Tax Court of the United States, manifest error occurred and intervened to the prejudice of the Commissioner who now assigns the following errors and each of them, which he avers occurred in said record, proceedings, opinion and final decision so rendered and entered by The Tax Court of the United States:

1. The Tax Court erred in failing and refusing to sustain the deficiency in tax determined by the Commissioner.

2. The Tax Court erred in entering its decision wherein and whereby it was ordered and decided that there is a deficiency in income tax of only $27.77 for the calendar year 1938.

3. The Tax Court erred in holding and deciding that the amount of the mortgage was not part of the "amount realized" by the taxpayer from the sale and that the only amount realized by her was $2,500.

4. The Tax Court erred in holding and deciding that the basis of the property in the hands of the taxpayer was zero.

5. The Tax Court erred in failing and refusing to hold and decide that, as determined by the Commissioner, the amount realized by the taxpayer upon the sale of the apartment house property was $257,500, that the basis to [fol. 63] the taxpayer of said property was $262,042.50, of which amount $207.042.50 was allocable to the apartment building, that the adjusted basis of the said building to the faxpayer at the date of sale was $178,997.40 ($207,042.50 minus $28,045.10 depreciation), and that, accordingly, the taxpayer realized a taxable ordinary gain of $24,031.50 from the sale of the building and a capital loss of $528.85 from the sale of the land.

6. The Tax Court erred in that its holding and decision are not supported by bu' are contrary to its findings of fact and the facts as stipulated by the parties.

7. The Tax Court erred in that its opinion and decision are not supported by its findings of fact and are contrary to law.

Wherefore, the Commissioner petitions that the decision of The Tax Court of the United States be reviewed by the United States Circuit Court of Appeals for the Second Circuit, that a transcript of the record be prepared in accordance with law and with the rules of said Court and transmitted to the Clerk of said Court for filing, and that appropriate action be taken to the end that the erors complained of may be reviewed and corrected by said Court.

Samuel O. Clark ——, Assistant Attorney General;
J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, Attorneys for Petitioner on Review.

Of Counsel: Charles E. Lowery, Special Attorney, Bureau of Internal Revenue.

[fol. 64] *Duly sworn to by Charles E. Lowery. Jurat omitted in printing.*

[fol. 65] [File endorsement omitted.]

IN THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

[Title omitted]

NOTICE OF FILING PETITION FOR REVIEW—Filed Aug. 21, 1944

To Mrs. Beulah B. Crane, 35-64 80th Street, Jackson Heights, County of Queens, New York, New York.

You are hereby notified that the Commissioner of Internal Revenue did, on the 16th day of August, 1944, file with the Clerk of the Tax Court of the United States, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Second Circuit of the decision of the Tax Court heretofore rendered in the above-entitled cause. A copy of the petition for review, and assignments of error as filed is hereto attached and served upon you.

Dated this 16th day of August, 1944.

(Signed) J. P. Wenchel, CAR, Chief Counsel, Bureau of Internal Revenue.

Personal service of the above and foregoing notice, together with a copy of the petition for review and assignments of error mentioned therein, is hereby acknowledged this 18 day of August, 1944.

Beulah B. Crane, Respondent on Review.

[fols. 66-88] [File endorsement omitted.]

IN THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

[Title omitted]

NOTICE OF FILING PETITION FOR REVIEW—Filed Aug. 21, 1944

To Edward S. Bentley, Esq., 20 Exchange Place, New York, New York.

You are hereby notified that the Commissioner of Internal Revenue did, on the 16th day of August, 1944, file with the Clerk of The Tax Court of the United States, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Second Circuit of the decision of the Tax Court heretofore rendered in the above-entitled cause. A copy of the petition for review and assignments of error as filed is hereto attached and served upon you.

Dated this 16th day of August, 1944.

(Signed) J. P. Wenchel, CAR, Chief Counsel, Bureau of Internal Revenue.

Personal service of the above and foregoing notice, together with a copy of the petition for review and assignments of error mentioned therein, is hereby acknowledged this 17th day of August, 1944.

(S.) Edward S. Bentley, Attorney for Respondent on Review.

[fol. 89] IN UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT, OCTOBER TERM, 1945

No. 23

(Argued November 14, 1945. Decided December 28, 1945.)

Docket No. 19825

COMMISSIONER OF INTERNAL REVENUE, Petitioner,

vs.

BEULAH B. CRANE, Respondent

Before: L. Hand, Swan and Frank, Circuit Judges

On petition of the Commissioner of Internal Revenue to review an order of the Tax Court, expunging a deficiency, assessed against the respondent in her income tax for the year 1938.

Morton K. Rothschild, for the petitioner.

Edward S. Bentley, for the respondent.

OPINION

[fol. 90] L. HAND, Circuit Judge:

The Commissioner appeals from an order of the Tax Court, expunging a deficiency assessed against the taxpayer in her income tax for the year 1938. The question is of the amount of the gain realized upon a sale in that year of a parcel of real property. The facts were as follows. The taxpayer was the widow of one, Crane, who died on January 11, 1932, and who by his will devised to her an apartment house in Brooklyn, on which at the time there was a mortgage of $262.042.50, and which was appraised at his death at exactly that amount. The taxpayer allowed the mortgage to remain in default (accounting to the mortgagee for rentals), until the accumulated interest had risen to $15,857.71, and the mortgagee threatened to foreclose. To avoid this on November 29, 1938, she sold the property for $3000 to a realty corporation, subject to the mortgage and to past due taxes; but, since the expenses of the sale were $500, she received only $2500 net. In the

years 1932-1936, inclusive, she had filed income tax returns as executrix of the devisor, in each of which she had claimed and had been allowed deductions for depreciation upon the building; and in the years 1937 and 1938 she had claimed and been allowed similar deductions in her individual income tax return. In the year here in question the Commissioner allowed her a loss upon the land, measured by the difference between its value at the time of the devise and its proper proportion of the sum of the principal of the mortgage and $2500. However, he also assessed her for a gain measured by the difference between the building's proper proportion of the same sum and its value at the time of the devise, which however he reduced by the deductions for depreciation. The appeal does not concern the figures; it only raises the question whether the taxpayer [fol. 91] is right—as the Tax Court held, two judges dissenting—in insisting that the only gain for which she was taxable was the $2500, which she received upon the sale.

Although the taxpayer was the devisor's sole legatee, the Commissioner does not suggest that she was liable upon his bond, if indeed he was himself liable. The case is therefore to be decided on the assumption that her only relation to the mortgagee was that as devisee of the land, she took it encumbered by the lien of the mortgage. When we speak of her as the "mortgagor," this must be implied. Section 113(a)(5) defines the "unadjusted basis" of property in the case of a devise as its "fair market value" when it was acquired, which in the case at bar was its appraised value as part of the devisor's estate. To find the "adjusted basis" under §111(a) an "adjustment • • • shall • • • be made • • • for • • • wear and tear • • • to the extent allowed (but not less than the amount allowable)": §113(b)(1)(B). Section 114(a) makes the "basis" for depreciation as a deduction from income the same as the "adjusted basis" fixed by §113(b); and it follows, if the value of mortgaged property at the time of its devise is the value of the equity, as the taxpayer asserts, that the annual allowance for depreciation must be computed upon that value, and that it will represent only that fraction of the actual "wear and tear" suffered by the buildings which their proportion of the equity bears to their actual value. The gain upon which the mortgagor must pay a tax will indeed be reduced so far as actual "wear and tear" reduces the selling price, and we may assume for

argument that the allowance for depreciation and this reduction will be the same. Yet, so far as the mortgagor has not been allowed for depreciation by progressive instalments, the allowance will all come in one year, which is clearly contrary to the intent of the act—§23(l)—and to [fol. 92] the uniform practice of the Treasury. Moreover, to treat the equity as the basis for depreciation requires repeated recomputations, if the mortgagor pays in instalments and introduces administrative complication and confusion extremely undesirable, if it is possible to avoid them. We cannot doubt, especially in view of the long uniform practice, that the right "basis" for depreciation is the actual value of the buildings.

If so, unless the "adjusted value" of the buildings is not computed upon the same value in finding the subtrahend in the equation of gain, the taxpayer gets a double deduction. By hypothesis he will have been allowed deductions seriatim, based upon the actual value of the buildings; and he will in addition have got a reduction in his gain to the extent to which actual "wear and tear" has reduced the selling price. Manifest justice demands that he must surrender one or the other, and the only question is whether the language of the statute forbids that result. The taxpayer concedes, as we understand it—in any event it is the law—that, if she had been liable upon the bond and the vendee had released her, the release would have been "property (other than money) received" within the meaning of §111(b). *United States* v. *Hendler*, 303 U. S. 564. She insists, however, that because she was not liable, the lien should not be considered as an equivalent. But the lien of a mortgage does not make the mortgagee a co-tenant; the mortgagor is the owner for all purposes; indeed that is why the "gage" is "mort," as distinguished from a "vivum vadium." *Kortright* v. *Cady*, 21 N. Y. 343, 344. He has all the income from the property; he manages it; he may sell it; any increase in its value goes to him; any decrease falls on him, until the value goes below the amount of the lien. The mortgagee is a creditor, and in effect nothing more than a preferred creditor, even though the [fol. 93] mortgagor is not liable for the debt. He is not the less a creditor because he has recourse only to the [illegible], unless we are to deny the term to one who may levy upon only a part of his debtor's assets. When therefore upon a sale the mortgagor makes an allowance to the ven-

dee of the amount of the lien, he secures a release from a charge upon his property quite as though the vendee had paid him the full price on condition that before he took title the lien should be cleared, or as though it were a condition upon the sale of Whiteacre that the vendee should clear the vendor's Blackacre of a mortgage. In neither case would anyone question the conclusion that the vendor had received "property (other than money)"; yet the effect is precisely the same of the transaction at bar.

To this the taxpayer answers that the result may be, as it was here, to subject the mortgagor to a tax upon a gain which is out of all proportion to what he in fact receives; to a tax which may indeed be greater than the whole consideration received. That is true, but it is the consequence of his continuing in a venture from which he is free to retire whenever he concludes that all opportunity for gain has ended. He is not charged with gain except upon "a sale or other disposition" of the property—§111(a)—and if he abandons it to the mortgagee there is no gain. *Bingham* v. *Commissioner*, 105 Fed. (2) 971 (C. C. A. 2); *Polin* v. *Commissioner*, 114 Fed. (2) 174 (C. C. A. 3); *Commissioner* v. *Hoffman*, 117 Fed. (2) 987 (C. C. A. 2). Nor has the mortgagor been deprived of this expedient by the decision of the Supreme Court in *Helvering* v. *Hammel*, 311 U. S. 504, which held that a foreclosure sale is a "sale" within §111(b). The Third Circuit has since then twice held that he may still abandon the property, forestalling a foreclosure sale by the tender of a deed to the mortgagee; and we agree. *Stokes* v. *Commissioner*, 124 Fed. (2) 335; *Commissioner* v. *Green*, 126 Fed. (2) 70. (*Semble*, *Stam-*

[fol. 94] *ler* v. *Commissioner*, 145 Fed. (2) 37 (C. C. A. 3). True, a slight sum of money will make the transaction a sale, even when the parties may not have looked on it as such (*Blum* v. *Commissioner*, 133 Fed. (2) 447 (C. C. A. 2); but escape is open to the mortgagor as soon as he decides to treat the venture as at an end. If he does not, especially when as here he seeks to realize a profit upon it, it is plain right that he should be compelled to take the transaction as a whole, including such past advantages as he may have been entitled to as allowances for depreciation.

Order reversed.

SWAN, Circuit Judge, dissenting:

I think that the order should be affirmed for the reasons stated in the Tax Court's opinion, 3 T. C. 585.

[fol. 95] IN UNITED STATES CIRCUIT COURT OF APPEALS,
SECOND CIRCUIT

COMMISSIONER OF INTERNAL REVENUE, Petitioner,

v.

BEULAH B. CRANE, Respondent

Appeal from The Tax Court of the United States

JUDGMENT—Filed December 28, 1945

This cause came to to be heard on the transcript of record from The Tax Court of the United States, and was argued by counsel.

On Consideration Whereof, it is now hereby ordered, adjudged, and decreed that the order of said The Tax Court of the United States be and it hereby is reversed.

It is further ordered that a Mandate issue to the said The Tax Court of the United States in accordance with this decree.

Alexander M. Bell, Clerk.

[File endorsement omitted.]

[fol. 96] Clerk's Certificate to foregoing transcript omitted in printing.

[fol. 97] SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed April 29, 1946

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit is granted, and the case is transferred to the summary docket.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied

the petition shall be treated as though filed in response to such writ.

Mr. Justice Jackson took no part in the consideration or decision of this application.

[fol. 98] IN THE SUPREME COURT OF THE UNITED STATES

STIPULATION—Filed May 28, 1946

Subject to the approval of this Honorable Court, it is hereby stipulated and agreed by and between the attorneys for the parties in the above-entitled cause that, for the purposes of the writ of certiorari, the printed record shall consist of the following:

1. Docket entries.
2. Petition for a redetermination by Tax Court.
3. Answer.
4. Stipulation of facts and Exhibits A to L inclusive attached thereto.
5. Findings of fact and opinion of Tax Court.
6. Decision of Tax Court.
7. Petition for review.
8. Notice of filing petition for review.
9. Proceedings in the Circuit Court of Appeals.
10. This stipulation.

——— ———, Attorney for Petitioner. J. Howard McGrath, Solicitor General of the United States, Attorney for Respondent.

Dated, this 21st day of May, 1946.

[fol. 99] [File endorsement omitted]

Endorsed on Cover: Enter Edward S. Bentley. File No. 50,697. U. S. Circuit Court of Appeals, Second Circuit. Term No. 68. Beulah B. Crane, Petitioner, vs. Commissioner of Internal Revenue. Petition for a writ of certiorari and exhibit thereto. Filed March 25, 1946. Term No. 68 O. T. 1946.