# GEORGE V. DELSON ASSOCIATES
# OFFICE MEMORANDUM

**TO:** Harry Beller

**DATE:** October 26, 2010

**FROM:** GVD

**PRIORITY STATUS:** Routine

**COPIES TO:** JEE

**SUBJECT:** **FTC/JEE Bear Stearns Stock Transaction**

This memorandum is intended to summarize the facts and accounting treatment of the above.

## A. The Relevant Facts:

1. On or about July 14, 2005, FTC purchased 100,000 shares of Bear Stearns ("BS") stock at a cost of $10,626,000 (106.26 per share).

2. On or about October 25, 2005, FTC, pursuant to instructions from JEE, transferred the 100,000 shares of BS stock to GM.

3. The transfer to GM has been recorded by FTC on its books as "Stock Loan Receivable" from JEE in the amount of $10,626,000.

4. The transfer to GM has been treated by JEE and GM as a gift from JEE to GM on October 25, 2005.

5. On or about March 14, 2008, GM sold the shares gifted to her for a price of $3,199,974.

6. Dividends from BS received by GM were as follows:

| | | |
|---|---|---|
| 2006 | -- | $112,000 |
| 2007 | -- | 128,000 |
| 2008 | -- | 32,000 |
| Total | | $272,000 |

7. On or about May 31, 2008, BS was merged into JP Morgan Chase ("JPM") with JPM the survivor; each BS shareholder receiving in exchange for one share of BS stock, .21753 shares of JPM stock. Thus, JEE could no longer return the BS stock; he could only return the equivalent number of JPM shares.

8. Dividends received by GM on JPM stock were a total of $108,765.

9. On or about September 22, 2010, JEE purchased 21,753 shares of JPM stock and had same "delivered to FTC thereby returning the BS loan equivalent in JPM stock.

10. On or about September 22, 2010, JEE paid $380,765 to FTC the amount equal to the dividends paid by BS and JPM during the stock loan period. (See items A.6 and A.8).

## B. Substantive Position

The facts related above come down to, in substance the following:

1. FTC had a position in BS stock;
2. JEE wanted to make a gift to GM;

3. He borrowed the BS stock from FTC;

4. He completed the gift by borrowing the BS stock from FTC and having same it delivered to GM;

5. He could not return BS stock to FTC because of the merger;

6. He returned the equivalent by purchasing JPM stock and delivering same to FTC;

## C. Required Accounting Entries

Since JEE has returned the stock he borrowed by delivering JPM stock (the equivalent of the BS stock), **he no longer has an obligation to FTC**. The basis to FTC of the JPM stock will be the basis of the BS stock on the books of FTC. (See item A.1., supra) **FTC has no gain or loss until it disposes of the JPM stock**.

Since FTC was "repaid" the original BS stock loan with equivalent JPM stock, there are no further accounting entries to be made unless and until it disposes of the JPM stock. At that time it will realize a gain or loss by reference to the original BS basis -- $10,626,000.

As to JEE, there should have been recorded on his books, the borrowing of the BS stock on July 14, 2005, as a stock loan payable and the ultimate satisfaction thereof, by return of JPM stock, consistent with FTC entries.

## D. Discussion

Since this loan was satisfied by property having a cost less than the borrowed stock, it may be suggested that there is a gain to JEE equal to the difference between the market value of the BS stock borrowed and the cost to return it. However, there is no "taxable" transaction to which this can be related. Even if, as a matter of "economics", JEE's financial position has "improved", then it is not the result of a tax "recognized" transaction. Any increase in net worth to be recognized to JEE is attributable to the gift transaction which is not an income tax transaction. It should be recorded as an increase in his personal equity and not the result of a taxable gain.

Had he used the borrowed stock to "close" a "short sale", then he would have realized a gain. But he did not do so – he used it to make a gift. **NO GAIN OR LOSS IS RECOGNIZED FROM MAKING A GIFT!**

Any balance remaining in the stock loan account on JEE's books should be **transferred to equity**.