

SURVEY OF INCOME TAX SLIDES	BRIEF HISTORY	CODE STRUCTURE	COURT SYSTEM
TOP 100 CODE SECTIONS	TOP 40 TAX DOCTRINES	TOP 100 TERMS	TAX ETHICS
ON-LINE TAX AUTHORITIES	OFFICIAL TAX AUTHORITIES	TAX LL.M. PROGRAMS	5 SUGGESTED READINGS
INDEX	TAX HUMOR	NAVIGATION INSTRUCTIONS	50 IMPORTANT FORMS

# INTRODUCTION TO TAX SCHOOL

## TOP 100 TAX CASES

(ALPHABETICAL ORDER)

1. [Albertson's Inc. v. Comm'r, 42 F.3d 537 \(9th Cir. 1994\).](#) **Section 404 defers the deduction for the interest component of non-qualified deferred compensation.** Section 404 applies both to the compensation and "interest" component of non-qualified deferred plans, resulting in deduction at the time of inclusion by the recipient. Effectively, the decision defines compensation for the use of money as something other than interest. This decision raised significant controversy in the mid-1990's. Some argued that it discourages non-qualified deferred compensation; others argue that indeed it encourages that which it intended to discourage. The case ignored contrary legislative history and effectively repealed section 467(g), an important time value of money provision. The Court applied what it termed the "matching principle" of tax law, which required income and deductions to match in terms of timing. Arguably, this strange aspect of the case reflects the Court's misunderstanding the Matching Principle of Accounting, which requires a person or entity to match income with the costs of producing that income and which has nothing to do with separate entities or persons.
2. [Arkansas Best Corp. v. Commissioner, 485 U.S. 212 \(1988\).](#) **The Corn Products Doctrine applies only to hedging transactions.** See *Corn Products v. Commissioner*, 350 U.S. 46 (1955). This decision largely ended the *Corn Products* debacle. Although the government won *Corn Products*, the decision largely favored taxpayers. It held that property "integrally related" to a trade or business could not be a capital asset; hence, security investments in an essential supplier or customer produced ordinary gains rather than capital gains. In reality, however, the government had difficulty using the decision. Taxpayers with gains tended to report them as capital – and relied on the government having a difficult task detecting contrary investment motivations. Taxpayers with losses tended to report them as ordinary, taking advantage of the Corn Products Doctrine.

3. *Arrowsmith v. Commissioner*, 344 U.S. 6 (1952). The character of a transaction is a function of the transaction as a whole, even if it transcends multiple years. The case involved the sale of property at a capital gain. Later, the seller learned of and accepted responsibility for an un-expected liability. Payment of the liability in a later year was not a “sale or exchange,” required for capital loss treatment; nevertheless, the Court required capital loss treatment, viewing the transaction as a whole. This is an important exception to the general rule that each year stands alone, as established by the *Burnet v. Sanford & Brooks*, 282 U.S. 359 (1931), *North American Oil Consolidated v. Burnet*, 286 U.S. 417 (1932) and *U.S. v. Lewis*, 340 U.S. 590 (1951) cases. Significantly, *Arrowsmith* affects neither whether an amount is deductible (or includible) nor when it would be so: the decision affects only the character of the item. Also, the case dealt with deductions; *whether it applies to income items is unsettled*.
4. *Artnell Co. v. Commissioner*, 400 F.2d 981 (7th Cir. 1968). Taxpayers may sometimes defer recognition of pre-paid service income until the year of performance. The Chicago White Sox baseball team was allowed to defer recognition of prepaid service income for ticket sales. The period was short and the accuracy was large. This often-cited decision is a very narrow exception to the Trilogy of cases, in which the Supreme Court thrice held that accrual method taxpayers must include amounts pre-paid for services. See, *Schlude v. Commissioner*, 372 U.S. 128 (1963). Those cases essentially place accrual method taxpayers on the cash method for the receipt of pre-paid items (but see section 467(f) which changes this rule for rent payments in excess of \$250,000).
5. *Battlestein v. Commissioner*, 631 F.2d 1182 (5th Cir. 1980) (*en banc*). A taxpayer may not “pay” an amount with funds borrowed from the creditor immediately prior to the attempted “payment.” Contrast this with the *Burgess v. Commissioner*, 8 T.C. 47 (1947) distinction. This decision is important for its attempt to define what constitutes “payment.” Note that “payment” is an important factor for the cash method of accounting and for many code sections, such as sections 170 and 461.
6. *Better Business Bureau of Washington, D.C., Inc. v. United States*, 326 U.S. 279 (1945). Organizations which are overly commercial are not entitled to exempt status under section 501(c)(3) and its precursors. They are not “charities” and thus are not entitled to the special treatment that accompanies that category. They may be “mutual benefit societies” and entitled to exempt status under another provision, such as section 501(c)(6). The court thus introduced what has become known as the “commerciality doctrine.”

7. *Blair v. Commissioner*, 300 U.S. 5 (1937). The Assignment of Income Doctrine does not apply to a gift of a portion of an income right if the donor only owns the income right and not the underlying property. Donor was a trust income beneficiary. He gave his daughter a portion of the income rights for the remainder of the trust. Because this was a gift of part of all he owned, it was not an assignment of income. Daughter was taxed. Contrast this with *Harrison v. Schaffner*, 312 U.S. 579 (1941) in which the donor gave away a portion of his income interest, but only for a term of years, rather than for the remaining life of the trust.
8. *United States v. Bliss Dairy, Inc.*, 460 U.S. 370 (1983). An event "Fundamentally Inconsistent" with a proper beneficial deduction in an earlier year sometimes results in income. The "recovery requirement" of the tax benefit rule no longer applies. This was a companion case to *Hillsboro National Bank v. Commissioner*, 460 U.S. 370 (1983). The tax benefit rule applies only if the original treatment resulted from a court-created policy doctrine rather than a congressionally created doctrine. In this case, the Courts permitted the deduction of some pre-paid expenses, but failed to create a provision triggered by an event fundamentally inconsistent with the deduction. Hence, the Court created a doctrine under which income resulted from such an event.
9. *Bob Jones University v. Simon*, 416 U.S. 725 (1974). Racial discrimination in schools violates fundamental public policy; as a result, organizations which practice such discrimination are not entitled to exempt status under section 501(c)(3). Also, Section 501(c)(3) organizations must demonstrably serve the "public interest." This second aspect of the case prompted some concurring objections and resulted in some academic controversy. The fears centered on whether the IRS would have the non-statutorily approved authority to define the "public interest." The Court's "public interest test," however, has not proved to have had much practical impact.
10. *Boise Cascade Corp. v. United States*, 530 F.2d 1367 (Ct. Cl. 1976). Taxpayers may sometimes defer recognition of pre-paid service income until the year of performance. This decision is a narrow exception to the Trilogy of cases, in which the Supreme Court thrice held that accrual method taxpayers must include amounts pre-paid for services. See, *Schlude v. Commissioner*, 372 U.S. 128 (1963). It is arguably the most important of six such exceptions because it involved a significant amount of money, a significant period of time, and uncertainty as to the time period. This importance is tempered by its being a mere Claims Court opinion.

11. *Commissioner v. Boylston Market Association*, 131 F.2d 966 (1942). A cash method taxpayer who acquires or creates an asset with a life extending substantially beyond the end of the current year must capitalize the cost of the asset and amortize it over its useful life. Subsequent cases and Treasury Regulations have focused on the meaning of “substantially,” generally defining it as more than twelve months. Without explanation as to why, the Court required straight-line amortization. As least as to pre-paid rent, section 467(f) changed this aspect of the case: it recognizes the interest and consequent time value of money components inherent in pre-payments.
12. *Helvering v. Bruun*, 309 U.S. 461 (1940). Lessee improvements result in “gross income” for the lessor equal to their fair market value. Section 109 subsequently modified this holding statutorily by excluding the value of such improvements unless they represent rent. Section 1019 limits the basis of the property by also excluding the non-rent improvements.
13. *Bull v. United States* 295 U.S. 247 (1935). The Doctrine of Equitable Recoupment applies to the government in District Court. As a result, the Court may deny a refund of an overpayment of tax if the taxpayer treated the same item inconsistently in another year. The same case, in the Tax Court, could not result in a deficiency because that would result in the forbidden offensive use of the doctrine. The District Court use of the Doctrine is a sometimes called an “offensive/defensive” use. It is used offensively to increase tax, but defensively to prevent a refund. This case also illustrates a problematic aspect of Equitable Recoupment: by filing with the Tax Court, the taxpayer effectively waives the government’s ability to use the Doctrine. See also, *Stone v. White*, 301 U.S. 532 (1937) and *United States v. Dalm*, 494 U.S. 596 (1990).
14. *Burgess v. Commissioner*, 8 T.C. 47 (1947). A taxpayer may “pay” an amount with borrowed funds, sometimes even if the creditor is also the lender. This is an important issue in what constitutes a “payment.” Many code sections depend upon the occurrence of a “payment,” as does, in general, the cash method of accounting. Compare to the *Battlestein v. Commissioner*, 631 F.2d 1182 (5th Cir. 1980) (*en banc*) distinction. See, *Davison v. Commissioner*, 141 F.3d 403 (2nd Cir. 1998) (significantly limiting, if not rejecting, *Burgess*).

15. *Burnet v. Logan*, 283 U.S. 404 (1931). A taxpayer need not recognize gain in an “open transaction” until he has recovered his capital. This involved the sale of stock in an iron mine for cash plus 60 cents per ton of ore mined by the buyer. The taxpayer argued for no income or gain recognition until she had recovered her investment in the stock. The Circuit Court of Appeals ruled it was impossible to determine with fair certainty the market value of the agreement by the buyer to pay 60 cents per ton. The taxpayer was thus entitled to the return of her capital before she could be charged with any taxable income. “When the profit, if any, is actually realized, the taxpayer will be required to respond.”
16. *Bynum v. Commissioner*, 46 T.C. 295 (1966). Whether an *investor* in specific property has converted his holding purpose to that of a *dealer* involves a balancing of specific factors. The Tax Court listed many specific important factors used in determining whether a taxpayer investor (whose status results in capital treatment) in specific property has converted his holding purpose to that of a dealer (resulting in ordinary treatment). This interprets the frequent code phrase, “property held primarily for sale to customers in the ordinary course of a trade or business.”
17. *Chevron, U.S.A., Inc. v. National Resources Defense Council, Inc.*, 467 U.S. 837 (1984). The judiciary must defer to an executive agency's interpretation of a statute that the agency administers, provided that the agency's interpretation is reasonable. This was not a tax case, but affects tax cases. In a later case, *United States v. Mead Corp.*, 533 U.S. 218 (2001), the Court clarified that *Chevron Deference* applies only to more formal types of agency interpretations. According to most tax authorities all Treasury regulations qualify for *Chevron Deference*; however, some confusion remains in the courts regarding this issue. For a discussion of this confusion, see *Swallows Holding, Ltd. v. Commissioner*, 126 T.C. No. 6 at 125-140, Doc 2006-1541, 2006 TNT 18-10 (2006) (J. Holmes dissenting). Steve R. Johnson, *Swallows as it Might Have Been--Regulations Revising Caselaw*, 112 Tax Notes 773 (Aug. 28, 2006) ; American Bar Association Section of Taxation Task Force on Judicial Deference (drafted by Irving Salem, Ellen P. Aprill, and Linda Galler), reprinted in Tax Notes, Sept. 13, 2004, p. 1231.
18. *Commissioner v. Clay Brown*, 380 U.S. 563 (1965). Risk shifting is not an essential element of a sale. This historically important decision prompted the unrelated debt financed provisions of section 514. It approved what was termed a “boot-strap” sale in which a tax exempt entity purchased a for-profit business and used the business operations to pay for itself. Essentially, the scheme converted ordinary income into capital gain through

the use of the entity's exempt status. The case remains important (not just historical) in that it elucidates the meaning of "ownership." Because many tax benefits and detriments follow ownership, it is important to understand who owns what in a tax sense. See *Frank Lyon Co. v. United States*, 435 U.S. 561 (1978). Congress enacted section 514, dealing with unrelated debt financed income of tax exempt organizations, as a result of this case.

19. *Cohan v. Commissioner*, 39 F. 2d 540 (2d Cir. 1930). If the amount deductible is not certain, a Court should estimate it. "Absolute certainty in such matters is usually impossible and is not necessary." The Court "should make as close an approximation as it can, bearing heavily if it chooses upon the taxpayer whose inexactitude is of his own making." Allowing nothing would be "inconsistent with saying that something was spent."
20. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977). A state tax on the "privilege of doing business" in the state is not per se unconstitutional when it is applied to interstate commerce. The Spector Rule from 1951 is overruled. The Court explained that its prior rule was frequently distinguished or even ignored; this case put it to rest. States may tax interstate commerce that has an impact on the state. The statute in question referred to taxing the "privilege" of doing business, as opposed to the action of doing business. The Court bemoaned cases that focused too heavily on the wording as opposed to the substance of the state statute.
21. *Cook v. Tait*, 265 U.S. 467 (1924) The United States can impose a tax even when the person receiving the income and the property from which he received it were not within the territorial limits of the United States. A native citizen who was taxed could be domiciled in a foreign country or the property that generated the income could be located in a foreign country and the U.S. still has power to impose the tax.
22. *Corn Products Refining Co. v. Commissioner*, 350 U.S. 46 (1955). The section 1221 list of non-capital assets is illustrative rather than exclusive. Of mostly historical importance this decision held that property "integrally related" to a trade or business was not a capital asset. Common scenarios involving the Corn Products Doctrine involved investment in the securities of a critical supplier or customer. As "integrally related" to the business, any resulting gains were ordinary rather than capital. Losses, too, resulted in ordinary treatment and proved to be the most common application of the decision. As a result, the government regretted winning this decision. The Court subsequently severely limited the case in *Arkansas Best v. Commissioner*, 485 U.S. 212 (1988).



23. *Cottage Savings Association v. Commissioner*, 499 U.S. 554 (1991). The “realization” requirement of gross income is a matter of administrative convenience rather than constitutional significance. Arguably, this limited the important *Glenshaw Glass* opinion (though the Court does not cite *Glenshaw Glass*, which dealt with income realization rather than loss realization). The matter involved the exchange of loan portfolios which were “materially different” from those received, although they were very similar. Because of the differences, the loss from the exchange was “sustained” under section 165. Much of the case rested on the lack of clear regulations defining a “material difference” standard. Absent such administrative authority, the Court looked to its own opinions. Arguably, the result (and thus the concept of “realization”) could be change prospectively by clear administrative pronouncements.
24. *Commissioner v. Court Holding Co.*, 324 U.S. 331 (1945). Under the assignment of income doctrine, transferee completion of a transaction negotiated and fully arranged by a transferor may be attributed to the transferor along with an imputed transfer of the proceeds. The *Court Holding* case involved a corporate transfer to shareholders. Subsequent cases have involved donor transfers to donees. For example, a parent may fully arrange the sale of property at a substantial gain. She might then transfer the “almost done deal” to her children for final arrangements. The *Court Holding Company Doctrine* will assign the profits to the transferor. How close a transferor can get to completion prior to transfer of such plans raises practical and ethical dilemmas. The scheme works best when the taxpayers are subject to substantially different brackets.
25. *Cowden v. Commissioner*, 289 F.2d 20 (5th Cir. 1961). 1. At the inception of a contract, a cash method taxpayer may defer the receipt of payments without triggering the constructive receipt doctrine. 2. A cash method taxpayer has income upon receiving a “cash equivalent”: an unconditional promise to pay of a solvent obligor, readily transferable, not subject to set-off and not subject to a discount substantially greater than the prevailing rate. The first holding is very important because few exceptions exist for deferrals after performance has begun. See, *Martin v. Commissioner*, 96 T.C. 814 (1991) and *Veit v. Commissioner*, 8 T.C. 809 (1947). The second holding creates the Cash Equivalency Doctrine.
26. *Crane v. Commissioner*, 331 U.S. 1 (1947). The amount realized in a taxable transaction includes the relief of non-recourse debt to which the property is subject. The case, in footnote 37, deferred resolution of whether this rule applied if the amount of the debt exceeded the fair market value of the property transferred. *Commissioner v. Tufts*, 461 U.S. 300

(1983) held that it did. Many people mistakenly cite *Crane* for the proposition that an asset's basis includes the amount of debt (recourse or non-recourse) incurred or acquired in connection with its acquisition. *Crane*, however, dealt only with the issue of the amount realized on disposition of an encumbered asset. See *Parker v. Delaney*, 186 F.2d 455 (1st Cir. 1950) for the proposition concerning basis.

27. *Crummey v. Commissioner*, 397 F. 2d 82 (9<sup>th</sup> Cir. 1968). A deposit into a trust which grants the beneficiary a *Crummey* power is a "completed" gift of a present interest and qualifies for the gift tax annual exclusion amount in §2503(b). A *Crummey* power entitles the beneficiary the right to withdraw the deposited amount for a period of time (usually 30 days is sufficient). The result is a present right to possession which is equivalent to actual possession. If the power is not exercised, then the power lapses and the deposit remains in the trust corpus.
28. *United States v. Dalm*, 494 U.S. 596 (1990). The Doctrine of Equitable Recoupment cannot be used to open a closed year; instead, it creates an open year refund right – or denies one – to offset erroneous treatment in a closed year. A donee paid the gift tax on a substantial gift. Later, the government sought income tax on the item. Mistakenly, the donee sought a District Court refund of the gift tax, which was barred by the statute of limitations. The donee should have sought Equitable Recoupment of the gift tax against the income tax deficiency in the Tax Court (which since 2006 clearly has jurisdiction to apply the Doctrine.)
29. *United States v. Davis*, 370 U.S. 65 (1962). The use of appreciated property to satisfy an obligation or to acquire something of value is a taxable event. The taxpayer used appreciated stock to satisfy marital obligations and had taxable gain as a result. The Court presumed the recipient had no income, but did not explain why. To the extent a *Davis* scenario involves a transfer of "property" between spouses or incident to divorce, section 1041 overrules this case. Exactly what constitutes "property" under section 1041, however, is uncertain. Along with the case *Kenan v. Commissioner*, 114 F.2d 217 (2d Cir. 1940) this type of income is sometimes referred to as Davis/Kenan Gain.
30. *Deputy v. du Pont*, 308 U.S. 488 (1940). An ordinary expense is one that is normal, usual or customary; a transaction that gives rise to it must be of common or regular occurrence in the type of business involved. This historic decision helped define ordinary and necessary business expenses. "But allowance of deductions from gross income does not turn on general



equitable considerations. It depends upon legislative grace. . . .” “To be sure, an expense may be ordinary though it happen but once in the taxpayer's lifetime. . . . Yet the transaction which gives rise to it must be of common or frequent occurrence in the type of business involved. . . . Hence, the fact that a particular expense would be an ordinary or common one in the course of one business and so deductible under § [162] does not necessarily make it such in connection with another business.”

31. **Diebold v. United States** 891 F.2d 1579 (Fed. Cir. 1989). Errors by a taxpayer in two consecutive years can amount to an “accounting method” such that the taxpayer must continue to make the same error in future years unless it receives permission to change accounting methods. As a result, such a change, whether requested or forced, will trigger section 481 adjustments, effectively repealing the statute of limitations on deficiencies. This important, but controversial decision has an impact on the application of the Tax Benefit Rule: it replace the Rule in cases to which it applies.
32. **Doyle v. Mitchell Brothers Company**, 247 U.S. 179 (1918). The taxpayer is entitled to recover the taxpayer's invested capital tax-free before deriving gain from the property. “In order to determine whether there has been gain or loss if any, we must withdraw from the gross proceeds an amount sufficient to restore the capital value that existed at the commencement of the period under consideration.” This early decision prompted current sections 1001 and 1012, deal with basis and basis recovery.
33. **Commissioner, v. Duberstein**, 363 U.S. 278 (1960). A gift for income tax purposes results from “detached and disinterested generosity.” In mixed motive cases (involving both gift and compensatory intent), the dominant motive controls. Clearly this case applies if the dominant motive is compensatory. Whether it would also apply if the dominant motive reflects a gift is doubtful: in such cases, some courts have bifurcated the transaction.
34. **Eisner v. Macomber**, 252 U.S. 189 (1920). Stock dividends do not result in “gross income.” The case explained that income derives from capital or labor. “Mere growth or increment of value in a capital investment is not income; income is essentially a gain or profit in itself of exchangeable value, proceeding from capital, severed from it, and derived or received by the taxpayer for his separate use, benefit and disposal.” This aspect of the case was of Constitutional importance, not just statutory. The later decision in *Commissioner, v. Glenshaw Glass*, 348 U.S. 426 (1955) expanded on the meaning of income,

35. *Helvering v. Eubank*, 311 U.S. 122 (1940). Service income is taxed to the person who performs the services. This is a companion case to *Helvering v. Horst*, 311 U.S. 112 (1940), which applied the Assignment of Income Doctrine to donative transfers of the income from property. *Eubank* involved a future stream of income from insurance renewal premiums.
36. *Flint v. Stone Tracy Co.*, 220 U.S. 107 (1911). The 1909 excise tax of 1% of a corporation's net earnings was a proper and constitutional excise tax rather than an unconstitutional "direct" income tax. Later the Sixteenth Amendment, in 1913, made possible the individual direct income tax. Previously, in 1895, the Supreme Court declared an individual income tax unconstitutional.
37. *Ford Motor Co. v. Commissioner*, 71 F.3d 209 (6th Cir. 1995). Time value of money principles apply to the deduction of tort obligations. This case is mostly of historical importance since the enactment of section 461(h) in 1986. An understanding of it, however, is helpful for two purposes: 1. It helps illustrate the effect of the time value of money, particularly for deductions; 2. It aids in an understanding of deductions related to torts and sections 461(h), 468B, 104 and 130. The case ended the common practice in which a tortfeasor deducted the face amount of future obligations rather than the present value. Section 461(h)(2)(C), instead, defers deduction of such amounts until payments, precluding the deduction of the present value, as approved by *Ford*. Sections 130 and 468B, however, permit the deduction of the present value in some instances. Whether the *Ford* approach or the current statutory scheme is better tax policy remains controversial and results in substantial practical implications.
38. *Frank Lyon Co. v. United States*, 435 U.S. 561 (1978). In a genuine multiple-party transaction with economic substance the Government should honor the contractual allocation of rights and duties effectuated by the parties, in particular the allocation of ownership versus lessee/creditor status. This controversial case involved a sale-leaseback in which the taxpayer took title to a building under construction and simultaneously leased the building back to the bank/seller for long-term use. The Court held this was not a simple sham; thus, the taxpayer could claim deductions such as interest and depreciation. The case helps distinguish ownership from creditor status. The taxpayer was the "owner," although the Bank had the risk of loss, as non-recourse creditor.

39. *General Utilities & Operating Co. v. Helvering*, 296 U.S. 200 (1935). The use of appreciated property to pay a dollar denominated dividend did not result in gain to the distributing corporation. This created what was known as, for many years, the *General Utilities Doctrine*. Legislatively repealed in 1986, this case permitted tax-free liquidations under former section 337.
40. *Commissioner, v. Glenshaw Glass*, 348 U.S. 426 (1955). Gross income results from “Undeniable accessions to wealth, clearly realized, and over which the taxpayers have complete dominion.” The matter involved the punitive two-thirds of a treble damage award. Despite language in *Eisner v. Macomber*, 252 U.S. 189 (1920), income is not limited to items derived from capital or labor. Subsequent cases have focused on the words “undeniable,” “accession to wealth,” “clearly realized,” and “complete dominion.” The 1991 *Cottage Savings* decision arguably demotes this case to one of administrative convenience rather than Constitutional importance. The “accession to wealth” factor raises significant accounting issues regarding whether an event, to be taxable, must result in “wealth” in an accounting (single year) or transactional sense.
41. *Golsen v. Commissioner*, 54 T.C. 742 (1970). The Tax Court is bound by case authorities from the circuit to which the case before it is appealable. Generally this is where the taxpayer lives, per section 7482. This is known as the *Golsen Rule*. It results in the Court rendering inconsistent opinions.
42. *Gregory v. Helvering*, 293 U.S. 465 (1935). Form controls over substance unless substance controls over form. This very frequently cited case appears to stand for conflicting propositions. The Court stated: “The legal right of a taxpayer to decrease the amount of what otherwise would be his taxes, or altogether avoid them, by means which the law permits, cannot be doubted.” But, the Court held: “The rule which excludes from consideration the motive of tax avoidance is not pertinent to the situation, because the transaction upon its face lies outside the plain intent of the statute. To hold otherwise would be to exalt artifice above reality and to deprive the statutory provision in question of all serious purpose.” The case is also the father of the Business Purpose Doctrine.
43. *Commissioner v. Groetzinger*, 480 U. S. 23 (1987). To be engaged in a trade or business, a taxpayer must be involved in an activity with continuity and regularity. The taxpayer’s primary purpose for engaging in the activity must be for income or profit. A sporadic activity, a hobby, or an amusement diversion does not qualify. The case involved a full-time gambler who was held to be engaged in a “trade or business” for purposes of section 162.

44. [Harrison v. Schaffner, 312 U.S. 579 \(1941\)](#). The [Assignment of Income Doctrine](#) imposes tax on the assignor of a partial income interest in a trust, if the donation consists of income from some but not all years. The case helps draw the line between a donation of property and an assignment of income from property: "It is enough that we find in the present case that the taxpayer, in point of substance, has parted with no substantial interest in property other than the specified payments of income which, like other gifts of income, are taxable to the donor. Unless in the meantime the difficulty be resolved by statute or treasury regulation, we leave it to future judicial decisions to determine precisely where the line shall be drawn between gifts of income-producing property and gifts of income from property of which the donor remains the owner, for all substantial and practical purposes." The court distinguished *Blair v. Commissioner, 300 U.S. 5 (1937)* which approved an assignment of a portion of an income interest for the entire term of the interest.
45. [Higgins v. Commissioner, 312 U.S. 212 \(1941\)](#). [Management of one's own investments in stocks and bonds does not constitute a trade or business; hence, expenses incident to such management are not deductible as "ordinary and necessary" business expenses.](#) Expenses attributable to management of a "real estate business" could be segregated and deducted. As a result of this decision, Congress enacted Section 212, which permits deduction of "ordinary and necessary" expenses for the "production of income." "Production of Income" deductions under section 212 are subject to different limitations than are "Trade or Business Expenses" under sections 162 and 167 or "Transaction for Profit Losses" under section 165.
46. [Hillsboro National Bank v. Commissioner, 460 U.S. 370 \(1983\)](#). [An event "fundamentally inconsistent" with a proper beneficial deduction in an earlier year sometimes results in income.](#) The "recovery requirement" of the tax benefit rule no longer applies. This was a companion case to *Bliss* (above). The tax benefit rule applies only if the original treatment resulted from a court-created policy doctrine rather a congressionally created doctrine. In this case, because Congress created a deduction but failed to create a provision triggered by an event fundamentally inconsistent with the deduction, no income resulted from such an event. Congress is entitled to make seemingly bad law. See also the companion case of *United States v. Bliss Dairy, Inc., 460 U.S. 370 (1983)*.
47. [Helvering v. Horst, 311 U.S. 112 \(1940\)](#). [Income from property is taxed to the owner of the property.](#) This case was a companion case to *Helvering v. Eubank, 311 U.S. 122 (1940)* which applied the Assignment of Income Doctrine to donative assignments of the right to income from service:

income is taxed to the person who performed the services. Subsequent cases illustrative the occasional difficulty of distinguishing an assignment of the income from property from an assignment of property itself: i.e., when does an income stream become “property.” The case involved interest coupons stripped from the underlying bond. Section 1286 later modified the result of this case with regard to the specific facts involved coupon bonds.

48. [Hughes & Luce L.L.P. v. Commissioner](#), 70 F.3d 16 (5th Cir. 1995). **The Tax Court’s “erroneous deduction exception” to the Tax Benefit Rule does not apply to cases in the Fifth Circuit.** Under the exception, the recovery of an item erroneously deducted in a prior year does not result in current income. Arguably, the *Hughes & Luce* holding prevents the operation of section 1312(7)(C)(iii) to mitigate the statute of limitations in such cases. See also, *Unvert v. Commissioner*, 656 F.2d 483 (9th Cir. 1981), which similarly excludes the exception in cases appealable to the Ninth Circuit.
49. [Commissioner v. Idaho Power Co.](#), 418 U.S. 1 (1974). **Depreciation expense and other material costs must be capitalized to the extent the underlying assets contributed to the cost of a long-term asset.** This results from section 263, even if the deductions are otherwise allowed under sections 167 or 162. The matter involved the use of heavy equipment – such as trucks – used in the construction of a building. The depreciation expense attributable to the trucks had to be capitalized into the basis of the building and then depreciated over a much longer period.
50. [Helvering v. Independent Life Insurance Co.](#), 292 U.S. 371 (1934). **A taxpayer’s use of his own property does not result in “gross income.”** Despite its seemingly obvious result, this important decision illustrates how the U.S. tax system favors some investments over others. For example, a taxpayer who owns his home has no income from his use of it; however, a taxpayer who leases his house to another has rental income even if he spends the money on comparable housing (and receives no comparable deduction). The two taxpayers have the same economic outcome, but different tax results.
51. [Commissioner v. Indianapolis Power & Light Co.](#), 493 U.S. 203 (1990). **Pre-payments for services produce income, while “deposits” do not.** This case focuses on the distinction between payments and deposits: “The key is whether the taxpayer has some guarantee that he will be allowed to keep the money.” In this case, no such guarantee existed because the customers had no obligation to purchase a minimum amount of electricity; hence, the taxpayer had no income from the advance receipts, which were

mere deposits. The distinction between a “payment” and a “deposit” is important both for income and for deductions (in relation to the treatment of advance “payments.”)

52. *INDOPCO v. Commissioner*, 503 U.S. 79 (1992). An expense that creates a benefit in a future year is a capital expenditure even if no separate asset is created by the expenditure (Future Benefit Test). Investment banker fees for a fairness opinion were not “ordinary” and had to be capitalized. Even if no separate asset is created, if the expenses create a more than incidental economic benefit extending beyond the year the expenses were incurred, the expenses must be capitalized. This case grew from *National Starch and Chemical Corporation v. Commissioner*, 918 F.2d 426 (3d Cir. 1990). (1) Although the presence of a separate and distinct asset is sufficient to treat an expenditure creating or enhancing that asset as capital, the lack of such an asset alone does not necessarily mean that an expenditure is ordinary and necessary under section 162(a). (2) Expenses incurred for the purpose of changing the corporate structure for the benefit of future operations are not ordinary and necessary expenses.
53. *Interstate Transit Lines v. Commissioner*, 319 U.S. 590 (1943). An income tax deduction is a matter of legislative grace. The burden of clearly showing the right to the claimed deduction is on the taxpayer. The matter involved an expense paid by a parent for a subsidiary. Even though the parent was contractually responsible for it, the expense was attributable to the subsidiary and not the parent. Nothing in the statute permitted the parent to take the deduction. See also, *Moline Properties v. Commissioner*, 319 U.S. 436 (1943), which respected the corporate form chosen by the taxpayer.
54. *James v. United States*, 366 U.S. 213 (1961). Stolen funds result in income, even if the taxpayer repays the amount stolen. Whether and when the repayment results in a deduction is a separate, unrelated matter.
55. *Kahler v. Commissioner*, 18 T.C. 31 (1952). Receipt of a “check” constitutes “receipt” for the recipient or “payment” for the transferor under the cash method of accounting. Receipt and payment are critical factors for cash method timing of income and deductions. A “check” is a term of art to be distinguished from a mere “draft.”
56. *Kenan v. Commissioner*, 114 F.2d 217 (2d Cir. 1940). The use of appreciated property to satisfy an obligation or to acquire something of value is a taxable event under section 1001. The case involved a trust



distribution of appreciated securities to satisfy an obligation to pay \$5,000,000. The trust had tax gain on the distribution of property. Along with the case *United States v. Davis*, 370 U.S. 65 (1962) this type of income is sometimes referred to as Davis/Kenan Gain.

57. *Kimbell-Diamond Milling Co. v. Commissioner*, 14 T.C. 74 (1950), *aff'd per curiam*, 187 F.2d 718 (5th Cir. 1951), *cert denied*, 342 U.S. 827 (1951). Where the essential nature of a transaction is the acquisition of property, it will be viewed as a whole, and closely related steps will not be separated either at the instance of the taxpayer or the taxing authority. The elective provision in section 338 traces its roots to the case of Kimbell-Diamond Mining Co. In *Kimbell-Diamond* the issue was the proper depreciable basis for a mill acquired by Kimbell-Diamond by purchasing the corporation that owned the mill and then liquidating the corporation. Kimbell-Diamond argued that it had liquidated the target which owned the asset the taxpayer then wanted to depreciate. In this case the target's basis was higher than the taxpayer's cost basis. The IRS argued successfully that the taxpayer intended a purchase and should have a cost basis in the underlying assets. The court viewed the transaction through the step-transaction doctrine to be in substance a purchase.
58. *United States v. Kirby Lumber Co.*, 284 U.S. 1 (1931). A discharge of indebtedness results in taxable income, at least in matters involving a "clear gain." The case involved a corporation purchasing and redeeming its own bonds at a price less than what was owed. Whether the result would be the same if the transaction occurred at a time of "insolvency" was not before the Court. Sections 108 and 1017 now affect the holding of this case, as well as the issue of insolvency.
59. *Knetsch v. U.S.*, 364 U.S. 361 (1960). "Sham" transactions are ignored for tax purposes. The matter involved the prepayment of interest with funds borrowed non-recourse and secured by an annuity purchased with other borrowed funds. The transaction was a "fiction" and a "sham." Section 1272 would not prevent the deduction of "pre-paid" interest, effectively defining interest as something which is impossible to prepay. The Court reiterated the *Gregory v. Helvering*, 293 U.S. 465 (1935) doctrine that form controls over substance except, as here, when substance controls over form (and the form is a sham).
60. *Kochansky v. Commissioner*, 92 F.3d 957 (9th Cir. 1996). Section 1041 does not apply to "income items". But see, Rev. Rul. 2002-22, which effectively holds that the section does so apply. Arguably, this repeals

important limitations in section 71 dealing with alimony and child support. Taxpayers who rely on the ruling may benefit; however, as a mere ruling, it could be withdrawn, resulting in a *Kochansky* nightmare: without the ruling, the transfer of an income item would result in Davis/Kenan Gain under the Acceleration of Income Doctrine of *P.G. Lake*.

61. *Commissioner v. P.G. Lake Inc.*, 356 U.S. 260 (1958). A taxpayer that carves out the income component of “property” – such as mineral royalty rights – and sells it separate from the “property” has ordinary income in the year of sale and no basis recovery. This decision created the Acceleration of Income Doctrine. This case has significant Time Value of Money implications and is partially affected by section 467.
62. *United States v. Lewis*, 340 U.S. 590 (1951). Tax consequences in one year are not a function of treatment of the same or similar items in another year. Taxpayer received a mistaken payment from his employer and properly had to report it as income even though, in a subsequent year, he had to restore the amount. That he failed to deduct the restoration in the later year, which was closed by the time of the decision, was irrelevant. This case, with *North American Oil*, 286 U.S. 417 (1932) and *Burnet v. Sanford & Brooks*, 282 U.S. 359 (1931) forms the basis for annual, rather than transactional, tax accounting. The harsh result prompted Congress to enact section 1341, which would now affect the outcome.
63. *Lucas v. Earl*, 281 U.S. 111 (1930). Income from services is taxed to the one who performs the services. The taxpayer husband contractually assigned part of his income to his wife. Although the contract was valid, it had no effect for tax purposes. Some famous language is: “There is no doubt that the statute could tax salaries to those who earned them and provide that the tax could not be escaped by anticipatory arrangements and contracts however skilfully devised to prevent the salary when paid from vesting even for a second in the man who earned it.” In its most famous part, the Court disapproved of schemes by which “fruits are attributed to a different tree from that on which they grew.” This case is distinguishable from *Poe v. Seaborn*, 282 U.S. 101 (1930) in which the Court recognized as valid the community property laws of several states which accomplished the assignment desired by the taxpayer in *Lucas v. Earl*. As a result of these two decisions, many states adopted community property laws. Later, after Congress permitted joint returns, most states repealed such laws.
64. *Malat v. Riddell*, 383 U.S. 569 (1966). The word “primarily” means “of first importance” in relation to the common code phrase “property held primarily for sale to customers in the ordinary course of a trade or business.” This

very important case is not fully satisfactory: it tells us what to do in a mixed motive case, but has no guidance for a “change of purpose” case or an “undetermined purpose” case.

65. [Martin v. Commissioner, 96 T.C. 814 \(1991\)](#). A cash method taxpayer may sometimes modify a contract, after partial performance, to defer receipt of payments without triggering the Constructive Receipt Doctrine. This expands on the Cowden decision, which permits a taxpayer, at the inception of a contract, to defer the receipt of payments without triggering the constructive receipt doctrine.
66. [U.S. v. Midland Ross, 381 U.S. 54 \(1965\)](#). Market discount on financial assets has the flavor of interest. As a result, it must be characterized as ordinary income when included. This case treated original issue discount interest and market discount interest the same for character purposes. Subsequent statutory changes have caused the timing of the two to diverge. Sections 1275 and 1276 now characterize the interest as ordinary, consistent with the Court decision. The case remains important, not only historically, but also because it characterizes some items as ordinary even though they result from a sale or exchange of a capital asset – a typical precipitator of capital gain treatment.
67. [Moline Properties v. Commissioner, 319 U.S. 436 \(1943\)](#). A corporation will be recognized as long as its purpose is the equivalent of business activity or it actively conducts business. The matter involved a gain on property by a corporation with a single shareholder. The shareholder wanted to disavow his corporation and be responsible for the tax himself. Subsequent to this decision, Congress enacted sub-chapter S of the Internal Revenue Code, recognizing some corporations as pass-through entities not subject to taxation themselves.
68. [C. F. Mueller Co. v. Commissioner, 190 F.2d 120 \(3rd Cir.1951\)](#). For years prior to 1950, the earning of income dedicated for charitable uses was an activity exempt from tax. At the time, Mueller, which manufactured macaroni, was wholly owned and operated by NYU School of Law. As a result of this case, Congress enacted in 1950, the unrelated business income tax rules and specifically the “Destination of Income Test”. Under the Test, the ultimate use of the funds for charitable purposes is irrelevant to whether the process of earning them is itself charitable.

69. *Estate of Mueller v. Commissioner*, 107 T.C. 189 (1996) (en banc). The Tax Court has jurisdiction to apply the Tax Benefit Rule. Reversed on appeal by the 6<sup>th</sup> Circuit, this case remains important in terms of cases appealable to other Circuits. Congress has since granted equitable recoupment jurisdiction to the Tax Court; however, its reach remains in doubt.
70. *National Carbide Corporation v. Commissioner*, 336 U.S. 422 (1949). Whether a corporation is an agent depends on many factors: (1) “whether the corporation operates in the name and for the account of the principal, (2) binds the principal by its actions, (3) transmits money received to the principal, and (4) whether receipt of income is attributable to the services of employees of the principal and to assets belonging to the principal. (5) “If the corporation is a true agent, its relations with its principal must not be dependent upon the fact that it is owned by the principal, if such is the case.” (6) “Its business purpose must be the carrying on of the normal duties of an agent.”
71. *North American Oil Consolidated v. Burnet*, 286 U.S. 417 (1932). (1) Under the Claim of Right Doctrine, “when a taxpayer receives funds with a contingent obligation to repay, either because the sum is disputed or mistakenly paid, and no limitation on the use of the funds exists, those funds are included in the taxpayer’s income in the year they are received.” (2) Tax consequences in one year are not a function of the treatment of similar items in another year. Many exceptions have arisen to the second proposition; however, it, along with *Burnet v. Sanford & Brooks*, 282 U.S. 359 (1931) and *U.S. v. Lewis*, 340 U.S. 590 (1951) forms the basis for annual, rather than transactional, tax accounting. North America Oil and U.S. Government disputed ownership of income from oil properties. North American Oil won in the lower court and received the profits in 1917. The U.S. appealed and North American had to return the profits in 1922. The Supreme Court held that the North America could take a deduction in 1922 when it lost its claim against the U.S. government. This deduction would be appropriate regardless of whether the receipt had been previously included. Also, the receipt constituted income in the year the taxpayer had a “Claim of Right” to it. That it included the income in a prior year – and could not seek a refund – was irrelevant.
72. *Old Colony Trust Co. v. Commissioner*, 279 U.S. 716 (1929). The form of the income does not matter in terms of “whether” an item is income. The taxpayer’s employer “paid” the income taxes due on the employee’s income. As a result, the employee had income equal to the taxes paid. The employer paid that tax, as well, which resulted in further income to the employee.

73. *Parker v. Delaney*, 186 F.2d 455 (1st Cir. 1950). The basis of property acquired with borrowed money includes an amount equal to the borrowed money used. The *Crane v. Commissioner*, 331 U.S. 1 (1947) decision is often cited as the father of this proposition; however, *Crane* merely held that the amount realized on the disposition of property included an amount equal to the debt assumed or to which the property was subject. The later First Circuit decision actually held that basis includes the debt.
74. *Peracchi v. Commissioner*, 143 F.3d 487 (9<sup>th</sup> Cir. 1998). A taxpayer will receive basis credit from his own note transferred to his wholly owned corporation if the note becomes a corporate asset subject to the claims of creditors.
75. *Philadelphia Park Amusement Co. v. United States*, 126 F. Supp. 184 (Cl. Ct. 1954). Section 1012 cost basis equals the fair market value transferred in an arm's length transaction, not the fair market value received. Also, the case creates a duality of value rule: If you cannot value one side of an arm's length transaction, but can value the other, you may presume they are equal. Although the main holding may seem counter-intuitive, it is profoundly important in tax accounting for multi-year transactions: the basis in acquired property is a function of how the acquisition *should have been* reported rather than how the transaction was *actually* reported. The section 1312(7)(C) circumstance of adjustment in the mitigation provisions, however, may be triggered by such inconsistent basis determinations.
76. *Podell v. Commissioner*, 55 T.C. 429 (1970). A joint venture is a "special combination of two or more persons, where in some specific venture a profit is jointly sought even without any actual partnership or corporate designation." This results in partnership tax treatment.
77. *Poe v. Seaborn*, 282 U.S. 101 (1930). The Assignment of Income Doctrine does not override state community property laws; hence, husband and wife are each taxed separately on half of the others' income. This case is distinguishable from *Lucas v. Earl*, 281 U.S. 111 (1930) in which the Court applied the Assignment of Income Doctrine to a contract between a married couple which assigned half of the husband's income to the wife. He remained taxable on the income. As a result of these two decisions, many states adopted community property laws. Later, after Congress permitted joint returns, most states repealed such laws.

78. *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992). The imposition of a state use tax against an out-of state mail-order business without a physical presence in the State is an unconstitutional burden on interstate commerce. The Court found no violation of Due Process. The Court considered, but declined to overrule *National Bellas Hess, Inc. v. Department of Revenue of Ill.*, 386 U.S. 753 (1967). *Bellas Hess* held that a state's imposition of a use-tax collection duty on an out-of-state mail order business violated Due Process and also placed an undue burden on interstate commerce.
79. *Reed v. Commissioner*, 723 F.2d 138 (1st Cir. 1983). The Economic Benefit Doctrine does not apply to a sale of property. This decision is subject to heavy criticism; however, it appears entrenched and is quite taxpayer friendly. As a result, a cash method taxpayer may arrange for the sale proceeds to be placed in an escrow account without triggering current gain or income. Essentially, the court held that the Economic Benefit Doctrine applies only to service income and contest winnings. Widely criticized, this case remains an important taxpayer weapon and a thorn for the government.
80. *Burnet v. Sanford & Brooks Co.*, 282 U.S. 359 (1931). Tax consequences in one year are not a function of the treatment of similar items in another year. Many exceptions have arisen to the second proposition; however, it, along with *North American Oil Consolidated v. Burnet*, 286 U.S. 417 (1932) and *U.S. v. Lewis*, 340 U.S. 590 (1951) form the basis for annual, rather than transactional, tax accounting. The taxpayer properly deducted costs from a transaction in one year and properly had to report income from receipts related to the prior costs in a later year. That the entire transaction was a "wash" was irrelevant: the U.S. does not use "transactional accounting." Also, whether the taxpayer deducted the prior items was irrelevant to whether the subsequent receipts were income.
81. *Schlude v. Commissioner*, 372 U.S. 128 (1963). Accrual method taxpayers that receive prepaid amounts for services must include them in income upon receipt. The third in a trilogy of cases effectively places accrual method taxpayers on the cash method for purposes of advance receipts. In addition, the case applied an extension of the Cash Equivalence Doctrine [*Cowden v. Commissioner*, 289 F.2d 20 (5th Cir. 1961)] to accrual method taxpayers. See also, *American Automobile Association v. United States*, 367 U.S. 687 (1961) and *Automobile Club of Michigan v. Commissioner*, 353 U.S. 180 (1957). To the extent the amounts received represent "rent," section 467(f) reverses these cases. *Artnell Co. v. Commissioner*, 400 F.2d 981 (7th Cir. 1968) and *Boise Cascade Corp. v. United States*, 530 F.2d 1367 (Ct. Cl. 1976) are very narrow exceptions to these cases.



82. *United States v. Skelly Oil Co.*, 394 U.S. 678 (1969). A deduction for repayment of an amount not fully taxed in a prior year may be limited to the portion taxed. Relying on the Arrowsmith Doctrine, the Court asserted this new rule does no harm to the Sanford & Brooks/North American Oil formula that keeps each year independent of other years. The Court also analogized its new rule to the Tax Benefit Rule, which operates in the reverse of *Skelly Oil*. In a critical limitation, the Court limited the Skelly Oil Rule with the following explanation: "In other situations when the taxes on a receipt do not equal the tax benefits of a repayment, either the taxpayer or the Government may, depending on circumstances, be the beneficiary. Here, the taxpayer always wins and the Government always loses." Hence the Skelly Oil Rule applies in those limited scenarios in which the taxpayer always benefits. Whether it also applies to case in which the government always benefits is unclear. The case involved mineral income not fully taxed because of a percentage depletion allowance. The receipts, when later repaid, could not be fully deducted.
83. *Sproull v. Commissioner*, 194 F.2d 541 (6th Cir. 1952). A cash method taxpayer has income when he receives the economic benefit of the proceeds. This occurs even if he has no constructive receipt and has not received a cash equivalent. The case thus created the Economic Benefit Doctrine. This case is almost always cited in matters involving the Economic Benefit Doctrine; however, the facts of the case would not likely result in application of the Doctrine as currently understood.
84. *Starker v. United States*, 602 F.2d 1341 (9<sup>th</sup> Cir. 1979). Like-kind exchange was appropriate even though the replacement property was acquired after transfer property was given up. Congress later amended section 1031 to conform essentially to this decision. Such exchanges are still often called Starker Exchanges.
85. *R.H. Stearns Co.*, 291 U.S. 54 (1934). "No one shall be permitted to found any claim upon his own inequity or take advantage of his own wrong." This case precipitated the occasionally imposed Duty of Consistency. A 1997 Tax Court case listed the Duty's factors as: "(a) The taxpayer made a representation of fact or reported an item for tax purposes in one tax year; (b) the Commissioner acquiesced in or relied on that fact for that year; and (c) the taxpayer desires to change the representation previously made in a later tax year after the earlier year has been closed by the statute of limitations." *Estate of Letts v. Commissioner*, 109 T.C. 290, 296 (1997).

86. *Stone v. White*, 301 U.S. 532 (1937). The government may use the Doctrine of Equitable Recoupment to defeat a refund of a tax paid by a trust beneficiary if the trust improperly excluded the income in another year. This case, along with *Bull v. United States* 295 U.S. 247 (1935), created the Doctrine of Equitable Recoupment. It applies to double tax benefits or tax detriments with regard to the same transaction or fund and the same taxpayer (or taxpayer with identity). Section 1312(3)(A) would define these facts today as a circumstance of adjustment and would thus preclude application of the Doctrine; however, it might trigger statutory mitigation of the statute of limitations. The case is particularly important in that it involved two different taxpayers.
87. *Strekfus Steamers Inc. v. Commissioner*, 19 T.C. 1 (1952). The tax benefit rule does not apply to the recovery of erroneously deducted items. This important case remains valid in the Tax Court for cases appealable to circuits other than the Fifth and Ninth. *Unvert v. Commissioner*, 656 F.2d 483 (9th Cir. 1981); *Hughes & Luce L.L.P. v. Commissioner*, 70 F.3d 16 (5th Cir. 1995). Most, if not all, cases under the Erroneous Deduction Exception to the Tax Benefit Rule create section 1312(7)(C)(iii) circumstances of adjustment.
88. *Commissioner v. Sullivan*, 356 U.S. 27 (1958). Rent and salaries are ordinary and necessary expenses for illegal gambling businesses. See also *Commissioner v. Groetzinger*, 480 U.S. 23 (1987) on whether and when gambling constitutes a trade or business. Under *Sullivan*, illegal income is taxed, but ordinary and necessary expenses attributable to it are deductible. Contrast this with the rule of *Tank Truck Rentals v. Commissioner*, 356 U.S. 30 (1958).
89. *Commissioner v. Sunnen*, 333 U.S. 591 (1948). Every year is a different cause of action for purposes of res judicata. “The general rule of *res judicata* applies to tax proceedings involving the same claim and the same tax year, while the doctrine of collateral estoppel, which is a narrower version of the *res judicata* rule, applies to tax proceedings involving similar or unlike claims and different tax years.” The matter involved the treatment and assignment of royalties under a contract. In a prior year, similar royalties from the contract were litigated and an assignment of them approved. This case, however, was not *res judicata* as to other royalties under the contract for a different year. Collateral estoppel was the appropriate preclusion device; however, intervening jurisprudential changes prevented its application.

90. *Tank Truck Rentals v. Commissioner*, 356 U.S. 30 (1958). Fines for overweight trucks are not "ordinary and necessary" expenses. This important policy decision prevents the tax system from partially subsidizing fines and penalties.
91. *Thor Power Tool v. Commissioner*, 439 U.S. 522 (1979). The Commissioner has broad discretion in determining what constitutes "clear reflection of income." Generally Accepted Accounting Principles do not control. Under § 471 inventories must (1) conform "as nearly as may be" to the "best accounting practice" and (2) "must clearly reflect the income." Even though taxpayer's write-down of "excess" inventory conformed to generally accepted accounting principles, Commissioner acted within his discretion in deciding that taxpayer's write-down of "excess" inventory failed to reflect income clearly. Until the taxpayer scraps the excess inventory, it must carry it at the lower of cost or market; however, market, for tax purposes, refers to replacement cost. Without a sale or "scrap" the taxpayer has no realization event to justify the loss.
92. *Commissioner v. Tufts*, 461 U.S. 300 (1983). The amount realized in a taxable disposition includes debt relief: the *Crane* rule applies, even if the non-recourse debt exceeds the fair market value of the property transferred. This important case answered the previously unanswered question in footnote 37 of *Crane v. Commissioner*, 331 U.S. 1 (1947). The case is related to the Tax Benefit Rule in that a taxpayer's behavior in one year – because of a Court-created doctrine (*Crane*) – affects his proper treatment in another year. This is an exception to the annual rather than transaction approach of *North American Oil Consolidated v. Burnet*, 286 U.S. 417 (1932), *Burnet v. Sanford & Brooks*, 282 U.S. 359 (1931) and *U.S. v. Lewis*, 340 U.S. 590 (1951).
93. *Turner v. Commissioner*, 13 T.C.M. (CCH) 462 (1954). The concept of fair market value can have a personal element: *i.e.*, the value to the taxpayer may be a function of what the item is worth to that person as opposed to the market in general. Few cases have illustrated this point; hence, this mere T.C.M. opinion is quite important. The taxpayer won a first class trip to Brazil with a retail value far greater than he would or could have ever realistically paid. The court found he had income equal to the value the property had to him as opposed to the value it might have in the market place.

94. *Unvert v. Commissioner*, 656 F.2d 483 (9th Cir. 1981). The Tax Court's "erroneous deduction exception" to the Tax Benefit Rule does not apply to cases in the Ninth Circuit. Under the exception, the recovery of an item erroneously deducted in a prior year does not result in current income. Arguably, the *Unvert* holding prevents the operation of section 1312(7)(C)(iii) to mitigate the statute of limitations in such cases. See also, *Hughes & Luce L.L.P. v. Commissioner*, 70 F.3d 16 (5th Cir. 1995), which similarly excludes the exception in cases appealable to the Fifth Circuit.
95. *Vander Poel, Francis & Co. v. Commissioner*, 8 T.C. 407 (1947). The constructive payment doctrine does not exist. Under the Constructive Receipt Doctrine, a cash method taxpayer has income when the cash income item has been offered to him without substantial limitations or restrictions, if he refuses the item. Also, this case suggests that no general principle of tax law requires consistency or matching between different taxpayers. (Compare to *Albertsons Inc. v. Commissioner*, 42 F.3d 537, (9th Cir. 1994), *rev'g* 12 F.3d 1529 (1993) (requiring consistency between unrelated taxpayers). Hence, if one person constructively offers an income item, the recipient of the offer has income but the offeror is not entitled to a deduction based on the item having been constructively paid (although the offeror may be able to accrue a deduction, subject to section 461(h)).
96. *Veit v. Commissioner*, 8 T.C. 809 (1947). A cash method taxpayer may sometimes modify a contract to defer receipt of payments without triggering the Constructive Receipt Doctrine. Until 1991, this case stood alone in its holding. *Martin v. Commissioner*, 96 T.C. 814 (1991).
97. *Welch v. Helvering*, 290 U.S. 111 (1933). "Ordinary and necessary" are not easily defined terms. Justice Cardozo's poetic language is famous: "Here, indeed, as so often in other branches of the law, the decisive distinctions are those of degree and not of kind. One struggles in vain for any verbal formula that will supply a ready touchstone. The standard set up by the statute is not a rule of law; it is rather a way of life. Life in all its fullness must supply the answer to the riddle."
98. *Williams v. McGowan*, 152 F.2d 570 (2<sup>nd</sup> Cir 1945). The purchase price of a business must be allocated among the various assets sold with the character of the gain or loss recognized on the sale of the business determined by that allocation. This important notion affects the sale of a going concern and illustrates a trap for unwary attorney/advisors. Generally, the government will respect the allocation of the purchase price

agreed upon by the parties – if they are at arm's length. The seller thus has incentive to maximize potential long-term capital gain, while the purchase has incentive to maximize quickly recovered costs (such as for inventory or short-lived assets). To a significant extent, the allocation can affect the after-tax value paid or received.

99. *Wisconsin Cheeseman v. United States*, 388 F.2d 420 (7<sup>th</sup> Cir. 1968). For section 265 to disallow interest on a loan, there must be a sufficiently direct relationship between the continuance of the debt and the continued ownership of tax-exempt bonds. The Court denied the interest deduction on short-term loans for which the bonds served as collateral: the taxpayer could have reasonably sold the bonds to meet the seasonal liquidity needs. The Court, however, allowed the interest deduction on long-term debt used to finance plant and equipment, finding that a reasonable taxpayer would not sacrifice short-term liquidity for long term borrowing needs. This case is important in its illustrations of the section 265 relationship of one activity to another. Analogous activity to activity relationship tests appear throughout the Code. For example, see the tests in section 514 with regard to unrelated debt financed income of a tax exempt organization. Whether the *Wisconsin Cheeseman* analysis of the types of debt is useful outside the section 265 arena is unclear.
100. *Zenz v. Quinlivan*, 213 F.2d 914 (6<sup>th</sup> Cir 1954). A complete redemption of stock is not “essentially equivalent to a dividend.” A shareholder who, as part of an overall plan to terminate her beneficial interest in a corporation, sells some stock to a third party and has the remainder redeemed by the corporation, will be held to have received from the corporation a payment for stock surrender, not a dividend. Expanded by Rev. Rul. 75-447. This case looked at the “overall result” of a series of transactions when they were part of an “overall plan.” The *Zenz* holding ‘proscribes the fragmenting of the whole transaction into its component parts.’