20 T.C. 734 (1953)

The settlement of a judgment by the judgment debtor is not considered a "sale or exchange" of a capital asset, and therefore, any gain realized by the judgment holder is not eligible for capital gains treatment under the Internal Revenue Code.

Summary

Galvin Hudson and Hillsman Taylor purchased a judgment against Howard Cole. They later settled the judgment with Cole for a sum greater than their purchase price. The Commissioner of Internal Revenue determined that the profit from the settlement was ordinary income, not capital gain. The Tax Court agreed, holding that the settlement of a judgment is not a "sale or exchange" of a capital asset, as required for capital gains treatment under the Internal Revenue Code. The Court reasoned that the judgment debtor did not acquire any property from the settlement; he merely extinguished a debt.

Facts

Mary Mallory Harahan obtained a judgment against Howard Cole in 1929. In 1943, Hudson and Taylor purchased the Cole judgment from the residuary legatees of Harahan's estate. In 1945, Cole paid Hudson and Taylor a sum to fully settle the judgment. Hudson and Taylor reported their profit from the settlement as long-term capital gain on their income tax returns. The Commissioner determined that the profit was ordinary income.

Procedural History

The Commissioner of Internal Revenue determined deficiencies in Hudson and Taylor's income taxes, reclassifying the gain from the judgment settlement as ordinary income. Hudson and Taylor contested the deficiencies in the U.S. Tax Court.

Issue(s)

Whether the gain realized by petitioners from the settlement of a judgment is ordinary income or capital gain.

Holding

Yes, the gain realized by petitioners from the settlement of a judgment is ordinary income because the settlement did not constitute a "sale or exchange" of a capital asset.

Court's Reasoning

The court focused on whether the settlement of the judgment constituted a "sale or

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exchange" of a capital asset, a requirement for capital gains treatment under Section 117(a)(4) of the Internal Revenue Code. The court defined a

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