5-1-2017

Statutory Interpretation Lessons Courtesy of *Pilgrim's Pride*

Philip G. Cohen

Statutory Interpretation Lessons Courtesy of *Pilgrim's Pride*

Philip G. Cohen*

In Pilgrim's Pride Corp. v. Commissioner, the Fifth Circuit reversed the Tax Court and held that the taxpayer was entitled to an ordinary loss deduction from its abandonment of securities. While the conclusion reached by the Fifth Circuit has been overshadowed by the promulgation of Treasury Regulation section 1.165-5(i) that effectively treats an abandoned security as worthless and thus characterizes the loss as capital, the case remains noteworthy because it provides an opportunity to examine the statutory interpretation of two distinct Internal Revenue Code sections, section 165(g)(1) and section 1234A. The article focuses on what methods of statutory construction should have been utilized to determine the application of these sections to the Pilgrim's Pride fact-*pattern.*

Ordinary loss treatment for an abandoned security seems conceptually incorrect when both a worthless security and a sale of the security for a de minimis amount would generally result in a capital loss. The article analyzes whether, and if so, under what theory did the courts deciding Pilgrim's Pride possess the statutory authority to treat the abandonment as a capital loss. Furthermore, assuming the courts had such authority, the article considers whether it was proper to do so under the particular factual circumstances surrounding this case.

---

* Associate Professor of Taxation, Pace University Lubin School of Business; Retired Vice President-Tax & General Tax Counsel, Unilever United States, Inc.; New York University, B.A., 1971; Duke University School of Law, J.D., 1974; New York University School of Law, LL.M.(Labor Law), 1975; LL.M. (Taxation), 1982; George Washington University, M.B.A., 1979. The author would like to thank Michael Schler and Professor Richard Kraus for their helpful comments on an earlier draft and his graduate teaching assistant, Huirong (Helena) Tang for her assistance with the article. All errors or omissions are his own.

There are a variety of statutory construction methodologies each with erudite proponents making very persuasive contentions. Applying an Internal Revenue Code section to a particular fact-pattern, however, it can often be wiser not to be wedded to one approach, e.g., textualism. Instead, it is submitted that employing disparate methodologies depending on the particular circumstances may be sounder. Pilgrim's Pride provides a focal point for examining statutory interpretation methodologies and illustrating the foregoing. As such, reflecting on the case has continuing relevance despite the widespread application of Treasury Regulation section 1.165-5(i) to the abandonment of securities.

As demonstrated by the different approaches that I believe were proper here for considering the applicability of sections 165(g)(1) and 1234A to Pilgrim's Pride, distinct circumstances require discrete approaches to applying a statutory provision to a case. Our democratic institutions are not put at risk, by foregoing dogmatic textualism where this would lead to a result wherein "no conceivable tax policy . . . supports this interpretation" or deeming, in the case of section 165(g)(1), an abandoned security to be per se worthless. Restraint, however, from deviating from the clear language of the text, such as applying section 1234A to inherent rights, may be in order where there are no overriding reasons not to do so.

I. INTRODUCTION 3
II. PILGRIM'S PRIDE V. COMMISSIONER 8
A. The Tax Court Decision *8*
B. The Fifth Circuit Decision *12*
II. AN INTRODUCTION TO SOME STATUTORY INTERPRETATION METHODOLOGIES 13
III. OBSERVATIONS 21
A. Section 165(g)(1) and Abandonment of Securities *21*
B. Section 1234A *32*
IV. CONCLUSION 44

I. INTRODUCTION

In *Pilgrim's Pride Corp. v. Commissioner*,[1] the Fifth Circuit reversed the Tax Court and held that the taxpayer was entitled to an ordinary loss deduction from its abandonment of securities. While the conclusion reached by the Fifth Circuit has been overshadowed by the promulgation of Regulation section 1.165-5(i)[2] that effectively treats an abandoned security as worthless and thus characterizes the loss as capital, reflecting on the case remains noteworthy because it provides an opportunity to examine the statutory interpretation of two distinct Internal Revenue Code sections, section 165(g)(1) and section 1234A. The article focuses on what methods of statutory construction should have been utilized to determine the application of these sections to the *Pilgrim's Pride* fact-pattern.

Ordinary loss treatment for an abandoned security seems conceptually incorrect when both a worthless security and a sale of the security for a *de minimis* amount would generally result in a capital loss. The article analyzes whether, and if so under what theory did the courts deciding *Pilgrim's Pride* possess the statutory authority to treat the abandonment as a capital loss. Furthermore, assuming the courts had such authority, the article considers whether it was proper to do so under the particular factual circumstances surrounding this case.

With respect to section 165(g)(1), the issue, which was eschewed by the Tax Court, was whether a court should consider an abandoned security having objective value as being worthless. There was an absence of any evidence that Congress contemplated such treatment and the regulation mandating such an outcome was not effective for the year in question. Furthermore, there was a revenue ruling and court decisions that could be interpreted, at least by analogy as precedent for an ordinary loss. Notwithstanding the foregoing, per se capital loss characterization for an abandoned security, absent taxpayer reliance on guidance from the Service, is both logical and consistent with sound public policy.

Section 1234A is a provision described by one author as "cumbersome"[3] and whose existence might not survive tax reform of derivative instruments.[4] For both section 165(g)(1) and section 1234A, the

---

1 Pilgrim's Pride Corp. v. Comm'r, 779 F. 3d 311 (5th Cir. 2015), *rev'g* 141 T.C. 533 (2013).

2 *See* Abandonment of Stocks or Other Securities, 73 Fed. Reg. 13,124 (Mar. 12, 2008) (to be codified at 26 C.F.R. pt. 1).

3 *See* David J. Roberts, *Law Treating Certain Terminations as Sales Needs Clarification*, 150 TAX NOTES 337 (2016).

4 The Modernization of Derivatives Tax Act of 2016, S. __, introduced in May 2016 by Senate Finance Committee ranking minority member Ron Wyden (D-OR) would, if enacted, repeal section 1234A. It would have also been repealed under the legislation proposed a few years ago by then House Ways and Means Committee Chair Dave Camp

article seeks to examine what were the appropriate methodologies for construing the respective provisions in connection with the abandonment of a security.

By way of background**,** generally, the sale or exchange of a capital asset for a loss is treated as a capital loss.[5] Capital losses are only allowed to a corporate taxpayer to the extent of capital gains,[6] although such capital losses can be carried back three taxable years and forward for five taxable years if there is insufficient capital gain in the year of the capital loss.[7]

Section 165 (a) sets forth a general rule permitting a deduction for losses "not compensated for or by insurance or otherwise."[8] Treasury Regulation section 1.165-2(a) specifies in pertinent part that

> A loss incurred in a business or in a transaction entered into for profit and arising from the sudden termination of the usefulness in such business or transaction of any non-depreciable property, in a case where such business or transaction is discontinued or where such property is permanently discarded from use therein, shall be allowed as a deduction under section 165(a) for the taxable year in which the loss is actually sustained.[9]

Pursuant to Treasury Regulation section 1.165-2(b), however, Treasury regulation section 1.165-2(a) is not applicable "to losses sustained upon the sale or exchange of property."[10]

Treasury regulation section 1.165-1(b) provides in pertinent part that

> To be allowable as a deduction under section 165(a), a loss must be evidenced by closed and completed transactions, fixed by identifiable events, and, except as otherwise provided in section 165(h) and § 1.165-11, relating to disaster losses, actually sustained during the taxable year.[11]

(R.-MI). *See* JOINT COMMITTEE ON TAXATION, *Technical Explanation, Estimated Revenue Effects, Distributional Analysis, and Macroeconomic Analysis of the Tax Reform Act of 2014, A Discussion Draft of the Chairman of the House Committee on Ways and Means to Reform the Internal Revenue Code*, JCS-1-14, at 281-293 (2014).

5 *See* I.R.C. § 1222 (2014).

6 *See* I.R.C. § 1211(a) (2012).

7 *See* I.R.C. § 1212(a) (2012).

8 I.R.C. § 165(a) (2012).

9 Treas. Reg. § 1.165-2(a) (2014).

10 Treas. Reg. § 1.165-2(b) (2014).

11 Treas. Reg. § 1.165-1(b) (2014).

The requirement for a "closed and completed" transaction is met, as the Service observed in Revenue Ruling 2004-58, when the "taxpayer . . . show[s] both (1) an intention to abandon the asset, and (2) an affirmative act of abandonment."[12] The Service conceded that the taxpayer in *Pilgrim's Pride* satisfied these requirements.[13]

The amount of the loss should equal to the taxpayer's basis in the security.[14] Thus, ignoring the character of the loss, the taxpayer should have realized a $98.6 million loss in the abandoned securities equal to its basis.

Section 165(g)(1) provides as a general rule for capital loss treatment in the case of a worthless security stating that "(i)f any security which is a capital asset becomes worthless during the taxable year, the loss resulting therefrom shall, for purposes of this subtitle, be treated as a loss from the sale or exchange, on the last day of the taxable year, of a capital asset."[15] A security is defined for this purpose to mean

> (A) a share of stock in a corporation; (B) a right to subscribe for, or to receive, a share of stock in a corporation; or (C) a bond, debenture, note, or certificate, or other evidence of indebtedness, issued by a corporation or by a government or political subdivision thereof, with interest coupons or in registered form.[16]

In 2008, the Treasury Department promulgated Regulation section 1.165-5(i), which provides that an abandoned security is deemed worthless

---

12 Rev. Rul. 2004-58, 2004-1 C.B. 1043 (2004).

13 Opening Brief for Respondent at 16, Pilgrim's Pride Corp. v. Comm'r, 141 T.C. 533 (2013).

14 Section 165(b) provides that "[f]or purposes of subsection (a), the basis for determining the amount of the deduction for any loss shall be the adjusted basis provided in section 1011 for determining the loss from the sale or other disposition of property." I.R.C. § 165 (2014).

15 IRC § 165(g)(1) (2014). Thus, by deeming "a sale or exchange" to occur a necessary element for capital loss treatment under § 1222(10), is met. While not germane to *Pilgrim's Pride*, as noted, section 165(g)(1) only applies if the security is a capital asset. For example, it would be inapposite if the taxpayer were a dealer and held the security in its inventory. *See* I.R.C. § 1221(a)(1). Treas. Reg. § 1.165-5(b) provides that "[i]f any security which is not a capital asset becomes wholly worthless during the taxable year, the loss resulting therefrom may be deducted under section 165(a) as an ordinary loss." A major exception to the general rule of § 165(g)(1), is contained in § 165(g)(3) addressing securities in affiliated corporations. If the requirements of that section are met, the loss is an ordinary loss because the security is deemed not to be a capital asset. Treas. Reg. § 1.165-5(b) (2014).

16 *See* I.R.C. § 165(g)(2) (2014).

and thus generally comes within the capital loss rule of section 165(g)(1).[17] The regulation is legally inapplicable to *Pilgrim's Pride* because it is effective only to abandonment of stock or other securities after March 12, 2008.[18]

Ignoring both Treasury Regulation section 1.165-5(i) and the potential applications of sections 1234A or 165(g)(1), the latter two of which if pertinent would furnish the requisite "sale or exchange" treatment necessary for a net capital loss,[19] the abandonment of a security would generally give rise to an ordinary loss because of the lack of consideration received regardless of whether the security is a capital asset. As was observed by the Tax Court in *La Rue v. Commissioner*, "[t]he touchstone for sale or exchange treatment is consideration."[20]

If either section 1234A or section 165(g) were determined to be applicable to an abandonment of a security, then section 165(f) would come into play. Section 165(f) addresses capital losses providing that that "[l]osses from sales or exchanges of capital assets shall be allowed only to the extent allowed in sections 1211 and 1212."[21]

Section 1234A deems the requisite "sale" treatment for capital gains and losses to occur for certain transactions. Specifically, this includes generally the "[g]ain or loss attributable to the cancellation, lapse, expiration, or other termination of – (1) a right or obligation . . . with respect to property which is (or on acquisition would be) a capital asset in the hands of the taxpayer . . . ."[22] Had the Tax Court's holding in *Pilgrim's Pride* been affirmed, i.e., that section 1234A was applicable to an abandonment of the securities in question, the taxpayer would be denied an ordinary loss, but could avail itself of a capital loss pursuant to section

---

17 Abandonment of Stocks or Other Securities, 73 Fed. Reg. 13,124 (Mar. 12, 2008). The regulation was initially proposed in 2007. *See* Prop. Treas. Reg. § 1.165-5(i), 72 Fed. Reg. 41468 (July 30, 2007).

18 Treas. Reg. § 1.165-5(i)(2) (2014).

19 *See* I.R.C § 1222(10) (2014).

20 La Rue v. Comm'r, 90 T.C. 465,483 (1988). While not relevant to the taxpayer's fact-pattern, there are instances where an abandonment is a sale or exchange because consideration is received. Pursuant to Treas. Reg. § 1.1001-2(a), if abandoned property results in the taxpayer being relieved of liabilities, taxpayer would generally be treated as receiving consideration and thus regarded as a "sale or exchange." In Yarbro v. Comm'r, 737 F.2d 479 (5th Cir. 1984), *reh. denied*, 742 F.2d 1453 (1984), *cert. denied*, 469 U.S. 1189 (1985), the taxpayers abandoned property for the sole purpose of avoiding further property taxes and mortgage payments when the fair market value was exceeded by the outstanding debt. The Fifth Circuit held that even when the abandoned property contained only non-recourse debt, the loss was properly characterized as a capital loss because "an abandonment that is deemed to bring in return relief from a nonrecourse debt is a sale or exchange." *Id*. at 487.

21 I.R.C. § 165(f) (2014).

22 I.R.C. § 1234A (2002).

165(f) assuming it had sufficient capital gain to allow the loss to be utilized. [23]

In contrast, the Fifth Circuit, concluded that section 1234A (1) was inapposite because it determined that the section "only applies to the termination of contractual or derivative rights, and not to the abandonment of capital assets . . . ."[24] The taxpayer's predecessor had rejected $20 million offered to redeem certain securities it held, opting instead to abandon the securities and it expected obtain a $98.6 million ordinary loss. This was worth considerably more than $20 million that had been proposed by the issuer. In Tax Court, the taxpayer and the Service initially "focused their arguments on whether the abandonment caused the securities to become 'worthless' making the loss a capital loss . . . ." [25] The Tax Court, however, requested briefs on whether section 1234A applied and ultimately decided that it did.[26] The Fifth Circuit, however, reversed the Tax Court and found section 1234A to be inapplicable to an abandonment of a security.[27] The Court of Appeals also concluded that that the Service's alternative argument that capital loss treatment was mandated by section 165(g)(1) to be erroneous.[28]

There are a variety of statutory construction methodologies each with erudite proponents making very persuasive contentions. Applying an Internal Revenue Code section to a particular fact-pattern, however, it can often be wiser not to be wedded to one approach, e.g., textualism. Instead, it is submitted employing disparate methodologies depending on the particular circumstances may be sounder. *Pilgrim's Pride* provides a focal point for examining statutory interpretation methodologies and illustrating the foregoing. As such, reflecting on the case has continuing relevance despite the widespread application of Treasury Regulation section 1.165-5(i) to the abandonment of securities.

---

23 As noted above, in the absence of sufficient capital gains in the year of the capital loss, corporations can carry back net capital losses to three preceding years and carry forward such losses for five years. I.R.C. § 1212(a) (2010).

24 Pilgrim's Pride v. Comm'r, 779 F.3d 311, 312 (5th Cir. 2015), *rev'g* 141 T.C. 533 (2013).

25 *Id*. at 313.

26 *Id*.

27 Pilgrim's Pride Corp. v. Comm'r, 779 F. 3d 311 (5th Cir. 2015), *rev'g* 141 T.C. 533 (2013).

28 *Pilgrim's Pride*, 779 F.3d at 317-18.

II. PILGRIM'S PRIDE V. COMMISSIONER

A. *The Tax Court Decision*

The background to the case is as follows. The taxpayer is Pilgrim's Pride Corporation. In 1998, a predecessor of the taxpayer, Gold Kist Inc. ("GK Co-op") sold its agriculture services business to Southern States Cooperatives, Inc. ("Southern States") for $255 million for cash and assumption of certain liabilities.[29] In order to finance the acquisition, Southern States obtained a bridge loan that was secured by a commitment letter between Southern States and GK Co-op.[30] Pursuant to this commitment letter, Southern States had a period of time to raise $100 million through a public offering.[31] Under this arrangement, if Southern States failed to undertake the offering within the time provided, Southern States could elect to require GK Co-op to purchase certain Southern State securities.[32] As a result, "on October 5, 1999, GK Co-op purchased 40,000 shares of Step-Up Rate Series B Cumulative Redeemable Preferred Stock . . . of Southern States for $39.2 million and 60,000 shares of Step-Up Rate Capital Securities, Series A . . . issued by . . . [Southern States Capital Trust I, a Delaware statutory trust established by Southern States] for $59.4 million."[33] The aggregate total of these securities (collectively referred to as "Securities") was $98.6 million. The Securities met the definition of securities in section 165(g)(2).[34]

The Securities "generally provided for quarterly dividend payments that under certain circumstances could be unilaterally deferred by Southern States."[35] Southern States began deferring dividends on the Securities in 2002.[36] In 2004, Southern States offered to redeem the Securities for less than what GK Co-op had paid.[37] GK Co-Op's proposal of $31.5 million was rejected by Southern States, which countered $20 million.[38] At that time, i.e., 2004, "GK Co-op was planning to merge with and into its wholly owned subsidiary . . . and to take the company

29 *Pilgrim's Pride*, 141 T.C. at 537, n. 4.
30 *Pilgrim's Pride*, 779 F.3d at 312.
31 Opening Brief for Respondent at 4, Pilgrim's Pride v. Comm'r, 141 T.C. 533 (2013).
32 *Pilgrim's Pride*, 141 T.C. at 537, n.4.
33 *Id*. at 535-36 (footnotes omitted).
34 *Id*. at 537.
35 *Id*.
36 *Id.*
37 *Id*.
38 *Pilgrim's Pride*, 141 T.C. at 537.

public . . . ."[39] It also wanted "to remove [the Securities] . . . from its balance sheet before making the public offering."[40]

In May 2004, GK Co-op's Board of Directors determined that the best course of action was to reject Southern State's $20 million offer and instead abandon the Securities.[41] The Board did this based on its belief that the tax benefit of an ordinary loss of $98.6 million far exceeded the $20 million offered by Southern States.[42] On June 24, 2004 GK Co-op irrevocably surrendered the Securities to the issuers for no consideration.[43] It recorded a $38.8 million loss on its financial statements, which was at the time the value recorded by GK Co-op on its financial statements prepared in accordance with GAAP.[44] It claimed an ordinary loss of $98.6 million on its 2004 federal tax return.[45]

The Service in 2009 issued a notice of deficiency to the taxpayer on grounds that the loss was a capital loss and the taxpayer subsequently filed a petition in the Tax Court.[46] The taxpayer's position was that section 165(g) should be inapplicable because the securities had value when they were abandoned.[47] The Service asserted that the abandonment should be treated as a deemed sale pursuant to section 165(g) and as such should be characterized as a capital loss.[48] The Tax Court then issued a *sua sponte* order requesting briefs as to whether section 1234A was applicable and, if so, it would be a capital loss from the abandonment.[49]

As noted, Section 1234A provides in pertinent part that

> Gain or loss attributable to the cancellation, lapse, expiration, or other termination of—(1) a right or obligation . . . with respect to property which is (or on acquisition would be) a capital asset in the hands of the taxpayer . . . shall be treated as gain or loss from the sale of a capital asset.[50]

The taxpayer contended, "that under section 1234A a right or obligation with respect to property refers only to a contractual or other

---

39 *Id*.
40 *Id*.
41 *Id*.
42 *Id*.
43 *Id.* at 537-38.
44 *Pilgrim's Pride*, 141 T.C. at 537-38.
45 *Id*. at 538.
46 *Id*. at 539.
47 Opening Brief, *supra* note 31, at 19- 20.
48 Opening Brief for Respondent, *supra* note 13, at 14-21.
49 Pilgrim's Pride v. Comm'r, 779 F.3d 311, 313 (5th Cir. 2015).
50 I.R.C. § 1234A (2002).

derivative right to property and not property rights inherent in the ownership of the property."[51] The Tax Court rejected the taxpayer's assertion holding "that that the plain meaning of the phrase 'a right or obligation . . . with respect to property' encompasses the property rights inherent in intangible property as well as ancillary or derivative contractual rights."[52] In support of its position, the Tax Court reasoned that "[i]n its everyday usage the phrase 'rights with respect to property' includes the rights inherent in the ownership of the property, including stock."[53] Furthermore, the Tax Court noted that "[m]ost significantly, Congress has used the phrase 'with respect to property' in other provisions of the Code to include rights arising out of the ownership of the property or characteristics of the property."[54]

The Tax Court also rebuffed the taxpayer's contention:

> [T]hat the legislative history to the 1997 amendment of section 1234A [including no example of a termination of direct stock ownership] shows that Congress intended that section 1234A apply only to contractual and other derivative rights and obligations with respect to property and not to the inherent property rights and obligations arising from the ownership of the property.[55]

The Tax Court's response to the taxpayer's assertion was that "we do not think that the examples do more than show that section 1234A applies broadly to derivative contractual rights and obligations as well as inherent property rights."[56] The Tax Court also observed that "the Senate Finance Committee was critical of the existing law because it taxed similar economic transactions differently . . . ."[57] The court indicated that "[t]he intended effects [made by the Taxpayer Relief Act of 1997] of extending section 1234A to all types of property that are capital assets 'would be to remove the effective ability of a taxpayer to elect the character of gains and losses from certain transactions . . . .'"[58] The Tax Court also noted that an example in the legislative history involving the redemption of a bond is

---

51 *Pilgrim's Pride*, 141 T.C. at 542.
52 *Id*. at 544.
53 *Id*. at 543.
54 *Id*. at 544 (citing §§ 126(e), 704(c)(1)(A), 772(c)(3)(A), 877A(h)(1)(A), 954(i)(4)(A), 301(a), and 993(a)(1)(E)).
55 *Id*. at 545. Pursuant to The Taxpayer Relief Act of 1997, Congress amended section 1234A(1) by replacing the phrase "personal property (as defined in section 1092(d)(1)" with the term '"property." Pub. L. No. 105-34, § 1003(a), 111 Stat. 788, 909-910 (1997).
56 *Pilgrim's Pride*, 141 T.C. at 547.
57 *Id*. at 548.
58 *Id*.

further support for its position because "a bond which, like a share of stock, is intangible property--a bundle of contractual rights."[59]

The Tax Court also rejected the taxpayer's claim that amendments made in 2008 to Treasury Regulation section 1.165-5, promulgating Regulation section 1.165-5(i),[60] evidences that the Department of Treasury did not then subscribe to the belief that section 1234A was applicable to the abandonment of securities.[61] Treasury Regulation section 1.165-5(i), as noted above, provides in pertinent part that "[i]f the abandoned security is a capital asset and is not described in section 165(g)(3) . . . the resulting loss is treated as a loss from the sale or exchange . . . of a capital asset." In its dismissal of the taxpayer's contention, the Tax Court stated that "the regulation does not create an exception to section 1234A; it is the more specific provision of section 165(g)(3) that creates an exception for affiliated corporations. Thus, [Treasury Regulation] section 1.165-5(i) . . . gives effect to, and is consistent with, section 1234A . . . ."[62]

Finally, the Tax Court rejected the taxpayer's assertion that the Commissioner's failure to revise Revenue Ruling 93-80,[63] after the amendments to section 1234A under the Taxpayer Relief Act of 1997,[64] constitutes further support for its position that the provision is inapposite to the abandonment of securities. Revenue Ruling 93-80 holds that "[a] loss from the abandonment or worthlessness of a partnership interest will be ordinary if there is neither an actual nor a deemed distribution to the partner . . . ."[65] The Tax Court stressed that the ruling "was issued four years before section 1234A was amended in 1997 to apply to all property that is (or would be if acquired) a capital asset in the hands of the taxpayer."[66] Furthermore, the Tax Court commented that the Service "is not required to assert a particular position as soon as the statute authorizes such an interpretation, whether that position is taken in a regulation or in a revenue ruling."[67]

The Tax Court never addressed the applicability of section 165(g)(1) to *Pilgrim's Pride*. The taxpayer filed a motion for reconsideration, which

---

59 *Id*. at 547.

60 Abandonment of Stocks or Other Securities, 73 Fed. Reg. 13,124 (Mar. 12, 2008) (to be codified at 26 C.F.R. pt. 1).

61 *Pilgrim's Pride*, 141 T.C. at 549.

62 *Id*.

63 Rev. Rul. 93-80, 1993-2 C.B. 239 (1993).

64 Taxpayer Relief Act of 1997, Pub. L. No. 105-34, § 1003(a), 111 Stat 788, 909-910 (1997).

65 Rev. Rul. 93-80, 1993-2 C.B. 239 (1993).

66 *Pilgrim's Pride*, 141 T.C. at 550.

67 *Id*.

was denied.[68] The taxpayer subsequently appealed the Tax Court decision to the Fifth Circuit.

B. The Fifth Circuit Decision

On appeal, the decision of the Tax Court was reversed and the Fifth Circuit concluded that section "1234A(1) only applies to the termination of contractual or derivative rights, and not to the abandonment of capital assets . . . ."[69] The Court of Appeals observed that section 1234A was enacted as part of the Economic Recovery Tax Act of 1981[70] to address tax straddles, which it defined as "transactions in which taxpayers acquire offsetting contractual positions to obtain tax benefits without any economic risk."[71] The Fifth Circuit cited to an example in the legislative history wherein the "taxpayer simultaneously enter[ed] into a contract to buy German marks for future delivery and a contract to sell German marks for future delivery with very little risk."[72] Congress was concerned that under pre-section 1234A law, in the event of a decline in the price of German marks, taxpayer would cancel his obligation to buy the marks achieving an ordinary loss and obtain capital gain treatment from assigning his contract to sell the marks.[73]

The Fifth Circuit pointed out that the Service had conceded that section "1234A does not *directly* apply to the abandonment of a capital asset itself."[74] The Court of Appeals then rejected the Service's assertion that section 1234A "*indirectly* applies to the abandonment of a capital asset because the abandonment of a capital asset involves the termination of certain rights and obligations 'inherent in' those assets."[75] The Fifth Circuit indicated that "Congress does not legislate in logic puzzles . . . ."[76] The Court of Appeals quoted from the Supreme Court that it must "assume that 'the ordinary meaning of [statutory] language accurately expresses the legislative purpose."[77]

The Fifth Circuit also noted that the Service failed to identify "any other statute referring to so-called 'inherent rights, as 'rights[s] or obligation[s] with respect to a capital asset.'"[78] Furthermore, the Court of

---

68 Pilgrim's Pride v. Comm'r, 779 F.3d 311, 313 (5th Cir. 2015).

69 *Id*. at 312.

70 The Economic Recovery Act of 1981, Pub L. No. 97-34, § 507(a), 95 Stat. 172, 333 (1981).

71 *Pilgrim's Pride*, 779 F.3d at 314.

72 *Id*. at 315 (citing S. Rep. No 97-144, at 171 (1981).

73 *Id*. at 314-15 (citing S. Rep. No. 97-144, at 171 (1981)).

74 *Id*. at 315 (emphasis from the original).

75 *Id*. (emphasis from the original).

76 Pilgrim's Pride v. Comm'r, 779 F.3d 311 (5th Cir. 2015).

77 *Id*. (quoting Gross v. FBL Fin. Servs., Inc, 557 U.S. 167, 175 (2009)).

78 *Id*.

Appeals maintained that the Service had not cited any case that had interpreted section "1234A(1) –or any similarly worded statute—in the manner . . . [it] proposes."[79]

As the final nail in the coffin to the Service's contention regarding inherent rights, the Fifth Circuit commented that its argument would render section 1234A(2) "superfluous."[80] Section 1234A(2) provides for capital gain or loss treatment with respect "to the cancellation, lapse, expiration, or other termination of . . . (2) a section 1256 contract . . . which is a capital asset in the hands of the taxpayer."[81] The Fifth Circuit indicated that "the termination of any Section 1256 contract which is a capital asset would terminate those inherent rights and obligations . . . As a result § 1234A(2) would not serve any function."[82]

The Court of Appeals also dismissed the alternative argument put forward by the Service that section "165(g) requires Pilgrim's Pride's abandonment loss to be treated as capital."[83] The Fifth Circuit observed that the Service's position was irreconcilable with earlier decisions that it had rendered. The Court of Appeals quoted *Echols v. Commissioner* that "[p]roperty cannot be treated as worthless for tax purposes if at the time it, objectively, has substantial value."[84] Furthermore, the Court of Appeals commented that in a second Fifth Circuit decision that involved the same taxpayer, the court had stated that "[w]orthlessness and abandonment are separate and distinct concepts and are not, as urged by the Commissioner, simply two sides of the same coin . . . ."[85]

II. AN INTRODUCTION TO SOME STATUTORY INTERPRETATION METHODOLOGIES

In *Pilgrim's Pride*, the courts faced two provisions of the Internal Revenue Code, section 165(g)(1) and section 1234A, neither of which clearly address the tax consequence of an abandonment of a security and the strong possibility that the issue wasn't even considered when the provisions, or in the case of section 165(g)(1), its predecessor, was

---

79 *Id*.
80 *Id*. at 316.
81 I.R.C. § 1234A (2012).
82 *Pilgrim's Pride*, 779 F.3d at 316. The Court of Appeals notes in a footnote that the Service's interpretation of § 1234A is also inconsistent with two administrative actions by the Service. First, that Rev. Rul. 93-80 allowed an ordinary loss on the abandonment of a partnership interest, and second, that Treas. Reg. § 1.165-5(i) provides that an abandoned security is *per se* worthless resulting in a capital loss under § 165(g)(1). *Id*. at 317, n. 8.
83 *Id*. at 317.
84 *Id*. (quoting Echols v. Comm'r, 935 F.2d 703, 707 (5th Cir. 1991).
85 *Id*. (quoting Echols v. Comm'r, 950 F.2d 209, 211 (5th Cir. 1991).

enacted. Under these circumstances, how should a court interpret the meaning of these sections with respect to the issue at hand, i.e., the character of a loss upon the abandonment of a security having objective value? In this respect, it may be worthwhile to consider what some scholars have said about statutory interpretation and then to reflect on some methodologies for addressing the problem.

The late Professor Edward H. Levi, who served as Dean of the University of Chicago Law School, President of the University of Chicago, and Attorney General of the United States, wrote about judges that "[w]e mean to accomplish what the legislature intended . . . The difficulty is what the legislature intended is ambiguous."[86] In *United States v. Klinger*, Judge Learned Hand commented that

> When we ask what Congress 'intended,' usually there can be no answer, if what we mean is what any person or group of persons actually had in mind. Flinch as we may, what we do, and must do, is to project ourselves, as best we can, into the position of those who uttered the words, and to impute to them how they would have dealt with the concrete occasion. He who supposes that he can be certain of the result is the least fitted for the attempt.[87]

Professor Michael Sinclair observed that "[s]tatutory reasoning is the process by which a statute is brought to bear on a particular set of facts. Statutes are verbal formulations of some generality. Judicial decisions are particular. Therein lies the difficulty."[88]

The Supreme Court set forth in *United States v. Quality Stores, Inc.* that "[t]he beginning point [for applying a statute to particular case] is the relevant statutory text."[89] What, if any, the next steps should be is in some dispute. Professors Noel B. Cunningham and James R. Repetti wrote that "[s]cholars have identified four methods of statutory interpretation that courts have used: intentionalism, purposivism, textualism, and the

---

86 EDWARD H. LEVI, AN INTRODUCTION TO LEGAL REASONING 30 (2013, originally published 1949).

87 United States v. Klinger, 199 F.2d 645, 648 (2d Cir. 1952), *aff'd per curiam*, 345 U.S. 979 (1953).

88 MICHAEL SINCLAIR, GUIDE TO STATUTORY INTERPRETATION 17 (2013).

89 United States v. Quality Stores, Inc. 134 S.Ct. 1395, 1399 (2014). The Supreme Court has also stated that "[s]tatutory construction must begin with the language employed by Congress and the assumption that the ordinary meaning of that language accurately expresses the legislative purpose." Park 'N Fly, Inc. v. Dollar Park & Fly, Inc., 469 U.S. 189, 194 (1985).

practical reason (or dynamic) method."[90] Professors Cunningham and Repetti describe intentionalism as an approach that

> [S]eeks to determine what the legislature intended the statute to mean by examining committee reports and floor statements by sponsors. This method . . . reflects a view that in interpreting a statute, a court acts as the agent of Congress. Under this view, it is appropriate to consult legislative history, even where the statutory language is clear, to insure that the interpretation does not conflict with the legislature's intent . . . .[91]

In comparison, "t]he purposivist . . . does not inquire what the legislature intended the statute to mean, but rather asks what the statute's purpose was as the time of enactment in order to interpret the statute in a manner consistent with that purpose."[92] According to Professors Cunningham and Repetti, the key distinction one makes between intentionalism and purposivism

> [I]s that while the intentionalists try to determine what the legislature's intent actually was at the time of enactment, the purposivists try to determine what the statute would have meant at the time of enactment when read by a reasonably intelligent and informed reader.[93]

To accomplish this objective, the purposivist also considers legislative history.[94]

There is some dispute among the scholars as to what role legislative history should play in statutory construction and what constitutes valid legislative history for this purpose. According to Bradford L. Ferguson, Fredric W. Hickman, and Donald C. Lubick, in their article, *Reexamining the Nature and Role of Tax Legislative History in Light of the Changing Realities of the Process*, "[l]egitimate tax legislative history, insofar as it is explicit and specific, should be considered as having virtue parity with the statute itself."[95] Among their arguments for deference to legislative

---

90 Noel B. Cunningham & James R. Repetti, *Textualism and Tax Shelters*, 24 VA. TAX REV. 1, 7 (2004).

91 *Id*. at 7-8 (footnotes omitted).

92 *Id*. at 8 (footnote omitted).

93 *Id*.

94 *Id*.

95 Bradford L. Ferguson, Fredric W. Hickman & Donald C. Lubick, *Reexamining the Nature and Role of Tax Legislative History in Light of the Changing Realities of the Process*, 67 TAXES 804, 823 (1989). They defined "[l]egitimate [tax] legislative history" to "include . . . expressions of congressional intent set forth, in substantially similar forms,

history in federal taxation is that the Internal Revenue Code is the "lengthiest, most complex, most internally interrelated statute on the books today"[96] and that tax legislative history is "much more focused and comprehensive than legislative history in nontax areas."[97]

In contrast to the first two approaches, i.e., intentionalism and purposivism, "[t]he textualist . . . eschews all legislative history, considering it highly suspect."[98] Professors Cunningham and Repetti note that "[t]he textualist looks to the statute's language and other sources to identify the text's meaning."[99] A major proponent of textualism, or more aptly originalism,[100] the late Justice Antonin Scalia wrote in his concurring opinion in *Green v. Bock Laundry Machine Co.* that

---

in both the Ways and Means and Finance Committee reports, in the Statement of the Managers issued with respect to a conference report, or in orchestrated floor colloquies involving the respective bill managers." *Id.* They contrast this with post enactment explanations such as the Joint Committee on Taxation's Blue Book. *See also, e.g.,* United States v. Woods, 134 S. Ct. 557 (2013) where Justice Scalia, writing for the Court, stated with respect to consideration given Blue Books that

> Blue Books are prepared by the staff of the Joint Committee on Taxation as commentaries on recently passed tax laws. They are 'written after passage of the legislation and therefore d[o] not inform the decisions of the members of Congress who vot[e] in favor of the [law]' . . . . We have held that such '[p]ost-enactment legislative history (a contradiction in terms) is not a legitimate tool of statutory interpretation.' . . . .While we have relied on similar documents in the past, . . . our more recent precedents disapprove of that practice. Of course the Blue Book, like a law review article, may be relevant to the extent it is persuasive.

Id. at 568; *but see* Michael Livingston, *Congress, the Courts and the Code: Legislative History and the Interpretation of Tax Statutes*, 69 TEX. L. REV. 819, 885-86 (1991). Professor Livingston maintained

> [t]here is no clear line between contemporaneous and subsequent commentary on a tax bill . . . the Blue Book appears to be on similar ground with the committee reports: both are unenacted expressions of intent that are persuasive to the extent they explain the constitutionally enacted statute and less persuasive when they exceed this function.

Id. at 885-86 (footnote omitted).

96 Michael Livingston, *Congress, the Courts and the Code: Legislative History and the Interpretation of Tax Statutes,* 69 TEX. L. REV. 819 (1991).

97 *Id*.

98 Cunningham & Repetti, *supra* note 90, at 8 (footnote omitted).

99 *Id*.

100 Justice Scalia espouses "originalism," which is "the original public meaning of the text at the time of its enactment." *See* Randy E. Barnett, *Scalia's Infidelity: A Critique of 'Faint-Hearted' Originalism*, 75 U. CIN. L. REV. 7, 9 (2006). The reference in the title of the article was Justice Scalia's comment in an earlier lecture that "I hasten to confess that in a crunch I may prove a faint-hearted originalist. I cannot imagine myself, any more than any other federal judge, upholding a statute that imposes the punishment of flogging" even though it was not considered "cruel and unusual punishment" in 1791, i.e., at the time the Eighth Amendment became part of the Constitution. Antonin Scalia, *Originalism: The*

> The meaning of terms on the statute books ought to be determined, not on the basis of which meaning can be shown to have been understood by a larger handful of the Members of Congress; but rather on the basis of which meaning is (1) most in accord with context and ordinary usage, and thus most likely to have been understood by the *whole* Congress which voted on the words of the statute (not to mention the citizens subject to it), and (2) most compatible with the surrounding body of law into which the provision must be integrated—a compatibility which, by a benign fiction, we assume Congress always has in mind.[101]

Justice Scalia and Brian A. Garner in their book, *Reading Law: The Interpretation of Legal Texts*, asserted that "[a] system of democratically adopted laws . . . makes no sense . . . without the belief that words convey discernible meanings and without the commitment of legal arbiters to abide by those meanings."[102]

A court employing textualism "is not limited to examining the text of the statute, itself, and related statutes, but may also consult various textual authorities existing at the time of enactment, such as dictionaries, case law, and possibly treatises."[103] Justice Scalia declared that the textualist should pursue "'objectified' intent-the intent that a reasonable person would gather from the text of the law, placed alongside the remainder of the corpus juris."[104]

Lesser Evil, 57 U. CIN. L. REV. 849, 864 (1989). Justice Antonin Scalia and Professor Bryan Garner gave an example of and the rationale for "originalism" as follows:

> If you want to understand now what Queen Anne was saying about St. Paul's Cathedral, you do not ask what the phrase *awful, artificial, and amusing* means today. That alone is reason enough for using originalism to interpret private documents. But where public documents—constitutions, statutes, ordinances, regulations—are at issue, there is a still more important reason: Originalism is the *only* approach that is compatible with democracy.

ANTONIN SCALIA & BRYAN A. GARNER, READING LAW: THE INTERPRETATION OF LEGAL TEXTS 82 (2012) (emphasis in original).

101 Green v. Bock Laundry Machine Co., 490 U.S. 504, 528 (1989) (Scalia, J. concurring) (emphasis in original).

102 Antonin Scalia & Bryan A. Garner, *supra* note 100, at xxix.

103 Cunningham & Repetti, *supra* note 90, at 9 (footnote omitted).

104 ANTONIN SCALIA, COMMON-LAW COURTS IN A CIVIL-LAW SYSTEM: THE ROLE OF UNITED STATES FEDERAL COURTS IN INTERPRETING THE CONSTITUTION AND LAWS, IN A MATTER OF INTERPRETATION 3, 17 (Amy Gutmann ed., 1997). Justice Antonin Scalia and Professor Bryan Garner advised judges that when they interpret legislation they engage in "(1) giving effect to the text that lawmakers have adopted and that the people are entitled

Professors Cunningham and Repetti averred that "the ascendancy of textualism has had its greatest impact by facilitating the promotion and sale of 'abusive' tax shelters."[105] They were concerned that "textualism permits the attorney to ignore or reduce the importance of legislative history that would argue against the desired tax results [and that] . . . textualism challenges the validity of applying various judicial doctrines to complex statutory provisions."[106]

The fourth methodology, cited by Professors Cunningham and Repetti, i.e., practical reasoning or dynamic interpretation, was developed by Professors William N. Eskridge, Jr. and Philip P. Frickey.[107] According to Professors Cunningham and Repetti, this approach "holds that all three foundational methods are not only flawed but also do not reflect what the courts actually do."[108] Professors Cunningham and Repetti point out that this approach "does not reject the foundational methods per se, but rather 'refuses to privilege intention, purpose or text as the sole touchstone of interpretation.'"[109] Professors Eskridge and Frickey opine that a court should

> [L]ook at a broad range of evidence -- text, historical evidence, and the text's evolution -- and thus form a preliminary view of the statute. The interpreter then develops that preliminary view by testing various possible interpretations against the multiple criteria of fidelity to the text, historical accuracy, and conformity to circumstances and values. Each criterion is relevant, yet none necessarily trumps the others.[110]

Professor Eskridge in a later work indicated that the focus of the court should be

> [N]ot only what the statute means abstractly, or even on the basis of legislative history, but also what it ought to mean in terms of the needs and goals of our present day society . . . sometimes the circumstances will be

---

to rely on, and (2) giving no effect to lawmakers' unenacted desires." Scalia & Garner, *supra* note 100, at 29.

105 Cunningham & Repetti, *supra* note 90, at 20.

106 *Id*. at 62.

107 *See* William N. Eskridge, Jr. & Philip P. Frickey, *Statutory Interpretation as Practical Reasoning*, 42 STAN. L. REV. 321 (1990).

108 Cunningham & Repetti, *supra* note 90, at 9 (citing Eskridge & Frickey, s*upra* note 107, at 321-22).

109 *Id*. (quoting Eskridge & Frickey, *supra* note 107, at 345).

110 *Id*. at 9-10 (citing Eskridge &. Frickey, *supra* note 107, at 352).

> materially different from those contemplated by the statutory drafters, and in that event any application of the statute will be dynamic in a strong sense, going against the drafters' expectations, which have been negated because important assumptions have been undone.[111]

Other academics have used different terms for dividing the universe of statutory interpretation methodologies. For Professor William D. Popkin, a noted income tax as well as statutory construction scholar, there are two approaches, "pragmatism" and "anti-pragmatism."[112] He indicated that "in one camp are the pragmatists who view judging as a lawmaking partnership with the legislature."[113] He referred to Seventh Circuit Judge and prolific author Richard A. Posner and Professor Eskridge as "the best known advocates of pragmatic judging."[114]

Judge Posner defined his version of "a pragmatic approach to the law" as asking "judges to focus on the practical consequences of their decisions . . . ."[115] With respect to interpreting the Constitution, in criticizing textualism, Judge Posner commented that "[l]ike most judges, Supreme Court Justices prefer in their opinions to remain on the semantic surface of issues, arguing over the meaning of malleable terms such as 'public use' or 'cruel and unusual punishments' rather than over the consequences of adopting one meaning over another. Trying to decide what a term means by staring at it is a form of naval gazing."[116]

Professor Popkin notes that "the anti-pragmatists reach their conclusions by very different routes."[117] He writes that "[Justice Antonin] Scalia and [Harvard Law School Professor John] Manning are textualists who rely on various arguments that the Constitution prevents the judge from being a pragmatic lawmaking partner."[118] According to Professor Popkin, other anti-pragmatists include Harvard Law Professor Einer

---

111 WILLIAM N. ESKRIDGE, JR., DYNAMIC STATUTORY INTERPRETATION 50 n.7 (1994) (quoting Arthur Phelps, *Factors Influencing Judges in Interpreting Statutes*, 3 VAND. L. REV. 456, 469 (1950)).

112 WILLIAM D. POPKIN, THE JUDICIAL ROLE: STATUTORY INTERPRETATION & THE PRAGMATIC JUDICIAL PARTNER xi-xii (2013).

113 *Id*. at xi.

114 *Id*. In an earlier work, Professor Popkin advocated a "collaborative model of statutory interpretation." William D. Popkin, *The Collaborative Model of Statutory Interpretation*, 61 S. CAL. L. REV. 541, 543 (1988).

115 Richard A. Posner, *The Supreme Court, 2004 Term Foreword: A Political Court*, 119 HARV. L. REV. 31, 90 (2005) (footnote omitted).

116 *Id*. at 98-99. At least with respect to the application of pragmatism to Constitutional interpretation, he advocates the Supreme Court should be "restrained in the exercise of its power." *Id*. at 102.

117 Popkin, *supra* note 112, at xii.

118 *Id*.

Elhauge, who "adopts a version of intentionalism—what he calls judicial deference to 'enactable preferences,' stressing democratic values."[119]

Professor Popkin is firmly in the pragmatists school for construing a statute. He "argues that pragmatic judicial partnering is both descriptively accurate and normatively desirable. It describes and justifies judging as a creative act of judgment rather than discovery of the right answer in the text, legislative intent, or in a decision about policy consequences."[120] Professor Popkin asserted that this style of judging which is "persuasion through the transparent judicial opinion that acknowledges indeterminacy and the potential relevance of policy considerations" is superior to the alternative.[121]

Professor Paul R. Caron, another noted tax law scholar, splits the statutory interpretation world into three groups: "intentionalism", "purposivism" and "new textualism."[122] He writes that

> Under the traditional intentionalism approach, legislative history is used in conjunction with the statutory text to divine the legislative intent behind a particular provision. In contrast, the purposivism approach, as formulated by Professors Hart and Sacks, seeks to construe a statute in light of the goals the legislature had in mind when it enacted the statute. Finally, the new textualism approach of Judge Easterbrook and Justice Scalia places primary emphasis on the literal language of the statute.[123]

Professor Caron was critical of "[s]ome courts and commentators [that] have seized upon . . . [the tax law's] complexity and the nature of the tax legislative process to justify approaches to statutory construction that differ from those employed in construing nontax statutes."[124]

---

119 *Id*. Another leading anti-pragmatist Professor Popkin indicates is Harvard Law Professor Adrian Vermeule, who "is a literalist who does not base his approach on constitutional or democratic values. He instead relies on an institutional model of judging that emphasizes the more or less certain costs and uncertain benefits that judges encounter in trying to find the right answer . . . ." *Id.*

120 *Id*.

121 *Id*. at 81.

122 Paul L. Caron, *Tax Myopia, or Mamas Don't Let Your Babies Grow Up to Be Tax Lawyers*, 13 VA. TAX REV. 517, 540 (1994).

123 *Id*. (footnotes omitted) (referring to HENRY M. HART, JR. & ALBERT M. SACKS, THE LEGAL PROCESS: BASIC PROBLEMS IN THE MAKING AND APPLICATION OF LAW (10th ed. 1958); Frank H. Easterbrook, *The Role of Original Intent in Statutory Construction,* 11 HARV. J.L. & PUB. POL'Y 59 (1988); Antonin Scalia, *Assorted Canards of Contemporary Legal Analysis*, 40 CASE W. RES. L. REV. 581 (1989-90)).

124 *Id*. at 531.

Another noted tax expert, Professor Lawrence Zelenak, has promoted the position that in construing a statute, "[t]he statutory context may clearly indicate that the only sensible, logical interpretation is a nonliteral interpretation. If this is the case, the nonliteral interpretation should be regarded as the statute's meaning."[125] He maintained that "[n]onliteral interpretations are justified primarily, if not exclusively, when a statute must be applied to fact patterns that Congress did not consider when it enacted the statute."[126]

Professor Michael Livingston indicated he "would go further than [Professor] Zelenak"[127] in stressing the importance of context in interpreting an Internal Revenue Code provision. Professor Livingston stated "that contextual interpretation is not only appropriate in individual tax cases, but is in fact the dominant approach—and properly so—to tax interpretation."[128] He commented that "[f]ew if any tax terms have a 'plain' meaning that can be divorced from the statutory and decisional context in which the terms arise."[129] Professor Livingston asserted that contextual interpretation "in many respects follows the Hart and Sacks approach, identifying the underlying purpose of the statute and interpreting individual provisions consistently with that purpose."[130] He argued that legislative history has a vital role but that "[c]ourts [should] . . . restrict legislative history to its proper explanatory function . . . ."[131] He counselled against a court "refus[ing] to consider any legislative history, or, at the opposite extreme, if they seek to reconstruct the legislative process in deciding each tax case."[132]

III. OBSERVATIONS

A. Section 165(g)(1) and Abandonment of Securities

Had Regulation section 1.165-5(i) been promulgated prior to the abandonment of the Securities in 2004, this would have been an easy case for the courts to decide assuming the taxpayer continued to challenge

---

125 Lawrence Zelenak, *Thinking About Nonliteral Interpretations of the Internal Revenue Code*, 64 N.C.L. REV. 623, 637 (1986).

126 *Id*. at 659 (footnote omitted).

127 Michael Livingston, *Congress, the Courts and the Code: Legislative History and the Interpretation of Tax Statutes,* 69 TEX. L. REV. 819, 830 (1991).

128 *Id*. at 830-31.

129 *Id*. at 831.

130 *Id*. at 829.

131 *Id*. at 886.

132 *Id*. (advising Congress that they could assist the judiciary "by providing more of the 'why' and less of the 'how' in the legislative history").

capital loss treatment. The courts should and presumably would utilize the test set forth for deference to the judgment of an administrative agency by the Supreme Court in *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*,[133] i.e., "whether it is a reasonable choice within a gap left open by Congress"[134] and conclude the regulation met the test. Because the regulation was legally ineffective for the 2004 transaction, the courts faced a much more difficult but more thought-provoking exercise that required an analysis of the applicability of section 165(g)(1) and section 1234A. That is, should either section 165(g)(1) or section 1234A be interpreted as obligating the taxpayer to treat the loss as a capital loss?

Prior to the promulgation of Treasury regulation 1.165-5(i), there was certainly support, including both a revenue ruling as well as decisions in the Fifth Circuit, for the view that an abandonment of a security should be treated as an ordinary loss. Nevertheless, even prior to the effective date of Treasury Regulation section 1.165-5(i), a logical argument, consistent with some of the methodologies employed in statutory interpretation, can be made that a taxpayer, such as Pilgrim's Pride should not be accorded ordinary loss treatment under section 165(a) upon abandonment of securities, when a sale for the offered $20 million or any amount, no matter how small (but less than basis) would have resulted in a capital loss. That

---

133 *See* Chevron U.S.A., Inc. v. Natural Resources Def. Council, Inc., 467 U.S. 837 (1984).

134 *Id*. at 866. The often-quoted two-prong test for deference in *Chevron* is:

> [f]irst, always, is the question whether Congress has directly spoken to the precise question at issue. If the intent of Congress is clear, that is the end of the matter; for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress. If, however, the court determines Congress has not directly addressed the precise question at issue, the court does not simply impose its own construction on the statute, as would be necessary in the absence of an administrative interpretation. Rather, if the statute is silent or ambiguous with respect to the specific issue, the question for the court is whether the agency's answer is based on a permissible construction of the statute.

Id. at 842-43 (footnotes omitted). The other frequently cited passage from *Chevron* on deference is that "legislative regulations are given controlling weight unless they are arbitrary, capricious, or manifestly contrary to the statute." *Id*. at 844 (footnote omitted). In Mayo Foundation for Medical Education and Research v. United States, 562 U.S. 44, 45 (2011), the Supreme Court indicated this standard also applied to Treasury Department interpretative regulations. Mayo Found. for Med. Educ. and Research v. United States at 45. It should be noted, however, that on June 8, 2016, the House Judiciary Committee reported out H.R. 4768, the Separation of Powers Restoration Act of 2016, which, if enacted, according to a statement at the markup, by the Chairman of the Judiciary Committee, Rep. Robert "Bob" Goodlatte (R-VA) would "legislatively overturn . . . the *Chevron* doctrine." On July 12, 2016, the U.S. House of Representatives passed H.R. 4768. The House of Representatives passed a similar provision contained in the Regulatory Accountability Act of 2017, H.R. 5, on January 11, 2017.

is, section 165(g)(1) should be read to treat an abandoned security as worthless.

The case for this position is that had it focused on the issue when section 165(g)(1) and its predecessor was enacted, Congress would find, or at least should find, that ordinary loss treatment for an abandoned security, even if it has objective value prior to its abandonment, to be a "peculiar and anomalous result."[135] The policy rationale behind section 165(g)(1), i.e., that a taxpayer should not be accorded ordinary loss treatment when a security becomes worthless, but obtain a capital loss if the security is sold or exchanged for a *de minimis* amount of consideration, equally applies to a security abandonment. It makes no sense that a taxpayer can obtain a better tax treatment, i.e., ordinary loss vs. capital loss, by abandoning a security rather than by selling or exchanging it. Certainly, construing the statute in such a manner, i.e., an abandoned security is deemed worthless because it has no remaining value to the taxpayer, would be consistent with "conformity to contemporary circumstances and values."[136]

As discussed above, on its face, Treasury Regulation section 1.165-5(i) is not effective for *Pilgrim's Pride* since this regulation only applies prospectively, consistent with section 7805(b), "to any abandonment of stock or other securities after March 12, 2008."[137] Courts have refrained from applying a regulation prior to its effective date.[138] This does not mean that a court should be oblivious to the policy issues raised by the regulation.

As noted, one argument that abandoned securities should come within section 165(g)(1) and thus give rise to a capital loss is that by the taxpayer abandoning the securities, the securities have become worthless to it. That is, an abandoned security should be treated as per se worthless for purposes of section 165(g)(1). While the decisions involve different legal issues and concern the abandonment of a partnership interest and not a security, there

---

135 The language "peculiar and anomalous results" was cited in the Proposed Rulemaking for Prop. Reg. § 1.165-5(i) as follows:

> [t]he legislative history of the predecessor of section 165(g) indicates that the provision was enacted to remove the 'peculiar and anomalous results' that followed from treating losses from the worthlessness of securities as ordinary losses or deductions, and losses from the sale or exchange of securities as capital losses, because both losses represent a loss of capital in a transaction entered into for profit. *See* H. Rep. No. 1860, 75th Cong., 3d Sess., at 18-19 (1938).

72 Fed. Reg. 41468 (proposed July 30, 2007) (codified at 26 C.F.R. pt. 1).

136 Cunningham & Repetti, *supra* note 90, at 10 (citing Eskridge & Frickey, *supra* note 107, at 352).

137 Treas. Reg. § 1.165-5(i)(2) (2008).

138 *See, e.g.*, Hunter v. Comm'r, 87 T.C.M. (CCH) 1143 n.3 (2004).

is certainly somewhat adverse precedent to this position by the Fifth Circuit in *Echols v Commissioner* (referred to by the Fifth Circuit in *Pilgrim's Pride* and hereinafter as "*Echols II*")[139] and its predecessor (referred to hereinafter as "*Echols I*").[140] In Echols II, as quoted by the Fifth Circuit in *Pilgrim's Pride*, the court said "[w]orthlessness and abandonment are separate and distinct concepts and are not, as urged by the Commissioner, simply two sides of the same coin . . . ."[141]

In *Echols II*, the Fifth Circuit's denied the Service's petition for a rehearing requesting that the Fifth Circuit withdraw its original "alternate holding [in *Echols I*] that the taxpayers were entitled . . . to take a loss deduction under Code § 165(a) based on their determination, grounded in demonstrable facts, that their interest in the partnership was 'worthless.'"[142] The Court of Appeals rejected the Service's position "which, if accepted, would totally subsume 'worthlessness' in 'abandonment.'"[143]

In *Echols I*, the Fifth Circuit set forth that "a property cannot be treated as worthless for tax loss purposes if at the time it, objectively, has substantial value."[144] This obviously undermined the argument that an abandoned security having real worth prior to its abandonment can be considered worthless for purposes of section 165(g)(1). This was cited by the Fifth Circuit in *Pilgrim's Pride* for its rejection of the Service's alternative argument that "a security becomes 'worthless' when it is 'useless' to its owner, regardless of its market value."[145]

In *Echol*s I, the taxpayers (John C Echols and his wife Deanna O. Nichols) owned an interest (initially 37.5% but later 75%) in a Texas

---

139 *See*, Echols v. Comm'r, 950 F.2d 209 (5th Cir. 1991).

140 Echols v. Comm'r, 935 F.2d 703 (5th Cir. 1991).

141 Pilgrim's Pride Corp. v. Comm'r, 779 F.3d 311, 317 (5th Cir. 2015) (quoting *Echols*, 950 F.2d at 211).

142 *Echols*, 950 F.2d at 210.

143 *Id*. at 211 (indicating that "the Commissioner would have us hold that there can be no loss deduction under Code § 165 without either a transfer of title or an act of abandonment . . . . Despite the Commissioner's wishful thinking to the contrary, taxpayers are entitled to take loss deductions under Code § 165(a), not only for assets that the taxpayer has abandoned, with or without their having become worthless, but also for assets that have become worthless, with or without having been abandoned.").

144 *Echols*, 935 F.2d at 707.

145 *Pilgrim's Pride*, 779 F.3d at 317; *see* Reply Brief of Appellant at 22, Pilgrim's Pride Corp. v. Comm'r, 779 F.3d 311 (5th Cir. 2015) (No. 14-60295)(emphasis in original) (citing to Boehm v. Comm'r, 326 U.S. 287, 292-93 (1945); Genecov v. United States, 412 F.2d 556, 560-61 (5th Cir. 1969); Miami Beach Bay Shore Co. v. Comm'r, 136 F.2d 408, 409 (5th Cir. 1943)) (citing several additional cases in support of its argument that "securities must be *both* objectively and subjectively worthless to be considered worthless for purposes of section 165(g)," however the cited cases do not address the factual situation present in *Pilgrim's Pride*).

limited partnership whose only asset was a tract of unimproved real estate in Houston, Texas. A third party developer (hereinafter, "the Developer") also had an interest in this land. In 1976, the Developer defaulted on a payment owed for this land when its value had declined, and John Echols called a meeting of the partners, at which time he indicated he would no longer contribute funds needed for the mortgage and ad valorem payments due on the land. Eventually the land was foreclosed upon.

Near the outset of its analysis with respect to the character of the taxpayers' loss, the Fifth Circuit in *Echols I* stated that there was an important

> [D]istinction between 'abandonment' and 'worthlessness'; either concept can, under proper circumstances, justify a deduction pursuant to I.R.C. § 165(a), but each is different in theory, and the elements of one are separate and distinct from the elements of the other.[146]

The Fifth Circuit, in *Echols I* determined that the taxpayers were entitled to a loss deduction under section 165(a) on the basis of abandonment of their interest in the partnership as well as on the basis of worthlessness.[147]

The Service itself has recognized that abandonment and worthlessness are not always coterminous in that something can be worthless even though not abandoned. In Revenue Ruling 54-581, the Service held that if property became worthless in a prior year, "the taxpayer may not, by subsequent act of abandonment establish a deductible loss for the year of such abandonment."[148] Treasury Regulation section 1.165-2(a) reiterates this point by providing that "the taxable year in which the loss is sustained is not necessarily the taxable year in which the overt act of abandonment, or the loss of title to the property, occurs."[149]

In *Citron v. Commissioner*, the Tax Court held that an abandonment of a partnership interest resulted in ordinary loss.[150] The Tax Court observed that the court had "not, under the 1954 or later versions of the Internal Revenue Code, decided whether abandonment of assets (including partnership interests), where no partnership liabilities exist, results in ordinary, rather than capital, loss."[151] The Tax Court commented,

---

146 *Echols*, 935 F.2d at 706.
147 *Id*. at 709.
148 Rev. Rul. 54-581, 1954-2 C.B. 112
149 Treas. Reg. § 1,165-2(a).
150 Citron v. Comm'r, 97 T.C. 200, 200-01 (1991).
151 *Id*. at 215.

however, that it had decided "in the context of the Internal Revenue Code of 1939 . . . that abandonment (forfeiture) of a partnership interest was not a sale or exchange and could be accorded ordinary (rather than capital) loss treatment."[152] The Tax Court, furthermore, noted "[n]o changes were made in the loss provisions of the Internal Revenue Code of 1954 which would dictate a change in the case precedent under the 1939 Code."[153] It also pointed out that "[t]here is limited precedent, in other courts, under the Internal Revenue Code of 1954 that the worthlessness of a partnership interest (a capital asset) may result in an ordinary loss."[154]

Revenue Ruling 93-80,[155] like *Echols* decisions and *Citron*, also involved the abandonment and worthlessness of a partnership interest. The ruling examined two fact-patterns, one involving a deemed distribution to the taxpayer partner, in a situation, in which the partnership had nonrecourse liabilities in which the taxpayer partner shared and another in which the taxpayer limited partner "did not bear the economic risk of loss for any of the partnership liabilities in the basis of the partnership interest . . . [and] did not receive any money or property upon leaving the partnership."[156] While the Service concluded that the first fact-pattern resulted in a capital loss because "a deemed distribution" is made to the taxpayer partner in question, it determined that in the second situation, the taxpayer partner was entitled to an ordinary loss "because . . . [the partner] did not receive any actual or deemed distribution from the partnership."[157] While the Fifth Circuit in Pilgrim's Pride did not cite Rev. Rul. 93-80, and it did not involve an abandonment of a security, it too is arguably supportive of taxpayer's ordinary loss argument.

Notwithstanding Revenue Ruling 93-80, the decisions in *Echols* and *Citron*, the Service was not dissuaded from arguing in *Pilgrim's Pride* that a disposition of securities through abandonment resulted in a capital loss. The Service cited *Proesel v. Commissioner*[158] in support of its position that "an act of abandonment is an identifiable event that reflects the worthlessness of the property at that point to petitioner and fixes the loss."[159] *Proesel* is not a very persuasive precedent for this position. There is merely dicta in *Proesel*, a case involving taxpayer's worthless loss claim

---

152 *Id.* at 213.

153 *Id.*

154 *Id.*

155 Rev. Rul. 93-80, 1993-2 C.B. 239. Abandonment losses were also discussed in a later revenue ruling. Rev. Rul. 2004-54, 2004-1 C.B. 1043 (discussing whether there were effective acts of abandonment with respect to several factual situations relating to motion picture rights, although the ruling has limited applicability to the issues in *Pilgrim's Pride*).

156 Rev. Rul. 93-80, 1993-2 C.B. 239.

157 Rev. Rul. 93-80, 1993-2 C.B. 241.

158 Proesel v. Comm'r, 77 T.C. 992 (1981).

159 Opening Brief for Respondent, *supra* note 13, at 17.

from an involvement in a motion picture project through two layers of partnerships, that “an abandonment . . . reflect[s] the fact that the property is worthless.”[160]

Despite the somewhat adverse authority, and *Proesel* being of limited support, the Service’s position was far from baseless. While a security or other property can be worthless, without being abandoned, it does not necessarily follow that an abandoned security should not by such act alone not be deemed to be worthless. There is logic to the Service’s assertion that “the act of surrendering the securities established that they were worthless to Gold Kist . . . that the securities were of no ‘use’ or ‘profit’ to Gold Kist, i.e. useless.”[161] The Treasury Department’s Preamble to Proposed Regulation section 1.165-5(i) stated that

> The legislative history of the predecessor of section 165(g) indicated that the provision was enacted to remove the “peculiar and anomalous results” that followed from treating losses from the worthlessness of securities as ordinary losses or deductions, and losses from the sale or exchange of securities as capital losses, because both losses represent a loss of capital in a transaction entered into for profit.[162]

It would indeed be an anomaly for a taxpayer to be accorded capital loss treatment if he sells a security bought for $100 for $1 but would be entitled to an ordinary loss if the same security bought for $100 becomes worthless. Similarly, it is an anomaly that Pilgrim’s Pride should be in a better position after tax, by abandoning the Securities in question, than it would have been if its predecessor accepted the $20 million offered from

---

160 *Proesel*, 77 T.C. at 1005.

161 Brief for the Appellee at 55, Pilgrim’s Pride Corp. v. Comm’r, 779 F.3d 311 (5th Cir. 2015) (No. 14-60295).

162 Abandonment of Stock and Other Securities, 72 Fed. Reg. 41468 (proposed July 30, 2007)(to be codified at 26 C.F. R. pt.1). Interestingly, the citation provided there, H.R. Rep. No. 1860, at 18-19 (1938), does not specifically refer to “peculiar and anomalous results.” Neither does the citation for this language provided for by the IRS Chief Counsel in its Opening Brief at 14, Pilgrim’s Pride v. Comm’r, 141 T.C. 533 (2013)(No. 12089-10), i.e., H.R. Rep. No. 75-2330, at 44-46 (1938). Nevertheless, this language was in fact quoted in J.S. SEIDMAN, SEIDMAN’S LEGISLATIVE HISTORY OF FEDERAL INCOME TAX LAWS, 1938-1861, 12 (The Law Exchange, Ltd. 2003), referring to House Ways & Means Subcommittee Report, H.R. Rep. No. (1938). Section 23 of the Revenue Act of 1938 stated that

> [i]f any securities . . . are ascertained to be worthless and charged off within the taxable year and are capital assets, the loss resulting therefrom shall . . . be considered as a loss from the sale or exchange, on the last day of such taxable year, of capital assets.

Pub. L. No. 75-554, 52 Stat. 447 (1938).

Southern States. It is certainly bad public policy to encourage and subsidize taxpayers like Pilgrim's Pride to act in such a manner that is commercially irrational absent tax considerations. While Treasury Regulation 1.165-5(i) is not effective, courts should not be unmindful of the policy concerns raised by it. Like a proposed regulation, it is not entitled to deference prior to its effective date, but as the Tax Court indicated about proposed regulations, under certain circumstances, "they can be useful guidelines . . . ."[163]

In other words, why isn't it reasonable to follow the premise of Treasury Regulation section 1.165-5(i), despite its legal inapplicability to the tax year in question, and determine the worth of the security to be the subjective value to the taxpayer the second after its abandonment? There is nothing per se in section 165(g)(1) instructing one not to ascertain a security's worth by deeming it to be that of the taxpayer post abandonment nor any indication that Congress disfavored such an approach. Wouldn't a court's determination that section 165(g)(1) should characterize a security that is abandoned as worthless to the taxpayer and thus generally a capital loss be consistent with those who espouse dynamic statutory interpretation, i.e., what the provision "ought to mean in terms of the needs and goals of our present day society?"[164]

I do recognize that the logic of the position that an abandoned security should be treated as worthless can be arguably challenged as follows. When someone gifts an item, except in unusual circumstances, it has value. That is, it would not be considered worthless simply because the donated property no longer has value to the donor. Why shouldn't abandonment be treated similarly, i.e., a gift to the issuer that is not treated as worthless? I think there is a distinction between these fact-patterns. With a gift, while generally made out of "out of affection, respect, admiration, charity or like impulses,"[165] the donor presumably receives non-monetary consideration of value, i.e., the emotional satisfaction of giving to the donee. In this respect, the donor has retained in a sense continuing value from the property. This is different from an abandonment, which, unlike a donation, is done invariably solely, as exemplified by *Pilgrim's Pride*, to obtain a tax benefit. With an

---

163 *See, e.g.*, Seawright v. CIR, 117 T.C. 294, 300 (2001) (stating that "they can be useful guidelines where, as here, they closely follow the legislative history of the statutory provision in question."). *Id*. *Pilgrim's Pride*, 779 F.3d 311 (5th Cir. 2015) (stating that the final regulations do not follow the legislative history per se except arguably for eliminating another "anomaly" with loss characterization of securities).

164 Eskridge, *supra* note 111.

165 *See* Comm'r v. Duberstein, 363 U.S. 278, 285 (1960) (citing Robertson v. United States, 343 U.S. 711, 714 (1952)).

abandonment, there is no remaining value to the donor, excluding the tax subsidy.

From the vantage point of a purposivist, construing section 165(g)(1) as establishing the test of worthlessness of a security to be the subjective value to the taxpayer post abandonment would be reasonable. The overarching point of the section was for the "sale or exchange" requirement for capital loss treatment not to enable a taxpayer to have a more optimal tax result by having a security become worthless rather than selling it for a *de minimis* amount. One does not have to construe the provision very expansively to apply this same rationale to an abandoned security, which by such act no longer has any worth to the taxpayer. As Professor Popkin observed "the statute's coverage can be extended to cases not within the text's plain meaning in order to serve the statute's purpose."[166]

Craig W. Friedrich, in discussing the reason why Proposed Regulation section 1.165-5(i)[167] was issued, referred to a

> [S]tatutory accident [that] created a plain, if not rational, opportunity for tax planning that the fisc decided, quite reasonably in my view should not be there. Taxpayers and their advisors [are] seeking to avail themselves of the linguistic permission granted by the sale-or-exchange requirement by abandoning securities . . . .[T]he new rule . . . [is] giving effect to the legislative intent . . . .[168]

Friedrich believes that solution crafted, i.e., regulations to be effective prospectively upon finalization, was the correct way of addressing the problem.[169] I contend that a fact-pattern, like *Pilgrim's Pride*, can be viewed not as "statutory accident" but a situation simply not addressed in the four corners of the provision and that a court's "giving effect to the legislative intent . . .",[170] i.e., the purpose of the statute to address "anomalies" with respect to characterization of losses in securities, could, under certain circumstances, be proper.

Would such a result offend a textualist? Perhaps, since there is nothing in the statutory text that specifically treats an abandoned security having objective value prior to its abandonment as coming within the reach of

---

166 William D. Popkin, *The Collaborative Model of Statutory Interpretation,* 61 S. CAL. L. REV. 541, 604 (1988).

167 Abandonment of Stock and Other Securities, 72 Fed. Reg. 41468 (proposed July 30, 2007) (to be codified at 26 C.F.R. pt. 1).

168 Craig W. Friedrich, *Proposed Regs Make Abandonment of 'Securities' Sale-or-Exchange Under Section 165*, 35 CORP. TAX'N 45, 46 (2008).

169 *Id*.

170 *Id*.

section 165(g)(1). On the other hand, the statute is silent as to how one should test for worthlessness.

Absent Revenue Ruling 93-80,[171] I believe the courts should have distinguished *Echols I* [172] and *Echols II*[173] and other non-security decisions and treated the taxpayer's loss to be a capital loss. There is a question, however, if it would be equitable to do so when the taxpayer undoubtedly considered the guidance as well as court decisions discussed above when it undertook the transaction. A taxpayer should be entitled to rely on published IRS guidance. Revenue Procedure 89-14 provides in pertinent part "[t]axpayers generally may rely upon revenue rulings . . . in determining the tax treatment of their own transactions."[174] Revenue rulings are thus binding on the Service until revoked. The Tax Court has rebuked the Service for taking a litigating position contrary to a revenue ruling stating:

> [T]he IRS has committed itself "to increased and more timely published guidance," in the form of revenue rulings and revenue procedures, in the hopes of achieving increased taxpayer compliance and resolving "frequently disputed tax issues." These stated goals will not be achieved if the Commissioner refuses to follow his own published guidance and argues in court proceedings that revenue rulings do not bind him or that his rulings are incorrect. Certainly, the Commissioner's failure to follow his own rulings would be unfair to those taxpayers, such as petitioners herein, who have relied on revenue rulings to structure their transactions.[175]

The issue becomes whether a taxpayer could reasonably rely on a revenue ruling addressing the abandonment of a partnership interest to be applicable to that of a security. The Service does specifically caveat revenue ruling reliance stating that "[b]ecause each revenue ruling represents the conclusion of the Service regarding the application of law to the entire statement of facts involved, taxpayers . . . are cautioned against reaching the same conclusion in other cases unless the facts and

---

171 Rev. Rul. 93-80, 1993-2 C.B. 239.
172 Echols v. Comm'r, 935 F.2d 703 (5th Cir. 1991).
173 Echols v. Comm'r, 950 F.2d 209 (5th Cir. 1991).
174 Rev. Proc. 89-14, 1989-1 C.B. 815, § 7.01(5).
175 *See* Rauenhorst v. Comm'r, 119 T.C. 157, 183 (2002). In Estate of Delaune v. United States, 143 F.3d 995, 1005 (5th Cir. 1998), the Fifth Circuit stated "[a]s we recently held in Estate of McLendon . . . 'the Commissioner will be held to his published rulings in areas where the law is unclear, and may not depart from them in individual cases.'"

circumstances are substantially the same."[176] In *Pilgrim's Pride*, the taxpayer argued that "the general legal standards described in Revenue Ruling 93-80[177] regarding the abandonment of a partnership interest should be considered to be equally applicable to the abandonment of stock because stock, like a partnership interest, is an intangible asset."[178]

While Revenue Ruling 93-80[179] can be distinguished from *Pilgrim's Pride*, in the absence of other guidance differentiating it from losses from abandoned securities, it served to undermine its litigating position in *Pilgrim's Pride*. While it is a close question, for me it tipped the scales in taxpayer's favor. Had the ruling not been issued or had it been distinguished from an abandonment of securities, I believe the Service's position on this issue should have prevailed. One lasting lesson for the Service is that if it intends to litigate an issue, it should be very careful about clarifying published guidance that is at least arguably inconsistent with the view embraced in court.

As a final point, one can only speculate as to why the Tax Court did not specifically address the applicability of section 165(g)(1) to the *Pilgrim's Pride* fact-pattern. For one, the court might have believed that it would serve as a distraction to what it considered was its compelling analysis of section 1234A. Perhaps, it deemed section 165(g)(1) simply inapt. It could have been concerned about the precedent set by the Tax Court in *Citron*[180] and the possible application of the *Golsen* rule [181] by virtue of the Fifth Circuit decisions in *Echols I* [182] and *Echols II*,[183] or that taxpayer had undertaken the transaction in reliance of Revenue Ruling 93-80.[184] It would have been helpful, however, at least to legal scholars if the Tax Court addressed application of the section.[185]

---

176 Rev. Proc. 2016-4, 2016-1 I.R.B. 142, § 3.07.

177 Rev. Rul. 93-80, 1993-2 C.B. 239.

178 Brief for the Appellant at 38-39 (footnotes omitted), Pilgrim's Pride Corp., 779 F.3d 311 (5th Cir. 2015).

179 Rev. Rul. 93-80, 1993-2 C.B. 239.

180 *Citron*, 97 T.C. at 200.

181 Golsen v. Comm'r, 54 T.C. 742 (1970) (establishing a rule whereby the Tax Court is bound to follow the decisions of a court of appeals to which a particular case is appealable to).

182 *Echols*, 935 F.2d 703 (5th Cir. 1991).

183 *Echols*, 950 F.2d 209 (5th Cir. 1991).

184 Rev. Rul. 93-80, 1993-2 C.B. 239.

185 *Cf., e.g.,* Framatome Connectors USA, Inc. v. Comm'r, 118 T.C. 32 (2002), *aff'd without published opinion*, 108 F. App'x 683 (2d. Cir. 2004) (addressing a Tax Court case involving whether a foreign subsidiary was a controlled foreign corporation). After first holding that taxpayer could not prevail because it could not avail itself of the doctrine of substance over form, the court then spent considerable analysis determining that the taxpayer would also lose on the basis of the substance of the arrangement.

B. Section 1234A

Section 1234A is a conundrum of a provision that given the circumstance here, I believe, necessitates a different methodology for statutory interpretation than was advanced above for section 165(g)(1). Jasper L. Cummings, Jr. commented that

> Section 1234A suffers from multiple impediments: It is too brief, never explained by a regulation (the regulation proposed in 2004[186] is yet to be finalized and does not deal with the issues addressed here [or in *Pilgrim's Pride*], and located in the region of the code that tends to deal with derivatives, which causes everyone else to ignore it and the financial institutions and products folks to believe it was written just for them. In other words, section 1234A is a perfect setup for confusion.[187]

Professor David J. Roberts was also highly critical of section 1234A. He wrote that "[s]ection 1234A cries out for clarification . . . Whatever Congress intended, the entire provision was simply not well thought out."[188] Linda E. Carlisle, in a similar vein, declared that "section 1234A has increased uncertainty and muddied the treatment of some contract rights."[189]

In *Pilgrim's Pride*, both parties and courts embrace the concept of following the "plain terms"[190] and/or "plain meaning"[191] of the provision but not surprisingly, given the enigma of section 1234A, reached different conclusions. In its brief to the Fifth Circuit, the taxpayer stated, "[w]hen

---

186 Prop. Treas. Reg. § 1.1234A-1 (Mar. 29, 2004) covers payments to terminate notional principal contracts, bullet swaps, and forward contracts.

187 Jasper L. Cummings, Jr., *Reexamining Capital Gains for Real Estate*, 146 TAX NOTES 1409, 1413 (2015). While not directly relevant to the application of I.R.C. § 1234A to *Pilgrim's Pride*, there have been a few recent developments concerning the interpretation of I.R.C. § 1234A worth noting. In CRI-Leslie, LLC v. Comm'r, 147 T.C. No. 8 (2016), the Tax Court determined that I.R.C. § 1234A does not apply to section 1231 property. The IRS also provided guidance that it is now of the opinion that IRC § 1234A resulted in capital losses to the party that paid termination fees upon the breakup of a planned merger. *See* C.A.M. 2016-42035 (Feb. 9, 2016); F.A.A. 20163701F (May 3, 2016). This contrasts with older guidance by the Service holding that I.R.C. § 1234A does not result in capital gain treatment to the recipient of a termination fee. *See* I.R.S. Priv. Ltr. Rul. 140872-07 (Mar. 10, 2008).

188 *See* David J. Roberts, *Law Treating Certain Terminations as Sales Needs Clarification*, 150 TAX NOTES 337, 345 (2016).

189 Linda E. Carlisle, *Gain or Loss on Termination*, in James N. Calvin et al., *Examining the Straddle Rules After 25 Years*, 125 TAX NOTES 1301, 1320 (2009).

190 *See, e.g.*, *Pilgrim's Pride*, 779 F.3d at 315.

191 *See, e.g.*, *Pilgrim's Pride*, 141 T.C. at 542.

the language of the statute is clear on its face, it must be enforced according to its terms because 'courts must presume that a legislature says in a statute what it means and means in a statute what it says there.'"[192] The Service also cited the same quote in its brief to the Fifth Circuit, and followed with a further quote from *Connecticut National Bank v. Germain* that "[w]hen the words of a statute are unambiguous, then this first canon is also the last: 'judicial inquiry is complete.'"[193] While the Tax Court spent considerable analysis on what it believed to be Congress' intentions, it too declared that "[s]tatutes are to be construed so as to give effect to the plain meaning of the words in the text unless we find that a word's plain meaning is inescapably ambiguous"[194] and that "where a statute is clear on its face, we require unequivocal evidence of legislative purpose before construing the statute so as to override the plain meaning of the words used therein."[195] The Fifth Circuit, at the outset of its analysis, sets forth its conclusion that

> By its plain terms, § 1234A(1) applies to the termination of rights or obligations with respect to capital assets (e.g. derivative or contractual rights to buy or sell capital assets). It does not apply to the termination of ownership of the capital asset itself. Applied to the facts of this case, Pilgrim's Pride abandoned the Securities, not a "right or obligation . . . with respect to" the Securities.[196]

A textualist would be presumably pleased with the Fifth Circuit's persuasive analysis. I concur that it was the appropriate methodology in this instance.

As noted above, the Court of Appeals rejected the Service's assertion that section 1234A(1) should be germane to the taxpayer's fact-pattern on the basis that ownership of stock by its nature contains inherent rights that are the subject of section 1234A. The Court of Appeals held that "Congress does not legislate in logic puzzles, and we do not 'tag Congress with an extravagant preference for the opaque when the use of a clear adjective or noun would have worked nicely.'"[197] The Fifth Circuit also commented that the Service "does not provide us any reason to forego that

192 Brief for the Appellant, *supra* note 178, at 13 (citing Connecticut Nat'l Bank v. Germain, 503 U.S. 249, 253-54 (1992) and United States v. Ron Pair Enters., Inc., 489 U.S. 235, 241-42 (1989)).
193 Brief for the Appellee, *supra* note 161, at 21 (citing Connecticut Nat'l Bank v. Germain, 503 U.S. 249, 254 (1992)).
194 *Pilgrim's Pride*, 141 T.C. at 542.
195 *Id*.
196 *Pilgrim's Pride*, 779 F. 3d at 315.
197 *Id*. (citing Gutierrez v. Ada, 528 U.S. 250, 256 (2000)).

assumption"[198] that "the ordinary meaning of [statutory] language accurately expresses the legislative purpose."[199] The Fifth Circuit concluded that the Service's construction of the statute was "far too convoluted to believe Congress intended it."[200]

The Fifth Circuit, cited for support, *inter alia*, lines from a Bible for textualists and originalists, *Reading Law: The Interpretation of Legal Texts* by the late Justice Antonin Scalia and Bryan A Garner.[201] The Court of Appeals opined that "[t]he Commissioner's interpretation of § 1234A(1) also would render superfluous § 1234A(2), violating the rule of statutory interpretation that 'we are obligated to give effect, if possible, to every word Congress used.'"[202] That is, as noted above, the Fifth Circuit essentially asked why would it be necessary to enact section 1234A(2) if the Service's construction of section 1234A(1) was correct since under such interpretation "the termination of any section 1256 contract which is a capital asset would be covered . . . "[203] already by section 1234A(1).

The Court of Appeals was properly dismissive of the Service's assertion that section 1234A(2) was not "superfluous because it ensures that 'gain or loss from a deemed termination by offset will be treated as gain or loss from the sale of a capital asset.'"[204] The Fifth Circuit's reasoned that offsets are included in section 1234 A(1) by virtue of the words "or other terminations" in the opening line of section 1234A.[205] Furthermore, the Fifth Circuit correctly concluded that the Service's

---

198 *Id*.

199 *Id*. (citing Gross v. FBL Fin. Servs., Inc., 557 U.S. 167, 175 (2009)).

200 *Id*. at 316 (citing Chickasaw Nation v. United States, 534 U.S. 84, 90 (2001)). It is interesting to note that the Fifth Circuit's focus on textualism in construing I.R.C. § 1234A in contrast to a somewhat more intentualist approach by the Tax Court is consistent with Professor David F. Shores' review of tax litigation in the Tax Court and Court of Appeals between 2000 and 2006, where he concluded that the Tax Court is more likely to be more receptive to intentionalism theories while the Court of Appeals was found to have generally embraced textualism. David F. Shores, *Textualism and Intentionalism in Tax Litigation*, 61 TAX L. 53 (2007). Jasper Cummings recently observed that in the period from 2008- to 2015, while there was "a sharp decline in the number of reversals of Tax Court interpretations of statutes that the appellate court found to 'clearly' have a different meaning . . . the Tax Court was still on the intentionalist side of the interpretation and the appellate courts on the literalist side." Jasper L. Cummings, Jr., *Trending Literalism in the Tax Court*, 153 TAX NOTES 1461, 1466 (2016).

201 *See* Note 100, *supra* at 174. The Fifth Circuit's quote from the text was: "If possible, every word and every provision is to be given effect. None should needlessly be given an interpretation that causes it to duplicate another provision or to have no consequence." *Pilgrim's Pride Corp.*, 779 F.3d at 316.

202 *Pilgrim's Pride Corp.*, 779 F.3d at 316 (citing Reiter v. Sonotone Corp., 442 U.S. 330, 339 (1979)).

203 *Id*.

204 *Id*. (footnote omitted).

205 *Id*.

position "would require us to hold that § 1234A(2)'s only purpose is to address termination by offset, and that Congress chose a remarkably convoluted way to effectuate that purpose."[206]

Why was it proper for the Fifth Circuit to reach its decision *vis-à-vis* section 1234A using a textualist approach but this methodology was unsuitable for construing section 165(g)(1)? I would argue that unlike section 165(g)(1), except for some legitimate questions about what Congress intended when section 1234A was amended by the Taxpayer Relief Act of 1997,[207] there was no compelling policy reason for deviating from the construing section 1234A in conformity with the plain meaning of the text. That is, if one examines the intention and purpose of the provision as well as how it should apply from a policy standpoint by "what it ought to mean in terms of the needs and goals of our present day society,"[208] including the existence already in the Internal Revenue Code of section 165(g)(1), there does not seem to be a convincing case that it should not be deemed to impose a sale on the abandonment of a security.

I am not unmindful of the justifiable concern raised by Professors Cunningham and Repetti, as well as others, that "[t]he ascendancy of textualism has had its greatest impact by facilitating the promotion and sale of 'abusive' tax shelters."[209] An example of how utilizing a textualist methodology can serve to permit a taxpayer to obtain an unjustifiable tax benefit is the recent Sixth Circuit decision *Wright v. Commissioner*.[210] The case dealt with section 1256, another section, like section 1234A, enacted as part of the Economic Recovery Tax Act of 1981[211] that addressed tax abuse with financial instruments. A textualist approach was employed in interpreting the statute in a manner that blatantly ignored the policy concerns of the provision. In *Wright*, the taxpayers "claimed a large tax loss by marking to market a euro put option upon the . . . [taxpayers'] assignment of the option to charity."[212] The Sixth Circuit acknowledged that the "transactions [undertaken] appear to have allowed the . . . [taxpayers] to generate a large tax loss at minimal economic risk or out-of-pocket expense."[213]

---

206 *Id*.

207 Taxpayer Relief Act of 1997, Pub. L. No. 105-34, § 1003, 111 Stat.788, 909-910 (1997).

208 Eskridge, *supra* note 111, at 50, n.7.

209 Cunningham & Repetti, *supra* note 90, at 20.

210 Wright v. Comm'r, 809 F.3d 877 (6th Cir. 2016).

211 The Economic Recovery Tax Act of 1981, P.L. 97-34, 95 Stat. 172 (1981).

212 *Wright*, 809 F.3d at 878.

213 *Id*. The Sixth Circuit, quoting from the Service's brief, described the tax shelter strategy utilized in *Wright* as follows:

> The major-minor tax shelter was designed to manipulate the mark-to-market rules . . . . The taxpayer arranges with a counterparty for four

The issue in *Wright* was whether an over-the-counter option in a major currency, was a "foreign currency contract" within the meaning of section 1256(g)(2)(A) as taxpayer contended, allowing them to trigger large tax losses on the-mark-to-market rules of section 1256. The Sixth Circuit reversed the Tax Court, which had held for the Service. The Sixth Circuit stated that "the Tax Court's reasoning [finding section 1256(g)(2)(A) inapplicable] appears to be supported by sound tax policy, but nonetheless conflicts with the plain language of § 1256."[214]

In reaching its conclusion, the Sixth Circuit rejected the need to examine the provision's legislative history,[215] and ignored the fact that "no conceivable tax policy . . . supports this interpretation of the plain language of § 1256 . . . ."[216] This statement presumably would make a pragmatist, like Judge Posner, cringe. Jasper L. Cummings Jr. was very disparaging of this statement that Cummings indicated "bragged" about this ignorance of any tax policy concerns.[217] Cummings condemned the blind textualism employed in Wright with the comment that "if appellate judges do no more than parse the grammar of statutes, they might as well

---

> OTC [over-the-counter] options. The taxpayer buys from the counterparty a euro call and a euro put on mirror-image terms. The taxpayer also sells to the counterparty a krone call and a krone put on mirror-image terms. The premiums paid to and received from the counterparty mostly offset each other. Because the call and put for each currency are mirror images of each other, one will rise while the other will fall. Because the krone is closely tied to the euro, both calls should largely offset each other, as should both puts. The taxpayer and the counterparty then retain their premiums, but the taxpayer assigns to a charity his rights and obligations under the depreciated euro option and the appreciated (and offsetting) krone option (*i.e.*, the charity receives both calls or both puts). The taxpayer asserts that the assignment of the losing euro option is a recognition event under § 1256(c)(1), and he invokes the mark-to-market rules to claim a loss . . . . Because [the taxpayer takes the position that] the krone option is not a § 1256 contract, the taxpayer recognizes gain, if ever, when his obligation to perform is terminated by the closing or lapse of the option. The taxpayer and the counterparty then terminate the unassigned options so that the gain on one offsets the loss on the other. If the taxpayer's reading of § 1256 is correct, he receives a large tax loss with minimal economic risk or out-of-pocket expense. Moreover, because the options are offsetting and can be settled in dollars, the nominal amounts of foreign currency can be set well beyond the means of the parties, so as to generate the tax loss desired by the taxpayer.

Id. at 880.

214 *Id*. at 882.

215 *Id*. at 884.

216 *Id*.

217 Jasper L. Cummings, Jr., *Are Judges Just English Teachers?*, 151 TAX NOTES 1553 (2016).

be English teachers and not lawyers."[218] The Sixth Circuit clearly did not adhere to the advice of Judge Posner to "focus on the practical consequences of their decision . . . ."[219]

One other aspect of the *Wright* decision is worth mentioning relating to a self-inflicted wound on the part of the Service. This is somewhat comparable to concerns expressed herein regarding both the issuance of Revenue Ruling 93-80[220] without distinguishing guidance until 2007 relating to the characterization of losses upon the abandonment of securities, as well as the failure to promulgate regulations under section 1234A addressing the issue at hand. While Cummings and others justifiably criticized the Wright decision,[221] the Sixth Circuit was correct in faulting the Service for the failure to issue regulations "that excludes foreign currency options from the definition of a 'foreign currency contract.'"[222] John Kaufmann commented about *Wright* that

> Regardless of the merits of the 'plain meaning' argument, the estoppel argument made by the court near the end of the opinion seems to be a winner. When Congress passed the 1982 act, it granted the IRS the authority to issue regulations interpreting the meaning of the term 'foreign currency contract.' The IRS knew that there was a difference of opinion regarding the interpretation of the term, and it had the power to clarify that foreign currency options do not constitute foreign currency contracts simply by declaring so in a regulation. The IRS can hardly complain that it lost a case because it sat on the right to settle the issue in its favor for 34 years.[223]

While denying ordinary loss treatment on the abandonment of a security could and should have been dealt with prior to the effective date of 1.165-5(i), by a somewhat expansive interpretation of section 165(g)(1), this was thwarted by the Service's issuance of Revenue Ruling 93-80[224] without other guidance distinguishing it from a security abandonment. Unlike the partnership provisions that Professors Cunningham and Repetti

---

218 *Id*.
219 Posner, *supra* note 115, at 90.
220 Rev. Rul. 93-80, 1993-2 C.B. 239.
221 *See, e.g.*, William R Davis, *Court Decision Spurs Foreign Currency Option Treatment Debate*, TAX NOTES TODAY (Mar. 10, 2016).
222 Wright v. Comm'r, 809 F.3d 877, 885 (6th Cir. 2016).
223 John Kaufmann, *Sixth Circuit Follows Plain Meaning; Tax Bar Up in Arms*, 150 TAX NOTES 923, 926 (2016).
224 Rev. Rul. 93-80, 1993-2 C.B. 239.

allude to,[225] the ordinary loss on abandonment of securities was not created by section 1234A, and it should not serve as the proverbial finger in the dyke when there was, I believe, a more artful method for solving the problem, absent the Service's misstep.

In terms of the legislative history to section 1234A, it was enacted in 1981 as part of the provisions addressing tax straddles in the Economic Recovery Tax Act of 1981.[226] As originally enacted section 1234A provided:

> Gain or loss attributable to the cancellation, lapse, expiration or other termination of a right or obligation with respect to personal property (as defined in section 1092(d)(1)) which is (or on acquisition would be) a capital asset in the hands of the taxpayer shall be treated as gain or loss from the sale of a capital asset.[227]

The key wording insofar as to whether or not section 1234A should apply to the abandonment of a security, i.e., "cancellation, lapse, expiration or other termination of a right or obligation with respect to property" was never revised. According to the legislative history of the Economic Recovery Tax Act of 1981, section 1234A was enacted because "the change in the sale or exchange rule is necessary to prevent tax-avoidance transactions designed to create fully-deductible ordinary losses on certain dispositions of capital assets, which if sold at a gain, would produce capital gains."[228] Congress was concerned that "[s]ome taxpayers and tax shelter promoters have attempted to exploit court decisions holding that ordinary income or loss results from certain dispositions of property whose sale or exchange would produce capital gain or loss."[229] Its target was apparently a limited class of capital assets and transactions including "ordinary loss and capital gain transactions [that] involve cancellations of forward contracts for currency or securities."[230]

Linda E. Carlisle reflected on the background to section 1234A as follows:

> Before 1981, commodity transactions were used to create "silver butterflies," "gold cash-and-carry transactions," and "T-bill rolls" to defer and convert ordinary income

225 Cunningham & Repetti, *supra* note 90, at 20-63.

226 The Economic Recovery Tax Act, Pub L. No. 97-34, § 507(a), 95 Stat. 172, 333 (1981).

227 *Id*.

228 H.R. Rep. No. 97-201, at 212 (1981).

229 *Id.*; *see also* S. Rep. No. 97-144, at 170 (1981).

230 *Id*.

> into capital gains. In June 1980, however, the process of tax reform in the commodity area began, and the butterflies began to take flight.
>
> The Economic Recovery Tax Act of 1981 (ERTA) enacted a set of new rules to reform the world of financial transactions, which at that time consisted mainly of commodity derivative transactions. ERTA dealt comprehensively with commodity transactions by imposing the recognition of losses on straddle positions under section 1092, requiring regulated futures contracts to be marked to market under section 1256, requiring the capitalization of interest and carrying charges for straddle positions under section 263(g), and settling the "confusion" that had arisen regarding the treatment of some contract rights under section 1234A.[231]

A forerunner to the enactment of section 1234A, was proposed legislation introduced by Senator Daniel P Moynihan. Senator Moynihan's bill, if enacted, would have addressed the character arbitrage in straddle transactions by incorporating a very broad definition of "sale or exchange" in section 7701(a) that would have provided that "[t]he term 'sale or exchange' when used with reference to any capital asset means any disposition of such asset."[232] The legislative history does not explain why Congress chose to address the perceived abuse differently.

There is also a possible disconnect between how both the House Ways and Means and Senate Finance Committee reports accompanying the Economic Recovery Tax Act of 1981 described the tax loss character manipulation section 1234A was intended to address and the final language of the provision. The Congressional reports in describing the problem indicated that

> [A]s a result of these interpretations, losses from the termination, cancellation, lapse, abandonment and other dispositions of property, which are not sales or exchanges of the property, are reported as fully deductible ordinary losses instead of as capital losses.[233]

---

231 Carlisle, *supra* note 189, at 1319-20.

232 Commodity Straddles Tax Act of 1981, S. 626, § 6 (1981).

233 H.R. Rep. No. 97-201, at 212 (1981); *see also* S. Rep. No. 97-144, at 170 (1981). It should also be noted that the word "abandonment" was also not included in the group of actions triggering the operative provision of the section.

Nevertheless, section 1234A, as enacted, was more narrowly crafted, i.e., it only addressed "gain or loss attributable to the cancellation, lapse, expiration or other termination of *a right or obligation* with respect to personal property . . . ."[234]

There were a number of modifications to section 1234A after 1981 but, very significantly, the term "right or obligation with respect to" was never altered. Shortly after its enactment, Congress made a technical correction to section 1234A, adding section 1234A(2), to have it also apply to "a regulated futures contract (as defined in section 1256) not described in paragraph (1), which is a capital asset in the hands of the taxpayer . . . ."[235] This change was made in association with a revision to section 1256 which removed the condition that a contract must require delivery of "personal property," as defined in section 1092(d)(1), to be treated as a regulated futures contract.[236] Unlike 1234A(1), Section 1234A(2) as both initially enacted and as written throughout its history does not refer to "a right or obligation."[237]

The Deficit Reduction Act of 1984 made further revisions to 1234A.[238] With respect the *Pilgrim's Pride* fact-pattern, more scrutiny is required as to the changes made to section 1234A by the Taxpayer Relief Act of

---

234 The Economic Recovery Tax Act, Pub L. No. 97-34, § 507(a), 95 Stat. 172, 333 (1981) (emphasis added).

235 Technical Corrections Act of 1982, Pub. L. No. 97-448, § 105(e), 96 Stat. 2365, 2387 (1983).

236 *Id*. at 2365, 2385.

237 According to Linda Carlyle,

> Congress was concerned that those contracts, which settle only in cash, would not be treated as rights or obligations regarding capital assets because cash is not a capital asset. The legislative history makes it clear that capital gain or loss treatment under section 1234A(1) was based on the termination of contracts with respect to *property* that is, or on acquisition would be, a capital asset in the hands of the taxpayer.

Carlisle, *supra* note 189, at 1320. In a recent thought-provoking article on section 1234A, Professor David J. Roberts raises the question as "[w]hen section 1234A(1) refers to 'a right or obligation . . . with respect to property which is (or on acquisition would be) a capital asset,' what is supposed to be the capital asset- the right or obligation, or the property itself?" He answers his question that "[p]resumably it is the property itself . . . . But how sure are we of this?" *See* Roberts, *supra* note 3, at 338.

238 The Deficit Reduction Act of 1984, Pub. L. No. 98-369, 98 Stat. 494 (1984). One change made was that Section 1234A(2) was amended to delete the phrase "a regulated futures contract" and replace it with "a section 1256 contract." *Id*. § 102(e)(4), 98 Stat. 494, 624 (1984). This was made in connection with section 1256's amendment to apply to additional financial contracts. *Id.* § 102(a)(2), 98 Stat. 494, 620 (1984). Another change made by the Deficit Reduction Act of 1984 was the addition of a final sentence, effective as if included in the original provision, clarifying that section 1234A would "not apply to the retirement of any debt instrument (whether or not through a trust or other participation arrangement)." *Id*. § 102(e)(9), 98 Stat. 494, 625 (1984). The word "arrangement" was subsequently changed to "agreement."

1997.[239] In 1997, Congress amended Section 1234A(1) by substituting the phrase "personal property (as defined in section 1092(d)(1)" with the term "property."[240]

The Senate Finance Committee Report, in explaining the reason for the amendment, stated that it "believes that present law is deficient since it (1) taxes similar economic transactions differently, (2) effectively provides some, but not all, taxpayers with an election [as to the character of the gain or loss], and (3) its lack of certainty makes the tax laws unnecessarily difficult to administer."[241] The Senate Finance Committee also pointed out that "some transactions, such as settlements of contracts to deliver a capital asset, are economically equivalent to a sale or exchange of such contracts since the value of any asset is the present value of the future income that such asset will produce."[242]

The taxpayer characterized the change as "cover[ing] contractual and other derivative rights with respect to all types of property, not just publicly traded personal property."[243] Section 1234A's scope was certainly expanded by the 1997 statutory modification. Thus, after this amendment to the provision, section 1234A(1) was applicable to "cancellation, lapse, expiration, or other termination of a right or obligation" of any property, including real property, and non-actively traded personal property, assuming the property" is (or on acquisition would be) a capital asset in the hands of the taxpayer." The original limitation of section 1234A(1) to a "right or obligation with respect to" such property, was, however, not removed from the provision. That is, the amendments made in 1997 retained the restriction as to its applicability to "the cancellation, lapse, expiration, or other termination of a right or obligation . . . with respect to property which is (or on acquisition would be) a capital asset . . . ."

Did Congress intend that the amendment would broaden section 1234A(1) to cover the abandonment of a security? It certainly did not

---

239 The Taxpayer Relief Act of 1997, Pub. L. No. 105-34, § 1003(a), 111 Stat. 788, 909-10 (1997).

240 *Id*.

241 S. Rep. No. 105-33, at 134 (1997).

242 *Id*.

243 Brief for the Appellant, *supra* note 178, at 28 (footnote omitted). H.R. Rep, No. 105-148 explained that Congress was concerned that

> to the extent that present law treats modification of property rights as not being a sale or exchange, present law effectively provides, in many cases, taxpayers with an election to treat the transactions as giving rise to capital gain, subject to more favorable rates than ordinary income, or ordinary loss that can offset higher-taxed ordinary income and not be the subject to limitations on use of capital losses.

Id. at 453.

specifically mention this transaction in the legislative history. There is, I believe, a legitimate question, as to what exactly Congress envisioned by the 1997 changes. Did they mean for the section to expand beyond derivatives? If so, why were the words "right or obligation with respect to" property retained? Perhaps this was faulty drafting, but alternatively it is also quite plausible that the scope of its objective was more limited.

In arguing for applying section 1234A to the abandonment of a security, the Tax Court referred to the fact that the Senate Finance Committee report cited *Fairbanks v. United States*,[244] where the Supreme Court held that gain realized on the redemption of bonds before their maturity was not entitled to capital gain treatment because the redemption was not a "sale or exchange."[245] The Tax Court stated that "[t]he example of a redemption of a bond is most significant given that Congress had long since overturned the result in Fairbanks by enacting the predecessor of section 1271(a) in the Revenue Act of 1934 . . . ."[246] The Service asserted that "[t]he citation of *Fairbanks* as an example in the legislative history demonstrates that Congress was concerned about court decisions addressing termination of rights inherent in property and not merely derivative rights."[247] The point regarding *Fairbanks* is certainly not unfounded. There is some discrepancy between the legislative history to the changes made to section 1234A in 1997 and the literal language of the amended section. Furthermore, there may be justifiable policy reasons for section 1234A to mandate capital treatment not only for rights and obligations in securities but for the security itself.

In contrast to the Service's position, the taxpayer described the legislative history to the section 1234A amendment to the Taxpayer Relief Act of 1997[248] as follows:

> The House Committee on the Budget restated some of the same issues addressed in the legislative history to the 1981 Act, broadly described the sale or exchange requirement, and then went on to focus specifically on the termination of contractual interests or the modification of property rights under contracts where the asset underlying the contract is a capital asset.[249]

---

244 Fairbanks v. United States, 306 U.S. 436 (1939).
245 *Pilgrim's Pride*, 141 T.C. at 546; *see also* Brief for the Appellee, *supra* note 192, at 42-43.
246 *Id*. at 547-48.
247 *See supra* note 161, at 47.
248 The Taxpayer Relief Act of 1997, Pub. L. No. 105-34, § 1003(a), 111 Stat. 788 (1997).
249 *See supra* note 178, at 28 (citing H.R. Rep. No. 105-148, at 451-55(1997)).

The taxpayer also observed that the reference in the legislative history to *U.S. Freight Co. v. United States*[250] is proof that Congress envisioned that section 1234A continue to target derivatives because:

> The stock example used by Congress solely involved a *contract to purchase stock*, and not the direct ownership of the stock itself. Had Congress intended to cover the termination of direct ownership of stock, one has to presume Congress would have provided an example of a termination of direct ownership. [251]

While the foregoing is hyperbole on the part of the taxpayer, absent a clear indication that the text of the statute did not mirror Congressional objectives, I believe one should be reticent to assume the latter.[252] If the language did not reflect what it intended, why wasn't it amended through a technical correction or otherwise? Furthermore, regulations should have been promulgated incorporating the Service's interpretation of section 1234A to "inherent" rights.[253] Additionally, it is certainly not a situation where "[t]he statutory context . . . clearly indicate[s] that the only sensible, logical interpretation is a nonliteral interpretation."[254] Finally, as was discussed, absent the issuance of Revenue Ruling. 93-80, [255] there was, under my analysis, a statutory vehicle for addressing the abuse in this case already in place in the form of section 165(g)(1). Thus, while admittedly I am not free from doubt, I believe Fifth Circuit was correct in finding section 1234A inapplicable to *Pilgrim's Pride*.

With respect to the failure to promulgate regulations under section 1234A, I recognize that the same criticism could be leveled toward my view that, absent the issuance of Revenue Ruling 93-80,[256] a court should have held the abandonment resulted in a capital loss even prior to Treasury

---

250 U.S. Freight Co. v. United States, 422 F.2d 887 (Ct. Cl. 1970).

251 *See supra* note 178, at 29 (emphasis in the original; footnote omitted) (citing H.R. Rep. No. 105-148, at 454 (1997); S. Rep. No. 105-33, at 135-36 (1997)).

252 Several commentators, writing both before and after the Fifth Circuit decided *Pilgrim's Pride* indicated they believed § 1234A should not apply to the abandonment of securities. *See, e.g.*, Michael J. Kliegman and Anna Turkenich, *Worthless Stock or Securities: Timing and Character Issues Revisited*, 111 J. TAX'N 70 (2009); Gerald V. Thomas II, *The Art of Abandoning Securities and Taking an Ordinary Loss*, 104 J. TAX'N 22 (2006); William M. Funk, *Abandonment Doctrine and Its Discontents: Claiming Ordinary Losses After Pilgrim's Pride*, 31 Real Estate Journal 267 (2015). In a very recent Tax Notes article, Jasper L. Cummings, Jr. referred to the Service's interpretation of I.R.C. § 1234A in *Pilgrim's Pride* as "far-out." Cummings, *supra* note 200, at 1469. Nevertheless, the author was told by one of the smartest tax lawyers in the U.S., whose judgment on federal income tax matters is impeccable, that in his opinion, the Tax Court's analysis of § 1234A was correct.

253 *Pilgrim's Pride*, 779 F.3d at 315.

254 Zelenak, *supra* note 125, at 637.

255 Rev. Rul. 93-80, 1993-2 C.B. 239.

256 *Id*.

Regulation section 1.165-5(i) becoming legally effective. In my opinion, the difference is that Treasury Regulation section 165 (g)(1) is silent as to how the determination of worthlessness is made. In comparison, section 1234A(1) contains the specific condition of there being "a right or obligation," a requirement that has not been altered. For section 1234A to apply to *Pilgrim' s Pride*, it is necessary to subscribe to the Tax Court's "inherent" right theory,[257] compelling one to "tag Congress with an extravagant preference for the opaque . . . ."[258] This, for me, is a bridge too far.

IV. CONCLUSION

There are some lessons that can be gained from studying *Pilgrim's Pride*. While not of major consequence for either of the courts, I believe it is fair to conclude that Revenue Ruling 93-80[259] undercut the Service's position that the loss from abandonment of the securities should be considered as a capital loss pursuant to section 165(g)(1). The Service needs to be very careful when issuing guidance that can potentially be used against it in litigation. Furthermore, prior to taking the position in court that section 1234A addressed "inherent" rights[260] such as in *Pilgrim's Pride*, it should have at least promulgated regulations covering this point. This teaching has application well beyond section 1234A, as shown in *Wright v. Commissioner*.[261]

Pilgrim's Pride also most importantly illustrates the wisdom of utilizing a disparity of statutory interpretation methodologies depending upon the circumstances. As demonstrated by the different approaches that I believe were proper here for considering the applicability of sections 165(g)(1) and 1234A to *Pilgrim's Pride*, distinct circumstances require discrete approaches to applying a statutory provision to a case. Surely, our democratic institutions are not put at risk, by foregoing dogmatic textualism where this would lead to a result where "no conceivable tax policy . . . supports this interpretation"[262] or deeming an abandoned security to be per se worthless. Restraint, however, from deviating from the clear language of the text, such as applying section 1234A to inherent rights, may be in order where there are no overriding reasons not to do so.

---

257 *Pilgrim's Pride*, 141 T.C. at 543.

258 *Pilgrim's Pride*, 779 F.3d at 315 (citing Gutierrez v. Ada, 528 U.S. 250, 256 (2000)).

259 Rev. Rul. 93-80, 1993-2 C.B. 239.

260 *Pilgrim's Pride*, 141 T.C. at 543.

261 *Wright*, 809 F.3d 877(6th Cir. 2016).

262 *Id*. at 884.

An eclectic utilization of methodologies may be optimal for a court in arriving at the right conclusion.[263]

---

[263] Professor Popkin philosophizes that in "the process of judging . . . there is often no right answer. The fact that the judge is required to reach a decision by the best possible method means only that the judge must *seek* a right answer, not that he or she will be successful." *See* Popkin, note 112, at 76 (emphasis in the original).