Volume 73
Issue 1 *Dickinson Law Review - Volume 73, 1968-1969*

10-1-1968

Recent Cases

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PURCHASER'S ASSUMPTION OF SELLER'S BUSINESS LIABILITIES HELD PAYMENT IN THE YEAR OF SALE UNDER SECTION 453 OF THE INTERNAL REVENUE CODE

Irwin v. Commissioner, 390 F.2d 91 (5th Cir. 1968).

In *Irwin v. Commissioner*[1] the Court of Appeals for the Fifth Circuit ruled that in a sale of partnership assets the purchaser's assumption and payment of the partnership's current liabilities in the year of sale did not constitute a "payment in the year of sale" for purposes of deferring payment of taxes until the year payment for a sale is received. Section 453[2] of the Internal Revenue Code

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1. 390 F.2d 91 (5th Cir. 1968), *rev'g* 45 T.C. 544 (1966).
2. INT. REV. CODE of 1954 § 453.

INSTALLMENT METHOD

(a) Dealers in Personal Property—

(1) In General—Under regulations prescribed by the Secretary or his delegate, a person who regularly sells or otherwise disposes of personal property on the installment plan may return as income therefrom in any taxable year that proportion of the installment payments actually received in that year which the gross profit, realized or to be realized when payment is completed, bears to the total contract price.

(2) Total Contract Price.—. . . .

(b) Sales of Realty and Casual Sale of Personalty.—

(1) General Rule—Income from—

(A) a sale or other disposition of real property, or

(B) a casual sale or other casual disposition of personal property (other than property of a kind which would properly be included in the inventory of the taxpayer if on hand at the end of the taxable year) for a price exceeding $1,000, may (under regulations prescribed by the Secretary or his delegate) be returned on the basis and in the manner prescribed in subsection (a).

(2) Limitation—Paragraph (1) shall apply—

(A) In the case of a sale or other disposition during a tax-

permits the seller of a business who makes a deferred payment sale for a price in excess of $1,000 to report the gain from the sale in the year payment is actually received; provided that, in the taxable year of sale there are: (1) no payments to the seller, or (2) that the payments to the seller, exclusive of evidences of the purchaser's indebtedness, does not exceed 30% of the selling price.[3] If the payments in the year of sale exceed 30% of the selling price or if for another reason the taxpayer is deprived from electing to use section 453, he may be confronted with the burden of paying the full tax on his realized gain in the taxable year of sale. This may result in a tax which is greater than the amount of cash actually received in the year of sale.[4]

The decision by the fifth circuit in *Irwin* reverses an earlier Tax Court decision,[5] and resolves a conflict between the views of the Tax Court and those of the ninth circuit as expressed in *United States v. Marshall.*[6] The Court of Appeals for the Fifth Circuit agreed with the ninth circuit and held in *Irwin* that, although the liabilities were assumed and paid in the year of sale, Congress intended that the benefits of section 453 should not be denied the taxpayer if the payments to him, exclusive of the liabilities, did not exceed 30% of the selling price. As the benefit of applying section 453 results in a tax *deferral* rather than a tax *avoidance* it is submitted that the broad interpretation of *Irwin* is justified as being within the spirit of Congress' purpose in enacting section 453.

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able year beginning after December 31, 1953 . . . only if in the taxable year of the sale or other disposition—
(i) there are no payments, or
(ii) the payments (exclusive of evidences of indebtedness of the purchaser do not exceed 30 per cent of the selling price. . . .

3. INT. REV. CODE of 1954 §§ 453b(1) B, b(2)(A)(i),(ii).

4. *E.g.*, Peter Mamula, 41 T.C. 572 (1964), *rev'd*, 346 F.2d 1016 (9th Cir. 1965) (the taxpayer was burdened with a tax in excess of $30,000 but received only $10,000 in the year of sale); Joseph Hormberger, CCH Tax Ct. Mem. 1960-43 (1960) (upholding a tax deficiency of over $200,000 where the taxpayer received only $7500 in cash in the year of sale). However, even if section 453 is not available perhaps the taxpayer may still avoid the burden of an unduly large tax payment through the use of (1) The Deferred Payment Method provided by Treas. Reg. 1.453-6(a)(1), or (2) The "Return of Capital" Method as found in Burnet v. Logan, 283 U.S. 404 (1931). *See*, Comment, *Taxation of Deferred Payment Sales of Realty and Casual Sales of Personalty*, 1966 UTAH L. REV. 195 (1965).

5. Ivan Irwin, Jr., 45 T.C. 544 (1966).

6. 357 F.2d 294 (9th Cir. 1966), *aff'g*, 241 F. Supp. 30 (S.D. Cal. 1964). The Court of Appeals decision in *Marshall* was reported just nine days prior to the Tax Court's determination of *Irwin*. See Koblenz, *Installment Sales—Purchasers Assumption of Liability to Third Party*, 18 WEST. RESERVE LAW REV. 906 (1967); Berger, *Installment Sales With Assumed Liabilities*, 122 J. ACCOUNTANCY, 41 (1966); De Castro and Chodorow, *Can Buyers Payment of Assumed Debt Kill Sellers Installment Election? Courts Disagree*, 25 J. TAXATION 130 (1966); Comment, *Assumption and Discharge of Sellers Liabilities as Year of Sale Payments For Purposes of I.R.C. Section 453*, 16 BUFF. L. REV. 758 (1967); Note, *Installment Sales Report of Income are Current Liabilities Similar to Mortgages*, 1 CALIF. WEST. L. REV. 154 (1965).

THE IRWIN SITUATION

The taxpayers[7] in *Irwin* owned a fire and casualty insurance agency which acted as an intermediary between selling agents and insurance companies. The agents, upon making a sale, would remit the premium to the agency, retaining their commission. When an agent reported a sale, the agency, which operated on an accrual accounting basis, would debit accounts receivable from agents and credit accounts payable to insurance companies (and commissions earned).[8] The payment to the insurance company was ordinarily due within ninety days from the date a policy was sold.[9]

The agency was sold for $471,539.64, of which the purchaser paid $81,539.64 in cash and delivered notes for the balance of $390,000.[10] The purchaser acquired all the assets of the business and agreed to assume all of the agency's liabilities.[11] The accounts receivable from agents constituted the bulk of the assets, and the accounts payable to insurance companies was the greatest liability.[12] The amount of cash received from the sale was less than 30 per cent of the selling price, and when apportioned among the partners remained less than 30%. The partners, regarding this as the only "payment in the year of sale," elected to report their in-

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7. The agency was owned on a partnership basis. Barney and Margaret Vanston owned 70%, Edmund F. Vanston owned 15% and Ann Vanston Irwin owned 15%. Ann Vanston Irwin is the wife of Ivan Irwin under whose name the case was decided. Ivan Irwin, Jr., 45 T.C. 544, 545 (1966).

8. Assuming the agent's commission to be 20% and the agency's commission to be 10%, the sale of a policy with a $100.00 annual premium would result in the following accounting entries:

Accounts Receivable Agents	$80	
Accounts Payable to Insurance Companies		$70
Commission Income		$10

45 T.C. at 546.

9. *Id.* at 546.

10. *Id.* at 547. The selling price was based on the book value of net assets of $78,002.91 plus unrecorded goodwill in the amount of $393,536.73.

11. *Id.* at 547.

12. On the date of sale the balance sheet would have read in a manner similar to the following:

Total Assets			$349,189.86
Accounts Receivable from Agents	$236,535.17		
Total Liabilities			271,186.95
Premium Notes Payable	69,623.46		
Accounts payable to:			
Insurance companies		$194,299.67	
Accrued Payroll taxes		1,480.70	
Notes Payable (automobile)		3,596.51	
Accounts Payable (other)		2,186.61	

45 T.C. at 547.

come under the installment method of section 453.[13] The Commissioner, however, determined that the liabilities of the partnership which were assumed by the purchaser amounted to $271,186.95 of which $237,904.05 were paid in the year of sale.[14] The Commissioner sought to have the entire long term capital gain reported as income in 1959.[15] This was rejected by the Tax Court, but the court did rule that the amount of liabilities *assumed and paid* ($237,974.05) constituted a payment in the year of sale.[16] Each partner's ratable share of this amount, said the court, would have to be attributed to the amount received in 1959, the taxable year of sale; this resulted in each taxpayer receiving an amount in excess of 30% of the portion of the entire selling price due him, so that none of the taxpayers was eligible to elect under 453. The court therefore assessed a total deficiency of $82,029.55.[17]

The Tax Court regarded the final payment of the seller's debt in the year of sale as tantamount to the seller's receipt of cash or other tangible property. The court also regarded as controlling those cases which held that a cancellation or payment of the seller's indebtedness as part of the consideration is a payment to the seller if the seller's liability is "extinguished" in the year of sale.[18] These cases involve: (1) the vendee's cancellation of the vendor's prior indebtedness to him;[19] (2) the payment of the vendor's legal ex-

13. The following represents the manner in which the partners received and divided the proceeds of the sale and reported to the Internal Revenue in their joint returns for 1959.

Partners	Ann V. Irwin	Barney and Margaret Vanston	Edmund Vanston
1. Sales Price	$70,910.61	$336,884.33	$63,744.70
2. Basis in Partnership Interest	11,744.93	61,618.96	4,609.02
3. Net Long-Term Capital Gain	59,135.68	275,265.37	59,135.68
4. Percent of Gain	81.3947	81.71	92.77
5. Cash received in 1959	12,410.61	63,844.33	5,244.70
6. 30% of Sale price	21,273.18	101,065.30	19,123.41
7. Gain recognized in 1959 (Col. 4 x Col. 5)	10,399.79	52,199.88	4,865.51

45 T.C. at 548.

14. *Id.* at 548, 552.

15. *Id.* at 548.

16. *Id.* at 552.

17. 45 T.C. 545. This demonstrates the hardship that the unavailability of section 453 can work. In the case of Edmund Vanston and his wife, who received a cash payment of $5,244.70 in 1959, his 1959 tax *deficiency* alone amounted to $13,921.12 or more than 2½ times the amount actually received in the year the tax was imposed. The deficiency of Ivan and Ann Irwin amounted to $11,401.45, compared to cash received of $12,410.61. The deficiency of Barney and Margaret Vanston was $56,707.98 compared to $63,884.33 cash received. It is likely in the latter two cases that when coupled with the tax originally reported in 1959 the deficiency caused the total tax bill to exceed the total cash received.

18. 45 T.C. at 551.

19. W. H. Batcheller, 19 B.T.A. 1050 (1930).

penses of the sale by the vendee;[20] and (3) the cancellation of the vendor's notes to a third party.[21] Other indications of this principle can be found in rulings of the Internal Revenue Service which (1) regard the value of the mortgage as a payment in the year of sale when the mortgaged property is sold to the mortgagee,[22] and (2) hold that in sales of realty where the purchaser assumes and pays liabilities of the seller which represent "liens, accrued interest and taxes," these liabilities are deemed payments in the year of sale.[23] The court conceded that if the obligations were merely assumed and *not* paid they would not constitute payments in the year of sale.[24] In summation the Tax Court stated:

> We recognize as an established general rule that if, as part of the consideration for a sale, a seller's liability is paid or cancelled in the year of sale, the amount of the liability so extinguished is properly included in the year-of-sale payments, but if the liability is merely assumed (or the asset transferred 'subject to' the liability) the liability is not necessarily deemed to be a year of sale payment . . . . [W]e consider this dichotomous general rule to be in accord with the policy and rationale which underlie the installment reporting privilege and its presently existing 30-percent test.[25]

The Tax Court felt justified in reaching this result, for it also was of the opinion that, although the cash which is paid to a third party in discharging a seller's obligation is not available to the seller to enable him to pay his taxes, the payment releases the seller's non-business assets held in reserve to pay these debts.[26] The major fallacy of this reasoning is the assumption that, where business obligations are assumed and paid by the purchaser of the business, the seller has held non-business assets in reserve to discharge these obligations (which reserves are now released to pay the tax).[27]

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20. Wagegro Corp., 38 B.T.A. 1225 (1938).
21. James Hammond T.C. 198 (1942).
22. I.T. 2351, VI-1 CUM. BULL. 43 (1926) (distinguishing the situations where the mortgage was assumed by a third party purchaser).
23. REV. RUL. 60-52, 1960-1 CUM. BULL. 186.
24. 45 T.C. at 551. *See*, Estate of Lipman v. United States, 245 F. Supp. 393 (E.D. Tenn. 1965); Schneeder v. Lucas, 15 Am. Fed. Tax R. 572 (W.D. Ky. 1929), *rev'd on other grounds*, 47 F.2d 1006 (6th Cir. 1931), *cert. denied*, 284 U.S. 622 (1931); Katherin H. Watson, 20 B.T.A. 270 (1930). *Cf.* Stephen A. Cisler, Jr., 39 T.C. 458 at 465 (1962).
25. 45 T.C. at 552.
26. *Id.* at 550.
27. *See*, Comment, *Assumption and Discharge of Seller's Liabilities as Year of Sale Payments for Purpose of I.R.C. Section 453*, 16 BUFF. L. REV. 756, 766 (1967) (hereinafter cited as Comment).

Almost as an after thought, the Tax Court also rejected the final argument of the taxpayer. This argument was based on a regulation which excluded the assumption of a mortgage on realty by the purchaser from being considered as year-of-sale payments unless the liabilities assumed exceeded the seller's basis for the property sold.[28] The taxpayer sought to extend this regulation to his casual sale of personalty, but the analogy was not accepted.[29] The Tax Court's reasoning was rejected by the fifth circuit, which chose instead to follow the decision reached by the Ninth Circuit in *United States v. Marshall*.[30]

In *Marshall* an agricultural business, which was a sole proprietorship, was sold for a price of $110,513.22 of which $14,000 in cash was paid by the purchaser in the year of sale.[31] The purchaser, however, in the year of sale paid over $25,000 of business obligations (which he had assumed along with the business assets) for which the seller would ultimately have been personally liable. This payment, contended the Commissioner, had to be included as a payment to the seller, so that the seller's total payments in the year of sale exceeded 30% of the selling price. This contention, if upheld, would have resulted in the taxpayer-seller owing a tax in excess of $20,000.[32] The Ninth Circuit Court of Appeals affirmed the district court's rejection of the Commissioner's contention. The court appeared particularly concerned that the seller apparently had no way to control the purchaser's payment. It followed that the seller could not control the imposition of the tax.[33] The *Marshall* court regarded the Commissioner's contention as untenable when the congressional purpose of enacting section 453 was considered; it accordingly extended to this sale of a business its earlier mortgage exclusion rulings.[34] It was this giving of effect to congressional intent to provide a tax relief measure that was relied on by the

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28. Treas. Reg. § 1.453-4(c). *See* note 40 *infra* and accompanying text.

29. We can not agree that this regulation applies as petitioner argues it should in the instant case, even in principle.

In the case before us not only was there no mortgage, but the liabilities assumed were short term, and in fact the vendee paid off most of them in the year of sale. We are convinced that the regulation should be read to apply only to liabilities which are assumed but not paid in the year of sale.

45 T.C. at 553. See discussion accompanying notes 40-46 *infra*.

30. 357 F.2d 294 (9th Cir. 1966). The Tax Court in *Irwin* realized that the decision of the district court in this case was on appeal at the time of its determination and specifically rejected the reasoning of the district court, 241 F. Supp. 30 (S.D. Calif. 1964) which was specifically upheld. *See* 45 T.C. at 554, 555.

31. 357 F.2d at 296.

32. *Id.* at 295.

33. *Id.* at 296. In addition the Court expressed concern over the tax attributable to the sale exceeding the amount realized in cash in the year of sale and also the difficulty of the seller's ascertainment of what obligations had been paid.

34. *Id.* at 295.

fifth circuit in its reversal of the Tax Court in *Irwin*.

HISTORICAL DEVELOPMENT OF SECTION 453

The rationale of Installment Sales Reporting provided for by section 453 did not originate in the 1954 Internal Revenue Code but was actually promulgated by the Commissioner about 1920. The Commissioner sought to issue regulations which would allow taxpayers to avoid the potential tax hardship connected with installment sales.[35] The hardship was the same as presented in the *Marshall* and *Irwin* cases; the taxpayer who realized a gain from an installment sale often lacked sufficient liquidity to pay the tax on the realized gain if the full amount of the tax were imposed in the year of sale. The Commissioner, by regulation, sought to allow the tax to be paid in the year payment was received.[36] It was ruled, however, that the Commissioner lacked authority to issue such a regulation.[37] The logic and fairness of the Commissioner's position was not to be denied, however, and in 1926 Congress adopted the Installment Method of Reporting Income into statutory form and gave the Commissioner authority to implement the intent of the act through additional regulations.[38]

In response to this legislation the courts recognized the congressional intent to alleviate a potential burden and hardship on the taxpayers when in fact the selling taxpayer received only a small portion of the selling price in the year of sale.[39] The Commissioner also responded in a way calculated to benefit the taxpayer. Regulation 1.453-4[40] concerning the sale of mortgaged property pro-

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35. TREAS. REG. 45, Art. 42 (1919); TREAS. REG. 33, Art. 117 (1918).

36. *Id.* See, COMMENT, *supra* note 27, at 759.

37. *E.g.*, Six Hundred and Fifty West End Ave. Co., 2 B.T.A. 958 (1925); Hoover Bond Co., 1 B.T.A. 929 (1925); B.B. Todd, Inc., 1 B.T.A. 762 (1925).

38. REVENUE ACT of 1926, c. 27 § 212(d), 44 STAT. 23 (1926).

39. Commissioner v. South Texas Lumber Co., 333 U.S. 496, 503 (1948). See Burnet v. S. and L. Building Corp., 288 U.S. 406 (1933); S. REP. No. 52, 69th CONG., 1st SESS. 19 (1925); *Hearings Before the House Committee on Ways and Means of Revenue Revision*, 69th CONG. 80 (1925); 2 J. MERTENS, LAW OF FEDERAL INCOME TAXATION § 15.01 (*Rev. ed.* 1961).

40. TREAS. REG. § 1.453-4. Sale of real property involving deferred periodic payments—

(a) *In general.* Sales of real property involving deferred payments include (1) agreements of purchase and sale which contemplate that a conveyance is not to be made at the outset, but only after all or a substantial portion of the selling price has been paid, and (2) sales in which there is an immediate transfer of title, the vendor being protected by a mortgage or other lien as to deferred payments.

(b) *Classes of sales.* Such sales, under either paragraph (a)(1) or (2) of this section, fall into terms of sale, as follows:

vides in section (c) that if the property is sold subject to a mortgage, the amount of the mortgage assumed and paid by the purchaser is not to be calculated as a payment in the year of sale for purposes of of the 30% test of section 453.[41] This regulation has been extended to apply to personal property.[42]

The merits of extending the mortgage exclusion regulation to personalty by analogy have been discussed by two articles in which the authors proposed opposing views.[43] The view which criticizes the extension of regulation 1.453-4(c) to personalty sales asserts that if such extension is valid at all, it is valid only in cases where the debts of the vendor are similar to mortgages.

> Neither *McWilliams* nor *Cisler* would appear to support . . . [the statement that] . . . 'Debts of the vendor assumed by the purchaser are treated the same way as mortgages.' These cases stand only for the proposition that debts of the

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(1) Sales of real property which may be accounted for on the installment method, that is sales of real property in which (i) there are no payments during the taxable year of the sale or (ii) the payments in such taxable year (exclusive of evidences of indebtedness of the purchaser) do not exceed 30 per cent of the selling price.

(c) *Determination of "selling price."* In the sale of mortgaged property the amount of the mortgage, whether the property is merely taken subject to the mortgage or whether the mortgage is assumed by the purchaser; shall, for the purposes of determining whether a sale is on the installment plan, be included as a part of the "selling price"; and for the purpose of determining the payments and the total contract price as those terms are used in section 453, and §§ 1.453.1 through 1.453.7, the amount of such mortgage shall be included only to the extent that it exceeds the basis of the property. The term "payments does not include amounts received by the vendor in the year of sale from the disposition to a third person of notes given by the vendee as part of the purchase price which are due and payable in subsequent years. Commissions and other selling expenses paid or incurred by the vendor shall not reduce the amount of the payments, the total contract price, or the selling price.

The validity of this regulation would seem to be assured from the upholding of its virtually identical predecessor by the Supreme Court in Burnet v. S. and L. Building Corp., 288 U.S. 406 (1933). *See generally*, Stonecrest Corp. 24 T.C. 659, 665 (1955).

41. The regulation provides an exception when the mortgage assumed exceeds the basis of the property sold. Stephen A. Cisler, Jr., 39 T.C. 458 (1962).

42. *E.g.*, I.T. 2468 VIII-1 CUM. BULL. 159 (1929) (a ruling by the Commissioner in regards to the purchasers assumption of a debt still owed for the stock he purchased, it was ruled that such assumption is to be considered the same as the assumption of a mortgage); Stephen A Cisler, Jr. 39 T.C. 458, 466 (1962) (dictum which approves the application of the regulation to casual sales of personalty); Katherine H. Wilson, 20 B.T.A. 270 (1930) (sum of assumed liabilities such as taxes and mortgage interest governed by the regulation); J. W. McWilliams, 15 B.T.A. 329 (1929) (the term mortgages regarded as including the sellers long-term indebtedness on installment contracts for the sale of realty).

43. *Compare* Note, *Installment Sale Reporting of Income—Are Current Liabilities Similar to Mortgages?*, 1 CALIF. WEST. LAW REV. 154, 156 (1965) *with* Comment, *Assumption and Discharge of Seller's Liabilities as Year of Sale Payments for Purposes of I.R.C. Section 453*, 16 BUFF. LAW. REV. 758, 763 (1967) (hereinafter cited as Note and Comment respectively).

> vendor *similar to mortgages* are to be treated the same way as mortgages. . . . To extend the construction of the regulation beyond this rather narrow proposition would appear to stretch the role of judicial construction into the area of legislation.[44]

It would seem however that this author as well as the Tax Court

> fails to recognize the Commissioner's 1929 ruling which apparently involved the assumption of an unsecured debt [see note 42].
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> If, however, a similarity to mortgages is necessary in order for an assumed debt to be treated like a mortgage, a similarity in effectuating the Congressional intent of section 453 should be sufficient.[45]

This latter article, which advocates giving effect to Congress' intent, points out that regardless of whether a mortgage or an unsecured liability is assumed, excluding payments under both as year of sale payments relieves the seller from a "disproportionate tax liability, a liability which in some instances is greater than the down payment."[46]

The Spirit of 453 Prevails

The circuit court decisions in both the *Marshall* and the *Irwin* cases relied primarily on the intent of Congress which fostered the enactment of section 453. Citing *Commissioner v. South Texas Lumber Co.*[47] as authority, the *Irwin* court said that the purpose in enacting section 453 was

> to relieve taxpayers from having to pay an income tax in the year of sale based on the full amount of anticipated profits when in fact they had received in cash only a small portion of the sales price. . . .[48]

In their determination to give effect to this underlying philosophy, the fifth circuit in *Irwin* refused to be bound by the cases which the Tax Court had found to be controlling.[49] The court examined each case and found that none was directly in line with the fact situation presented in *Irwin*. The court, however, felt it necessary to distinguish these cases on the basis that they *cancelled* a debt of the seller, whereas in *Irwin* the seller's debt was

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44. Note, *supra* note 43, at 156.
45. Comment, *supra* note 43, at 763.
46. *Id.* at 763.
47. 333 U.S. 496 (1948). See note 39 *supra* and accompanying text.
48. Irwin v. Commissioner, 390 F.2d 91, 94 (5th Cir. 1968).
49. See cases and rulings cited notes 18 through 24 *supra* and accompanying text.

assumed.[50] Indeed, this may be the case, but the distinction seems somewhat tenuous. Regardless of whether the debt of the seller is cancelled or assumed, the effect is the same; the seller's liability is relieved, and, in a sense, he realizes the amount of his debt.[51] As suggested in an article which appeared while the appeal in *Irwin* was pending, it appears that the court would have been on firmer ground had they simply overruled the earlier cases. These cases appear to have been erroneously decided at least to the extent that they distinguished a cancellation from an assumption.[52]

The *Irwin* court criticized the distinction made by the Tax Court between cases where the seller's debt was *assumed* and those where it was *assumed and paid.*[53] Using the mortgage analogy derived from regulation 1.453-4(c) and the decision in *Marshall*, the court determined that assumed liabilities which were in fact paid must not be considered payments in the year of sale.[54] The *Irwin* court was convinced that there was no justice in distinguishing mortgages on real property from obligations connected with personal property. In either situation the taxpayer may be forced to liquidate his assets if he is to meet the burden of the tax imposed without the benefit of 453. If the spirit of section 453 will support the mortgage exclusion regulation of the Commissioner, it is difficult to see why it will not also support the Court's holding in *Irwin*. The court therefore concluded:

> We agree with the *Marshall* Court that these current liabilities, although assumed and paid, are not, under the statute, payments within the year of sale. They are excluded by reason of the mortgage assumption exception of the Regulation.[55]

Conclusion

This paper has attempted to present a summation as to the difficulties and issues presented by the assumption and payment of seller's obligations by the purchaser. Perhaps it would be preferable for prospective vendors and vendees to avoid the assumption and payment of these obligations; unfortunately this is not always possible. This is especially true where the sale involves a going concern and the obligations are connected to the operation of the business. It is often necessary, as well as practical, for the vendee to assume and pay the business obligations, many of which will be short term obligations which require payment in the year of

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50. Irwin v. Commissioner, 390 F.2d 91, 95 (5th Cir. 1968).
51. Although where the debt is assumed the seller may remain secondarily liable unless there is a novation. This should not be a ground for distinguishing the cancellation cases from the assumption cases. Furthermore, in *Irwin* the debt assumed was, in fact, paid.
52. Comment, *supra* note 43 at 764-5.
53. See cases cited note 24 *supra* and accompanying text.
54. Irwin v. Commissioner, 390 F.2d 91, 95 (5th Cir. 1968).
55. *Id.* at 96. *See*, 2 J. Mertens, *supra* note 39, § 15.16 (rev. ed. 1967).

sale. *Irwin* and *Marshall* are recognitions of this practical dilemma, and until some new argument is advanced by the Commissioner, they are a resolution of the problem. The result seems just as: (1) it is the implementation of a mere tax deferral not a tax avoidance; (2) the necessity for relief is apparent; and (3) the business liabilities are as much a part of the business as a mortgage is a part of the realty. It is hoped, therefore, that rather than attempting to frustrate the opinion of the two circuit courts, the Commissioner will enact detailed regulations for factual settings which may differ from that of *Irwin*, and have those regulations reflect the spirit of section 453.

WILLIAM S. KEISER

NEGLIGENCE—SCHOOL BUS DRIVER HELD TO ABSOLUTE LIABILITY

Van Gaasbeck v. Webatuck Central School District No. 1, 21 N.Y.2d 239, 234 N.E.2d 243 (1967)

In *Van Gaasbeck v. Webatuck Central School District No. 1*,[1] the Court of Appeals of New York held that a fourteen year old boy's contributory negligence did not prevent recovery in an action against a school district whose bus driver failed, as required by statutes: (1) to instruct the boy to cross the highway in front of the stopped bus; and (2) to keep the school bus halted with red signal lights flashing until the boy reached the opposite side of the highway. While recognizing that most statutory violations do not result in absolute liability, the court felt that such liability should apply to this particular violation of New York's Vehicle and Traffic Law.[2] The court held that violation of the statute resulted in absolute liability, and the pupil's contributory negligence was not a defense to the action against the school district.

Michael Van Gaasbeck and a friend were discharged from a school bus. The bus driver drove away before the boys crossed to the other side of the highway where they lived.[3] When the boys attempted to cross the highway, Michael was struck by an automobile. Michael, then fourteen years old, died a few days later. Wrongful death actions were commenced against the school district and the driver of the car that struck Michael. The trial court charged that Michael's contributory negligence would bar recovery against any of the defendants. The trial court felt that the bus driver's violation of the school bus statute was negligence *per se* and that contributory negligence would be a proper defense in such a case. A verdict for both defendants resulted and the appellate division affirmed.[4] The Court of Appeals, in a split decision, reversed as to the defendant school district but affirmed as to the driver of the automobile and ordered a new trial for a jury determination of proximate cause.

There is disagreement as to the common law duty owed by a

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1. 21 N.Y.2d 239, 234 N.E.2d 243 (1967).
2. N.Y. VEH. & TRAF. LAW § 1174 (McKinney 1960) provides:
   (b) The driver of school bus, when discharging pupils who must cross the highway, shall instruct such pupils to cross in front of the bus and the driver thereof shall keep such school bus halted with red signals flashing until such pupils have reached the opposite side of the highway.
3. The bus driver readily admitted that she had not performed her required duties. See Record at p. 189, Van Gaasbeck v. Webatuck Central School District No. 1, 21 N.Y.2d 239, 234 N.E.2d 243 (1967).
4. Van Gaasbeck v. Webatuck Central School District No. 1, 25 A.D. 2d 820, 270 N.Y.S.2d 384 (1966).

school bus driver to the students riding in a school bus.[5] Some courts have held that a school bus driver owes the highest degree of care to the students he is transporting.[6] Others have held that he is required to exercise only ordinary care and prudence.[7] Which alternative is adopted often depends on whether the school bus is acting as a common or private carrier of the children.[8]

Statutes in many states increase the bus driver's common law duty by requiring him to stop to the right of the road and use a flashing stop signal whenever a child must cross the highway on which the bus is stopped.[9] Many statutes also impose a duty on approaching motorists to stop while a bus driver is discharging or picking up passengers.[10] In actions against either an approaching

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5. *See generally*, 4 BLASHFIELD, CYCLOPEDIA OF AUTOMOBILE LAW AND PRACTICE § 2177 (1946).

6. See, *e.g.*, Van Cleave v. Illini Coach Co., 344 Ill. App. 127, 100 N.E.2d 398 (1951); Lincoln City Lines v. Schmidt, 245 F.2d 600 (8th Cir. 1957); Fidelity & Casualty Company of New York v. Talbot, 234 F.2d 425 (5th Cir. 1956); Landry v. Travelers Indemnity Company, 155 So. 2d 102 (La. App. 1963); Hawkins County v. Davis, 216 Tenn. 262, 391 S.W.2d 658 (1965); Sheffield v. Lovering, 51 Ga. App. 353, 180 S.E. 523 (1935) (statutory duty).

7. See, *e.g.*, Weems v. Robbins, 243 Ala. 276, 9 So. 2d 882 (1942); Shannon v. Central-Gaither Union School Dist., 133 Cal. App. 124, 23 P.2d 769 (1933); Campbell v. Patton, 227 Md. 125, 175 A.2d 761 (1961); Gaudette v. McLaughlin, 88 N.H. 368, 189 A. 872 (1937); Archuleta v. Jacobs, 43 N.M. 425, 94 P.2d 706 (1939).

8. See discussion in Hawkins County v. Davis, 216 Tenn. 262, 391 S.W.2d 658 (1965).

9. ARK. STAT. ANN. § 75-658(c) (Supp. 1967); CAL. VEHICLE CODE § 22112 (West 1960); COLO. REV. STAT. ANN. § 13-5-83(2) (1963); CONN. GEN. STAT. ANN. § 14-277 (Supp. 1967); DEL. CODE ANN. tit. 21 § 4166(b) (Supp. 1967); ILL. ANN. STAT. ch. 95½, § 196(b) (Smith-Hurd Supp. 1967); IOWA CODE ANN. § 321.372(1) (Supp. 1968); KY. REV. STAT. ANN. § 189.375 (1963); LA. REV. STAT. § 32:80(B) (1963); MASS. GEN. LAWS ANN. ch. 90, § 7B (Supp. 1968); MINN. STAT. ANN. § 169.43 (Supp. 1967); NEV. REV. STAT. § 392.410 (1963); N.H. REV. STAT. ANN. § 263:38-a (1966); N.J. REV. STAT. § 39:4-128.1 (Supp. 1967); N.D. CENT. CODE § 39-10-46(2) (Supp. 1967); PA. STAT. ANN. tit. 75 § 1018(d.1) (Supp. 1967); VT. STAT. ANN. tit. 23 § 1281(10); WASH. REV. CODE ANN. § 46.61.370(2) (Supp. 1967); WYO. STAT. ANN. § 31-150(b) (1967).

10. See, *e.g.*, ARK. STAT. ANN. § 75-658(d) (1957); COLO. REV. STAT. ANN. § 13-5-83(1) (1963); CONN. GEN. STAT. ANN. § 14-279 (Supp. 1967); DEL. CODE ANN. tit. 21 § 4166(a) (Supp. 1967); FLA. STAT. ANN. § 234.04 (1) (Supp. 1968); GA. CODE ANN. § 68-1667(a) (1967); ILL. ANN. STAT. ch. 95½, § 196(a) (Smith-Hurd Supp. 1967); IND. ANN. STAT. §§ 47-2131, 47-2132 (1965); IOWA CODE ANN. § 321.372 (Supp. 1968); LA. REV. STAT. § 32:80(A) (1963); MASS. GEN. LAWS ANN. ch. 90, § 14 (Supp. 1968); MINN. STAT. ANN. § 169.43 (Supp. 1967); MO. STAT. ANN. § 304.050 (1967); NEB. REV. STAT. § 79-488.02 (1966); N.J. REV. STAT. § 39:4-128.1 (Supp. 1967); N.M. STAT. ANN. § 64-18-46 (1953); N.C. GEN. STAT. § 20-217 (1965); N.D. CENT. CODE § 39-10-46(1) (Supp. 1967); PA. STAT. ANN. tit. 75 § 1018(a) (Supp. 1967); R.I. GEN. LAWS ANN. § 31-20-12 (Supp. 1966);

motorist or the school bus driver it has been held that proof of contributory negligence will generally bar recovery.[11]

In *Van Gaasbeck* the court had to decide what effect should be given to the bus driver's violation of a state statute requiring the driver to: (1) instruct all pupils to cross in front of the school bus; and (2) employ the stop signals of the bus while a student is crossing the street. If the violation of the statute were treated as negligence *per se* or merely evidence of negligence, contributory negligence would be a defense. If, on the other hand, the court ruled the statutory breach resulted in absolute liability, contributory negligence would not be a defense. Since the action against the approaching motorist was based solely on the common law duty of ordinary care, contributory negligence barred a recovery against him.

Where a statute prescribes a standard of conduct for the purpose of protecting persons from a certain type of risk, the statutory prescription of conduct is considered in determining civil liabilities when the harm to the person sought to be protected results from the breach of the statutory standard.[12] The courts are divided, however, on the effect to be given to the violation of the statute. A majority of American courts treat the unexcused violation of the statutory standard as negligence *per se*,[13] while a substantial minor-

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TENN. CODE ANN. § 59-851(a) (Supp. 1967); TEX. REV. CIV. STAT. art. 6701d § 104(a) (1960); VA. CODE ANN. § 46.1-190 (1967); WASH. REV. CODE ANN. § 46.61.370(1) (Supp. 1967); W. VA. CODE ANN. § 17C-12-7 (Supp. 1968); WYO. STAT. ANN. § 31-150(a) (1950).

11. See, *e.g.*, Lange v. Hoyt, 114 Conn. 590, 159 A. 575 (1932); Pond v. Somes, 302 Mass. 587, 20 N.E.2d 449 (1939); Hughes v. Thayer, 229 N.C. 773, 51 S.E.2d 488 (1949); Fedorovich v. Glenn, 337 Pa. 60, 9 A.2d 358 (1939); Ashley v. Ensley, 44 Wash. 2d 74, 265 P.2d 829 (1954); Machenheimer v. Falknor, 144 Wash. 27, 255 P. 1031 (1927); Foster v. Einer, 69 Cal. App. 341, 158 P.2d 978 (1945); Shannon v. Central-Gaither Union School Dist., 133 Cal. App. 124, 23 P.2d 769 (1933); Wheaton v. Conkle, 57 Ohio App. 373, 14 N.E.2d 363 (1937). *But see* International Harvester Co. v. Williams, 222 Ala. 595, 133 So. 275 (1931); Sepulvado v. General Fire & Casualty Co., 146 So. 2d 428 (La. App. 1962). *See generally*, Prosser, *Contributory Negligence As Defense to Violation of Statute*, 32 MINN. L. REV. 105 (1948).

12. *See generally*, HARPER AND JAMES, 2 THE LAW OF TORTS §§ 17.5, 17.6 (1956); PROSSER, LAW OF TORTS 202 (1964); Lowndes, *Civil Liability by Criminal Legislation*, 16 MINN. L. REV. 361 (1932); Morris, *Criminal Statutes and Tort Liability*, 46 HARV. L. REV. 453 (1932).

13. See, *e.g.*, Dobbertin v. Johnson, 95 Ariz. 356, 390 P.2d 849 (1964); Lambotte v. Payton, 147 Colo. 207, 363 P.2d 167 (1961) (ordinance); Richardson v. Fountain, 154 So. 2d 709 (Fla. 1963) (statutes other than traffic); Teague v. Keith, 214 Ga. 853, 108 S.E.2d 489 (1959); Bale v. Perryman, 85 Idaho 435, 380 P.2d 501 (1963); New York Central R.R. v. Glad, 242 Ind. 450, 179 N.E.2d 571 (1962); Kroblin Refrigerated X-Press, Inc. v. Ledvina, 256 Iowa 229, 127 N.W.2d 133 (1964); Commonwealth v. Ragland Potter Company, 305 S.W.2d 915 (Ky. App. 1957); Moses v. Mosley, 146 So. 2d 263 (La. 1962); Breezley v. Spiva, 313 S.W.2d 691 (Mo. 1958); Hayes v. Hagemeir, 75 N.M. 70, 400 P.2d 945 (1963); Drum v. Bisaner, 252 N.C. 305, 113 S.E.2d 560 (1960); Kaplan v. Philadelphia Trans. Co.,

ity have held that it is merely evidence of negligence.[14] Where a violation of a statute constitutes evidence of negligence or negligense *per se*, contributory negligence and assumption of risk are proper defenses just as in an action based on a violation of a common law duty.[15]

There are, however, statutes intended to protect a particular class of persons against their own inability to protect themselves and courts have usually found a legislative intent to remove the defense of contributory negligence from actions based on the violations of these statutes.[16] These statutes have been construed as placing the entire responsibility upon the defendant, requiring him to protect those persons who are exercising reasonable care as well as those who may be exercising no care at all.[17] Typical of this type of statute are child labor acts,[18] safety statutes for the benefit

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404 Pa. 147, 171 A.2d 166 (1961); Green v. Sparks, 232 S.C. 414, 102 S.E.2d 435 (1958); Zakizewski v. Hyronimus, 81 S.D. 428, 136 N.W.2d 572 (1965); Alex v. Armstrong, 215 Tenn. 276, 385 S.W.2d 110 (1964); Eubanks v. Wood, 304 S.W.2d 567 (Tex. Civ. App. 1967); Klafta v. Smith, 17 Utah 2d 65, 404 P.2d 659 (1965); White v. Gore, 201 Va. 239, 110 S.E.2d 228 (1959); Clevenger v. Fonseca, 55 Wash. 2d 70, 345 P.2d 1098 (1959); Meihost v. Meihost, 29 Wis. 2d 537, 139 N.W.2d 537 (1966).

14. *E.g.*, Martinson v. Scherbel, 268 Minn. 509, 129 N.W.2d 802 (1964) (prima facie); Alston v. Forsythe, 226 Md. 121, 172 A.2d 474 (1961); Falvey v. Hamelburg, 347 Mass. 430, 198 N.E.2d 400 (1964); Peterson v. Skiles, 173 Neb. 470, 113 N.W.2d 628 (1962); Mattero v. Silverman, 71 N.J. Super. 1, 176 A.2d 270 (1961); Smith v. Ohio Oil Co., 10 Ill. App. 2d 67, 134 N.E.2d 526 (1956).

15. *E.g.*, Richardson v. Fountain, 154 So. 2d 709 (Fla. 1963); Bale v. Perryman, 85 Idaho 435, 380 P.2d 501 (1963); Dart v. Pure Oil Co., 223 Minn. 526, 27 N.W.2d 55 (1947); Mattero v. Silverman, 71 N.J. Super. 1, 176 A.2d 270 (1961). *See generally*, Annot. 10 A.L.R.2d 853 (1950); Prosser, *Contributory Negligence as Defense to Violation of Statute*, 32 MINN. L. REV. 105 (1948).

16. See, *e.g.*, Schmid v. United States, 154 F. Supp. 81 (E.D. Ill. 1957); Tamiami Gun Shop v. Klein, 116 So. 2d 421 (Fla. 1959); Bryntesem v. Carroll Const. Co., 27 Ill. 2d 566, 190 N.E.2d 315 (1963); Koenig v. Patrick Const. Corp., 298 N.Y. 313, 83 N.E.2d 133 (1948); Schelin v. Goldberg, 188 Pa. Super. 341, 146 A.2d 648 (1958).

The Restatement of Torts 2d. § 483 (1965) comment c states:

> There are, however, exceptional statutes which are intended to place the entire responsibility upon the defendant. A statute may be found to have that purpose particularly where it is enacted in order to protect a certain class of persons against their own inability to protect themselves. . . . In such a case the purpose of the statute would be defeated if . . . contributory negligence . . . were permitted to bar his recover.

17. *E.g.*, Osborne v. Salvation Army, 107 F.2d 929 (2d Cir. 1939); Tamiami Gun Shop v. Klein, 116 So. 2d 421 (Fla. 1959); Bryntesen v. Carroll Const. Co., 27 Ill. 2d 566, 190 N.E.2d 315 (1963); Koenig v. Patrick Const. Corp., 298 N.Y. 313, 83 N.E.2d 133 (1948); Schelin v. Goldberg, 188 Pa. Super. 341, 146 A.2d 648 (1958).

18. *E.g.*, Terry Dairy Co. v. Nalley, 146 Ark. 448, 225 S.W. 887

of employees,[19] statutes for the protection of intoxicated persons,[20] and statutes forbidding the sale of dangerous articles to minors.[21]

Statutes concerning school buses are very common in the United States,[22] and violations thereof by school bus drivers or approaching motorists have generally been construed as constituting, at most, negligence *per se*.[23] Contributory negligence, therefore, has been a proper defense to actions brought on behalf of injured students.[24] *Van Gaasbeck*, by treating the statutory violation as imposing absolute liability, in effect eliminated the defense of contributory negligence in this type of case.

The statute in *Van Gaasbeck* did not expressly state that a violation thereof was to create absolute liability.[25] The court inferred absolute liability since the statute was designed to protect a class of persons from a definable hazard which they were incapable of avoiding.[26] The driver, according to the court, had an unvarying duty to supervise and secure the safety of the school children. In considering a similar factual situation the Supreme Court of Wisconsin stated:

> No rule could completely eliminate the hazards of crossing but a rule which requires a driver to see that the road is clear and that the children cross under his observation comes as close to securing safety as is reasonably possible. . . . Even when the children know the rules of care it is within their nature at times to be careless, hurried and impulsive and it is these propensities the rule seeks to guard against.[27]

(1920); Dusha v. Virginia & Rainey Lake Co., 145 Minn. 171, 176 N.W. 482 (1920); Washburn v. Empire Printing Co., 249 S.W. 709 (Mo. 1923); Lenahan v. Pittston Coal Mining Co., 218 Pa. 311, 67 A. 642 (1907).

19. *E.g.*, Osborne v. Salvation Army, 107 F.2d 929 (2d Cir. 1939); Schmid v. United States, 154 F. Supp. 81 (E.D. Ill. 1957); Bryntesen v. Carroll Const. Co., 27 Ill. 2d 566, 190 N.E.2d 315 (1963); Koenig v. Patrick Const. Corp., 298 N.Y. 313, 83 N.E.2d 133 (1948).

20. *E.g.*, Mayes v. Byers, 214 Minn. 54, 7 N.W.2d 403 (1943); Soronen v. Olde Milford Inn, Inc., 46 N.J. 582, 218 A.2d 630 (1966); Schelin v. Goldberg, 188 Pa. Super. 341, 146 A.2d 648 (1958). *But see* Ramsey v. Anctil, 106 N.H. 375, 211 A.2d 900 (1965).

21. See, *e.g.*, Bass v. Flowers, 177 So. 2d 239 (Fla. 1965); Tamiami Gun Shop v. Klein, 116 So. 2d 421 (Fla. 1959); McMillen v. Steele, 275 Pa. 584, 119 A. 721 (1923).

22. See statutes cited in notes 9 and 10 *supra*.

23. See, *e.g.*, Morgan v. Carolina Coach Co., 225 N.C. 668, 36 S.E.2d 263 (1945) (approaching motorist); Reeves v. Tittle, 129 S.W.2d 364 (Tex. Civ. App. 1939); Dishinger v. Suburban Coach Co., 84 Ga. App. 498, 66 S.E.2d 242 (1951). *Cf.* Clevenger v. Fonseca, 55 Wash. 2d 25, 345 P.2d 1098 (1959).

24. See cases cited in note 11 *supra*.

25. The court felt, however, that such an intent could be implied from the language which stated that the driver "*shall* instruct such pupils" and he "*shall* keep such school bus halted. . . ." Van Gaasbeck v. Webatuck Central School District No. 1, 21 N.Y.2d 239, 244, 234 N.E.2d 243, 246 (1967).

26. Van Gaasbeck v. Webatuck Central School District No. 1, 21 N.Y.2d 239, 244, 234 N.E.2d 243, 246 (1967).

27. Verbetem v. Huettl, 253 Wis. 510, 520, 34 N.W.2d 803, 808 (1948). In the *Verbetem* decision, the Supreme Court of Wisconsin apparently eliminated contributory negligence as a defense but the court erroneously held that the violation of the statute was only negligence *per se*.

While *Van Gaasbeck* imposes absolute liability for a violation of a motor vehicle statute, it is doubtful that the New York Court of Appeals will extend absolute liability beyond school bus cases. The court specifically stated that absolute liability will not usually be imposed for a violation of a statute. The New York courts, furthermore, have consistently held that a violation of a motor vehicle statute is negligence *per se* and the court in *Van Gaasbeck* expressed no intent to overrule these cases.

Whether the doctrine of absolute liability will be imposed against approaching motorists who fail to stop at a school bus's signal was not discussed in *Van Gaasbeck*. While courts have imposed the doctrine of negligence *per se* in these cases, no court appears to have imposed absolute liability on an approaching motorist. Perhaps the distinguishing factor between an approaching motorist and a school bus driver is the latter's duty and ability to supervise the children to see that their safety is secure from all hazards while they are crossing the highway.

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