1950 Tax Ct. Memo LEXIS 180

The holding period of stock, for capital gains tax purposes, ends on the date of sale, regardless of contingent payment terms or later modifications to the sale agreement.

Summary

Campagna sold stock less than six months after acquiring it, with payments contingent on future production. The Tax Court addressed whether the gain realized from these sales in 1945 qualified as a short-term capital gain, even though the sale occurred in 1942 and payments were contingent. The court held that the sale occurred in 1942 when the stock was transferred, establishing the end of the holding period. Because the stock was held for less than six months, the gain was properly classified as a short-term capital gain, irrespective of payment contingencies or later modifications to the sales contract.

Facts

The petitioner, Campagna, purchased shares of stock on June 1, 1942. On July 29, 1942, Campagna sold these shares under contracts that stipulated future payments contingent on the production and sale of certain products. The shares were delivered to the purchaser's agent around July 30, 1942, and receipts were issued. In 1944, the contracts were modified. Campagna, using a cash accounting basis, reported a short-term capital gain in 1944 when the payments received exceeded the cost basis. The Commissioner determined that an amount received in 1945 from the stock sale also constituted a short-term capital gain.

Procedural History

The Commissioner of Internal Revenue determined that Campagna realized a short-term capital gain in 1945 from the sale of stock. Campagna petitioned the Tax Court, contesting this determination.

Issue(s)

Whether the Tax Court erred in determining that the amount received in 1945 from stock purchased on June 1, 1942, and sold on July 29, 1942, was a short-term capital gain, despite contingent payment terms and later modifications to the sale agreement.

Holding

Yes, because the holding period ended on the date of sale (July 29, 1942), which was less than six months from the date of acquisition (June 1, 1942), and the contingent payment terms and later modifications did not affect the length of time the stock was held.

Court's Reasoning

The court reasoned that the transaction in 1942 was a sale, not an exchange for property with an indeterminate fair market value. The contracts, receipts, and the petitioner's initial tax return all indicated a sale. The court emphasized that the holding period terminated on the day of the sale, July 29, 1942. Since the shares were held for less than six months, the gain was a short-term capital gain under Section 117 of the Internal Revenue Code. The court stated, "The provisions of the contracts of sale for future payments contingent on the production and sale of certain products, and the modifications in 1944, have no bearing on the length of time petitioner held the shares in question." The court also noted that as a cash basis taxpayer, Campagna properly reported no gain in 1942 because the cost basis had not yet been recovered. Only when payments exceeded the cost basis in subsequent years was the gain reportable.

Practical Implications

This case clarifies that the date of sale, when ownership and control of stock transfer, is the determining factor for calculating the holding period for capital gains purposes. Contingent payment terms or later modifications to the sale agreement do not alter the holding period. For tax planning, sellers should be aware that even if they receive payments over an extended period, the character of the gain (short-term or long-term) is determined by the time elapsed between the purchase and sale dates. This case reinforces the importance of accurately documenting the dates of acquisition and sale. It has been cited in subsequent cases regarding the timing of sales for tax purposes, particularly where complex sales agreements are involved. The ruling highlights that a cash basis taxpayer only recognizes gain when payments actually exceed their basis.