14 T.C. 97 (1950)

A taxpayer seeking relief from excess profits taxes due to a depressed industry must prove that its average base period net income is an inadequate standard of normal earnings and that the depression stemmed from temporary economic events unusual for that industry.

Summary

Harlan Bourbon and Wine Company, a Kentucky wholesale liquor dealer, sought relief from excess profits taxes for 1941-1943 under Section 722(b)(2) of the Internal Revenue Code, arguing that a price war depressed its base period earnings. The Tax Court denied relief, holding that Harlan Bourbon failed to demonstrate that its average base period net income was an inadequate measure of normal earnings or that the liquor industry experienced a depression due to temporary economic events unusual for the industry. The court emphasized that increased competition and business fluctuations are normal and do not automatically qualify for relief.

Facts

Harlan Bourbon and Wine Company, established in 1934, operated as a wholesale liquor dealer in Kentucky. Following the repeal of Prohibition, Kentucky legalized liquor manufacturing and sales, leading to a surge of new businesses. The market initially saw high sales due to initial stocking by retailers and demand from neighboring states where liquor sales were not yet legal. As the market matured and supply increased, profit margins decreased due to competition, particularly from warehouse receipt sales that allowed retailers to bottle and sell liquor under their own labels at lower prices.

Procedural History

Harlan Bourbon filed applications for relief from excess profits taxes for 1941, 1942, and 1943, which were rejected by the Commissioner of Internal Revenue. The Commissioner also determined a deficiency in excess profits tax for 1943. Harlan Bourbon petitioned the Tax Court, contesting the disallowance of its claims for relief under Section 722 of the Internal Revenue Code.

Issue(s)

1. Whether Harlan Bourbon’s average base period net income was an inadequate standard of normal earnings.
2. Whether the alleged depression in Harlan Bourbon’s business resulted from temporary economic events unusual in the liquor industry.

Holding

1. No, because Harlan Bourbon’s average base period net income, as adjusted by

© 2025 SCOTUSreports.com. All rights reserved.

the Commissioner, was comparable to industry averages and represented a reasonable return on net worth.
2. No, because increased competition and business fluctuations were considered normal conditions in the liquor industry, not temporary economic events unusual to the industry.

Court's Reasoning

The Tax Court reasoned that Harlan Bourbon failed to prove that its average base period net income was an inadequate standard of normal earnings. The court highlighted that the high profits in the initial years after Prohibition were unsustainable and that the subsequent decline was a normal market correction. The court noted that the Commissioner's adjustments resulted in an average base period net income that was approximately 20% of Harlan Bourbon's net worth, a figure comparable to the industry average. The court stated that fierce competition, even leading to business failures, did not constitute a temporary economic event unusual in the industry. The court emphasized that Treasury Regulations 112, section 35.722-3(b) recognizes that a ruinous price war may be a temporary economic event unusual in the case of the industry and constitute a basis for relief under section 722 (b) (2). On the other hand, competition can not be considered a temporary economic event unusual in the case of a taxpayer or its industry, as competition is a normal factor in almost any business. The court found that Harlan Bourbon had not proven that a "ruinous price war," as distinguished from keen competition, depressed the industry of which petitioner was a member in the base period years. Further, the court found that they did not establish

© 2025 SCOTUSreports.com. All rights reserved.