10 T.C. 191 (1948)

Under the World War II excess profits tax, a deduction is abnormal if it is different in kind from the taxpayer's typical deductions; however, the mere absence of a deduction in the taxable year that was present in the base period does not automatically make it abnormal.

Summary

Frank H. Fleer Corp. sought to reduce its excess profits tax liability for 1942 by arguing that certain deductions taken during the base period years (1936-1939) were abnormal and should be disallowed under Section 711(b)(1)(J) of the Internal Revenue Code. The disputed deductions included excise taxes on chewing gum, a bad debt from a failed business venture, and sales promotion expenses. The Tax Court held that the excise taxes were not an abnormal class of deduction, the bad debt was abnormal, and the sales promotion expenses were not separable enough from other sales expenses to be considered abnormal in amount. This case clarifies the criteria for determining abnormal deductions for excess profits tax purposes.

Facts

Frank H. Fleer Corp., a chewing gum manufacturer, paid excise taxes on its products from 1932 to June 1938, when the tax was repealed. In 1939, Fleer advanced funds to the Alexander Corporation, an advertising novelty producer, but wrote off the debt as worthless when Alexander's business faltered. Fleer also incurred various sales promotion expenses, including bonuses to jobbers' salesmen, premiums, and novelty advertising. These expenses fluctuated over the years.

Procedural History

The Commissioner of Internal Revenue determined a deficiency in Fleer's 1942 excess profits tax. Fleer contested this determination in the Tax Court, arguing that certain deductions from the base period years should be disallowed as abnormal under Section 711(b)(1)(J) of the Internal Revenue Code. The Tax Court partially agreed with Fleer, finding one deduction to be abnormal.

Issue(s)

1. Whether excise taxes on chewing gum, paid during part of the base period but not during the taxable year, constitute an abnormal class of deduction under Section 711(b)(1)(J)(i).
2. Whether a bad debt, resulting from a transaction not directly connected with the taxpayer's business, is an abnormal class of deduction under Section 711(b)(1)(J)(i).
3. Whether sales promotion expenses are separable from other sales expenses for the purpose of determining abnormality in amount under Section 711(b)(1)(J)(ii).

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Holding

1. No, because deductions of that class were not abnormal for the taxpayer.
2. Yes, because the bad debt resulted from a transaction not directly connected with the business.
3. No, because, in this case, the sales promotion expenses were not sufficiently distinct from the other expenses.

Court’s Reasoning

The court reasoned that the excise taxes were not an abnormal class of deduction because Fleer paid such taxes regularly during the years 1932-1938. The court emphasized that while Congress intended Section 711(b)(1)(J) to permit taxpayers to eliminate unusual deductions from the base period, it did not follow that every deduction of a base year which does not have a counterpart in the excess profits tax year shall be disallowed. As to the bad debt, the court found it to be an abnormal deduction because it arose from a transaction distinct from Fleer’s ordinary business operations (sales to customers). The court stated that “*t*he evidence fairly preponderates in favor of the petitioner’s contention that a deduction of this kind was abnormal for the petitioner.” Regarding sales promotion expenses, the court found that these expenses were too intertwined with other sales expenses to be separately classified. All expenditures connected with selling, were made to sell the petitioner’s product, and the purpose of each was closely related to that of every other one. The court emphasized the need for a

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