

CALIFORNIA FRANCHISE TAX BOARD

Legal Ruling No. 257

August 21, 1964

PERSONAL INCOME – HOLDING PERIOD – UNHARVESTED CROPS

Syllabus:

For a number of years the taxpayers owned and operated a ranch on which they grew grain, tomatoes, peaches, prunes and other agricultural products. Various parcels of land which comprises the ranch were purchased by the taxpayers in 1930, 1944 and 1954. The fruit trees in the orchards were planted shortly after the land was acquired. In 1956 the land together with the unharvested crops thereon was sold.

There is no question but that the property sold constituted property used in a trade or business. From information submitted the taxpayer's gains from the sale of property used in their trade or business exceeded their losses, therefore, the gains are entitled to capital gain treatment (Section 18181).

What is the holding period of the unharvested crops in order that the proper percentage of gain may be included in taxable income?

Section 18182(c) provides that where land is used in a trade or business and is held for more than one year the unharvested crop growing on that land is also considered as "property used in the trade or business" if the crop and the land are sold at the same time and to the same person. The regulations (Reg. 17721-17724(d)) state that "the length of time for which the crop, as distinguished from the land, has been held is immaterial".

The above section and regulation were adopted from and are substantially the same as Section 117(j) of the Federal 1939 Code, now Section 1231(b)(4) of the 1954 Internal Revenue Code and Regulation 1.1231 (f) issued thereunder. The federal provision was originally enacted in 1951 due to a split of opinions between the various district courts and the tax court. Some courts held that an unharvested crop or immature fruit was property held for sale in the ordinary course of business, the sale of which resulted in ordinary income. The other courts rejected this position and held the sale of unharvested crops together with the land to which they were affixed constituted sales of real property used in the trade or business. Congress adopted the latter view, i.e., that (1) unharvested crops are real property and (2) unharvested crops in any stage of development are not property held primarily for sale to customers in the ordinary course of the taxpayer's trade or business.

The Senate Finance Committee Report (U.S. Code Cong. and Adm. Service, 1st

Session, 82nd Congress, p. 2017) clearly indicates that it was contemplated by Congress, and the state legislature in adopting the federal statute, that growing crops and fruit were to receive identical treatment. Since the land and the unharvested crop is treated as an inseparable unit, it is of no consequence when the crop was planted or when the trees bear fruit. Thus, it is clear that the holding period of the land is controlling. Any other construction of the statute would lead to a conclusion not contemplated by the legislature and must be avoided. San Joaquin Irrigation Co. v. Stevinson, 164 Cal. 221.