## *10 T.C. 600 (1948)*

When a corporation elects to compute income from long-term contracts using the percentage of completion method for excess profits tax purposes, that method must be used for all calculations within the excess profits tax provisions, including the 80% limitation.

### Summary

Basalt Rock Co. elected to use the percentage of completion method for reporting income from its long-term contracts for excess profits tax purposes, while regularly using the completed contract method for income tax. The Tax Court addressed whether the corporation's surtax net income for the 80% limitation on excess profits tax should be computed using the percentage of completion or the completed contract method. The court held that the election to use the percentage of completion method applied to all aspects of the excess profits tax computation, including the 80% limitation.

### Facts

Basalt Rock Co. was a California corporation engaged in shipbuilding and manufacturing. It regularly used the completed contract method for its long-term contracts when filing its federal income and declared value excess profits tax returns. However, when filing its excess profits tax return for 1942, the company elected to compute its income from long-term contracts using the percentage of completion method, as permitted by Section 736(b) of the Internal Revenue Code.

### Procedural History

The Commissioner of Internal Revenue determined a deficiency in Basalt Rock's excess profits tax liability. Basalt Rock disputed the deficiency and claimed an overpayment. All issues were settled except whether the surtax net income for the 80% limitation should be computed using the percentage of completion or the completed contract method. The Tax Court heard the case.

### Issue(s)

Whether, for purposes of the 80% limitation provided in Section 710(a)(1)(B) of the Internal Revenue Code, Basalt Rock's surtax net income should be computed according to the percentage of completion method or the completed contract method, given its election under Section 736(b) to report income from long-term contracts on the percentage of completion method.

### Holding

Yes, because the election to use the percentage of completion method for long-term contracts applies to all calculations within the excess profits tax provisions, including the computation of the corporation surtax net income for the 80% limitation under Section 710(a)(1)(B).

## Court’s Reasoning

The Tax Court reasoned that Section 736(b) specifically allows a taxpayer to elect the percentage of completion method for purposes of the excess profits tax subchapter (Subchapter E of Chapter 2). The court emphasized that the election, once made, is irrevocable and applies to all contracts. The court relied heavily on the regulatory interpretation of the statute, finding it neither unreasonable nor inconsistent with the statutory language. The court stated, “The only reasonable interpretation of the statute, in our view, requires the use of the basis elected, for *every* purpose of subchapter E of chapter 2.” The Court emphasized that the term “corporation surtax net income, computed under section 15” did not preclude using the percentage of completion basis, as Section 15 itself allows for different accounting methods. The Court referenced prior cases like *Kimbrell’s Home Furnishings, Inc. v. Commissioner* to underscore the need for consistency in applying the elected accounting method for all excess profits tax calculations. Dissenting opinions argued that the statute clearly dictates using the actual corporation surtax net income for the 80% limitation, as computed under Chapter 1, and that the regulation was an invalid expansion of the statute.

## Practical Implications

This case clarifies that taxpayers electing a specific accounting method for long-term contracts under Section 736(b) must consistently apply that method throughout all calculations related to the excess profits tax, including limitations and credits. This decision emphasizes the importance of carefully considering the ramifications of such an election, as it affects not only the calculation of excess profits net income but also any limitations based on corporation surtax net income. Later cases would rely on this decision to enforce consistency in accounting methods within the complex framework of the excess profits tax.

 