17 T.C. 1364 (1952)

A taxpayer is not entitled to relief under Section 722 of the Internal Revenue Code if its proposed excess profits tax credit under the income method is smaller than the credit actually allowed under the invested capital method.

Summary

Block One Thirty-Nine, Inc. petitioned the Tax Court for relief from excess profits taxes under Section 722(c)(3) of the Internal Revenue Code, arguing its invested capital was abnormally low. The Tax Court denied relief, holding that even if the petitioner qualified for relief under Section 722(c)(3), it failed to prove a constructive average base period net income that would result in a larger excess profits tax credit than what was already allowed under the invested capital method. The court emphasized that merely proving eligibility for relief is insufficient; the taxpayer must demonstrate that the proposed income method yields a greater credit.

Facts

Block One Thirty-Nine, Inc. was formed in 1941 to acquire downtown properties in Houston, Texas, largely from related entities. Its capital stock was $1,000. The company obtained a $4,170,000 loan commitment from Equitable Life Assurance. The company computed its excess profits credit using the invested capital method. The Commissioner determined deficiencies in the company's excess profits taxes but the company argued it was entitled to relief under Section 722 because its invested capital was abnormally low.

Procedural History

Block One Thirty-Nine, Inc. filed applications for relief under Section 722, which were denied by the Commissioner. The company then petitioned the Tax Court, contesting the Commissioner's denial of relief. The Tax Court consolidated multiple dockets related to different tax years. The Tax Court ruled against the petitioner, sustaining the Commissioner's denial of relief.

Issue(s)

Whether Block One Thirty-Nine, Inc. is entitled to relief from excess profits taxes under Section 722(c)(3) of the Internal Revenue Code because its invested capital was abnormally low, and whether it established a constructive average base period net income that would result in a larger excess profits tax credit than what was already allowed under the invested capital method.

Holding

No, because even assuming the company qualified for relief under Section 722(c)(3),

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it failed to demonstrate that using a constructive average base period net income would result in a larger excess profits tax credit than the credit already determined under the invested capital method.

Court's Reasoning

The Tax Court emphasized that to qualify for relief under Section 722, a taxpayer must not only prove eligibility under one of the specified grounds but also establish a constructive average base period net income that yields a larger excess profits credit than the invested capital method. The court found that Block One Thirty-Nine's proposed constructive average base period net income, even if accepted, would result in a smaller credit than the one already allowed. The court noted the company seemed to object to the statutory treatment of interest under the invested capital method (where the interest deduction is reduced), but the court found the Commissioner correctly applied the statutory requirements. Citing *Danco Co.*, the court stated, "The mere existence of the qualifying features of section 722 (c) does not establish a taxpayer's right to relief. The petitioner must further demonstrate the inadequacy of its excess profits credit based upon invested capital by establishing under section 722 (a) a fair and just amount representing normal earnings to be used as a constructive average base period net income."

Practical Implications

This case clarifies the burden of proof for taxpayers seeking relief from excess profits taxes under Section 722 of the Internal Revenue Code. It reinforces that merely demonstrating eligibility under one of the qualifying conditions is insufficient. Taxpayers must also prove that the alternative method they propose (using a constructive average base period net income) would result in a greater excess profits credit than the standard invested capital method. This decision highlights the importance of thoroughly documenting and substantiating the claimed constructive average base period net income to ensure it provides a tangible benefit in terms of tax relief. The case also illustrates the importance of presenting all relevant facts and arguments to the Commissioner during the administrative phase, as the Tax Court is unlikely to consider new arguments raised for the first time during litigation. Later cases have cited this decision for its articulation of the requirements for obtaining relief under Section 722.

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