

**TAXATION OF PROPERTY DISPOSITIONS**

**VILLANOVA UNIVERSITY  
GRADUATE TAX PROGRAM**

**FALL 2004**

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# TAXATION OF PROPERTY DISPOSITIONS

## Villanova University Graduate Tax Program

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### **Course Materials**

Required:

Freeland, Lind and Stephens, Fundamentals of Federal Income Taxation, (13<sup>th</sup> ed. 2004).

Internal Revenue Code of 1986, as amended.

Treasury Regulations on Income Tax

Note: You can use any current Code and Regulations, e.g., those published by CCH or RIA (Prentice Hall).

Program Supplemental Materials

### **Course Outline and Syllabus**

### **References**

Sec	=	Internal Revenue Code of 1986
Reg	=	Treasury Regulations on Income Tax
FLS	=	Freeland, Lind and Stevens text
Prob	=	Problem
SupMat	=	Program Supplemental Materials
Skim	=	Read Only Once

### **Course Outline**

- I. Introduction
  - a. Administrative Matters
  - b. Course Overview
  - c. Statutory Pattern
  - d. Constitutional Background

- II. Basis of Property
  - a. Basic Concepts
  - b. Statutory Pattern
  - c. Cost Basis (unadjusted)
    - i. Cash
    - ii. Property Generally
      - 1. Property Received in a Taxable Exchange
      - 2. Property Received as Compensation
      - 3. Bargain Purchase
    - iii. Property Acquired by Gift: Transferred Basis
      - 1. General
      - 2. Part Gift, Part Sale
    - iv. Property Acquired from a Spouse or Incident to Divorce: Transferred Basis
    - v. Property Acquired from a Decedent: Stepped-up Basis
  - d. Adjusted Basis
    - i. Concepts and Statutory Pattern
    - ii. Time Value of Money
      - 1. General
      - 2. Deferral, Present Value, Timing
    - iii. Major Items of Basis Adjustment
      - 1. Capital Costs versus Deductions
      - 2. Depreciation
        - a. Introduction
        - b. Special Depreciation Rules for Personal Property
        - c. Special Rules for Realty
      - 3. Amortization, Depletion
  - e. Joint Interests in Property: Apportionment of Basis
  - f. Negative Basis
- III. Amount Realized from Property Dispositions
  - a. Introduction
  - b. Realization
    - i. The Taxable Event
      - 1. General
      - 2. Taxable Year Concept
    - ii. Recognition Distinguished
    - iii. Taxable Disposition of Mortgaged Property
      - 1. Sale or Exchange
        - a. Quantum of Interest Disposed Of



- e. The Sale or Exchange Requirement
    - i. General
    - ii. Correlation with Prior Transactions
  - f. Holding Period
- VI. Recharacterization: Gain from the Sale of Depreciable Property
- a. Section 1231 Quasi Capital Assets
  - b. Section 1239
  - c. Section 1245 Recapture
  - d. Section 1250 Recapture
  - e. Other Recapture Concepts
- VII. Treatment of Losses
- a. General
    - i. Closed Transaction Requirement
    - ii. Amount of Loss
    - iii. Compensation for Loss
  - b. In Business and Profit-making Activities
    - i. General
    - ii. Personal Losses
    - iii. Changed Use
  - c. Capital versus Ordinary Loss
  - d. Losses Distinguished from Expenses and Bad Debts
  - e. Casualty Loss
  - f. Net Operating Loss
  - g. Losses in Transactions Between Related Parties
    - i. General
    - ii. Other Related-party Transactions
      - 1. Personal Service Corporations
      - 2. Allocation of Income and Deductions
  - h. Loss Limitations
    - i. General
    - ii. At Risk Rules
    - iii. Passive Activity Losses
- VIII. Nonrecognition
- a. General
  - b. Wash Sales
  - c. Like Kind Exchanges of Property
  - d. Involuntary Conversions

- e. Other Nonrecognition Provisions
    - i. General
    - ii. Contribution of Property to a Controlled Enterprise
- IX. Sale of Principal Residence
- a. Statutory Pattern

### **Course Syllabus**

Class No.

1. I. Introduction
  - A. Administrative Matters
  - B. Course Overview
  - C. Statutory Pattern (Sec 61(a)(3), 1001(a)-(c), 1011(a) , 1012, 1016(a); FLS 117-118)
  - D. Constitutional Background (FLS 14-21); SupMat 1
  
- II. Basis of Property
  - A. Basis Concepts (FLS 118-134)
  - B. Statutory Pattern (Sec 1001(a), 1011(a), 1012, 1016)
  - C. Cost Basis (unadjusted) (Sec 1012)
    1. Cash (Reg 1.1012-1(a))
2.
  2. Property Generally (Reg 1.1012-1(a))
    - a. Property Received in a Taxable Exchange (FLS 118-122; SupMat 2, 3)
    - b. Property Received as Compensation (Sec 83, 132, Reg 1.83-4(a), (b), 1.132-3(b); FLS 134-136; SupMat 4, 5, 6)
    - c. Bargain Purchase (SupMat 7)
  3. Acquired by Gift: Transferred Basis (Property FLS 122-129)
    - a. General (Sec 1015; Reg 1.1015-1(a)(2) Example; FLS 69-81, Prob 1 p. 121-122)
    - b. Part Gift, Part Sale (Reg 1.1001-1(e), 1.1015-4; Prob 1 and 2 p.128-129; SupMat 8, 35)
3.
  4. Property Acquired from a Spouse or Incident to Divorce: Transferred Basis (Sec 1041; Reg 1.1041-1T(a) and (d); FLS 129-131, 208-220; SupMat 9, 10, 11, 12, 13)
  5. Property Acquired from a Decedent: Stepped-up Basis (Sec 1014; Reg 1.1014-3(a), -4, -5; FLS 131-133)

- D. Adjusted Basis
    - 1. Concepts and Statutory Pattern (Sec 1011, 1016; Reg 1.1011-1, 1.1016-2, -3, -10)
    - 2. Time Value of Money
      - a. General (Sec 461(h); Skim FLS 631-641)
      - b. Deferral, Present Value, Timing (Skim FLS 820-866)
    - 3. Major Items of Basis Adjustment
      - a. Capital Costs versus Deductions (e.g. Sec 109, 162(a), 263, 263A, 266, 1016, 1019; FLS 582-586)
      - b. Depreciation
        - III. Introduction (Sec 167, 168; FLS 403-428)
        - IV. Special Depreciation Rules for Personal Property (Sec 167, 168, 179; FLS 428-440; SupMat 14, 41)
        - V. Special Rules for Realty (Sec 168; FLS 440-443)
      - c. Amortization, Depletion (Sec 167, 197, 611, 613, 1016; Reg 1.1016-3(a)(1), (b); FLS 414-415)
  - E. Joint Interests in Property: Apportionment of Basis (Reg 1.61-6(a), 1.1014-4, -5; Skim SupMat 15)
  - F. Negative Basis
5. III. Amount Realized from Property Dispositions
  - A. Introduction
  - B. Realization
    - 1. The taxable event
      - (a) General (Sec 61(a)(3), 1001(a), (b), (c), 1011(a), 1012, 1016(a)(1)-(2); Reg 1.61-3, -6(a), 1.1001-1(a)-(c), 1.1011-1, 1.1012-1(a), (c)(3))
      - (b) Taxable year concept (Sec 441; FLS 645-653 (Skim))
    - 2. Nonrecognition distinguished: the timing event (Sec 1001(c))
    - 3. Taxable disposition of mortgaged property
      - (a) Sale or exchange (Reg. 1.1001-2; FLS 137-154, Prob 1(a)-(i), 2, 3(a), (b) and (c); SupMat 16)
        - (i) Quantum of interest disposed of (SupMat 17)
        - (ii) When sale occurs (SupMat 18)

- 6.
  - (b) Abandonment (Sec 165(a), (b); SupMat 19)
  - (c) Transfer in satisfaction of a debt; foreclosure (FLS 165-175; Sup Mat 20)
  - (d) Disposition and leaseback (Sec 1031; Reg 1.1031(a)-1(c); FLS 883-890; SupMat 21, 22, 28)
  - (e) Inventory sales distinguished (Sec 61(a)(2), 446 (a); Reg 1.61-3, 1.446-1(c)(2)(i); FLS 628-630 (Skim))
  - (f) Disposition within an affiliated group
  - 4. Grant of an option (Sec 1234; FLS, Prob 2 p. 717)
  - 5. Sale of a sole proprietorship (FLS 748-751)
  - 6. Sale of a partnership interest (Sec 741 (Skim), 751 (Skim); Sup Mat 38 (Skim))
  - 7. Corporate distribution of appreciated property; partial liquidation (Sec 331 (Skim), 336 (Skim))
- 7.
  - 8. Computation of amount realized in property, services, and assumption of liabilities (FLS 118-121, 134-136; Reg 1.1001-2(a)(2); SupMat 23)
- C. Charitable contribution of appreciated property (Sec 170; Reg 1.170A-1(c); FLS 793-804)

#### IV. Treatment of Indebtedness and Credit Sales

- A. Debt discharge vs. debt relief (Sec 61 (a)(12), 108, 1017; Reg 1.1001-2(a)(1), (2), (c) Examples; FLS 165-180)
- B. Purchase-money debt: basis and amount realized (Reg 1.1001-2(c) Example 1; FLS 131-153; SupMat 24)
  - 1. Effect of contingent liabilities (SupMat 25)
  - 2. Inflated purchase-money debt (Reg 1.1001-2(a)(3); SupMat 26, 27)
  - 3. Sale for a future payment
    - (a) Open transactions (FLS 838-844)
    - (b) Installment Sales
      - (i) Sales of realty and casual sales of personal property (Sec 453 (a)-(g), (i)-(k), 453A; FLS 820-838)
      - (ii) Disposition of installment obligation (SupMat 29, 30)
      - (iii) Wrap-around mortgages (SupMat 31, 32)
  - 4. Mortgage foreclosures
- C. Hidden interest (FLS 847-862 (Skim))
- 8.

1. Interest-free loans (Sec 7872)
  2. Original issue discount (Secs 483, 1271-1274A)
9. V. Characterization: Capital Gain and Loss
- A. Introduction (FLS 676-682)
  - B. Mechanics of capital gains (Sec 1(a)-(e), (h), 1201(a), 1221, 1222; FLS 682-689)
  - C. Mechanics of capital losses (Sec 165(c), (f), 1211(a), (b), 1212(a), (b)(1), 2(B)(i), 1221, 1222; FLS 690-694)
  - D. The meaning of "capital asset"
    1. Statutory definition (Sec 1221, 1234, 1236, 1237; FLS 695-702)
    2. Income producing property (Sec 102(b), 273, 1001(e), 1241; Reg 1.11014-5, 1.1015-1(b), (c); FLS 718-727, Prob 1, 3, 4 p. 726-727)
    3. Is it or isn't it? (Prop Reg 1.1221-2; FLS 700-702, SupMat 33, 34, 42, 43)
  - E. The sale or exchange requirement
    1. General (Sec 1222; FLS 703-711, Prob p. 711)
    2. Correlation with prior transactions (FLS 727-736)
10. F. Holding period (Sec 1223 (1), (2), (11); see 1014(a), 1015(a), 1041(b), 1222, 1223; FLS 712-718, Prob 1 and 2 p. 717)
- VI. Recharacterization: Gain on the Sale of Depreciable Property
- A. Section 1231 quasi capital assets (FLS 741-748; SupMat 36)
  - B. Section 1239 (skim FLS 754-760)
  - C. Section 1245 recapture (FLS 760-766)
  - D. Section 1250 recapture (FLS 766-769)
11. VII. Treatment of Losses
- A. General (Sec 1(a), 11(a), 61, 63(a), 165, 172)
    1. Closed transaction requirement (Sec 165 (g), Reg 1.165-1(b))
    2. Amount of loss (Sec 111, 165(b))
    3. Compensation for loss (Sec 165(a), (h); Reg 1.165-1(d)(2))
  - B. In business and profit-making activities
    1. General (Sec 62, 63, 165(c)(1), (c)(2); FLS 444-448)
    2. Personal losses (Sec 165, 262; Reg 1.165-9(b); FLS 415-420)

- 3. Changed use (Reg 1.165-9(b))
- C. Capital vs. ordinary loss (Sec 165(f), (g)(1), 1231)
- D. Losses distinguished from expenses and bad debts (Sec 162, 165, 166, 212; FLS 770-783)
- 12. E. Casualty loss (Sec 165(c)(3), (h); Reg 1.165-7; FLS 806-812, Prob 1 p. 812)
- F. Net operating loss (Sec 172; FLS 672-674)
- G. Losses in transactions between related persons
  - 1. General (Sec 267; Reg 1.267(d)-1; FLS 867-874, Prob 1, 4 pp. 873-874)
  - 2. Other related-party transactions
    - (a) Personal service corporations (Sec 269A)
    - (b) Allocation of income and deductions (Sec 482; FLS 303-311 (Skim))
- H. Loss limitation
  - 1. General (FLS 509-512)
  - 2. At risk rules (Sec 465; FLS 513-516, Prob 1 at p 515-516)
- 13. 3. Passive activity losses (Sec 469; FLS 523-537, Prob 6 at p. 537)

#### VIII. Nonrecognition

- A. General (FLS 877-879)
- B. Wash Sales (Sec 1091, 1223(4); FLS 513-516; 874-876, Prob 1 p. 876, Sup Mat 40)
- C. Like-kind exchanges of property (sec 1001(c), 1031, 1223(1), 1231; FLS 879-899, Sup Mat 37, 30)
- 14. D. Involuntary conversions of property (Sec 1001(c), 1033, 1223(1), 1231; FLS 899-908)
- E. Other nonrecognition provisions
  - 1. General (FLS 909-912)
  - 2. Contribution of property to a controlled enterprise (Sec 351 (Skim), 721 (Skim))

#### IX. Sale of Principal Residence

- A. Exclusion of Most of All Gain (FLS 221-226, Prob 1 p. 226)