*6 T.C. 1188 (1946)*

When stock is acquired via a will subject to a binding option, the fair market value (and thus the basis) of the stock is limited to the option price, and the assumption of tax liabilities by the seller in a stock transfer agreement reduces the amount realized in the transaction.

**Summary**

Helen Delone inherited stock subject to an option agreement. She later sold the stock, assuming certain tax liabilities related to the option. The Tax Court addressed how to determine the basis of the stock and the amount realized from the sale. The court held that the basis was the option price ($100/share) because the option restricted the stock's value. Further, the amount realized was reduced by the estate and inheritance taxes Delone assumed as part of the agreement, regardless of when those taxes were actually paid.

**Facts**

C.J. Delone willed his estate, including 2,544 shares of Revonah Spinning Mills stock, to his wife, Helen Delone. The will directed Helen to sell the Revonah stock to three named individuals (Shafer, Malcolm, and Shafer) at $100 per share. Helen also owned 865 shares of Revonah stock independently with a basis of $100 per share. The estate tax appraisal valued the Revonah stock at $125 per share. Helen and the three individuals entered into an agreement whereby Helen transferred 693 of her shares to them. She transferred her remaining 2,716 shares to Revonah for cash and preferred stock. Helen also assumed the responsibility for Federal and state estate and inheritance taxes attributable to the benefit received by the three individuals due to the option.

**Procedural History**

The Commissioner of Internal Revenue determined a deficiency in Helen Delone's income tax for 1940. The Commissioner calculated gain based on a higher stock basis and did not allow a reduction for the assumed tax liabilities. Delone petitioned the Tax Court for a redetermination of the deficiency.

**Issue(s)**

1. Whether the basis of stock acquired through a will, but subject to a mandatory option to sell at a fixed price, is the estate tax value of the unencumbered stock or the option price.
2. Whether the amount realized in a stock sale is reduced by the seller's assumption of estate and inheritance tax liabilities related to an option agreement, even if those taxes were not paid during the taxable year.

**Holding**

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1. No, because the existence of a binding option limits the fair market value to the option price.
2. Yes, because the assumption of these liabilities is considered part of the consideration for the transaction and reduces the amount realized.

**Court's Reasoning**

The court reasoned that Helen Delone received the stock encumbered by a binding option, which significantly affected its fair market value. Citing *Helvering v. Salvage, 297 U.S. 106 (1936)*, the court emphasized that a binding, irrevocable option enforceable against the shareholder fixes the market value at the option price. The court stated, "We think the last stated rule applies to the instant case. Petitioner enjoyed no freedom of determination as to whether, when, or at what price to sell the shares of Revonah stock which she received under the will." Therefore, the basis for calculating gain or loss was $100 per share, the option price. The court further held that Helen's assumption of the estate and inheritance tax liabilities reduced the amount she realized from the sale. Even though the taxes were not paid during the tax year, her obligation to pay them was fixed by the agreement. The court likened this assumption of liability to a cash payment, stating that "the assumption of liabilities must be regarded as the equivalent of cash paid as part of the consideration for the transaction."

**Practical Implications**

This case clarifies the valuation of assets subject to restrictions like options for tax purposes. It establishes that a binding option limits the fair market value to the option price, impacting both basis and potential capital gains or losses. The decision also highlights that assuming liabilities in a transaction can be equivalent to receiving less cash, thus reducing the amount realized. This influences how similar transactions are structured and reported, particularly in estate planning and corporate reorganizations. Later cases have cited *Delone* to emphasize the importance of legally binding agreements in determining fair market value and to support the principle that assumption of liabilities affects the calculation of gain or loss in taxable transactions.

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