

## CASE NOTES

### INTERNAL REVENUE—A Taxpayer's Motivation in Purchasing an Asset Is Irrelevant to the Question Whether It Falls Within the Broad Definition of "Capital Asset" in Internal Revenue Code Section 1221—*Arkansas Best Corp. v. Commissioner*, 108 S. Ct. 971 (1988).

Arkansas Best Corporation (hereinafter Arkansas Best) is a diversified holding company.<sup>1</sup> In 1968 it acquired approximately 65% of the shares of the National Bank of Commerce (hereinafter Bank) of Dallas, Texas.<sup>2</sup> Between 1969 and 1974 Arkansas Best purchased additional shares of the Bank's stock so that by the end of 1974, Arkansas Best had more than tripled the number of shares it owned in the bank.<sup>3</sup> Arkansas Best's percentage interest in the Bank remained relatively stable, however, because these additional purchases were prompted principally by the Bank's need for added capital.<sup>4</sup> From 1968 to 1972 the Bank appeared to be successful and added capital was necessary to accommodate the Bank's growth.<sup>5</sup> However, a severe decline in the Dallas real estate market precipitated a similar decline in the financial health of the Bank since the Bank had a heavy concentration of loans in the local real estate industry.<sup>6</sup> In 1972 federal bank examiners classified the Bank as a problem bank.<sup>7</sup> After 1972 Arkansas Best's infusion

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1. *Arkansas Best Corp. v. Commissioner*, 108 S. Ct. 971, 973 (1988). A holding company is a company whose only assets are the stock and securities of other corporations. BLACK'S LAW DICTIONARY 658 (5th ed. 1979). In this case the petitioner was the nucleus of a diversified conglomerate having subsidiaries engaged in the businesses of transportation, consumer goods, and financial services. *Arkansas Best Corp. v. Commissioner*, 83 T.C. 640, 650 (1984).

2. *Arkansas Best Corp. v. Commissioner*, 108 S. Ct. at 973.

3. *Id.*

4. *Id.* The petitioner acquired 585,795 additional shares by means of various purchases, stock dividends, conversions, and responses to capital calls. *Arkansas Best Corp. v. Commissioner*, 83 T.C. at 646. When added capital was required, shares were offered to existing shareholders on a pro rata basis through the issuance of preemptive rights. Brief for Respondent at n.1. *Arkansas Best v. Commissioner*, 108 S. Ct. 971 (1988). The stock dividends served the purpose of increasing capital by capitalizing earnings. *Id.*

5. *Arkansas Best Corp. v. Commissioner*, 108 S. Ct. at 973.

6. *Id.*

7. *Id.* Weak loans in a bank's portfolio are denoted by four classifications assigned by the

of capital was in response to the Bank's loan-portfolio problem.<sup>8</sup>

On June 30, 1975, Arkansas Best sold the majority of its Bank shares, leaving it with only a 14.7% share in the Bank.<sup>9</sup> On its federal income tax return for 1975, Arkansas Best claimed a deduction for an ordinary loss of \$9,995,688 resulting from the sale of Bank shares.<sup>10</sup> The Commissioner of Internal Revenue disallowed this deduction, finding that the loss from the sale of the stock was a capital loss rather than an ordinary loss.<sup>11</sup> Since it was a capital loss, the loss was subject to the capital loss limitations of Internal Revenue Code (hereinafter I.R.C.) section 1211(a) which states, in part, that "[i]n the case of a corporation, losses from sales or exchanges of capital assets shall be allowed only to the extent of gains from such sales or exchanges."<sup>12</sup>

Arkansas Best sought a redetermination of the Commissioner's characterization of the loss in the tax court.<sup>13</sup> The tax court agreed that the Bank shares acquired by Arkansas Best before the end of 1972 were capital assets which gave rise to a capital loss upon disposition.<sup>14</sup> Relying on cases interpreting the Supreme Court's decision in *Corn Products Refining Co. v. Commissioner*,<sup>15</sup> the tax court held that stock purchased with a substantial investment purpose is a capital asset which, when sold, gives rise to a capital gain or loss.<sup>16</sup> The tax court also held that stock purchased and held for a business purpose without any substantial investment motive is an ordinary asset whose sale gives rise to ordinary gains and losses.<sup>17</sup> The tax court characterized the acquisitions made through 1972 as capital assets because they occurred during the Bank's growth phase, were motivated primarily by in-

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examiners. *Arkansas Best Corp. v. Commissioner*, 83 T.C. at 647. In order of increasing gravity, the classifications are: (1) loans especially mentioned; (2) substandard loans; (3) doubtful loans; and (4) loss loans. *Id.* When a bank has more than fifty percent of its loan portfolio classified as weak loans, the bank is considered a "problem bank". *Id.*

8. *Arkansas Best Corp. v. Commissioner*, 108 S. Ct. at 973. The petitioner participated in these capital calls for various reasons. *Arkansas Best Corp. v. Commissioner*, 83 T.C. at 648. First, participation of the controlling shareholder was essential to save the Bank and thus Arkansas Best was compelled to participate if it wished to preserve its equity in the Bank. *Id.* Second, failure to participate with the resultant demise of the Bank exposed Arkansas Best to potential liability in any suit on behalf of the minority shareholders. *Id.* Third, permitting the Bank to fail would reflect adversely on Arkansas Best so that its sources of financing might be jeopardized and its reputation for skilled management might be tarnished. *Id.*

9. *Arkansas Best Corp. v. Commissioner*, 108 S. Ct. at 973.

10. *Id.*

11. *Id.*

12. I.R.C. § 1211(a) (Supp. IV 1986).

13. *Arkansas Best Corp. v. Commissioner*, 108 S. Ct. at 973.

14. *Id.* (citing *Arkansas Best v. Commissioner*, 83 T.C. at 654-55).

15. *Corn Prod. Refining Co. v. Commissioner*, 350 U.S. 46 (1955).

16. *Arkansas Best Corp. v. Commissioner*, 108 S. Ct. at 973 (citing *Arkansas Best Corp. v. Commissioner*, 83 T.C. at 653-54).

17. *Id.* (citing *Arkansas Best Corp. v. Commissioner*, 83 T.C. at 653-54).

vestment purposes, and were only incidental to any business purpose.<sup>18</sup> However, the Tax Court determined that the share acquisition made after 1972 occurred during the Bank's problem phase.<sup>19</sup> These later acquisitions, with minor exceptions, were made and held exclusively for business purposes.<sup>20</sup> They were designed to preserve Arkansas Best's business reputation because absent the added capital, the Bank probably would have failed.<sup>21</sup> Thus, the loss realized on the sale of the post-1972 shares was held to be an ordinary loss.<sup>22</sup>

On appeal the eighth circuit reversed the tax court's determination that the loss realized on the sale of the post-1972 shares was subject to ordinary loss treatment.<sup>23</sup> The eighth circuit held that all of the bank shares sold in 1975 were subject to capital loss treatment.<sup>24</sup> The appellate court based its decision on the fact that the bank stock clearly fell within the general definition of "capital asset" in I.R.C. section 1221 and that the stock did not fall within any of the specific statutory exceptions to the definition.<sup>25</sup> The court concluded that Arkansas Best's purpose in acquiring and holding the bank stock was irrelevant to the determination whether the stock was a capital asset.<sup>26</sup> The United States Supreme Court granted certiorari<sup>27</sup> and in a unanimous decision *held, affirmed*.<sup>28</sup> A taxpayer's motivation in purchasing an asset is irrelevant to the question whether it falls within the broad definition of "capital asset" in I.R.C. section 1221. *Arkansas Best Corp. v. Commissioner*, 108 S. Ct. 971 (1988).

The statutory section at issue in *Arkansas Best* was I.R.C. section 1221.<sup>29</sup> This section states that the term "capital asset" includes:

[P]roperty held by the taxpayer (whether or not connected with his trade or business), but does not include—  
(1) stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business;  
(2) property, used in his trade or business, of a character which is subject to the allowance for depreciation provided in section 167, or real prop-

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18. *Id.* (citing *Arkansas Best Corp. v. Commissioner*, 83 T.C. at 654).
19. *Id.* (citing *Arkansas Best Corp. v. Commissioner*, 83 T.C. at 654).
20. *Id.* (citing *Arkansas Best Corp. v. Commissioner*, 83 T.C. at 656).
21. *Id.* (citing *Arkansas Best Corp. v. Commissioner*, 83 T.C. at 656-57).
22. *Id.* (citing *Arkansas Best Corp. v. Commissioner*, 83 T.C. at 657).
23. *Id.* (citing *Arkansas Best Corp. v. Commissioner*, 800 F.2d 215, 216 (8th Cir. 1986)).
24. *Id.* (citing *Arkansas Best Corp. v. Commissioner*, 800 F.2d at 218).
25. *Id.* (citing *Arkansas Best Corp. v. Commissioner*, 800 F.2d at 218).
26. *Id.* at 973-74 (citing *Arkansas Best Corp. v. Commissioner*, 800 F.2d at 221).
27. *Arkansas Best Corp. v. Commissioner*, 107 S. Ct. 1564 (1984).
28. *Arkansas Best Corp. v. Commissioner*, 108 S. Ct. 971, 974 (1988).
29. *Id.*

erty used in his trade or business;

(3) a copyright, a literary, musical, or artistic composition, a letter or memorandum, or similar property . . .;

(4) accounts or notes receivable acquired in the ordinary course of trade or business . . .;

(5) a publication of the United States Government . . . .<sup>30</sup>

The petitioner argued that the bank shares acquired after 1972 were not capital assets within the definition of I.R.C. section 1221 because they were acquired for a business motive.<sup>31</sup> The thrust of the petitioner's arguments in support of this contention focused on the Supreme Court's 1955 decision in *Corn Products Refining Co. v. Commissioner*,<sup>32</sup> and on the application of what has become known as the *Corn Products* doctrine. Under this doctrine a taxpayer's motivation in purchasing an asset, whether for business purposes or for investment purposes, was deemed relevant to the question whether the asset was defined as a capital asset.<sup>33</sup>

In *Corn Products* the Supreme Court considered whether income arising from a taxpayer's dealings in corn futures was entitled to capital gains treatment.<sup>34</sup> The taxpayer was a nationally known manufacturer of products made from grain corn.<sup>35</sup> After corn prices increased drastically due to the droughts of the 1930s, the company began a program of buying corn futures to ensure itself of an adequate supply of corn and to protect itself against price increases.<sup>36</sup> The company took delivery on the futures contracts it found necessary to meet its manufacturing needs.<sup>37</sup> If no corn shortage was imminent, however, the company sold any remaining contracts in early summer.<sup>38</sup> The company claimed that these hedging activities did not fall into any of the exclusions of I.R.C. section 1221 and that they therefore fell into the general definition of "capital asset."<sup>39</sup> The company asserted that the sale of corn futures resulted in capital gains and losses.<sup>40</sup>

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30. I.R.C. § 1221 (Supp. IV 1986).

31. *Arkansas Best Corp. v. Commissioner*, 108 S. Ct. at 974.

32. *Corn Prods. Ref. Co. v. Commissioner*, 350 U.S. 46 (1955).

33. See, e.g., *Campbell Taggart, Inc. v. United States*, 744 F.2d 442, 456-58 (5th Cir. 1984); *Steadman v. Commissioner*, 424 F.2d 1, 5 (6th Cir.), cert. denied, 400 U.S. 869 (1970); *W. W. Windle Co. v. Commissioner*, 65 T.C. 694, 707-13 (1976); *Booth Newspapers, Inc. v. United States*, 157 Ct. Cl. 886, 893-96 (1962).

34. *Arkansas Best Corp. v. Commissioner*, 108 S. Ct. at 975 (citing *Corn Prod. Refining Co. v. Commissioner*, 350 U.S. at 47).

35. *Id.* (citing *Corn Prods. Ref. Co. v. Commissioner*, 350 U.S. at 48).

36. *Id.* (citing *Corn Prods. Ref. Co. v. Commissioner*, 350 U.S. at 48). A commodity future is a contract to purchase some fixed amount of a commodity at a future date for a fixed price. *BLACK'S LAW DICTIONARY* 609 (5th ed. 1979).

37. *Id.* (citing *Corn Prods. Ref. Co. v. Commissioner*, 350 U.S. at 48).

38. *Id.* (citing *Corn Prods. Ref. Co. v. Commissioner*, 350 U.S. at 48).

39. *Id.* at 976 (citing *Corn Prods. Ref. Co. v. Commissioner*, 350 U.S. at 49). The capital-asset provision then in effect was section 117 of the Internal Revenue Code of 1939.

40. *Id.* (citing *Corn Prods. Ref. Co. v. Commissioner*, 350 U.S. at 49).

The Supreme Court agreed that the corn futures did not come within the literal language of the I.R.C. section 1221 exclusions.<sup>41</sup> The futures were not stock in trade, actual inventory, property held for sale to customers, or depreciable property used in a trade or business.<sup>42</sup> The Court stated, however, that the capital asset provisions of I.R.C. section 1221 should not be so broadly construed as to defeat rather than further the purpose of Congress, and that Congress intended that profits and losses arising from the everyday operation of a business should be considered ordinary income or loss rather than capital gain or loss.<sup>43</sup> The Court proffered the often quoted rule of construction that the definition of "capital asset" must be narrowly applied and its exclusions interpreted broadly.<sup>44</sup> Applying this rule of construction, the Court concluded that the corn futures were subject to ordinary asset treatment.<sup>45</sup> In so holding, however, the Court failed to state explicitly whether the decision was based on a narrow reading of the phrase "property held by the taxpayer" or on a broad reading of the inventory exclusion of I.R.C. section 1221.<sup>46</sup>

Arkansas Best acknowledged that the bank stock fell within the literal definition of "capital asset" in I.R.C. section 1221 and was outside the five statutory exclusions.<sup>47</sup> The petitioner argued, however, that in *Corn Products* the Supreme Court rejected a literal reading of I.R.C. section 1221 in favor of a standard intended to distinguish between assets acquired and held in connection with the taxpayer's usual trade or business and those acquired principally for investment.<sup>48</sup> In essence the petitioner argued that an evaluation of the taxpayer's motives and business circumstances was essential under *Corn Products* and that an asset could not be classified as capital without regard to the factual circumstances of the particular case under consideration.<sup>49</sup> The Supreme Court, however, rejected this motive test because it was not mentioned anywhere in the language of I.R.C. section 1221 or in its legislative history, and because it was in direct conflict with the parenthetical phrase in I.R.C. section 1221 which defines a capital asset as "property held by the taxpayer (whether or not connected with his trade or business)."<sup>50</sup> According to the Court, the broad definition of the term "capital asset," by its words, explicitly rendered irrelevant any consideration

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41. *Id.* (citing *Corn Prods. Ref. Co. v. Commissioner*, 350 U.S. at 51).

42. *Id.* (citing *Corn Prods. Ref. Co. v. Commissioner*, 350 U.S. at 51-52). See *supra* note 30 and accompanying text.

43. *Id.* (citing *Corn Prods. Ref. Co. v. Commissioner*, 350 U.S. at 52).

44. *Id.* (citing *Corn Prods. Ref. Co. v. Commissioner*, 350 U.S. at 52).

45. *Id.* (citing *Corn Prods. Ref. Co. v. Commissioner*, 350 U.S. at 52-53).

46. *Id.*

47. *Id.* at 974.

48. *Id.*

49. *Id.*

50. *Id.*

of whether the property was connected with the taxpayer's business.<sup>51</sup> Application of the petitioner's motive test would be erroneous because it would make motive dispositive.<sup>52</sup>

In a second argument the petitioner contended that the five exceptions for certain kinds of property listed in I.R.C. section 1221 were illustrative rather than exhaustive.<sup>53</sup> Since the exceptions were illustrative (according to the petitioner), the courts were free to create additional exclusions in order to effectuate the general purpose of the capital asset provisions.<sup>54</sup> The Supreme Court rejected this second argument, citing the language of the statute.<sup>55</sup> Section 1221 stated that "capital asset" means "property held by the taxpayer . . . but does not include" the five classes of property listed as exceptions to the general definition.<sup>56</sup> The Supreme Court stated that the particular phrasing of the statute signified that the listed exceptions were exclusive.<sup>57</sup> Section 1221 establishes a broad definition of the term capital asset and the phrase "does not include" excludes from that broad definition only those classes of property specifically mentioned.<sup>58</sup> According to the Court, this interpretation was supported by the legislative history of I.R.C. section 1221 and the applicable Treasury regulations.<sup>59</sup> In addition, the Court stated that the petitioner's reading of the statute would render the exceptions "superfluous if assets acquired primarily or exclusively for business purposes were not capital assets."<sup>60</sup> Inventory and real or depreciable property used in the taxpayer's trade or business would satisfy the business motive test, yet these exceptions were specifically created by Congress.<sup>61</sup> The Supreme Court was hesitant to read I.R.C. section 1221 in a manner which would make these statutory exceptions superfluous.<sup>62</sup>

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51. *Id.*

52. *Id.* The Court also expressed concern that the business motive test advocated by the petitioner would be subject to abuse. *Id.* at 977. If capital stock purchased and held for a business purpose is an ordinary asset, while the same stock purchased and held for a mixed motive is a capital asset, a taxpayer could have significant influence over whether the asset would receive capital or ordinary treatment. *Id.* A taxpayer might be able to qualify for ordinary loss treatment by emphasizing some business purpose which lay behind the acquisition of the stock. *Id.*

53. *Id.* at 975.

54. *Id.*

55. *Id.*

56. *Id.*

57. *Id.*

58. *Id.*

59. *Id.* See also H.R. REP. No. 704, 73d Cong., 2d Sess. 31 (1983) ("[T]he definition includes all property, except as specifically excluded"); H.R. REP. No. 1337, 83d Cong., 2d Sess. A273 (1954) ("[A] capital asset is property held by the taxpayer with certain exceptions"); 26 C.F.R. § 1.1221-1(a) (1987) ("The term 'capital asset' includes all classes of property not specifically excluded by section 1221").

60. *Arkansas Best Corp. v. Commissioner*, 108 S. Ct. at 975.

61. *Id.*

62. *Id.*

After dismissing the petitioner's two arguments based upon section 1221, the Court considered the petitioner's argument based upon its interpretation of the *Corn Products* decision.<sup>63</sup> The Court was thus presented with the opportunity to clarify its holding in *Corn Products*.

As indicated earlier, the Court in *Corn Products* did not adequately articulate whether its holding was based on a narrow reading of the phrase "property held by the taxpayer" or on a broad reading of the inventory exclusion in section 1221.<sup>64</sup> The Court in *Arkansas Best*, however, concluded that *Corn Products* was properly interpreted narrowly and involved an application of the section 1221 inventory exception.<sup>65</sup>

Several reasons were advanced to support the Court's determination. The Second Circuit Court of Appeals in *Corn Products* stated that when commodity futures are "utilized solely for the purpose of stabilizing inventory cost [they] cannot reasonably be separated from the inventory terms,"<sup>66</sup> and concluded that "'property used in hedging transactions properly comes within the exclusions of [§ 1221].'"<sup>67</sup> The Court in *Arkansas Best* emphasized that this same conclusion was accepted by the Supreme Court's decision in *Corn Products*.<sup>68</sup> In *Corn Products* the Supreme Court began the central paragraph of its opinion with the statement: "'Nor can we find support for petitioner's contention that hedging is not within the exclusions of [§ 1221] . . . .'"<sup>69</sup> It later stated that the company's futures transactions were "'an integral part of its business designed to protect its manufacturing operations against a price increase in its principal raw material and to assure a ready supply for future manufacturing requirements.'"<sup>70</sup> In a subsequent paragraph the Court in *Corn Products* argued that the Treasury had consistently viewed such hedging transactions as a form of insurance to stabilize the cost of inventory and cited a Treasury ruling which stated that "the value of a manufacturer's raw material inventory should be adjusted to take into account hedging transactions in futures contracts."<sup>71</sup> For the foregoing reasons the Supreme Court in the present case was convinced that, although the corn futures were not actual inventory, their use as an integral part of the taxpayer's inventory-purchase system made them substitutes for corn inventory, so that they came within a broad reading of "property of a kind which would properly be included in the inventory of

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63. *Id.*

64. *Id.* at 976.

65. *Id.* at 977.

66. *Id.* at 976 (quoting *Corn Prods. Ref. Co. v. Commissioner*, 215 F.2d 513, 516 (2d Cir. 1954)).

67. *Id.* (quoting *Corn Prods. Ref. Co. v. Commissioner*, 215 F.2d at 516).

68. *Id.*

69. *Id.* (quoting *Corn Prods. Ref. Co. v. Commissioner*, 350 U.S. at 51).

70. *Id.* (quoting *Corn Prods. Ref. Co. v. Commissioner*, 350 U.S. at 50).

71. *Id.* (quoting *Corn Prods. Ref. Co. v. Commissioner*, 350 U.S. at 52-53 (citing G.C.M. 17322, XV-2 Cum. Bull. 151 (1936))).

the taxpayer" as specified in section 1221.<sup>72</sup>

In *Arkansas Best* the Court did not expressly reject any inquiry into the motivation for the acquisition of a particular asset.<sup>73</sup> The Court did, however, reject the petitioner's argument that, by focusing attention on whether the asset was acquired and sold as an integral part of the taxpayer's everyday business operations, the Court in *Corn Products* generally exempted assets acquired for business purposes from capital asset status.<sup>74</sup> The Court interpreted *Corn Products* "as standing for the narrow proposition that hedging transactions that are an integral part of a business' inventory-purchase system fall within the inventory exclusions of § 1221."<sup>75</sup> Therefore, a business connection, although irrelevant to the initial determination of whether an item is a capital asset, is relevant in determining the application of a statutory exception.<sup>76</sup> In *Corn Products* the close connection between the futures transactions and the taxpayer's business was "crucial to whether the corn futures could be considered surrogates for the stored inventory of raw corn."<sup>77</sup> The Court stated that *Corn Products* was inapplicable in the case at bar because the petitioner never suggested that the bank stock fell within the inventory exclusion of section 1221.<sup>78</sup>

Over thirty years have passed since the Supreme Court's decision in *Corn Products*. During this span the original holding of *Corn Products* has been applied in a multitude of contexts primarily because of the ambiguities surrounding the use of the doctrine. In *Arkansas Best* the Court de-emphasized the business motive and the investment motive tests which sprang from the progeny of *Corn Products*, and instead focused on the narrow holding of *Corn Products*. The Court found that the *Corn Products* doctrine had been expanded beyond the point where it could still be considered statutorily based.

Prior to the Court's decision in *Arkansas Best*, great diversity among the district and circuit courts existed with regard to the proper application of *Corn Products*. The consequences of this diversity were confusion, inequitable results, and an unnecessary burden imposed on the judicial system by the need to establish the proper apportionment of tax liability. The *Arkansas Best* decision obviates the problems which were a result of the misapplication of *Corn Products*, and properly removes the subjective element from

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72. *Id.* at 976-77.

73. *Id.* at 977.

74. *Id.*

75. *Id.* The Court mentioned the fact that Congress has remained silent during the years since the *Corn Products* decision. *Id.* at n.7. No matter how reticent Congress has been, however, the Court felt that it could not ignore the unambiguous language of § 1221. *Id.* The Court indicated that, if a broad exclusion from capital asset status is to be created for assets acquired for business purposes, it must come from congressional action and not congressional silence. *Id.*

76. *Id.*

77. *Id.*

78. *Id.*

the determination of whether an asset is capital or ordinary by limiting this question to the confines of the statute as enacted and intended by Congress.

The *Arkansas Best* decision has general impact in three independent areas.<sup>79</sup> First, the decision has thrown into disarray a body of law which has evolved over more than thirty years.<sup>80</sup> Business, investment, and tax decisions made by corporations and individuals will have to be reexamined for their continued viability.

Second, the decision impacts "all pre-1988 tax years for which returns have not been filed or still remain open for audit."<sup>81</sup> Prior to 1988, capital gains and losses were treated differently than ordinary gains and losses:<sup>82</sup> "pre-1988 long-term capital gains were taxed at lower rates and pre-1988 ordinary losses could be used immediately to reduce taxable income."<sup>83</sup> Taxpayers thus preferred that pre-1988 gains be characterized as capital and pre-1988 losses be characterized as ordinary in order to reduce tax liability.<sup>84</sup> For these years the *Corn Products* case was a boon to both the taxpayer and the IRS since the decision "could be used by taxpayers to convert unfavorably treated capital losses into more desirable ordinary losses, and by the IRS to convert favorably taxed long-term capital gains into ordinary income."<sup>85</sup> The *Arkansas Best* decision can also be considered a boon to both the taxpayer and the IRS for pre-1988 years.<sup>86</sup> The IRS has been given the opportunity to scrutinize all ordinary losses in pre-1988 returns and recharacterize such losses as capital under the *Arkansas Best* interpretation of *Corn Products* in order to restrict deductibility.<sup>87</sup> This same interpretation, however, provides the taxpayer with the opportunity to recharacterize ordinary gains on pre-1988 returns as long-term capital gains in order to take advantage of the favorable tax treatment of such gains in pre-1988 years.<sup>88</sup>

Third, the decision impacts post-1987 tax years.<sup>89</sup> For the years after 1987, the Tax Reform Act of 1986 eliminated differential tax rates for long-term capital gains as compared to the tax rates applied to ordinary gains.<sup>90</sup> After 1987 the taxpayer is indifferent as to whether gains are characterized as capital or ordinary.<sup>91</sup> Thus, the application of *Corn Products* to post-1987

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79. Boyles, *The Supreme Court Kills the Corn Products Doctrine—But Will It Rest in Peace?*, 66 TAXES 723, 727 (1988).

80. *Id.* at 735.

81. *Id.* at 727.

82. *Id.* See also I.R.C. §§ 1201-1202, 1211-1212 (Supp. IV 1986).

83. Boyles, *The Supreme Court Kills the Corn Products Doctrine—But Will It Rest in Peace?*, 66 TAXES 723, 727 (1988).

84. *Id.*

85. *Id.*

86. *Id.*

87. *Id.*

88. *Id.*

89. *Id.*

90. *Id.*

91. *Id.* at 727-28.

years is relevant only for recharacterizing capital losses as ordinary losses.<sup>92</sup> The *Arkansas Best* interpretation of *Corn Products* "is unfavorable to taxpayers with respect to tax years after 1987 since it restricts the applicability of a judicial doctrine which is favorable only to the taxpayer."<sup>93</sup>

Currently, *Arkansas Best* is "a powerful tool to be used primarily by the IRS in order to classify potential ordinary deductions into capital losses that are restricted as to deductibility."<sup>94</sup> However, the Tax Reform Act of 1986 retained the statutory structure for capital gains in order to facilitate its reinstatement in the event of future tax rate increases.<sup>95</sup> These future tax rate increases and accompanying reinstatement of the capital gains provision seem inevitable because of the present United States budget deficit. One commentator predicts that such reinstatement will generate further judicial inquiry.<sup>96</sup> If the capital gains provision is reinstated, *Arkansas Best* will not only be a powerful tool for the IRS but will also be an equally powerful tool for the taxpayer for converting potential ordinary gains into the more favorably treated capital gains.<sup>97</sup>

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92. *Id.*

93. *Id.*

94. *Id.* at 735.

95. See I.R.C. §§ 1201-1202 (Supp. IV 1986).

96. *Id.*

97. *Id.*