Stevenson Co-Ply, Inc. v. Commissioner, 76 T. C. 637 (1981)

A cooperative can reduce its capital gains for alternative tax computation by the amount of patronage dividends distributed to its stockholder employees.

Summary

Stevenson Co-Ply, Inc. , a cooperative producing and marketing plywood, sought to reduce its section 631(a) capital gains by the amount of patronage dividends distributed to its stockholder employees for computing the alternative tax under section 1201(a). The Tax Court, relying on the precedent set by United California Bank v. United States, allowed this reduction to prevent double taxation, acknowledging the cooperative's role as a conduit for income distribution. This decision reinforced the principle that patronage dividends should be treated similarly to exclusions or deductions for tax purposes, ensuring that income is taxed only once.

Facts

Stevenson Co-Ply, Inc. , a Washington-based cooperative, produced and marketed plywood and related products. In 1973, it realized long-term capital gains from timber cutting under section 631(a) amounting to $2,428,428. Stevenson operated as a cooperative, distributing patronage dividends to its stockholder employees, which for 1973 totaled $2,900,763. These dividends were calculated based on the proportion of work performed by stockholder employees relative to all employees. The cooperative sought to reduce its capital gains by the amount of these dividends for computing the alternative tax under section 1201(a).

Procedural History

The Commissioner of Internal Revenue determined a deficiency in Stevenson's 1973 federal income tax and argued that the full amount of section 631(a) gains must be included in the alternative tax computation. Stevenson contested this, filing a petition with the United States Tax Court. The court ruled in favor of Stevenson, allowing the cooperative to reduce its capital gains by the amount of patronage dividends distributed to its stockholder employees.

Issue(s)

1. Whether, for the purpose of computing the alternative tax under section 1201(a), a cooperative may reduce its section 631(a) gains by the amount of patronage dividends distributed to its stockholder employees?

Holding

1. Yes, because the court found that failing to allow such a reduction would lead to double taxation, which is contrary to the legislative intent behind the taxation of

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cooperatives.

Court’s Reasoning

The court relied on the precedent set by United California Bank v. United States, where the Supreme Court permitted an estate to deduct charitable contributions for alternative tax purposes to avoid double taxation. The Tax Court extended this reasoning to cooperatives, acknowledging their role as conduits for income distribution. Historically, patronage dividends have been treated as exclusions or deductions to prevent double taxation. The court noted that while subchapter T introduced some ambiguity regarding the classification of patronage dividends, the underlying intent to avoid double taxation remained clear. The court rejected the Commissioner’s argument that Stevenson could avoid double taxation by choosing to compute its tax under section 11, emphasizing the need to ensure that income is taxed only once. The court also found that the relevant regulation, section 1. 1382-1(b), did not explicitly prohibit the deduction of patronage dividends from capital gains for alternative tax purposes.

Practical Implications

This decision allows cooperatives to reduce their capital gains by the amount of patronage dividends distributed to their members when computing the alternative tax. It reinforces the principle that cooperatives should not be subject to double taxation on the same income, aligning with the legislative intent behind subchapter T. Legal practitioners representing cooperatives should consider this ruling when advising clients on tax planning strategies, ensuring that patronage dividends are properly accounted for in tax calculations. This case may also influence how other types of entities structured similarly to cooperatives approach their tax obligations. Subsequent cases, such as Riverfront Groves, Inc. v. Commissioner, have cited Stevenson to support the tax treatment of patronage dividends as deductions or exclusions.

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