

1 Taxes - Claim of Right Doctrine
2 Condition Subsequent

3 In re Lynn A. Apsel

Case No. 695-60419-fra13

4 8/27/96

FRA

Unpublished

5 The debtor sold timber to Rosboro Lumber Co. in 1992 for
6 \$207,000. Payment was made on 6/5/92 in the form of satisfaction by
7 Rosboro of two mortgages against the debtor's real property.
8 Provisions of the sale required the debtor to provide additional
9 timber to Rosboro if there was less than \$207,000 worth of timber in
10 the parcel sold or, in the alternative, a cash payment equalling the
11 difference between the value of timber and \$207,000, with interest.
12 The debtor subsequently denied Rosboro access to her land to harvest
13 the timber and Rosboro filed a lawsuit in Lane County Circuit Court
14 for specific performance. A judgment was entered in favor of
15 Rosboro which allowed the debtor to elect to pay Rosboro \$280,000
16 with interest rather than have the timber harvested. The debtor
17 paid Rosboro \$286,558 pursuant to the judgment on 5/2/94 which
18 extinguished Rosboro's interest in the timber.

19 The IRS filed a claim in debtor's bankruptcy based largely on
20 the debtor's omission of the \$207,000 from gross income on her 1992
21 federal income tax return. Debtor objected to the claim on the
22 grounds that there was never a completed sale - that Rosboro never
23 had more than a contingent right to the timber because the sale was
24 subject to a condition subsequent, namely, the ability of Rosboro to
25 determine the value of the timber which was in the designated parcel
26 sold. Since the debtor never allowed Rosboro to make that
determination, the condition was never fulfilled and Rosboro's
rights were extinguished upon payment of the \$286,558.

27 The court held that under the claim of right doctrine, the
28 receipt of any funds or accessions to wealth is taxable unless
29 exempted by a provision of the tax code, the presence of a
30 condition subsequent notwithstanding. There was a completed sale in
31 1992 and the receipt of \$207,000 is includable in gross taxable
32 income in that year. The debtor's remedy is a possible deduction in
33 1994, the year that the money was paid back to Rosboro.

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UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF OREGON

IN RE)
LYNN A. APSEL,) Case No. 695-60419-fra13
Debtor.) MEMORANDUM OPINION

This matter is before the court on cross-motions for summary judgment. There are no material issues of fact outstanding; therefore the case may be decided on the motions. The Internal Revenue Service ("IRS") has filed a claim in this case based on revenue it asserts was received by the debtor in 1992 for the sale of timber to Rosboro Lumber Co. ("Rosboro"). The debtor disputes that the sale constitutes taxable income in 1992 as no timber was ever harvested and the debtor repaid amounts received from Rosboro in 1994 pursuant to the provisions of a judgment obtained by Rosboro in Lane County Circuit Court. Other matters concerning the debtor's filing status and allowable tax exemptions have been settled by the parties and are therefore not part of this summary judgment

1 proceeding. For the reasons that follow, summary judgment will be
2 granted to the IRS.

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4 I. FACTS

5 1. On June 5, 1992, the debtor received a payment from Rosboro
6 in the amount of \$207,000 in consideration of a timber deed granted
7 to Rosboro on that date.¹ The payment was in the form of
8 satisfaction by Rosboro of two mortgages against the debtor's real
9 property upon which the merchantable timber was located. The
10 \$207,000 was not reported as income on the debtor's 1992 income tax
11 return.

12 2. The debtor subsequently denied Rosboro access to her land
13 and Rosboro was unable to harvest the timber.

14 3. In 1993, Rosboro filed a lawsuit against the debtor in Lane
15 County Circuit Court seeking specific performance of the contract.
16 The judgment granted Rosboro the right to specific performance of
17 the contract, but allowed the debtor until May 2, 1994 to pay
18 Rosboro \$280,000, with post-judgment interest, to extinguish
19 Rosboro's rights in the timber.

20 4. On May 2, 1994, the debtor paid to Rosboro \$286,558 pursuant
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22 ¹The timber deed granted to Rosboro the right to all
23 merchantable timber up to a value of \$207,000 within certain
24 specified boundries of debtor's property as well as the right to
25 enter upon debtor's land to remove the timber until a specified
26 date. It further provided that should the value of timber which was
the subject of the deed be less than \$207,000, the seller [the
debtor] must, upon demand, provide Rosboro with either replacement
timber so as to provide a total value of \$207,000 or, alternatively,
a cash payment equalling the difference between the value of the
timber and \$207,000, with interest.

1 to the judgment. The money was obtained, at least in part, by
2 remortgaging the debtor's real property.

3 5. On February 3, 1995, the debtor filed a bankruptcy petition
4 under Chapter 13 of the Bankruptcy Code.² The IRS filed a claim for
5 taxes, penalty, and interest relating to the year 1992 in the amount
6 of \$76,443 after adjusting for unreported income of \$207,000
7 relating to the timber sale. A claim for tax due of \$1,000 was made
8 for tax year 1994 based on an estimate of tax, due to the debtor's
9 failure to file a tax return for that year. The IRS's claim
10 totalled \$77,443.

11 6. On 10/13/95, the debtor filed an objection to the IRS's
12 claim for tax year 1992 with respect to inclusion of the \$207,000
13 Rosboro payment in income.³

14 II. DISCUSSION

15 The debtor argues that she did not receive \$207,000 in taxable
16 income in 1992 from the Rosboro payment because there was not a
17 completed sale when she signed the timber deed and Rosboro made the
18 \$207,000 payment to satisfy the mortgages against the debtor's
19 property. Instead, the debtor argues that the timber deed granted
20 Rosboro only contingent rights in the debtor's property and those
21 rights were extinguished in 1994 when the debtor paid Rosboro the
22 \$286,558. Because the deed specified that \$207,000 of timber would
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24 ²11 U.S.C. § 101 et seq.

25 ³Objection was later made to the IRS's denial of head-of-
26 household status and to denial of a dependent exemption. Those
matters have since been settled between the parties in the debtor's
favor.

1 be cut, subject to the provisions previously described, it was
2 necessarily subject to a condition subsequent, namely, a
3 determination of the value of the timber to be removed. Since the
4 debtor would not allow Rosboro onto her land to determine the value
5 of or to harvest the timber, the condition was never fulfilled and
6 there was never a completed sale. Rosboro never had, according to
7 debtor's argument, more than a contingent right to the timber and
8 that right was subsequently extinguished.

9 Burden of Proof

10 F.R.B.P. 3001(f) establishes that a proof of claim filed in a
11 timely manner constitutes prima facie evidence of the validity and
12 amount of the claim. There is therefore a presumption in favor of
13 the validity and amount of the claim filed by the IRS which must be
14 overcome by the debtor.

15 Gross Income Defined

16 The Internal Revenue Code defines gross income as "all income
17 from whatever source derived, including (but not limited to) the
18 following items: . . . (3) Gains derived from dealings in property."
19 26 U.S.C. § 61(a)(3). The Internal Revenue Code's definition is
20 given a "sweeping scope" and exclusions from income are to be
21 narrowly construed. Commissioner v. Schleier, 115 S.Ct. 2159, 2163
22 (1995). Unless excluded from income by a specific provision of the
23 Internal Revenue Code, "funds or other accessions to wealth received
24 by a taxpayer are presumed to be gross income and are includable as
25 such in the taxpayer's return." Getty v. Commissioner, 913 F.2d
26 1486, 1490 (9th Cir. 1990).

1 Gain From Timber Sale Reportable in 1992

2 The debtor sold timber to Rosboro in 1992 pursuant to the
3 Timber Deed and received \$207,000 for that timber. The sale was a
4 completed sale: there was an offer, an acceptance, and consideration
5 paid. The fact that the exact amount of timber to be cut had not
6 yet been determined did not render the sale invalid. Both parties
7 to the transaction knew that Rosboro had purchased \$207,000 worth of
8 the debtor's timber, however much that turned out to be. The Lane
9 County Circuit Court determined that the contract was valid and
10 enforceable when it granted judgment to Rosboro for specific
11 performance of that contract.⁴ Even assuming, *arguendo*, that one
12 could characterize as a "condition subsequent" Rosboro's need to
13 enter upon the debtor's land to determine the exact quantity of
14 timber to be cut, that in itself would not render untaxable the
15 receipt of funds in 1992. See, Consolidated-Hammer Dry Plate & Film
16 Co. v. Commissioner, 21 T.C.M. 528 (1962) ("In instances where the
17 happening of a condition subsequent has been required to compel
18 return of payments received, the receipt was held to have given rise
19 to taxable income"). This is consistent with the claim of right
20 doctrine which

21 is firmly established in our tax law. If a taxpayer
22 receives earnings under a claim of right, without
23 restriction as to its use, it is taxable income in the
24 taxable year when he receives the earnings. The principal
25 applies even though in a later year he may be required to
26 refund all or part of the money. It applies whether
returns are on the cash or accrual basis. Any amount

⁴The fact that the debtor was given the option of paying damages for breach of her obligations under the timber deed does not affect the status of the completed sale in 1992.

1 repaid is deductible in the year of repayment (on the cash
2 basis) or the year in which the liability to repay becomes
fixed (on the accrual basis).

3 Whitaker v. Commissioner, 259 F.2d 379 (5th Cir. 1958).

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5 The debtor received \$207,000 in 1992 for the sale of timber on
6 her land. Under the claim of right doctrine, that \$207,000 is
7 includable in gross income in 1992 even though the debtor was
8 subsequently given the option to, and in fact did, repay the money
9 in 1994. The debtor has provided no reference to any provision of
10 the Tax Code which would except this receipt from the "sweeping
11 scope" of 26 U.S.C. 61(a).

12 III. CONCLUSION

13 For the reasons given, the debtor must report the \$207,000
14 received from Rosboro as gross income on her 1992 federal income tax
15 return.⁵ The claim as it relates to 1992 should be amended by the
16 IRS consistent with this opinion and taking into account the
17 settlement reached between the parties with regard to filing status
18 and exemptions claimed. The debtor will be given 30 days from the
19 date of this opinion to file her 1994 federal income tax return.
20 The IRS's motion for summary judgment is granted and the debtor's
21 motion is denied.

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24 FRANK R. ALLEY, III
Bankruptcy Judge

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⁵This court makes no determination as to basis, if any, that
debtor may have in the timber which was the subject of the timber
deed.