***Bentley Laboratories, Inc. v. Commissioner, 77 T. C. 152 (1981)***

An accrual basis taxpayer must recognize income from sales to a Domestic International Sales Corporation (DISC) in the year the sales occur, even if the exact transfer price is determined at the end of the DISC's fiscal year.

**Summary**

Bentley Laboratories, Inc. , an accrual basis taxpayer, sold products to its wholly-owned DISC, Bentley International Ltd. , with differing fiscal year-ends. The issue was whether Bentley Labs could defer income recognition until the DISC's year-end when the transfer price was finalized. The Tax Court held that Bentley Labs must accrue income from these sales in the year they were made, as the company had a fixed right to receive income and could reasonably estimate the transfer price at its fiscal year-end. This decision underscores that accrual basis taxpayers cannot delay income recognition for sales to DISCs based solely on the timing of transfer price determination.

**Facts**

Bentley Laboratories, Inc. (Bentley Labs) was an accrual basis taxpayer with a fiscal year ending November 30. It sold paramedical equipment to its wholly-owned subsidiary, Bentley International Ltd. , a DISC, which had a fiscal year ending January 31. The transfer price for these sales was determined at the end of the DISC's fiscal year under the intercompany pricing rules of section 994 of the Internal Revenue Code. Bentley Labs did not report income from these sales until the following fiscal year, after the DISC's year-end when the transfer price was finalized.

**Procedural History**

The Commissioner of Internal Revenue determined deficiencies in Bentley Labs' 1972 and 1973 income taxes, asserting that the income from sales to the DISC should have been reported in the year the sales were completed. Bentley Labs petitioned the U. S. Tax Court for a redetermination of these deficiencies. The case was submitted based on a stipulation of facts, and the court issued its decision on July 30, 1981, holding that Bentley Labs must accrue the income in the year the sales occurred.

**Issue(s)**

1. Whether Bentley Laboratories, Inc. , an accrual basis taxpayer, must include income from sales to its DISC in its taxable income for the year in which such sales are completed, or may defer such income until the succeeding taxable year when the transfer price is finally determined?

**Holding**

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1. Yes, because Bentley Labs had a clear and indefeasible right to receive income from its sales to the DISC in the year the sales occurred, and the amount of such income could be reasonably estimated at the end of Bentley Labs' fiscal year.

**Court's Reasoning**

The court applied the "all events" test under section 1. 451-1(a) of the Income Tax Regulations, which requires income to be included when the right to receive it is fixed and the amount can be determined with reasonable accuracy. Bentley Labs had a contractual right to receive income from the DISC upon sale of the products, and the sales agreement allowed for estimated billings at interim periods. The court found that Bentley Labs could have reasonably estimated the transfer price at its fiscal year-end using the information available in its and the DISC's books, despite the final price being determined at the DISC's year-end. The court emphasized that the DISC provisions were intended to defer taxation of DISC profits, not to delay recognition of the parent's income from sales to the DISC. The court also noted that Bentley Labs failed to provide evidence that the income could not be reasonably estimated at its year-end.

**Practical Implications**

This decision impacts how accrual basis taxpayers with DISCs should account for income from intercompany sales. It establishes that such taxpayers cannot defer income recognition until the DISC's year-end when the transfer price is finalized if the amount can be reasonably estimated earlier. This ruling affects tax planning for companies utilizing DISCs, as it requires them to recognize income in the year of sale, potentially affecting cash flow and tax liability timing. It also informs practitioners that they must carefully document the basis for any estimates used in income recognition to withstand IRS scrutiny. Subsequent cases have followed this principle, reinforcing the need for timely income recognition in similar scenarios.

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