Constitution Publishing Co. v. Commissioner, 20 T.C. 1028 (1953)

When calculating capital gains on the sale of property acquired before March 1, 1913, the fair market value on that date can be used for land, while the adjusted cost basis can be used for buildings, even when sold as a single unit.

<p>Summary</p>

The Constitution Publishing Company purchased land and a building in 1899. In 1948, it sold the property. The company sought to use the fair market value of the land as of March 1, 1913, and the adjusted cost basis for the building to calculate the capital gain. The Tax Court held that the company could use different bases for the land and building. The court reasoned that, for tax purposes, the land and building could be treated as separate assets, allowing the company to take advantage of the higher valuation method for each component to determine capital gains.

<p>Facts</p>

In 1899, Constitution Publishing Co. purchased land and a building in Atlanta for $125,000. The company allocated $25,000 to the land and $100,000 to the building. Significant improvements were made to the building before March 1, 1913. Depreciation was taken on the building before and after March 1, 1913. The fair market value of the land and building on March 1, 1913, was determined to be $58,000 and $56,550, respectively, by the Atlanta Real Estate Board. The property was sold in 1948 for $185,769.25. Constitution merged with Atlanta Journal Company to form Atlanta Newspapers, Inc., in 1950.

<p>Procedural History</p>

Constitution Publishing Company filed its 1948 tax return, reporting a capital gain from the sale of the property. The Commissioner of Internal Revenue determined a higher gain. The Tax Court reviewed the case to determine the proper basis for calculating the capital gain, considering the fair market value of the land and the adjusted cost basis of the building as of March 1, 1913. The Tax Court ruled in favor of the taxpayer, leading to a recomputation under Rule 50.

<p>Issue(s)</p>

1. Whether Constitution was entitled to use the fair market value as of March 1, 1913, for the land and the adjusted cost basis for the building when calculating capital gains from the sale of the property.

<p>Holding</p>

1. Yes, because the court found sufficient justification to treat the land and building

as separate assets, allowing the application of the basis that yields the maximum value for each in computing capital gain.

<p>Court's Reasoning</p>

The court referenced Kinkead v. United States, noting that common law typically treated land and its improvements as a single asset, but this was not always applicable for federal taxation. It emphasized that the IRS allowed separate treatment of land and buildings for depreciation purposes because land is not depreciable. The court also stated that “the law of taxation deals with realities,” and that to force the use of a single basis for both assets would be “unrealistic and a distortion of the meaning” of the relevant tax code. The Court found that the petitioner owned two separate assets, land and building, and the IRS had no basis to merge them into one to compute gain. The Court recognized the appraisals of the Atlanta Real Estate Board as credible evidence of the fair market value of the land and building.

Practical Implications</p>

This case is crucial for taxpayers who owned property before March 1, 1913, as it allows them to use the fair market value from that date to determine the basis for capital gains on the sale of the land. It established that, even when selling property as a whole, components like land and buildings can be treated separately for tax purposes, allowing for a more favorable capital gains calculation. This impacts how property sales involving pre-1913 assets are structured and how valuations are conducted. It emphasizes the importance of obtaining expert appraisals to establish fair market values as of the critical date.

