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**Internal Revenue Code Section 735(b)**

Character of gain or loss on disposition of distributed property

(a) Sale or exchange of certain distributed property.

(1) Unrealized receivables.

Gain or loss on the disposition by a distributee partner of unrealized receivables (as defined in section 751(c) ) distributed by a partnership, shall be considered as ordinary income or as ordinary loss, as the case may be.

(2) Inventory items.

Gain or loss on the sale or exchange by a distributee partner of inventory items (as defined in section 751(d)) distributed by a partnership shall, if sold or exchanged within 5 years from the date of the distribution, be considered as ordinary income or as ordinary loss, as the case may be.

(b) Holding period for distributed property.

In determining the period for which a partner has held property received in a distribution from a partnership (other than for purposes of subsection (a)(2) ), there shall be included the holding period of the partnership, as determined under section 1223, with respect to such property.

(c) Special rules.

(1) Waiver of holding periods contained in section 1231 .

For purposes of this section, section 751(d) (defining inventory item) shall be applied without regard to any holding period in section 1231(b).

(2) Substituted basis property.

(A) In general. If any property described in subsection (a) is disposed of in a nonrecognition transaction, the tax treatment which applies to such property under such subsection shall also apply to any substituted basis property resulting from such transaction. A similar rule shall also apply in the case of a series of nonrecognition transactions.

(B) Exception for stock in C corporation. Subparagraph (A) shall not apply to any stock in a C corporation received in an exchange described in section 351.