Ransohoffs, Inc. v. Commissioner, 9 T.C. 376 (1947)

A partnership can, by prior agreement, continue as the same entity for tax purposes even after the death of a partner, allowing a successor corporation to utilize the partnership's income history for excess profits tax credit calculations.

Summary

Ransohoffs, Inc. sought to compute its excess profits tax credit using the income method, relying on the earnings history of its predecessor partnership. The Commissioner argued that the death of a partner in 1938 dissolved the original partnership, creating a new entity and breaking the continuity required by the statute. The Tax Court held that the partnership agreement specifically provided for the continuation of the partnership after a partner's death, and such agreements are valid under California law and federal tax statutes. Therefore, the corporation could use the partnership's income history.

Facts

Ransohoffs, a family-owned business, operated as a partnership between Robert, James, and Howard Ransohoff. The partnership agreement, dated May 20, 1938, stipulated that the partnership would continue until the death of two partners. It further stated that upon the death of any partner, the surviving partners would continue the partnership under the same firm name, subject to the existing agreement. Howard Ransohoff died in October 1938. Subsequently, the business was incorporated as Ransohoffs, Inc. The corporation sought to calculate its excess profits tax credit using the income method, based on the partnership's historical earnings.

Procedural History

The Commissioner of Internal Revenue disallowed Ransohoffs, Inc.'s calculation of excess profits tax credit using the income method. The Commissioner contended that the partnership's continuity was broken by Howard's death. Ransohoffs, Inc. petitioned the Tax Court for review.

Issue(s)

Whether the death of Howard Ransohoff dissolved the original partnership, thereby precluding Ransohoffs, Inc. from using the partnership's income history to calculate its excess profits tax credit under the income method.

Holding

No, because the partnership agreement explicitly provided for the continuation of the partnership after the death of a partner, and such agreements are enforceable under California law and not prohibited by federal tax statutes.

© 2025 SCOTUSreports.com. All rights reserved.

Court’s Reasoning

The court emphasized that the key question was whether the partnership contract continued the partnership or merely the business after Howard’s death. The court found that the intent, as expressed in the partnership agreement, was to continue the family partnership. The agreement stated that “the partnership shall continue in existence until the death of two of the parties hereto * * *” and provided for the continuation by the survivors. The court cited California Civil Code section 2496, which allows for the continuation of a partnership after a partner’s death if provided for in the partnership agreement or with the consent of all members. The court distinguished between the general rule that death dissolves a partnership and the specific exception where the partners agree otherwise. The court also highlighted that Section 740 of the Internal Revenue Code is a remedial measure intended to allow corporations to benefit from the business experience of their predecessors and should be construed liberally. As such, the corporation could utilize the partnership’s income history.

Practical Implications

This case clarifies that a properly drafted partnership agreement can ensure the continuity of the partnership entity for tax purposes, even after the death or withdrawal of a partner. This is particularly relevant for businesses that later incorporate, as it allows the resulting corporation to take advantage of the partnership’s prior earnings history for tax benefits, such as calculating excess profits tax credits or other tax-related computations tied to past income. Attorneys drafting partnership agreements should explicitly include provisions for the continuation of the partnership upon the death or withdrawal of a partner to ensure the desired tax treatment. This case also reinforces the principle that remedial tax statutes should be interpreted liberally to achieve their intended purpose. Later cases have cited Ransohoffs for the principle that partnership agreements govern the continuity of a partnership for tax purposes, overriding general statutory provisions regarding dissolution upon death, when the agreement clearly expresses the intent to continue.

© 2025 SCOTUSreports.com. All rights reserved.