31 T.C. 777 (1959)

To qualify for relief under Section 722(b)(2) of the Internal Revenue Code, a taxpayer must demonstrate that its business was depressed during the base period due to temporary economic circumstances that were unusual in the taxpayer's case, and that depression cannot be attributed to normal business competition.

Summary

In this case, the United States Tax Court addressed whether Blue Diamond Coal Company was entitled to relief from excess profits taxes under Section 722 of the Internal Revenue Code of 1939. The company argued it was entitled to relief under Section 722(b)(2) because its business was depressed during the base period due to increased labor costs from unionization, while the value of its coal did not increase proportionately. The court determined that the company's situation was primarily due to competitive market conditions, which the court deemed to be a normal business hazard rather than a temporary and unusual economic circumstance. The court also considered whether the company's properties were "in operation" during strike periods for the purpose of calculating the exempt excess output under Section 735, deciding they were not. The court held that Blue Diamond Coal Company did not qualify for relief under Section 722(b)(2) and that the strike periods should be excluded.

Facts

Blue Diamond Coal Company (the "taxpayer") was in the business of mining and selling bituminous coal. The taxpayer's primary argument was that it was entitled to relief under Section 722(b)(2) of the Internal Revenue Code because of its increased labor costs, due to unionization, during the base period (1936-1939), which were not matched by a corresponding increase in the value of its coal at the mine. The labor cost during the 1936-1939 base period was 65.54% of the company's revenues, as compared to 58.31% during 1922-1935. The taxpayer also maintained that the mines were in operation during periods of strikes in the base period. The Commissioner of Internal Revenue (the "Commissioner") denied relief, and the Tax Court upheld the Commissioner's decision.

Procedural History

Blue Diamond Coal Company filed claims for refunds of excess profits taxes under Section 722 of the Internal Revenue Code of 1939 for the fiscal years ending March 31, 1943, 1944, 1945, and 1946. The Commissioner denied these claims. The taxpayer then brought the case before the United States Tax Court.

Issue(s)

1. Whether the taxpayer's business was depressed during the base period due to temporary economic circumstances that were unusual in the case of such taxpayer,

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thus qualifying for relief under Section 722(b)(2) of the Internal Revenue Code.

2. Whether the taxpayer's coal mining properties were "in operation," within the meaning of Section 735 of the Internal Revenue Code, during periods when such mining properties were closed because of coal strikes.

Holding

1. No, because the business depression was attributed to competition, not temporary or unusual economic circumstances.

2. No, because the properties were not actively producing coal during the strikes.

Court's Reasoning

The court focused on Section 722(b)(2) of the Internal Revenue Code, which provided relief if a business's base period net income was inadequate due to "temporary economic circumstances unusual in the case of such taxpayer." The court emphasized that the increased labor costs were a "normal business hazard," and the lack of a corresponding increase in the value of coal at the mine was due to competition. The court cited prior cases that said competition is not an unusual economic circumstance and, therefore, not a valid basis for Section 722 relief. "Competition is present in almost any business…it is quite common. It is of the very essence of our capitalistic system." The court found that, from the perspective of the base period, the taxpayer's profits were likely to diminish because of the forces of competition and did not indicate an expectation that the situation would normalize.

The court also addressed the issue under Section 735, concerning the deduction for exempt excess output. The court ruled that, for purposes of Section 735, a mineral property is considered

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