Kimbell-Diamond Milling Co. v. Commissioner, 14 T.C. 74 (1950)

When a corporation purchases the stock of another corporation with the intent to acquire its assets and subsequently liquidates the acquired corporation, the transaction is treated as a direct purchase of the assets for tax purposes, disregarding the intermediate step of stock acquisition.

Summary

In *Kimbell-Diamond Milling Co.*, the taxpayer acquired the stock of another company to obtain its assets and then liquidated the acquired company. The Commissioner argued the transaction should be treated as a stock purchase, with a carryover basis for the assets under Internal Revenue Code § 112(b)(6) and § 113(a)(15). The Tax Court, however, applied the 'step transaction' doctrine, viewing the entire process as a single transaction: a direct purchase of the assets. This allowed the taxpayer to use the purchase price, including liabilities assumed, as the asset's basis for depreciation purposes, rather than the lower basis that the acquired company had.

Facts

Kimbell-Diamond Milling Company sought to acquire the assets of the Diamond Milling Company. The stockholders of Diamond Milling Company were unwilling to sell the assets directly. Kimbell-Diamond, therefore, purchased Diamond Milling's stock and immediately liquidated Diamond Milling. Kimbell-Diamond then sought to use the price paid for the Diamond Milling stock plus the assumed liabilities as the basis for depreciating the acquired assets.

Procedural History

The Commissioner of Internal Revenue determined that the transaction should be treated as a stock acquisition followed by liquidation, triggering the application of Internal Revenue Code § 112(b)(6) and § 113(a)(15), and that the basis of the assets was the same as in the hands of the Diamond Milling. The Tax Court disagreed. The Tax Court ruled that the series of steps was effectively a purchase of assets, not a stock acquisition. This decision was affirmed per curiam by the Court of Appeals for the Fifth Circuit.

Issue(s)

1. Whether the acquisition of the stock of Diamond Milling Company, followed by the immediate liquidation of that company, should be treated as a purchase of the company's stock or a purchase of its assets.

2. Whether, if the transaction is considered an asset purchase, the liabilities assumed by Kimbell-Diamond are included in the basis of the assets for depreciation purposes.

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Holding

1. Yes, because the court applied the step transaction doctrine. The court held that the substance of the transaction was a purchase of assets, not stock.

2. Yes, because the liabilities assumed by Kimbell-Diamond upon liquidation are included as part of the cost basis of the assets.

Court’s Reasoning

The court focused on the intent and the substance of the transaction, applying the

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