Rauenhorst v. Commissioner, 119 T. C. 157 (2002)

In Rauenhorst v. Commissioner, the U. S. Tax Court ruled that the transfer of stock warrants to charitable organizations did not constitute an anticipatory assignment of income. The court applied a bright-line test from Rev. Rul. 78-197, stating that income is only taxable to the donor if the donee is legally bound to sell the contributed property. This decision reinforces the principle that donors can claim charitable deductions without incurring immediate tax on the property's subsequent sale, provided the donee has control over the disposition of the asset.

Parties

Plaintiffs/Appellants: Gerald A. Rauenhorst and Henrietta V. Rauenhorst, as petitioners in the U. S. Tax Court.

Defendant/Appellee: Commissioner of Internal Revenue, as respondent in the U. S. Tax Court.

Facts

Gerald A. and Henrietta V. Rauenhorst, through their partnership Arbeit & Co. , owned warrants to purchase shares of NMG, Inc. On September 28, 1993, World Color Press, Inc. (WCP) expressed its intention to purchase all of NMG's issued and outstanding stock. Subsequently, on November 9, 1993, Arbeit assigned its NMG warrants to four charitable institutions: the University of St. Thomas, Marquette University, the Mayo Foundation, and the Archdiocese of St. Paul and Minneapolis. At the time of the assignment, these institutions were under no legal obligation to sell the warrants. The warrants were reissued to the donees on November 12, 1993. On November 19, 1993, the donees entered into agreements to sell their warrants to WCP, and the transaction closed on December 22, 1993. The Commissioner of Internal Revenue asserted that the Rauenhorsts should be taxed on the income from the sale of the warrants, claiming it was an anticipatory assignment of income.

Procedural History

The Rauenhorsts filed a petition in the U. S. Tax Court challenging the Commissioner's determination of a deficiency in their 1993 federal income taxes and an accuracy-related penalty. They moved for partial summary judgment on the issue of whether they were taxable on the gains from the sale of the warrants by the charitable donees. The Commissioner opposed the motion, arguing that genuine issues of material fact remained. The Tax Court granted the Rauenhorsts' motion for partial summary judgment.

Issue(s)

Whether the transfer of NMG stock warrants to charitable institutions by the Rauenhorsts constituted an anticipatory assignment of income under the Internal

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Revenue Code?

Rule(s) of Law

The court applied the principle from Rev. Rul. 78-197, which states that the proceeds from the sale of contributed property will be treated as income to the donor only if, at the time of the gift, the donee is legally bound, or can be compelled, to surrender the shares for redemption or sale. The court also referenced the general principles of the anticipatory assignment of income doctrine, as established in cases such as *Helvering v. Horst*, which taxes income to those who earn or otherwise create the right to receive it.

Holding

The U. S. Tax Court held that the Rauenhorsts' transfer of NMG stock warrants to charitable institutions did not constitute an anticipatory assignment of income. The court found that the donees were not legally bound or compelled to sell the warrants at the time of the assignment, and thus, the Rauenhorsts were entitled to judgment as a matter of law.

Reasoning

The court's reasoning centered on the application of Rev. Rul. 78-197, which provided a bright-line test for determining whether a charitable contribution of appreciated property results in income to the donor. The court treated this ruling as a concession by the Commissioner, given its long-standing nature and the Commissioner's continued reliance on it in other contexts. The court rejected the Commissioner's argument that the sale of the warrants had ripened to a practical certainty at the time of the assignment, emphasizing that the donees had full control over the disposition of the warrants at the time of the gift. The court also distinguished prior case law cited by the Commissioner, finding that those cases involved situations where the donees were powerless to reverse the course of events, unlike the present case where the donees could decide not to sell the warrants. The court noted the absence of any legally binding agreements at the time of the assignment and affirmed the validity of the completed gift to the charitable institutions.

Disposition

The U. S. Tax Court granted the Rauenhorsts' motion for partial summary judgment, holding that they were not taxable on the gains realized from the sale of the NMG stock warrants by the charitable donees.

Significance/Impact

The Rauenhorst decision reinforces the application of Rev. Rul. 78-197 in the context of charitable contributions, providing clarity and predictability for taxpayers and

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their advisors. It underscores the importance of the donee’s control over contributed property in determining the tax treatment of subsequent sales. The ruling supports the principle that taxpayers can structure charitable contributions to maximize tax benefits without incurring immediate tax liability on the property’s sale, provided the donee has the legal power to decide on the disposition of the asset. This case also highlights the binding nature of revenue rulings on the Commissioner in litigation, emphasizing the need for consistency and fairness in tax administration.

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