14 T.C. 1312 (1950)

To qualify for excess profits tax relief under Section 722(b)(2) of the Internal Revenue Code, a taxpayer must demonstrate that its base period earnings were depressed due to temporary economic circumstances unusual to the taxpayer or its industry.

Summary

Winter Paper Stock Co. sought relief from excess profits tax for 1943, arguing its base period earnings (1936-1939) were depressed by a "price war" instigated by a competitor. The Tax Court denied relief, finding Winter Paper failed to prove its average base period net income was an inadequate standard of normal earnings or that its business was depressed due to temporary economic events unusual for its industry. The court reasoned intense competition, even if driven by a competitor's animosity, did not constitute a temporary and unusual economic event under Section 722(b)(2).

Facts

Winter Paper Stock Co., an Ohio corporation, collected, graded, and sold waste paper. A competitor, National Waste Material Co., entered the Cleveland market in 1925. From 1936-1939, National's president, harboring a grudge against Winter Paper, instructed his solicitors to offer higher prices to Winter Paper's customers. Winter Paper contended this created a "price war," depressing its earnings during the base period. The price for waste paper fluctuated wildly from month to month and year to year.

Procedural History

Winter Paper filed an application for relief under Section 722 of the Internal Revenue Code, seeking an increase in its excess profits credit. The Commissioner of Internal Revenue rejected the application and disallowed the claim for refund. Winter Paper petitioned the Tax Court for review, contesting the disallowance of relief under Section 722(b)(2).

Issue(s)

Whether the Commissioner erred in disallowing Winter Paper's application for excess profits tax relief under Section 722(b)(2) of the Internal Revenue Code, because its business was depressed in the base period due to temporary economic circumstances unusual to the taxpayer or its industry.

Holding

No, because Winter Paper failed to demonstrate that its base period earnings were depressed due to temporary economic circumstances unusual to itself or the waste

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paper industry; the intense competition was not considered a temporary and unusual event under the statute.

Court’s Reasoning

The Tax Court applied Section 722(b)(2) of the Internal Revenue Code, which allows excess profits tax relief if a taxpayer’s base period net income is an inadequate standard of normal earnings due to business depression caused by temporary economic circumstances unusual to the taxpayer or its industry. The court found that while National’s actions may have increased Winter Paper’s costs, this resulted from intense competition, not a temporary economic event. Active competition is a normal business factor, not a temporary or unusual circumstance. The court noted that the alleged “price war” had been ongoing since 1929, making it difficult to characterize the conditions as temporary. Furthermore, Winter Paper’s tonnage increased during the period, undermining the claim of significant depression. The court concluded that the price practices were part of the regular economic climate and not a temporary or unusual occurrence.

Practical Implications

This case clarifies the high burden of proof required to obtain excess profits tax relief under Section 722(b)(2). Taxpayers must demonstrate a clear causal link between a truly temporary and unusual economic event and the depression of their base period earnings. Intense competition, even if aggressive or fueled by animosity, is generally considered a normal business risk, not a qualifying event for tax relief. To establish eligibility for relief, a taxpayer needs to provide compelling evidence that the economic circumstances were both temporary and distinctly unusual compared to normal cyclical business fluctuations or competitive pressures. The case emphasizes that ongoing conditions, even if unfavorable, are unlikely to be deemed temporary.

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