The Fair Store, Inc. v. Commissioner, 20 T.C. 289 (1953)

To qualify for relief under the excess profits tax regulations due to a depressed business, a taxpayer must demonstrate that the depression resulted from temporary economic circumstances unusual for that specific business, not merely from poor business decisions or general market conditions.

Summary

The Fair Store, Inc. sought relief from excess profits taxes, claiming its business was depressed during the base period due to the failure of a refinancing plan and other factors. The Tax Court denied relief, finding that the business's poor performance was not due to temporary, unusual economic circumstances as required by the statute. Instead, the court determined the decline resulted from poor management decisions, unwise business policies, and general market competition. The court emphasized that the refinancing failure was not due to a unique circumstance but to the general state of the stock market. The court also found the taxpayer changed the character of its business by acquiring additional stores.

Facts

The Fair Store, Inc. (taxpayer) acquired two department stores and contracted to purchase a third. The purchase was contingent on securing $3 million in preferred stock financing. The taxpayer's financing failed due to a downturn in the stock market. The taxpayer also adopted a "no-profit plan" and "share-the-profit plan," and reduced inventory. The taxpayer's business declined during the base period (1936-1939). The taxpayer's owners had no prior experience in running a department store. The Taxpayer sought relief under section 722(b)(2) and 722(b)(4) of the Internal Revenue Code for excess profits tax relief. The Commissioner of Internal Revenue denied relief.

Procedural History

The case was heard before the United States Tax Court. The Tax Court reviewed the Commissioner's denial of the taxpayer's claims for relief under Section 722 of the Internal Revenue Code of 1939.

Issue(s)

1. Whether the taxpayer's business was depressed due to temporary economic circumstances unusual in the taxpayer's case, entitling it to relief under section 722(b)(2).

2. Whether the taxpayer changed the character of its business entitling it to relief under section 722(b)(4).

Holding

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1. No, because the failure to secure refinancing and business depression resulted from general economic conditions and poor business decisions, not from unusual circumstances.

2. Yes, because acquiring new stores and changing business policies constituted a change in the business's character.

Court's Reasoning

The court analyzed the requirements for excess profits tax relief. The court determined that the refinancing failure was not due to a unique circumstance but to the general state of the stock market. The court found that the downturn in the stock market that prevented the refinancing was not a "temporary economic circumstance unusual in the case of the taxpayer." The court cited cases holding that the statute was not meant to counteract bad business decisions or unwise policies. The Court noted the taxpayer's decision to buy additional stores, lack of experience, and unwise business policies. The court emphasized that the taxpayer's management had made a series of poor decisions, including adopting a "no-profit plan" and reducing inventory at the wrong time. The court concluded that the taxpayer failed to prove any "factor affecting the taxpayer's business which may reasonably be considered as resulting in an inadequate standard of normal earnings." The court held that the taxpayer's business changed with the acquisition of two additional stores.

Practical Implications

This case is a good example of the stringent requirements of extraordinary circumstances needed to gain relief from excess profits tax. Attorneys handling similar cases must: prove the existence of genuine, temporary, and unusual economic conditions specific to the taxpayer, showing that poor business decisions or general market downturns are not enough to trigger the relief. The court's emphasis on unusual circumstances means that a taxpayer needs to establish a clear nexus between external, unusual events and a demonstrable negative impact on their business performance. The case also highlights the importance of solid financial records. Later cases dealing with similar tax code provisions may cite *The Fair Store, Inc.* to emphasize the need for demonstrating unusual circumstances, rather than poor management or market conditions, to get excess profits tax relief.

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