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COMMENTS

Tufts—THE RESURRECTION OF Crane's FOOTNOTE 37

JANET JACOBOWITZ

I. INTRODUCTION

The message of what appeared to be “obvious” to the Supreme Court in “the most famous footnote in tax history,” footnote 37 of Crane v. Commissioner, has at last surfaced. The Fifth Circuit, in Tufts v. Commissioner, became the first court to concede to the “obviously” with which footnote 37 begins. The Tufts decision, however, is in direct conflict with both the Third Circuit and the Tax Court. Although Tufts may be indicative of a judicial desire to impede the expansion of the Crane doctrine, to the tax shelter industry it renews the speculation that has surrounded footnote 37 and its implication of help for tax shelters ever since the Supreme Court decided Crane.

2. 331 U.S. 1 (1947). Footnote 37 states:

Obviously, if the value of the property is less than the amount of the mortgage, a mortgagor who is not personally liable cannot realize a benefit equal to the mortgage. Consequently, a different problem might be encountered where a mortgagor abandoned the property or transferred it subject to the mortgage without receiving boot. That is not this case.


Briefly, Crane stands for the dual principles that the basis of property includes nonrecourse debt encumbering it, and that upon disposition of such property, at a time when the value of the property exceeds the debt, the amount realized includes the full amount of the nonrecourse debt. See discussion accompanying notes 7-31, infra. See generally, Adams, Exploring the Outer Boundaries of the Crane Doctrine: An Imaginary Supreme Court Opinion, 21 Tax L. Rev. 159 (1966); Bittker, supra note 1; Del Cotto, Basis and Amount Realized Under Crane: A Current View of Some Tax Effects in Mortgage Financing, 118 U. PA. L. Rev. 69 (1969); Weiss, The Crane Case Updated, 32 Tax Law. 289 (1978).

3. 651 F.2d 1058 (5th Cir. 1981). Tufts held that where the fair market value of property is less than the amount of the nonrecourse mortgage, the amount realized upon disposition is limited to the fair market value. See discussion accompanying notes 85-105 infra.


The purpose of this comment is to examine Tufts v. Commissioner, specifically its interpretation of footnote 37. This will be accomplished through an analysis of Crane and post-Crane case law, to the extent that this is necessary to understand the impact that Crane has had on tax law. Since Tufts is the most recent and divergent post-Crane decision, the bulk of the ensuing discussion will focus on the underlying rationale of Tufts and its potential effects.

II. Crane v. Commissioner

In order to comprehend the meaning and impact of footnote 37, it is necessary to look to its progenitor, Crane v. Commissioner. The petitioner, Beulah Crane, inherited from her husband a building and lot subject to a mortgage of approximately $262,000. The value of the property at the time of the inheritance was equal to the amount of the encumbrance. During the next seven years, Crane reported the gross rentals as income and claimed the allowable deductions for taxes, expenses, and physical exhaustion of the building. She was at no time personally liable on the mortgage. After seven years, Crane sold the property, subject to the mortgage, for $3,000 cash, out of which she paid $500 in expenses.

Crane reported a capital gain of $1,250. She contended that the property she had acquired and sold was the equity only, which was the value of the building and lot in excess of the mortgage. Since the equity was zero when Crane acquired the property, she argued that she realized a net capital gain of $2,500. The Commissioner, however, contended that Crane realized a net gain of approximately $27,500, reasoning that the "property' acquired and sold was not the equity . . . but rather the physical property itself, or the owner's rights to possess, use, and dispose of it, undiminished by the mortgage." From the original basis of $262,000, the allowable depreciation of $28,000 was subtracted, resulting in an adjusted basis of $179,000. The amount realized on the sale of the property, the Commissioner argued, included both the $2,500 cash and the amount of the mortgage, which totaled $257,500 and which

7. 331 U.S. at 3. The principal of the mortgage was $255,000 and interest in default amounted to approximately $7,000. Id.
8. Id. at 4.
9. She realized a net amount of cash of $2,500. Under § 117(a),(b), Int. Rev. Code of 1939, (now I.R.C. § 1221), 50% of the gain realized upon the sale of capital asset was taxable. 331 U.S. at 4 n.3.
10. Id. at 4.
produced a taxable gain of $27,500.11

The Supreme Court upheld the Commissioner on several grounds. It first determined that “property” as used to determine “basis” under the applicable statutory provision must be construed according to its “ordinary, everyday” meaning. This does not encompass the definition of equity.12 Thus, property must mean a physical object which is owned, or the legal rights to control that object.13 The Court also refused to construe “equity” to mean “property” for basis purposes because such a construction would hinder the determination of depreciation deductions and subsequent adjustments to basis. If the “basis” is the equity, and the depreciation is computed on an “equity basis,” the deductions would “represent only a fraction of the cost of the corresponding physical exhaustion.”14 On the other hand, if depreciation were computed on the full value of the property, but deducted from an “equity basis,” the result would be a negative basis or the denial of deductions altogether. The Court was unwilling to approve either of these results.15 Thus, the Court summarized that “the applicable provisions . . . expressly preclude an equity basis, and the use of it is contrary to certain implicit principles of income tax depreciation, and entails very great administrative difficulties.”16

The next hurdle for the Court was to determine the “amount realized” upon the sale of the property. The Court decided that the term “property” as used to determine “amount realized” must have the same meaning as used to determine “basis.”17

11. Id. at 4-5. Crane sustained a capital loss on the land, of which $264 was taken into account, and an ordinary gain on the building of $24,000. The adjusted basis included the $179,000 allocable to the building and $55,000 to the land. Id.

12. Int. Rev. Code of 1939 § 113(a)(5) (now I.R.C. § 1014). Section 113(a)(5) was applicable to determine her basis since the property was acquired by devise.


14. Id. at 9.

15. Id. at 9-10.

16. Id. at 10.

17. Int. Rev. Code of 1939, § 111(b) (now I.R.C. § 1001(b)).

18. 331 U.S. at 13. Gain or loss and amount realized are defined in I.R.C. § 1001(a) and (b) (substantially unchanged from §§ 111(a) and (b), respectively, of the 1939 Code) as follows:

(a) Computation of Gain or Loss—The gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in section 1011 for determining gain, and the loss shall be the excess of the adjusted basis provided in such section for determining loss over the amount realized.

(b) Amount Realized—The amount realized from the sale or other disposition of property shall be the sum of any money received plus the fair market value of...
Therefore, the amount of the mortgage should be included in the amount realized on the sale of the property. The "gain" was the amount realized less the "adjusted basis." Thus, the definition of amount realized was expanded to include a nonrecourse mortgage as the economic equivalent to cash. In recognition of the fact that the seller need not receive money or property to realize gain, the Court stated:

[A] mortgagor, not personally liable on the debt, who sells the property subject to the mortgage and for additional consideration, realizes a benefit in the amount of the mortgage as well as the boot. If a purchaser pays boot, it is immaterial as to our problem whether the mortgagor is also to receive money from the purchaser to discharge the mortgage prior to sale, or whether he is merely to transfer subject to the mortgage . . . . We are rather concerned with the reality that an owner of property, mortgaged at a figure less than that at which the property will sell, must and will treat the conditions of the mortgage exactly as if they were his personal obligations. If he transfers subject to the mortgage, the benefit to him is as real and substantial as if the mortgage were discharged, or as if a personal debt in an equal amount had been assumed by another.

This statement by the Court would appear to limit Crane to those situations in which a mortgagor sells the property subject to a (nonrecourse) mortgage and receives additional consideration in the form of "boot." It implies that the value of the property must be greater than the mortgage.

Footnote 37, however, casts doubt on whether Crane is so limited. It states:

Obviously, if the value of the property is less than the amount of the mortgage, a mortgagor who is not personally liable cannot realize a benefit equal to the mortgage. Consequently, a different

the property (other than money) received . . . .

(emphasis added). The code obviously defines "amount realized" in terms of money or property actually received. Thus, Crane was a judicial expansion of the statutory meaning of "amount realized."

19. Adjusted basis is defined in I.R.C. § 1011 (which is substantially unchanged from § 113(b), 1939 Code):

(a) GENERAL RULE—The adjusted basis for determining the gain or loss from the sale or other disposition of property, whenever acquired, shall be the basis . . . . adjusted as provided in Section 1016.

Section 1016 provides the guidelines for adjustments to basis.

20. 331 U.S. at 14.
problem might be encountered where a mortgagor abandoned the property or transferred it subject to the mortgage without receiving boot. That is not this case.\textsuperscript{21}

This footnote has evoked a great deal of controversy and speculation.\textsuperscript{22} It has been construed as mere dictum,\textsuperscript{23} an answer to a hypothetical question,\textsuperscript{24} and finally in Tufts v. Commissioner as an express limitation on Crane.

A. The Theories Behind Crane

Crane is often justified on two theories: the tax benefit theory and the economic benefit theory.\textsuperscript{25} The rationale of the tax benefit theory is that since a taxpayer claims deductions computed upon basis including the nonrecourse mortgage, the amount realized upon disposition must include the amount of the mortgage. The taxpayer must "pay back" any previously claimed deductions.\textsuperscript{26} In Crane, this rationale is readily apparent; the taxpayer claimed deductions on basis which included the mortgage and therefore must pay back the previously claimed deductions by realizing the amount of the equity and the mortgage upon disposition and paying income tax on the total gain. The Court seemed to emphasize this rationale when it stated, "[t]he crux of this case, really, is whether the law permits [taxpayers] to exclude allowable deductions from consideration in computing gain."\textsuperscript{27}

The Crane Court also relied on the economic benefit theory.\textsuperscript{28}

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21. Id. at n.37.
24. Del Cotto, supra note 2, at 83-85. See also, Bittker, supra note 1, at 282.
25. Del Cotto, supra note 2, at 83-84 and n.81; Comment, supra note 23, at 73.
26. Del Cotto, supra note 2, at 83-84 and n.81; Comment, supra note 23, at 74; cf. Bittker, supra note 1, at 282. Professor Bittker feels that the Supreme Court chose to treat nonrecourse loans the same as personal liability for "administrative simplicity," and not because the taxpayer received an economic benefit. He states:
Relief from a nonrecourse debt is not an economic benefit if it can be obtained only by giving up the mortgaged property. It is analogous to the relief one obtains from local real property taxes by disposing of the property: Like nonrecourse debt, the taxes must be paid to retain the property; but no one would suggest that the disposition of unprofitable property produces an economic benefit equal to the present value of the taxes that will not be paid in the future.

Id.
27. 331 U.S. at 15.
28. Del Cotto, supra note 2, at 84.
The thrust of this theory is that when property is subject to nonre- 
course liens totalling less than (or equal to) the value of the prop-
erty, the owner is, in effect, personally liable since he can lose the 
value of the property if it is foreclosed in satisfaction of the lien.29
The Court explained that if a mortgagor "transfers subject to the 
mortgage, the benefit to him is as real and substantial as if the 
mortgage were discharged, or as if a personal debt in an equal 
amount had been assumed by another."30 Although, this economic 
benefit may be apparent under the facts of Crane,31 the rationale 
precludes its application when the value is less than the mortgage 
since the value of property in a foreclosure cannot satisfy the lien. 
Therefore, unlike Beulah Crane, the owner cannot be said to real-
ize an economic benefit equivalent to cash.32 Nevertheless, the 
Crane doctrine—that the amount realized includes nonrecourse 
debt—has been rigidly followed despite the fact that Crane was 
limited to situations in which fair market value exceeded the non-
recourse liability.

B. The Crane Tax Shelter

Crane, by requiring nonrecourse debt to be included in basis, 
has had a continuous impact on tax shelters structured with nonre-
course loans. High depreciation deductions can create losses which 
the investor can offset against other income, thereby saving income 
tax. At an extreme, an investor can, with minimal personal invest-
ment and large nonrecourse loans, secure a high basis for deprecia-
tion purposes. The result is deductions taken in excess of actual 
cash investment, a process known as leveraging. The drawback to 
leveraging stems from the other holding in Crane. Upon disposi-
tion (be it sale, foreclosure or abandonment), the amount realized 
includes the full amount of the nonrecourse loan. The gain often 
greatly exceeds any cash received. Such a gain is known as phan-
tom gain. Thus, the tax benefits incurred initially by the investor 
in a typical tax shelter with nonrecourse debt are paid back as 
taxes on the amount realized upon disposition. The investor might 
still realize a benefit in that his taxes are deferred to a later date 
and he might realize a capital gain although the deductions were

29. See Del Cotto, supra note 2, at 84; note 26 supra. But see Bittker, supra note 1, at 
282.
30. 331 U.S. at 14.
31. Del Cotto, supra note 2, at 84; Comment, supra note 23, at 74.
32. See, e.g. Tufts v. Commissioner, 651 F.2d 1058, 1060-63 (5th Cir. 1981).
ordinary. In essence, the taxpayer receives an interest-free loan from the government and an opportunity to convert ordinary income to capital gain.\textsuperscript{33}

The use of nonrecourse loans in tax shelters, however, was substantially curtailed by the “at risk” limitations incorporated into the Internal Revenue Code (I.R.C.) by the Tax Reform Act of 1976.\textsuperscript{34} As a result of these changes, in most types of investments, deductions are allowed only to the extent of personal liability, i.e. cash “at risk.” This severely curtails the utility of nonrecourse loans. But, because real estate investments are not included in the “at risk” limitation the implication of Crane on the use of nonrecourse debt in tax shelters continues. Furthermore, the disposition of pre-“at risk” shelters will still be governed by Crane and footnote 37.\textsuperscript{35}

The implication of footnote 37 to investors disposing of tax shelters is that it presents the possibility of a great “bonanza.” One commentator, in discussing the surprisingly small number of cases that have arisen from all the investments that lost money, suspected the reason to be a reliance on footnote 37. As he put it:

\begin{quote}
[I]t is not uncommon for them [taxpayers and the professionals who prepare tax returns] to disregard the possibility of gain on the foreclosure or abandonment of a tax shelter on the authority
\end{quote}

\textsuperscript{33} See generally Tax Sheltered Investments (H. Enberg, ed. 1973); Del Cotto, supra note 2, at 95; Comment, supra note 23, at 57.

\textsuperscript{34} I.R.C. § 465, as amended by The Tax Reform Act of 1976, Pub. L. No. 94-455, § 204, 90 Stat. 1531 (1976). This section applies to individuals, electing small business corporations, and personal holding companies. Id. at 465(a). Under § 465(c), as enacted in 1976, the limitations apply to the following activities: production or distribution of motion picture films or video tapes, farming, equipment leasing, and the exploration or exploitation of oil and gas resources. This was expanded in 1978 to cover all activities other than real estate. The effect of this is that deductions are allowable only to the extent that the taxpayer contributed money or other property, or is personally liable on amounts borrowed to finance the investment. Id. at (b).

Section 465, as amended to apply to all activities other than real estate, curtailed the use of nonrecourse debt in most tax shelters. In real estate, nonrecourse debt still provides tax shelter opportunity.

The Economic Recovery Tax Act of 1981 (ERTA) provides additional legislative remedies to the tax shelter problem. It establishes a penalty for tax deductions taken from an inflated basis. This new penalty is not deductible.

Additionally, as a result of ERTA, the incentive of tax shelters is reduced. The maximum income tax rate is reduced from seventy to fifty percent effective in 1982. Thus, tax deductions will be less beneficial to the taxpayer. [1981] 13 Tax Notes 15, at 863, 865 (hereinafter Tax Notes).

\textsuperscript{35} See e.g., Tufts v. Commissioner, 651 F.2d 1058 (5th Cir. 1981); Millar v. Commissioner, 577 F.2d 212 (3d Cir.), cert. denied, 439 U.S. 1046 (1978); Freeland v. Commissioner, 74 T.C. 970 (1980); Broutnas v. Commissioner, 73 T.C. 491 (1979).
of . . . [footnote 37], suggesting that gain cannot be realized on the disposition of property subject to a nonrecourse debt in excess of its basis, unless the taxpayer receives cash or other property to boot.\(^36\)

Until *Tufts*, those who invested in unprofitable tax shelters paid a price; they had to pay back, at least in part, their interest-free loans to the government. As a result of *Tufts* they no longer have to repay this tax benefit.

### III. Post-Crane Case Law

#### A. In General

The fact that *Crane* has had such continuous impact upon tax law is testimony to its significance. Good or bad, *Crane* apparently is here to stay and the *Crane* doctrine—that amount realized includes nonrecourse loans—has grown considerably since its birth.

The facts in *Crane* involved the acquisition of property by devise and its subsequent disposition by sale. Theoretically, *Crane* could have been limited precisely to this situation. In *Blackstone Theatre Co.*,\(^37\) however, the Tax Court held that the *Crane* doctrine also applies to acquisitions by purchase. The petitioner in *Blackstone* had purchased real estate subject to outstanding tax liens in excess of $120,000. The tax liens were included in the property's cost basis for purposes of depreciation. Several years later, the petitioner purchased the tax liens for a reduced price of approximately $50,000. The issue before the court was whether the petitioner's basis, for purposes of depreciation, included the original full amount of the outstanding tax liens.\(^38\) The court, on the authority of *Crane*, held that the liens were part of the cost basis,\(^39\) thereby expanding the *Crane* doctrine to purchased property.

Shortly thereafter, *Parker v. Delaney* settled the debate whether *Crane* applies when property is abandoned upon foreclosure, rather than is sold.\(^40\) The First Circuit Court of Appeals held that

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36. See Bittker, *supra* note 1, at 277. The "bonanza" lies in the fact that taxpayers have been able to take large deductions, based upon a high basis which consists mostly of nonrecourse debt. Then, if the fair market value is lower than the debt at the time of disposition, according to footnote 37, the amount realized is limited to the fair market value (rather than the amount of the debt). See, e.g., *Tufts* v. Commissioner, 651 F.2d at 1058.

37. 12 T.C. 801 (1949).

38. *Id.* at 802.

39. *Id.* at 804-05.

40. 186 F.2d 455 (1st Cir. 1950); see Del Cotto, *supra* note 2, at 89.
abandonment was within the meaning of "sale or other disposition." Therefore, the taxpayer realized a gain equal to the full amount of the mortgage when he abandoned the property. The court reasoned:

They [the liens] are treated as cost at the earlier time [acquisition] and so must be treated as value at the later time [disposition]. The result in the end is that the taxpayer accounts to the taxing authorities for the gain realized by his deductions for depreciation in excess of his own investment.

The court was apparently relying on the tax benefit theory because its concern was that the taxpayer was able to claim deductions and therefore he must repay them upon disposition.

Parker also applied Crane to dispositions of property in which the value equals the amount of the mortgage. In Crane, the value of the property upon disposition exceeded the amount of the mortgage. The court stated:

The added factor there [in Crane], not present here, that boot was paid over and above the mortgage, is not material so long as the value of the properties was not less than the liens. Boot served to show this in the Crane case but the payment of boot is of course not the only means of showing whether or not value is equal to or more than the liens on the property disposed of.

This was the first explicit recognition that Crane applies when the value equals the debt.

In Johnson v. Commissioner, the Sixth Circuit Court of Appeals held that a gift is a disposition that is equivalent to a sale in the amount of a mortgage encumbering it. In Johnson, the taxpayer transferred stock, which was the security for a loan taken the same day, to an irrevocable trust. The amount of the loan was held to be an amount realized to the taxpayer at the time of the gift, thus resulting in taxable income. The court recognized that

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41. Int. Rev. Code of 1931, § 111 (now I.R.C. § 1001(a)(b)).
42. 186 F.2d at 458-59.
43. Id. at 459.
44. Id. at 458.
46. Joseph W. Johnson, 59 T.C. 791, aff'd 495 F.2d 1079; see Weiss supra note 2, at 303.
47. The value of the stock above the amount of the loan subjected the taxpayer to gift tax liability. 495 F.2d at 1082.
"[t]he substance of a transaction rather than its form must ultimately determine the tax liabilities of individuals," and further that "[t]he substance of the transactions in this case was a gift of $500,000 worth of stock in exchange for $200,000." Accordingly, the $200,000 was an amount realized for purposes of computing gain.

Efforts have been made to expand Crane in ways other than widening its application to different methods of disposition. Investors in tax shelters have relied on Crane to create high basis through the use of large, sometimes questionable, nonrecourse notes. Crane seemed to provide the authority for taxpayers to enlarge their basis as much as possible. Some efforts succeeded; some did not.

In Manual D. Mayerson, the I.R.S. tried unsuccessfully to prevent the taxpayer from including a purchase-money mortgage in the basis of property he purchased. The taxpayer bought a $332,500 building, financed by a 99-year nonrecourse note and $10,000 cash payment. The Tax Court first determined that, under authority of Crane, the absence of personal liability on the note did not preclude its inclusion in basis. Furthermore, since the court had already decided that the transaction was bona fide and created a valid debt obligation, it determined that the length of the term for maturity did not affect the validity of the debt obligation.

48. Id. (citations omitted).
49. Id.
50. A voluntary reconveyance, as opposed to the foreclosure in Parker, was held to constitute a sale or disposition in Freeland, 74 T.C. 970 (1980). The taxpayer realized the amount of the mortgage upon the voluntary abandonment. The court also stated, possibly as dictum, that "the fact that petitioner realized no tax benefits in the form of depreciation deductions while he held the property" should not determine the character of the transaction. Id. at 982. This too, can be considered an expansion of Crane.
52. 47 T.C. 340 (1966). See David F. Bolger, 59 T.C. 760 (1973) for an even more extreme application of the Crane rule; see also Weiss, supra note 2, at 293-94.
53. 47 T.C. at 351.
54. Id. at 352. Cf. Del Cotto, supra note 2, at 76, (critical of the Mayerson decision): [T]he Mayerson court was so concerned with the general rule that it failed to recognize the crucial difference between Mayerson and Crane. In Mayerson, no payments beyond the initial $10,000 were due for ninety-nine years; therefore, there was greater doubt than in Crane that the mortgage would be paid. To give advance credit for the amount of the mortgage when there is such uncertainty that the mortgage would be paid can only be viewed as an extreme application of the Crane doctrine.

Id. (emphasis added).
light of Crane as precedent, since the transaction was determined to be bona fide.\textsuperscript{55}

The I.R.S. acquiesced in the Mayerson decision in a Revenue Ruling, but indicated that "the fair market value of the property was not put at issue in the case."\textsuperscript{56} The ruling warned that "[t]he Service will continue to review transactions involving purported purchases of depreciable property where, in the light of all the facts and circumstances, it appears that the transactions were designed to improperly create or inflate depreciation deductions. In cases of this type, the Service will disallow unwarranted depreciation deductions."\textsuperscript{57}

In \textit{Marvin M. May}\textsuperscript{58} the Tax Court disallowed deductions because the transaction was a sham. The taxpayer claimed a basis of $365,000 in several television episodes of which he personally paid only $35,000. The transaction was found to be a sham because the taxpayer never owned the films, he never intended to repay the loan, and the true owners never intended that he pay. The court concluded that "[a]lthough the transaction was dressed up to look like a sale on the basis of which petitioner might claim $365,000 depreciation deductions, all that really occurred here was petitioner's payment of $35,000 for a facade to enable him to claim such deductions."\textsuperscript{59}

Similarly, the Tax Court has disallowed deductions attributable to basis which included debt obligations which were contingent and unascertainable.\textsuperscript{60} The Ninth Circuit has also held that a transaction which, in essence, consisted of an \textit{option} to purchase a motel was not an investment.\textsuperscript{61} Since no cash would change hands for ten years and the taxpayer could show no correlation between

\textsuperscript{55} \textit{But see} Arnold L. Ginsberg, 35 T.C.M. 860 (1976); Mark Bixby, 58 T.C. 757 (1972); Marvin M. May, 31 T.C.M. 279 (1972); Leonard Marcus, 30 T.C.M. 1263 (1971).

An argument in support of \textit{Mayerson} can be made that the taxpayer's actions (purchasing an aging, dilapidated building and rejuvenating it) should not be discouraged. Thus, there should be an incentive, in the form of large tax deductions, available to those willing to invest in such ventures.

\textsuperscript{57} \textit{Id.}
\textsuperscript{58} 31 T.C.M. 279 (1972).
\textsuperscript{59} \textit{Id.} at 284.
\textsuperscript{60} Leonard Marcus, 30 T.C.M. 1263 (1971); \textit{see also} Gibson Products Co. v. United States, 460 F. Supp. 1109 (N.D. Tex., 1978) (court held that the liability on a nonrecourse note was contingent upon oil and gas production and therefore not a true liability); \textit{but see} Paul P. Brountas, 73 T.C. 491 (1979) (court determined nonrecourse notes on oil and gas payments had value despite their contingent nature).
\textsuperscript{61} Estate of Franklin v. Commissioner, 544 F.2d 1045 (9th Cir. 1976).
fair market value and the purchase price, the court disallowed the claimed deductions.\(^6\)

**B. The History of Footnote 37**

When one considers the potential impact of footnote 37 on dispositions of failing tax shelters, it is indeed surprising that it has been the subject of little litigation.\(^6\) For the most part, references to it were made regarding its inapplicability or that the footnote was merely dictum. The impression is that footnote 37 has long been considered a dead argument and those who attempted to rely on it did so in vain. Additionally, the I.R.S., in Revenue Ruling 76-111, expressly rejected any inference that footnote 37 could limit the amount realized on disposition.\(^6\)

The first attempt to rely on footnote 37 did not aid the taxpayer. In *Parker v. Delaney*, the taxpayer argued that the value of the property was less than the mortgage and therefore *Crane* did not apply. The court was able to dismiss this contention without discussion since it found nothing in the record suggesting the value was lower than the mortgage. The court implied, however, that if the value was indeed less than the mortgage, the amount realized might be limited to the value of the property.\(^6\) The door to foot-

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\(^6\) Id.

\(^63\) Of course, this may change in response to the *Tufts* decision. 651 F.2d 1058 (5th Cir. 1981). See discussion accompanying notes 106-123 infra.

\(^64\) Rev. Rul. 76-111, 1976-1 C.B. 214. This Revenue Ruling involved a reconveyance of secured property to the seller, in consideration of the cancellation of the buyer's indebtedness. After deciding that the transaction was equivalent to a sale, the Commissioner held "whatever inference may be drawn from footnote 37 in the *Crane* case, the unpaid balance on the sales contract, which indebtedness was cancelled upon the transfer . . . is the amount realized . . . regardless of the fair market value of the [property] . . . ." Id. at 215.

\(^65\) 186 F.2d at 458. Cf. *Woodsam Associates v. Commissioner*, 198 F.2d 357 (2d Cir. 1952). The petitioner in *Woodsam* had requested a finding that the value of property disposed of was less than the mortgage which, under footnote 37 of *Crane*, he would have only realized the fair market value of the property. The petitioner subsequently disclaimed any reliance on footnote 37, which according to the court was "advisedly so." Id. at 358 n.1. *Woodsam*, however, involved the determination of amount realized when the taxpayer borrowed cash from nonrecourse borrowings after the property was already acquired. *See also* Mendham Corp., 9 T.C. 320 (1947). In both these cases, the court stressed the fact that "postacquisition borrowings" for the taxpayers' benefit were involved. *See McGuire, supra* note 2, at 1443 and 1447-49 (1978).

*Davis v. Commissioner*, 585 F.2d 807 (6th Cir. 1978), involved conveyances by a corporation of property valued at least equal to the liens securing it. The court remarked in a footnote that "[c]onsequently, there will be no issue in this case as to what footnote 37 meant in *Crane v. Commissioner*." Id. at 810 n.4 (citation omitted). The Tax Court in Joseph W. Johnson, quoted part of *Crane* and in reference to footnote 37 stated: "The [Crane] Court indicated in fn. 37 that a different problem might be encountered if the value of the
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note 37 was opened slightly.

It was not until the latter part of the seventies that the strength of footnote 37 was put to the test. Economic conditions in that period apparently resulted in many "tax shelters in ruins," in that tax shelters, upon disposition, had fair market values of less than their outstanding mortgages. This fact pattern arose in a group of cases, and the applicability of footnote 37 was scrutinized.

In the first case, *Gavin S. Millar*, the Tax Court held that the value of the property was immaterial in determining the amount realized. The issue arose when R. H. Jamison organized a strip mining corporation which elected to be taxed as a small business corporation (subchapter S). The stock was issued to the petitioners for no consideration. Jamison then advanced $500,000 to the shareholders who each issued a nonrecourse note payable to Jamison for the amount advanced. The security for the notes was the stock in the corporation. The shareholders then contributed the money advanced by Jamison to the corporation.

In the first few years, the corporation operated at a loss. Because of the subchapter S status, the shareholders realized significant tax benefits in the form of loss deductions. By 1967, the corporation faced imminent bankruptcy, rendering the stock worthless. At this time, Jamison demanded payment on the notes. When no payments were made, he foreclosed on the stock.

None of the petitioners reported any gain upon the transfer of their stock to Jamison. They argued that they did not realize a gain because the value of the stock was worthless and therefore less than the value of the nonrecourse note at the time of foreclosure. Footnote 37 was the exclusive source of their argument. The Commissioner, however, argued that the petitioners realized a tax-

property was less than the amount of the mortgage, but stated that was not the case there. It is also not the case here." 59 T.C. 791 at 809 n.3, aff'd 495 F.2d 1079 (6th Cir.) cert. denied, 419 U.S. 1040 (1974).


67. 67 T.C. 656 (1977), aff'd sub nom. Millar v. Commissioner, 577 F.2d 212 (3d Cir.), cert. denied, 439 U.S. 1046 (1978). *See* Note, *supra* note 6. This case was originally heard by the Tax Court in 1975, 34 T.C.M. 554 (1975), and was then appealed to the Third Circuit, 540 F.2d 184 (3d Cir. 1976), which remanded the case to the Tax Court, 67 T.C. 656. It was appealed to the Third Circuit once again, 577 F.2d 212 (3d Cir. 1978). The Supreme Court eventually denied certiorari, 439 U.S. 1046 (1978).

68. I.R.C. §§ 1371-79.

69. 540 F.2d 184, 185 (3d Cir. 1976). The shareholders also benefitted by the investment tax credits earned by the corporation, and interest payments made by the corporation on the notes. *Id.*

70. 540 F.2d at 185.
able gain in the amount of the loan, less the adjusted basis. He too relied on *Crane*, but on the main principles of the case—that basis includes unassumed mortgages and that upon disposition, the amount realized includes the amount of the mortgage—rather than on footnote 37.71

The Third Circuit upheld the Tax Court's finding that according to the reasoning of *Crane*, the petitioners did incur a tax liability.72 The court explained that despite the factual difference between the two cases, the principle reasoning for the *Crane* decision applied to *Millar*. The taxpayers in both *Crane* and *Millar* had enjoyed tax benefits and must therefore include the full amount of the mortgage to pay back those benefits. The *Millar* court believed that "[a] finding that the taxpayers did not realize gain as a result of this exchange, after having realized the full economic benefit of this transaction, would entitle them to the type of double deductions which the Supreme Court so clearly disapproved in *Crane*."73 Thus, the court was relying almost exclusively on the tax benefit theory of *Crane* as the justification for its decision.

The court did acknowledge that if footnote 37 were taken literally, it "might" provide support for the petitioners' contention that they did not realize the amount of the loan. The court did not accept this reasoning, however, and explained:

[I]n the analysis of this problem, the footnote should be evaluated in the proper context. First, it must be remembered that the footnote in *Crane* was *dictum*. Furthermore, the footnote was but a postulate or hypothetical observation with respect to a hypothetical set of facts not before the Court and, indeed, involving a clearly different time and clearly different legal circumstances. . . . Thus, applying *Crane* to the facts of the case before us, it is clear that the transaction resulted in taxable gain to the taxpayers by reason of the inclusion of the nonrecourse obligation in the calculation of basis as well as the amount realized when computing the presence or absence of gain resulting to the taxpayers from the foreclosure of the notes and surrender of the stock.74

*Millar* provided the precedent for several cases that followed. In *John F. Tufts*, the Tax Court reached the same conclusion as *Mil-

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71. 577 F.2d at 215.
72. Id.
73. Id. at 215.
74. Id. at 215-16.
lar. (This Tax Court decision was reversed by the Fifth Circuit in *Tufts v. Commissioner.*\(^{75}\) In *Tufts* the members of a partnership used borrowed, nonrecourse funds to construct an apartment complex. They sold the complex subject to the mortgage when the value was less than the outstanding mortgage and claimed they realized only the fair market value as gain.\(^{76}\) This claim was based on footnote 37—that they did not realize an economic benefit except the amount of the fair market value of the property.\(^{77}\) The Tax Court determined, however, that the petitioners realized the full amount of the outstanding liability.\(^{78}\)

The Tax Court has had several other opportunities to hold that upon the disposition of property valued at less than the nonrecourse loans, the amount realized was nevertheless the full amount of the mortgage. In *Estate of Delman,*\(^{79}\) the court relied heavily on the reasoning of *Millar* and *John F. Tufts.* The court explained the applicability of the tax benefit theory as the justification for *Millar, Tufts,* and its own decision.\(^{80}\)

In *Eugene L. Freeland,* the Tax Court seized the opportunity to once more reaffirm its holdings in *Tufts* (then on appeal to the Fifth Circuit) and *Delman.*\(^ {81}\) The petitioners purchased land valued at $50,000 with a $9,000 cash payment and a nonrecourse note for $41,000. The land value decreased to $27,000, at which time the petitioner reconveyed the land by quitclaim deed to the seller. After first determining that a voluntary abandonment was equivalent to a sale,\(^{82}\) the court concluded that the petitioner suffered a capital, rather than an ordinary loss. The reference to footnote 37 was merely a rejection of the petitioner's attempted reli-

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75. 70 T.C. 756 (1978), rev'd *Tufts v. Commissioner,* 651 F.2d 1058 (5th Cir. 1981).
76. 70 T.C. 756 (1978). *But see Tufts v. Commissioner,* 651 F.2d 1058 (5th Cir. 1981). *See* discussion accompanying notes 85-92, 105 infra. The petitioners made an alternative argument, that under I.R.C. § 752, which is considered a codification of the *Crane* doctrine in determining a partner's basis in a partnership, the fair market value limitation of (c) applied to the sale of a partnership interest under § 752(d). 70 T.C. at 766. *See also* Perry, *Limited Partnerships and Tax Shelters: The Crane Rule Goes Public,* 27 Tax L. Rev. 525, 543 (1972), (through an analysis of legislative history and regulations, the Tax Court concluded that § 752(c) was meant to be applied very narrowly and thus, did not apply in this case.) *Id.* at 767-68.
77. 70 T.C. at 764.
78. *Id.*
79. 73 T.C. 15, 28-30 (1979).
80. *Id.* at 30.
81. 74 T.C. 970. The court did this despite the fact that the issue before the court differed from that in *Tufts, Delman* (and *Millar*). *Freeland* concerned a determination of whether the loss incurred by petitioners was a capital or ordinary loss. *Id.*
82. *See* note 50 supra.
ance on it.\textsuperscript{83}

Several of the above cases relied, at least in part, upon the Tax Court decision in Tufts.\textsuperscript{84} All noted its forthcoming appeal, but certainly none expected a reversal. Nevertheless, the Fifth Circuit reversed the Tax Court decision. By doing so, it shook the foundation of those cases which had followed Tufts and gave renewed vigor to the argument in favor of footnote 37. More important, it has opened the door wider to what may be perceived as a loophole in the tax law.

IV. Tufts v. Commissioner

A. The Facts

In August 1970, John F. Tufts and several others formed a general partnership to construct an apartment complex. They obtained a loan of $1,851,500 which was insured under section 3221(d)(4) of the Federal Housing Act.\textsuperscript{85} The partnership itself was not personally liable on the loan. The mortgage covered the entire cost of construction which was completed in August of 1971. In the face of deteriorating economic conditions, the partnership was forced to lower the rents. Even so, the complex never attained full occupancy. As a result, the partnership was unable to reduce the mortgage principal.\textsuperscript{86}

From 1970 to 1972, each of the partners individually claimed his proportionate share of losses incurred by the partnership. By August of 1972, the fair market value of the apartment complex had fallen to $1,400,000. Although the principal due on the mortgage remained $1,851,500, the partnership's basis in the property had decreased to $1,455,740 because of the deductions taken.\textsuperscript{87} On August 28, 1972, the complex was sold to a third party. The buyer agreed to pay expenses up to $250, but paid no other considera-

\textsuperscript{83} 74 T.C. at 978.

\textsuperscript{84} See discussion accompanying notes 74-82, supra. See also Gibson Products Co. v. United States, 637 F.2d 1041 (5th Cir. 1981). In Gibson the Court of Appeals held that nonrecourse notes given for the purchase of oil and gas leases were too contingent upon potential production and thus were not loans. In a footnote, the court stated that, although it was not deciding whether the party could increase its basis by its proportionate share of the note, the argument that "nonrecourse indebtedness of a partnership can be included in a partner's basis only to the extent that it equals or exceeds the market value of the property securing the debt" was a valid one. \textit{Id.} at 1045 n.8.

\textsuperscript{85} Tufts v. Commissioner, 651 F.2d 1058, 1059 (5th Cir. 1981); Brief for Appellants at 3.

\textsuperscript{86} Brief for Appellants at 4.

\textsuperscript{87} \textit{Id.} at 5.
tion, thus acquiring the complex subject to the nonrecourse liability.88 Each partner had computed his basis to include his proportionate share of the mortgage. They did not, however, include the full amount of the nonrecourse liability in the determining the amount realized upon the disposition of the property. Rather, each partner took a long-term capital loss. The I.R.S. claimed that the full amount of the nonrecourse liability was the amount realized upon the sale and therefore each partner realized a taxable gain.89

The partners petitioned the Tax Court,90 arguing that under footnote 37 the amount realized should be limited to the fair market value of the property securing the liability. The court, however, relying heavily on Millar v. Commissioner, rejected the argument and held for the I.R.S.91

An appeal was taken to the Fifth Circuit. The decision, which reversed the Tax Court, must have been somewhat of a surprise to those familiar with the judicial trend.92

B. The Holding

The Court of Appeals phrased the question precisely: "[W]hether footnote 37 creates an exception to the Crane holding through its clear implication that the amount realized on the disposition of property encumbered by a nonrecourse mortgage cannot exceed the fair market value of the property."93 Through an exhaustive analysis of "the reasons underlying the Crane decision," the court concluded that a fair market value limitation was indeed justified.94

The court first addressed the Millar decision, which had rejected a "literal" interpretation of footnote 37.95 It criticized Millar, the Commissioner, and the Tax Court for their conclusion that the primary concern of Crane was that the taxpayer would enjoy a double deduction. Taxpayers should not be able to take large deductions, with only minimal personal investment, thereby benefitting by paying less in taxes. They must be required to pay for tax benefits

88. 651 F.2d at 1059.
89. Id.; John F. Tufts, 70 T.C. 756, 761 (1978).
90. 70 T.C. 756.
91. Id.; see discussion accompanying notes 67-74, supra.
92. 651 F.2d at 1060.
93. Id..
94. Id.
95. Id. See discussion accompanying notes 67-74, supra.
received. The double deduction language is invoked in support of the tax benefit theory which the other courts and Commissioner consider to be the principle rationale of Crane. On this reasoning alone, the tax benefit theory does justify the Commissioner's position in both Tufts and Millar.

The Fifth Circuit, however, disagreed that the concern for double deductions was the principle rationale underlying Crane. The court noted that the Supreme Court had already expanded the definition of amount realized to include its amount of nonrecourse loans. The Supreme Court's discussion of double deductions appeared in the last paragraph of the opinion, solely in response to Crane's alternative argument that she did not receive any income for which she could be taxed within the meaning of the sixteenth amendment. The Tufts court thus experienced an acute uneasiness with the double deduction and tax benefit theories as the principle justifications for the Crane holding. Additionally, the court found that deductions "have already been factored into the gain equation through adjustments to basis." Gain is computed by subtracting adjusted basis from amount realized. Since adjusted basis is the cost of property less any deductions, the amount of gain will reflect those deductions taken. The court reasoned:

To account for those deductions twice in the same equation by expanding the definition of amount realized as well as adjusting basis downward would, we think, be taxing the taxpayer twice on the same component of gain. The Commissioner's reliance on a theory of tax benefit, then, is misplaced. The Code clearly provides for a "recapture" of the prior deductions, but not through its definition of amount realized.

The Fifth Circuit saw the economic benefit theory as the princi-

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96. 651 F.2d at 1060.

97. Id.

98. The court explains this as an "uncertainty as to the exact nature of the 'double deductions' that concerned the [Crane] Court." Id. at n.4. It explains further:

We had always supposed that Congress chose to allow depreciation deductions on the assumption that wear and tear would diminish the value of the property. In other words, Congress decided to compensate a property owner, by allowing him to take depreciation deductions, for an expected loss in value due to deterioration of the property. We therefore do not understand why, if the property does in fact decline in value as was expected, "manifest justice" requires the taxpayer to somehow "surrender" the previous deductions or the gain that he never realized.

Id.

99. Id. at 1061.

100. Id. (footnotes omitted).
ple justification for the Crane holding. It concluded, however, that despite the initial "facial appeal of that notion," this theory too, is "seriously flawed."101 A taxpayer not personally liable on mortgaged property will treat the mortgage as a personal obligation only as long as he wants to keep the property.102 Thus, although Crane (and Tufts) did receive some benefit, the court "seriously question[ed] whether the full amount of nonrecourse debt is an accurate measure of that benefit."103

Because of its "reservations" about Crane, the Tufts court could not "extend [Crane] beyond the facts of that case."104 Thus, upon disposition of property, a seller can include only the fair market value of the property, as amount realized, when that value is less than the nonrecourse debt.105

C. Analysis

Clearly, the Tufts decision was a shock to the tax field. Imagine the reaction of the tax practitioner who, on the basis of Crane, Parker, and Millar advised his clients that on the foreclosure of burnt out tax shelters, the taxpayer would realize the full amount of the nonrecourse loans as gain—a phantom gain. Most tax practitioners undoubtedly told their clients that in view of the I.R.S. position and case law supporting it, there was no way to avoid this result and that efforts to do so would be futile. Tufts, however, changes the situation entirely.

101. Id. at 1062.
102. Id. The court refers to Professor Bittker, with whom it agrees. See discussion accompanying notes 27-32 supra.
103. Id. at 1063.
104. Id.
105. The taxpayers alternatively argued that § 752 requires a decision in their favor. Sections 752(c) and (d) are as follows:

(c) LIABILITY TO WHICH PROPERTY IS SUBJECT—For purposes of this section, a liability to which property is subject shall, to the extent of the fair market value of such property, be considered as a liability of the owner of the property.

(d) SALE OR EXCHANGE OF AN INTEREST—In the case of a sale or exchange of an interest in a partnership, liabilities shall be treated in the same manner as liabilities in connection with the sale or exchange of property not associated with partnerships.

Briefly, the taxpayers argued that the two sections should be read in conjunction. The Commissioner, with whom the Tax Court agreed, argued that the sections operate independently and actually conflict with one another. See 70 T.C. at 766-68 for a thorough discussion of the argument and the Tax Court's treatment of it.

The Fifth Circuit addressed this issue in a footnote only. It acknowledged both arguments but then stated that its holding eliminates any conflict the Commissioner construes to be within § 752. 651 F.2d at 1063 n.8. See note 75 supra.
Furthermore, tax practitioners are all too familiar with the liberality with which tax shelters have been structured to permit large tax deductions. The Millar decision seemed just, if not correct; the benefits of large tax deductions should be balanced against eventual tax liability upon disposition. Therefore, most tax advisors would instinctively accept Millar. Only the most aggressive would suggest reporting an amount realized limited to the fair market value under the authority of footnote 37.

Thus, the initial reaction to Tufts might be that it runs against the grain of fairness. The Tufts decision will inevitably reduce the taxes collected by the I.R.S. Many taxpayers will reap tax shelter benefits—large deductions and amount realized on disposition limited by the fair market value of encumbered property.106 Interestingly, the Tufts court did note that "it is somehow unfair for a taxpayer to enjoy the benefit of substantial deductions without having invested his own funds or placed his own assets at risk."107 This concern is made more credible by the prevalence of abusive tax shelters, created solely to obtain large tax deductions.108 But when the overall effect of Tufts is considered, it is not only a well reasoned opinion, but an equitable one as well.

The Tufts court did find it necessary to put its decision in its "proper perspective." It concluded with a long, explanatory footnote109 discussing the conflict with other courts and the impact that the decision will have on the tax shelter industry. The court detected "a legitimate concern for potential abuses or at least misuses of the tax law through various tax shelter schemes."110 The crux of Tufts, then, is not so much that the court applied footnote 37 literally, but rather the decision's effect on the tax shelter industry.

According to the I.R.S., an increasing number of shelters are abusive in that they involve inflated bases and lack "economic reality."111 Tufts correctly attributed this problem to the taxpayers' ability to "manipulate" basis and adjusted basis through the use of nonrecourse financing.112 The problem of abusive tax shelters, how-

106. 651 F.2d at 1063 n.9.
107. Id. at 1064 n.9.
108. See Bittker, supra note 1, at 283-84, for an example of an extreme application of footnote 37. See also Tax Notes, note 34 supra.
109. 651 F.2d at 1063 n.9.
110. Id.
111. Tax Notes, supra note 34, at 863.
112. 651 F.2d at 1064 n.9.
ever, cannot and should not be solved through a strained interpretation of the meaning of “amount realized,” as in *Millar*. I.R.C. § 1001(b) which defines amount realized, on its face does not require the inclusion of debt liability when the value of the property being disposed of is less than the encumbrance.113

*Crane* expanded the definition of amount realized to include nonrecourse liability where the value of the property exceeded the debt. In *Crane*, it is readily apparent that the taxpayer did, in fact, receive an economic benefit equivalent to cash.114 It is an illogical and unreasonable expansion of *Crane*, however, to find a similar economic benefit in the amount of the debt liability in situations where the value of the property is less than the debt. As the *Tufts* court stated: “It is not a solution to distort the definition of amount realized by finding an economic benefit equivalent to cash where none exists.”115 It follows that the solution to the problem of potential abuse lies in judicial, administrative, and legislative measures to prevent inflated basis and the claiming of unwarranted deductions on those investments which lack economic reality. This has been done to an extent by Congress with the “at risk” limitations of I.R.C. § 465.116 The judiciary, too, has refused to allow deductions computed on inflated basis and “sham” transactions.117 Regardless of how Congress chooses to prevent unwarranted tax benefits, the judiciary should not take it upon itself to do so by rewriting the statutory provision which defines amount realized.

The *Millar* approach to solve the abusive tax shelter problem requires the taxpayer to pay back the tax benefits he received. Presumably, this rights an assumed wrong—deductions which never should have been allowed. *Millar* errs in assuming that all transactions involving nonrecourse debt are abusive; it disregards the fact that many such investments, while tax-oriented, are economically motivated with reasonable expectations of profit. Thus, *Millar* goes too far; it penalizes the taxpayer who entered into a tax-oriented transaction to make a profit, along with the true target—the investor seeking tax deductions only. The control of abusive tax shelters should begin at their formation.118 The I.R.S. should disallow unwarranted deductions, through more effective auditing of tax shel-
ter returns. Millar cannot solve the problem. Tufts, on the other hand, recognizes that it is not the courts' role to solve the tax shelter problem by stretching the Code to "recapture" some of the benefits the taxpayers received. The court correctly states that it is Congress' responsibility to do this but that it "has not yet done so under the circumstances of this case."

The Tufts decision, by itself, will undoubtedly benefit many who have already received considerable tax advantages. But, if Tufts is the impetus for further legislative and administrative efforts to prevent the claiming of unwarranted tax deductions, the elimination of abusive tax shelters will be attained without violating the definition of amount realized. If these shelters are prevented before their inception, the Tufts decision will benefit only those involved in tax-oriented investments which are not abusive, and where the ultimate disposition occurs when the value is less than the debt.

There is an additional factor which the Tufts decision did not address. The taxpayers in Tufts (or as in any other similar investment) ordinarily have no control over fair market value. With valid investments, it must be assumed that the value of the property equals or exceeds the debt liability. Otherwise, deductions are disallowed. The reasonable expectation is that the value will not decrease below the amount of the debt. Since a change in fair market value is a fortuitous circumstance, a decrease is certainly beyond the control of the taxpayer. Abusive tax shelters should not distort the fact that legitimate tax-oriented deals are well within the limits of the law.

Furthermore, the nature of the taxpayers' investment in Tufts was of the type encouraged by the availability of tax deductions. The Internal Revenue Code is often used to "advance non-revenue needs." In Tufts, that need was private investment in subsidized housing. Unfortunately, the venture proved to be economically unsound, resulting in a decrease in value. It would be unreasonable to encourage this type of investment on the one hand, and to discourage it on the other by imposing of tax liability on phantom gain if the venture proves unprofitable. Thus, Tufts is consistent

119. See note 34 supra.
120. 651 F.2d at 1064 n.9.
121. See notes 58-62 supra.
123. Brief for Appellant at 43, Tufts v. Commissioner, 651 F.2d 1058.
with goals other than tax collection, which are inherent in the Internal Revenue Code.

V. CONCLUSION

*Tufts v. Commissioner* is clearly a landmark decision in several regards. The first is obvious; it is the first decision to literally apply footnote 37. But the true impact of *Tufts* does not lie in its deference to footnote 37.

The greater impact of *Tufts*, is its potential effect on the tax shelter industry. Undoubtedly, there are many happy tax shelter investors as a result of this decision. The reason is simple; they will save taxes when they dispose of burnt-out tax shelters. *Tufts* can be viewed as creating a loophole in the broad sweep of the *Crane* doctrine; that upon disposition of property, the amount realized includes nonrecourse debt. But, the *Tufts* decision is premised upon the fact that it is not a loophole, but merely a refusal to unreasonably extend the *Crane* doctrine to accomplish a legislative function.

The Fifth Circuit refused to extend the *Crane* doctrine to a fact situation to which it cannot logically apply. The fact that benefits will accrue to undeserving investors because of the *Tufts* decision must not mar the logic of its reasoning.

The fact remains that *Tufts* conflicts with decisions of the Third Circuit and the Tax Court. Inevitably, footnote 37 will face the ultimate test—the Supreme Court. Hopefully, the Court will not be swayed by the appeal of what superficially appears fair. It need look only as far as the logic underlying *Tufts* to make the correct decision.