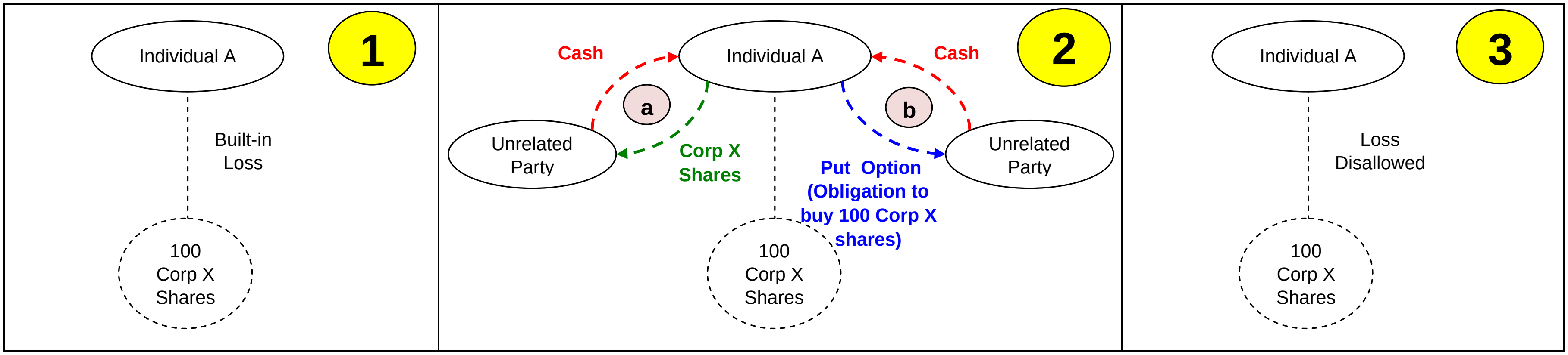
Revenue Ruling 85-87

"In-the-Money" Put Option Treated as Contract to Acquire Stock for Wash Sale Rule

Initial Structure | **Stock Sale & Put Option Sale** | **Ending Point (after re-purchase)**



On December 3, 1984, A, an individual, sold 100 shares of X corporation stock and realized a loss with respect to the shares. On December 4, 1984, A sold a put option obligating A to buy 100 shares of X corporation stock prior to February 1, 1985, at a particular price (the "exercise price") if the holder of the put option exercised the option. When the put was sold by A, the market price of the stock was substantially less than the exercise price of the put. In light of the spread at the time the put was sold between the value of the underlying stock and the exercise price of the put, the term of the put, the premium paid, the historic volatility in the value of the stock, and other objective factors, there was, at that time, no substantial likelihood that the put would not be exercised. Because the fair market value of the stock at the time the put was sold was less than the exercise price of the put, the put option sold by A is referred to as an "in-the-money" put.

Section 165(a) generally provides that a deduction is allowed for any loss sustained during the taxable year that is not compensated for by insurance or otherwise. Section 165(c) provides that in the case of an individual the deduction under section 165(a) is limited to losses incurred in a trade or business; losses incurred in any transaction entered into for profit, though not connected with a trade or business; and certain casualty losses. Section 1091(a) provides, in part, that in the case of any loss claimed to have been sustained from any sale of shares of stock where it appears that, within a period begining 30 days before the date of such sale and ending 30 days after such date, the taxpayer has acquired, or has entered into a contract or option so to acquire, substantially identical stock, then generally no deduction for the loss is allowed under section 165. The substance, rather than the form, of a transaction in which a taxpayer is involved governs the tax consequences of the transaction. In the instant case, at the time the put was sold there was no substantial likelihood that the put would not be exercised. Thus, for purposes of section 1091(a), the put sold by A is in substance a contract to acquire stock.