John Breuner Co. v. Commissioner, 41 B.T.A. 567 (1942)

When a taxpayer elects to compute income from installment sales on the accrual basis for excess profits tax purposes, the normal tax net income used in calculating the adjusted excess profits net income (and thus the related tax credit) must also be computed on the accrual basis.

Summary

John Breuner Co., a furniture retailer, computed its income tax on the installment basis but elected to use the accrual basis for excess profits tax, as permitted by Section 736(a) of the Internal Revenue Code. The company then attempted to calculate its Section 26(e) income tax credit using its normal tax net income computed on the installment basis. The Board of Tax Appeals held that because the taxpayer elected to compute its excess profits tax liability on the accrual basis, its adjusted excess profits net income (and thus its Section 26(e) credit) had to be calculated using the accrual method as well, irrespective of whether excess profits taxes were ultimately paid.

Facts

John Breuner Co. sold furniture at retail, largely on the installment plan. For income tax purposes, it computed its net income on the installment basis under Section 44(a) of the Internal Revenue Code. For excess profits tax purposes, the company elected to compute its income on an accrual basis under Section 736(a), a relief provision enacted in 1942. This resulted in an adjusted excess profits net income of $9,032.04, but no excess profits tax due because of the 80% limitation in the statute.

Procedural History

The Commissioner initially disallowed a portion of the Section 26(e) credit claimed by the taxpayer. The taxpayer then argued it was entitled to a larger credit than originally claimed, based on using the installment method to calculate normal tax net income. The Commissioner amended his answer, arguing that no credit should be allowed because the taxpayer paid no excess profits tax. The Board of Tax Appeals reviewed the case to determine the proper amount of the Section 26(e) credit.

Issue(s)

1. Whether a taxpayer who elects to compute income from installment sales on the accrual basis for excess profits tax purposes can calculate the Section 26(e) income tax credit using normal tax net income computed on the installment basis.
2. Whether a taxpayer is entitled to a Section 26(e) credit based on its adjusted excess profits net income even if it did not pay any excess profits tax due to the 80% limitation.

Holding

1. No, because the election to compute excess profits tax on the accrual basis requires that all elements of the calculation, including normal tax net income, also be computed on the accrual basis.
2. Yes, because Section 26(e) provides a credit equal to the adjusted excess profits net income, regardless of whether the tax was actually imposed on that amount, except in four specific circumstances not applicable here.

Court’s Reasoning

The Board reasoned that allowing the taxpayer to use the installment basis for normal tax net income while using the accrual basis for excess profits tax would render the election under Section 736(a) meaningless. It emphasized that the term “normal-tax net income” as used in Section 711(a) does not always mean the income used for income tax purposes; it must be consistent with the method elected for excess profits tax. Regarding the Commissioner’s argument, the Board pointed to its own regulations and the language of Section 26(e) which indicated that the credit should be based on adjusted excess profits net income, irrespective of the actual tax paid, except in certain enumerated cases. The Board stated that the legislative intent of Section 26(e) was to provide a credit based on adjusted excess-profits net income, whether or not the tax was actually imposed on that amount.

Practical Implications

This case clarifies that an election under Section 736(a) to compute income on the accrual basis for excess profits tax purposes requires consistent application of the accrual method throughout the excess profits tax calculation, including the calculation of the Section 26(e) credit. It prevents taxpayers from selectively applying accounting methods to minimize their overall tax liability. Furthermore, the case confirms that the Section 26(e) credit is generally based on adjusted excess profits net income, even if no excess profits tax is ultimately paid, offering a specific interpretation of the statute that impacts tax planning in situations with similar statutory limitations.

