Douglas Hotel Co. v. Commissioner, T.C. Memo. 1956-242

Property donated to a corporation by a non-stockholder is includible in the corporation's equity invested capital for excess profits tax purposes, and the basis for valuation is the fair market value of the property at the time of acquisition, not its value enhanced by its intended use.

Summary

Douglas Hotel Company sought to include land donated to it as part of its invested capital for excess profits tax calculations. The land was donated by a non-stockholder for the specific purpose of building a hotel. The Tax Court addressed whether this donated land qualified as a contribution to capital and, if so, at what value it should be included. The court held that the donated land was indeed a contribution to capital and should be included in invested capital. However, the court determined that the land's value should be based on its fair market value at the time of donation, not inflated by its intended use as a hotel site or the potential income from a lease agreement.

Facts

In 1913, Mr. Brandéis donated land to Douglas Hotel Company as a site for a hotel.

The deed was delivered and recorded in March 1913, although executed in January 1913.

The company sought to include this land in its invested capital for excess profits tax purposes, valuing it at $246,275, based on the par value of stock they claimed was issued for it.

The Commissioner determined the land's value to be no more than $125,000 and reduced the invested capital accordingly.

The company had also made cash withdrawals, which the Commissioner determined were not from accumulated earnings and profits, further reducing invested capital.

Procedural History

The Commissioner issued a notice of deficiency, reducing Douglas Hotel Company's invested capital for excess profits tax purposes.

Douglas Hotel Company petitioned the Tax Court, contesting the Commissioner's valuation of the donated land and the reduction for cash withdrawals.

The Tax Court heard the case to determine the proper inclusion of the donated land in invested capital and the treatment of cash withdrawals.

Issue(s)

1. Whether land donated to a corporation by a non-stockholder as a hotel site is includible in the corporation's equity invested capital for excess profits tax purposes as a contribution to capital?

2. If the donated land is includible, what is the proper basis for determining its value for inclusion in invested capital: the fair market value at the time of acquisition, or a value reflecting its intended use and potential income?

3. Whether cash withdrawals made by the sole stockholder were properly excluded from accumulated earnings and profits, thus reducing the equity invested capital?

4. Whether the taxpayer is exempt from excess profits tax under Section 727(g)(2) of the Internal Revenue Code?

Holding

1. Yes, because the Supreme Court in *Brown Shoe Co. v. Commissioner*, 339 U.S. 583, held that property donated to a corporation by non-stockholders is includible in equity invested capital as a contribution to capital.

2. The proper basis is the fair market value at the time of acquisition, because the court found the donation was not in exchange for stock, and the value should not be inflated by its intended use or potential lease income.

3. Yes, because the evidence showed the withdrawals were from a depreciation reserve and the corporation had no accumulated earnings and profits from which distributions could have been made.

4. No, because the corporation did not meet the requirement of deriving 95% or more of its gross income from sources outside the United States, as required by Section 727(g)(1).

Court's Reasoning

Inclusion of Donated Land: The court relied on *Brown Shoe Co. v. Commissioner*, stating, "On authority of that case we hold that the land deeded to petitioner by Brandéis for the hotel site in 1913 is includible in petitioner's equity invested capital as a contribution to capital under section 718 (a) (2), Internal Revenue Code."