United Mail Order House v. Commissioner of Internal Revenue, 27 T.C. 534 (1956)

To qualify for excess profits tax relief under Section 722(b)(4) of the Internal Revenue Code, a taxpayer must demonstrate a substantial change in the character of its business during the base period, which significantly impacted its earning potential, and provide a sound basis for reconstructing base period earnings.

Summary

The United States Tax Court denied United Mail Order House's claims for excess profits tax relief, holding that the company failed to prove a substantial change in its business's character during the base period (1936-1939). The company argued that moving to a larger office, acquiring client accounts from competitors, and expanding service offerings constituted qualifying changes. However, the court found insufficient evidence that these actions significantly increased the company's earning capacity or provided a reliable method to reconstruct base period earnings to justify relief. The court emphasized that any changes had to have a substantial impact on earnings.

Facts

United Mail Order House operated a merchandise bulletin and resident buying service. During the base period, the company: (1) moved to a larger office space; (2) acquired client accounts through agreements with former competitors; (3) expanded services by offering new services like "unit inventory control" and R.A.D. promotion; and (4) entered into an agreement with another company to share office space and facilities for a fee. The company sought relief under Section 722(b)(4) for excess profits tax liabilities from 1941 to 1945, arguing these changes substantially increased its earning potential.

Procedural History

The Commissioner of Internal Revenue disallowed United Mail Order House's claims for excess profits tax relief for the years 1941-1945. The company then petitioned the United States Tax Court, seeking a review of the Commissioner's decision. The Tax Court considered the evidence, including the company's activities and financial records, and rendered a decision in favor of the Commissioner.

Issue(s)

1. Whether the petitioner's move to a larger office constituted a "change in the character" of its business under Section 722(b)(4)?
2. Whether acquiring client accounts from competitors constituted a "change in the character" of its business?
3. Whether the expansion of service offerings constituted a "change in the character" of its business?

© 2025 SCOTUSreports.com. All rights reserved. 

4. Whether the agreement to share office space constituted a “change in the character” of its business?
5. If any of the above constituted a change in the character of business, did it result in a constructive average base period net income that would justify relief under Section 722?

Holding

1. No, because the company failed to demonstrate a direct link between the larger office and increased earnings.
2. Potentially yes, the court assumed this was a qualifying change, but it didn’t lead to excess profit credit.
3. No, because the expansions were not substantial enough to be qualifying.
4. Potentially yes, the court assumed this was a qualifying change, but it didn’t lead to excess profit credit.
5. No, because the petitioner failed to establish a constructive average base period net income of sufficient magnitude to warrant the relief sought.

Court's Reasoning

The court applied the principles of Section 722 of the 1939 Internal Revenue Code, focusing on whether the company’s actions during the base period represented a

© 2025 SCOTUSreports.com. All rights reserved. 