24 T.C. 809 (1955)

To qualify as a tax-free corporate reorganization under section 112 of the Internal Revenue Code, the acquisition of stock must be made “solely for stock,” meaning no other consideration, like cash, can be included in the exchange.

Summary

The case concerns a tax dispute over a corporate reorganization. Truax-Traer acquired Binkley and Pyramid by issuing its stock and paying cash to Binkley and Pyramid shareholders. The IRS determined the transaction was taxable because it involved cash in addition to stock. The Tax Court sided with the IRS, holding that the “solely for stock” requirement of Section 112(g)(1)(B) of the Internal Revenue Code meant that to qualify for non-taxable treatment, the acquiring corporation must provide only its stock as consideration. The court rejected the argument that 80% of the target corporation’s stock exchanged for stock satisfies the requirement if more than 80% of the stock exchanged for stock. The court focused on the “solely” requirement, emphasizing that even a small amount of consideration other than stock disqualifies the reorganization for non-taxable status.

Facts

Hubert and Helen Howard were stockholders of Binkley and Pyramid companies. Truax-Traer sought to acquire Binkley and Pyramid. As part of the acquisition, Truax-Traer acquired all the stock of Binkley for its stock and cash. The issue was whether this constituted a nontaxable exchange under Section 112(b)(3) of the Internal Revenue Code, which requires the exchange to be “solely for stock.” The IRS asserted the transaction was taxable since it included cash as part of the exchange.

Procedural History

The Commissioner determined that the exchange was taxable under section 112(a) of the Internal Revenue Code. The petitioners contested this determination. The case was heard before the Tax Court.

Issue(s)

1. Whether the transaction should be treated as a nontaxable exchange of some Binkley shares for stock of Truax-Traer and a separate sale of other Binkley shares for cash.

2. Whether the acquisition of stock by Truax-Traer for its stock and cash was an acquisition “solely” for stock, meeting the requirements for a tax-free reorganization under Section 112 of the Internal Revenue Code.

Holding

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1. No, because the court found the entire transaction was a single, unified event.

2. No, because the court held that the consideration for the stock acquired by the acquiring corporation must be solely the acquirer's voting stock, and the inclusion of cash as consideration violated this requirement, and therefore, the exchange did not qualify for tax-free treatment.

Court's Reasoning

The court relied on the statutory interpretation of Section 112 of the Internal Revenue Code, specifically, the requirement that the exchange be "solely for stock." The court analyzed the overall transaction, determining that it was a unified agreement where Truax-Traer acquired Binkley and Pyramid using both stock and cash. The court rejected the argument that only 80% of stock acquisition needed to be solely for stock, and that the remaining portion could involve cash. The court cited *Helvering v. Southwest Corp.*, which stated that the exchange must be "solely" for stock and that "Solely" leaves no leeway. The court also cited *Central Kansas T. Co. v. Commissioner* which supported their decision that the exchange should not qualify as a tax-free reorganization because cash was included in the exchange.

Practical Implications

This case provides a strict interpretation of the "solely for stock" requirement in corporate reorganizations. It emphasizes that any consideration other than voting stock, even if it's a small percentage of the transaction, can disqualify the exchange for tax-free treatment under Section 112(g)(1)(B). Tax advisors must carefully structure corporate reorganizations to comply with this strict requirement, and carefully consider all consideration involved in a corporate reorganization transaction. This case should inform how similar cases are analyzed. It highlights the need to ensure that the consideration is exclusively voting stock to ensure that it is not a taxable event. Future cases dealing with corporate reorganizations and the interpretation of the "solely for stock" requirement will likely cite this case.

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