18 T.C. 1255 (1952)

For excess profits tax purposes, the amount included in equity invested capital when a corporation issues stock for property is generally the cost of the property to the corporation, but this rule is subject to exceptions, particularly where the transfer qualifies as a tax-free reorganization.

Summary

Bard-Parker Co. involved a dispute over the proper calculation of equity invested capital for excess profits tax purposes. The Tax Court addressed whether the par value of common stock issued by the petitioner for assets, goodwill, and patents should be included in its equity invested capital. The court held that the transfer of assets from the old corporation to the new one constituted a tax-free reorganization, meaning the petitioner's basis in those assets was the same as the old corporation's. The court also determined the value of patents paid in for stock, which was used as the cost basis of the patents for inclusion within equity invested capital.

Facts

An old corporation, Bard-Parker Company, manufactured surgical knives and blades. To expand into manufacturing detachable-blade scissors, a plan was devised involving the creation of a new corporation (the petitioner). The old corporation's assets, goodwill, and corporate name were transferred to the petitioner in exchange for stock. Separately, Morgan Parker, an inventor and stockholder, transferred scissors patents to the petitioner for additional stock. The Commissioner challenged the petitioner's inclusion of the full par value of the stock issued for these assets in its equity invested capital.

Procedural History

The Commissioner of Internal Revenue determined deficiencies in the petitioner's excess profits taxes for the years 1941-1944. The Bard-Parker Company, Inc. (the new corporation) petitioned the Tax Court for a redetermination of these deficiencies. The primary issue was the determination of equity invested capital.

Issue(s)

1. Whether the transfer of assets, goodwill, and the corporate name from the old Bard-Parker Company to the petitioner constituted a tax-free reorganization.
2. Whether the transfer of scissors patents from Morgan Parker to the petitioner qualified for non-recognition of gain or loss under Section 112(b)(5) of the Revenue Act of 1928.
3. What is the cost basis of the patents paid in for stock, for use as the cost basis of the patents for inclusion within equity invested capital?

Holding

1. Yes, because the transfer met the definition of a reorganization under Section 112(i)(1)(B) of the Revenue Act of 1928, as the old company’s assets were transferred for petitioner’s stock, and immediately after, control of the new company was vested in the stockholders of the old company.
2. No, because Morgan Parker did not have the requisite 80% control of the petitioner corporation immediately after the exchange to qualify under Section 112(b)(5).
3. The fair market value in 1930 of the scissors patents transferred to the petitioner, was $300,000.

Court’s Reasoning

The court reasoned that the transfer of assets from the old company to the petitioner constituted a reorganization. The court emphasized that "[t]he parts of a reorganization must be considered as a whole rather than separately", citing *Helvering v. Alabama Asphaltic Limestone Co., 315 U.S. 179*. Because the transfer was part of a reorganization where no gain or loss was recognized, the petitioner’s basis in the assets was the same as the old company’s basis, under Section 113(a)(7) of the Internal Revenue Code. Regarding the transfer of patents, the court found that Section 112(b)(5) did not apply because Morgan Parker did not control the petitioner after the transfer. Therefore, the petitioner’s basis in the patents was its cost, which the court determined to be the fair market value of the stock issued in exchange for the patents. The court, considering all factors, determined the fair market value of the scissors patents to be $300,000.

Practical Implications

This case clarifies how to determine the basis of assets acquired in a reorganization for excess profits tax purposes. It highlights the importance of determining whether a transfer qualifies as a tax-free reorganization, as this significantly impacts the basis of the assets acquired. Specifically, it demonstrates that if a transaction qualifies as a reorganization, the acquiring corporation takes the transferor’s basis in the assets. The case also reinforces that the fair market value of assets, not the par value of stock, determines the cost basis when stock is issued for property in a non-recognition transaction. Legal practitioners must carefully analyze the steps of complex corporate restructurings to determine whether they meet the statutory definition of a tax-free reorganization, which in turn will govern the basis of the acquired assets.

