesses that are messy to run must clean up after themselves and maintain proof that they have the means to do so.

The TC concluded that the term “taxpayer” in Section 468 includes cash-method taxpayers (like TDSL). It noted that Section 468 does not define the term. Therefore, the Court held that the general definition under Section 7701(a)(14) applies. TDSL was therefore deemed eligible to currently deduct its estimated clean-up costs under Section 468.

[A copy of the decision can be downloaded here.](#)