Arrowsmith Doctrine

- How is character determined of a transaction related to a prior year transaction?

Scope of Arrowsmith Doctrine

- Character based on earlier transaction
Application of Arrowsmith
- Initial gain – later loss
- Initial loss – later gain
- Initial gain – later gain
- Initial loss – later loss

Inapplicability of Arrowsmith
- Must be integral relationship between the transactions

Statutory Relief
- Section 1341 enacted to provide relief
  - Applies where the taxpayer’s deduction in a later year does not reduce its tax
Tax Benefit Rule

- Where an item deducted in one year is recovered, the recovery must be included in income except to the extent that no tax benefit resulted from the prior deduction.

Applications of the Tax Benefit Rule

- Judicial Applications
  - Previously expensed items
  - Charitable contributions returned
  - Casualty losses
  - Reimbursed losses
  - Unpaid accrued expenses

- Legislative application
  - Code Section 111
Exceptions to the Tax Benefit Rule

- Erroneous Deductions
- Absence of Deduction