

DEER PARK PINE INDUSTRIES, INC., v. SQUIRE
Memorandum of Law, 60-2 USTC ¶ 9608;
6 AFTR 2d 5349 (WI). Wash. 1960).
Findings of Fact and Conclusions of Law
6 AFTR 2d 5899 (WI). Wash. 1960).

Editor's Summary

Key Topics

FAIR MARKET VALUE OF TIMBER

- Not capable of determination with mathematical certainty

Facts

The taxpayer elected to treat its cutting of timber during the years 1950 through 1953 as a sale or exchange under section 117(k)(1). Its valuation of the timber cut during those years was contested by the Commissioner. At the trial, foresters testifying for the taxpayer differed widely from those testifying for the Government as to the valuation of the timber.

District Court

Held: After full and careful evaluation of the expert testimony and the entire record, it is held that the fair market value of the timber lies substantially below all of the opinion figures expressed by the taxpayer's experts and substantially above those expressed by the Government's experts. For the reasons stated in *Cascade Lumber Company v. Squire* and *Murphy v. United States*, discussion of the details of the evidence would serve no useful purpose. The differing opinions of expert foresters make it plain that fair market value is a matter subject to substantial difference of opinion and that it cannot be determined with mathematical certainty. The Court determines the fair market value of the timber in question.

Case Text

MEMORANDUM DECISION

BOLDT, District Judge: The ultimate issues in this case primarily involve questions of fact. The general principles of law to be applied in solving those questions have been stated in *Cascade Lumber Co. v. Squire*, 52 AFTR 1290, ¶ 72,871 P-H Federal 1957 and *Murphy v. United States*, Civ. 2418 this court. For the reasons stated at the conclusion of the argument, discussion of the details of the evidence and of the facts found by the court would serve no useful purpose and will not be undertaken herein.

Opinions on fair market value as of the decisive dates of the timber in question were presented in

evidence by six highly qualified foresters. All are experts in the quality and value of timber and each has a record of extensive and creditable practical experience. Four of those witnesses were presented by plaintiff and two by defendant. The opinions of all six experts were remarkably similar, with a narrow spread between high and low figures, as to the fair market value of both the Ponderosa Pine and mixed species distributed to plaintiff in the December 29, 1953 dissolution of North Columbia Company. That unanimity of opinion is particularly noteworthy, when contrasted to the wide spread in the figures and in the variation of expert opinion as to fair market value in both categories of timber as of the first day of each of the four fiscal years in question. In the latter valuations, the experts called as witnesses by plaintiff, as well as those testifying for defendants, were in substantial disagreement among themselves. This variety of opinion possibly was due to the differing views of the witnesses as to the fair market value of timber sold at "retail" rather than "wholesale," as those terms were used in the trial. In any event, the unanimity of opinion in the one instance makes determination of the facts therein relatively simple. In the other instance the differences in the value figures testified to by the several reputable, experienced and credible foresters make it plain that on the evidence presented in this case fair market value for each type of timber for the first date of each particular fiscal year in question is a matter subject to substantial difference of expert opinion and cannot be determined with mathematical certainty.

After full and careful evaluation of all of the testimony of each of the experts and the entire record, the court has the firm conviction that on the evidence now before the court the correct figure representing fair market value on the first date of each fiscal year in each instance lies substantially below all of the opinion figures expressed by plaintiff's experts and substantially above the opinion figures of defendants' experts.

The specific amounts of fair market value in issue are found by the court as follows:

The fair market values for the property received by plaintiff on the dissolution of North Columbia Company are:

Ponderosa Pine		\$14.50 per M
Mixed Species	5.50 per M	
Land		2.00 per Acre

The fair market values (per M) of the timber subject to treatment under Sec. 117(k)(1) as of the first day of each fiscal year in question are:

Fiscal Year			
1950-1951	1951-1952	1952-1953	1 953-1954
P. Pine Mixed	P. Pine Mixed	P. Pine Mixed	P. Pine Mixed
\$17.50 \$9.00	\$20.00 \$10.50	\$22.50 \$9.50	\$21.00 \$7.00

While plaintiff's assertions as to the quality of the timber in question were seriously impeached by plaintiff's prior written representations concerning the Blue Creek timber (Exhibits A-35 and A-36),¹ on the whole record the quantities of timber involved are found to be as contended for by plaintiff.

Whether it is necessary to decide the fact and law issues pertaining either to the validity of the reallocation by the Commissioner under Section 45 of the 1939 Code or to the limitations defense asserted by defendants cannot readily be determined without mathematical computations of tax liability based on the fact findings above stated. By pretrial agreement computations of such nature are to be prepared by accountants and the issues referred to will be given further consideration by the court when such computations are available. Defendants' counsel are directed within 30 days of this date to serve and file a memorandum of computations as indicated with analysis of their relationship to the reallocation and limitation issues. Counsel for plaintiff may serve and file a response to defendants' memorandum within 10 days of service thereof. Following receipt and study of such data the court will take final action on the reallocation and limitation issues. Thereafter Findings of Fact, Conclusions of Law and Judgment as indicated herein and in the further rulings of the court may be presented at the convenience of counsel.

FINDINGS OF FACT

I. This is an action for the refund of income and excess profits taxes, plus interest as provided by law, assessed against and collected from plaintiff by the Commissioner of Internal Revenue through the defendants for the fiscal years July 1, 1950, through and including June 30, 1954. Jurisdiction of this action is invoked by virtue of Section 1346 of the United States Code.

II. Plaintiff is a corporation organized and existing under the laws of the State of Washington since July 1, 1946, the date of its incorporation, with its principal place of business in Deer Park, Washington.

III. The defendant, Clark Squire, at all times mentioned herein until October 30, 1952, was the duly appointed and acting Collector of Internal Revenue for the Collection District of Washington, and said defendant is now residing within the Western Judicial District of Washington. The defendant, William E. Frank, has been at all times from and after October 31, 1952, and now is, the duly appointed and acting District Director of Internal Revenue for the Internal Revenue District of Washington, and said defendant is now residing within the Western Judicial District of Washington.

IV. For each of the fiscal years shown in the following table the plaintiff timely filed a federal income and excess profits tax return with one of the defendants, indicating taxes due in the following amounts which were paid by the plaintiff on the dates and to the defendants indicated in the following table:

Fiscal Year Ending	Tax Reported Due	Date	Payment Amount	Paid to
6-30-51	\$439,501.71	9 – 14 – 51	129,112.87	Squire
		1 – 14 – 52	129,112.87	Squire
		3 – 17 – 52	93,375.63	Squire
		6 – 13 -52	87,900.34	Squire
6-30-52	\$253,022.69	9 – 15 – 52	88,557.94	Squire
		12 – 15 – 52	88,557.94	Frank

		3 – 13 – 53	37,953.41	Frank
		6 – 15 – 53	37,953.40	Frank
6-30-53	\$143,772.31	9 – 14 – 53	57,508.93	Frank
		12 – 14 – 53	57,508.93	Frank
		3 – 12 – 54	14,377.23	Frank
		6 – 11 - 54	14,377.22	Frank
6-30-54	\$155,193.49	9 –14 - 54	69,837.07	Frank
		12 – 15 –54	69,837.07	Frank
		3 – 15 – 55	7,759.68	Frank
		6 – 13 - 55	7,759.67	Frank

On or about January 10, 1953, the Commissioner of Internal Revenue allowed and paid to plaintiff a refund of taxes of \$36,444.41, arising from adjustments involving issues unrelated to this case as a result of which the total amount of taxes paid to the defendant Squire for the fiscal year ending June 30, 1951, was \$403,057.30.

V. For each of the three fiscal years ending June 30, 1951, 1952 and 1953, the plaintiff and the Commissioner of Internal Revenue executed one or more timely and valid consents whereby the periods of limitations for the assessment of income and excess profits taxes were, for each year, properly extended to June 30, 1957.

VI. On or about June 14, 1957, the Commissioner of Internal Revenue executed and mailed to the plaintiff a notice of deficiency ("90 day letter") whereby income and excess profits tax deficiencies were determined against the plaintiff for the fiscal years involved in this proceeding. On or about September 6, 1957, plaintiff paid said deficiencies, with interest, to the defendant Frank as follows:

Fiscal Year Ending	Deficiency determined and Paid	Interest Paid	Total Paid
6-30-51	\$ 82,408.81	\$ 27,904.97	\$110,313.78
6-30-52	159,417.75	47,604.76	207,022.51
6-30-53	46,553.18	11,108.35	57,661.53
6-30-54	<u>124,816.96</u>	<u>22,294.36</u>	<u>147,111.32</u>
	\$413,196,70	\$108,912.44	\$522,109.14

VII. On or about March 26, 1958, the plaintiff filed timely claims for refunds in the amount of \$110,313.78 for the fiscal year ending June 30, 1951; in the amount of \$207,022.51 for the fiscal year ending June 30, 1952; in the amount of \$57,661.53 for the fiscal year ending June 30, 1953, and in the amount of \$147,111.32 for the fiscal year ending June 30, 1954, total for said four fiscal years being \$522,109.14.

VIII. On August 20, 1958, a notice of disallowance of each of said claims for refund was given by registered mail to the plaintiff by the direction of the Commissioner of Internal Revenue. No part of said claims for refund have been paid to the plaintiff by either of the defendants.

IX. For each of the fiscal years involved in this action, plaintiff reported on its income tax return an amount itemized as a gain on the cutting of timber under Sec. 117(k)(1), I.R.C.

X. The fair market value on July 1, 1950, of the timber cut by plaintiff during the fiscal year ending June 30, 1951, to which the election under Sec. 117(k)(1) applied was \$416,585.98, computed as follows:

Species	Board Feet Cut	Fair Market Value per M Bd. Ft.	Total Fair Market Value
Ponderosa Pine	16,588,240	\$17.50	\$290,294.20
Mixed	14,032,420	9.00	<u>126,291.78</u>
			\$416,585.98

XI. The adjusted basis for depletion of the timber cut by plaintiff during the fiscal year ending June 30, 1951, to which the election under 117(k)(1) applied was \$390,402.04.

XII. The 117(k)(1) gain of plaintiff for the fiscal year ending June 30, 1951, was \$26,183.94.

XIII. The fair market value on July 1, 1951, of the timber cut by plaintiff during the fiscal year ending June 30, 1952, to which the election under Sec. 117(k)(1) applied was \$471,822.64 computed as follows:

Species	Board Feet Cut	Fair Market Value per M Bd. Ft.	Total Fair Market Value
Ponderosa Pine	16,752,670	\$20.00	\$335,053.40
Mixed	13,025,640	10.50	<u>136,769.22</u>
			\$471,822.62
			\$416,585.98

XIV. The adjusted basis for depletion of the timber cut by plaintiff during the fiscal year ending June 30, 1952, to which the election under 117(k)(1) applied was \$459,726.64.

XV. The 117(k)(1) gain of plaintiff for the fiscal year ending June 30, 1952, was \$12,095.98.

XVI. The fair market value on July 1, 1952, of the timber cut by plaintiff during the fiscal year ending June 30, 1953, to which the election under Sec. 117(k)(1) applied was \$404,978.91, computed as follows:

Species	Board Feet Cut	Fair Market Value per M Bd. Ft.	Total Fair Market Value
Ponderosa Pine	12,741,460	\$22.50	\$286,682.85
Mixed	12,357,480	9.50	<u>117,396.06</u>
			\$404,078.91

XVII. The adjusted basis for depletion of the timber cut by plaintiff during the fiscal year ending June 30, 1953, to which the election under Sec. 117(k)(1) applied was \$390,917.59.

XVIII. The 117(k)(1) gain of plaintiff for the fiscal year ending June 30, 1953, was \$13,161.32.

XIX. The fair market value on July 1, 1953, of the timber cut by plaintiff during the fiscal year ending June 30, 1954, to which the election under Sec. 117(k)(1) applied was \$367,054.69, computed as follows:

Species	Board Feet Cut	Fair Market Value per M Bd. Ft.	Total Fair Market Value
Idaho White Pine	157,670	\$30.00	\$ 4,732.80
Ponderosa Pine	13,086,650	21.00	274,819.65
Mixed	12,500,320	7.00	<u>87,502.24</u>
			\$367,054.69

XX. The adjusted basis for depletion of timber cut by plaintiff during the fiscal year ending June 30; 1954, to which the election under Sec. 117 (k) (1) applied was \$431,990.07.

XXI. The 117(k)(1) loss of plaintiff for the fiscal year: ending June 30, 1954, was \$64,935.38.

XXII. The North Columbia Co. was a corporation organized and existing under the laws of the State of Washington from the date of its incorporation on March 1, 1939, to the date of its dissolution on December 29, 1953. The North Columbia Co. had its principal place of business in Deer Park, Washington, and principal business activity related to the holding of various timber rights. The Chicago & Riverdale Lumber Company was a corporation organized and existing under the laws of the State of Illinois and during all of the times involved in this action had its principal place of business in Chicago, Illinois, and a principal business activity of engaging in the lumber business.

XXIII, During each of the fiscal years involved in this action, the plaintiff controlled North Columbia Co., within the meaning of Section 45 of the Internal Revenue Code of 1939.

XXIV. On December 29, 1953, the plaintiff owned 750 shares of the 1,000 shares of the outstanding capital stock of North Columbia Company and the adjusted basis of the 750 shares of stock owned by plaintiff was \$1,800,000.00. On said date North Columbia Company distributed to plaintiff inter alia in complete liquidation of North Columbia Company, in a taxable transaction in which long-term capital gain or loss was recognized by plaintiff, the property shown in the following table, of the net value shown therein:

Property	Unit Value	Gross Value
Cash	\$1,868.36	\$ 1,868.36
An undivided 75% interest in 104,915,620 board feet of Ponderosa Pine (per M)	14.50	1,140,957.37
An undivided 75% interest in 114,172,665 feet of Mixed species (per M)	5.50	470,962.24
An undivided 75% interest in 77,119.44 acres of uncut and cut-over land (per acre)	2.00	115,679.16
An undivided 75% interest in 3,236.40 acres of land only, minus timber (per acre)	2.00	<u>4,854.60</u>
		\$1,734,321.73
Less liabilities of North Columbia Co. assumed by plaintiff		<u>76,611.14</u>
Net Value		\$1,657,710.59

XXV. Plaintiff's contract price paid by plaintiff to North Columbia Co. was \$142,289.41.

XXVI. The contract price paid by plaintiff to North Columbia Co. for timber purchased during the four fiscal years involved in this action was a reasonable price and was not adopted for the purpose of tax evasion, and the Commissioner of Internal Revenue, through the defendants, was not warranted in adjusting such prices under Section 45 of the Internal Revenue Code of 1939.

XXVII. Plaintiff on his original income tax return for the fiscal year ending June 30, 1952, erroneously claimed a deduction of \$7,211.21 for insurance expense. Said deduction should have been taken in the fiscal year ending June 30, 1953.

XXVIII. The price plaintiff was charged by the Interior Department for timber under Indian Service cutting contracts was not determinative of the fair market value of such timber for the purpose of determining gain or loss under Sec. 117(k)(1).

XXIX. The Commissioner of Internal Revenue's determination of the fair market value of both pine and mixed species as of July 1, 1950, July 1, 1951, July 1, 1952, and July 1, 1953, for the purpose of applying Sec. 117(k)(1) was in fact erroneous.

XXX. On September 6, 1957, plaintiff made an overpayment of principal and interest of Federal Income and: Excess Profits Taxes to defendant William E. Frank for the fiscal years involved in this action in the amounts shown in the following table:

Fiscal Year Ending	Overpayment of Principal	Overpayment on Interest	Total Overpayment of Taxes
6-30-51	\$ 39,683.20	\$ 15,355.56	\$ 55,038.76
6.30-52	138,636.89	41,399.25	180,036.14
6.30-53	16,820.57	4,013.66	20,834.23
6-30-54	<u>116,777.00</u>	<u>20,858.29</u>	<u>137,635.29</u>
	\$311,917.66	81,626.76	\$ 393,544.42

CONCLUSIONS OF LAW

I. This Court has jurisdiction of the above entitled action, the parties hereto and the subject matter thereof.

II. The Sec. 117(k)(1) gain of plaintiff for the fiscal year ending June 30, 1951, was \$26,183.94.

III. The Sec. 117(k) (1) gain of plaintiff for the fiscal year ending June 30, 1952, was \$12,095.98.

IV. The Sec. 117(k) (1) gain of plaintiff for the fiscal year ending June 30, 1953, was \$13,161.32.

V. The Sec. 117(k)(1) loss of plaintiff for the fiscal year ending June 30, 1954, was \$64,935.38.

VI. Plaintiff's capital loss on the liquidation of North Columbia Co. on December 29, 1953, was \$142,289.41.

VII. The action of the Commissioner of Internal Revenue in re-allocating gross income of the plaintiff and North Columbia CO. Was unreasonable in that such action Was not necessary to clearly reflect the income of such businesses within the meaning of Section 45, Internal Revenue Code of 1939.

VIII. Plaintiff is entitled to a judgment because of total overpayment of taxes as set forth in Finding of Fact XXX against defendant William E. Frank in the sum of \$393,544.42, together with interest thereon at the rate of six percent per annum from September 6, 1957, together with plaintiff's costs and disbursements herein taxed.

IX. Defendant William E. Frank is entitled to the issuance by this Court of a Certificate of Probable Cause pursuant to 28 U.S. Code, Section 2006.

X. Defendant Clark Squire is entitled to a judgment of dismissal of the action against him.

JUDGEMENT

BOLDT, District Judge: The above entitled cause having come on regularly for trial before the Honorable Geo. H. Boldt, presiding in the above entitled Court, sitting without a jury, plaintiff and defendants appearing by their respective attorneys, the Court having considered the evidence and the arguments on behalf of the respective parties and having taken the matter under

advisement and rendered his Memorandum Decision July 1, 1960, and having made and entered Findings of Fact and Conclusions of Law, it is hereby

Certified and Decreed that probable cause existed for the defendant William E. Frank to collect the federal taxes subject to this cause of action and in so doing the defendant William E. Frank acted under the direction of the Secretary of the Treasury; it is further

Ordered, Adjudged and Decreed that judgment be and is hereby entered in favor of the plaintiff and against the defendant William E. Frank in the sum of \$393,544.42, together with interest thereon at the rate of 6% per annum from September 6, 1957, and together with plaintiff's costs and disbursements herein taxed; it is further

Ordered that judgment be and is hereby entered dismissing the above entitled action against the defendant, Clark Squire.

1 Exhibit A-35 – letter from plaintiff's manager to Assistant Secretary Department of Interior , dated March 26, 1945 in which it is stated "8. Now the last and by far the most important, point in this discussion is the fact that everyone connected with the forestry end of the Indian Service knows that the timber located on the Blue Creek Unit is the lowest quality of Ponderosa Pine in Northwestern United States."

Exhibit A-36 – letter from plaintiff's manager to Assistant Secretary, Department of Interior, dated September 21, 1945 in which it is stated: "According to the last paragraphs of your letter I am entirely mistaken regarding the quality of the Ponderosa Pine on the Blue Creek Unit. It will be a great favor if you will advise me where there is a stand of ponderosa pine in Northwestern United States of lower quality than is located on the Blue Creek Unit. Upon receiving this information I will go immediately to inspect it