20 T.C. 615 (1953)

Gains from the sale of a citrus grove that are attributable to the unmatured fruit on the trees are taxed as ordinary income, because the fruit is considered property held primarily for sale to customers in the ordinary course of business; however, the installment method of reporting income may be available for such sales.

Summary

The Ann Edwards Trust case involves the tax implications of selling citrus groves with unmatured fruit. The Tax Court addressed whether the portion of the gain attributable to the growing crops should be taxed as ordinary income or capital gains, and whether the installment method of reporting income was available. The court held that the gain attributable to the unmatured fruit was ordinary income, aligning with the Supreme Court's decision in Watson v. Commissioner. However, the court also found that the trust petitioners could report the ordinary income on the installment basis.

Facts

The Edwards brothers and two family trusts each sold citrus groves in Florida to Triple E. Development Company in 1945. The sales included unmatured citrus fruit on the trees, which was not yet ready for harvest. The Ann Edwards Trust and Nancy Edwards Trust were established in 1940. All expenses related to cultivation and fertilization were deducted against ordinary income prior to the sale. The Trusts elected to treat the sales as installment sales on their tax returns.

Procedural History

The Commissioner of Internal Revenue determined deficiencies in the petitioners' income tax for the taxable year 1945. The petitioners contested the deficiencies in the Tax Court. The Tax Court consolidated the cases for trial. The Tax Court ruled against the petitioners on the ordinary income issue but in favor of the trust petitioners on the installment method issue.

Issue(s)

1. Whether the gain realized upon the sale of citrus groves, attributable to the growing crop on the trees, is taxable as ordinary income or as long-term capital gain.

2. If the gain attributable to the growing crop is ordinary income for the Ann Edwards Trust and Nancy Edwards Trust, whether they may report such income on the installment basis under Section 44 of the Internal Revenue Code.

Holding

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1. No, because the fruit on the trees was property held primarily for sale to customers in the ordinary course of business.

2. Yes, because the sales of the growing crops were casual sales of personalty or sales of realty, and the requirements of Section 44(b) of the Internal Revenue Code were met.

Court's Reasoning

The court relied on the Supreme Court's decision in *Watson v. Commissioner, 345 U.S. 544 (1953)*, which held that the gain from the sale of unmatured fruit on trees is ordinary income because it represents the sale of property held primarily for sale to customers in the ordinary course of business. Regarding the installment method, the court reasoned that if the fruit is personal property, the sales were casual sales, not in the ordinary course of business, and the fruit was not inventory. If the growing crop was realty, Section 44(b) had no further conditions beyond the timing and amounts of payments, which were satisfied. The court stated, "If the fruit be regarded as personal property, the facts show that the sales in question were casual sales and not sales in the ordinary course of the petitioners' trade or business, even though the fruit on the trees at the time of the sale was held primarily for sale to customers in the ordinary course of such trade or business. Furthermore, there can be no question, we think, that a growing crop of citrus fruit would not be '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.'"

Practical Implications

This case clarifies the tax treatment of gains from the sale of land with growing crops, particularly in agricultural settings. It reinforces that the portion of the sales price attributable to the crop is generally treated as ordinary income, impacting tax planning for farmers and landowners. Furthermore, it highlights that the installment method of reporting income may still be available in these transactions, providing a potential tax benefit. Legal practitioners must carefully allocate the sales price between the land and the crops to ensure proper tax reporting. Later cases distinguish the *Edwards Trust* ruling by focusing on whether the taxpayer is in the business of selling crops. For example, a real estate developer selling land with incidental crops may have different tax implications.

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