Anderson v. Commissioner, 75 T. C. 30 (1980)

The adjusted basis in reacquired real property under IRC Section 1038(c) is determined by adding the adjusted basis of the indebtedness secured by the property at reacquisition to the basis of any canceled indebtedness from the original sale.

Summary

In Anderson v. Commissioner, the Tax Court determined the Andersons' tax liability from the sale of their reacquired home. The key issue was how to calculate the adjusted basis of the property under IRC Section 1038(c) after the Andersons reacquired it following a failed sale. The court found that the basis included both the remaining mortgage at reacquisition and the basis of the canceled note from the original sale, totaling $11,053. 59. Additional improvements and depreciation adjustments brought the basis to $10,496. 80 at the time of the final sale. The court also ruled that certain payments received were part of the sales price, leading to a taxable gain.

Facts

In 1962, Eugene and Jean Anderson bought a home, assuming a $9,000 mortgage and paying $500 in cash. They made $1,936. 71 in improvements before selling it in 1966. The buyers assumed the mortgage ($7,626. 45) and gave the Andersons a note for $3,810. 26. The buyers defaulted, and in 1967, the Andersons reacquired the property, canceling the buyers' note and reassuming the mortgage ($7,243. 33). After spending $593. 21 on further improvements and claiming $1,150 in depreciation, they resold the property in 1969. The buyer assumed the mortgage ($6,216. 49), paid $1,000 in cash, and provided $988. 96 to clear liens, resulting in a dispute over the taxable gain.

Procedural History

The Commissioner determined a tax deficiency of $755. 34 for the Andersons' 1969 income tax. The Andersons contested this in the Tax Court, which had to determine the adjusted basis of the property at the time of the 1969 sale and the amount realized from the sale.

Issue(s)

1. Whether the Andersons' adjusted basis in the property at the time of the 1969 sale should include the adjusted basis of the mortgage and the canceled note from the 1966 sale under IRC Section 1038(c)?
2. Whether certain payments received by the Andersons in the 1969 sale should be included in the amount realized?

Holding

1. Yes, because IRC Section 1038(c) requires the adjusted basis to include both the remaining mortgage at reacquisition and the basis of the canceled note, resulting in an adjusted basis of $11,053. 59 at reacquisition, adjusted to $10,496. 80 at the time of the 1969 sale.
2. Yes, because the payments were made to clear liens and thus constituted part of the sales price, as per Crane v. Commissioner.

Court's Reasoning

The court applied IRC Section 1038(c) to determine the Andersons' basis in the reacquired property. The section specifies that the basis includes the adjusted basis of the indebtedness secured by the property at reacquisition plus the basis of any canceled indebtedness from the original sale. The Andersons' basis in the canceled note was calculated as their initial investment minus the mortgage at the time of the 1966 sale. The court also considered the subsequent improvements and depreciation to arrive at the final basis. Regarding the payments received in 1969, the court relied on Crane v. Commissioner, which established that payments to clear liens are part of the sales price. The court rejected the Andersons' argument that these were refunds, as they could not substantiate this claim.

Practical Implications

This decision clarifies how to calculate the basis in reacquired property under IRC Section 1038(c), which is crucial for determining gain or loss on subsequent sales. Practitioners should ensure they account for both the remaining mortgage at reacquisition and any canceled indebtedness from the original sale. The inclusion of payments for lien clearance in the sales price underscores the importance of properly categorizing all amounts received in a sale. This case has been cited in subsequent tax disputes involving reacquired property, such as Pittsburgh Terminal Corp. , reinforcing its significance in tax law.

