*17 T.C. 1199 (1952)*

To qualify for excess profits tax relief under Section 722(b)(1) due to a business interruption, a taxpayer must demonstrate that the interruption resulted in an inadequate standard of normal earnings compared to the invested capital method and prove the constructive average base period net income would result in a greater excess profits credit.

**Summary**

D. L. Auld Company sought relief under Section 722(b)(1) of the Internal Revenue Code, claiming a strike in 1936 significantly impacted its earnings during the base period (1937-1940). The company argued that the strike caused loss of dies, trained personnel, and contracts, making its excess profits tax excessive. The Tax Court denied relief, holding that while the strike did interrupt production, the company failed to prove that its constructive average base period net income, absent the strike, would result in a higher excess profits credit than the credit already computed using the invested capital method. The court emphasized that the company's production and operation returned to normal levels after the initial impact of the strike.

**Facts**

D. L. Auld Company, an Ohio corporation, manufactured metal trim for the automotive and appliance industries. A strike began on October 19, 1936, closing the plant until November 12, 1936, and ending completely in December 1936. Automotive customers removed their dies from the plant due to the strike. The company's excess profits credits were computed under the invested capital method for the fiscal years 1941, 1942, and 1943. The company applied for relief under Section 722, claiming the strike caused significant financial losses during the base period years (1937-1940), which resulted in negative net income for those years.

**Procedural History**

The D. L. Auld Company filed income and excess profits tax returns for the fiscal years ending June 30, 1941, 1942, and 1943. In September 1943 and August 1944, the company applied for relief under Section 722, which was disallowed by the Commissioner of Internal Revenue on June 9, 1948, resulting in determined deficiencies. The company then petitioned the Tax Court contesting the disallowance.

**Issue(s)**

Whether the Commissioner erred in disallowing the petitioner's application for relief under Section 722(b)(1) of the Internal Revenue Code for the fiscal years ending June 30, 1941, June 30, 1942, and June 30, 1943, based on the argument that a strike in 1936 caused an inadequate standard of normal earnings during the base

© 2025 SCOTUSreports.com. All rights reserved. 

period.

## Holding

No, because the petitioner failed to demonstrate that the average base period net income, if normal production had not been interrupted by the strike, would result in an excess profits credit greater than that already computed on the basis of invested capital.

## Court’s Reasoning

The Tax Court reasoned that to qualify for relief under Section 722(b)(1), the petitioner had to show the 1936 strike interrupted or diminished normal production in one or more base period years and that the constructive average base period net income (absent the strike) would result in a greater excess profits credit than that computed on the invested capital basis. While the strike did interrupt production in the fiscal year ending in 1937, evidence showed the company’s operations returned to normal levels in subsequent years. The court noted that while the company sustained losses during the base period, there was insufficient evidence linking these losses directly to the strike, as opposed to other factors like increased competition and decreased overall automobile production. The court also considered the statements of the company’s officers at stockholder and director meetings, which indicated a general slump in business and competitive pressures, not solely the lingering effects of the strike. The court stated that the language of the statute does not refer to an event which only affects the profit-making ability of the corporation without affecting production.

## Practical Implications

This case illustrates the high burden of proof required to obtain excess profits tax relief under Section 722(b)(1) due to business interruptions. Taxpayers must provide concrete evidence demonstrating a direct causal link between the interrupting event and the inadequacy of their average base period net income. It emphasizes the importance of substantiating claims with production data and distinguishing the impact of the interrupting event from other market forces affecting profitability. The case underscores that a temporary interruption alone is insufficient; the taxpayer must prove lasting, quantifiable effects on their earnings potential and the inadequacy of their excess profits credit. Later cases applying this ruling often focus on the degree to which the taxpayer can isolate the impact of a specific event from broader economic trends.

© 2025 SCOTUSreports.com. All rights reserved. 