

STATE OF NEW YORK,
County of New York, ss:

On the 28th day of Nov., one thousand nine hundred and thirty-eight, before me came Beulah B. Crane to me known to be the individual described in, and who executed, the foregoing instrument, and acknowledged that she executed the same.

Raymond C. Cochrane.

Raymond D. Cochrane, Notary Public, Kings Co. Clk. No. 506, Reg. No. 9156. New York County Clks. No. 293, Reg. No. 9C343. Bronx County Clks. No. 3, Reg. No. 122C89. Queens County Clks. No. 1712, Reg. No. 6675. Nassau County Clks. No. 9C22 Certificate filed in Westchester County. Commission expires Mar. 30, 1939.

[fol. 46] [Endorsed:] No. —. to Deed the land affected by the within instrument lies in Block — in Section — on the Land Map of the County of Title Guarantee and Trust Company. Offices: 176 Broadway, New York; 175 Remsen Street, Brooklyn; 160-08 Jamaica Ave., Jamaica; 6 East 45th Street, New York; 370 East 149th Street, Bronx; Bridge Plaza North, L. I. City; 56 Bay Street, St. George, S. I.; Mineola, Long Island; Riverhead, Long Island, White Plains, New York.

[fol. 47] IN THE TAX COURT OF THE UNITED STATES

BEULAH B. CRANE, Petitioner,

COMMISSIONER OF INTERNAL REVENUE, Respondent

Docket No. 110361.

Promulgated April 7, 1944

Under the will of her husband petitioner acquired improved real property consisting of an apartment house and the land upon which it was located, which at the date of his death was subject to a mortgage in an amount equal to the fair market value of the property at that date. Petitioner never assumed the mortgage debt. She sold the property

and received \$2,500 in cash from the vendee, who took title subject to the mortgage. Held:

(1) The amount of the mortgage is not part of the "amount realized" by the petitioner from the sale and the only amount realized by her was \$2,500.

(2) The basis of the property in the hands of the petitioner is zero.

(3) Under the provisions of section 113 (b), (1) (B) of the Revenue Act of 1938, the basis of zero can not be reduced on account of depreciation of the building.

(4) The apartment house on the land was not a capital asset, as was the land within the meaning of section 117 (a) of the Revenue Act of 1938, and the portion of the gain allocable to the sale of the building is taxable in full as an ordinary gain, while the portion allocable to the sale of the land is taxable as a capital gain.

Edward S. Bentley, Esq., for the petitioner.
Carl A. Philipps, Esq., for the respondent.

Respondent determined a deficiency of \$1,932.99 in income tax for 1938. The sole question for determination is the amount of the gain realized by the petitioner from the disposition in the taxable year of property previously acquired by her by devise from her deceased husband. The parties have filed a stipulation of facts, which we adopt as part of our findings of fact. The stipulated facts not set forth herein are included by reference.

[fol. 48]

FINDINGS OF FACT

The petitioner, a resident of Jackson Heights, New York, is the widow of William M. Crane, who died on January 11, 1932. She filed her 1938 income tax return in the first district of New York.

William M. Crane (hereinafter referred to as the decedent) was a resident of Westchester County, New York, at the time of his death. His will was probated in the Surrogate's Court of that county on January 31, 1932, and under the provisions thereof the petitioner was his sole legatee and devisee. The petitioner was also the duly qualified executrix of the decedent's estate. The estate was settled and distributed on December 31, 1936.

The decedent owned an apartment house and the premises on which it was located in Brooklyn, New York, which, at the time of his death, was subject to a first mortgage held by the Bowery Savings Bank, on which there was due at that time \$255,000 principal and \$7,042.50 accrued interest, or the total sum of \$262,042.50. For the purpose of the Federal estate tax the property was appraised as of January 11, 1932, at a value of \$262,042.50 and the amount due on the mortgage was likewise appraised at \$262,042.50. In the Federal estate tax return filed by the petitioner as executrix of the estate of the decedent, the property was reported at the value of \$262,042.50 and the amount due on the mortgage was reported as an indebtedness of the estate in the same amount.

On February 1, 1932, and at all times thereafter until the property was sold and conveyed on November 29, 1938, as hereinafter stated, the mortgage was in default for the nonpayment of interest. In the early part of 1932 the petitioner and the Bowery Savings Bank entered into an agreement whereby the petitioner was to operate the apartment house property, collect the rents, and pay for all necessary repairs, wages, and other expenses, reserve \$200 a month for the payment of taxes, and remit the balance, or net rentals, to the bank at the end of each month on account of the mortgage. The net rentals from the premises for the years 1932 to 1938, inclusive, were paid to the bank by the petitioner in accordance with the agreement and applied to the payment of interest on the mortgage.

In 1938 the mortgage was in default for nonpayment of principal in the amount of \$255,000, and interest in the amount of \$15,857.71, and the bank was about to foreclose its mortgage. In order to avoid such action the petitioner in October 1938 entered into a contract to sell the property to the Avenue C Realty Corporation. The contract of sale provided, in part, as follows:

• • • the seller [petitioner] agrees to sell and convey, [here follows a description of the real estate] • • •

[fol. 49] Subject to a first mortgage now a lien on said premises, held by Bowery Savings Bank, upon which there is due the principal sum of • • • (\$255,000.) and ar-

rears of interest in the sum of • • • (\$15,857.71) and interest to accrue after this date.

Subject to real estate taxes for the second half of the year 1938 and to water meter charges.

The purchase price is • • • (\$3,000.) for the equity conveyed by the seller and without deduction for the mortgage principal, interest or taxes or meter charges hereinabove referred to; and the purchaser has deposited the sum of • • • (\$1,000.) in escrow to be paid to the seller at the time of closing title under this contract • • •

The deed shall • • • convey to the purchaser, the fee simple of the said premises, free of all encumbrances except as herein stated.

Pursuant to the contract, title was closed on November 29, 1938, and on that date the petitioner, individually and as executrix of the decedent's estate and as sole devisee and legatee, conveyed the property to the purchaser, "subject to a first mortgage now a lien on said premises, held by Bowery Savings Bank, upon which there is due the principal sum of • • • (\$255,000.) and arrears of interest." The petitioner received \$3,000 in cash from the purchaser and paid expenses of the sale in the amount of \$500. The petitioner was not a party to the mortgage or to the bond which secured it. She did not at any time assume any personal liability upon the mortgage.

Petitioner filed income tax returns for the estate of the decedent covering the period January 11 to December 31, 1932, and the years 1933, 1934, 1935, and 1936, and individual income tax returns for the years 1937 and 1938. In those returns, in addition to income from other sources, she reported the rentals from the apartment house as gross income and claimed deductions for interest paid on the mortgage, and for the taxes on and operating expenses of the property. She also claimed deductions for depreciation on the building as follows:

| | | | |
|------|---------|------|---------|
| 1932 | \$3,500 | 1936 | \$3,900 |
| 1933 | 3,800 | 1937 | 3,500 |
| 1934 | 3,800 | 1938 | 3,200 |
| 1935 | 3,800 | | |

In her income tax return for 1938 the petitioner reported a net loss of \$2,164.15. She reported a capital gain

of \$2,500 from the sale of the apartment house property and included one-half thereof, or \$1,250, in her income.

The respondent determined that the petitioner sustained a capital loss of \$528.85 (allowable to the extent of 50 percent) from the sale of the land, and that she realized an ordinary gain of \$24,031.45 from the sale of the building. The loss and gain were computed in the following manner:

[fol. 50]

| | | |
|--------------------------------------------------------------|--------------|----------------|
| Selling price | \$54,471.15 | \$203,028.85 |
| Cost or basis: | | |
| Land | 55,000.00 | |
| Building | \$207,042.50 | |
| Less depreciation at 2% on \$207,042.50: | | |
| 1932-38 | \$24,845.10 | |
| 1938 (claimed and allowed) | 3,200.00 | |
| | 28,045.10 | 178,997.40 |
| 50% of loss allowable | Loss 528.85 | Gain 24,031.45 |
| 100 of gain on sale of a building which is not capital asset | 244.42 | 24,031.45 |

The "selling price" set out in the tabulation just above is comprised of the \$2,500 net cash received by petitioner on the sale and the \$255,000 principal due on the mortgage.

The parties have stipulated that the appraised value of the property as of the date of the decedent's death, namely, \$262,042.50, may be considered as having been allocated as follows: land, \$55,000; improvements, \$207,042.50; that the "selling price" of the property may be considered as having been allocated in the proportion determined by the respondent, namely 5447115/25750000 to the land and 20302885/25750000 to the improvements; and that the rate of depreciation applicable to the building is 2 percent per annum.

OPINION

Tyson, Judge:

The question for determination is the amount of the petitioner's gain or loss from the sale of the property which she had acquired by devise. The applicable statutory pro-

visions found in the Revenue Act of 1938 are set forth in the margin.

[1. 51] The respondent found the amount realized by petitioner on the sale to be \$257,500 and the basis to be \$262,042.50. The amount realized is composed of the \$255,000 principal due on the mortgage at the time of the sale and the \$2,500 net cash received from the purchaser, as conceded by respondent at the hearing and on brief; and the basis is the value at which the property was appraised for the purpose of the Federal estate tax, which value was in an amount identical with the amount of \$255,000 principal due on the mortgage at decedent's death plus \$7,042.50 accrued interest thereon. The respondent allocated the basis and the amount realized between the land and the building, as shown in our findings of fact, and then reduced the portion of the basis allocated to the build-

SEC. 111. DETERMINATION OF AMOUNT OF, AND RECOGNITION OF, GAIN OR LOSS.

(a) Computation of Gain or Loss.—The gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in section 113(b) for determining gain, and the loss shall be the excess of the adjusted basis provided in such section for determining loss over the amount realized.

(b) Amount Realized.—The amount realized from the sale or other disposition of property shall be the sum of any money received plus the fair market value of the property (other than money) received.

SEC. 113. ADJUSTED BASIS FOR DETERMINING GAIN OR LOSS.

(a) Basis (Unadjusted) of Property.—The basis of property shall be the cost of such property; except that—

(5) Property Transmitted at Death.—If the property was acquired by bequest, devise, or inheritance, or by the decedent's estate from the decedent, the basis shall be the fair market value of such property at the time of such acquisition.

(b) Adjusted Basis.—The adjusted basis for determining the gain or loss from the sale or other disposition of property, whenever acquired, shall be the basis determined under subsection (a), adjusted as hereinafter provided.

ing (\$207,042.50) by \$28,045.10 on account of Depreciation on the building for the years 1932 to 1938. This resulted in an adjusted basis of \$178,997.40 for the building. On the basis of his findings, he determined an ordinary gain of \$24,031.45 from the sale of the building and a capital loss of \$528.85 from the sale of the land.

The petitioner's first contention is that the inclusion of the amount of the mortgage in the amount realized for the property is improper, on the ground that she acquired that property encumbered by the mortgage debt, which she never assumed and for which she was never personally liable; and that consequently she did not receive, and could not have received, any benefit or consideration, as regards the mortgage, by reason of her transfer of the property subject to the mortgage. Petitioner's second contention is that, having acquired the property with a mortgage encumbrance thereon equal to its fair market value, she acquired a mere equity in the property the value of which was zero, and that when she sold the property she realized a taxable gain of only \$2,500 (the \$3,000 cash received less \$500 as expenses of the sale).

The respondent's position is that his action in including the amount of the mortgage in the amount realized from the sale, in fixing the basis at \$262,042.50, and in reducing

(1) General Rule.—Proper adjustment in respect of the property shall in all cases be made—

(B) in respect of any period since February 28, 1913, for exhaustion, wear and tear, obsolescence, amortization, and depletion, to the extent allowed (but not less than the amount allowable) under this Act or prior income tax laws.

SEC. 114. BASIS FOR DEPRECIATION AND DEPLETION.

(a) Basis for Depreciation.—The basis upon which exhaustion, wear and tear, and obsolescence are to be allowed in respect of any property shall be the adjusted basis provided in section 113(b) for the purpose of determining the gain upon the sale or other disposition of such property.

that basis by the amount of \$28,045.10 for depreciation, was not in error, and that petitioner's gain is not to be determined on the theory that she acquired and sold a mere equity in the property.

[fol. 52] The first question presented by the respective contentions of the parties is whether the amount of the mortgage constitutes part of the "amount realized" by petitioner from the sale. Section 111(b), *supra*, provides that the "amount realized" from the sale of property shall be "the sum of any money received plus the fair market value of the property (other than money) received." The facts show and the respondent concedes, that petitioner received money to the extent of only \$2,500 from the sale. If the petitioner had assumed liability for the payment of the mortgage debt and her vendee had in turn assumed petitioner's liability, such assumption by the vendee would be the equivalent of the receipt of "money" by the petitioner to the extent of the amount of the liability so assumed. *Brons Hotels, Inc.*, 34 B. T. A. 376; *Walter F. Haass*, 37 B. T. A. 948. Cf. *United States v. Hendler*, 303 U. S. 564; *Pender v. Commissioner*, 110 Fed. (2d) 477. However, the petitioner acquired the property by devise and did not assume liability for payment of the mortgage debt. She took title "subject to the mortgage and never was under a personal obligation to pay it, or any part of it." *Helvering v. Southwest Consolidated Corporation*, 315 U. S. 194. As she was never under any personal obligation to pay the mortgage debt she received no consideration whatever when she sold and conveyed the property subject to the mortgage, except the \$2,500 in money mentioned above. *Commonwealth, Inc.*, 36 B. T. A. 850; *James B. Lapsley*, 44 B. T. A. 1105; and *Polin v. Commissioner*, 114 Fed. (2d) 174. Except for the \$2,500, the petitioner thus did not receive money, or the equivalent of money, or property (other than money) having a fair market value, and it was error for the respondent to include the amount of the mortgage in the "amount realized" from the sale.

In support of his contention that the amount of the mortgage should be included in the amount realized from the sale of the property, respondent relies upon article 44-2 of Regulations 101, which provides that in the case of a sale on the installment basis of mortgaged real property, "the amount of the mortgage, whether the property is merely taken subject to the mortgage or whether the

mortgage is assumed by the purchaser, shall be included as a part of the 'selling price.' It suffices to say that this regulation applies only to sales, on the installment plan, of real property involving deferred payments to the vendor and relates to the returning of profits from such sales. It is obvious that the sale by petitioner was not such a sale and that the regulation has no application here.

The amount realized by the petitioner from the sale, therefore, was \$3,000 less the \$500 paid for conveyancing, or \$2,500.

The next question presented is the proper basis of the property for the determination of petitioner's gain or [fol. 53] loss on her sale. The first and essential factor to be determined in this connection is the unadjusted basis of the property. This unadjusted basis is that established by section 113(a)(5), *supra*, to wit, the fair market value of the property at the time of its acquisition. Time of acquisition here means the date of the husband's death. *Brewster v. Gage*, 280 U. S. 327; *Elizabeth G. Augustus*, 40 B. T. A. 1201; *affd.*, 118 Fed. (2d) 38; *certiorari denied*, 313 U. S. 585.

There is no dispute here as to the fair market value of the apartment house property at the basic date. That value is \$262,042.50, which was used for estate tax purposes. However, the property when acquired by the petitioner was encumbered by a mortgage in an amount which, together with the accrued interest thereon, was equal to the fair market value of the property. It is thus apparent that the interest of petitioner in the apartment house property had no fair market value whatever when acquired by her. It further appears that petitioner paid nothing on the mortgage during her ownership of the property, except the interest which she paid out of the rentals received by her from the property, and this would preclude any claim of a cost basis on account of an investment in the property by the petitioner even if such claim were made. *Fulton Gold Corporation*, 31 B. T. A. 519; *cf. P. J. Hiatt*, 35 B. T. A. 292; and *Hotel Astoria, Inc.*, 42 B. T. A. 759. It follows that petitioner's unadjusted basis is zero.

The issue then narrows down to the question of whether petitioner's unadjusted basis of zero should be adjusted

on account of the depreciation allowed in prior years and in the taxable year.

In the ordinary case, that is where there is a basis for property, the adjustment on account of depreciation operates to reduce that basis, which, as so reduced, is to be offset against the amount realized in determining the gain or loss; and section 113(b)(1)(B), *supra*, in providing that the adjusted basis for determining gain or loss "shall be the basis determined under [section 113(a)(5)] adjusted" for depreciation, obviously contemplates the existence of an unadjusted basis—that there exists a minuend from which depreciation allowed, or allowable can be deducted. See *Woolford Realty Co. v. Rose*, 286 U. S. 319, 327. We have determined that the unadjusted basis of the property in question, under section 113(a)(5), is zero, and, this being true, there is, in the very nature of things, nothing to adjust—nothing from which depreciation can be deducted.

Having found that petitioner's unadjusted basis is zero and that such basis can not be adjusted to a minus quantity, we conclude and so hold that the proper basis to be used in computing petitioner's gain is zero, and, as the amount realized by her from the sale of the property was only \$2,500, that her gain from the sale is in the same [fol. 54] amount. In view of this holding it is unnecessary to decide or consider the question of whether or not depreciation on the property for prior years was properly allowed or allowable in those years; but since depreciation in the amount of \$3,200 was allowed for the taxable year 1938, and that year is before us, we hold that such depreciation was improperly allowed for the reason that there is no basis upon which to compute depreciation—the unadjusted basis being zero.

In her income tax return for 1938 the petitioner reported a gain of \$2,500 from the sale of the property and included one-half thereof in her income as a capital gain. In her petition she alleges error by the respondent in ruling that the building was not a capital asset and in treating the gain as an ordinary gain taxable in full. The petitioner does not argue this question and contends in her brief only that her gain was not in excess of \$2,500. The respondent contends that the building is not a capital asset within the meaning of section 117 of the Revenue Act of

1933,² and that the profit realized from the sale of the building is an ordinary gain taxable in full. We think the respondent's contention is sound.

Section 117, in subdivision (a), defines the term "capital assets" and states that the term "does not include . . . property, used in the trade or business, of a character which is subject to the allowance for depreciation provided in section 23(1)." The allowance provided in section 23(1) is "a reasonable allowance for exhaustion, wear and tear." The apartment house building is property which loses value through exhaustion, wear, and tear, and hence is property of a character which is subject to the allowance provided in section 23(1). *Even Realty Co.*, 1 B. T. A. 355, 359, 362. The petitioner, upon default in the mortgage, was permitted to remain in possession and operate the property under an arrangement whereby the net rents or profits were applied on payment of taxes and payment of interest on the mortgage. This, in our opinion, was use of the property in the petitioner's trade or business. The building thus meets the tests of depreciable character and business use, and it is a noncapital asset and not subject to the capital gain and loss provisions of section 117, *supra*.

² SEC. 117. CAPITAL GAINS AND LOSSES.

(a) Definitions.—As used in this title—

(1) Capital Assets.—The term "capital assets" means property held by the taxpayer (whether or not connected with his trade or business), but does not include . . . property, used in the trade or business, of a character which is subject to the allowance for depreciation provided in section 23(1):

(b) Percentages Taken Into Account.—In the case of a taxpayer, other than a corporation, only the following percentages of the gain or loss recognized upon the sale or exchange of a capital asset shall be taken into account in computing net income:

50 per centum if the capital asset has been held for more than 24 months.

[fol. 55] The parties have stipulated that, for the purpose of this proceeding, the "selling price" or the amount realized from the sale of the property "may be considered as having been allocated" between the land and building in the proportions set forth in our findings of fact. Inasmuch as \$2,500 was the total "selling price," or amount realized, and such amount also constituted the sole gain derived from the sale, such gain should be allocated as follows: 5447115/25750000 to the land and 20302885/25750000 to the building. The amount allocated to the land constitutes capital gain, taxable at capital gain rates, and the amount allocated to the building constitutes ordinary gain, taxable in full.

Reviewed by the Court.

Decision will be entered under Rule 50.

SMITH and DISNEY, JJ., dissent.

[fol. 56] IN THE TAX COURT OF THE UNITED STATES,
WASHINGTON.

Docket No. 110361

BEULAH B. CRANE, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

DECISION

Pursuant to the Court's Findings of Fact and Opinion, promulgated April 7, 1944, the respondent having filed a recomputation of tax on May 9, 1944, and the petitioner having filed an acquiescence in said recomputation on May 15, 1944, it is:

Ordered and Decided: That there is a deficiency in income tax of \$27.77 for the calendar year 1938.

Enter:

(Signed) John A. Tyson, Judge.

Entered May 19, 1944.

[fol. 57] IN THE UNITED STATES CIRCUIT COURT OF APPEALS
FOR THE SECOND CIRCUIT

[File endorsement omitted]

[Title omitted]

PETITION FOR REVIEW AND ASSIGNMENTS OF ERROR—Filed
August 16, 1944

To the Honorable Judges of the United States Circuit Court
of Appeals for the Second Circuit:

Now Comes Joseph D. Nunan, Jr., Commissioner of Internal Revenue, by his attorneys; Samuel O. Clark, Jr., Assistant Attorney General; J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and Charles E. Lowery, Special Attorney, Bureau of Internal Revenue, and respectfully shows:

I

Jurisdiction

That he is the duly appointed, qualified and acting Commissioner of Internal Revenue of the United States; holding his office by virtue of the laws of the United States; that the respondent on review, Beulah B. Crane (hereinafter called the taxpayer), is a citizen of the United States residing at 35-64 80th Street, Jackson Heights, in the County of Queens, City and State of New York. The taxpayer filed her Federal income tax returns for the calendar year 1938, the taxable year here involved, with the Collector of Internal Revenue for the First District of New York [fol. 58] whose office is located in the City of Brooklyn, New York, and within the jurisdiction of the United States Circuit Court of Appeals for the Second Circuit.

The Commissioner files this petition pursuant to the provisions of Sections 1141 and 1142 of the Internal Revenue Code.

II

Prior Proceedings

On January 5, 1942, the Commissioner determined a deficiency in Federal income tax liability against the taxpayer in the amount of \$1,932.99 for the taxable year 1938

and sent to the taxpayer, by registered mail, a notice of said deficiency in accordance with the provisions of existing internal revenue laws. Thereafter and on April 1, 1942, the taxpayer filed an appeal from the Commissioner's determination with The Tax Court of the United States. The case was duly tried and submitted to the Tax Court and on April 7, 1944, the court promulgated its findings of fact and opinion pursuant to which opinion decision was entered on May 19, 1944 "that there is a deficiency in income tax of \$27.77 for the calendar year 1938."

III

Notice of Controversy

The taxpayer is the widow of William M. Crane who died on January 11, 1932. She was the sole legatee and devisee under the will of her deceased husband and the executrix of his estate which was settled and distributed on December 31, 1936. At the time of his death the decedent owned an apartment house and the premises on which it was located [fol. 59] in Brooklyn, New York, which property was on that date subject to a first mortgage on which there was due a principal of \$255,000 and accrued interest in the amount of \$7,042.50. In the Federal estate tax return filed by the taxpayer as executrix the property was reported at the value of \$262,042.50, the amount of the unpaid mortgage and interest, and the amount so due on the mortgage was reported as an indebtedness of the estate. The property was appraised, for purposes of the Federal estate tax, at the value of \$262,042.50 as of January 11, 1932 and the amount due on the mortgage was likewise appraised at \$262,042.50.

The mortgage was in default for the nonpayment of interest at all times after January 31, 1932 (the date on which decedent's will was probated in the Surrogate's Court of Westchester County, New York) until the property was sold and conveyed by the taxpayer on November 29, 1938 as hereinafter stated.

Early in the year 1932 the taxpayer entered into an arrangement with the Bowery Savings Bank, the holder of the first mortgage on the property in question, whereby she was to operate the apartment house property, collect the rents, and pay for necessary repairs, wages, and other

expenses, reserve \$200 a month for the payment of taxes, and turn the balance over to the bank at the end of each month on account of the mortgage. Accordingly the net rentals from the property for the years 1932 to 1938, inclusive, were paid to the bank by the taxpayer and applied to the payment of interest on the mortgage. In 1938, in order to avoid a threatened foreclosure action by the bank, the taxpayer entered into a contract to sell the property to the Avenue C Realty Corporation, subject to the first mortgage, which was due in the amount of \$255,000 and upon which interest was in arrears in the sum of [fol. 60] \$15,857.71, and subject to real estate taxes for the second half of the year 1938 and to water meter charges. In the contract of sale the purchase price was designated as: " . . . (\$3,000) for the equity conveyed by the seller and without deduction for the mortgage principal, interest or taxes or meter charges hereinabove referred to; . . . " The property was conveyed to the purchaser, or its assignee, on November 29, 1938 by the taxpayer "individually and as sole executrix and devisee and legatee under the Last Will and Testament of William M. Crane, deceased, probated in the Surrogate's Court of Westchester County" subject to the first mortgage lien thereon and arrears of interest. The taxpayer received the \$3,000 in cash specified in the contract of sale and paid expenses of the sale amounting to \$500.

The rentals received from the apartment house were returned as gross income in the Federal income tax returns filed for decedent's estate for the period January 11 to December 31, 1932 and the years 1933, 1934, 1935 and 1936, and in the individual Federal income tax returns of the taxpayer for the years 1937 and 1938. Deductions were claimed in those returns for interest paid on the mortgage, for the taxes on and operating expenses of the property, and for depreciation on the building. In her individual Federal income tax return for the year 1938, the taxpayer reported a capital gain of \$2,500 from the sale of the apartment house property one-half of which, or \$1,250, she returned as taxable income. In his examination of the taxpayer's Federal income tax liability for that year the Commissioner determined a capital loss of \$528.85 from the sale of the land and an ordinary gain of \$24,031.45 from the sale of the building, both determinations having been based on allocations, as between the land and the building,

of the appraised value of the property as of the date of [fol. 61] decedent's death and the "selling price" of the property by the taxpayer in 1938, as to the correctness of which allocations the parties have agreed for the purpose of this proceeding. In his determination the Commissioner likewise reduced the basis allocated to the building (\$207,042.50) by \$28,045.10 representing depreciation on the building for the years 1932 to 1938, inclusive.

The taxpayer disputed the inclusion by the Commissioner of the amount of the mortgage as having been realized by the taxpayer for the property when it was transferred by her, on the ground that since she had not assumed the mortgage she was never personally liable thereon. She contended that she had acquired a mere equity in the property the value of which was zero and that when she sold the property her taxable gain was measured by the difference between the \$3,000 cash received by her in the transaction and the expense of \$500 incurred by her on the sale.

In deciding the issue for the taxpayer and contrary to the holding of the Commissioner, the Tax Court held that the amount of the unsatisfied mortgage was not part of the "amount realized" by the taxpayer from the sale, that her basis was zero, and that the only amount realized by her was \$2,500 (\$3,000 for her equity less \$500 expenses). The court sustained the Commissioner's determination that the apartment house was not a capital asset within the meaning of Section 117(a) of the Revenue Act of 1938, and that the portion of the gain allocable to the sale of the building is taxable in full as an ordinary gain. The court held further that depreciation in the amount of \$3,200 was improperly allowed for the taxable year 1938 "for the reason that there is no basis upon which to compute depreciation—the unadjusted basis being zero." [fol. 62] Based on its holding, as aforementioned, the Tax Court redetermined a deficiency in income tax against the taxpayer in the amount of \$27.77 for the taxable year 1938.

IV

Assignments of Error

The Commissioner avers that in the record and proceedings before The Tax Court of the United States and in the opinion and final decision rendered and entered by The

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 taxpayer 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 but 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 Cir-

cuit, 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 errors 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.