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Income Taxes -- Installment Method of Reporting: Lessor's Release of Restoration Rights in Exchange for Three Notes of the Lessee Was Not a "Sale or Other Disposition" Which Could Qualify for the Installment Method of Reporting Income -- Billy Rose's Diamond Horseshoe, Inc. v. United States

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Income Taxes—Installment Method of Reporting: Lessor's Release of Restoration Rights in Exchange for Three Notes of the Lessee was not a "Sale or Other Disposition" Which Could Qualify for the Installment Method of Reporting Income.—*Billy Rose's Diamond Horseshoe, Inc. v. United States.*[1]—By an agreement of August 26, 1955, Billy Rose's Diamond Horseshoe, Inc. (Billy Rose) leased premises known as the Ziegfield Theatre to the National Broadcasting Company (NBC) for a term ending October 31, 1962. Under the lease, NBC covenanted to surrender ". . . the demised premises, in good order and repair in approximately the same condition as received by the lessee, depreciation and reasonable wear and tear excepted."[2] Upon taking possession, NBC made substantial physical alterations to the leased building in order to accomodate the requirements of television production. These alterations were acknowledged by Billy Rose as within NBC's rights under the lease. On June 28, 1962, the parties agreed to terminate the lease prior to its expiration, and to release each other from any cause of action arising out of the lease. However, one of several covenants which was not included in the mutual discharge of obligations was the lessee's duty to return the premises in the same condition as when received. In a "Compromise Agreement," the parties agreed that lessee NBC would deliver three promissory notes in the total amount of $300,000 in "full satisfaction and compromise of [NBC's] obligation to restore the Ziegfield Theatre to approximately the same conditions as the same was in when received by [NBC] as required by . . . the lease."[3]

In reporting income for its fiscal year ending August 31, 1962, Billy Rose elected the installment method[4] of reporting the receipts. Since the first promissory note was not payable until September 4, 1962, no part of the $300,000 was included as income in the taxpayer's fiscal 1962; rather, the proceeds of the notes were reported as ordinary income in the fiscal years in which they were received, 1963 and 1964. With the omission of those proceeds from its 1962 return, the taxpayer showed a net operating loss of $111,452.50 for that year. Thereafter Billy Rose filed a claim for refund of taxes paid in its taxable year ending August 31, 1959, based on the carryback[5] of its fiscal year 1962 net operating loss. The Commissioner rejected that claim. He determined that the entire face amount of the notes was includible as ordinary income in Billy Rose's fiscal year 1962, the year in which the

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1 448 F.2d 549 (2d Cir. 1971).

2 Billy Rose's Diamond Horseshoe, Inc. v. United States, 322 F. Supp. 76, 77 (S.D. N.Y. 1971).

3 448 F.2d at 550.

4 Int. Rev. Code of 1954, § 453. The requirements for installment reporting under § 453 are, generally, (1) a transaction rising to the level of a "sale" (2) involving property.

5 Int. Rev. Code of 1954, § 172(b)(1)(A)(i). The subsection provides that a taxpayer may "carryback" a net operating loss to each of the three taxable years preceding the taxable year of such loss.

Compromise Agreement was signed by Billy Rose and NBC, although payment on the notes was not actually received during that year. Thus, the claimed net operating loss carryback to fiscal 1959 was eliminated.

In Billy Rose's suit for a refund,[6] the District Court for the Southern District of New York denied taxpayer's motion for summary judgment for income taxes allegedly illegally assessed and collected, and held that the proceeds from the transaction between Billy Rose and NBC did not qualify for the installment method of reporting income.[7] On appeal, the Court of Appeals for the Second Circuit HELD: the release by lessor Billy Rose of its right to enforce restoration of the leased property in exchange for three notes of lessee NBC was not a "sale or other disposition" of property which would qualify under section 453 for the installment method of reporting income; thus, the notes constituted income to Billy Rose in the year when they were received rather than in later years when they were paid.[8]

In arriving at its holding, the court applied the capital gains "sale or exchange" requirement of section 1222 to the analogous "sale or other disposition" requirement of section 453. Hence the holding in *Billy Rose* could signal a departure from the treatment given to capital gains classification in *Commissioner v. Ferrer*.[9] The minimum impact of the court's holding will be the establishment of conflicting criteria for definition of the terms "sale or other disposition" of property for capital gains treatment on the one hand, and for the installment accounting method on the other.

This casenote will review the development of the criteria for classification of releases of contract rights as capital gains, culminating in the Second Circuit's *Ferrer* case. It will then examine the court's refusal to apply the *Ferrer* criteria to the analogous "sale or other disposition" requirement of section 453 involved in *Billy Rose*. Finally, it will be submitted that the court has laid the foundation either for movement away from the *Ferrer* criteria in the capital gains area, or alternatively for using different, and inconsistent, criteria for classifying a transaction as a "sale or other disposition," depending upon the purpose of such classification—i.e., for capital gains treatment, or for the installment accounting method.

Under Section 453 of the Internal Revenue Code of 1954, a taxpayer who correctly elects the installment method need only report as income in a given year the proportion of installment payments actually received in that year which the gross profit realized bears to the total contract price.[10] To qualify for treatment under the installment

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[6] Section 7422 of the Int. Rev. Code of 1954 permits a taxpayer to sue in federal court provided he has filed a timely claim for refund or credit with the Secretary or his delegate under § 6511 of the Int. Rev. Code of 1954.

[7] 322 F. Supp. 76, 79 (S.D.N.Y. 1971).

[8] 448 F.2d at 550-51.

[9] 304 F.2d 125 (2d Cir. 1962).

[10] For a full discussion of the installment method of reporting income, see Emory,

accounting method, income—other than the receipts of dealers in personal property—must be derived from:

(A) a sale or other disposition of real property, or
(B) a casual sale or other casual disposition of personal property . . .[11]

In determining whether Billy Rose's claim for the installment reporting procedure met the statutory criteria, the only question considered by the court was whether the transaction under review, involving as it did a contract right, constituted the required "sale" or "other casual disposition." Nowhere in the installment sale section or elsewhere in the Code is the term "sale" defined.[12] However, the question of "sale" on the disposition of contract rights has been a frequent source of litigation in the context of determining whether a transaction qualifies for capital gain treatment: the Code requires, inter alia, a "sale or exchange" of a capital asset before granting such treatment.[13] Accordingly, the *Billy Rose* court sought to define "sale" for purposes of installment reporting by utilizing the "sale or exchange" criteria which courts have developed in determining whether a transaction in contract rights qualified for capital gains treatment.

In approaching the question of "sale" of contract rights for capital gains purposes the courts have employed two rationales. One focuses upon the outcome of the transaction by examining the subject matter of the transaction in the hands of the transferee; the other asks whether the contract right involved in the transaction did or did not constitute a capital asset.[14] Under the former approach, the primary consideration is whether the contract rights transferred or assigned survived the transaction and maintained their existence in the hands of the transferee.[15] The latter approach looks to the nature of the contract right; i.e., did the contract right transferred constitute in the hands of the transferor an independent interest in an underlying capital asset, regardless of whether or not the contract right survived the particular transaction.[16] Neither of these rationales actually sets a standard for

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The Installment Method of Reporting Income: Its Election, Use, and Effect, 53 Cornell L. Rev. 181 (1968).

11 Int. Rev. Code of 1954, § 453(b)(1)(A)-(B).

12 See Commissioner v. Brown, 380 U.S. 563 (1965), in which the Court observed:

> A "sale" . . . is a common event in the non-tax world; and since it is used in the Code without limiting definition and without legislative history indicating a contrary result, its common and ordinary meaning should at least be persuasive of its meaning as used in the Internal Revenue Code.

Id. at 570-71.

13 Int. Rev. Code of 1954, § 1222(3).

14 See Eustice, Contract Rights, Capital Gain, and Assignment of Incomes—the *Ferrer* Case, 20 Tax L. Rev. 1, 6-7 (1964) (hereinafter cited as Eustice).

15 Commissioner v. Pittston Co., 252 F.2d 344 (2d Cir. 1958); General Artists Corp. v. Commissioner, 205 F.2d 360 (2d Cir. 1953); Commissioner v. Starr Bros., Inc., 204 F.2d 673 (2d Cir. 1953).

16 Commissioner v. Ferrer, 304 F.2d 125, 131 (2d Cir. 1962).

"sale or exchange" under the tax laws. Rather they have produced categories of contract rights which upon disposition may qualify for capital gain. Although in applying the survival analysis to contract rights controversies courts may insist that they are examining the form of the transaction for a "sale or exchange," they are in fact relying on the nature of the contract rights involved to "survive" and thus constitute a sale. Similarly, when courts apply the "independent interest" analysis they reject the necessity of an inquiry into the form of the transaction and go directly to an analysis of the asset.

In reviewing the Compromise Agreement of the parties in the instant case, the *Billy Rose* court applied the "survival" analysis to determine whether Billy Rose's transfer of his right of restoration could qualify as a "casual sale or casual disposition" for the installment reporting of income. Essentially the court reasoned that Billy Rose had merely surrendered a right for a sum of money. Billy Rose's right of restoration "vanished" in the transaction and did not "survive" in the hands of NBC. Thus the transaction was viewed as having merely extinguished the rights and obligations of the parties under the lease. The court held that Billy Rose had not "sold" or "otherwise disposed" of "property" and concluded that the release of a contract right which merely relieves the transferee from a contractual obligation is not a "sale" for purposes of the installment method of reporting income.[17]

The court's standard for "sale" was derived from its earlier decision in *Commissioner v. Starr Bros., Inc.*[18] There the question presented was whether proceeds, received by the taxpayer from a manufacturer of drugs for agreeing to terminate a contract under which the taxpayer had been granted the exclusive right to distribute the manufacturer's products in a particular community, should be treated as capital gain. The *Starr Bros.* court, although conceding that the taxpayer's rights under the contract were property and by definition capital assets, emphasized that the transaction merely released the manufacturer from its obligations and that accordingly it did not constitute a sale. The court reasoned: "[s]uch release not only ended the promisor's previously existing duty but also destroyed the promisee's rights. They were not transferred to the promisor; they merely came to an end and vanished."[19] Consequently capital gain treatment was denied, apparently because nothing had survived the transaction and nothing vested in the purchaser after the taxpayer's release of his contractual claim.

Shortly thereafter, the Second Circuit developed its *Starr Bros.* rationale by focusing on the "survival" of the contract rights in question rather than looking to the form in which the parties cast the transaction. In *General Artists Corp. v. Commissioner*,[20] the taxpayer,

[17] 448 F.2d at 551-52.
[18] 204 F.2d 673 (2d Cir. 1953).
[19] Id. at 674.
[20] 205 F.2d 360 (2d Cir. 1953).

a booking agency for entertainers, sought capital gains treatment for proceeds from an agreement with another booking agency whereby the taxpayer transferred its rights as the exclusive agent for a particular singer. Under the agreement the taxpayer's contracts were cancelled and new ones were executed between the singer and the transferee booking agency. The *General Artists* court held that a sale had not occurred despite the fact that the taxpayer had apparently transferred his rights in an exclusive contract to a third party. The court viewed the agreement between the two booking agencies essentially as a release by the taxpayer to its obligor, the singer, in order to allow the singer to contract with another booking agency.[21] Thus, the *General Artists* decision stands for the proposition that the "survival" analysis may extend beyond consideration of the formal contract language to a determination of whether the obligor's contractual liabilities have in fact survived the transactions. This, then, was the analysis employed by the Second Circuit in its examination of the *Billy Rose* transaction. In focusing on whether anything "survived" the transaction, rather than analyzing the nature of the asset sold, the court determined that for a sum of money the taxpayer had merely surrendered its right under a lease to have the Ziegfield Theatre restored. The Compromise Agreement was viewed as a "release" and in no sense a "sale," at least insofar as the latter term was defined in the *Starr Bros.-General Artists* cases.[22]

In disposing of the case as it did the court explicitly rejected as a basis for decision a completely different conception of "sale." Billy Rose had argued that in *Commissioner v. Ferrer*[23] the *Starr Bros.* "sale or exchange" test had been materially altered if not overruled, and hence should no longer control the federal tax treatment afforded income received upon the disposition of contract rights. In *Ferrer*, the taxpayer had acquired the exclusive dramatic production rights to a novel. Although the author had retained the full legal and equitable title to the copyright property, taxpayer Ferrer was granted a "lease" of the exclusive theatrical production rights and the power to prevent the author's transfer of retained film rights in the copyright property until the play had been running for a specified period of time. Shortly thereafter, a motion picture company purchased the film and television rights from the author and simultaneously obtained a release of Ferrer's rights in the copyright property. For his release Ferrer received a seventeen percent interest in the net profits of the film production. In the Court of Appeals for the Second Circuit the question was whether the amounts received by Ferrer under the release could constitute capital gain. Since Ferrer had actually released a "bundle of rights" to the film company, the court considered precisely what Ferrer had given up and concluded that with the exception of the con-

[21] Id. at 361.
[22] 448 F.2d at 551-52.
[23] 304 F.2d 125 (2d Cir. 1962).

sideration received for one of the rights involved,[24] Ferrer was entitled to treat the amounts received under the release as capital gain.

The *Ferrer* court observed that where capital gains are in issue, the trend of decisions was to move away from an examination of the *form of the transaction* under review toward a thorough analysis of whether the contract rights involved could be characterized as capital assets.[25] In *Ferrer,* the court criticized the *Starr Bros.* decision for its restrictive "sale or exchange" test which denied capital gain to income derived from the cancellation or release of contract rights.[26] The *Ferrer* court chose a test which examined the nature of the contract rights in the hands of the taxpayer before the "sale" rather than an analysis focusing on whether anything "survived" the transaction in the purchaser's hands. The court concluded that contract rights could qualify for capital gains treatment if in the seller's hands they constituted an "estate" or an "encumbrance"[27] on property, which, if itself held, would be a capital asset.[28] Thus, by explicitly refusing to be concerned with the form in which the parties cast their particular transaction,[29] the court in *Ferrer* materially downgraded the sale inquiry stressed in *Starr Bros.* In shifting the focus of its capital gains test to a precise in-

[24] Id. at 133-35. Ferrer owned a contingent royalty interest in any consideration earned by the taxpayer from his sale of the retained film rights. The court concluded that the portion of the proceeds received by Ferrer from his release which could be allocated to this right was ordinary income. Ferrer did not obtain a property interest, legal or equitable, in the film rights; the contract specifically provided that the entire property interest was retained by the author. Ferrer's only interest was his right to share in the proceeds from exploitation of property owned by the author and, consequently, the receipts could only be treated as ordinary income. See Eustice, supra note 14, at 7-9.

[25] 304 F.2d at 131.

[26] Id. The *Ferrer* court observed:

> Tax law is concerned with the substance, here the voluntary passing of "property" rights allegedly constituting "capital assets," not with whether they are passed to a stranger or to a person already having a larger "estate." So we turn to an analysis of what rights Ferrer conveyed.

[27] The *Ferrer* court cited several decisions in which capital gains treatment was allowed and where the survival of the contract rights was completely irrelevant for purposes of a "sale": lessee's surrender of his lease to the lessor, Commissioner v. Golonsky, 200 F.2d 72 (3d Cir. 1952), cert. denied, 345 U.S. 939 (1953); lessee's relinquishment of a right to restrict lessor's renting to another tenant in the same business, Commissioner v. Ray, 210 F.2d 390 (5th Cir.), cert. denied, 348 U.S. 829 (1954); lessee's release of his entire interest to a sublessee, Metropolitan Bldg. Co. v. Commissioner, 282 F.2d 592 (9th Cir. 1960).

[28] 304 F.2d at 130-31. See Eustice, supra note 14, at 12-13.

[29] See Eustice, supra note 14, at 6-7. The author maintains that in fact the court could have found a traditional *Starr Bros.* sale since ". . . before the cancellation the author could deal *only* with Ferrer, while after the cancellation he was free to deal with anyone. Thus the author's rights were 'enlarged' by the cancellation transaction and, in a sense at least, something did survive the transfer in the hands of the transferee, thereby suggesting that a true sale was probably present." Thus, the *Ferrer* court clearly broke with the *Starr Bros.* sale or exchange test and established that the question of sale is not resolved by merely determining whether contract rights "survive" but rather by a determination of the nature of the transferor's underlying interest in the asset involved.

quiry into the nature of the property involved in a transaction, the *Ferrer* court established that previously disqualifying labels such as "cancellation" and "release" were subsumed in the term "sale" where the contract rights involved in a transaction could be characterized as a capital asset. The *Ferrer* court emphasized that this shift in focus was especially justified when there existed no "sensible business basis" for distinguishing between a hypothetical sale and the disposition—a release—which actually took place.[80]

When the *Billy Rose* issue came before the district and appellate courts of the Second Circuit, then, they were presented with the task of choosing between the *Ferrer* criteria, which utilize the property concept in testing for a sale, and the *Starr Bros.* criteria, which look to the form of the transaction and hence stress the "survival" standard. Billy Rose's restoration right under the lease with NBC would qualify, at least arguably, as "property" under the *Ferrer* test. The right to have leased premises restored to a previous condition would appear to constitute something tantamount to a property right which Billy Rose could have sold or assigned. Moreover, by *Ferrer*, the restoration right was in a capital asset—the leasehold interest of NBC.[81] The cancellation of that right should thereby qualify as the "sale" of "property."[82] However, the *Ferrer* criteria were considered only briefly by the district court in *Billy Rose* and were rejected out of hand by the Second Circuit. Instead, both courts riveted their decisions to the "survival" standard of *Starr Bros.*

The district court in *Billy Rose* dismissed the argument that the *Starr Bros.* cases had been overruled by *Ferrer* and distinguished the *Ferrer* rationale as being of limited application. The court explained:

> [I]n capital gains cases, the focus in the Second Circuit has been on the type of property, not the nature of the disposition. . . . [I]n the instant case, the focus is on the nature of

[80] 304 F.2d at 131.

[81] A lease is normally considered a capital asset of the lessee. See, e.g., J. Chommie, Federal Income Taxation 272 (1968); Rev. Rul. 56-531, 1956-2 Cum. Bull. 983.

[82] Indeed, precisely this tax treatment was accorded in an earlier case involving proceeds allocable to the restoration of a leasehold. In Waggoner v. Commissioner, 15 T.C. 496 (1950), gain realized upon receipt of cash compensation from the United States for property damaged or converted while in possession of the United States under a lease entered into under threat of condemnation proceedings was held taxable as long term capital gain. The court characterized the proceeds as payments to the lessor for a portion of his building and as the substitution of "one obligation for another; that is [the United States] made restitution to the petitioners for the property [as required under the lease] in cash instead of property." Id. at 502-03. See also Washington Fireproof Bldg. Co., 31 B.T.A. 824 (1934). There, the taxpayer received a lump sum payment from a lessee to cover both rent and restoration of the lessor's property. In deciding whether any or all of the payment was allocable to the restoration obligation, the court held that "the transaction was substantially similar to a sale and must be treated for income tax purposes as a 'sale or other disposition' of a portion of [the taxpayer's] building." Id. at 827, citing § 111 of the Revenue Act of 1928. The case was commented upon with approval in Waggoner v. Commissioner, 15 T.C. at 502.

> the disposition (i.e., whether it was a "sale" for the purposes of installment sales provisions), and the . . . *Starr Bros.* cases still speak with authority to that question irrespective of what the holding may be when the question of capital gains treatment is raised.[33]

The district court further emphasized that "[h]ere, unlike *Ferrer*, there is a 'sensible business basis' for distinguishing between the release which occurred and the sale which did not."[34] Billy Rose had merely transferred his right to have the Ziegfield Theatre restored. The court felt that a "sale" of that right to a party other than NBC would have no practical or legal significance independent of the underlying leasehold. It viewed the right of restoration as unenforceable except in the hands of the owner of the leasehold, and contrasted the situation in *Ferrer* where the taxpayer's rights in the play could have been sold to anyone. Thus, for purposes of applying section 453 to transactions involving contract rights, the district court identified as the linchpin of "sale" the value of the contract right in question to a party other than the obligor.[35]

It is submitted that the *Billy Rose* district court failed to distinguish *Ferrer* satisfactorily when it characterized that case as one of limited application. The district court maintained that *Ferrer* could be properly applied only where the taxpayer was seeking capital gains treatment.[36] However, there is nothing in *Ferrer* to require so narrow an interpretation or, indeed, anything in the Internal Revenue Code which suggests a basis for the court's reasoning. Rather it is reasonable to conclude that the *Ferrer* decision rejected the *Starr Bros.* survival standard for all purposes by utilizing criteria which tested the nature of the property in the hands of the transferor just prior to the transaction. Yet, by limiting *Ferrer* to capital gains and installing the "survival" standard for section 453 transactions, the district court in *Billy Rose* impliedly recognized two tests for defining a sale, the applicability of which would depend on the income tax treatment sought.

Although affirming the holding of the district court, the Court of Appeals for the Second Circuit ignored the dual interpretation of "sale" which the lower court had implicitly recognized. Instead, the appellate court in *Billy Rose* refused to apply *Ferrer* because that case "involved the release of motion picture rights which could have been sold to any third person. A release of a right to restoration is entirely different and is not a 'sale' . . . ."[37] Thus, while there exists in the Second Circuit's decision the inference that the *Ferrer* criteria for "sale" can lie only where the contract right involved has a market

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[33] 322 F. Supp. 76, 81 (S.D.N.Y. 1971).
[34] Id.
[35] Id.
[36] Id.
[37] 448 F.2d at 552.

value to parties other than the original obligor, the court never confronted the significance of *Ferrer*. In resurrecting *Starr Bros.* and attempting to distinguish *Ferrer* on the ground that that case involved a contract right which could have been resold to third parties and hence was a contract right which could have been "sold" even under the *Starr Bros.* formula, the *Billy Rose* court appeared to rule, sub silentio, that the *Ferrer* test was applicable only to the characterization of the property right involved rather than to the characterization of the entire transaction. It is submitted, then, that the *Billy Rose* court would have been satisfied that a court applying the *Ferrer* rationale to any transaction involving an exclusive contract right such as that in *Billy Rose* would be required to reach the same result as a court applying the *Starr Bros.* test. For the *Billy Rose* court, the *Ferrer* case can be properly employed only where a contract right is clearly capable of resale to a third party and hence passes the *Starr Bros.* survival test.

It is also submitted that the court of appeals was less than accurate in assuming, as an initial premise, that Billy Rose's right of restoration could not have been sold to a third party. Indeed, the district court in *Billy Rose,* while pointing out the impracticality in the instant situation of the "sale" of the restoration right to any party but NBC, implied that under different circumstances the right would have been capable of "sale" to a third party.[88]

Thus the Court of Appeals for the Second Circuit failed to distinguish *Ferrer* in meaningful terms. *Ferrer* examined the nature of the contract right involved as it existed before the transaction under review and so avoided inquiry into whether anything survived the transaction and hence into the nature of the transaction itself. Given a certain kind of property and a transaction in which the transferor for value divested himself of that property, the *Ferrer* rationale would rule that the "sale or exchange" requirement of capital gains was satisfied, without any discussion of whether the precise nature of the transaction constituted a "sale." In *Billy Rose,* however, the court refused to consider the nature of the property as it existed before the transaction and returned to the *Starr Bros.* survival standard as a means of defining "sale" for the first time since the 1962 *Ferrer* decision.[89] Under *Starr Bros.*, the court was required to examine the nature of the contract right but only to determine whether the right still "existed" in the hands of the transferee. That is, it asked whether the contract right could be sold yet again. If not, the transaction was

[88] In Hamilton & Main, Inc. v. Commissioner, 25 T.C. 878, 882 (1956), the Tax Court held that the right of restoration under a lease had been "sold" for purposes of capital gains where the leased premises had been sold and the restoration right assigned with them. The district court in *Billy Rose* appeared to indicate that it would also recognize "sale" under similar circumstances for purposes of installment reporting of income. 322 F. Supp. at 82 n.7.

[89] After *Ferrer,* the Second Circuit cited the *General Artists* and *Starr Bros.* cases in Brook v. Commissioner, 360 F.2d 1011 (2d Cir. 1966), in dicta only and not as a controlling factor in its decision.

a release and not the "sale" required under section 453 for installment accounting of income.

The *Billy Rose* court limited, indeed rendered meaningless, the remarks made in *Ferrer* concerning congressional disapproval of the *Starr Bros.* "sale or exchange" test. In *Ferrer* the court noted that Section 1241 of the 1954 Internal Revenue Code—enacted after *Starr Bros.*—provides that amounts received for the cancellation of a lease or a distributor's agreement were to be considered for tax purposes as amounts received in *exchange* for rights under such agreements.[40] The *Ferrer* court vigorously maintained that section 1241 reflected congressional disapproval with the *Starr Bros.* distinction between "sale" and "release" of contract rights.[41] In *Billy Rose* the court expressly rejected *Ferrer's* criticism of *Starr Bros.*, ruling that it was relevant only to cases involving section 1241, and in a footnote there exists the inference that further application of *Ferrer* may be of no future significance in the Second Circuit.[42] Thus, where *Ferrer* had regarded section 1241 as a buttress to its argument that the *Starr Bros.* rationale erroneously distinguished between "sale" and "release,"[43] the *Billy Rose* court may have effectively restricted *Ferrer* to those specific transactions qualifying under section 1241.

The consequences of the *Billy Rose* decision are not clear. While establishing the survival test of *Starr Bros.* for installment reporting, the court failed to articulate a satisfactory position on the viability of *Ferrer*. Although it may appear that there now exist two approaches to the requirement of "sale" in the Second Circuit—one for installment reporting and another for capital gains treatment—*Billy Rose* may have precluded any further application of *Ferrer*. In other words, it is uncertain whether the resurrection of the *Starr Bros.* rationale can be narrowly viewed as an implicit recognition that the concept of "sale" should differ according to the income tax treatment sought. Indeed, it would be a curious result if, in the aftermath of *Billy Rose*, the Second Circuit followed the *Starr Bros.* rationale in defining the "casual sale or other casual disposition" required for installment reporting and retained the *Ferrer* treatment for the literally more demanding "sale or exchange" requirement of capital gains. Thus the question after *Billy Rose* is whether the *Starr Bros.* rationale will now be extended and reintroduced as a test for capital gains. The resolution of this

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40 Section 1241 of the Int. Rev. Code of 1954 provides:

> Amounts received by a lessee for the cancellation of a lease, or by a distributor of goods for the cancellation of a distributor's agreement (if the distributor has a substantial capital investment in the distributorship), shall be considered as amounts received in exchange for such lease or agreement.

41 304 F.2d at 130-31.

42 448 F.2d at 552 n.1.

43 Two federal circuits having embraced *Ferrer* also reject *Starr Bros.* as having created an unnecessary distinction between sale and release. See, e.g., Commissioner v. Goff, 212 F.2d 875 (3d Cir. 1954), and United States v. Dresser Industries, Inc., 324 F.2d 56 (5th Cir. 1963).

issue will presumably be delayed until a taxpayer seeks capital gains treatment on the disposition of an exclusive contract right such as that in *Billy Rose*. Meanwhile, the *Billy Rose* decision reveals a firm intention on the part of the Second Circuit to examine the form of transactions which give rise to taxpayers' claims for preferred income tax treatment.

JOHN J. GOGER

Labor Law—Successor Employers—Duty to Honor Predecessor's Collective Bargaining Agreement—*NLRB v. Burns Int'l Security Services*.[1]—For five years (1962-67) guard services at the Lockheed Aircraft Service Company at the Ontario International Airport in California were provided by the Wackenhut Corporation. In 1967, United Plant Guard Workers of America (UPG) won a representation election and was certified by the NLRB as exclusive bargaining representative of the Wackenhut employees at the Lockheed plant. Wackenhut and the Union entered into a three-year collective bargaining contract on April 29, 1967. Because Wackenhut's service contract with Lockheed was due to expire on June 30, Lockheed called for bids from various suppliers of guard services; the contract was awarded to Burns International Security Services, Inc. Burns, slated to take over on July 1, had learned at a pre-bid conference on May 15 of the Union's certification and subsequent contract with Wackenhut.

Burns retained twenty-seven of the Wackenhut guards and added fifteen Burns guards, brought in from other locations. Burns informed the former Wackenhut employees that they would have to join the American Federation of Guards (AFG), a union with which Burns had contracts at other locations, inasmuch as Burns "could not live with" the Wackenhut contract.[2] On June 29, Burns recognized the AFG as bargaining representative of the plant guards at the Lockheed unit. On July 12, UPG demanded that Burns not only recognize it as bargaining representative, but also honor the terms of the existing contract with Wackenhut. These demands were refused, whereupon UPG filed unfair labor practice charges.[3]

The NLRB found a violation of Sections 8(a)(1) and (2)[4] of the National Labor Relations Act (NLRA or Act) in Burns' recognition and assistance of the AFG, and a violation of Sections 8(a)(1) and (5)[5] in Burns' failure to recognize and bargain with UPG and refusal

1 406 U.S. 272 (1972).
2 Id. at 275.
3 Id. at 276.
4 29 U.S.C. §§ 158(a)(1),(2) (1970).
5 Section 8(a)(5) provides that

It shall be an unfair labor practice for an employer— . . .
(5) to refuse to bargain collectively with the representatives of his employees, subject to the provisions of section 159(a) of this title.

29 U.S.C. § 158(a)(5) (1970).