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Taxation - Capital Gains - Immature Fruit as Real Property

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TAXATION—CAPITAL GAINS—IMMATURE FRUIT AS REAL PROPERTY. Plaintiff, a Florida farmer, was engaged in growing and selling mature or ripe citrus fruit; she had owned the citrus grove for over six months. In 1945, the plaintiff sold the grove, with a crop of immature, unsevered fruit, for a lump sum consideration. She reported the sale on her income tax return as a gain from the sale or exchange of a capital asset held for more than six months. Upon reviewing the plaintiff's tax return, the Commissioner allocated $6000.00 of the gain realized to the citrus fruit on the trees, taxable as ordinary income. Plaintiff paid the deficiency, then filed for a refund. Her claim was rejected by the Commissioner. Plaintiff instituted this suit and the court *held* that the entire gain from the sale was a capital gain, not ordinary income, and was to be taxed accordingly, therefor allowed her a refund. *Irrgang v. Fahs*, 94 F.Supp. 206 (S.D. Fla. 1950).

A recent California case,[1] although possessing a similar factual situation, declared the profits attributable to the citrus fruit was to be taxed as ordinary income.

It has often been stated that federal revenue laws are designed to facilitate a national scheme of taxation; their provisions are not to be deemed subject to state laws unless the language or necessary implication of the section involved so requires.[2] It is also well settled that state law determines legal rights and interests and where they have become vested the federal revenue laws designate which interests and rights should be taxed.[3]

Both Florida and California jurisdictions recognize that crops of fruit growing on trees, whether immature or mature, are parts of the realty and, unless reserved, go with the realty in its transfer.[4] The court in the *Watson* case,[5] stated that whether the immature fruit is treated as realty or personalty is of little consequence. The fact remains the fruit was held primarily for sale and should be taxed as ordinary income, as stipulated in a Bureau of Internal Revenue ruling of 1946.[6] The Florida court adopted a more liberal view in favor of the taxpayer which, the court believed was the intent of Congress.[7]

The mere fact that property is realty does not allow it to be taxed as a capital gain, nor does the manner of sale or method of liquidation determine whether the seller is within the provisions of

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1 Earnest A. Watson, 15 T.C. No. 104 (1950).

2 Helvering v. Stuart, 317 U.S. 154 (1942); *cf.*, Morgan v. Commissioner, 309 U.S. 78 (1939).

3 Morgan v. Commissioner, *supra* note 2.

4 *E.g.*, Adams v. Adams, 28 So.2d 254 (1946); Simmons v. Williford, 53 So. 452 (1910); Earnest A. Watson, *supra* note 1. (Tax Court states there is no hard and fast rule under California law, but concedes the question in favor of realty as pertaining to this case).

5 Earnest A. Watson, *supra* note 1.

6 I.T. 3815, 1946-2 *Cum. Bull.* 30. (Ruled the seller of a citrus grove with fruit on the trees must allocate a portion of the selling price to the fruit and the balance to the land. The portion of the price representing the gain from the fruit will be taxed as ordinary income.)

7 H.R. Rep. No. 2333, 77th Cong., 2d Sess. 97 (1942); Sen. Rep. No. 1631, 77th Cong., 2d Sess. 120 (1942); For a discussion favoring the view of the Irrgang case, see Hill, *Ordinary Income or Capital Gain on the Sale of an Orange Grove*, 4 Miami L.Q. 145 (1950).

Section 117 (j)[8] allowing the property to be taxed as a capital gain.[9] The Internal Revenue Code clearly shows that it is either the purpose for which the property is acquired or held or its use that determines whether it will be taxed as a capital gain.[10] The question usually asserted is: "Was the property sold, held by the taxpayer, primarily for sale to customers in the ordinary course of his business?" If this question is answered in the affirmative then it does not qualify to be taxed as a capital gain. The facts considered necessary to create the status of one engaged in a trade or business within the capital gains provisions revolve largely around the frequency or the continuity of the transaction, which it is claimed, results in a business status.[11] Some courts have stated that in the absence of the elements of development and sales activity and the impracticability of disposing of the property in one tract, then the frequency and continuity is in and of itself a narrow definition of a business transaction.[12]

The aforementioned test of frequency and continuity when used to determine the ordinary course of business has been applied in the four following instances. (1) The sale, by a coal mining company, of land possessing "coal in place" was held not to be in the ordinary course of business and was deductible as a capital loss rather than as an ordinary loss because the company was in business to sell mined coal to regular cutomers.[13] (2) The profits resulting from the sale of growing timber by a firm engaged in manufacturing and selling finished lumber also were taxable as a capital gain.[14] (3) Where lumber was sold, for the purpose of liquidating a partnership formerly engaged in the management of family properties and investments, the profits realized were held taxable as "capital gains."[15] (4) A farmer, engaged in producing and marketing dairy products, who sold his non-profit milking cows, was allowed to treat the profits realized as "capital gains".[16]

The *Irrgang* case follows the test of frequency and continuity as the determinant by stating that the taxpayer was in the business of selling ripe oranges, not real estate possessing citrus trees with immature fruit; thus extending the view of *Butler Consolidated Coal Co. v. Commissioner*[17] to apply to the citrus industry. The Watson case[18] justified its *contra* holding by stating: "We are unable to see

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[8] 26 U.S.C.A. §117 (j). In order to tax the profit as a capital gain, the taxpayer must show that the property: (1) was used in his trade or business, (2) was realty or property of a kind subject to an allowance for depreciation, (3) was held for more than six months, (4) not of a kind includible in the inventory of taxpayer at the close of the taxable year, (5) of a kind not held by the taxpayer for sale to customers in the ordinary course of trade or business.

[9] Ehrman v. Commisisoner, 120 F.2d 607 (1941).

[10] See note 8 *supra*.

[11] Commissioner v. Boeing, 106 F.2d 305 (1939); *accord*, Welsh v. Soloman, 99 F.2d 41 (1938); Ehrman v. Commissioner, *supra* note 9.

[12] See Frieda E. J. Farley, 7 T.C. 198, 202, 203, (1946) (sale of residential lots, out of a large tract of land, used by the taxpayer for growing flowers); *accord*, United States v. Robinson, 129 F.2d 297 (1942).

[13] Butler Consolidated Coal Co. v. Commissioner, 6 T.C. 183 (1946).

[14] Camp Manufacturing Co. v. Commissioner, 3 T.C. 467 (1944); *accord*, Carroll v. Commissioner, 70 F.2d 806 (1934).

[15] United States v. Robinson, *supra* note 12.

[16] Albright v. United States, 173 F.2d 339 (1949).

[17] Butler Consolidated Coal Co. v. Commissioner, *supra* note 13.

[18] Earnest A. Watson, *supra* note 1.

how the holding of the oranges primarily for sale to customers is changed to a holding primarily for some other purpose because the grower manages to realize his purpose to sell by making a sale to his liking before the oranges mature, or because as a part of the same transaction the land was also sold."

The problems raised in these cases are not confined solely to the citrus industry, but are of utmost importance to every farmer.[19] Not until the unique problems of the farmer are taken into consideration will uniformity be obtained, and a satisfactory solution to the capital gains provisions be a reality.

William E. Porter

TORTS—PARENT AND CHILD—PARENTS' IMMUNITY FROM LIABILITY TO CHILD FOR TORT COMMITTED BY PARENT. Plaintiff, an illegitimate child, sued her father's estate to recover for shock, mental anguish and permanent nervous and physical injuries resulting from her father's murdering the plaintiff's mother, imprisoning the plaintiff with the corpse, and subsequently committing suicide in her presence. Defendant demurred, relying on the generally recognized exception to tort liability that a parent is immune from liability to an unemancipated minor child.[1] It was *held* that this was not an action by the child against the parent for simple negligence, and since the family relations have been previously undermined, the reason for the parent's immunity does not exist. The child may therefore recover against the estate for malicious and wanton wrongs. *Mahukee* v. *Moore*. 77 A.2d 923 (Md. 1951).

Lacking English precedent, the American rule exempting a parent from tort liability to its minor child dates back to 1891.[2] In the vast majority of cases the immunity privilege will promote discipline and domestic harmony and encourage the most beneficial development of children. However, the reason for the exception no longer exists when the tort destroys the close family relationship intended to be protected. Nevertheless, the rule has generally been followed unwaveringly although the reason for it had entirely failed.[3] The few decisions which refuse to follow the rule do so on the grounds that: (1) allowing suit by the child will, in certain cases, promote and secure family ties rather than jeopardize them,[4] (2) controlling statutes forming public policy overrule any contrary policy[5] or (3) the close family ties meant to be protected have

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[19] Thomas J. McCoy, P-H T.C. 15.106, 15 T.C. 106 (1950). (income realized by a Kansas wheat farmer on the sale of a farm upon which there was a growing crop of wheat, was held to be ordinary income, and not capital gains, to the extent that it represented payment for the growing crop.).

[1] Taubert v. Taubert, 103 Minn. 247, 114 N.W. 763 (1908); Ciani v. Ciani, 127 Misc. Rep. 304, 215 N.Y. Supp. 767 (1926); Smith v. Smith 81 Ind. App. 566, 142 N.E. 128 (1924).

[2] Hewellette v. George, 68 Miss. 703, 9 So. 885 (1891).

[3] Roller v. Roller, 37 Wash. 242, 79 Pac. 788 (1905); Lasecki v. Kabara, 235 Wis. 645, 294 N.W. 33 (1940); Small v. Morrison, 185 N.C. 577, 118 S.E. 12 (1923).

[4] Worrell v. Worrell, 174 Va. 11, 4 S.E.2d 343 (1939); Lusk v. Lusk, 113 W.Va. 17, 166 S.E. 538 (1932).

[5] Minkin v. Minkin, 336 Pa. 49, 7 A.2d 461 (1939); Marchand v. Marchand, 4 D.L.R. 157 (Canada 1924).