INTERNAL REVENUE SERVICE
NATIONAL OFFICE TECHNICAL ADVICE MEMORANDUM

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CASE-MIS No.: TAM-138778-16

Associate Area Counsel, Manhattan
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Taxpayer's Name:

Taxpayer's Address:

Taxpayer's Identification No.:

Year(s) Involved:
Date of Conference:

LEGEND:

Taxpayer =
A =
Broker =
Trading Account =
Parent =
Advisor =
Hedge Fund =
General Partner =
a =
b =
c =
Year 1 =
Year 2 =

ISSUES:

1. Did A realize losses under § 1001 of the Internal Revenue Code ("Code") upon the transfer of securities from A's personal brokerage accounts held at Broker (the "Hedge Accounts") to a proprietary trading account held at Broker ("Trading Account")?

2. Did Hedge Fund realize losses under § 1001 upon the transfer of securities to Trading Account held at Broker?

3. If Hedge Fund realized losses upon the transfer of securities to Trading Account under § 1001, were the losses disallowed as a deduction by reason of § 707(b)?

4. If the losses were disallowed under § 707(b), does the wash sale exception under § 267(d)(2) apply for purposes of determining subsequent gain, or are the losses permanently disallowed to Hedge Fund under § 267(d)(1)?

CONCLUSIONS:

1. A did not realize losses under § 1001 upon the transfer of securities from the Hedge Accounts to Trading Account.

2. Hedge Fund realized losses under § 1001 upon the transfer of securities to Trading Account.

3. Losses sustained by Hedge Fund were disallowed as a deduction by reason of § 707(b).

4. The wash sale exception under § 267(d)(2) does not apply for purposes of determining subsequent gain. Thus, the losses are permanently disallowed to Hedge Fund under § 267(d)(1).

FACTS:

For the tax years Year 1 and Year 2, which are the tax years at issue in this technical advice memorandum, A, through A's Hedge Accounts, and Hedge Fund transferred publicly traded securities to Trading Account. A and Hedge Fund reported the transactions as sales for federal income tax purposes and claimed losses on their respective federal income tax returns. At issue, is whether the losses that A and Hedge Fund claimed are allowable, deferred, or disallowed for federal income tax purposes.

A. Ownership Structure

1. A / Broker

A is the chief executive officer (CEO) and a majority shareholder of Broker, a self-clearing broker-dealer, organized as a subchapter S corporation. A is also a majority shareholder of Parent, which is a percent owner of Advisor, an investment adviser. During the tax years at issue, A owned approximately b percent of both Broker and Parent, with most of the remainder of each entity equally owned by A's children.

During the tax years at issue, A regularly directed publicly traded securities owned by A, through the Hedge Accounts[1], or by Hedge Fund to be transferred to Trading Account. Although Broker held legal title to Trading Account, as well as to the securities held in the account, A had exclusive and complete discretion, voting power and control over the investments in Trading Account, including all acquisitions and dispositions of the securities held in Trading Account. In addition, under a Compensation Agreement, discussed in more detail below, A possessed the economic benefits and burdens (including dividends) associated with the securities in Trading Account.

2. Hedge Fund

Advisor manages a group of hedge funds. The hedge fund group includes Hedge Fund, a partnership. A serves as the portfolio manager for these hedge funds, including Hedge Fund, and, as such, controls Hedge Fund's investment activities.[2] The stock portfolio of Hedge Fund is held in custody at Broker, which has served as its primary broker since the formation of Hedge Fund.

During the tax years at issue, Hedge Fund had three classes of partners: limited partners ("LPs"), special limited partners ("SLPs"), and a general partner ("GP"). Hedge Fund's partnership agreement provided that the management and control of partnership activities, including the investment in, and disposition of, securities, rested exclusively with the GP.

Unrelated investors in Hedge Fund held either LP or SLP interests. A owned a certain SLP interest. General Partner was the GP of Hedge Fund and A owned c percent of, and fully controlled, General Partner. Thus, A indirectly owned and controlled the GP interest in Hedge Fund. A's interest varied over time, but for at least some of the time during the years at issue, A possessed a greater than 50 percent capital or profits interest, taking into account interests attributed from A's children.

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[1] A's ownership of the securities held in the Hedge Accounts is not at issue in this technical advice memorandum.

[2] Although A was the principal adviser to Hedge Fund, A had delegated some portfolio discretion to one of A's children.

Hedge Fund's brokerage account at Broker was a margin account and Hedge Fund received all of the economic benefits and suffered all of the economic burdens of that account. The transaction price for securities traded between Hedge Fund and Trading Account was not paid in cash. Instead, the price was paid through an adjustment to Hedge Fund's cash credits or margin debits, which were treated for book and legal purposes by Broker as accounts receivable (in the case of Hedge Fund margin debits) or payable (in the case of Hedge Fund cash credits). Broker paid interest to Hedge Fund's account on cash credits, and received interest from Hedge Fund's account on margin debits, in each case at a negotiated interest rate.[3]

B. The Compensation Agreement

Prior to the tax years at issue, A and Broker executed a compensation agreement (the "Compensation Agreement"). The Compensation Agreement related to investment activities in four proprietary trading accounts ("TCA Accounts") held at Broker, including Trading Account. The Compensation Agreement entitled A to receive all of the gains from the TCA Accounts, reduced by losses, as well as any dividends paid on the securities in the TCA Accounts. Any expenses associated with the TCA Accounts (e.g., third-party brokerage fees and interest expense) were allocated to A under the Compensation Agreement.

For U.S. tax purposes, Broker treated itself as the owner of Trading Account and the shares held therein. Broker was a dealer in securities under § 475 and did not identify the securities held in Trading Account as held for investment under § 475(b). Thus, in computing its taxable income that was allocated to its shareholders, Broker took into account realized gains and net realized losses as well as mark-to-market gains and losses under § 475 and any dividends (i.e., all amounts that are recognized for federal income tax purposes). Amounts paid out to A under the Compensation Agreement were treated as ordinary compensation income to A and as deductible expenses by Broker that were allocated to Broker's shareholders.

C. The Reported Loss Trades

A, through A's Hedge Accounts, and in A's own discretion, and Hedge Fund, at A's direction, engaged in purported "sale and/or repurchase" trade transactions with Trading Account, during the tax years at issue. These transactions were accomplished through the following steps:

1) A, through A's Hedge Accounts, and Hedge Fund, through its brokerage account at Broker, transferred shares of stock to Trading Account in order to realize tax losses on the shares and reported the losses for federal

[3] The mechanics, pricing, and interest described in this paragraph generally apply to trades between the Hedge Accounts and Trading Account as well.

income tax purposes. Sometime after 31 days, A would determine whether to "repurchase" the security from Broker.

2) In most cases (about 75 percent of the time), at A's direction, identical shares of stock were transferred from Trading Account back to the transferor at the then current fair market value.

3) In the remaining cases (about 25 percent of the time), the shares were sold into the market rather than transferred back to the transferor. The direct sales into the market generally took place after 31 days.

Notwithstanding the Compensation Agreement between A and Broker, Taxpayer concedes that there was never a formal written or oral option agreement between the parties to reacquire the transferred securities "or even a conscious realization by the parties that they were entering into a legal option." The sales and repurchases did not involve commissions and were completed without affecting the market prices of the securities.

All of the reported loss trades between A, as the owner of the Hedge Accounts, or Hedge Fund, and Trading Account involved shares that were traded on NASDAQ or a major stock exchange and for which market quotations of the "Bid" or "Ask" prices were readily available. Moreover, the transactions were executed at the prevailing market prices at or between the Bid and the Ask. All of the shares that were the subject of the reported loss trades were held in "street name" with the Depository Trust & Clearing Corporation.

LAW AND ANALYSIS:

ISSUES 1 AND 2: Did A, through A's Hedge Accounts, or Hedge Fund realize losses under § 1001 upon the transfer of securities to Trading Account?

Under § 1001(a), gain from the sale or other disposition of property is the excess of the amount realized therefrom over the adjusted basis provided in § 1011 for determining gain, and the loss is the excess of the adjusted basis provided in § 1011 for determining loss over the amount realized. Under § 1.1001-1(a) of the Income Tax Regulations, the gain or loss realized from the conversion of property into cash, or from the exchange of property for other property differing materially in kind or in extent, is treated as income or loss sustained.

Section 1001(b) provides that the amount realized from the sale or other disposition of property shall be the sum of any money received plus the fair market value of the property (other than money) received. Under § 1001(c), except as otherwise provided in subtitle A, the entire amount of gain or loss, determined under § 1001, on the sale or exchange of property shall be recognized.

The term "sale" is given its ordinary meaning for federal income tax purposes and is generally defined as a transfer of property for money or a promise to pay money. *Commissioner v. Brown*, 380 U.S. 563, 570-571 (1965). The key to deciding whether a sale has occurred is whether the benefits and burdens of ownership have passed from the transferor to the transferee. *Grodt & McKay Realty v. Commissioner*, 77 T.C. 1221, 1238 (1981); *Calloway v. Commissioner*, 135 T.C. 26 (2010); *Anschutz v. Commissioner*, 135 T.C.78 (2010), *aff'd* 664 F.3d 313 (10th Cir. 2011). There are no hard and fast rules of thumb that can be used in determining, for taxation purposes, when a sale was consummated, and no single factor is controlling; the transaction must be viewed as a whole and in the light of realism and practicality. *Commissioner v. Segall*, 114 F.2d 706, 709 (6th Cir. 1940).

(A) Loss Trades Between the Hedge Accounts and Trading Account

On numerous occasions, A transferred securities from A's Hedge Accounts to Trading Account and claimed a loss deduction for federal income tax purposes. Each purported sale from the Hedge Accounts to Trading Account transferred legal title from the Hedge Accounts to Broker.

Taxpayer concedes that, although Broker acquired legal title to Trading Account, A retained exclusive and complete discretion and control over the securities held in Trading Account, personally directing all purchases into, and sales from, Trading Account. Pursuant to the Compensation Agreement, A retained all gains from the TCA Accounts (including Trading Account), reduced by losses, as well as any dividends paid on the securities in the TCA Accounts. Any expenses associated with the TCA Accounts (for example, third-party brokerage fees and interest expense) were allocated to A. Taxpayer agrees that, under the terms of the Compensation Agreement, A "generally enjoyed all of the economic risks and rewards associated with the shares in Trading Account." A controlled voting decisions with respect to the securities in Trading Account. Taxpayer states that there was no formal investment management agreement between A and Broker with respect to Trading Account.

Under these facts, A retained the benefits and burdens of ownership of the securities A transferred from A's Hedge Accounts to Trading Account, and, therefore, the transfers were not sales under § 1001. Although Broker held legal title to the securities in Trading Account, Broker did not acquire a possessory interest in those securities. A held the rights to dividends on those securities as well as the benefit of gains and the burden of losses due to fluctuations in prices. A, in A's sole discretion, made all determinations as to the retention or disposition of securities in Trading Account. Broker did not retain any control over voting or investment decisions, directly or indirectly through an investment management agreement. Accordingly, A did not realize losses under § 1001 upon the transfer of securities from the Hedge Accounts to Trading Account.

(B) Loss Trades Between Hedge Fund and Trading Account

In contrast to A's direct ownership of the securities held in A's Hedge Accounts, the securities held by Hedge Fund in its brokerage accounts at Broker were not owned by A. In A's capacity as Hedge Fund's investment advisor, A directed trades for the economic benefit of Hedge Fund's investors, which included A and A's children, and third-party investors, who owned a significant portion of the capital interest, or the profits interest, in Hedge Fund.

Additionally, Hedge Fund did not retain the benefits and burdens of ownership of the securities transferred to Trading Account, and, therefore, the transfers were sales under § 1001. The Tax Court in *Grodt & McKay Realty, Inc. v. Commissioner* lists several factors previous courts have used in determining "whether the benefits and burdens of ownership have passed" to classify a transfer as a sale. 77 T.C. at 1237-1238. The applicable factors to the issue at hand are (1) whether legal title passes; (2) how the parties treat the transaction; (3) whether the contract creates a present obligation to execute or make payments; (4) whether the right of possession has vested; (5) which party bears the risk of loss; and (6) which party benefits from the profits. *Id.*, *citing Commissioner v. Segall*, 114 F.2d at 709; *Oesterreich v. Commissioner*, 226 F.2d 798, 803 (9th Cir. 1955); *Wiseman v. Scruggs*, 281 F.2d 900, 902; *Harmston v. Commissioner*, 61 T.C. 216, 229 (1973).

Applying the *Grodt & McKay Realty* factors to the present situation establishes the transactions as sales. Each sale transferred legal title from Hedge Fund to Trading Account, which was owned by A. All parties reported the transactions as sales for regulatory, accounting, and tax purposes. Each sale from Hedge Fund to Trading Account was priced at an amount equal to the current trading price of the stock on NASDAQ at the time of the transaction. Because Broker served as Hedge Fund's broker, payment was made by credits and debits to Trading Account and Hedge Fund's brokerage account. Thus, Trading Account incurred an obligation to make payment and paid for the stock it acquired from Hedge Fund.

As discussed above, A, as the tax owner of Trading Account, was in full possession of the securities, including voting rights, A acquired from Hedge Fund, and A bore the full market risk of losses as well as the benefit of gains, including any dividends declared during the time Trading Account possessed the securities. Accordingly, Hedge Fund realized losses under § 1001(a) upon the transfer of securities to Trading Account.

Furthermore, because A was the tax owner of the securities held in Trading Account during the tax years at issue, the transfers between Hedge Fund and Trading Account occurred between a partnership and a partner.

ISSUE 3: Are the losses sustained by Hedge Fund upon the transfer of securities to Trading Account disallowed as a deduction by reason of § 707(b)?

Section 267(a)(1) disallows a deduction for any loss from the sale or exchange of property, directly or indirectly, between persons, who, on the date of the sale or exchange, are within one of the relationships specified in § 267(b). *See* § 1.267(a)-1. In 1954, Congress enacted § 707(b) to extend the § 267 loss disallowance rules to transactions between a partnership and a partner. Section 707(b)(1)(A) provides that no deduction is allowed for losses arising from the sale or exchange of property (other than an interest in the partnership), directly or indirectly, between a partnership and a person owning, directly or indirectly, more than 50 percent of the capital interest, or the profits interest, in such partnership. The Senate Report to the 1954 Code states:

> Subsection (b) provides an exception to the general rule in the case of sales of property between the partnership and a controlling partner which is designed to prevent tax avoidance through the realization of fictitious losses or increasing the basis of property for purposes of depreciation. The provisions of the House bill, however, have been amended by your committee by adopting the rules comparable to those which are applicable in the case of sales of property between corporations and controlling shareholders under sections 267 and 1240.

S. Rep. No. 83-1622 at 387 (1954), *reprinted in* 1954 U.S.C.C.A.N. 4621, 5028.

A's interest varied over time, but for at least some of the time during the years in issue, A possessed a greater than 50 percent capital or profits interest in Hedge Fund at the time of some of the transfers by Hedge Fund to A. Taxpayer represents that the reported losses are not bona fide losses for purposes of § 165. However, Taxpayer asserts that § 267 and § 707(b) only apply to losses that are bona fide losses under § 165.

The loss disallowance rules of § 267 and § 707(b) are unambiguous; a loss is disallowed once a statutorily-prescribed relationship is met. Congress enacted objective tests in order to avoid evidentiary issues previously faced by the Internal Revenue Service ("Service") in determining whether or not loss sales between related parties were bona fide. The House Ways and Means Report to the Revenue Bill of 1937 explains:

> However, because the evidence necessary to establish the fact that a sale or exchange was not made in good faith is almost wholly within the knowledge of the person containing the deduction, the Government has encountered considerable difficulty in sustaining the disallowance of the deduction in a great many cases. Moreover, the specific provisions of section 24(a)(6) of existing law have proved inadequate to meet many situations of this type. Accordingly, your committee proposes the amendment of this section to provide certain additional restrictions on deductions of this character.

H. Rep. No. 1546, 75th Cong., 1st Sess., p. 26 (1939-1 Cum.Bull. (Part 2) 704, 722-723).[4] The Supreme Court has recognized that the loss disallowance rules under § 267 serve as a prohibition, rather than a rebuttable presumption, against a loss deduction once a statutorily-prescribed relationship is met. In *McWilliams v. Commissioner*, 331 U.S. 694, 699 (1947), the Court stated:

> Moreover, we think the evidentiary problem was not the only one which Congress intended to meet. Section 24(b) states an absolute prohibition – not a presumption – against the allowance of losses on any sales between the members of certain designated groups. The one common characteristic of these groups is that their members, although distinct legal entities, generally have a near-identity of economic interests. It is a fair inference that even legally genuine intra-group transfers were not thought to result, usually, in economically genuine realizations of loss, and accordingly that Congress did not deem them to be appropriate occasions for the allowance of deductions.

Thus, it is clear that the loss disallowance rules under § 267 were not intended to be limited by the non-bona fide standard of § 165.[5] Taxpayer's interpretation would put the Service in the position of needing to prove (rather than disprove) the bona fide nature of a related-party loss before applying the loss disallowance rules of § 267 and § 707(b). It is clear that Congress intended for the objective loss disallowance rules to co-exist with the non-bona fide § 165 standard as tools for the Service to use to ensure that reported loss deductions represent economically genuine loss realizations. Likewise, it is equally clear that Congress did not intend for the loss disallowance rules under § 267 to supplant the Service's use of the non-bona fide standard under § 165. As explained by the House Ways and Means:

> Under existing law, section 24(a)(6) of the Revenue Act of 1936, losses are specifically denied in the case of sales or exchange of property between members of a family or between a shareholder and a corporation in which such shareholder and his immediate family owns more than 50 percent in value of the outstanding stock. This provision of existing law is not exclusive and the Government may still deny losses in the case of sales or exchanges not specifically covered thereby (for instance, between uncle and nephew) if such sales or exchanges are not bona fide.

H. Rep. No. 1546, 75th Cong., 1st Sess., p. 26 (1939-1 Cum.Bull. (Part 2) 704, 722-723). *See also* § 1.267(a)-1(c) ("However, section 267 is not exclusive. No deduction

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[4] Section 24 was the predecessor of § 267. Section 267 expanded the constructive ownership rules of § 24 to reach more situations in which artificial losses might be created.

[5] Section 165 is not at issue in this technical advice memorandum. Taxpayer's view is that the losses are not bona fide under § 165. Whether the losses are bona fide under § 165 is irrelevant to the Service's analysis under § 267.

for losses or unpaid expenses or interest arising in a transaction which is not bona fide will be allowed even though section 267 does not apply to the transaction.”).

Based upon the foregoing, Taxpayer’s assertion that the reported losses do not represent bona fide losses for purposes of § 165, even if accepted as true, does not bar the Service’s application of the loss disallowance rules of § 267 and § 707(b). Accordingly, § 707(b) disallows losses on transfers from Hedge Fund to A in situations in which A owned, directly or indirectly, more than 50 percent of Hedge Fund’s capital or profits interests at the time of the sale.

ISSUE 4: Does the wash sale exception under § 267(d)(2) apply for purposes of determining subsequent gain, or are the losses permanently disallowed to Hedge Fund under § 267(d)(1)?

Section 707(b) provides that, in the case of a subsequent sale or exchange by a transferee described in § 707(b), § 267(d) shall apply as if the loss were disallowed under § 267(a)(1).

Under § 267(d)(1), upon the subsequent sale or exchange of property with respect to which a loss deduction was disallowed to the transferor by reason of § 267(a)(1) (or, in the instant case, § 707(b)), the transferee recognizes gain only to the extent it exceeds the disallowed loss properly allocable to the property.

Section 267(d)(2) provides an exception to § 267(d)(1) if the loss sustained by the transferor is not allowable to the transferor as a deduction by reason of § 1091 (relating to wash sales).

Section 1091 generally disallows any claimed loss arising from the sale of stock or securities by a taxpayer if the taxpayer acquires such stock or securities, or has entered into an option or a contract to acquire such stock or securities, within the relevant time period prescribed under § 1091(a). More particularly, § 1091(a) provides that:

> In the case of any loss claimed to have been sustained from any sale or other disposition of shares of stock or securities where it appears that, within a period beginning 30 days before the date of such sale or disposition and ending 30 days after such date, the taxpayer has acquired (by purchase or by an exchange on which the entire amount of gain or loss was recognized by law), or has entered into a contract or option so to acquire, substantially identical stock or securities, then no deduction shall be allowed under section 165 unless the taxpayer is a dealer in stock or securities and the loss is sustained in a transaction made in the ordinary course of such business.

Taxpayer argues that Hedge Fund’s disallowed losses arising from the transfer of securities to Trading Account are preserved through the operation of § 1091(d).

Section 1091(d) applies to property consisting of stock or securities the acquisition of which (or the contract or option to acquire which) resulted in the nondeductibility of losses under § 1091(a). Therefore, § 1091 does not apply to Hedge Fund's transfers to Trading Account.

In the instant case, § 1091(a) does not apply to disallow the losses on Hedge Fund's transfer of securities to Trading Account. Section 1091(a) would apply only if Hedge Fund had either reacquired these securities within 30 days of their transfer to Trading Account or entered into a contract or option to acquire those securities. Hedge Fund did neither.

(A) Hedge Fund Did Not Enter into an Option or Contract to Reacquire the Securities

Hedge Fund did not reacquire any of the securities it transferred to Trading Account within 30 days. In a substantial number of cases, Hedge Fund never reacquired the securities it transferred to Trading Account. In the cases where Hedge Fund reacquired securities, its reacquisition occurred more than 30 days after the initial transfer. As stated earlier, Taxpayer concedes that there was no actual option or other agreement between Hedge Fund and A or Broker to reacquire the securities.

(B) Hedge Fund Should Not Be Treated, for § 1091 Purposes, as if Hedge Fund Had Acquired Options to Reacquire Securities Transferred to Trading Account

Taxpayer argues that Hedge Fund, upon the transfer of securities to Trading Account, should be viewed as if it had acquired options ("Implied Options") to repurchase the securities at their fair market value. Taxpayer states "[o]bviously, there was never a formal written or oral option agreement between the parties or even a conscious realization by the parties that they were entering into a legal option; rather these Implied Options are inferred as a legal conclusion from the stated intentions and understandings of the parties and their conduct." According to Taxpayer, the Implied Options had fair market value strike prices. The securities at issue were publicly traded, fungible, and could be readily purchased at fair market value. Generally, options on publicly traded securities provide for fixed strike prices that permit the value of an option to fluctuate with changes in the value of the underlying securities. Moreover, Taxpayer's representatives acknowledge that they do not know of options with a fair market value strike price being available in the market for publicly traded securities.

Taxpayer asserts that the ability of Hedge Fund to reacquire the securities was an "option-like" right because those repurchases were made without commissions and without affecting the market pricing of the repurchased securities. Although Hedge Fund's ability to efficiently repurchase securities had value, that value did not give Hedge Fund an economic interest in the performance of the securities and should not

be confused with an option. *See Fed. Home Loan Mortg. Corp. v. Commissioner*, 125 T.C. 248, 263-264 (2005) ("An essential part of any option is that its potential value to the optionee and its potential future detriment to the optionor depends on the uncertainty of future events. An optionee is willing to pay for potential future value, and the optionor is willing to accept a potential future detriment for a price."); *Halle v. Commissioner*, 83 F.3d 649, 657 (4th Cir. 1996) ("Option contracts permit parties to shift the risks of contingencies that may affect the value of the property subject to the contract; the buyer of a call option receives the benefit of any future increases in the value of the property, while the option's seller bears the cost of any future depreciation. Where there are no significant risks to apportion, therefore, there is little reason for the parties to contract for an option.").

Taxpayer bases its Implied Option argument on decisions involving situations in which taxpayers sought tax losses for sales of securities to an alter ego or an accommodation party and subsequently reacquired the securities. *See Shoenberg v. Commissioner*, 30 B.T.A. 659 (1934), *aff'd*, 77 F.2d 446 (8th Cir. 1935); *Powell v. Commissioner*, 34 B.T.A. 655 (1936), *aff'd*, 94 F.2d 483 (1st Cir. 1938); *Commissioner v. Dyer*, 74 F.2d 685 (2nd Cir. 1935); *Mellon v. Commissioner*, 36 B.T.A. 977 (1937); *Du Pont v. Commissioner*, 37 B.T.A. 1198 (1938), *aff'd*, 118 F.2d 544 (3rd Cir. 1941). These decisions do not provide authority for Taxpayer's position that Implied Options were entered into by Hedge Fund to reacquire the securities.

For instance, in *Dyer*, all seven shareholders of a closely held corporation acted in concert to sell shares of the corporation to a wholly owned subsidiary. Each of the shareholders simultaneously bought back such shares just over 30 days later. The court viewed the shareholders to have "a mutual understanding that the transfers would be rescinded." 74 F.2d at 686. The court concluded that the shareholders had not completely terminated their interest in the shares sold and therefore had not realized a loss.

Similarly, in *Shoenberg*, the Board of Tax Appeals concluded that the taxpayer had not completed a bona fide sale of securities when an investment company simultaneously purchased the same securities and, slightly more than 30 days later, the taxpayer caused the investment company to transfer the shares to him at the market price. The Board of Tax Appeals stated "we start with a taxpayer who possessed, to all practical purposes, as an *alter ego*, a corporation entirely dominated by him" for which he acted alone under a blanket grant of authority. 30 B.T.A. at 661 (emphasis in original). On appeal, the Eighth Circuit Court of Appeals affirmed, stating that its analysis was predicated upon "realities" and that the taxpayer had not experienced "any real change in his position."[6]

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[6] 77 F.2d at 449. The other decisions cited by Taxpayer also do not provide authority to imply the existence of an option under § 1091. *See Powell*, 34 B.T.A. 655, 659, 661 (concluding that "sales were not final dispositions" and "alleged losses" were not "sustained" when a taxpayer sold property, had a trust purchase the same property, after slightly more than 30 days reacquired the same property, and "had the power within himself to reacquire property from the trust identical with that which he sold"); *Du*

Given that third party investors owned a significant portion of the capital or profits interests in Hedge Fund in the tax years at issue, Hedge Fund was not the alter ego of A or Broker. Hedge Fund experienced a real change in its position by selling the securities to Trading Account. Hedge Fund divested itself of all of its interests in the performance of the securities during the time that the securities were held in Trading Account.

Hedge Fund did not reacquire the securities within 30 days. Taxpayer concedes that the parties had no agreement that the securities transferred by Hedge Fund would be repurchased. Moreover, in a substantial portion of the transactions in issue, Hedge Fund never repurchased the securities.

None of the decisions relied upon by Taxpayer conclude that a taxpayer selling securities and subsequently reacquiring some of the securities entered into an implied option. To the contrary, in *Gutmann v. Commissioner*, 38 B.T.A. 679 (1938), the Board of Tax Appeals concluded that the wash sale rule did not apply to a sale of stock by an employee to his employer even though the grant of an option to repurchase the shares was discussed by the employer's treasurer and counsel within 30 days of the employee's sale, because "no contract in respect of the option existed between [the employee] and [the employer until] the option was ratified by the corporation's directors," more than 30 days after the employee's sale of the stock. *Id*. at 686. Accordingly, § 1091(a) does not apply to disallow losses on the transfers made by Hedge Fund to Trading Account. As a result, the exception under § 267(d)(2) does not apply for purposes of determining subsequent gain. Thus, the § 1091(d) basis rule does not apply.

* * *

In summary, based upon the facts presented, Trading Account served as an alter ego of A who was the tax owner of Trading Account and all securities held therein. As a result, A did not realize losses under § 1001 on transfers from A's Hedge Accounts to Trading Account.

As a partnership separate from A, Hedge Fund realized losses under § 1001 on transfers to Trading Account. However, because A is the tax owner of Trading Account, all transfers between Hedge Fund and Trading Account are transactions between a partner and a partnership and subject to § 707(b). As a result, § 707(b) disallows

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Pont, 37 B.T.A. 1198, 1266 (disallowing losses claimed by two associates stating that they had only entered into "pretended sales" that were not "bona fide" dispositions and that the sales were "contrived and consummated through mutual understanding and agreement between the two parties for the reacquisition of the stocks originally owned by each"); *Mellon*, 36 B.T.A. 977, 1053 (concluding under unique circumstances in which relevant parties were deceased that the taxpayer failed to prove "that he suffered a deductible loss" or that the agreement to reacquire was not entered into within 30 days of the original sale).

losses on transfers from Hedge Fund to Trading Account in situations in which A owned, directly or indirectly, more than 50 percent of Hedge Fund's capital or profits interest at the time of the transfer. Finally, for purposes of determining a transferee's gain upon a subsequent disposition of the securities, the rules of § 267(d)(1) are applicable.

CASE DEVELOPMENT, HAZARDS AND OTHER CONSIDERATIONS:

No opinion is expressed or implied as to whether the reported losses constitute bona fide losses under § 165 or any other provision of the Code or by operation of common law doctrines, including the doctrine of substance over form.

In a supplemental submission, Taxpayer states that in one instance the price for the repurchase of a security by Hedge Fund was set at the fair market value a few days before the repurchase and just prior to an announced acquisition of the company. The use of the pre-announcement fair market value for the repurchase price of the security gave Hedge Fund the benefit of the post-announcement increase in the value of the security. Taxpayer's stated facts in the supplemental submission are inconsistent with the joint statement of facts submitted in connection with this technical advice memorandum and have not been relied upon in this memorandum.

This writing may contain privileged information. Any unauthorized disclosure of this writing may undermine our ability to protect the privileged information. If disclosure is determined to be necessary, please contact this office for our views.

CAVEAT(S):

A copy of this technical advice memorandum is to be given to the taxpayer(s). Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Please call (202) 317-7007 if you have any further questions.