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### The Federal Income Tax Consequences of the Bobble Supreme Phenomenon

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The Federal Income Tax Consequences  
of the Bobble Supreme Phenomenon

*Leandra Lederman*

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# The Federal Income Tax Consequences of the Bobble Supreme Phenomenon

*Leandra Lederman*

“*B*EWARE THE IDES OF APRIL ... .”

(With apologies to William Shakespeare, and  
admitted artistic license in that the Ides  
of April is the thirteenth of April.)



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*Leandra Lederman is the William W. Oliver Professor of Tax Law at Indiana University School of Law – Bloomington. Portions of this document were drafted while she was on the faculty of the George Mason University School of Law. Adrianna Marks, Rachel Polsky, Amanda Roettger, and Mandi Scott provided valuable research assistance.*

**DEPARTMENT OF TAXATION****The Green Bag Journal****26 GBJ Part 1**

[REG-10401008-06]

RIN 2848-LL66

**Taxation of Bobble Supreme Transactions**

**AGENCY:** Green Bag Journal (GBJ).  
**ACTION:** Notice of proposed rulemaking.

**SUMMARY:** This document contains proposed regulations that provide guidance regarding the income tax consequences of the receipt of bobble Supremes, events in the course of ownership of bobble Supremes, and the disposition of bobble Supremes. The proposed regulations will affect owners and custodians, former owners and custodians, and prospective owners and custodians of bobble Supremes, as well as anyone who does not read this document in full and send it to ten friends.

**DATES:** Written or electronic comments must be received by April 16, 2007 to be assured of consideration.

**ADDRESSES:** Send submissions to: L:LED:GBJ (REG-10401008-06), room 415, George Mason University School of Law, 3301 N. Fairfax Drive, Arlington, VA 22201. Submissions may be hand-delivered Monday through Friday between the capriciously selected hours of 10 a.m. and 3 p.m. to L:LED:GBJ (REG-10401008-06), room 415, George Mason University School of Law, 3301 Fairfax Drive, Arlington, VA 22201, or sent electronically via the *Green Bag Journal* Internet site at [www.greenbag.org/regis](http://www.greenbag.org/regis).

**FOR FURTHER INFORMATION CONTACT:** Concerning the proposed regulations, Leandra Lederman, (812) 855-6149; concerning submission of comments, Ross E. Davies, (703) 993-8049 (not toll-free numbers).

**SUPPLEMENTARY INFORMATION:****Paperwork Production Act**

The information contained in this

notice of proposed rulemaking has been submitted to the *Green Bag Journal* Editorial Office for review in accordance with the Paperwork Production Act (44 GBJ 3507(d)).

*Estimated total annual reading burden:* 855 hours.

*Estimated average burden per reader:* .5 hours.

*Estimated number of readers:* 1,710.

*Estimated annual frequency of reading:* once.

**Background**

In 2003, the Editorial Board of the *Green Bag Journal* commissioned and distributed a total of 1,008 then-Chief Justice Rehnquist bobbleheads, each one individually numbered on the bottom. In early 2004, the bobble Chief was followed by a Justice Stevens bobblehead. Next, the Justice O'Connor bobblehead appeared, standing alongside a bobbling bovine. She was followed by a Justice Scalia bobblehead, and, most recently, Justice Kennedy. These Supreme figurines (or their equivalent in the form of bearer certificates) were sent by the *Green Bag* to many subscribers as well as other friends of the *Green Bag*.<sup>1</sup>

Demand for the bobble Supremes has not been limited to existing recipients, however, and bobble longing has even inspired poetry.<sup>2</sup> Given the importance of the bobble Supreme phenomenon to the national economy, the time has come for guidance on the federal income tax consequences of their receipt and transfer. Fortunately, draft proposed regulations on the federal income tax treatment of the *Green Bag's* bobbleheads recently surfaced.<sup>3</sup> Unfortunately, proposed regulations cannot be relied upon not to change. See CC-2003-014, *reprinted at* 2003 TNT 93-7. Even worse, these particular proposed regulations are a mere draft that have not been officially sanctioned. As they will

never appear in the **Federal Register**, they are offered below for their novelty value.<sup>4</sup>

**Explanation of Provisions***Overview*

The purpose of the proposed rules is to address the federal income tax consequences of receipt of bobble Supremes, events in the course of ownership of bobble Supremes, and dispositions of bobble Supremes; that is, to provide the income tax law of the bobble Supreme.<sup>5</sup>

*Found Bobble Supremes*

The proposed regulations provide guidance on the tax treatment of acquisitions of bobble Supremes, including found bobble Supremes. The proposed regulations provide that found bobble Supremes are governed by Treasury Regulation section 1.61-14(a), which provides that “[t]reasure trove, to the extent of its value in United States currency, constitutes gross income for the taxable year in which it is reduced to undisputed possession.”

An important example of putative treasure trove was the 1998 season home run baseballs. “In the rather quaint language of the regulations, the baseball is a sort of treasure trove, and like all treasure trove its value is included in gross income on accession to ownership. Or so says the regulation.” Lawrence A. Zelenak & Martin J. McMahon, Jr., *Taxing Baseballs and Other Found Property*,

<sup>4</sup> As the text suggests, this document is for recreational use only. Actual tax results may vary. Any resemblance of the contents of this document to tax or legal advice to any person, real or hypothetical, living or dead, is entirely coincidental. Of course, no implication that tax advice does not constitute legal advice is intended. *Cf.* United States v. Lawless, 709 F.2d 485, 487 (7th Cir. 1983) (“Several courts have held that the preparation of a tax return, while it may require some knowledge of the law, is primarily an accounting service.”).

<sup>5</sup> DISCLOSURE: Even though this document contains the word “tax,” it is not intended to be used (1) to avoid any tax penalty; (2) to promote, market or recommend to any other party any transaction or other matter discussed in it; or (3) as a replacement for the Internal Revenue Code. *Cf.* Sheryl Stratton, *Circular 230 E-Mails, T-Shirts Attain “Legendary” Status*, 2005 TNT 127-1 (July 5, 2005).

<sup>5</sup> *Cf.* Frank H. Easterbrook, *Cyberspace and the Law of the Horse*, 1996 U. CHI. LEGAL F. 207 (1996).

<sup>1</sup> See <http://www.greenbag.org/bobbleheads>.

<sup>2</sup> See MacKenzie Fallow, *Waiting for Scalia*, 6 GREEN BAG 2D inside cover (Spring 2006).

<sup>3</sup> Footnotes to the draft proposed regulations were added by the author. *Cf.* Andrew J. McClurg, *The World's Greatest Law Review Article*, 81 A.B.A. J. 84, 85 n.28343 (Oct. 1995); Arthur D. Austin, *Footnotes as Product Differentiation*, 40 VAND. L. REV. 1131 (1987).

84 TAX NOTES 1299, 1300 (1999) (arguing that the regulation is wrong).

The result is not necessarily the same for a hypothetical finder who returns a wayward baseball or bobble Supreme to its rightful owner. In the baseball situation, then-Commissioner of the IRS, Charles Rossotti, promptly "explained that a fan who caught a valuable ball and immediately returned it would not have taxable income, 'based on an analogy to principles of tax law that apply when someone immediately declines a prize or returns unsolicited merchandise.'" *Id.* at 1299. His statement that the Internal Revenue Service (IRS) would not play hardball on this issue forestalled Congress from acting on a special bill providing that catching and returning a home run baseball did not give rise to tax consequences. *Id.* at 1300. (Instead, Congress called the IRS out that year, and passed a bill to reform it.) No one has yet pitched a bill to benefit bobble Supreme finders, perhaps because the *Green Bag's* bobble Supremes have not yet attained the iconic status of baseballs, nor is the value of bobble Supremes in the same ballpark as the 1998 home run baseballs.<sup>6</sup> As bobble Supremes are certainly treasured, the Supreme Court may ultimately have to play the role of umpire on this important issue.

#### Depreciation of Bobble Supremes

The proposed regulations treat bobble Supremes as nondepreciable. Although, in general, property used in a trade or business, including office furniture, can be depreciated, art objects cannot. In a pair of cases, the United States Tax Court considered the depreciability of an antique violin bow and an antique bass viol. In those cases, the antique instruments were used by musicians because of their superior sound quality. The instruments had increased in value, although they had experienced wear and tear from active use. The Tax Court ruled that the instruments were depreciable, and was affirmed in both cases. See *Simon v. Commissioner*, 103 T.C. 247

(1994), *aff'd*, 68 F.3d 41 (2d Cir. 1995); *Liddle v. Commissioner*, 103 T.C. 285 (1994), *aff'd*, 65 F.3d 329 (3d Cir. 1995).

These cases suggest that what categorizes a collectible as a nondepreciable work of art on the one hand or a depreciable business asset on the other is whether it "suffer[s] substantial wear and tear through regular, active, and physical use in the . . . business." Anthony P. Polito, *Fiddlers on the Tax: Depreciation of Antique Instruments Invites Reexamination of Broader Tax Policy*, 13 AM. J. TAX POL'Y 87, 111 (1996). The proposed regulations reflect the view that a bobble Supreme kept on display in an office is distinguishable from a musical instrument played by a professional musician, although some wax lyrical about bobble Supremes and claim that bobble Supremes actually invite physical contact that subjects them to wear and tear.

#### Character of Bobble Supremes

The proposed regulations provide that bobble Supremes constitute capital assets unless they fall within any of the exceptions in section 1221 of the Internal Revenue Code (Code).

The Code does not expressly provide whether capital gain on the sale of a bobble Supreme will be taxed at general capital gains rates or at the higher 28 percent rate applicable to collectibles. See I.R.C. § 1(h)(4)(A)(i). Code section 1(h)(5) uses the definition of collectible in section 408(m). That section defines "collectible" as: "(A) any work of art, (B) any rug or antique, (C) any metal or gem, (D) any stamp or coin, (E) any alcoholic beverage, or (F) any other tangible personal property specified by the Secretary for purposes of this subsection." I.R.C. § 408(m)(2). In a 1982 proposed regulation, the Secretary designated as collectibles (1) musical instruments and (2) "[a]ny historical object (documents, clothes, etc.)" Prop. Treas. Reg. § 1.408-10(a)(6), (7). Notice of Proposed Rulemaking EE-148-81 (9/14/82), 46 Fed. Reg. 2794 (1984). We have determined that it is the age of the bobble Supremes, not that of the Supreme Court Justices they represent, that determines "historical object" status, and that the bobble Supremes do not constitute

historical objects at the present time.

If the bobble Supremes do not fall within the categories provided in section 408(m) and its accompanying regulations, we question whether their alleged collectible status nonetheless renders them collectibles for tax purposes. An article on the taxation of eBay auctions, Susan Albring et al., *Beanie Baby Billions? Unpaid Taxes on Internet Auctions*, 87 TAX NOTES 1153, 1157 (2000), assumes that Beanie Babies and other "collectibles" sold on eBay are subject to a 28 percent tax rate under section 1(h). Beanie Babies do not seem to be historical objects; the first Beanie Babies were produced in 1993. See <http://www.aboutbeanies.com/original9.html> (describing the introduction of the "original 9"<sup>7</sup> at the World Toy Fair in New York City in 1993). The proposed regulations do not determine whether a bobble Supreme (or a Beanie Baby) constitutes "a work of art" under section 408(m)(2)(A) or otherwise qualifies as a collectible for purposes of section 1(h). The *Green Bag Journal* invites comments on this important character issue.

#### Bartered Bobble Supremes

Barter exchanges generally are taxed in the same manner as sales. For example, Treasury Regulation section 1.61-6 provides, "[g]ain realized on the sale or exchange of property is included in gross income, unless excluded by law." Treas. Reg. § 1.61-6(a); see also Treas. Reg. § 1.1001-1(a) ("Except as otherwise provided in subtitle A of the Code, the gain or loss realized from the conversion of property into cash, or from the exchange of property for other property differing materially either in kind or in extent, is treated as income or as loss sustained.").

However, gain realized in an exchange for "like kind" property may not be recognized (except to the extent of non-like kind property, i.e., boot,<sup>8</sup> received, see I.R.C. § 1031(b)), if

<sup>7</sup> Possibly a reference to the number of players on a baseball team—or to the number of innings in a game. Also possibly a code (but not Code) reference to the eventual number of original Green Bag bobble Supremes.

<sup>8</sup> Boot may, but generally does not, constitute footwear.

<sup>6</sup> See generally Michael J. Yelnosky, *If You Write It, (S)he Will Come: Judicial Opinions, Metaphors, Baseball, and "The Sex Stuff,"* 28 CONN. L. REV. 813 (1996).

the property exchanged was held for productive use in a trade or business or for investment and the property received will be held either for productive use in a trade or business or for investment, I.R.C. § 1031(a)(1).

Although the regulations under section 1031 group property into classes, see Treas. Reg. § 1.1031(a)-2(b), because, under the proposed regulations, bobble Supremes are not depreciable, an exchange of a bobble Supreme for property that will be held for productive use in a trade or business or for investment will be covered by section 1031 only if the property received is “like kind” property; “[n]o like classes are provided for these properties.” Treas. Reg. § 1.1031(a)-2(c).

“As used in section 1031(a), the words like kind have reference to the nature or character of the property and not to its grade or quality.” Treas. Reg. § 1.1031(a)-1(b). Based on the nature and character of bobble Supremes, the proposed regulations provide that bobble Supremes are like kind to other like bobble Supremes. They do not provide guidance on what constitutes likeness for the Justices themselves. They also do not address the important question of what other property, if any, shares the underlying nature or character a bobble Supreme investment represents. The *Green Bag Journal* invites comments on this set of issues.

**Proposed Effective Date**

These regulations are proposed to be applicable to taxable years beginning on or after sunset on the date that is 60 days after they are first applied.

**Special Analyses**

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It has also been determined that section 553(b) of 5 U.S.C. chapter 5 does not apply to these regulations, and, because these regulations do not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant

to section 7805(f) of the Code, this notice of proposed rulemaking will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact on small businesses.<sup>9</sup>

**Request for Comments**

Although these proposed regulations will never be adopted as final regulations, consideration will be given to any written (a signed original) or electronic comments that are submitted timely to the *Green Bag Journal*. The *Green Bag* invites suggestions for rules regarding other transactions, particularly potentially abusive transactions (such as the recently discovered SOL transaction), involving bobble Supremes. Comments may be made available for public inspection in the offices of the *Green Bag Journal* or on its Internet site.

**Drafting Information**

The principal author of these proposed regulations is Leandra Lederman of Indiana University School of Law—Bloomington. However, other tax professionals participated in their development. Of course, responsibility for any errors rests solely with them.

**List of Subjects**

26 GBJ Part 1  
Income taxes.

**Proposed Amendments to the Regulations**

Accordingly, 26 GBJ part 1 is proposed to be amended as follows:

Section 1.1111-1 is added to read as follows:

**§ 1.1111-1 Taxation of Bobble Supreme transactions.**

Q-1. How are transactions in bobble Supremes treated for federal income tax purposes?

A-1. (a) General rule. The federal income tax treatment of a bobble Supreme transaction depends on the

<sup>9</sup> Okay, okay, this notice will not really be submitted to the Chief Counsel for Advocacy of the Small Business Administration (at least not by the drafter). In fact, the whole [text redacted] paragraph is a quotation from REG-135866-02, reprinted at 2006 TNT 106-9.

type of transaction and the tax status of those engaging in the transaction, except as otherwise provided.

(b) Definitions. For purposes of this section, the following definitions apply—

(1) Bobble Supreme means a limited edition bobblehead figure in the image of a Justice of the Supreme Court of the United States and originally distributed by the *Green Bag Journal*, including the Chief Justice Rehnquist bobblehead, the Justice Stevens bobblehead, the Justice O’Connor bobblehead, the Justice Scalia bobblehead, and the Justice Kennedy bobblehead.

(2) Chief Justice Rehnquist bobblehead means any of the 1,008 bobblehead figures in the image of the late United States Supreme Court Chief Justice Rehnquist and originally distributed by the *Green Bag Journal*.

(3) Justice Stevens bobblehead means any of the 1,116 bobblehead figures in the image of United States Supreme Court Justice Stevens and originally distributed by the *Green Bag Journal*.

(4) Justice O’Connor bobblehead means any of the 1,386 bobblehead figures in the image of retired United States Supreme Court Justice O’Connor and originally distributed by the *Green Bag Journal*.

(5) Justice Scalia bobblehead means any of the 1,710 bobblehead figures in the image of United States Supreme Court Justice Scalia and originally distributed by the *Green Bag Journal*.

(6) Justice Kennedy bobblehead means any of the 1,710 bobblehead figures in the image of United States Supreme Court Justice Kennedy and originally distributed by the *Green Bag Journal*.

(7) Qualified bobble Supreme transaction means a transaction involving one or more bobble Supremes that is designated as such by the Secretary.

(a) Receipt of bobble Supremes.

Q-2. Do *Green Bag* subscribers have income on the receipt of bobble Supremes from the *Green Bag* sent to them in their capacity as subscribers?

A-2. No. Subscribers who receive a bobble Supreme or bobble Supremes along with a paid subscription will

be treated as having purchased the bobble Supreme(s).<sup>10</sup>

Q-3. Does a case of bobble Supremes found on the street constitute gross income under section 61?

A-3. Yes. Although the number of bobble Supremes in a case is less than a gross, the case of bobble Supremes constitutes gross income. See section 1.61-14(a) for further guidance concerning treasure trove.

Q-4. Does a bobble Supreme found in someone else's mailbox constitute gross income under section 61?

A-4. Yes. The "check-the-box" regulations are not a reference to a means of tax-free acquisition of bobble Supremes.

Q-5. Do bobble Supremes received as compensation constitute gross income?

A-5. Yes, bobble Supremes received as compensation constitute gross income, except as otherwise provided.

Q-6. Is there a special exclusion from gross income for reality show survivors?

A-6. See A-13.<sup>11</sup>

Q-7. Is there a special exclusion from gross income for parents of airline employees?

A-7. Not yet, but see A-1(b)(7).

Q-8. How much gross income must be reported on the receipt of a bobble Supreme received as compensation?

A-8. The fair market value of a bobble Supreme received in a taxable transaction must be reported as gross income. We will presume bobble Supreme markets fair in the absence of clear and convincing contrary evidence presented by the taxpayer.

Q-9. What are the income tax consequences of receiving a bobble Supreme by bequest, devise or inheritance?

A-9. Under section 102, property received by bequest, devise or inheritance does not constitute gross income. The provisions of section 1014 apply to determine the recipient's basis in the bobble Supreme unless the decedent dies

after December 31, 2009; what the law will be once 2010 rolls around is one's guess.

*(b) Events during the course of ownership of bobble Supremes.*

Q-10. Can bobble Supremes displayed in a law or business office be depreciated?

A-10. No, bobble Supremes displayed in a law or business office cannot be depreciated.

Q-11. May a taxpayer take a deduction if the taxpayer's bobble Supreme experiences theft, decapitation, defenestration, or other casualty?

A-11. Subject to the provisions of section 165 and the regulations thereunder, a taxpayer is entitled to a theft loss or casualty loss deduction (as the case may be). However, your kinder, gentler tax authority recommends a closed and locked display case in a windowless room to reduce the likelihood of such an eventuality.

*(c) Dispositions of bobble Supremes.*

Q-12. What are the tax consequences of the sale of a bobble Supreme by its owner?

A-12. The tax consequences of the sale of a bobble Supreme are determined under Code sections 61, 1001, 1221, and the regulations thereunder, except as otherwise provided.

(a) Gain or loss. Except as otherwise provided in Subtitle A of the Code, the gain or loss realized from the conversion of a bobble Supreme into cash is treated as income or loss sustained.

(b) Character. A bobble Supreme is a capital asset except to the extent that it falls within an exception in Code section 1221.

Q-13. [This question intentionally left blank.]

A-13. Under Code section 7623, the IRS has the authority "to pay such sums as [it] deems necessary for— (1) detecting underpayments of tax, and (2) detecting and bringing to trial and punishment persons guilty of violating the internal revenue laws or conniving at the same . . . ."

Q-14. Is a donation of a bobble Supreme to charity deductible?

A-14. A contribution of a bobble Supreme to a charitable organization within the definition of Code section 170(c) actually paid during the taxable year will be allowable as a deduction to the extent allowable by the Code.<sup>12</sup> Bobble Supremes are tangible personal property, so the deduction for a donated bobble Supreme with a value greater than its basis will be limited to basis unless the bobble Supreme would have given rise to long-term capital gain if sold on the date of the contribution and it is contributed to either (1) a charity that will use it in a manner related to the purpose or function that constitutes the basis for the charity's tax exemption or (2) a governmental unit for a use related to any of the tax-exempt purposes listed in Code section 170(c).

Q-15. How do the like kind exchange provisions of Code section 1031 apply to bobble Supremes?

A-15. The exchange of a bobble Supreme held for productive use in a trade or business or for investment for like kind property which is to be held either for productive use in a trade or business or for investment is subject to the provisions of Code section 1031.

(a) Examples of exchanges of bobble Supremes of a "like kind." Code section 1031 applies to the exchange of (1) a Justice Stevens bobblehead held for productive use in a trade or business or for investment for another Justice Stevens bobblehead which is to be held either for productive use in a trade or business or for investment or (2) the exchange of a Justice O'Connor bobblehead held for productive use in a trade or business or for investment for another Justice O'Connor bobblehead which is to be held either for productive use in a trade or business or for investment.

(b) Examples of exchanges of bobble Supremes not of a "like kind." Code section 1031 does not apply to the exchange of a bobble Supreme for unimproved real estate. Similarly, section 1031 does not apply to the exchange of a bobble Supreme for an extension of a railroad franchise.

<sup>12</sup> Rulings will not be granted on the question of whether a specified individual (such as the party requesting the ruling), constitutes a charity for this purpose.

<sup>10</sup> The receipt of a bobble Supreme as a "premium" with a subscription may be analogized to receiving a "free" meal on an airline flight, *cf.* Treas. Reg. § 1.132-2(a)(5)(ii) (if such meals still exist), though the bobble Supreme is more tasteful.

<sup>11</sup> There is no escape, Hatch.

Approved: July 31, 2006.

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[GB] Doc. 06-411 Filed 7-31-06; 1:00 am]

**BILLING CODE 0000-00-NA**

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