King v. Commissioner, 87 T. C. 1213 (1986)

Losses on commodity straddles entered into before 1982 by commodities dealers are deductible without regard to a profit motive.

Summary

Marlowe King, a commodities dealer, sought to deduct losses from gold futures straddles in 1980. The IRS challenged these deductions, arguing they were sham transactions and not for profit. The U. S. Tax Court granted King's motion for summary judgment, holding that his losses were deductible under Section 108 of the Tax Reform Act of 1984, which allows losses for commodities dealers without requiring a profit motive. Additionally, the court ruled that King's gain from selling gold bars was long-term capital gain, not short-term as argued by the IRS, due to Section 1233 not applying to physical commodities.

Facts

Marlowe King, a registered member of the Chicago Mercantile Exchange, actively traded commodities and futures since 1950. In 1980, he incurred losses from disposing of positions in gold futures straddles. King also realized a gain from selling gold bars that year, which he reported as long-term capital gain. The IRS issued a notice of deficiency, disallowing the losses and recharacterizing the gain as short-term capital gain, claiming the transactions were shams and lacked economic substance.

Procedural History

King filed a motion for partial summary judgment in the U. S. Tax Court to address the IRS's determinations regarding the deductibility of his straddle losses and the classification of his gold bar sale gain. The court reviewed the motion under its rules for summary judgment, considering the affidavits and arguments presented by both parties.

Issue(s)

1. Whether King's losses on dispositions of gold commodity futures straddles in 1980 are deductible under Section 108 of the Tax Reform Act of 1984.
2. Whether King's gain from the sale of gold bars in 1980 qualifies as long-term capital gain under Section 1233 of the Internal Revenue Code.

Holding

1. Yes, because King's losses are deductible under Section 108(b) as a commodities dealer without needing to establish a profit motive.
2. Yes, because Section 1233 does not apply to physical commodities, thus King's gain from selling gold bars is properly classified as long-term capital gain.

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Court’s Reasoning

The court applied Section 108 of the Tax Reform Act of 1984, which allows commodities dealers to deduct losses on straddles entered into before 1982 without needing to prove a profit motive. The IRS’s arguments that the transactions were shams were unsupported by specific facts, failing to meet the court’s requirements for summary judgment opposition. For the gold bar sale, the court interpreted Section 1233 narrowly, ruling that it only applies to stocks, securities, and commodity futures, not physical commodities like gold bars. The legislative history and statutory language supported this interpretation, leading to the conclusion that King’s gain was long-term.

Practical Implications

This decision clarifies that commodities dealers can deduct straddle losses without proving a profit motive if the transactions were entered into before 1982, impacting how similar cases involving pre-1982 commodity transactions are analyzed. It also establishes that Section 1233 does not apply to physical commodities, affecting the classification of gains from such assets. This ruling may influence future tax planning strategies for commodities dealers and the IRS’s approach to challenging such deductions and classifications. Subsequent cases have cited King v. Commissioner when addressing the deductibility of losses and the classification of gains under similar circumstances.

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