

FEDERAL TAXATION OF PROPERTY TRANSACTIONS

LexisNexis GRADUATE TAX SERIES

Series Editor

Paul L. Caron

*Charles Hartstock Professor of Law
Director, Faculty Projects
University of Cincinnati College of Law*

Board of Editors

Ellen P. Aprill

*John E. Anderson Chair in Tax Law
Past Director, Graduate Tax Program
Loyola Law School*

Elliott Manning

*Professor of Law
Faculty Chair, Graduate Tax Program
University of Miami School of Law*

Philip F. Postlewaite

*Professor of Law
Director, Graduate Tax Program
Northwestern University School of Law*

David M. Richardson

*Professor of Law
Past Director, Graduate Tax Program
University of Florida College of Law*

FEDERAL TAXATION OF PROPERTY TRANSACTIONS

DAVID L. CAMERON

ELLIOTT MANNING

Casebook ISBN: 978-1-5934-5886-7

eBook ISBN: 978-0-3271-7690-9

Library of Congress Cataloging-in-Publication Data

Cameron, David L., 1957-
Federal taxation of property transactions / David L. Cameron, Elliott Manning
p. cm.
Includes index.
ISBN 978-1-5934-5886-7
1. Capital gains tax--Law and legislation--United States. 2. Property tax--Law and legislation--United States. 3. Income tax deductions for losses--United States. I. Manning, Elliott. II. Title.
KF6566.C36 2012
343.7305*245--dc23 2011048187

This publication is designed to provide authoritative information in regard to the subject matter covered. It is sold with the understanding that the publisher is not engaged in rendering legal, accounting, or other professional services. If legal advice or other expert assistance is required, the services of a competent professional should be sought.

LexisNexis and the Knowledge Burst logo are registered trademarks of Reed Elsevier Properties Inc., used under license. Matthew Bender and the Matthew Bender Flame Design are registered trademarks of Matthew Bender Properties Inc.

Copyright © 2012 Matthew Bender & Company, Inc., a member of LexisNexis. All Rights Reserved.

No copyright is claimed by LexisNexis or Matthew Bender & Company, Inc., in the text of statutes, regulations, and excerpts from court opinions quoted within this work. Permission to copy material may be licensed for a fee from the Copyright Clearance Center, 222 Rosewood Drive, Danvers, Mass. 01923, telephone (978) 750-8400.

NOTE TO USERS

To ensure that you are using the latest materials available in this area, please be sure to periodically check the LexisNexis Law School web site for downloadable updates and supplements at www.lexisnexis.com/lawschool.

Editorial Offices

121 Chanlon Rd., New Providence, NJ 07974 (908) 464-6800
201 Mission St., San Francisco, CA 94105-1831 (415) 908-3200
www.lexisnexis.com

MATTHEW  BENDER

PREFACE

The Lexis Graduate Tax Series grew out of the recognition that the goals of a graduate tax program are different from those of the tax curriculum at the J.D. level. J.D. tax courses are introductory in nature. Although many J.D. tax courses provide a good overview of their targeted areas of law, time rarely permits either an in-depth analysis of the more complicated provisions of the Code or Regulation or the application of those provisions to real-life problems. In essence, J.D. tax courses provide students a foundation in the core statutory and judicial concepts while a graduate tax program requires that students confront and apply the tax law that is applicable to sophisticated business transactions.

LL.M. programs build on, and significantly expand, students' knowledge of the Code, Regulations, and judicial doctrines, and enhance their Code and Regulations reading skills. LL.M. programs typically require students to concentrate on the primary sources of the law—the Code and Regulations. Students are expected to improve their ability to read, comprehend, and apply the Code and Regulations, and they do so by working on complex fact patterns that raise difficult legal issues.

At the same time, the regulatory construct has been in a state of considerable flux. Historically, matters were neatly divided between the SEC and the states. With its creation in 1934, the SEC was assigned the task of regulating corporate disclosure, particularly financial disclosure, while states continued to regulate the substantive standards of corporate governance. But in response to various corporate scandals and crises — most significantly, after the collapse of Enron and WorldCom in 2001 and 2002 — the post-Depression division of authority has shifted.

An important, but different, driving force behind the development of specially designed course materials for LL.M. programs is the dramatic expansion of the quantity and complexity of tax law over the past 40 to 50 years. The current commercially available versions of the Code and Regulations are roughly four times as large as their 1970 predecessors. Over that period, class time dedicated to tax has grown very little at the J.D. level. Covering much more material in the same period has led authors to write longer J.D. textbooks, many of which exceed one thousand pages. Such comprehensive coverage leads to extended textbook assignments. This both forces and permits students to bypass the assigned Code and Regulations provisions and spend their available time answering problems by reference solely to the author's explanation of the law in the textbook. Tax casebooks written primarily for the larger J.D. market that purport to be suitable for both J.D. and LL.M. tax courses also lean toward comprehensive explanations of the Code and Regulations, which tend to deflect students away from the primary sources.

Books in the Graduate Tax Series are designed to be read with, and complement, the study of the Code, Regulations, and underlying principles of the tax law. Although some chapters of the books in the Series provide a detailed explanation of a topic, more frequently the chapters provide a general, typically brief, overview of the topic together with more complete explanations of the applicable portions of the Code and Regulations that are particularly difficult to understand. Also, many of the problems are based on situations encountered in practice or found in decided cases. Although some of the questions either state or disclose the issues and even the applicable statutes, many of them require analysis of a given set of facts to first determine and then resolve the critical issues.

Students need to recognize that shifting the emphasis to primary sources and

practice-based problems, which is made possible by reducing the time spent reading and analyzing cases and various secondary sources, increases the responsibility of the student for his or her education. It is harder to master a complex statute or regulation by studying it than it is to have someone explain it. It is also harder to identify the issues and applicable law from a group of facts than it is to answer short problems that identify the issue and the applicable law.

Students in an LL.M. program should be able to handle the higher level of personal responsibility. Furthermore, if one accepts the premise that students in an LL.M. program should develop the reading and comprehension skills necessary to interpret the Code and Regulations as well as master the core substantive concepts of the tax law, it is clear that students must dedicate a significant portion of their study time to the primary sources of the law. Like other books in the series, the focus of this book on the taxation of property transactions requires that students read, and grapple with, significant portions of the Code and Regulations.

In one sense, the taxation of property transactions is relatively straightforward. Tax practitioners typically think in terms of the taxpayer's investment in acquired property (i.e., the taxpayer's basis in that property), the possible recovery by the taxpayer of that investment while holding the property (i.e., depreciation or amortization), and the taxation of any gain or loss on a subsequent disposition of the property (i.e., gain or loss realization and recognition). But each of these areas involves considerable complexity, depending on the way in which the taxpayer acquired the property, whether the property was acquired separately or as part of an existing trade or business, the existence of any debt or other liability incurred in acquiring the property, the purpose for which the taxpayer holds the property, and the manner in which the property is disposed of. In addition, consideration must be given to the differences that exist between the treatment of tangible and intangible property, many of which are based on the historical evolution of the tax law and some of which reflect the increasing importance and value of intangible property as a business asset. At every step in this process, planning opportunities arise that permit tax practitioners to minimize the tax implications for their clients.

Two significant complications affect the taxation of property transactions. The first complication is the special treatment of capital gains and losses. Net capital gain in the hands of individuals is eligible for preferential rate rates while the deduction of capital losses is limited for both individual and corporate taxpayers. Transactions are frequently structured in an attempt to create net capital gain and avoid the characterization of losses as capital. Consequently, a thorough grounding in the characterization provisions of the Code and the effects of characterization on the taxpayer is essential to understand the application of the tax law. The second complication arises from the time value of money. Tax provisions that permit the generation of tax losses, in the form of interest and depreciation deductions, for example, may result in tax savings in early years even when these tax savings are offset by greater tax liability in later years. Taxpayers take these tax effects into account when evaluating different investments, and Congress has adopted a number of provisions to reduce the distortion of investment decisions that the tax law would otherwise create. This book aims to provide students with an appreciation for these two significant complexities through the descriptive materials and problems presented.

More specifically, Chapter 1 introduces the concepts of basis and realization that are fundamental to the taxation of all transactions involving property. Chapter 2 follows with the effects of taxing gains and losses from capital assets differently from ordinary gains

and losses. Chapter 3 deals with liabilities, which are essentially the opposite of assets or property, so that they can be considered negative property. The tax effect of liabilities is, however, governed by different rules from those that relate to property. Although they affect the taxation of capital gains and losses, they are not similarly classified, so that relief from liability depends on the nature of the transaction giving rise to that relief. Chapter 4 covers the rules applicable to the capitalization of costs incurred in the creation or acquisition of property and the recovery of those costs through a variety of expensing, amortization, and depreciation provisions. Chapter 5 covers non-recognition transactions (other than transfers involving partnerships, corporations or trusts) in which gain or loss is not recognized on disposition but is deferred through the mechanism of substituted basis. Chapter 6 deals with deferred compensation issues and other special problems arising in executive compensation arrangement using employer stock or stock options that reflect the lure of capital gain treatment. Chapter 7 covers the complexities that arise from the cliché that property is a bundle of rights, particularly when the ownership and long-term right to possession is divided under a lease or similar arrangement. This chapter also includes issues involving transfers of partial interests in property, including life estates and remainders, and transfers of interests in intangible property represented by patents, copyrights, goodwill and similar intangible assets. Finally, Chapter 8 covers a number of special provisions that affect the deductibility of losses, including the wash sales rules, limitations on related party transactions, the at-risk and passive loss rules, and losses arising in certain leasing transactions.

In this course, students should focus on the assigned provisions of the Internal Revenue Code and Treasury Regulations, as well as the text and materials in the book, in analyzing the problems. The problems are designed to cover all of the core principles. Many of the problems include citations to cases or rulings, sometimes cases or rulings on which the problems are based. Students are encouraged to explore the cited cases and rulings in connection with working out the problems, although it is preferable that students try first to analyze them on their own. Students should also be aware that the law in many areas is uncertain and that practitioners (as well as the authors) do not necessarily agree with the analysis or results in some of the cited cases or rulings.

The material covered in a LL.M. course on the taxation of property transactions may also include some topics that are not addressed in this book, such as deferred payment sales, limitations on interest deductions, and the original issue discount rules. These topics are covered in another book in the Graduate Tax Series written by Professors Michael Lang, Elliott Manning, and Mona Hymel: Lang, Manning & Hymel, *Federal Tax Accounting* (Lexis/Nexis 2d ed., 2011). Their book, which also covers capitalization, amortization, and depreciation issues, is a useful complement to the material present here.

Although there is a vast literature on taxation of property transactions—principally in the form of articles in tax journals—most such articles focus on detailed aspects of the Code and Regulations. For students looking for additional discussion of the topics covered in this book, a helpful study guide is the last half of CHIRELSTEIN & ZELENAK, *FEDERAL INCOME TAXATION* (Foundation Press 12th ed., 2011). Students might also consider reading relevant portions of two excellent treatises for further coverage: BITTKER & LOKKEN, *FEDERAL TAXATION OF INCOME, ESTATES AND GIFTS* (WG & L 3d ed., 2005), and BITTKER, MCMAHON & ZELENAK, *FEDERAL INCOME TAXATION OF INDIVIDUALS* (WG & L 3d ed., 2002).

Portions of Chapter 2, Capital Gains and Losses, have been reprinted by permission of

CCH, a Wolters Kluwer business, from *Taxation of Capital Gains and Losses*, by John H. Birkeland and David Cameron.

Elliott Manning thanks his wife, Gail, for putting up with him during the writing process and otherwise. David Cameron thanks his spouse, Jane, for her support and encouragement during this and other taxing projects.

TABLE OF CONTENTS

Chapter 1	BASIS AND REALIZATION	1
§ 1.	INTRODUCTION	1
§ 2.	BASIS	2
§ 2.01.	In General	2
	<i>Gladden v. Commissioner</i>	3
	Notes and Comments	7
	Problems for Discussion	8
§ 2.02.	Tax Cost Basis	9
§ 2.03.	Basis of Gifts	10
§ 2.04.	Basis of Inherited Property	12
§ 2.05.	Substituted Basis	13
§ 2.06.	Basis of Property Received in a Taxable Exchange	15
	<i>Philadelphia Park Amusement Co. v. United States</i>	15
	Notes and Comments	18
	Problem for Discussion	20
§ 2.07.	Split Basis	20
§ 2.08.	Inclusion of Debt in Basis	22
§ 2.09.	Adjustments to Basis	22
§ 3.	REALIZATION OF GAIN OR LOSS	23
§ 3.01.	In General	23
§ 3.02.	Sale or Exchange	24
	<i>Cottage Savings Association v. Commissioner</i>	25
	Notes and Comments	32
	Problems for Discussion	35
§ 3.03.	Other Dispositions	35
§ 3.03(a)	Casualties and Abandonment	35
§ 3.03(b)	Transfer in Satisfaction of a Claim	36
	<i>International Freighting Corporation, Inc. v. Commissioner</i>	37
	Notes and Comments	39
	Problems for Discussion	41
§ 3.03(c)	Mortgaging Property as a Realization Event	41
	<i>Woodsam Associates, Inc. v. Commissioner</i>	42
	Notes and Comments	44
§ 3.04.	Part Sale/Part Gift	44
	Problem for Discussion	45
§ 3.05.	Inclusion of Debt in the Amount Realized	46
§ 3.06.	Recognition and Allowance	46
§ 4.	SALE OF A BUSINESS	47

TABLE OF CONTENTS

§ 4.01.	Overview	47
	<i>Williams v. McGowan</i>	47
	Notes and Comments	50
	Problem for Discussion	50
§ 4.02.	§ 1060 And the Residual Allocation Method	50
	<i>Concord Control, Inc. v. Commissioner</i>	51
	Notes and Comments	54
	Problem for Discussion	56
§ 4.03.	Contingent Payments and Liabilities	56
	<i>Illinois Tool Works, Inc. v. Commissioner</i>	58
	Notes and Comments	66
Chapter 2	CAPITAL GAINS AND LOSSES	69
§ 1.	INTRODUCTION	69
§ 2.	MECHANICS OF DETERMINING NET CAPITAL GAIN	73
§ 2.01	Non-Corporate Taxpayers	73
(a)	Applicable Tax Rates	73
(b)	Netting Capital Gains and Losses	75
(c)	Look-Through Rules Applicable to Pass-Through Entities	80
(d)	Capital Loss Limitations	80
	Problem for Discussion	83
§ 2.02	Capital Gain and Loss Treatment for Corporate Taxpayers	83
§ 3.	DEFINITION OF A CAPITAL ASSET	84
§ 3.01	Overview	84
§ 3.02	Definition of “Property”	85
	<i>Lattera v. Commissioner</i>	88
	Problems for Discussion	97
§ 3.03	Capital Asset Defined	98
(a)	Dealer Property	100
	<i>Suburban Realty Company v. United States</i>	103
	NOTES	114
(b)	Property Used in a Trade or Business	124
(c)	Intellectual and Artistic Property	124
(d)	Certain Notes and Accounts Receivable	127
(e)	Government Publications	128
(f)	Hedging Transactions	129
(g)	Commodities Derivative Financial Instruments	132
(h)	Trade or Business Supplies	133
§ 4	SALE OR EXCHANGE	133
§ 4.01	Overview	133
§ 4.02	Judicial Interpretation	135

TABLE OF CONTENTS

	<i>Freeland v. Commissioner</i>	136
	Notes	140
	Problems for Discussion	141
§ 4.03	Extinguishment Doctrine	141
	<i>Pounds v. United States</i>	143
§ 4.04	Statutory Sales	145
(a)	Worthless Securities and Nonbusiness Bad Debts	146
(b)	Loss on the Lapse of an Option	146
(c)	Amounts Received on the Cancellation of a Lease	146
(d)	Amounts Received on the Cancellation of Certain Property Rights	147
	Problems for Discussion	148
(e)	Miscellaneous Statutory Sales	149
§ 5.	HOLDING PERIOD	149
§ 5.01	Overview	149
§ 5.02	Basic Rules for Determining Holding Period	150
	Problem for Discussion	151
§ 5.03	Split Holding Periods	151
§ 5.04	Holding Period for Inherited Property	155
§ 5.05	Tacked Holding Periods	155
(a)	Tacking Permitted in Substituted Basis Transactions	155
(b)	Tacking Permitted in Carryover Basis Transactions	157
(c)	Miscellaneous Tacking Provisions	158
	Revenue Ruling 62-140	160
	NOTE	161
	Problem for Discussion	161
§ 6.	SECTION 1231 GAINS AND LOSSES	161
§ 6.01	Overview	161
§ 6.02	The Mechanics of Section 1231	166
(a)	Types of Property Included Under § 1231	166
(b)	The Preliminary Hotchpot	167
(c)	The Primary Hotchpot	169
(d)	Non-Recaptured Net § 1231 Losses	171
§ 6.03	Definition of Property Used in the Trade or Business	173
(a)	Property Used in the Trade or Business	174
(b)	The Inventory Exclusion	175
(c)	Miscellaneous Property Under § 1231	176
	Problem for Discussion	177

TABLE OF CONTENTS

Chapter 3	LIABILITIES: DISCHARGE OF INDEBTEDNESS; MORTGAGED PROPERTY	179
<hr/>		
§ 1.	WHAT IS A LIABILITY?	180
§ 1.01.	Conditions and Contingencies	181
	<i>Milenbach v. Commissioner</i>	181
	<i>Milenbach v. Commissioner</i>	185
	Notes and Comments	186
	Problems for Discussion	187
§ 1.02.	Obligations v. Liabilities	188
	Rev. Rul. 80-198, 1980-2 C.B. 113	188
	Rev. Rul. 88-77, 1988-2 C.B. 129	190
	Notes and Comments	191
	<i>Albertson's, Inc. v. Commissioner</i>	191
	Notes and Comments	196
	Problems for Discussion	198
§ 2.	DISCHARGE OF INDEBTEDNESS (DOI)	199
§ 2.01.	What Is DOI Income?	199
	<i>United States v. Kirby Lumber Co.</i>	199
	Notes and Comments	200
	Problems for Discussion	202
§ 2.02.	Medium of Payment	203
	<i>United States v. Centennial Savings Bank FSB</i>	204
	Notes and Comments	207
	Problems for Discussion	209
§ 2.03.	Disputed or Contingent Liability	210
	<i>Zarin v. Commissioner</i>	210
	Notes and Comments	217
	Problems for Discussion	219
§ 3.	MORTGAGED PROPERTY	221
§ 3.01.	In General	221
§ 3.01(a).	Basis	221
	<i>Crane v. Commissioner</i>	222
	Notes and Comments	228
	Problems for Discussion	228
§ 3.01(b).	Amount Realized	229
	<i>Estate of Levine v. Commissioner</i>	229
	Notes and Comments	234
	Problem for Discussion	234
	<i>Commissioner v. Tufts</i>	235
	Notes and Comments	241
	Problem for Discussion	241

TABLE OF CONTENTS

§ 3.02.	Contingencies	242
	<i>Mayerson v. Commissioner</i>	242
	Notes and Comments	247
	<i>Est. of Franklin v. Commissioner</i>	248
	Notes and Comments	251
	Problems for Discussion	251
§ 3.03.	Speculative Security	252
	<i>Brountas v. Commissioner</i>	252
	Notes and Comments	258
	Problem for Discussion	259
§ 3.04.	<i>Tufts</i> and § 108(e)(5)	260
	<i>Fulton Gold Corp. v. Commissioner</i>	261
	Notes and Comments	262
	Rev. Rul. 91-31, 1991-1 C.B. 19	262
	Notes and Comments	263
	Problems for Discussion	265
§ 4.	LIABILITY TRANSFER	266
§ 4.01.	Primary and Secondary Liability	266
	<i>Lessinger v. Commissioner</i>	268
	Notes and Comments	274
	Problems for Discussion	276
§ 4.02.	Deficiency	278
	<i>Aizawa v. Commissioner</i>	278
	Notes and Comments	280
	Problem for Discussion	281
§ 4.03.	Deductible Items	281
	<i>Commercial Security Bank v. Commissioner</i>	281
	Notes and Comments	284
	Problem for Discussion	286
§ 5.	DOI INCOME AND § 108	287
§ 5.01.	Insolvency	288
	<i>Carlson v. Commissioner</i>	288
	Notes and Comments	293
	<i>Merkel v. Commissioner</i>	293
	Notes and Comments	297
	Rev. Rul. 90-16, 1990-1 C.B. 12	298
	Notes and Comments	299
	Problem for Discussion	299
§ 5.02.	Attribute Reduction	299
§ 5.03.	Basis Reduction — § 1017	300
	Problem for Discussion	302

TABLE OF CONTENTS

Chapter 4	CAPITALIZATION AND COST RECOVERY	305
§ 1.	INTRODUCTION	305
§ 1.01.	In General	305
§ 1.02.	The Economics of Capitalization and Cost Recovery	306
§ 2.	CAPITALIZATION	312
§ 2.01.	In General	312
	<i>Indopco, Inc. v. Commissioner</i>	316
	<i>Commissioner v. Idaho Power Co.</i>	321
	<i>Encyclopaedia Britannica, Inc. v. Commissioner</i>	328
	Notes and Comments	331
§ 2.02.	Uniform Capitalization Rules	332
	Problem for Discussion	336
§ 2.03.	Tangible Assets	337
	Problem for Discussion	342
§ 2.04.	Intangible Assets	342
	Problems for Discussion	347
§ 2.05.	Disputes and Litigation — Origin of the Claim	348
	<i>Woodward v. Commissioner</i>	348
	Problem for Discussion	351
§ 3.	COST RECOVERY FOR TANGIBLE ASSETS	351
§ 3.01.	In General	351
§ 3.02.	Start-Up Expenditures	352
	Revenue Ruling 99-23	354
	Problem for Discussion	359
§ 3.03.	Election to Expense Certain Business Assets	359
§ 3.04.	Expensing of Certain Capital Expenditures	361
(a)	Research and Experimental Expenses	361
	Notes and Comments	363
(b)	Environmental Remediation Costs	364
	Revenue Ruling 94-38	365
	Notes and Comments	368
	Problem for Discussion	368
(c)	Intangible Drilling Costs	369
(d)	Mining Exploration and Development	371
§ 3.05.	Bonus Depreciation	373
§ 3.06.	Modified Accelerated Cost Recovery System	375
(a)	General Principals	375
	<i>Simon v. Commissioner</i>	376
	Notes and Comments	387
(b)	Mechanics of Depreciation	387
	Revenue Procedure 87-56	392

TABLE OF CONTENTS

	Revenue Procedure 87-57	399
	Notes and Comments	418
(c)	Special Provisions	420
	Problems for Discussion	427
§ 3.07.	Amortization of Intangible Assets	428
(a)	Section 197 Intangibles Assets	429
(b)	Non-Section 197 Intangible Assets	432
	<i>Associated Patentees, Inc. v. Commissioner</i>	433
	Revenue Ruling 60-358	435
	Notes and Comments	437
	Problems for Discussion	440
§ 3.08.	Depletion	441
§ 4.	DEPRECIATION RECAPTURE	444
§ 4.01.	Personal Property	445
§ 4.02.	Real Property	448
§ 4.03.	Mining Interests and Timber	449
Chapter 5	NONRECOGNITION TRANSACTIONS	451
§ 1.	LIKE-KIND EXCHANGES	452
§ 1.01.	Exchange	453
	<i>Century Electric Co. v. Commissioner</i>	453
	<i>Jordan Marsh Co. v. Commissioner</i>	455
	Notes and Comments	459
	Problems for Discussion	461
§ 1.02.	Boot, Liabilities and Basis	462
§ 1.02(a).	Liabilities	464
	<i>Garcia v. Commissioner</i>	465
	Rev. Rul. 79-44, 1979-1 C.B. 265	467
	Notes and Comments	468
	Problem for Discussion	469
§ 1.02(b).	Boot and Installment Sales	470
	Installment Sales Revision Act of 1980	470
	Notes and Comments	472
	Problem for Discussion	474
§ 1.03.	Multiparty Exchanges	474
	Rev. Rul. 75-291, 1975-2 C.B. 332	474
	Rev. Rul. 77-297, 1977-2 C.B. 304	475
	<i>Barker v. Commissioner</i>	476
	Notes and Comments	479
	Problem for Discussion	481
§ 1.04.	Deferred Exchanges	483

TABLE OF CONTENTS

	<i>Starker v. United States</i>	483
	Notes and Comments	491
	Problem for Discussion	494
§ 1.05.	Reverse <i>Starker</i> Exchanges	496
	Rev. Proc. 2000-37, 2000-2 C.B. 308, <i>as modified by</i> Rev. Proc. 2004-51, 2004-2 C.B. 294	497
	Notes and Comments	502
	Problem for Discussion	504
§ 1.06.	Like Kind	506
	Rev. Rul. 82-96, 1982-1 C.B. 113	507
	Rev. Rul. 82-166, 1982-2 C.B. 190	508
	Notes and Comments	508
	Problems for Discussion	515
§ 1.07.	Held	516
	<i>Magneson v. Commissioner</i>	516
	Notes and Comments	521
	Problems for Discussion	523
§ 1.08.	Related Parties	524
	<i>Teruya Bros., Ltd. v. Commissioner</i>	525
	Notes and Comments	531
	Problem for Discussion	532
§ 2.	INVOLUNTARY CONVERSION	533
§ 2.01.	Involuntary	534
	<i>Willamette Industries, Inc. v. Commissioner</i>	535
	Notes and Comments	541
	Problem for Discussion	543
§ 2.02.	Similar in Service or Use	544
	Rev. Rul. 67-254, 1967-2 C.B. 269	544
	Notes and Comments	545
	Problem for Discussion	546
§ 2.03.	Investor-Lessor	546
	Rev. Rul. 64-237, 1964-2 C.B. 319	546
	Notes and Comments	547
	Problem for Discussion	548
§ 2.04.	Like Kind Revisited	549
	Rev. Rul. 67-255, 1967-2 C.B. 270	549
	Notes and Comments	550
	Problems for Discussion	552
§ 2.05.	Proceeds	552
	<i>Buffalo Wire Works Co. Inc. v. Commissioner</i>	553
	Notes and Comments	560

TABLE OF CONTENTS

	Problems for Discussion	561
§ 3.	OTHER NONRECOGNITION PROVISIONS	562
§ 3.01.	Installment Sales and Repossessions	562
	<i>Greene v. Commissioner</i>	563
	Notes and Comments	567
	Problems for Discussion	568
§ 3.02.	Principal Residences	569
	Rev. Proc. 2005-14, 2005-7 I.R.B. 528	571
	Notes and Comments	576
	Problem for Discussion	576
§ 3.03.	Charitable Contributions	578
	<i>Haverly v. United States</i>	578
	Notes and Comments	580
	Problem for Discussion	581
Chapter 6	EXECUTIVE COMPENSATION AND STOCK OPTIONS	583
<hr/>		
§ 1.	DEFERRED COMPENSATION	584
§ 1.01.	Traditional Deferred Compensation Principles	584
	Rev. Rul. 60-31, 1960-1 C.B. 174, <i>modified by</i> Rev. Rul. 64-279, 1964-2 C.B. 121 and Rev. Rul. 70-435, 1970-2 C.B. 100	584
	Notes and Comments	589
	Problem for Discussion	592
§ 1.02.	2004 Limitations — § 409A	593
	Problem for Discussion	598
§ 2.	RESTRICTED PROPERTY	599
§ 2.01.	Stock Appreciation Rights (SARs)	599
	Rev. Rul. 80-300, 1980-2 C.B. 165	599
	Notes and Comments	600
	Problem for Discussion	601
§ 2.02.	Restricted Property — § 83	602
	<i>Alves v. Commissioner</i>	607
	Notes and Comments	610
	Problems for Discussion	613
§ 2.03.	Shareholder Grants	614
	Rev. Rul. 80-76, 1980-1 C.B. 15	614
	Notes and Comments	615
	Problems for Discussion	615
§ 3.	NONSTATUTORY STOCK OPTIONS (NSOs)	616
§ 3.01.	Purchased Options	616
	Rev. Rul. 78-182, 1978-1 C.B. 265	617

TABLE OF CONTENTS

	Notes and Comments	623
	Problem for Discussion	624
§ 3.02.	Grant, Exercise and Lapse of NSOs	624
	<i>Commissioner v. Lo Bue</i>	625
	Notes and Comments	628
	Problems for Discussion	631
§ 3.03.	Transfers of NSOs	632
	<i>Weigl v. Commissioner</i>	632
	Notes and Comments	642
	Problems for Discussion	644
§ 3.04.	Noncompensatory NSOs	645
§ 3.04(a).	Determining Whether NSO Is Compensatory or Noncompensatory	646
	<i>Centel Communications Co., Inc. v. Commissioner</i>	647
	Notes and Comments	655
	Problem for Discussion	656
§ 3.04(b).	Noncompensatory Options Taxed on Exercise	657
	<i>Sun Microsystems, Inc. v. Commissioner</i>	657
	Notes and Comments	662
	Problems for Discussion	664
§ 3.05.	Valuing NSOs	665
	Problems for Discussion	666
§ 4.	INCENTIVE STOCK OPTIONS (ISOs)	667
§ 4.01.	ISO Requirements and Effects	667
	<i>Schumann v. Commissioner</i>	670
	Notes and Comments	672
	Problems for Discussion	674
§ 4.02.	Alternative Minimum Tax (“AMT”) and ISOs	676
§ 4.02(a).	Computing the AMT	676
	Notes and Comments	678
	Problem for Discussion	678
§ 4.02(b).	The AMT and ISOs	679
	<i>Gresham v. Commissioner</i>	679
	Notes and Comments	682
	<i>Merlo v. Commissioner</i>	682
	Notes and Comments	686
	Problem for Discussion	687
§ 4.02(c).	Net Operating Loss (“NOL”) Carryovers Under the AMT (“ATNOL”) and ISOs	688
	<i>Spitz v. Commissioner</i>	688
	Notes and Comments	692

TABLE OF CONTENTS

Chapter 7	ADVANCED CHARACTERIZATION PROBLEMS	695
§ 1.	REALITY OF SALE (SALE v. LEASE)	696
§ 1.01.	Bootstrap Sales	697
	<i>Commissioner v. Brown</i>	697
	Notes and Comments	704
	Problem for Discussion	705
§ 1.02.	Natural Resource Interests	706
	<i>Wood v. United States</i>	706
	Rev. Rul. 69-352, 1969-1 C.B. 34	710
	Notes and Comments	711
	Problem for Discussion	712
§ 1.03.	Retained Interest v. Amount Realized	713
	<i>Alstores Realty Corp. v. Commissioner</i>	713
	Notes and Comments	718
	Problems for Discussion	719
§ 1.04.	Lease versus Sale	721
	Rev. Rul. 55-540, 1955-2 C.B. 39	722
	Notes and Comments	726
	<i>Est. of Starr v. Commissioner</i>	726
	Notes and Comments	729
	Problem for Discussion	729
§ 1.05.	Leveraged Leasing	729
	<i>Frank Lyon Co. v. United States</i>	731
	Notes and Comments	742
	Rev. Proc. 2001-28, 2001-1 C.B. 1156	744
	Notes and Comments	751
	Problems for Discussion	751
§ 2.	TRANSFERS OF PARTIAL INTERESTS	752
§ 2.01.	Gratuitous Transfers of Partial Interests	752
§ 2.01(a).	Income from Services	753
	<i>Lucas v. Earl</i>	753
	Notes and Comments	754
	Problems for Discussion	755
§ 2.01(b).	Income from Property	756
	<i>Blair v. Commissioner</i>	757
	<i>Helvering v. Horst</i>	757
	<i>Harrison v. Schaffner</i>	760
	Notes and Comments	761
	Problems for Discussion	762
§ 2.01(c).	Appreciated Property versus Realized Income (How Ripe is the Fruit?)	762

TABLE OF CONTENTS

	<i>Ferguson v. Commissioner</i>	762
	Notes and Comments	767
	Problem for Discussion	768
§ 2.01(d).	Escrows	769
	Problems for Discussion	770
§ 2.02.	Sales of Partial Interests — Ordinary Income Substitute	770
	<i>Hort v. Commissioner</i>	771
	<i>McAllister v. Commissioner</i>	773
	<i>Metropolitan Building Co. v. Commissioner</i>	775
	<i>Commissioner v. P. G. Lake, Inc.</i>	776
	Notes and Comments	779
	Problems for Discussion	781
§ 3.	INTANGIBLES — CONTRACT RIGHTS, SELF-CREATED PROPERTY, AND GOODWILL (AND GOING CONCERN VALUE)	781
§ 3.01.	Contract Rights	782
	<i>Commissioner v. Ferrer</i>	782
	Notes and Comments	789
	Problem for Discussion	790
§ 3.02.	Future Services versus Goodwill	791
	<i>Bisbee-Baldwin Corp. v. Tomlinson</i>	791
	Notes and Comments	796
	Problems for Discussion	800
§ 3.03.	Artists, Inventors, Franchises	801
§ 3.03(a).	Copyrights	802
	Rev. Rul. 54-409, 1954-2 C.B. 174	802
	Rev. Rul. 54-599, 1954-2 C.B. 52	803
	Notes and Comments	804
	Problem for Discussion	805
§ 3.03(b).	Patents	805
	<i>Kueneman v. Commissioner</i>	806
	Notes and Comments	808
	Problem for Discussion	809
§ 3.03(c).	Franchises and Trade Names	810
	<i>Stokely USA, Inc. v. Commissioner</i>	810
	Notes and Comments	817
	Problem for Discussion	818
§ 4.	RELATED TAXPAYERS	818
§ 4.01.	§ 482 — Applicability	818
	<i>Foglesong v. Commissioner</i>	819
	<i>Foglesong v. Commissioner</i>	825
	Notes and Comments	829
	Problem for Discussion	830

TABLE OF CONTENTS

§ 4.02.	§ 482 — Applied	831
	<i>Hamburgers York Road, Inc. v. Commissioner</i>	831
	Notes and Comments	839
	Problems for Discussion	840
Chapter 8	LIMITATIONS ON DEDUCTIONS AND LOSSES	843
<hr/>		
§ 1.	INTRODUCTION	843
§ 2.	WASH SALES OF SECURITIES	844
	<i>Estate of Estroff v. Commissioner</i>	847
	Notes and Comments	850
	Problems for Discussion	852
§ 3.	LOSSES BETWEEN RELATED PARTIES	852
	Rev. Rul. 76-377, 1976-2 C.B. 89	855
	Notes and Comments	856
	Problem for Discussion	857
§ 4.	AT-RISK RULES	857
§ 4.01.	In General	858
	Staff of the Joint Committee on Taxation	862
	Notes and Comments	868
§ 4.02.	At-Risk Amount	872
	<i>Hubert Enterprises, Inc. v. Commissioner</i>	874
	Notes and Comments	879
§ 4.03.	Stop Loss Agreements	881
	<i>American Principals Leasing Corp. v. United States</i>	882
	Notes and Comments	891
§ 4.04.	Qualified Nonrecourse Financing	894
	Problem for Discussion	895
§ 5.	PASSIVE LOSSES	896
§ 5.01.	In General	896
	S. Rep. No. 99-313, 99th Cong., 2d Sess. 713-718 (1986)	897
§ 5.02.	Passive, Non-Passive, and Investment Activities	902
§ 5.03.	Material and Significant Participation	905
	<i>Thompson v. United States</i>	907
	Notes and Comments	917
§ 5.04.	Rental Activities	918
	<i>Bailey v. Commissioner</i>	920
§ 5.05.	Self-Charged Items	928
	<i>Hillman v. Internal Revenue Service</i>	929
§ 5.06.	Disposition of a Passive Activity	934
	Problems for Discussion	935
§ 6.	LIMITATIONS ON LOSSES FROM LEASING TRANSACTIONS	936

TABLE OF CONTENTS

U.S. TREASURY DEPARTMENT 937
H.R. Rep. No. 108-755, 108th Cong., 2d Sess. 654–663 (2004) 940

TABLE OF CASES TC-1

TABLE OF STATUTES TS-1

TABLE OF SECONDARY AUTHORITIES TA-1

INDEX I-1
