

There Are Some “Guaranties” in Life, But Do You Want to Be the One Making Them? Analyzing the Unique Rules for Bad Debt Losses of Guarantors

By Hale E. Sheppard

Hale Sheppard examines the complexities of bad debt deductions claimed by third-party guarantors.

Introduction

People are fond of saying that there are only two guaranties in this world: death and taxes. This is simply not the case, particularly in tough financial times. As the economy deteriorates, the credit scores of many borrowers and the risk tolerance of most lenders seem to fall precipitously. The show must go on, though.

To obtain the necessary business capital from financial institutions in these bleak conditions, potential borrowers often seek backing from third parties with better financial resumes. In short, borrowers frequently need to find a guarantor, another layer of protection for the financial institution, in order to qualify for the loan. The guarantor, of course, does not put his neck on the line for nothing. He ordinarily demands various forms of compensation, as well as certain rights of recourse against the borrower in case of default. The theory is relatively straightforward: if the guarantor is going to incur a significant risk, he is entitled to a handsome reward.

Optimistic expectations notwithstanding, many business ventures do not turn out as planned, and borrowers fail to make timely, full payments to the

lender, as required by the loan documents. When this occurs, many lenders immediately opt to exercise their collection rights against the guarantors instead of pursuing the struggling borrowers. Once the guarantor recovers from the blow of having to make good on the borrower's financial blunder, his mind tends to be focused on two things: recouping the money from the borrower and claiming the most favorable tax treatment possible. This article examines these two interrelated issues, which will become increasingly prevalent (and thus important to tax practitioners) as the U.S. economy continues to flounder.

Overview of the Applicable Law

To appreciate the special rules applicable to losses incurred by guarantors of debts that become worthless, it is important first to understand some general legal principles under Code Sec. 166 and the corresponding regulations.¹

In the case of a taxpayer other than a corporation, where any “nonbusiness debt” becomes worthless during the year, the resulting loss generally is treated as a loss from the sale or exchange of a capital asset held for not more than one year.² In other words, the loss from the worthlessness of a nonbusiness debt ordinarily is considered a short-term capital loss, with all that entails.³

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In this context, the term “nonbusiness debt” generally means a debt other than (i) a debt that is created or acquired in connection with the taxpayer’s trade or business or (ii) a debt the loss from the worthlessness of which is incurred in the taxpayer’s trade or business.⁴ However, a nonbusiness debt does not include certain securities, such as bonds, debentures, notes, certificates or other evidence of debt that are issued by a corporation, a government or a political subdivision of a government, with interest coupons or in registered form.⁵ Whether a debt is a nonbusiness debt is a question of fact in each case, and the use to which the debtor puts the borrowed funds has no bearing on the analysis.⁶

Only “*bona fide*” debts qualify for purposes of Code Sec. 166. A debt is *bona fide* if it “arises from a debtor-creditor relationship based upon a valid and enforceable obligation to pay a fixed or determinable sum of money.”⁷ A gift or a contribution to capital, therefore, is not considered a *bona fide* debt.⁸

As mentioned above, there are special rules in cases of losses sustained by *guarantors* of debts that become worthless.⁹ The legislative history is instructive on this topic. The general rule allowing a short-term capital loss is stated in the following manner:

[W]hen a taxpayer has a loss arising from the guaranty of a loan, he is to receive the same treatment as where he has a loss from a loan which he makes directly. Thus, if the guaranty agreement arose out of the guarantor’s trade or business, the guarantor would still be permitted to deduct the loss resulting from the transaction against ordinary income. If the guaranty agreement was a transaction entered into for profit by the guarantor (but not as part of his trade or business), he would be able to deduct the resulting loss as a nonbusiness debt.¹⁰

The legislative history also clarifies that short-term capital loss treatment generally is appropriate in cases of *corporate* debt. It states the following in this regard:

Congress also wishes to make it clear that in the case of a guarantor of a corporation obligation,

any payment under the guaranty agreement must be deducted (if at all) as nonbusiness bad debt, regardless of whether there is any right of subrogation, unless the guaranty was made pursuant to the taxpayer’s trade or business.¹¹

According to the regulations interpreting this legislative history, a payment in discharge of part or all of the taxpayer’s agreement to act as guarantor should be treated as worthless debt only if (i) the guaranty agreement was entered into in the course of the taxpayer’s trade or business, or as a transaction for profit;¹² (ii) there was an enforceable legal duty imposed upon the taxpayer, as guarantor, to make the payment, though it is not necessary that the party collecting

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from the guarantor actually brings a legal action to force payment;¹³ (iii) the guarantor entered into the guaranty agreement before the obligation became worthless (or partially worthless in the case of an agreement entered into in the course of a guarantor’s trade or business);¹⁴ and (iv) the guarantor received reasonable consideration for entering into the guaranty agreement.¹⁵

There is another key issue: timing. Simply stated, in what tax year may the guarantor claim the bad debt deduction? The relevant legislative history sets forth two different rules, the application of which depends on whether the guarantor has the right of subrogation or other right of recourse against the borrower.

If the guarantor has no right over against the maker of the obligation, the payment under the guaranty is deductible as a bad debt for the year in which the payment is made.

[On the other hand]

If the guaranty agreement . . . requires payment by the guarantor upon default by the maker of the note (*i.e.*, the borrower), and the guarantor has a right to subrogation or other right against the maker, [then] no deduction will be allowed to the guarantor until the year in which the right over against the maker becomes worthless (or partially

worthless, where the guaranty occurs in connection with the guarantor's trade or business).¹⁶

There are special rules where the second scenario applies. In particular, where the guaranty agreement provides for a right of subrogation or other similar right against the borrower, the guarantor may not treat the debt as worthless for federal income tax purposes until the year in which the right of subrogation or other similar right becomes "totally worthless" (or partially worthless in the case of an agreement that arose in the course of the guarantor's trade or business).¹⁷

The regulations are liberal with respect to the types of evidence that are relevant to the worthlessness issue. They generally state that in determining whether a debt is wholly or partially worthless, the IRS will consider "all pertinent evidence," including the value of any collateral securing the debt and the debtor's financial condition.¹⁸ The regulations further clarify that in certain circumstances a taxpayer is not required to take legal action in order to claim that a debt is worthless. On this score, they state the following:

Where the surrounding circumstances indicate that a debt is worthless and uncollectible and that legal action to enforce payment would in all probability not result in the satisfaction of execution on a judgment, a showing of these facts will be sufficient evidence of the worthlessness of the debt for purposes of the deduction under Section 166.¹⁹

It is also important to note that the relevant regulations generally provide that a payment of *principal and interest* made during the year by the guarantor in discharge of all or part of his obligation as a guarantor is treated as a worthless nonbusiness debt in the year in which payment is made.²⁰

Description of Relevant Case Law and IRS Rulings

Bad debt deductions are at the center of many tax disputes, particularly those concerning the issue

of worthlessness. According to one tax court judge citing John Milton's *Paradise Lost*, "[t]he cases involving the issue of when a debt becomes worthless are as 'thick as autumnal leaves that strow the brooks in Vallombrosa.'"²¹

Bad debt disputes are highly fact sensitive; no two cases are exactly alike. Nevertheless, a review of various cases and IRS rulings addressing pertinent issues provides valuable guidance as to the likelihood of withstanding scrutiny if the IRS challenges a bad debt deduction. These issues, which are discussed in greater detail below, include (i) when a payment is made; (ii) whether a guarantor has a right of subrogation or other right of recourse against the debtor; and

(iii) if so, when the debt becomes totally worthless for purposes of Code Sec.

When Is Payment Made?

A guarantor may not claim a bad debt deduction before making payment on the guaranty, regardless of whether the guarantor is a cash-basis or accrual-basis taxpayer. With respect to the former, the courts have held that "[w]hen a cash basis guarantor pays a debt with cash or its equivalent, then and only then has he realized a loss."²² The courts have arrived at the same conclusion in the case of the latter, explaining that:

[U]ntil a payment is made, the guarantor's obligation remains undischarged [and] there is no indebtedness running to the guarantor that has the potential of being worthless. Rules of tax accounting have little, if anything, to do with that result. Until payment is made, and the guarantor is discharged of his liability, the debt in question is . . . immune from worthlessness. By definition the debt is not worthless; how it is otherwise accounted for simply is of no relevance.²³

When payment actually occurred may not be clear. In one case, a guarantor of multiple promissory notes was denied a nonbusiness bad debt deduction during the year that the creditor obtained a judgment against the guarantor on the guaranty, and the guarantor made

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an irrevocable transfer of property to a third party with a provision that such party must pay the creditor directly (instead of paying the guarantor). Despite the guarantor's instructions, the purchasers of the property did not pay the creditor until the subsequent year; therefore, the district court disallowed the bad debt deduction in the previous year, *i.e.*, the year of the judgment and property transfer.²⁴ Other cases have recognized that nonjudicial foreclosure on a guarantor's personal property that the guarantor pledged as security for a loan to the borrower qualifies as a bad debt deduction.²⁵

Does the Guarantor Have the Right to Subrogation or Other Right of Recourse Against the Debtor?

Paraphrasing the holding in the seminal case, the tax court explained the essence of a guaranty for federal income tax purposes: the guarantor pays the creditor under the obligation arising from the guaranty agreement; the guarantor's loss does not arise because of such payment, but rather because of the debtor's inability to reimburse the guarantor; and the debtor is indebted to the guarantor by application of the doctrine of subrogation, under which a guarantor who is required to make payment pursuant to the guaranty agreement succeeds to the rights of the original creditor.²⁶ The tax court went on to clarify that "[t]he courts have held that, even without the existence of a technical right of subrogation, a guarantor's loss is in the nature of a bad debt loss, and, thus, is subject to the bad debt regime of Section 166."²⁷ In a subsequent case, the tax court discussed a guarantor's implied right of subrogation and reimbursement:

[The relevant regulation under Code Sec. 166], properly read, stands for the proposition that where a guarantor does have rights of subrogation and reimbursement from the original debtor (*regardless of whether or not these rights are expressly stated in the guaranty agreement*), the provisions of section 1.166-9(e)(2), Income Tax Regs., apply, and the guarantor is not entitled to a bad debt deduction until the rights of subrogation and reimbursement are shown to be worthless.²⁸

Consistent with federal tax law, many states grant subrogation rights to guarantors. In Georgia, for instance, the relevant provision states that "[a] surety who has paid the debt of his principal shall be subrogated, both at law and in equity, to all the rights of the creditor and, in a controversy with other creditors, shall rank in dignity the same as the creditor whose claim he paid."²⁹

When Does a Debt Become Worthless?

As mentioned above, the regulations are liberal with respect to the types of evidence that are relevant to the worthlessness issue. They generally state that in determining whether a debt is worthless, the IRS will consider "all pertinent evidence."³⁰ This includes the value of any collateral securing the debt, as well as the debtor's financial condition.³¹ The regulations further state that a guarantor does not need to take legal action against the debtor for a debt to be considered worthless, provided that the surrounding circumstances indicate that the debt is uncollectible and that legal action to enforce payment likely would not serve its purpose.³²

Applying these regulations, certain IRS pronouncements have interpreted the concept of worthlessness broadly. In one private letter ruling, the IRS held that the payment by the taxpayers, as guarantors, based on the debtor's "precarious economic condition" entitled the taxpayers to a nonbusiness bad debt in the year of payment.³³ There, the debtor's annual revenues had fallen significantly, its staff had been reduced by approximately two-thirds, it had a loss during the year in question, and collecting its receivables had been "extremely difficult."³⁴

Tax cases involving bad debt deductions are plentiful and highly fact-sensitive. Several of these cases summarize the standards for establishing worthlessness and provide insight beyond that offered by the regulations. In other words, they demonstrate how the courts have interpreted and applied the applicable rules, which can be pivotal. The relevant portions of three instructive cases are set forth below.

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particular event or group of facts that proves worthlessness. [The taxpayer] must establish sufficient objective facts from which worthlessness could be determined. A debt is considered worthless when there are reasonable grounds for abandoning hope that the debt will be repaid. The decision must be made in the exercise of sound business judgment. Legal action is not required to enforce payment where the surrounding facts and circumstances indicate that, in all probability, the action would not result in an enforceable judgment in favor of the lender. The determination by the trier of fact that a debt has become worthless requires an examination of all the facts and circumstances.³⁵

There is no standard test for determining worthlessness; whether and when a debt becomes worthless depends on all the facts and circumstances. It is generally accepted, however, that the year of worthlessness is to be fixed by identifiable events constituting reasonable grounds for abandoning any hope of recovery. It is often very difficult to determine the precise moment a debt becomes worthless. This is particularly true when a debtor's financial situation deteriorates over time. However, it is clear that in making the determination, the creditor must be neither an "incorrigible optimist" nor a "stygian pessimist." The creditor's decision must be made in the exercise of sound business judgment, based upon information that is as complete as is reasonably obtainable.³⁶

[The test for worthlessness] must be flexible in nature, varying according to the circumstances of each particular case, so that whatever inferences a court might draw from a particular fact in another case are not binding on the examining court, although the same fact may be present . . . To be deductible, a debt need not be proven worthless beyond all peradventure, since a bare hope that something might be recovered in the future constitutes no sound reason for postponing the time for taking a deduction. The taxpayer is not required to postpone his entitlement to a deduction in the expectancy of uncertain future events nor is he called to wait until some turn of the wheel of fortune may bring the debtor into affluence. It appears that the taxpayer must strike a middle course between optimism and

pessimism and determine debts to be worthless in the exercise of sound business judgment based upon as complete information as is reasonably obtainable.³⁷

In applying the preceding standards, the courts have considered several factors, including (i) the subordinated status of the debt; (ii) a decline in the debtor's business; (iii) a reduction in value of the property secured by the debt; (iv) claims of prior creditors that far exceed the fair market value of all assets available for payment; (v) the overall business climate; (vi) the debtor's earning capacity; (vii) the debtor's serious financial reverses; (viii) guaranties on the debt; (ix) events of default, whether major or minor; (x) insolvency of the debtor; (xi) the debtor's refusal to pay; (xii) abandonment by the debtor of his assets or business; (xiii) ill health, death or disappearance of the debtor's principals; (xiv) bankruptcy or receivership; (xv) actions of the guarantor in pursuing collection, *i.e.*, whether the guarantor unreasonably failed to take collection action and then claimed the deduction; (xvi) subsequent dealings between the guarantor and the debtor; and (xvii) the debtor's lack of assets.³⁸ The courts have clarified that "there are no absolutes in this area," and no single factor is conclusive or controlling.³⁹

Three additional points are noteworthy. First, various courts have recognized that lenders or guarantors who have a particularly close relationship with the borrower are in a unique position to determine when a debt has become worthless for purposes of Code Sec. 166. In one case, for example, the taxpayers successfully argued before a federal district court that they were able to reasonably conclude that the debt became worthless during the year in question because of their "longstanding personal and business relationship" with the debtor and their "personal familiarity" with the debtor, her project, and the effect of such project on her financial condition.⁴⁰

Second, in accordance with the regulations, many courts have recognized that a lender or guarantor is not required to take legal action against the borrower as a prerequisite to claiming a bad debt deduction where such action would be useless. For instance, the tax court recently held that "[w]here a creditor is familiar with the debtor's circumstances and knows that the debtor is hopelessly insolvent, he need not attempt to collect the debt where his attempts to do so would be futile."⁴¹ In an earlier case involving this same is-

sue, the tax court explained that the law “does not require a creditor to engage in futile acts” and “[i]f the creditor can show that the debtor’s financial condition was such that attempts to collect would have been useless, then the creditor is excused from collection activities.”⁴² Likewise, in a situation where the book value of the debtor’s assets was substantially lower than that of the liabilities, the court of claims excused the taxpayer from taking legal actions, acknowledging that “[a]s with a turnip, squeezing [the debtor] would produce neither blood nor money.”⁴³ Recent IRS rulings also demonstrate that worthlessness exists where collection efforts would be fruitless.⁴⁴

Third, over the years many courts have underscored the importance of respecting the guarantor’s business judgment when it comes to writing-off debts.⁴⁵ Recently, the Tax Court exhibited the general judicial reluctance to allow the IRS to substitute its judgment for that of the guarantor. In upholding the bad debt deduction, the court explained the following:

While the management group may have made other choices if they had the benefit of hindsight, they did what they thought was best for [the company] based on the circumstances at the time [The IRS’s] hypothesizing over what could or should have been done ignores the realities of the business and is unreasonable. [The IRS’s] determination that the . . . loan was not worthless in 1995 therefore was arbitrary, unreasonable, and an abuse of discretion.⁴⁶

Conclusion

If one heeds the predictions of many economic pundits, the U.S. economy will continue to struggle, at least in the near term. This financial slowdown should have several consequences, including greater restrictions on lenders. Logic dictates, therefore, that many borrowers will be required to present a guarantor as a condition to obtaining the much-needed business capital. Logic further dictates that, despite high hopes of success, many borrowers will be unable to fulfill their financial obligations, and the lenders will look to the guarantors for payment. Once guarantors satisfy the outstanding debt, they often begin to focus on tax issues. In particular, they want to salvage a bad situation by claiming the most beneficial tax treatment.

This article demonstrates that the rules applicable to bad debt deductions by guarantors are unique and complex. Indeed, it is difficult for guarantors and their advisors to determine, for purposes of Code Sec. 166, when a payment on the guaranty is made, whether a guarantor has a right of subrogation or other right of recourse against the debtor, and when a debt becomes “totally worthless.” This article also shows that there is a considerable body of case law interpreting and applying the statutory and regulatory rules, sometimes in unexpected ways. Finally, this article confirms that bad debt deductions are heavily scrutinized by the IRS, which results in frequent litigation. In light of these circumstances, guarantors would be wise to consult tax professionals who regularly handle bad debt disputes before taking aggressive tax positions.

ENDNOTES

¹ Unless otherwise stated, all uses of the term “Section” or “Sections” refer to the Internal Revenue Code of 1986, as amended.

² Code Sec. 166(d)(1)(B); Reg. §1.166-5(a)(2).

³ This loss is subject to the limitations on capital losses described in Code Sec. 1211, as well as the rules on capital loss carrybacks and carryovers described in Code Sec. 1212, Reg. §1.166-5(a)(2).

⁴ Code Sec. 166(d)(2); Reg. §1.166-5(b).

⁵ Code Sec. 166(e); Reg. §1.166-5(b); Code Sec. 165(g)(2)(C).

⁶ Reg. §1.166-5(b).

⁷ Reg. §1.166-1(c).

⁸ Reg. §1.166-5(c).

⁹ Reg. §1.166-5(c). This regulation cross-references Reg. §1.166-8 and Reg. §1.166-9. The former is inapplicable here because it applies only to losses of guarantors on agreements made before January 1, 1976.

¹⁰ J.C.T. REP. NO. JCS-33-76, *General Expla-*

nation of the Tax Reform Act of 1976 (P.L. 94-455), at 158; *See also* H.R. REP. NO. 94-658, at 3069-3072 (Nov. 12, 1975).

¹¹ *Id.*

¹² Reg. §1.166-9(d)(1).

¹³ Reg. §1.166-9(d)(2). *See also* J.C.T. REP. NO. JCS-33-76, *General Explanation of the Tax Reform Act of 1976 (P.L. 94-455)* at 158, fn. 4. This report clarifies that “[i]t is not intended that legal action must have been brought against the guarantor in order to entitle him to take an otherwise available deduction; but there must be an enforceable legal obligation on his part to make payment.”

¹⁴ Reg. §1.166-9(d)(3). The regulations further state that an agreement is considered entered into before the obligation became totally or partially worthless if the taxpayer had a “reasonable expectation” at the time the taxpayer entered into the guaranty agreement that the taxpayer would not be called

upon to pay the debt without full reimbursement from the issuer of the obligation.

¹⁵ Reg. §1.166-9(e)(1). For purposes of this regulation, the term “reasonable consideration” includes not only direct consideration (such as cash or property), but also indirect compensation. *Id.*

¹⁶ J.C.T. REP. NO. JCS-33-76, *General Explanation of the Tax Reform Act of 1976 (P.L. 94-455)* at 158; *See also* H.R. REP. NO. 94-658, at 3069-3072 (Nov. 12, 1975).

¹⁷ Reg. §1.166-9(e)(2). *See also* Reg. §1.166-3(b), which provides that where a debt becomes “wholly worthless” during the taxable year the amount of such debt that has not been allowed as a deduction from gross income in any previous taxable year shall be allowed as a deduction in the current taxable year. *See also* Reg. §1.166-5(a)(2), which states that a loss on a nonbusiness debt shall be allowed “only if and when the debt has become

totally worthless," and no deduction shall be allowed for such any such debt that is recoverable in part during the taxable year.

- ¹⁸ Reg. §1.166-2(a); *See also* A. Serot, 68 TCM 1015, Dec. 50,199(M), TC Memo 1994-532 (stating that "[w]here a creditor takes collateral or otherwise secures a loan, there can be no worthlessness of the debt until the security itself becomes worthless.")
- ¹⁹ Reg. §1.166-2(b).
- ²⁰ Reg. §1.166-9(b); *See also* C.L. Fincher, 105 TC 126, 140, Dec. 50,859 (1995).
- ²¹ W.B. Gladstone, 59 TCM 53, Dec. 46,504(M), TC Memo 1990-173.
- ²² W.F. Bolt, DC-S.C., 80-2 USTC ¶9713.
- ²³ Black Gold Energy Corp., 99 TC 482, 488, Dec. 48,586 (1992) (*paraphrasing* the holding in *M. Putnam*, S Ct, 352 US 82, 57-1 USTC ¶9200, 77 S Ct 175).
- ²⁴ *Supra* note 22.
- ²⁵ R.W. Cox, CA-5, 95-2 USTC ¶50,595, 68 F3d 128. *See also* R.A. Read, 73 TCM 3000, Dec. 52,083(M), TC Memo 1997-262 (a bad debt case in which the court recognized that the taxpayer "could not have retrieved his pledged certificate of deposit from [the bank] because the certificate of deposit was collateral for the loan.")
- ²⁶ Black Gold Energy Corp., 99 TC 482, 486, Dec. 48,586 (1992).
- ²⁷ *Id.* at 487. *See also* B.A. Stratmore, CA-3, 70-1 USTC ¶9157, 420 F2d 461, 465 (explaining that "[i]t is not meaningful to em-

phasize unduly the common law principle of subrogation in analyzing the substantial realities upon which federal taxation is based. When the creditor turns to the guarantor for payment, the debt is already uncollectible.")

- ²⁸ *Intergraph Corp.*, 106 TC 312, 324, Dec. 51,337 (1996) (emphasis added).
- ²⁹ GA. CODE ANN. §10-7-56.
- ³⁰ Reg. §1.166-2(a).
- ³¹ Reg. §1.166-2(a).
- ³² Reg. §1.166-2(b).
- ³³ LTR 9441017 (July 07, 1994).
- ³⁴ *Id.*
- ³⁵ W.A. McFadden, 84 TCM 6, Dec. 54,803(M), TC Memo 2002-166, (citations omitted).
- ³⁶ *Mann Const. Co. Inc.*, 77 TCM 2098, Dec. 53,404(M), TC Memo 1999-183 (citations omitted).
- ³⁷ *Reading & Bates Corp.*, FedCl, 98-1 USTC ¶50,290 (citing *Minneapolis, St. Paul & Sault Ste. Marie Railroad Co.*, CtCls, 64-1 USTC ¶9213, 164 CtCls 226, 240).
- ³⁸ *American Offshore, Inc.*, 97 TC 579, 594-595, Dec. 47,750 (1991); *See also* M.J. Cole, CA-7, 89-1 USTC ¶9263, 871 F2d 64, 67.
- ³⁹ *American Offshore, Inc.*, 97 TC 579, 594-595, Dec. 47,750 (1991).
- ⁴⁰ R.J. Moore, DC-Va., 96-2 USTC ¶50,413, 943 FSupp 603, 622. *See also* G. Andrew, 54 TC 239, 245-246, Dec. 29,956 (1970); J.E. Mellen, 27 TCM 433, Dec. 28,970(M), TC Memo 1968-94.

- ⁴¹ *Mann Const. Co. Inc.*, 77 TCM 2098, Dec. 53,404(M), TC Memo 1999-183; *See also* H.C. Boler, 83 TCM 1879, Dec. 54,791(M), TC Memo 2002-155.
- ⁴² J. Diab, 39 TCM 561, Dec. 36,465(M), TC Memo 1979-475.
- ⁴³ *American Processing & Sales Co.*, CtCls, 67-1 USTC ¶9189, 371 F2d 842, 858.
- ⁴⁴ LTR 200453001 (Sep. 22, 2004).
- ⁴⁵ *See, e.g.,* G.L. Mann Est, CA-5, 84-1 USTC ¶9454, 731 F2d 267, 276; W.A. McFadden, 84 TCM 6, Dec. 54,803(M), TC Memo 2002-166 (stating that "[o]ur concern is whether petitioner exercised sound business judgment when he concluded the debt was worthless in 1995"); *PepsiAmericas, Inc.*, FedCl, 2002-1 USTC ¶50,326, 52 FedCl 41, 48; G.H. Flood, 81 TCM 1175, Dec. 54,247(M), TC Memo 2001-39 (explaining that "[a] debt becomes worthless in the tax year in which a creditor, using sound business judgment, abandons all reasonable hope of recovery on the basis of the available information regarding the surrounding circumstances of the debt"); *Mann Const. Co. Inc.*, 77 TCM 2098, Dec. 53,404(M), TC Memo 1999-183 (finding that the taxpayer's business judgment regarding worthlessness was "sound"); G. Andrew, 54 TC 239, 248, Dec. 29,956 (1970); H. Crown, 77 TC 582, 598, Dec. 38,251 (1981).
- ⁴⁶ *ABC Beverage Corp.*, 92 TCM 268, Dec. 56,620(M), TC Memo 2006-195.

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