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insurance rates.⁵⁹ In view of the fact that punishing negligence cannot deter, this is a feasible method to protect the interests of the community.

Fourth: exemplary damages in civil negligence cases. If a negligent individual's actions approach, though do not reach, the standard of criminal recklessness, exemplary damages can be awarded to an injured party.

It is likely that the suggested methods would be more effective than criminal punishment. However, if the New York Legislature should decide against the advisability of these alternatives, it still does not follow that criminal punishment is necessary or helpful. Moreover, criminal punishment must rest not upon the deficiencies of alternative methods, but, rather, on its own positive grounds.⁶⁰ As Professor Hall has stated, "When punishment sanctioned by law is not justifiable, the significance of just punishment is dissipated. . . ."⁶¹

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ASSUMPTION AND DISCHARGE OF SELLER'S LIABILITIES AS YEAR OF SALE PAYMENTS FOR PURPOSES OF I.R.C. SECTION 453

Two recent cases, *Ivan Irwin, Jr.*,¹ decided by the Tax Court, and *United States v. Marshall*,² decided by the Court of Appeals for the Ninth Circuit, have highlighted a problem arising under the installment provisions of section 453 of the Internal Revenue Code.³ In both cases, the issue presented was whether

59. *Id.* at 643. In addition, "accident-prone" victims of negligent wrongdoers should not have their insurance rates increased.

60. Hall, *supra* note 16, at 644.

61. *Ibid.*

1. 45 T.C. 544 (1966).

2. 357 F.2d 294 (9th Cir. 1966).

3. Int. Rev. Code of 1954, § 453, which provides in part:

(a) Dealers in Personal Property.

(1) In General. Under regulations prescribed by the Secretary or his delegate, a person who regularly sells or otherwise disposes of personal property on the installment plan may return as income therefrom in any taxable year that proportion of the installment payments actually received in that year which the gross profit, realized or to be realized when payment is completed, bears to the total contract price.

(b) Sales of Realty and Casual Sales of Personalty.—

(1) General Rule.—Income from—

(A) a sale or other disposition of real property, or

(B) a casual sale or other casual disposition of personal property (other than property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year) for a price exceeding \$1,000,

may (under regulations prescribed by the Secretary or his delegate) be returned on the basis and in the manner prescribed in subsection (a).

(2) Limitation.—Paragraph (1) shall apply—

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liabilities of the seller, assumed and paid in the year of sale by the purchaser, are to be considered "payments" in a taxable year of the sale, in determining whether the sale qualifies for installment reporting under the 30 per cent limitation of section 453(b)(2).⁴

The purpose of this Comment is to suggest an approach to the problem of what should be included or excluded as "payments" under section 453(b)(2), and to propose a solution to the precise issue raised by these two cases. In dealing with this narrower problem, several subsidiary issues require recognition and resolution. Should the mere assumption of liabilities by the purchaser be considered "payments" under the 30 per cent test? Is there a distinction between the assumption of secured liabilities and the assumption of non-secured liabilities which requires that they be treated differently? Should the discharge of the seller's liabilities at the time of the sale be considered a year-of-sale "payment"?

THE BACKGROUND OF SECTION 453 AND ITS OPERATION

The various income tax legislation enacted prior to 1926 explicitly provided for two accounting methods of reporting income: the accrual method and the cash receipts and disbursements method.⁵ These accounting methods were inadequate, however, for taxpayers who sold property under the installment method in return for long-term obligations of the buyer and relatively minor amounts of cash or liquid property. The entire gain realized from these sales was being taxed in the year of sale at which time the taxpayer typically had insufficient funds available with which to pay the tax. These taxpayers were generally dealers in personal property who regularly sold under installment contracts and those persons who sold realty or made casual sales of personal property under installment contracts. In order to alleviate this hardship, the commissioner promulgated regulations which allowed these taxpayers to report the income from such sales in proportion to and at the time of each installment payment.⁶ These regulations were struck down in the courts due to a lack of statutory authorization.⁷ In quick response, Congress enacted the first statutory provision authorizing installment reporting of income.⁸ This statute delegated authority to the Secretary of the Treasury or his designee to promulgate regulations imple-

(A) In the case of a sale or other disposition during a taxable year beginning after December 31, 1953 (whether or not such taxable year ends after the date of enactment of this title), only if in the taxable year of the sale or other disposition

(i) there are no payments, or

(ii) the payments (exclusive of evidences of indebtedness of the purchaser) do not exceed 30 per cent of the selling price.

4. Int. Rev. Code of 1954, § 453(b)(2)(ii).

5. See, e.g., Revenue Act of 1918, ch. 18, § 212(b), 40 Stat. 1064; *Burnet v. S. & L. Bldg. Corp.*, 288 U.S. 406, 413 (1933).

6. E.g., Treas. Reg. 33, art. 117 (1918); Treas. Reg. 45, art. 42 (1919).

7. *Six Hundred and Fifty West End Ave. Co.*, 2 B.T.A. 958 (1925); *Hoover-Bond Co.*, 1 B.T.A. 929 (1925); *H. B. Graves Co.*, 1 B.T.A. 859 (1925); *B. B. Todd, Inc.*, 1 B.T.A. 762 (1925).

8. Revenue Act of 1926, ch. 27, § 212(d), 44 Stat. 23.

menting the statutory scheme. These provisions were carried forward and substantially embodied in section 453 of the 1954 Code.⁹

Section 453(b) refers to sales of realty and casual sales of personal property for a price exceeding 1,000 dollars. It requires that the "payments" in the year of sale do not exceed 30 per cent of the "selling price." If the sale qualifies for installment reporting, the seller may *elect* to return as income from the sale, "that proportion of the installment payments actually received in that year which the gross profit, realized or to be realized when payment is complete, bears to the total contract price."¹⁰

A SUGGESTED APPROACH TO THE PROBLEM OF "PAYMENTS"

The Supreme Court, in discussing the predecessor of section 453, stated:

The installment basis of reporting was enacted, as shown by its history, to relieve taxpayers who adopted it from having to pay an income tax in the year of sale based on the full amount of anticipated profits when in fact they had received in cash only a small proportion of the sales price. Another reason was the difficult and time consuming effort of appraising the uncertain market value of installment obligations.¹¹

While two purposes are mentioned, the primary reason for the enactment of the installment section was the problem of the insufficiency of cash with which to pay the tax.¹² It is suggested that the problem of determining which items should be included or excluded as "payments" for purposes of the 30 per cent test should be resolved by reference to alleviating this hardship. If the inclusion of a particular item as a "payment" will require a substantial group of taxpayers to pay tax in the year of sale on their full anticipated profits from the sale, when in fact they have received only a small portion of the sales price in cash or other relatively liquid form, the item should be excluded. If the inclusion of the item will not tend to bring about such a result, it should be included as a "payment."

Section 453 expressly excludes from "payments" evidences of indebtedness of the purchaser.¹³ This exclusion was necessary since including these items as "payments" would neutralize the beneficial effect of the statute in a large area of installment sales. However, the fact that the statute expressly excludes this one particular item does not require that all other items, which may be referred to as cash or other property, must be included in year-of-sale "payments." Section 1221 of the 1954 Code,¹⁴ which defines the capital assets which are to receive

9. Int. Rev. Code of 1954, § 453.

10. Int. Rev. Code of 1954, § 453(a) (1).

11. *Commissioner v. South Texas Lumber Co.*, 333 U.S. 496, 503 (1948); *cf.* S. Rep. No. 52, 69th Cong., 1st Sess. 19 (1925).

12. The time-consuming problem of appraising the uncertain market value of installment obligations is most critical when dealing with dealers in personal property who regularly sell under installment contracts. It is also in this area where the problem of insufficient funds with which to pay the tax liability decreases in importance since dealers in personal property generally discount the installment obligations of their purchasers.

13. Int. Rev. Code of 1954, § 453(b) (2) (A) (ii).

14. Int. Rev. Code of 1954, § 1221.

capital gain or loss treatment, is similar in this respect. That section defines capital assets as "property held by the taxpayer"¹⁵ but then makes five categorical exclusions. The courts have not limited themselves to these exclusions and they have developed further exclusions which would otherwise come within the literal definition of capital assets.¹⁶ This "common law of capital gains and losses"¹⁷ resulted from the courts' attempt to limit capital asset treatment to those items which would effectuate the congressional intent of the statute. The courts have been subjected to much criticism in this area, focused on a failure to properly perceive and effectuate the congressional purpose rather than on the approach of effectuating this intent.¹⁸ Analysis of section 453 and the problem of "payments" has similarly suffered from a lack of properly applying the congressional purpose.

PAYMENT: THE ASSUMPTION OF THE SELLER'S LIABILITIES

With the enactment of the first installment reporting section,¹⁹ it was immediately recognized that many sales of real estate would not qualify for installment reporting if mortgages to which property was taken subject or which were assumed by the purchaser were considered "payments" under the 30 per cent test.²⁰ In 1926, the commissioner issued a regulation which entirely excluded these mortgages from being considered year-of-sale "payments."²¹ The regulation was subsequently amended so as not to exclude these mortgages to the extent they exceed the seller's basis.²² The amendment was promulgated for the purely administrative reason of preventing the taxed proportion of payments received by the seller in subsequent years from exceeding one hundred per cent.²³ The amendment also had the effect of increasing the amount of gain from the sale which is taxed in the year of sale. The regulation, as amended, was carried forward in substance to Regulation 1.453-4(c):

Sale of real property involving deferred periodic payments. . . .

(c) Determination of "selling price." In the sale of mortgaged 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, for the purpose of determining whether a sale is on

15. Int. Rev. Code of 1954, § 1221.

16. *E.g.*, *Corn Prods. Ref. Co. v. Commissioner*, 350 U.S. 46 (1955) (Capital asset treatment was denied a taxpayer who bought and sold corn futures related to his regular business.).

17. Bittker, *Federal Income, Estate and Gift Taxation* 490 (3d ed. 1964).

18. See generally Del Cotto, "Property" in the Capital Asset Definition: Influence of "Fruit and Tree," 15 *Buffalo L. Rev.* 1 (1965).

19. Revenue Act of 1926, ch. 27, § 212(d), 44 Stat. 23.

20. The per cent limitation upon year-of-sale "payments" in order for a sale to qualify for installment reporting has, at various times, been set at 25, 40 and 30 per cent. See, *e.g.*, Revenue Act of 1926, ch. 27, § 212(d), 44 Stat. 23; Revenue Act of 1928, ch. 852, § 44(b) (2), 45 Stat. 805; Revenue Act of 1934, ch. 277, § 44(b) (2), 48 Stat. 694.

21. Treas. Reg. 69, art. 44 (1926).

22. Treas. Reg. 69, art. 44 (1926), as amended, T.D. 4255, VIII-1 Cum. Bull. 165 (1929).

23. See Berger, *Installment Sales with Assumed Liabilities*, 122 *J. Accountancy* 41, 45-46 (Aug. 1966).

the installment plan, be included as part of the "selling price"; and for the purpose of determining *payments* and the total contract price as those terms are used in section 453 . . . , the amount of such mortgage shall be included only to the extent that it exceeds the basis of the property.²⁴

The Supreme Court upheld a substantially identical predecessor regulation as a proper exercise of the "broad discretion granted to the Commissioner" by section 453 and as not violative of any specific provision of the statute.²⁵ In applying this regulation, the Board of Tax Appeals held that where the purchaser of realty assumes the payment of accrued interest on mortgages, accrued taxes, paying liens and interest thereon as part consideration for the purchase, the sum of such assumed liabilities should not be treated as "payments" received in the taxable year of the sale.²⁶ The term "mortgages" in the regulation was extended even further by the Board to include the assumption of long-term installment contracts for the sale of land.²⁷ The Board reasoned that there was "no difference between the assumption by the purchaser of the contract obligation of the seller to pay a former owner a balance of \$130,000 due upon the property, and his assumption of a mortgage due that party."²⁸ Even if one adopts a narrow approach to the scope of this regulation, these extensions of its coverage still seem appropriate. Certainly, they each tend to serve the congressional purpose behind the statute.

It is not clearly settled whether the regulation or its principle extends to the casual sale of personal property. The first indication of its applicability in this area was a revenue ruling issued in 1929.²⁹ The commissioner ruled that the effect of the purchaser's assumption of an unpaid balance due from the taxpayer on stock purchased from him "is considered to be the same as that of the assumption of an existing mortgage in connection with the sale of real property."³⁰ The ruling quotes parts of the regulation but it does not specify that the regulation is itself applicable. Apparently, the taxpayer's creditor retained no security interest in the stock since no mention of it is made in the ruling. In *Stephen A. Cisler, Jr.*,³¹ the Tax Court approved the application of the regulation to the casual sale of personal property. The taxpayer had sold stock in which he had no adjusted basis and as part of the consideration, the buyer assumed the seller's obligation of 20,000 dollars against which the stock had been pledged. The court noted that both the taxpayer and the commissioner agreed that the

24. Treas. Reg. § 1.453-4(c) (1954) (Emphasis added.).

25. *Burnet v. S. & L. Bldg. Corp.*, 288 U.S. 406, 414 (1933).

26. *Kathrine H. Watson*, 20 B.T.A. 270 (1930); *accord*, I.T. 2468, VIII-1 Cum. Bull. 159 (1929); *cf.*, *Estate of Henry R. Lipman v. United States*, 245 F. Supp. 393 (E.D. Tenn. 1965) (No year-of-sale "payments" when as part of the consideration for a sale the vendee agreed to retire *upon maturity* certain debts of the vendor's husband running to the vendee.).

27. *J. W. McWilliams*, 15 B.T.A. 329 (1929).

28. *Id.* at 343.

29. I.T. 2468, VIII-1 Cum. Bull. 159 (1929).

30. I.T. 2468, VIII-1 Cum. Bull. 159, 160 (1929).

31. 39 T.C. 458 (1962).

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1929 ruling was applicable.³² However, since the taxpayer had no basis in the stock, the full amount of the assumed liability exceeded his basis and was treated as a "payment" in the year of sale.

When the District Court in *Marshall v. United States*³³ analogized from the regulation and held that the assumption of business liabilities in the sale of a partnership should be accorded the same treatment as mortgages, it was severely criticized.³⁴ The thrust of the criticism was that the court misinterpreted *Cisler* and other authorities. It was contended that these authorities only stood "for the proposition that debts of the vendor *similar to mortgages* are to be treated in the same way as mortgages, under Regulation 1.453-4(c)."³⁵ While there was no discussion as to what liabilities might be considered similar to mortgages, it was intimated that some sort of security interest might be required.³⁶ However, this fails to recognize the commissioner's 1929 ruling which apparently involved the assumption of an unsecured debt.³⁷

If, however, a similarity to mortgages is necessary in order for an assumed debt to be treated like a mortgage, a similarity in effectuating the congressional intent of section 453 should be sufficient. The congressional purpose is equally served by excluding the assumption of non-secured liabilities from year-of-sale "payments" as by excluding the assumption of secured debts. In both situations, the seller who receives, in relatively liquid form, a small amount of the purchase price as down payment, is relieved of a disproportionate tax liability, a liability which in some instances is greater than the down payment.

PAYMENT: DISCHARGE OF ALL OR PART OF THE ASSUMED LIABILITIES BY THE PURCHASER IN THE YEAR OF SALE

In *Ivan Irwin, Jr.*,³⁸ the Tax Court concluded that assumed liabilities, discharged by the purchaser in the year of sale, should be included in "payments" under the 30 per cent test. In *United States v. Marshall*,³⁹ the Court of Appeals came to the opposite conclusion. It has further been suggested that the discharged liabilities should be included as "payments," "*but only if the obligation assumed was, by its terms as of the date of sale, due and payable during the year of sale.*"⁴⁰

In *Irwin*, the taxpayers were partners conducting the business of a managing general fire and casualty insurance agency. The agency acted as an intermediary between large insurance companies and local insurance agents. The local agent collected the premiums and remitted eighty per cent of them to the agency. The

32. *Id.* at 466.

33. 241 F. Supp. 30 (S.D. Cal. 1964), *aff'd*, 357 F.2d 294 (9th Cir. 1966).

34. Note, *Installment Sale Reporting of Income—Are Current Liabilities Similar to Mortgages?*, 1 Calif. West. L. Rev. 154 (1965).

35. *Id.* at 156.

36. *Id.* at 157.

37. I.T. 2468, VIII-1 Cum. Bull. 159 (1929).

38. 45 T.C. 544 (1966).

39. 357 F.2d 294 (9th Cir. 1966), *affirming* 241 F. Supp. 30 (S.D. Cal. 1964).

40. DeCastro & Chodorow, *Can Buyer's Payment of Assumed Debt Kill Seller's Installment Election? Courts Disagree*, 25 J. Taxation 130 (1966). See Berger, *supra* note 23, at 42.

agency, pursuant to its contract, remitted seventy per cent of the premiums to the insurance companies within ninety days after the close of the month in which the business was written. In May of 1959 the taxpayers assigned the entire business to an independent corporation for a purchase price of \$471,539.67 and the assumption of partnership liabilities in the amount of \$271,186.95, seventy per cent of which were "Accounts Payable to Insurance Companies." The taxpayer received \$81,539.64 at the closing and, prior to the end of 1959, the purchaser discharged \$273,974.05 of the assumed liabilities.

The taxpayers argued that Regulation 1.453-4(c) was applicable and that the words of the regulation excluded assumed liabilities from year-of-sale "payments" except insofar they exceed the seller's adjusted basis in the assets sold.⁴¹ The Commissioner argued that the regulation did not apply, even in principle, to the assumption of business liabilities and, therefore, the mere assumption of these liabilities constituted "payments" in the year of sale.⁴² The court rejected both contentions and held that assumed liabilities, which are *discharged* in the year of sale, constitute year-of-sale "payments." The court concluded that this was the proper construction of the regulation, and as such it was applicable.

The court properly perceived that the inclusion of assumed liabilities in the amount realized on a sale does not govern the question of year-of-sale payments for purposes of the 30 per cent test.⁴³ After noting the congressional intent behind section 453, the court reached its conclusion by analogizing from a series of precedents which held that an indebtedness of the seller, which the purchaser cancels, discharges or otherwise extinguishes at the time of the sale, is the "equivalent of cash" and is therefore a "payment" to the seller in the year of sale.⁴⁴ The rationale of these cases is that the taxpayer's "net worth" is thereby increased and, while he never actually receives these funds, "the seller's other personal funds (which otherwise might have been required to be used to satisfy personal debts) are freed to be used in paying the tax."⁴⁵ The court noted that the seller's liabilities are completely extinguished in these cases, while in the situation where the liability is assumed, the seller remains secondarily liable. Since assumed liabilities are extinguished if they are discharged by the purchaser in the year of sale, they should be considered year-of-sale "payments."⁴⁶

While the court's reasoning from precedent appears sound, it is suggested

41. Ivan Irwin, Jr., 45 T.C. 544, 552-53 (1966).

42. *Id.* at 553.

43. *Id.* at 549.

44. James Hammond, 1 T.C. 198 (1942) (cancellation of seller's notes running to a third party); Wagegro Corp., 38 B.T.A. 1225 (1938) (payment by purchaser of seller's legal expenses of the sale); W. H. Batchellor, 19 B.T.A. 1050 (1930) (cancellation of vendor's indebtedness running to the vendee); Rev. Rul. 60-52, 1960-1 Cum. Bull. 186 (liabilities such as liens, accrued interest and taxes assumed and paid in the year of sale); I.T. 2351, VI-1 Cum. Bull. 43 (1927) (property sold to mortgagee thereby cancelling mortgage); *accord*, Sterling v. Ham, 3 F. Supp. 386 (D.C. Me. 1933) (cash payment by buyer directly to mortgagee).

45. Ivan Irwin, Jr., 45 T.C. 544, 550 (1966).

46. *Id.* at 551.

that the precedents themselves⁴⁷ were erroneously decided. There is no substantial difference between a debt which is extinguished and one which is reduced to a secondary liability. In determining what is income or what is the amount realized from the sale of property, there is no distinction made between the discharge of the seller's debt and the conversion of his liability into a secondary liability by the purchaser's assumption of the debt. In both situations, the full amount of the debt is treated as realized and the seller is immediately taxed upon the entire gain from the sale.⁴⁸ The assumed liability is considered to be the equivalent of money, as is the extinguished debt. Implicit in this rationale is a realization that, as a practical matter, the purchaser *is* relieved of his debt. This treatment is mandated by the remoteness of the possibility that the taxpayer will be called upon to satisfy this secondary liability, coupled with the administrative burden inherent in deferring taxation until the assumed liability is extinguished.

The distinction between extinguishing and assuming a liability is equally irrelevant for purposes of section 453, in which the problem is determining *when* the income will be taxed. Assumed mortgages are excluded from year-of-sale "payments" since the taxpayer would otherwise have "to pay an income tax in the year of sale based on the full amount of anticipated profits when in fact [he] had received in cash only a small portion of the sales price. . . ."⁴⁹ If one applies the same congressional purpose to a liability which is extinguished at the time of sale, it becomes apparent that it should be treated like an assumed mortgage. The taxpayer's ability or inability to pay the tax is identical. To argue that in one instance the taxpayer's assets are released to pay the tax liability and in the other they are not, is both erroneous and ignores the practical effect that, if they are freed at all, they are freed equally in both situations.

In the area of the cancellation of an indebtedness, the "freeing of assets" or "increase of net worth" theory is useful in determining what *is* income, but it has no rational nexus with the problem of determining *when* the tax should be paid under section 453. The theory is founded upon the fact that the discharge or assumption of the debt is the "equivalent of cash"⁵⁰ and, consequently, the taxpayer's net worth is increased. But in the case of the sale of an appreciated asset, the taxpayer's economic net worth is increased at the time of appreciation and it is reflected in his balance sheet when the asset is revaluated for accounting purposes. At the time of sale, the seller's net worth is not increased at all, but

47. See authorities cited *supra* note 44.

48. See *Lakeland Grocery Co.*, 36 B.T.A. 289 (1937) (creditors accepted \$15,472 in full payment of seller's debts amounting to \$104,710); *Brons Hotel, Inc.*, 34 B.T.A. 376 (1936) (assumption of seller's mortgage). Where the purchaser assumes the mortgage on property and the seller was not personally liable for the mortgage, the inclusion of the mortgage is justified on the basis that it is necessary to recover excessive depreciation deductions taken by the seller and to insure that mortgaged out value appreciation goes through the seller's tax account. See *Crane v. Commissioner*, 331 U.S. 1 (1947); *Parker v. Delaney*, 186 F.2d 455 (1st Cir. 1950).

49. *Commissioner v. South Texas Lumber Co.*, 333 U.S. 496, 503 (1948); see S. Rep. No. 52, 69th Cong., 1st Sess. 19 (1925).

50. See cases cited *supra* note 48; see generally *Bittker, op. cit. supra* note 17, at 89-96.

rather there is a substitution of assets and reduced liabilities for the transferred asset. The court, however, may be looking at the sale with reference to an appreciated asset which has not been revalued and which is carried on the taxpayer's books at its cost basis. In this situation, the seller's net worth is increased, from an accounting point of view, at the time of sale by the excess of the amount realized over the basis in the sold property.⁵¹ To the extent it exceeds the seller's basis, the assumption or discharge of his debt reduces his liabilities without a corresponding decrease in his assets. Where the seller does not eliminate the assumed liability from his balance sheet at the time of the sale, he must carry an increase in his assets in the amount of the debt assumption. When the purchaser discharges the assumed liability, there is either no change on the balance sheet or both assets and liabilities are reduced by equal amounts. In either event, there is no change in the seller's net worth and no assets are freed.⁵²

If the *Irwin* court is suggesting that the seller has other assets which he is holding to pay these liabilities and which are consequently freed when the debt is discharged, the rationale is based upon an assumption which has no foundation in fact. The seller may have no assets other than those which he has sold. In this situation, the only assets which could be "freed" for the payment of the tax levy are the installment obligations of the purchaser, which are not included in year-of-sale "payments" in order to not render the section nugatory. The fact that the taxpayer incurred these liabilities does not require that he have assets in addition to those involved in the sale. Consequently, the taxpayer's ability to pay the tax in the year of the sale is no greater than where the buyer merely assumes the liability.

It is further suggested that one need not rely upon the cases involving the

51. The following balance sheets demonstrate the accounting effect of a sale of property with a basis of \$100 for (a) \$200 cash, (b) \$100 cash plus the discharge of seller's debts in the amount of \$100, and (c) \$100 cash plus the assumption of seller's debts worth \$100.

Before sale:

Assets	Liabilities
Property 100	100
	Net Worth 0

After sale (a):

Assets	Liabilities
Cash 200	100
	Net Worth 100

After sale (b):

Assets	Liabilities
Cash 100	0
	Net Worth 100

After sale (c):

Assets	Liabilities
Cash 100	100
	Net worth 100
	Promise to discharge debt 100

52. See facts of example (c) *supra* note 51. After discharge of assumed liabilities:

Assets	Liabilities
Cash 100	0
	Net worth 100

payment of a debt at the time of the sale. These cases are firmly imbedded in the law and it is not likely that they will be overruled without a legislative change. But it would seem that the above analysis makes the discharge of assumed liabilities sufficiently analogous to the mere assumption of liabilities that they should be accorded equal treatment.

In *United States v. Marshall*,⁵³ on facts similar to *Irwin*, the Court of Appeals came to a contrary result and held for the taxpayer. The taxpayers sold their business for \$110,513.22, of which \$25,568.86 consisted of short-term business liabilities. In the year of sale the taxpayers received \$13,944.36 cash. The purchaser discharged all of the assumed liabilities in the year of sale. The taxpayer, as in *Irwin*, argued that Regulation 1.453-4(c) was applicable and that the words of the regulation precluded assumed liabilities from being included in year-of-sale payments, except to the extent they exceed the seller's basis in the property sold.⁵⁴ The commissioner took the position of the *Irwin* court and argued that the *payment* of these liabilities in the year of sale was determinative, rather than the mere assumption.⁵⁵ The court looked at the congressional purpose of section 453 and briefly reasoned that "the quoted reasoning applies with equal force . . . [because] here the sellers received less than \$14,000 in cash during the year of sale, and if the installment method is denied to them, they must pay taxes, in one year, on a gain that exceeds \$20,000."⁵⁶ The court emphasized the fact that "it may be extremely difficult for the seller to determine what obligations have been paid by the purchaser and the dates of payment."⁵⁷

A commentary on these two cases suggested that precedent supported the decision in *Irwin*.⁵⁸ But it deemed important, as did the court in *Marshall*, the taxpayer's problem in determining when and what liabilities have been discharged.⁵⁹ It then suggested that the *Irwin* rule presented the possibility of the purchaser subjecting the seller to "business blackmail."⁶⁰ To eliminate these problems, the two cases were compromised and the rule advanced "that liabilities of a going business which are assumed as part of the sale transaction and paid during the year of sale should constitute payments in the year of sale, *but only if the obligation assumed was, by its terms as of the date of sale, due and payable during the year of sale.*"⁶¹ This proposal is based on a "freeing of assets" or "increase of net worth" rationale, "but providing that assets which are not committed to pay off these current liabilities are not affected."⁶²

The infirmities of the "freeing of assets" or "increase of net worth" rationale have been discussed. The fact remains that the assets which the taxpayer has

53. 357 F.2d 294 (9th Cir. 1966), *affirming* 241 F. Supp. 30 (S.D. Cal. 1964).

54. *Ibid.*

55. *Ibid.*

56. *Id.* at 295.

57. *Id.* at 296.

58. DeCastro & Chodorow, *supra* note 40, at 131.

59. *Id.* at 132.

60. *Ibid.*

61. *Ibid.*

62. *Ibid.* See Berger, *supra* note 23, at 42.

committed to the discharge of the liabilities may well be, and in the case of a business probably are, the same assets which he has sold. Thus, the only asset with which he may discharge his tax liability is the purchaser's installment obligation which Congress has deemed inappropriate for that purpose.

The difficulty which the taxpayer has in determining when and in what amounts the buyer has discharged the assumed liabilities certainly exists, as does the potential for "business blackmail." But the correction of these problems is completely unrelated to the effectuation of the congressional intent of section 453. Therefore, it adds nothing and is immaterial to a discussion of what should be included in year-of-sale "payments."

CONCLUSION

It is well recognized that the issue of year-of-sale payments under section 453 is unsettled and subject to many conflicting views. This Comment has only attempted to address itself to one group of problems arising in this area. A clarification of this issue is desperately needed to provide at least some degree of predictability to the taxpayer since a misstep in this area can bring about disastrous consequences.⁶³ The statute delegates to the commissioner the authority to promulgate legislative regulations in order to implement this section of the code⁶⁴ and it seems that this authority extends to defining year-of-sale "payments" for the 30 per cent test.⁶⁵ Neither the courts nor Congress are likely to bring about the needed change. It is, therefore, incumbent upon the commissioner to take up the challenge of clarifying this problem area. If this is done from the proper reference point (*i.e.*, that the taxpayer in these situations is not attempting to avoid the tax but rather to defer payment of the tax to alleviate a congressionally recognized hardship) radical changes will properly be brought about in the law. Even in the event such changes do not occur, clarification is nonetheless imperative to both the taxpayer and the practitioner.

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63. In *Joseph Homberger, Jr.*, T.C.M. 1960-43, the taxpayer sold real property for \$1,099,600. His basis was \$43,984. The taxpayer received \$7,500 in cash at the time of the sale and the remainder of the purchase price (\$1,092,100) was represented by long-term installment notes payable over a thirteen-year period. Due to an error by the accounting firm, the taxpayer did not properly elect to report the sale on the installment basis. A tax deficiency of \$283,822.99 was assessed by the Commissioner and upheld by the Tax Court.

64. Int. Rev. Code of 1954, § 453(b)(1).

65. See *Burnet v. S. & L. Bldg. Co.*, 288 U.S. 406, 414 (1933).