CHAPTER 8007
DEPARTMENT OF REVENUE
INCOME TAX DIVISION
ACCOUNTING METHODS; TAXABLE YEAR

8007.0100 ACCOUNTING METHODS.

Except as specifically provided to the contrary by this act, net income and taxable net income shall be computed in accordance with the method of accounting regularly employed in keeping the taxpayer's books. Methods of accounting which are employed as standard for the kind of income-producing activities in which the taxpayer is engaged, will ordinarily be regarded as clearly reflecting income. However, an accounting system which does not treat all items of gross income and all deductions with reasonable consistency, will not be regarded as clearly reflecting income. In such cases the computation shall be made in accordance with a method which, in the opinion of the commissioner, clearly and fairly reflects income taxable under this act. All items of gross income shall be included in the gross income of the taxable year in which received by a taxpayer, unless another method of accounting will more clearly reflect taxable income.

Statutory Authority: *MS s 290.52*

8007.0200 CHANGE IN ACCOUNTING METHODS.

The taxpayer must secure permission from the commissioner to change his method of accounting or in reporting income and deductions. Such application must be filed within 90 days after the beginning of the taxable year to be covered by the return. A statement must be attached to the application setting forth in detail the variation in treatment of classes of items on the old and new basis. A change in the method of accounting or basis of reporting income and deductions means any change in the treatment of items of income and deductions such as change from cash receipts and disbursements basis to the accrual basis or vice versa; a change in the method of inventory valuations; or a change permitted by the commissioner involving any other specialized method of accounting for income and deductions except bad debts, the treatment of which is set forth in 2009 (6)-5 and parts 8009.2100 to 8009.2700.

For adjustments which are required when a change is made in an accounting method, see Minnesota Statutes, section 290.07, subdivision 3.

Statutory Authority: *MS s 290.52*

NOTE: Regulation 2009 (6)-5 has been repealed.

8007.0300 RESTORATION OF AMOUNTS RECEIVED OR ACCRUED UNDER CLAIM OF RIGHT.

Subpart 1. **In general.** If, during the taxable year, the taxpayer is entitled under other provisions of Minnesota Statutes, chapter 290 to a deduction of more than $3,000 because of the restoration to another of an item which was included in the taxpayer's gross income for a prior taxable year (or years) under a claim of right, the tax imposed by Minnesota Statutes, chapter 290 for the taxable year shall be the tax provided in subpart 2.

For the purpose of this part "income included under a claim of right" means an item included in gross income because it appeared from all the facts available in the year of inclusion that the taxpayer had an unrestricted right to such item, and "restoration to another" means a restoration resulting because it was established after the close of such prior taxable year (or years) that the taxpayer did not have an unrestricted right to such item (or portion thereof).

For purposes of determining whether the amount of a deduction described in Minnesota Statutes, section 290.07, subdivision 4 exceeds $3,000 for the taxable year, there shall be taken into account the aggregate of all such deductions with respect to each item of income (described in Minnesota Statutes, section 290.07, subdivision 4 of the same class).

Subp. 2. **Determination of tax.** Under the circumstances described in subpart 1, the tax imposed by Minnesota Statutes, chapter 290 for the taxable year shall be the lesser of:

A. the tax for the taxable year computed under Minnesota Statutes, section 290.07, subdivision 4 that is, with the deduction taken into account; or

B. the tax for the taxable year computed without taking such deduction into account, minus the decrease in tax under Minnesota Statutes, chapter 290 for the prior taxable year (or years) which would result solely from the exclusion from gross income of all or that portion of the income included under a claim of right to which the deduction is attributable.

For the purpose of this subpart, the amount of the decrease in tax is not limited to the amount of the tax for the taxable year. See item A where the decrease in tax for the prior taxable year (or years) exceeds the tax for the taxable year.

If the taxpayer computes his tax for the taxable year under item B, the amount of the restoration shall not be taken into account in computing taxable income or loss for the taxable year, including the computation of any net operating loss carryback or carryover or any capital loss carryover.

If the tax determined under item A is the same as the tax determined under item B, the tax imposed for the taxable year under Minnesota Statutes, chapter 290 shall be the tax determined under item A, and this part shall not otherwise apply.

Subp. 3. **Application to deductions which are capital in nature.** Minnesota Statutes, section 290.07, subdivision 4 and this part shall also apply to a deduction which is capital in nature otherwise allowable in the taxable year. If the deduction otherwise allowable is capital in nature, the determination of whether the taxpayer is entitled to the benefits of Minnesota Statutes, section 290.07, subdivision 4 and this part shall be made without regard to the net capital loss limitation imposed by Minnesota Statutes, section 290.16, subdivision 5. For example, if a taxpayer restores $4,000 in the taxable year and such amount is a long-term capital loss, the taxpayer will, nevertheless, be considered to have met the $3,000 deduction requirement for purposes of applying this part, although the full amount of the loss might not be allowable as a deduction for the taxable year. However, if the tax for the taxable year is computed with the deduction taken into account, the deduction allowable will be subject to the limitation on capital losses provided in Minnesota Statutes, section 290.16, subdivision 5 and the capital loss carryover provided in Minnesota Statutes, section 290.16, subdivision 6.

Subp. 4. **Determination of decrease in tax for prior taxable years.** The prior taxable year (or years) referred to in subpart 2 is the year (or years) in which the item to which the deduction is attributable was included in gross income under a claim of right and, in addition, any other prior taxable year (or years) the tax for which will be affected by the exclusion from gross income in such prior taxable year (or years) of such income.

A. The amount to be excluded from gross income for the prior taxable year (or years) in determining the decrease in tax under subpart 2, item B, shall be the amount restored in the taxable year, but shall not exceed the amount included in gross income in the prior taxable year (or years) under the claim of right to which the deduction for the restoration is attributable, and shall be adjusted as provided in item B.

B. If the amount included in gross income for the prior taxable year (or years) under the claim of right in question was reduced in such year (or years) by a deduction allowed under Minnesota Statutes, section 290.16, subdivision 4 then the amount determined under item A to be excluded from gross income for such year (or years) shall be reduced in the same proportion that the amount included in gross income under a claim of right was reduced.

C. The determination of the amount of the exclusion from gross income of the prior taxable year shall be made without regard to the capital loss limitation contained in Minnesota Statutes, section 290.16, subdivision 5 applicable in computing taxable income for the current taxable year. The amount of the exclusion from gross income in a prior taxable year (or years) shall not exceed the amount which would, but for the application of Minnesota Statutes, section 290.16, subdivision 5, be allowable as a deduction in the taxable year of restoration.

D. The rule provided in item C may be illustrated as follows: For the taxable year 1957, an individual taxpayer had long-term capital gains of $50,000 and long-term capital losses of $10,000, a net long-term gain of $40,000. He also had other income of $5,000. In 1961 taxpayer restored the $50,000 of long-term gain. He had no capital gains or losses in 1961 but had other income of $5,000. If his tax liability for 1961, the taxable year of restoration, is computed by taking the deduction into account, the taxpayer would be entitled to a deduction under Minnesota Statutes, section 290.16, subdivision 5 of only $1,000 on account of the capital loss. However, if the taxpayer computes his tax under subpart 2, item B, it is necessary to determine the decrease in tax for 1957. In such a determination, $50,000 is to be excluded from gross income for that year, resulting in a net capital loss for that year of $10,000, and a capital loss deduction of $1,000 under Minnesota Statutes, section 290.16, subdivision 5 with carryover privileges. The difference between the tax previously determined and the tax as recomputed after such exclusion for the years affected will be the amount of the decrease.

E. If the deduction otherwise allowable for the taxable year relates to income included in gross income under a claim of right in more than one prior taxable year and the amount attributable to each such prior taxable year cannot be readily identified, then the portion attributable to each such prior taxable year shall be that portion of the deduction otherwise allowable for the taxable year which the amount of the income included under the claim of right in question for the prior taxable year bears to the total of all such income included under the claim of right for all such prior taxable years.

The rule provided in this item may be illustrated as follows: Under a claim of right, A included in his gross income over a period of three taxable years an aggregate of $9,000 for services to a certain employer, in amounts as follows: $2,000 for taxable year 1952, $4,000 for taxable year 1953, and $3,000 for taxable year 1954. In 1955 it is established that A must restore $6,750 of these amounts to his employer, and that A is entitled to a deduction of this amount in the taxable year 1955. The amount of the deduction attributable to each of the prior taxable years cannot be identified. Accordingly, the amount of the deduction attributable to each prior taxable year is:

$$1952 \text{ -- } \$6{,}750 \text{ X } \frac{\$2{,}000}{\$9{,}000} = \$1{,}500$$

$$1953 \text{ -- } \$6{,}750 \text{ X } \frac{\$4{,}000}{\$9{,}000} = \$3{,}000$$

$$1954 \text{ -- } \$6{,}750 \text{ X } \frac{\$3{,}000}{\$9{,}000} = \$2{,}250$$

F. In computing the amount of decrease in tax for a prior taxable year (or years) resulting from the exclusion from gross income of the income included under a claim of right, there must first be ascertained the amount of tax previously determined for the taxpayer for such prior taxable year (or years). The tax previously determined shall be the sum of the amounts shown by the taxpayer on his return or returns, plus any amounts which have been previously assessed (or collected without assessment) as deficiencies or which appropriately should be assessed or collected, reduced by the amount of any refunds or credits which have previously been made or which appropriately should be made. After the tax previously determined has been ascertained, a recomputation must then be made to determine the decrease in tax, if any, resulting from the exclusion from gross income of all or that portion of the income included under a claim of right to which the deduction otherwise allowable in the taxable year is attributable.

No item other than the exclusion of the income previously included under a claim of right shall be considered in computing the amount of decrease in tax if reconsideration of such other item is prevented by the operation of any provision of the income tax laws or any other rule of law. However, if the amounts of other items in the return are dependent upon the amount of adjusted gross income, taxable income, or net income (such as charitable contributions, foreign tax credit, deductions for depletion, and net operating loss), appropriate adjustment shall be made as part of the computation of the decrease in tax. For the purpose of determining the decrease in tax for the prior taxable year (or years) which would result from the exclusion from gross income of the item included under a claim of right, the exclusion of such item shall be given effect not only in the prior taxable year in which it was included in gross income but in all other prior taxable years affected by the inclusion of the item (for example, prior taxable years affected by a net operating loss carryback or carryover or capital loss carryover).

The rules provided in this item may be illustrated as follows:

Example 1. For the taxable year 1954, a corporation has taxable income of $35,000, on which it paid a tax of $2,000. Included in gross income for the year was $20,000 received under a claim of right as royalties. In 1957, the corporation is required to return $10,000 of the royalties. It otherwise has taxable income in 1957 of $5,000, so that without the application of Minnesota Statutes, section 290.07, subdivision 4 it has a net operating loss of $5,000 in that year.

Facts also come to light in 1957 which entitle the corporation to an additional deduction of $5,000 for 1954. When a computation is made under subpart 2, item A, the corporation has no tax for the taxable year 1957. When a computation is made under subpart 2, item B, the tax for 1957, without taking the restoration into account, is $365, based on a taxable income of $5,000. The decrease in tax for 1954 is computed as follows:

Tax shown on return for 1954		$ 2,000
Taxable income for 1954 upon which tax shown on return was based		35,000
Less: Additional deduction (on account of which credit or refund could be made)		5,000
Total		30,000
Tax on $30,000 (adjusted taxable income for 1954		1,715
Taxable income for 1954, as adjusted	$30,000	
Less exclusion of amount restored	10,000	
Taxable income for 1954 by applying subpart 2, item B	20,000	
Tax on $20,000		1,145
Decrease in tax for 1954 by applying subpart 2, item B		570
Tax for 1957 without taking the restoration into account		365
Amount by which decrease exceeds the tax for 1957 computed without taking restoration into account		205

The $205 is treated as having been paid on the last day prescribed by law for the payment of the tax for 1957 and is available as a refund. In addition the taxpayer has made an overpayment of $285 ($2,000 less $1,715) for 1954 because of the additional deduction of $5,000.

Example 2. Assume the same facts as in example 1 except that, instead of the corporation being entitled to an additional deduction of $5,000 for 1954, it is determined that the corporation failed to include an item of $5,000 in gross income for that year. The decrease in tax for 1954 is computed as follows:

Tax shown on return for 1954		$ 2,000
Taxable income for 1954 upon which tax shown on return was based		35,000
Plus: Additional income (on account of which deficiency assessment could be made)		5,000
Total		40,000
Tax on $40,000 (adjusted taxable income for 1954)		2,285
Tax on $40,000 (adjusted taxable income for 1954)		2,285
Taxable income for 1954 as adjusted	$40,000	
Less exclusion of amount restored	10,000	
Taxable income for 1954 by applying subpart 2, item B	30,000	
Tax on $30,000		1,715
Decrease in tax for 1954 by applying subpart 2, item B		570
Tax for 1957 without taking the restoration into account		365
Amount by which decrease exceeds the tax for 1957 computed without taking the restoration into account		205

The $205 is treated as having been paid on the last day prescribed by law for the payment of the tax for 1957 and is available as a refund. In addition the taxpayer has a deficiency of $285 ($2,285 less $2,000) for 1954 because of the additional income of $5,000.

Subp. 5. **Method of accounting.** The provisions of Minnesota Statutes, section 290.07, subdivision 4 and this part shall be applicable in the case of a taxpayer on the cash receipts and disbursements method of accounting only to the taxable year in which the item of income included in a prior year (or years) under a claim of right is actually repaid. However, in the case of a taxpayer on the cash receipts and disbursements method of accounting who constructively received an item of income under a claim of right and included such item of income in gross income in a prior year (or years), the provisions of Minnesota Statutes, section 290.07, subdivision 4 and this part shall be applicable to the taxable year in which the taxpayer is required to relinquish his right to receive such item of income. Such provisions shall be applicable in the case of other taxpayers only to the taxable year which is the proper taxable year (under the method of accounting used by the taxpayer in computing taxable income) for taking into account the deduction resulting from the restoration of the item of income included in a prior year (or years) under a claim of right. For example, if the taxpayer is on an accrual method of accounting, the provisions of this section shall apply to the year in which the obligation properly accrues for the repayment of the item included under a claim of right.

Subp. 6. **Inventory items, stock in trade, and property held primarily for sale in the ordinary course of trade or business.** Except for amounts specified in the following paragraph, the provisions of Minnesota Statutes, section 290.07, subdivision 4 and this part do not apply to deductions attributable to items which were included in gross income by reason of the sale or other disposition of stock in trade of the taxpayer (or other property of a kind which would properly have been included in the inventory of the taxpayer if on hand at the close of the prior taxable year) or property held by the taxpayer primarily for sale to customers in the ordinary course of the taxpayer's trade or business. This part is, therefore, not applicable to sales returns and allowances and similar items.

The provisions of Minnesota Statutes, section 290.07, subdivision 4 and this part apply to deductions which arise out of refunds or repayments made by a regulated public utility, as defined in the Internal Revenue Code of 1954, section 1503 (c)(1) or (3) and the Federal Tax Regulations, section 1.1502-2 (g), if such refunds or repayments are required to be made by the government, political subdivision, agency, or instrumentality referred to in such regulation. Thus, deductions attributable to refunds of charges for the sale of natural gas under rates approved temporarily by a proper governmental authority are eligible for the benefits of Minnesota Statutes, section 290.07, subdivision 4 and this part, if such refunds are required by the governmental authority.

Subp. 7. **Bad debts.** The provisions of Minnesota Statutes, section 290.07, subdivision 4 and this part do not apply to deductions attributable to bad debts.

Subp. 8. **Legal fees and other expenses.** Minnesota Statutes, section 290.07, subdivision 4 and this part do not apply to legal fees or other expenses incurred by a taxpayer in contesting the restoration of an item previously included in income. This rule may be illustrated by the following example:

A sold his personal residence to B in a prior taxable year and realized a capital gain on the sale. C claimed that under an agreement with A he was entitled to a five percent share of the purchase price since he brought the parties together and was instrumental in closing the sale. A rejected C's demand and included the entire amount of the capital gain in gross income for the year of sale. C instituted action and in the taxable year judgment is rendered against A who pays C the amount involved. In addition, A pays legal fees in the taxable year which were incurred in the defense of the action. Minnesota Statutes, section 290.07, subdivision 4 applies to the payment of the five percent share of the purchase price to C. However, the payment of the legal fees, whether or not otherwise deductible, does not constitute an item restored for purposes of Minnesota Statutes, section 290.07, subdivision 4.

Subp. 9. **Refunds.** If the decrease in tax for the prior taxable year (or years) determined under Minnesota Statutes, section 290.07, subdivision 4, and subpart 2, item B, exceeds the tax imposed by Minnesota Statutes, chapter 290 for the taxable year computed without the deduction, the excess shall be considered to be a payment of tax for the taxable year of the deduction. Such payment is deemed to have been made on the last day prescribed by law for the payment of tax for the taxable year and shall be refunded or credited in the same manner as if it were an overpayment of tax for such taxable year.

Statutory Authority: *MS S 290.52*

8007.0400 TAXABLE YEAR OF INCLUSION.

Subpart 1. **General rule.** Gains, profits, and income are to be included in gross income for the taxable year in which they are actually or constructively received by the taxpayer unless includible for a different year in accordance with the taxpayer's method of accounting. Under an accrual method of accounting, income is includible in gross income when all the events have occurred which fix the right to receive such income and the amount thereof can be determined with reasonable accuracy. Therefore, under such a method of accounting if, in the case of compensation for services, no determination can be made as to the right to such compensation or the amount thereof until the services are completed, the amount of compensation is ordinarily income for the taxable year in which the determination can be made. Under the cash receipts and disbursements method of accounting, such an amount is includible in gross income when actually or constructively received. Where an amount of income is properly accrued on the basis of a reasonable estimate and the exact amount is subsequently determined, the difference, if any, shall be taken into account for the taxable year in which such determination is made. To the extent that income is attributable to the recovery of bad debts for accounts charged off in prior years, it is includible in the year of recovery in accordance with the taxpayer's method of accounting, regardless of the date when the amounts were charged off. For treatment of bad debts and bad debt recoveries, see Minnesota Statutes, section 290.09, subdivision 6 and the rules thereunder. For the year in which a partner must include his distributive share of partnership income, see Minnesota Statutes, section 290.31, subdivision 6, clause (1) and rules thereunder. If a taxpayer ascertains that an item should have been included in gross income in a prior taxable year, he should, if within the period of limitation, file an amended return and pay any additional tax due. Similarly, if a taxpayer ascertains that an item was improperly included in gross income in a prior taxable year, he should, if within the period of limitation, file claim for credit of refund of any overpayment of tax arising therefrom.

Subp. 2. **Special rule in case of death.** A taxpayer's taxable year ends on the date of his death. See Minnesota Statutes, section 290.40, clause (1) and the rules thereunder. In computing taxable income for such year, there shall be included only amounts properly includible under the method of accounting used by the taxpayer. However, if the taxpayer used an accrual method of accounting, amounts accrued only by reason of his death shall not be included in computing taxable income for such year. If the taxpayer uses no regular accounting method, only amounts actually or constructively received during such year shall be included. For rules relating to the inclusion of partnership income in the return of a decedent partner, see Minnesota Statutes, section 290.31 and the rules thereunder.

If the decedent owned an installment obligation the income from which was taxable to him under Minnesota Statutes, section 290.07, subdivision 5, no income is required to be reported in the return of the decedent by reason of the transmission at death of such obligation.

For treatment of installment obligations acquired by the decedent's estate or by any person by bequest, devise, or inheritance from the decedent, see Minnesota Statutes, section 290.077, subdivision 1, clause (4).

Statutory Authority: *MS s 290.52*

8007.0500 CONSTRUCTIVE RECEIPT OF INCOME.

Subpart 1. **General rule.** Income although not actually reduced to a taxpayer's possession is constructively received by him in the taxable year during which it is credited to his account or set apart for him so that he may draw upon it at any time. However, income is not constructively received if the taxpayer's control of its receipts is subject to substantial limitations or restrictions. Thus, if a corporation credits its employees with bonus stock, but the stock is not available to such employees until some future date, the mere crediting on the books of the corporation does not constitute receipt.

Subp. 2. **Examples of constructive receipt.** Interest coupons which have matured and are payable but which have not been cashed are constructively received in the taxable year during which the coupons mature, unless it can be shown that there are no funds available for payment of the interest during such year. Dividends on corporate stock are constructively received when unqualifiedly made subject to the demand of the shareholder. However, if a dividend is declared payable on December 31 and the corporation followed its usual practice of paying the dividends by checks mailed so that the shareholders would not receive them until January of the following year, such dividends are not considered to have been constructively received until January. Interest on savings bank deposits is income to the depositor when credited on the books of the bank, even though the bank has a rule, seldom or never enforced, that it may require a certain number of days' notice before withdrawals are permitted. Generally, the amount of dividends or interest credited to shareholders of organizations such as building and loan associations or cooperative banks, is income to the shareholders for the taxable year when credited. However, if the amount of such dividends or interest is not available for the shareholders' free and unrestricted use at the time credited, such amount is not constructively received and does not constitute income to the shareholder until the taxable year in which the amount is available. Accordingly, if the amount of dividends or interest is accumulated and is not available to the shareholder until the maturity of a share, the crediting thereof to the shareholder's account does not constitute constructive receipt. However, in such a case the total amount credited is income to the shareholder in the year of maturity.

Statutory Authority: *MS s 290.52*

8007.0600 LONG-TERM CONTRACTS.

Subpart 1. **Definition.** The term "long-term contracts" means building, installation, or construction contracts covering a period in excess of one year from the date of execution of the contract to the date on which the contract is finally completed and accepted.

Subp. 2. **Methods.** Income from long-term contracts as defined in subpart 1, determined in a manner consistent with the nature and terms of the contract, may be included in gross income in accordance with one of the following methods, provided such method clearly reflects income:

A. Gross income derived from long-term contracts may be reported according to the percentage of completion method. Under this method, the portion of the gross contract price which corresponds to the percentage of the entire contract which has been completed during the taxable year shall be included in gross income for such taxable year. There shall then be deducted all expenditures made during the taxable year in connection with the contract, account being taken of the material and supplies on hand at the beginning and end of the taxable year for use in such contract. Certificates of architects or engineers showing the percentage of completion of each contract during the taxable year shall be available at the principal place of business of the taxpayer for inspection in connection with an examination of the income tax return.

B. Gross income derived from long-term contracts may be reported for the taxable year in which the contract is finally completed and accepted. Under this method, there shall be deducted from gross income for such year all expenses which are properly allocable to the contract, taking into account any material and supplies charged to the contract but remaining on hand at the time of completion.

C. In general, long-term contract methods of accounting apply only to the accounting for income and expenses attributable to long-term contracts. Other income and expense items, such as investment income or expenses not attributable to such contracts, shall be accounted for under a proper method of accounting. See Minnesota Statutes, section 290.07, subdivision 2 and the rules thereunder. A taxpayer may change to or from a long-term contract method of accounting only with the consent of the commissioner. See Minnesota Statutes, section 290.07, subdivision 2 and the rules thereunder. When a taxpayer reports income under a long-term contract method, a statement to that effect shall be attached to his income tax return.

Statutory Authority: *MS s 290.52*

8007.0700 ACCOUNTING FOR REDEMPTION OF TRADING STAMPS AND COUPONS.

Subpart 1. **Computation.** If a taxpayer issues trading stamps or premium coupons with sales, which stamps or coupons are redeemable in merchandise or cash, he should, in computing the income from such sales, subtract only the amount which will be required for the redemption of such part of the total issue of trading stamps or premium coupons issued during the taxable year as will eventually be presented for redemption. This amount will be determined in the light of the experience of the taxpayer in his particular business and of other users of trading stamps or premium coupons engaged in similar businesses. The taxpayer shall file a statement showing with respect to each of the five preceding years, or such number of these years as stamps or coupons have been issued by him, the following:

A. the total issue of stamps or coupons during each year;

B. the total stamps or coupons redeemed in each year; and

C. such other information as is necessary to establish the correctness of the amount subtracted from sales in each of such years.

Subp. 2. **Adjustment.** Upon examination of the return, the amount subtracted in respect of such coupons will be adjusted, if, in the opinion of the commissioner, such amount is incorrectly computed.

Statutory Authority: *MS s 290.52*

8007.0800 TIME FOR TAKING DEDUCTIONS AND CREDITS.

Subpart 1. **In general.** Taxpayers should endeavor to ascertain all the facts necessary to make a correct return for each year. The return should be complete in itself, both as to gross income and deductions. The expenses of one year cannot be used to reduce the income of a subsequent year. If a taxpayer does not avail himself of the deductions authorized by the act for the year in which such deductions should be taken, he cannot charge them against the income of any other year.

Adjudications which are binding upon the taxpayer, such as decisions under workers' compensation laws, or judgments on account of damages for patent infringement, personal injuries, or other causes, are deductible from gross income when the claim is adjudicated if the taxpayer is reporting on an accrual basis, or when the claim is paid if the taxpayer is on the cash basis. In determining the extent of such deductions the amount shall be reduced by insurance or other compensation received.

If a taxpayer cannot ascertain the amount of a loss in the year in which it was sustained, but subsequently determines the amount of such loss, he may file a claim for refund under the provisions of Minnesota Statutes, section 290.50 for the year during which the loss actually occurred, if the statute of limitations set out in Minnesota Statutes, section 290.50 has not expired. However, losses arising from theft shall be treated as sustained in the taxable year in which the taxpayer discovers the theft. (See Minnesota Statutes, section 290.09, subdivision 5.)

For tax treatment of periodic payments of alimony, separate maintenance, or support by a divorced or separated spouse, see Minnesota Statutes, sections 290.072 and 290.09, subdivision 14.

Deductions and credits accrued only by reason of the death of the taxpayer shall not be allowed in computing the net income of the taxpayer for the period in which falls the date of the taxpayer's death. See 2007.7 (2).

Subp. 2. **Paid or incurred and paid or accrued.** The terms "paid or incurred" and "paid or accrued" will be construed according to the method of accounting upon the basis of which the net income is computed by the taxpayer. The deductions and credits provided for in Minnesota Statutes, sections 290.09 and 290.21 must be taken for the taxable year in which "paid or accrued" or "paid or incurred," unless in order clearly to reflect the income such deductions or credits should be taken as of a different period.

Interest received on refunds of taxes shall be included in gross income for the year received regardless of the method of bookkeeping employed by the taxpayer.

Subp. 3. **Contested liabilities.** With respect to taxable years beginning after December 31, 1964, if the taxpayer contests an ascertained liability but nevertheless causes the payment of said liability and such liability, except for the contest, would be a property deduction, then said payment shall be deductible for the year of such payment or for an earlier taxable year.

Statutory Authority: *MS s 290.52*

NOTE: Regulation 2007.7(2) has been repealed.

8007.2000 RECOVERY OF BAD DEBTS.

For all taxable years beginning after December 31, 1942, the recovery of all or part of a bad debt constitutes income only to the extent that a tax benefit resulted in a prior year.

To illustrate, assume that in 1943 a corporate taxpayer's taxable net income was $500 after deducting a $1,200 bad debt. Since the taxpayer was entitled to a specific credit of $1,000 in 1943, it was apparent that there was no tax benefit from $500 of the total bad debt deduction of $1,200. If the taxpayer recovers $250 in 1946 and $500 in 1947, such taxpayer may exclude the total $250 recovery in 1946 and $250 of the $500 recovery in 1947. The balance of the 1947 recovery and any subsequent recovery must be included in gross income.

If the taxpayer uses the reserve method, recoveries of bad debts previously charged against the reserve are not income as such but are credits to the reserve, thus decreasing the amount of addition to the reserve for the current year necessary to bring it up to a reasonable amount. It is this addition to the reserve which is deductible on the income tax return.

Statutory Authority: *MS s 290.52*

8007.3000 COMMODITY CREDIT LOANS.

Prior to the 1943 amendment, when a producer of agricultural commodities pledged them as security for a loan from the Commodity Credit Corporation, he was required to include the amount of these loans in his gross income for the year in which the security for the loan was sold. Under the 1943 amendment for all taxable years beginning with 1942, a taxpayer who receives a loan from the Commodity Credit Corporation may, at his election, include the amount of such loan in his gross income for the taxable year in which the loan is received or for the taxable year in which the security is sold. When the taxpayer makes such an election, then he shall be bound by that election for all taxable years, unless he secures the permission of the commissioner of taxation to change to a different method of accounting. Application for permission to change the method of accounting and the basis upon which such return is made shall be filed within 90 days after the beginning of the taxable year to be covered by the return.

If the taxpayer elects, he may report the income in the taxable year in which the security is sold rather than the year in which the loan is received. In that case, the income realized from the disposition of such security constitutes income for that taxable year.

If a taxpayer elects under Minnesota Statutes, section 290.073 to include in his gross income the amount of a loan from the Commodity Credit Corporation for the taxable year in which it is received, then:

A. no part of the amount realized by the Commodity Credit Corporation upon the sale or other disposition of the commodity pledged for such loan shall be recognized as income to the taxpayer, unless the taxpayer receives an amount in addition to that advanced to him as the loan, in which event such additional amount shall be included in the gross income of the taxpayer for the year in which received; and

B. no deductible loss to the taxpayer shall be recognized on account of any deficiency realized by the Commodity Credit Corporation on such loan if the taxpayer was relieved of liability for such deficiency.

Example: A, a taxpayer who elected for his taxable years 1942 and 1943, to include in gross income amounts received during those years as loans from the Commodity Credit Corporation, received as loans $500 in 1942 and $700 in 1943. In 1944 all of the pledged commodity was sold by the Commodity Credit Corporation for an amount of $200 less than the loan with respect to the commodity pledged in 1942 and for an amount of $150 greater than the loan with respect to the commodity pledged in 1943. A, in making his return for 1944, shall include in gross income the sum of $150 if it is received during that year, but will not be allowed a deduction for the deficiency of $200 unless he is required to satisfy such deficiency and does satisfy it during that year.

Statutory Authority: *MS s 290.52*

8007.4000 RENEGOTIATED WAR CONTRACTS.

A taxpayer who supplies goods, wares or merchandise, or performs services, or both, under a contract with the United States of America, or under a subcontract thereunder, or any agency thereof, and who is subject to renegotiation under the laws of the United States of America, or is required to renegotiate with his subcontractor, shall compute his tax liability without giving consideration to any adjustment of excessive profits renegotiated subsequent to the close of the taxable year.

In any case where a final determination of renegotiation has been completed subsequent to the close of any taxable year, the taxpayer shall be entitled to claim as a deduction from gross income in the year in which the determination is made the difference between (1) the amount determined to be excessive profits, and (2) the amount of federal income and excess profits taxes applicable thereto.

An example of this computation is shown in the following schedule:

Taxable net income--year 1952 (before any adjustment for renegotiation or federal income taxes paid)		$10,000,000
Federal income and excess profits taxes paid		5,000,000
Net		$ 5,000,000
Excess profits finally determined in 1952, applicable to the year 1951	$5,000,000	
Less applicable federal income and excess profits taxes on above	2,500,000	
Difference deductible		2,500,000
Taxable net income for the year 1952 on which tax is to be computed		$ 2,500,000

In any case where a final determination of renegotiation has been completed subsequent to the close of the taxable year, and the net income for the year in which such final determination is made, computed without regard thereto, is less than the amount deductible as a result thereof as shown in the preceding example, the taxpayer shall be entitled to a refund of any state income and excise taxes paid, to the extent they were paid on or measured by the excess of (1) the amount which would be deductible as a result of such determination (as shown in the preceding example) over (2) the taxable net income computed without regard to such determination. An example of this computation is shown as follows:

Taxable net income--year 1951 (before any adjustments for renegotiation or federal income taxes paid		$11,000,000
Federal income and excess profits taxes paid (for year 1950)		7,000,000
Net		$ 4,000,000
Excessive profits finally determined in 1953, applicable to the year 1951	$10,000,000	
Less applicable federal income and excess profits taxes on above	5,000,000	
Net renegotiated profits	$ 5,000,000	
Taxable net income year 1953 before renegotiation	4,000,000	
Amount of renegotiated profits deductible in year 1953	4,000,000	
Excess of difference over the amount of taxable income		1,000,000

State income and excise taxes computed on $1,000,000		54,000
Amount of refund of 1951 state income and excise taxes to which taxpayer is entitled		$ 54,000

The foregoing computations are based on the assumption that the taxpayer's entire taxable net income is assignable to Minnesota.

The following example illustrates a computation of taxable net income in cases where the total net income is subject to apportionment by formula:

Taxable net income--year 1952 (before any adjustment for renegotiation)		$20,000,000
Percentage of net income assignable to Minnesota		25%
Minnesota taxable net income--year 1952 (before any adjustments for renegotiation)		$ 5,000,000
Less excessive profits renegotiated and finally determined in 1962--applicable to year 1951	$10,000,000	
Deduct federal income and excess profits taxes applicable to above	6,000,000	
Net renegotiated profits	$ 4,000,000	
Percentage of taxable net income assigned to Minnesota--year 1951	15%	
Amount of net renegotiated profits deductible from Minnesota net income--year 1952		600,000
Minnesota taxable net income--year 1952		$ 4,400,000

Statutory Authority: *MS s 290.52*