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IN THE SUPREME COURT OF THE UNITED STATES

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DAVID A. and LOUISE A. :
GITLITZ, et al., :
Petitioners :
v. : No. 99-1295
COMMISSIONER OF INTERNAL :
REVENUE :
- - - - -X

Washington, D.C.
Monday, October 2, 2000

The above-entitled matter came on for oral
argument before the Supreme Court of the United States at
10:00 a.m.

APPEARANCES:
DARRELL D. HALLETT, ESQ., Seattle, Washington; on behalf
of the Petitioners.
KENT L. JONES, ESQ., Assistant to the Solicitor General,
Department of Justice, Washington, D.C.; on behalf of
the Respondent.

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1 P R O C E E D I N G S

2 (10:00 a.m.)

3 CHIEF JUSTICE REHNQUIST: We will hear argument
4 first this morning on number 99-1295 David A. Gitlitz
5 versus the Commissioner of Internal Revenue.

6 Mr. Hallett.

7 ORAL ARGUMENT OF DARRELL D. HALLETT

8 ON BEHALF OF THE PETITIONERS

9 MR. HALLETT: Mr. Chief Justice, may it please
10 the Court: As a result of the position taken by the
11 Commissioner of Internal Revenue on the brief before this
12 Court, the issue the Court needs to decide is a limited
13 one. And that issue is whether the amount of debt
14 discharge or cancellation of debt of an insolvent debtor
15 which is excluded from income under Section 108 is income,
16 such that it amounts to an item of income which increases
17 the shareholder's stock basis under Sections 1366 and
18 1367 of the Internal Revenue Code.

19 The Commissioner rests his entire case in his
20 brief on the argument that under Section 108 no income is
21 realized by the insolvent debtor. Your Honors, that
22 position is clearly contrary to the statute. And if I may
23 rather than paraphrasing initially, read the statute, I
24 think it's really critical to this issue and resolves this
25 issue. And that statute is section 108(a)(1) in the

1 appendix to the petition, at Page 34.

2 And it states as follows: Gross income does not
3 include any amount which, but for this subsection, would
4 be includable in gross income by reason of the discharge
5 of indebtedness of the taxpayer if the discharge occurs
6 when the taxpayer is insolvent.

7 To paraphrase that, Your Honors, what that
8 subsection (a) says in hopefully plain English is that an
9 item is only excluded under Section 108 if it otherwise
10 would have been included in gross income under Section 61.

11 QUESTION: Well, I think your argument under the
12 statute is a strong one. But is there any reason in tax
13 theory or practical equity why Congress would want to
14 allow this result in this particular case? I mean, I
15 understand that the statute may compel this, but is there
16 some underlying rationale to support your position?

17 MR. HALLETT: It may well be consistent with the
18 restructuring of the Internal Revenue Code in 1954, in
19 which Congress said very broadly in Section 61 that gross
20 income includes all income from whatever source derived,
21 and listed specific items, some 15 of those, and one of
22 them is income from subsection 12.

23 And then consistent with that over in Sections
24 101 through 138, those items that are included in income
25 are specifically excluded from gross income. So --

1 QUESTION: What I am asking is why would Congress
2 allow you to use income that you don't pay tax on, to
3 increase the basis and then which would allow you to
4 deduct additional unrelated losses?

5 MR. HALLETT: Well, first of all, because this
6 statute clearly says that --

7 QUESTION: I know that's position number one.
8 I'm asking, is there a reason for this?

9 MR. HALLETT: There's a reason for it is that in
10 the final analysis, the basis reflects the shareholder's
11 equity in the corporation, roughly speaking, and the
12 shareholder gets equity in the corporation by contributing
13 capital. He also gets equity in the corporation when
14 income is realized, taxable or nontaxable. And the
15 Congress recognized that if losses have accumulated such
16 that they are not deductible because they exceed the
17 basis, well when income is realized, nontaxable income
18 such as municipal bond interest, that income goes down to
19 increase the basis to reflect the fact that there now is
20 an increased equity investment.

21 QUESTION: Mr. Hallett, it seems that the
22 Subchapter S shareholder is the only solvent entity who
23 could take advantage of this. The peculiar thing about
24 this provision is that every other taxpayer, say a
25 Subchapter C corporation, a partner in a partnership, the

1 insolvent would have to be that entity, that tax paying
2 entity. But here you have the peculiarity that the
3 Subchapter S corporation, which is not itself a taxpayer,
4 is the insolvent, while the shareholders are highly
5 solvent. And is there any reason why Congress would want
6 to give those solvent taxpayers this advantageous
7 treatment?

8 MR. HALLETT: I think what -- they clearly did
9 that in 1984 when the Congress said that in the case of an
10 S corporation, the amount is excluded if there's
11 insolvency at the corporation level. They certainly
12 recognized that by doing that, the benefit of the
13 exclusion would come down to the shareholder who could
14 well be solvent.

15 And I think to the extent the legislative
16 history reflects why they did that, it made it simpler to
17 look to the insolvency of the corporation rather than up
18 to 75 shareholders. They may well have recognized that in
19 any situation, certainly not all, if the S corporation is
20 in trouble, the shareholder is in trouble as well.

21 QUESTION: But it wasn't that way up until --
22 and yet, in 1982 -- well, let me put it this way: Do you
23 recognize that if the 1982 law was still in place, the
24 government should win?

25 MR. HALLETT: Well, it would depend on whether

1 or not my clients the shareholders were insolvent. If
2 they were insolvent then they would be entitled to the
3 result that we are seeking.

4 QUESTION: Yes, but in this case where we have
5 very solvent shareholders and an insolvent Subchapter S
6 corporation.

7 MR. HALLETT: This particular case, if the law
8 would have remained as it was in 1982, then if the
9 shareholder were solvent he would not be able to exclude
10 the amount from gross income.

11 QUESTION: So it was the change in '84?

12 MR. HALLETT: It was a change in 1984.

13 QUESTION: And so we would look to a reason for
14 that change if we are trying to understand, as Justice
15 Kennedy asked, whether there might be something other than
16 the words of the statute going for the position you are
17 taking?

18 MR. HALLETT: That is true. We would look to
19 the change. But I think you would also look to the
20 critical statutes that existed prior to the change in 1984
21 and the statutes which provide for the basis increase, and
22 those are Sections 1366 and 1367.

23 Now when Congress made the change in 1984, they
24 did not change those provisions.

25 QUESTION: Mr. Hallett, is it invariably the

1 case that this comes as a windfall to the solvent
2 shareholder? Would the government never recapture the
3 benefit that the shareholder gets?

4 MR. HALLETT: Well, it's not the case that it's
5 a windfall. It's certainly not the case that it's a
6 windfall.

7 QUESTION: Accept my characterization of it as
8 a windfall. Would any events in the future enable that
9 benefit to the shareholder to be recaptured by the
10 government?

11 MR. HALLETT: Well, certainly if you view a
12 benefit excluding the debt discharge amount from gross
13 income, then if the attribute deduction provisions come
14 into play, you could view that as a recapture of the
15 benefit in the future.

16 QUESTION: Well, suppose the corporation
17 suddenly becomes solvent, its business picks up or in some
18 new sort of business. I assume that at that point the
19 distortion would even out for years, say one, two, three,
20 four and five, because the net operating losses which
21 might otherwise have been deducted against the new income
22 are now diminished by reason of the discharge of
23 indebtedness income.

24 MR. HALLETT: That's correct.

25 QUESTION: So there, to answer Justice Scalia's

1 question, there might be, I think there might be some
2 instances in which this distortion, if we can call it
3 that, or windfall, does even itself out?

4 MR. HALLETT: That's correct. And much as Your
5 Honor stated, the increase in basis by the amount of
6 discharged debt occurs at the time of the insolvency and
7 permits the taking of the losses. And by taking of the
8 losses, the losses of course go away.

9 QUESTION: So it isn't always a windfall or
10 distortion, accepting those characterizations?

11 MR. HALLETT: It's not always a windfall.

12 QUESTION: And I guess this was in Justice
13 Kennedy's question. The events that deny the windfall
14 character will be in subsequent tax years; is that
15 correct?

16 MR. HALLETT: That's correct. That's correct.

17 QUESTION: Going back to your very initial point
18 about Section 108, if Section 108 had read, items of
19 income shall not include , instead of gross income does
20 not include , then the government would be right; is that
21 correct?

22 MR. HALLETT: Well, I don't think so because it
23 -- it would still presuppose that the item is income. In
24 other words --

25 QUESTION: No. I'm saying if it specifically

1 said income from discharge of a debt shall not be treated
2 as an item of income.

3 MR. HALLETT: Yes.

4 QUESTION: Then your whole case would collapse.

5 MR. HALLETT: Yes. If Congress would have said
6 specifically that COD is not income.

7 QUESTION: So it s the difference between
8 excluding from gross income and specifically stating that
9 it's not an item of income, as the case turns out.

10 MR. HALLETT: Exactly. And that's a very
11 important distinction that was drawn when Section 108 was
12 enacted in 1980.

13 I'd also point out, Your Honor, that if the
14 Commissioner were correct, that COD is not income, then
15 Section 108 would never apply to an insolvent debtor. And
16 if we look at Section 108(b), it only comes into play if
17 an amount is excluded under Section 108(a). Now if it's
18 not income and it's therefore, doesn't come within 108(a)
19 because it otherwise wouldn't be income, then the
20 attribute reduction process which the Commissioner places
21 so much weight upon would never occur.

22 QUESTION: So what's supposed to happen? Some
23 disaster must occur in the tax code since the government
24 did at one point push this argument, but it stopped, I
25 want to know what disaster occurs if you just take

1 108(d)(7)(a), in which it says these things will apply at
2 the corporate level. It says it applies at the corporate
3 level, those three sub -- four subsections, (a), (b), (c)
4 and (g); (c) and (g) are just special cases, but (a) and
5 (b) is the main case. It says they apply at the corporate
6 level. What does that mean? It means it doesn't flow
7 through. It's very simple; nothing flows through. The
8 attributes don't flow through. Nothing flows through.

9 All right. Now once you say that, that cures
10 what seems an anomaly from a point of view of policy. Why
11 don't we interpret it that way?

12 MR. HALLETT: Because the statute doesn't say
13 that.

14 QUESTION: Well, let's see what it says. It
15 says, in the case of an S corporation, subsections (a),
16 (b), (c) and (g) shall be applied at the corporate level.
17 Now why can I not take those words to mean they shall be
18 applied at the corporate level and only the corporate
19 level, i.e., they do not flow through?

20 MR. HALLETT: Because we have to look at what is
21 applied at the corporate level. For example, subsection
22 (a), the exclusion from gross income is applied at the
23 corporate level. And that's logically because the
24 corporation realizes the income and it excludes it.

25 QUESTION: Right.

1 MR. HALLETT: Subsection (b), and this is the
2 critical part of the statute, an essential part of the
3 statute as amended in 1984, is that the insolvency is
4 determined at the corporate level. But those two
5 provisions do not say anything about the basis pass
6 through.

7 QUESTION: I know they say nothing. They say
8 nothing. So what I'm doing is suggesting that because
9 they say nothing one way or the other, one can interpret
10 those words shall be applied at the corporate level to
11 mean everything to do with 108 applies at the corporate
12 level in the case of the Subchapter S corporation, and
13 does not flow through. So what I'm asking you is why can
14 I not do that?

15 MR. HALLETT: Because the statute doesn't say
16 everything occurs at the corporate level. It says the
17 gross income is excluded --

18 QUESTION: I've got that point. Your point is
19 the language.

20 MR. HALLETT: Yes.

21 QUESTION: Is there anything other than the
22 language?

23 MR. HALLETT: The plain language of the
24 statute.

25 QUESTION: Nothing else.

1 MR. HALLETT: And the failure to say anything in
2 either 108 or Sections 1366 and 67 about the general rule
3 of basis -- pass through to basis not occurring.

4 QUESTION: So you're --

5 MR. HALLETT: There's nothing to suggest that.
6 Not a hint.

7 QUESTION: Is it an answer to Justice Breyer,
8 and I may be wrong about this, that if that interpretation
9 prevailed, there would be some instances in which the
10 shareholder was really entitled to a double tax. In other
11 words, if there were basis left and the basis were not
12 decreased as a result of this interpretation, then the
13 shareholder in effect would be paying a double tax in some
14 instances, or am I wrong about that?

15 MR. HALLETT: Well, I'm not sure it would result
16 in a double tax. I think it clearly would read into the
17 Code language that's simply not there.

18 QUESTION: Well, that the shareholder would be
19 taxed in effect for discharge of indebtedness income even
20 though the corporation was insolvent.

21 MR. HALLETT: That's true.

22 QUESTION: Because the basis would not be
23 reduced.

24 MR. HALLETT: That's true. That's true.

25 QUESTION: Mr. Hallett, may I go back to an

1 earlier colloquy, and that is, as I understand it in this
2 case, the tax attributes, at least under your theory, they
3 wouldn't -- that would be an academic question because the
4 losses here were entirely wiped out against the increased
5 basis. Isn't that right? There were no losses left.

6 MR. HALLETT: True. Once we go through the
7 process of determining how much the losses exceeded basis
8 for the taxable year, as the statute tells us to do, if
9 the losses are completely absorbed by the COD, if they are
10 completely absorbed because of the increase in basis, then
11 assuming there's no other attribute, assuming there's no
12 basis in assets that can be reduced, that would be true.

13 QUESTION: I take that to be the case here, that
14 the losses were totally absorbed.

15 MR. HALLETT: No. Actually, and I have to point
16 out, this is not in the record, Your Honor, the losses
17 were totally absorbed but there was some \$800 thousand
18 basis in assets and properly applied, even though the
19 losses were absorbed, the COD income is still there and
20 the COD income would be applied in the next taxable year
21 to reduce the basis in the assets.

22 QUESTION: But that's not -- we don't have the
23 next tax return before us, so we don't --

24 MR. HALLETT: No, no, that's true. That's
25 correct. And I would just point out, it's a very

1 important concept of Section 108 that, I think it's -- you
2 read the legislative history and it does admittedly talk
3 about a purpose is to pick up the income in the future
4 through the attribute reduction, but Congress allowed a
5 very very important exception to that. And that's the
6 full ability to use net operating loss carryovers or basis
7 in the case of property sold in the year of discharge.
8 Very very important, such that certainly many taxpayers
9 are going to have excluded COD income but they are not
10 going to have any attributes to be reduced.

11 I don't believe the situation we have here is in
12 any way an anomaly. We have absolute proof of that in one
13 of the cases. The Pugh case, there were no attributes at
14 all. There were no suspended losses, there was no basis
15 in assets to reduce. And the Court of Appeals of course
16 held that the COD passed through.

17 So we know that situation. We know that
18 situation exists.

19 QUESTION: Why do you say it's no anomaly? I
20 would think with an ordinary corporation the chance of an
21 insolvent corporation ending up with a lot of positive
22 income in the year of insolvency is pretty low. With an
23 individual, the chance of an individual ending up with a
24 lot of positive income in the year of insolvency is pretty
25 low.

1 In the case of an S corporation, the chance that
2 a shareholder of the insolvent S corporation could have a
3 lot of positive income in that year is pretty high. And
4 therefore, if we accept your intention for an S
5 corporation, your interpretation, we reach as a practical
6 matter quite a different result in terms of tax windfalls
7 than you do in the other two instances.

8 MR. HALLETT: Well, I think though in the other
9 two instances, take a corporation that's in trouble and
10 has net operating losses, it could well be the situation
11 that it doesn't have any basis in its assets in excess of
12 the liabilities. It excludes the amount from income and
13 it doesn't have any attributes to reduce. That's what I'm
14 saying; it's not an anomaly to have a situation such as we
15 have in this case that whether it's a corporation, a
16 regular corporation or a partnership, that we don't end up
17 with any attributes to reduce, particularly because they
18 can be used in the taxable year of the discharge.

19 QUESTION: May I ask you a question about --
20 nobody seems to discuss in the briefs about, 108(2)(e),
21 which says, it seems to say in so many words, (e)(1), it
22 says basis reduction, that -- why isn't that relevant,
23 that there's a direct reduction to basis under (e)? You
24 know what I'm talking about? It's on page 36 of the
25 appendix.

1 Reduction -- subsection (b) says reduction of
2 tax attribute and it lists the things that are reduced.

3 MR. HALLETT: Yes.

4 QUESTION: And the last thing listed is the
5 basis of the property of the taxpayer.

6 MR. HALLETT: Yes.

7 QUESTION: Why doesn't that --

8 MR. HALLETT: Well, that could come into play if
9 for example, if the taxpayer here had \$800 thousand of
10 basis in property, not the taxpayer, but if the S
11 corporation had the \$800 thousand basis in property, then
12 that would be reduced. That would be reduced. It would
13 be reduced though specifically, Section 1017 says it would
14 be reduced after the taxable year of the discharge, as of
15 the beginning of that year.

16 I would just call the Court's attention as well
17 to one other section that I think solidifies that income
18 is realized as a result of debt discharge and that's
19 Section 108(e)(1) on page 43. And it specifically says
20 there is no other insolvency exception to the general rule
21 that COD is income to be included in gross income. And
22 that general rule is provided in Section 61(a)(12).

23 And finally on this matter, the Commissioner
24 goes back to 1923 and cites court cases particularly in
25 the depression era, and a Treasury regulation that was

1 promulgated before the substantial 1980 revisions of
2 Section 108. And I would point out that those court cases
3 are flawed reasoning. The notion is that --

4 QUESTION: They are what, Mr. Hallett?

5 MR. HALLETT: They represent flawed reasoning.
6 The rationale in those cases that if a debtor realizes
7 debt discharge, that there is no income if he's insolvent.
8 Of course the Court held in 1931 in Kirby Lumber that as a
9 general proposition there is income. And these cases in
10 the depression era picked up on some language in Kirby
11 Lumber about the forgiveness of the debt frees up
12 assets . And they said well, if you're insolvent, it
13 doesn't add to assets. And so there is no realization of
14 income.

15 That was the rationale of those cases. And I
16 submit that just defies economic reality where a debtor
17 has \$2 million in debt, or \$1 million in debt, or \$100,000
18 in debt, and that is discharged. And if he's a few
19 hundred dollars or a few hundred thousand dollars still
20 insolvent after the discharge, that's a real economic
21 benefit. He can take the amount that otherwise would be
22 paid for principal and interest on that debt and apply it
23 to expenses to keep going. When you recognize that the
24 insolvency is determined based on the fair market value of
25 the assets, it could well have a situation where the real

1 estate operating assets, the value doesn't exceed the
2 debts.

3 But when a million dollars of debt is
4 discharged, that money is indeed freed up. It does
5 indeed free up the liquid assets to either pay down other
6 debts or refinance or pay expenses.

7 If that rationale applied, if that rationale
8 applied, that would mean where a debtor is insolvent and
9 sells an asset for a million dollar gain, that -- but is
10 still insolvent, and say he takes the million dollars and
11 uses it to pay off debt, if that rationale applied, there
12 would be no income in that situation. Because after the
13 transaction, even though he's had gain, he's still
14 insolvent. That's not the tax law.

15 And I submit that that transaction cannot be
16 meaningfully distinguished from the situation where the
17 debt is directly discharged.

18 Let me turn briefly to the specific language of
19 Sections 1366 and 1367. And I think there's a question
20 of where do you start here. Do you start with Section 108
21 or do you start with Sections 1366 and 67? I don't think
22 it makes a difference. Because if you start with Section
23 108, you go to 108(d)(7)(b). And that sends you over to
24 Sections 1366 and Sections 1367. Sends you over to
25 determine the amount of the losses that are disallowed for

1 the taxable year of the discharge before you can determine
2 that there is an attribute.

3 And those, I would just point out that 1366 and
4 67 are very, very broad. This isn't a narrowly drawn
5 statute. It says in 1366 that all items of income,
6 including tax exempt income, are taken into account in
7 determining shareholder basis.

8 Congress described the reason for the basis
9 increase in some of the legislative history as insuring
10 that if an item is nontaxable, then if there's later a
11 distribution, the shareholder doesn't have to recognize
12 income as a result of the -- it preserves its
13 nontaxability. The Commissioner seizes upon this stated
14 purpose of a shareholder basis increase and argues that,
15 well, that means that you only could increase basis for a
16 nontaxable item if you get cash, money in the till that
17 you can distribute in kind.

18 Well, the statutes don't require that there be a
19 distribution in kind. The statutes don't say that you
20 have to lock the cash up in a safe deposit box and use it
21 in the future for a distribution. The fact is if you have
22 municipal bond interest that's collected and used to pay
23 debt you are in the same situation on the bottom line
24 balance sheet situation of the shareholder and the
25 corporation.

1 But the critical event here, and this is -- I'm
2 glad the Commissioner brought up this notion of
3 realization of income, because commentators and some of
4 the courts have said that, well, you shouldn't give the
5 shareholder the losses because he hasn't had an economic
6 loss.

7 Well, the point is, he's had an economic gain.
8 It's the economic gain, the income, that Congress has
9 chosen not to tax, that permits the taking of the losses.

10 I would finally point out under Section 108 that
11 -- excuse me; before I get to that I would point out that
12 what we are asking for is consistent treatment here. An S
13 corporation that gets excludable municipal bond interest
14 is entitled to up the basis and take losses. And we ask
15 for the same thing.

16 The -- all other debtors who exclude COD income
17 get to use their attributes in the year of discharge and
18 we ask for the same thing. And this 108(d)(7)(b) has
19 really been a matter of confusion. It hasn't been read
20 closely. It requires that before you eliminate any losses
21 you have to go over to Sections 1366 and 67 and determine
22 if there is an excess of losses remaining after the COD
23 income is taken into account.

24 I will reserve the remainder of my time for
25 rebuttal.

1 QUESTION: Thank you, Mr. Hallett.

2 Mr. Jones, we'll hear from you.

3 ORAL ARGUMENT OF KENT L. JONES

4 ON BEHALF OF THE RESPONDENT

5 MR. JONES: Mr. Chief Justice, and may it please
6 the Court.

7 Congress did not provide to Subchapter S
8 shareholders the unique double tax benefit that
9 petitioners seek.

10 The simple question presented here is whether
11 the discharge of debt of an insolvent is an item of income
12 or tax exempt income that flows through to shareholders
13 and increases their basis under 1366.

14 The plain text of the directly applicable
15 statutes seems to provide a pretty clear answer to that.

16 QUESTION: Mr. Jones, would you clarify whether
17 you are indeed walking away from the rationale of the
18 Tenth Circuit which was not about the characterization of
19 this as income, but was a timing question, as I understand
20 it.

21 MR. JONES: The timing question, we don't think
22 the timing question ever arises in this case, nor has it
23 ever properly arisen in any of the other cases.

24 QUESTION: But you did argue the theory that the
25 Tenth Circuit accepted; you argued it in the Court of

1 Appeals.

2 MR. JONES: Actually, I believe the Tenth Circuit
3 developed that theory on its own. I believe that in the
4 Tenth Circuit as in the other cases our argument has been
5 twofold: that this item has never been regarded in the 80-
6 year history of the Internal Revenue Code as income for an
7 insolvent taxpayer. Secondly, that 108(d)(7) recognizes
8 and is an emanation of that fact.

9 The Tax Court rationale was that 108(d)(7) says
10 all of this happens at the corporate level. And it isn't
11 income because it's excluded and it's not tax exempt
12 income so nothing passes through.

13 QUESTION: To put Justice Ginsburg's question
14 another way, if you do not prevail on your argument that
15 it's not income, I take it you don't ask us to accept a
16 backup position that reflects the view of the Circuit on
17 timing.

18 MR. JONES: If the Court were to disagree with
19 our basic contentions, then you would be faced with a
20 problem -- then as a Court the problem would be that you
21 have the clear history of the statute that says this is
22 not to be treated as income. It's to be applied against
23 tax attributes and then to be disregarded. So you would
24 have that clear history. You would also have the
25 presumptive rule that tax statutes should not be

1 interpreted to provide a double benefit.

2 QUESTION: No, we don't think it's a problem.
3 Let's assume that we simply reject that argument. I want
4 to know if the backup argument, if you think that as a
5 matter of sound, statutory construction, I think this is
6 what Justice Ginsburg was asking, for us to accept the
7 timing rule adopted by the Circuit.

8 MR. JONES: It is an appropriate resolution of
9 the problem if you reach it, and the reason that is so, is
10 that 1336(d)(2) requires the losses, the suspended losses
11 from the prior year, to be brought into the corporation in
12 the year of the discharge. And then --

13 QUESTION: 1336 or 66?

14 MR. JONES: 1366(d)(2).

15 QUESTION: Now Mr. Jones, we've got some 20 pages
16 in the appendix of statutory sections. When you cite a
17 statutory section, could you refer us to the page of the
18 appendix on which it is?

19 MR. JONES: On Page 53 of the petition appendix.
20 It says, any loss or deduction which is disallowed for a
21 taxable year by reason of the prior paragraph of that same
22 page, shall be treated as incurred by the corporation in
23 the succeeding taxable year.

24 Now this is the point that the Tenth Circuit
25 made, that this provision brings back into the year of the

1 discharge the losses from the prior year, the suspended
2 losses from the prior year. And then --

3 QUESTION: But Mr. Jones, isn't that antithetical
4 to the -- is it in 1017 the general timing rule that you
5 take this in the next year, not in the year of the --

6 MR. JONES: It is a different treatment of
7 suspended losses. It is expressly a different treatment
8 of suspended losses and how they are handled on the
9 Subchapter S return. These are rules peculiar to
10 Subchapter S's. Yes. The answer to your question is yes.
11 It is a different treatment for suspended losses. It
12 brings them into the year of the discharge. And then
13 under 108 we know that the tax attribute reduction is to
14 apply at the corporate level.

15 QUESTION: If you think that the timing rule is
16 changed here, it's surprising that you didn't make any
17 suggestion of that in your brief.

18 MR. JONES: Well, I think that it's -- I wouldn't
19 call it a fall-back argument but I would call it not a
20 correct way to analyze the basic problem that we have in
21 this case, which is that the courts have glossed over the
22 question of whether this has ever been regarded as an item
23 of income, and in particular whether Congress intended it
24 to be treated as such, when the history of the statute
25 says as clearly as it could that Congress accepted the 80

1 year old position of the Treasury and the judicial
2 insolvency exception, did not regard this as an item of
3 income, said that it was to be applied to reduce tax
4 attributes and then in the words of both the House and
5 Senate reports, has no further tax consequences.

6 QUESTION: Let me see if I can get you to focus
7 precisely on the point I'm trying to understand. You have
8 just told us that in the Tenth Circuit brief we will not
9 have found this unusual approach to the timing question.
10 We would not have found that in the government's argument.
11 We certainly don't find it in our brief in this Court.
12 I'm just trying to determine whether the government at
13 least considered it an alternate argument in the lower
14 courts and for some reason abandoned it here.

15 MR. JONES: I think it -- I wouldn't quite put it
16 that way. I think that the right way to put it is the way
17 I have put it, which is that with proper -- we are
18 presenting this case to you with complete integrity. We
19 think this issue need not be reached in this case.

20 QUESTION: Did you present it the same way in the
21 Tenth Circuit?

22 MR. JONES: Actually, I believe in the Tenth
23 Circuit we didn't address the issue. I believe the Tenth
24 Circuit developed its analysis on its own.

25 QUESTION: So if I look at the government's

1 brief, I'll find that corroborated?

2 MR. JONES: I think that's correct.

3 QUESTION: Did you address the issue you are now
4 addressing in the Tenth Circuit?

5 Mr. JONES: I'm sorry, Justice?

6 QUESTION: Did you address the issue you're
7 presenting to us in the Tenth Circuit other than --

8 MR. JONES: Yes.

9 QUESTION: -- in footnote 14 of your brief.

10 MR. JONES: Although in the Tenth Circuit, we
11 were defending the tax court's ruling.

12 QUESTION: Yes, but for whatever reason, this
13 argument that you now say is so obvious on the face of the
14 Code, was this referred to in your argument to the Tenth
15 Circuit other than in a footnote, footnote 14 of your
16 brief?

17 MR. JONES: Well, you are expressing a close
18 familiarity with that and I don't remember footnote 14.

19 QUESTION: I didn't dig this out myself. It was
20 stated in your opponent's presentation. Is it inaccurate?

21 MR. JONES: It is -- I have recently looked at
22 our brief in the Tenth Circuit and my recollection of our
23 brief in the Tenth Circuit was that we made the same point
24 and we made the same argument in the context that the tax
25 court resolved the issue, which is that first they talked

1 about how it's all done at the corporate level. And then
2 having reached that conclusion, emphasized that there is
3 no item of income and no tax exempt income in connection
4 with this item.

5 QUESTION: This does not constitute income. You
6 made that explicit argument?

7 MR. JONES: Yes. In fact, we noted that the
8 Treasury regulations have provided this for 70 years, long
9 before 61 was enacted, long before 108, and that the
10 courts had adopted the judicial insolvency exception, had
11 agreed with the Commissioner that no income arises from
12 the discharge of the debt of the insolvent.

13 QUESTION: Are there past cases in which the IRS
14 has argued that something is not income, or is this a
15 first?

16 MR. JONES: Well, it's an uncomfortable position
17 for us. I mean, I would love to be able to resolve this
18 case properly without addressing that subject. But we
19 can't because Congress made that the fulcrum of its
20 legislative determination.

21 QUESTION: You know, it seems a little
22 contradictory to say that under Section 108, the taxpayers
23 here have to pay some sort of tax whether you call it a
24 deferred tax or just a price on something that you say
25 isn't income of any type. It just seems contradictory.

1 And I'm concerned, if we say it's not income, that there
2 may be other items that are currently considered to fall
3 within section 61 as income that all of a sudden we find
4 aren't. And I don't know how far that would take us if we
5 --

6 MR. JONES: I don't know of any other. And of
7 course I don't know if that provides you with any comfort,
8 but let me answer the first part of the question you
9 raised which is, are there other situations where
10 something that does not constitute income has an effect on
11 basis, or doesn't. The closest example, and I don't
12 believe it's quoted in the appendix, is 1368(b). And
13 1368(b) is a provision that says that if a Subchapter S
14 corporation has no earnings and profits and makes a
15 distribution to its shareholder, that won't be treated as
16 income and under 1367 it will reduce their basis.

17 Well, this is a similar determination. If
18 something has happened here that puts the shareholders in
19 a position whether they might --

20 QUESTION: Excuse me. That means it won't be
21 treated as income to the shareholder.

22 MR. JONES: Yes.

23 QUESTION: You are not talking about whether in
24 the abstract it's an item of income. They have to say
25 that it's not treated as an item of income because

1 otherwise it normally would be.

2 MR. JONES: Well, actually, if you look at the
3 close words of the statute, it doesn't say that. Section
4 61 begins with the phrase "except as otherwise provided,
5 discharge of a debt is not an item of income". And that
6 recognizes the historical distinction that Justice -- that
7 this Court had talked about in Commissioner versus Tufts,
8 in Justice Blackmun's opinion that the whole theory of the
9 discharge of indebtedness doctrine is that the discharge
10 frees up the assets of the debtors and he could use them
11 to --

12 QUESTION: May we go back to the formulation that
13 gross income does not include? Well, that same formulation
14 is also used for tax exempt bond interest.

15 MR. JONES: Yes.

16 QUESTION: For life insurance proceeds, and even
17 though it says the same exact words, does not -- gross
18 income does not include, we know that those do up the
19 basis.

20 MR. JONES: Not as an item of income though.
21 They come in as tax exempt income. 1366 raises the basis
22 for items of income including tax exempt income. Tax
23 exempt income is something that really is income, and it's
24 an accretion to wealth. The only example that --

25 QUESTION: But the words of the statute are the

1 same. Gross income does not include.

2 MR. JONES: Right. But tax exempt income is real
3 income. It's something that you receive. It's an asset.
4 It is an accretion to wealth within the concept of --

5 QUESTION: And forgiveness of indebtedness --

6 MR. JONES: Is not. Forgiveness of indebtedness
7 for an insolvent, as Justice Blackmun pointed out in
8 footnote 11 of Commissioner versus Tufts, doesn't free up
9 any assets.

10 QUESTION: But that was addressed by your
11 adversary. He said well, suppose you have a corporation
12 which is insolvent by a million dollars, and part of that
13 is a \$950,000 indebtedness. There's a world of
14 difference. It amazes me that the government says this
15 isn't income.

16 QUESTION: Or to put it more simply, if my bank
17 told me, you know, forget about your mortgage. Boy, I'd
18 feel a lot richer. You are telling me that that is not an
19 accretion of wealth? That's unbelievable.

20 MR. JONES: My responsibility to this Court is to
21 tell you how Congress, what we understand Congress used
22 these terms to mean. Congress could not have been more
23 clear. They adopted a judicial insolvency exception that
24 adopted a longstanding regulatory interpretation. It
25 doesn't matter, this Court doesn't have to resolve the

1 broader question of whether under Commissioner versus
2 Glenshaw Glass this might be thought to be an accretion of
3 wealth. You don't have to resolve this question because
4 what is before the court is how did Congress view that
5 difference.

6 QUESTION: Given that is before the Court, what
7 was your answer to Justice Ginsburg. I was having exactly
8 the same problem. I accept its a loophole, for argument's
9 sake. If it was a terrible loophole, this would not be the
10 first loophole that Congress wrote and it won't be the
11 last. And maybe it would be the last, marvelous. There
12 are 31 separate -- 29 separate subsections of this statute
13 that use the words "gross income does not include". And I
14 take it in respect to every one of those but one, you will
15 say they are items of income. And obviously one thing I
16 would be reluctant to do is to take those same words
17 "gross income does not include", and say that those are
18 items of income in every instance but this one.

19 Or in every instance but three. Or create a new
20 spider web of rules as to when the words "gross income
21 does not include" does mean it is none the less items of
22 income but doesn't in other. That's the problem I'm
23 facing. And to say "it's Congress's clear intent" doesn't
24 help me solve that problem.

25 MR. JONES: But it should help you resolve that

1 problem because what's at issue was what was Congress's
2 intent when it used the phrase "items of income."

3 QUESTION: And are you saying it's always the
4 same, those words "gross income does not include" in those
5 29 subsections whatever they are referring to is never an
6 item of income or do you mean sometimes is and sometimes
7 isn't?

8 MR. JONES: I think I'm focused on your problem.
9 I think the answer to your question is probably that in
10 all of those instances it wouldn't be an item of income.

11 QUESTION: Never? What for example about a
12 lessor's income? There's a reference here to a payment by
13 a lessor of a certain kind of rent which I thought surely
14 would increase basis.

15 MR. JONES: It wouldn't be income received in the
16 year. And what happens is you are supposed to reduce the
17 basis and recognize as this Court said in Centennial Bank,
18 recognize that deferred income in future years. And as
19 that's recognized then it becomes an item of income in
20 that sense. But in the first year it's not treated as an
21 item of income for this purpose.

22 QUESTION: Then it's income when it hurts the
23 taxpayer in later years?

24 MR. JONES: It's income -- if it's income then
25 it increases the basis. And if its not income, it

1 doesn't. And if its not income and doesn't increase the
2 basis then it's -- then any income effect would be
3 recognized in subsequent periods.

4 QUESTION: Could you answer one other question
5 which is, -- but it's going to sound as if it's on your
6 side so be tempted to agree but don't agree because you
7 haven't pushed this argument and I want to know why.

8 It seemed to me that the strongest point was the
9 words keeping it at the corporate level. Because if you
10 kept it at the corporate level no problem I can think of
11 would be caused and it eliminate the loophole and seems
12 consistent with the language, but you have not pushed that
13 argument. And therefore there must be some disaster in tax
14 law lurking.

15 MR. JONES: We do. We put it as our second point.
16 We don't abandon that argument. It's definitely addressed
17 in our brief. Its sort of an intellectual fussiness that
18 causes us to address the income issue first and then the
19 shareholder issue, I mean the corporate level issue. And
20 that is because (d)(7) wasn't enacted, as Justice Ginsburg
21 pointed out until 1984. But in 1980 Congress already went
22 ahead and said this is not to be treated as an item of
23 income; it's to be used to reduce attributes and it is to
24 have no further tax consequences. So we shouldn't have to
25 look to 1984 legislation in (d)(7) to answer this

1 question. Now (d)(7) is consistent with our answer and
2 therefore and it is a sufficient answer. But it seems to
3 me to be perfectly faithful to what Congress said they did
4 and to what the text of the these statutes permit us to
5 understand. We don't have to go to 84. We can go right
6 to where Congress said. And I want to point out in this
7 respect that it is solely on the 1980 legislation that
8 professors Victor and Lokin reviewed the history, reviewed
9 the provisions and agreed with us that the discharge of
10 indebtedness of an insolvent party does not represent an
11 item of income and is to be ignored after it's applied
12 against the tax attributes. Now what Petitioners' is:
13 let's not ignore it, let's get a tax benefit from it.
14 We'll pass it through as if it were income. We will get a
15 basis adjustment that allows us to deduct the standard
16 losses. And what they have done is used 108 to enhance
17 their tax attributes when section 108(b) makes it clear
18 that the whole point of 108(b) is to reduce tax
19 attributes.

20 QUESTION: What do you think Congress did then in
21 '84? I take it that taxpayer is conceding that if the 82
22 law remained in place a Subchapter S shareholder would be
23 just like a partner in partnership and could not get this
24 benefit?

25 MR. JONES: Well that --

1 QUESTION: But there was a change in 108, and it
2 seemed to me that what you were essentially arguing is
3 that we should undo the change that Congress made in 108.
4 And you are telling me, no, the change in 108 didn't do
5 anything? Or what?

6 MR. JONES: It didn't change the basic principles
7 of 108 that the amendment in 1984 simply said that the tax
8 attribute reduction would be applied at the corporate
9 level for Subchapter S corporations. This is in
10 108(d)(7)(a).

11 QUESTION: If they applied at the shareholder
12 level then you have a solvent shareholder.

13 MR. JONES: If they applied it at the shareholder
14 level for solvent shareholders they would recognize the
15 income and pay it on their own returns. It wouldn't have
16 any consequence.

17 QUESTION: Right. But what was the effect of
18 saying take it at the corporate level so that the
19 insolvent is the corporation?

20 MR. JONES: Congress said that they were doing
21 that because they wanted all shareholders to be treated
22 the same. That was the explanation that Congress gave.

23 QUESTION: Well, didn't somebody point out to
24 Congress or didn't Congress know that a Subchapter S
25 corporation is quite different from a Subchapter C

1 corporation?

2 MR. JONES: Well, this is a special rule actually
3 that applies only for Subchapter S's.

4 QUESTION: But you just me the rationale was that
5 all corporations should be treated alike.

6 MR. JONES: All shareholders of this Subchapter S
7 corporation should be treated the same. In other words
8 they didn't want to -- Congress said they didn't want to
9 have shareholder one to be treated differently from
10 shareholder two although as you are aware for partnerships
11 that kind of different treatment can result. But Congress
12 didn't think this had anything to do with - that the
13 change in 108(d)(7) had anything to do with the issue here
14 because they had already resolved the issue in 1980 when
15 they explained how these statutes were to work.

16 And I want to point out that in 1993 when
17 Congress amended Section 108 to extend its application to
18 qualified real property indebtedness, Congress went
19 through the operation of these same provisions and said
20 the same thing.

21 QUESTION: But Congress was explicit there in a
22 way it isn't here.

23 MR. JONES: I don't know how Congress could have
24 been more explicit in--

25 QUESTION: Didn't Congress say that there won't

1 be any increase in basis?

2 MR. JONES: That's true.

3 QUESTION: and here we don't have anything that
4 says it won't be an increase in basis.

5 MR. JONES: We have awfully good indication of
6 that. We have Congress saying it's not income. It's only
7 to be used to reduce tax attributes. It has no other tax
8 consequences.

9 QUESTION: But you will concede that to say basis
10 will not be increased is something a lot clearer than what
11 you are presenting to us?

12 MR. JONES: Yes, it's perfectly clear. But to me
13 it's -

14 QUESTION: So why didn't they make that same
15 statement with respect to this, knowing that the courts
16 were all over the lot?

17 MR. JONES: In 1980 the courts were not all over
18 the lot. In 1980 no court had ever suggested that the
19 discharge of the debt of an insolvent was income.

20 QUESTION: What was the year of the real estate
21 provision?

22 MR. JONES: 93.

23 QUESTION: 93.

24 MR. JONES: Yes.

25 QUESTION: So I am asking about when they made

1 that change in 93 and they said basis will not be
2 increased. Why didn't they just say, well, let's do the
3 same thing for subchapter S corporations?

4 MR. JONES: I am sorry. They were talking about
5 Subchapter S corporations in 1993. They were talking
6 about exactly the issue we have in this case.

7 QUESTION: But I'm just simply asking you why
8 didn't they make that same change to say explicitly basis
9 will not be increased, since that would have cured --

10 MR. JONES: The statute wasn't amended in any of
11 its substantive characters in 93. They just added another
12 provision to the same statute

13 QUESTION: Yes, but couldn't they have said "now
14 we are adding this provision. And we are making this
15 thing explicit. To make the statute compatible we ought
16 to make that same provision elsewhere."

17 MR. JONES: They were talking about, -- When they
18 said basis is not adjusted, they were talking about the
19 Subchapter S corporation provisions involved in this case.
20 So they were talking about previously enacted provisions
21 of Section 108 in describing how they applied.

22 QUESTION: There are certain words that are used.

23 MR. JONES: Basis is not increased by --

24 QUESTION: Yes. And why wasn't it made clear
25 then? Basis is not increased, with respect to this

1 subchapter S?

2 MR. JONES: That is exactly what they said at
3 that the time in '93. I'm sorry. We are not
4 communicating.

5 QUESTION: No, we are not. We have a provision
6 that says those words expressly. You are asking them -

7 MR. JONES: It's not a provision. It's just
8 legislative history.

9 QUESTION: I thought it was in the statute
10 itself.

11 MR. JONES: No, I am sorry. Now I understand. It
12 was in the history of --

13 QUESTION: Its not in the statute itself in any
14 case?

15 MR. JONES: It was in the history of the 93
16 amendment that Congress in going through how the statute
17 operates, explained that for subchapter S corporations
18 this is not an item of income; it doesn't adjust basis.
19 That is all I am saying. I am not saying that this is
20 binding history.

21 QUESTION: Is there a provision of the Internal
22 Revenue Code that says basis will not be increased that
23 was a change that was made in the statute, not legislative
24 history?

25 MR. JONES: I am not familiar with that, but it

1 is just the contrary. The statute says only that basis
2 will be adjusted if there's an item of income. An
3 Congress said this isn't an item of income. I know that
4 that's -

5 QUESTION: Perhaps I will look for it. It's that
6 real estate -- I am sure that you must be familiar with it
7 and I thought that in that statute itself those words
8 appeared.

9 MR. JONES: I am not familiar with that.

10 The contention that if it is not an item of
11 income then its tax exempt income is also fundamentally
12 flawed for the same reason. Its not tax exempt income
13 because its not an accretion to wealth. Its not income in
14 the first place.

15 QUESTION: Except that Section 61 of Title 26
16 says that income includes income from discharge of
17 indebtedness. I mean that's a germinal provision.

18 MR. JONES: It says "Except as otherwise provided
19 --"

20 QUESTION: Yes.

21 MR. JONES: Income includes income from discharge
22 --

23 QUESTION: So that is the normal rule.

24 MR. JONES: Well, that's the contingent rule. It
25 says except as otherwise provided, income includes income

1 from discharge. 108 says it does not include income from
2 discharge of an insolvent. And that is the 80 year history
3 of the Internal Revenue Code.

4 QUESTION: And it also says it does not include
5 income from a lot of other things. I mean, as Justice
6 Breyer was pointing out earlier, there are a lot of other
7 things as to which it says the same thing. And all it
8 means is that although gross income would normally mean
9 this, for purposes of subchapter S, it will not mean that.
10 But that does not mean -- it is in the abstract, not
11 income.

12 I thought the argument you are making here

13 MR. JONES: I don't have any objection to what
14 you just said. I think it is perfection correct. I think
15 it's a proper concern. But our point is that what you are
16 supposed to, what we have to resolve here is what did
17 Congress mean when it said items of income in 1366 because
18 that's what flows through. Congress said this is not an
19 item of income. And I say this, I mean the discharge of
20 the debt of an insolvent. My only point about the
21 congruence of 61 and 108 is that they cannot win on those
22 provision because all those provision say is what we say:
23 It's not income.

24 And what the legislative history of the
25 provisions say is exactly - is why we are here today

1 ,which is that Congress has always said this isn't income.
2 Has never permitted it to have any tax consequences other
3 than attribute reduction. And I go back again to Victor
4 and Loken. I mean, they are a pretty objective neutral
5 source on this, and they agree with us, that this is not
6 the way Congress used the term and that after it is used
7 to reduce attributes, it's to be ignored. The reason.

8 QUESTION: Was this some article in a law review
9 you are talking about.

10 MR. JONES: It's actually in their treatise.

11 QUESTION: In a treatise?

12 MR. JONES: Federal Income Taxation. It is a
13 pretty reliable guide.

14 QUESTION: How has the Court of Appeals come out
15 on this issue?

16 MR. JONES: The Court of Appeals have been sort
17 of all over the map. If you are talking about the Court
18 in this case,--

19 JUSTICE: No, I meant just the Court of Appeals.
20 The Court or Appeals ruled for the government on this
21 issue.

22 MR. JONES: Yes.

23 JUSTICE: Have other Court of Appeals ruled
24 against the government on this point?

25 MR. JONES: Yes, The Third Circuit in the Farley

1 case ruled against the United States, saying that the
2 plain language of 108 makes this an item of income. And I
3 don't understand their reasoning because the plain
4 language of 108 says it is not an item of income. And the
5 clear history of the statute says it should never be
6 treated as one. And instead it is to be ignored after you
7 reduce basis. I mean after you reduce the tax attributes.

8 QUESTION: In fact, no Court of Appeals has
9 agreed with the government on this point, has it? Is there
10 any Court of Appeals that has agreed with this argument?

11 MR. JONES: I don't think there is a Court of
12 Appeals that has gone through these arguments that we have
13 made the primary focus of our position in this court.

14 QUESTION: The answer is no.

15 MR. JONES: They haven't addressed them, Justice
16 Scalia.

17 QUESTION: Why didn't the government argue this
18 in the other courts?

19 MR. JONES: Again, I believe what we were doing
20 is that we were defending the rationale of the Tax Court.

21 QUESTION: Which you now disagree with?

22 MR. JONES: As I explained to Justice Breyer, we
23 think that the proper way to reach this, to analyze this
24 is the way Congress did, to start with 108 in 1980. And
25 then to point out that the amendment to (d)(7) in 1984 was

1 consistent with that result and promoted that conclusion.
2 Now, what the Tax Court did was different. They said, as
3 Justice Breyer points out that all of this should be done
4 at the corporate level and nothing escapes to the
5 shareholders because it's all handled at the corporate
6 level. I think that's a correct conclusion.

7 But I think one of the reasons it's a correct
8 conclusion is because there is no item of income that can
9 escape to the shareholders and add to their basis and give
10 them this double tax benefit wind fall. And I do want to
11 point out that in each of these cases when a basis
12 adjustment is allowed there is indeed a windfall there.

13 QUESTION: But that can't be controlling.
14 There's no reason to simply distort the tax code to avoid
15 a wind fall in this particular case.

16 MR. JONES: I don't its controlling but it is a
17 presumption that Congress doesn't intend to do that. And
18 so when you look at these statutes and you have the clear
19 history, and if you have any uncertainty about the
20 application of the plain text of those provisions, that
21 uncertainty should be resolved to avoid creating -- either
22 denying the intention of Congress or creating the windfall
23 benefits.

24 QUESTION: I'm sorry. What's the presumption you
25 refer to.

1 MR. JONES: The presumption is what this Court
2 said in Skelly Oil, that tax statutes should not be
3 interpreted to be provide the practical equivalent of a
4 double deduction, which is exactly what they have sought.

5 QUESTION: Could it not end up being a double tax
6 in the other direction? Let's assume an insolvent chapter
7 S corporation that later recovers. All right. The
8 taxpayer would never have gotten the increase of his basis
9 that arises from this reduction of indebtedness and
10 therefore could not offset against any future gain that he
11 gets from the corporation. Is that fair?

12 MR. JONES: I think that what you are pointing
13 out is exactly the opposite of how Congress looked this
14 situation. What Congress said was they are getting this
15 immediate benefit not having this treated as income in the
16 year that the debt is discharged. And recognize that they
17 might benefit from that in future periods if they have
18 income from other sources, Congress said I want to reduce
19 the tax attributes, the favorable tax attributes, like
20 suspended losses --

21 QUESTION: Than you, Mr. Jones. Mr. Hallett, you
22 have two plus minutes.

23 REBUTTAL ARGUMENT OF DARRELL D. HALLETT

24 ON BEHALF OF THE PETITIONERS

25 MR. HALLETT: With respect to Victor and Eustice

1 Treatise, what it actually says is that COD income of an
2 insolvent debtor is not gross income. And it's cited in
3 the brief. Not one of the authorities cited by the
4 government say that it is not realized. They say it's
5 excluded from gross income. With respect to -- if the
6 Commissioner were right that because an item is excluded
7 from gross income, then none of the items excluded from
8 gross income, life insurance proceeds, interest on
9 municipal bonds, none of those would increase basis
10 because they are not income and could not be an item of
11 income.

12 This double tax benefit. There is no tax benefit
13 at all without a basis increase. The item just as well
14 have been taxable. If it was taxable, the income would
15 flow down to the shareholder. His basis would go up and
16 he'd be able to his loss against the income. He'd end up
17 with zero basis and zero income just the same position
18 where the Commissioner urges he should end up here.

19 Finally the Tenth Circuit did not develop the
20 timing rule on its own. That rule is word for word what
21 was urged upon it by the Justice Department in that case.
22 This case has been a constant moving target. The only
23 time the Commissioner argued the no realization was the
24 first time this case was decided before then Chief Judge
25 Cohen in Tax Court. She rejected it. It was never raised

1 again until it was raised in the petition for certiorari
2 in this brief.

3 I submit, Your Honor, a plea on behalf of tax
4 practitioners in this country. They should be able to read
5 the Code as written. They shouldn't have to speculate as
6 to whether or not a result that is called for on the plain
7 language of the statute is too good to be true or is a
8 wind fall. The tax laws are too complicated to have to
9 get into that kind of speculation.

10 Thank you.

11 QUESTION: Thank you, Mr. Hallett. The case is
12 submitted.

13 (Whereupon, at 10:59 a.m., the case in the
14 above-entitled matter was submitted.)

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