Bercy Industries, Inc. v. Commissioner, 70 T. C. 29 (1978)

In corporate reorganizations, a post-reorganization net operating loss cannot be carried back to a pre-reorganization year of the acquired corporation unless the reorganization qualifies as a type (B), (E), or (F) under IRC Section 368(a)(1).

Summary

Bercy Industries, Inc. , a shell corporation, merged with Old Bercy, an operational company, in a reorganization where Old Bercy's shareholders received stock in Bercy's parent company, Beverly. The transaction was structured as a merger into the shell, with Old Bercy ceasing to exist. The IRS disallowed Bercy's attempt to carry back a post-reorganization net operating loss to Old Bercy's pre-reorganization tax years. The Tax Court held that the reorganization did not qualify as a type (B), (E), or (F) under IRC Section 368(a)(1), and thus, pursuant to IRC Section 381(b)(3), Bercy could not carry back the loss. The court's decision emphasized the importance of the reorganization type in determining carryback eligibility and the significance of the acquired corporation's continued existence post-reorganization.

Facts

Bercy Industries, Inc. , a wholly owned subsidiary of Beverly Enterprises, was incorporated in 1968 as a shell corporation with no business activity. In 1970, Bercy merged with Old Bercy, a corporation engaged in the design, manufacture, and distribution of personal care products. Pursuant to the merger agreement, Old Bercy shareholders received voting common stock of Beverly, representing about 4. 4% of its outstanding shares. Old Bercy ceased to exist after the merger, with Bercy assuming all its assets and liabilities. Post-merger, Bercy incurred a net operating loss and attempted to carry it back to Old Bercy's pre-reorganization tax years.

Procedural History

The Commissioner of Internal Revenue disallowed Bercy's net operating loss carryback, asserting it did not qualify under IRC Section 381(b)(3). Bercy petitioned the U. S. Tax Court for a redetermination of the deficiency. The Tax Court, in its decision dated April 17, 1978, upheld the Commissioner's determination, ruling that the reorganization did not fall within the statutory exceptions allowing carryback.

Issue(s)

1. Whether the reorganization between Bercy Industries, Inc. , and Old Bercy qualified as a type (B), (E), or (F) reorganization under IRC Section 368(a)(1)?
2. Whether Bercy Industries, Inc. , was entitled to carry back a post-reorganization net operating loss to Old Bercy's pre-reorganization taxable years under IRC Section 381(b)(3)?

Holding

1. No, because the transaction did not meet the requirements of a type (B), (E), or (F) reorganization as defined by IRC Section 368(a)(1). Old Bercy ceased to exist post-merger, and the transaction did not involve the acquisition of stock or a mere change in identity.
2. No, because under IRC Section 381(b)(3), a post-reorganization net operating loss cannot be carried back to a pre-reorganization year of the acquired corporation unless the reorganization qualifies as a type (B), (E), or (F).

Court's Reasoning

The court applied IRC Sections 368 and 381 to determine the nature of the reorganization and the applicability of net operating loss carrybacks. It found that the transaction was a hybrid (A) reorganization under Section 368(a)(2)(D) but did not qualify as a (B), (E), or (F) reorganization. The court emphasized that Old Bercy's cessation of existence disqualified the transaction from being a type (B) reorganization, as Bercy acquired assets, not stock. The court also rejected Bercy's argument that the reorganization should be treated as a type (F) for carryback purposes, citing a significant shift in proprietary interests and the lack of statutory support for such an interpretation. The decision was influenced by the policy considerations of Section 381(b)(3), which aims to prevent allocation and tracing problems in reorganizations involving corporations with prior tax histories.

Practical Implications

This decision clarifies the importance of the type of reorganization in determining the eligibility for net operating loss carrybacks under IRC Section 381(b)(3). Practitioners must carefully structure reorganizations to qualify under the appropriate section of IRC 368(a)(1) to ensure carryback eligibility. The ruling highlights the necessity of the acquired corporation's continued existence post-reorganization for certain reorganization types, particularly type (B). It also underscores the challenges of applying net operating loss carrybacks in transactions involving shell corporations, as the court rejected the argument that such transactions inherently present fewer accounting issues. Subsequent cases have considered this decision when analyzing the carryback provisions in corporate reorganizations, often distinguishing it based on the type of reorganization and the existence of the acquired entity post-transaction.