***Bausch & Lomb Optical Co. v. Commissioner*, 26 T.C. 646 (1956)**

When a parent corporation liquidates a wholly-owned subsidiary, the tax basis of the subsidiary's assets in the parent's hands is determined by whether the transaction is a true liquidation (carryover basis) or an asset purchase (stepped-up basis), based on the intent and purpose of the transaction.

Summary

The case concerns the determination of the tax basis for assets acquired by Bausch & Lomb (the parent company) from a merged subsidiary (New York company). The court addressed whether the transaction should be treated as a tax-free liquidation under I.R.C. § 112(b)(6), which would carry over the subsidiary's asset basis, or as an asset purchase, resulting in a stepped-up basis. The court held that the transaction qualified as a liquidation, because the acquiring corporation had no primary purpose or sole motive to acquire particular assets of the subsidiary. The court distinguished prior cases where the acquisition was deemed an asset purchase. This decision hinged on the business purpose of the transaction and the intent of the parties involved.

Facts

Bausch & Lomb, wholly owned the New York company. To facilitate a loan, Bausch & Lomb acquired all of the New York company's stock and then merged the subsidiary. The stock was cancelled, and the New York company's assets became assets of the petitioner. The IRS determined that the assets had a new basis measured by the amount paid by the petitioner for the stock. The petitioner contended that the basis was the same as that in the hands of the New York company.

Procedural History

The case was heard in the United States Tax Court. The taxpayer brought this action to contest the IRS's determination regarding the tax basis of the assets acquired from the liquidated subsidiary.

Issue(s)

1. Whether the acquisition of the New York company's assets by Bausch & Lomb constituted a liquidation under I.R.C. § 112(b)(6).

2. If the transaction was a liquidation, what was the tax basis of the acquired assets?

Holding

1. Yes, the acquisition of the New York company's assets qualified as a complete liquidation under I.R.C. § 112(b)(6) because the form of the transaction satisfied the

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statutory requirements.

2. The tax basis of the assets should be the same as it was in the hands of the New York company (carryover basis) under I.R.C. § 113(a)(15).

Court's Reasoning

The court stated, "it was the desire of the individuals who were then in active conduct of the business of the New York company to continue that business in corporate form." The court found that the primary purpose of the transaction was to continue the business, not to acquire specific assets. The court distinguished cases where the primary motive was asset acquisition. The court emphasized that since neither the acquiring corporation nor the individuals intended to acquire assets but the purpose was to acquire stock, the liquidation provisions applied.

The court addressed whether the prior case operated as an estoppel. The court said "the issue in this proceeding was not a matter which was 'actually presented and determined in the first case' and, therefore, the prior case does not estop the trial and consideration of the basis issue that is presented in these proceedings."

The court considered cases cited by the respondent and the court stated: "the principle enunciated therein was intended to be and should be limited to the peculiar situations disclosed by the facts in each of those cases and should not be extended to a case such as this, where the evidence establishes a wholly different origin and reason for the pattern of the transactions."

Practical Implications

This case clarifies the distinction between a tax-free liquidation and a taxable asset purchase in corporate reorganizations. It highlights the significance of the intent of the parties and the business purpose of the transaction. Legal practitioners must carefully analyze the facts and circumstances of each transaction to determine its tax consequences. Specifically, when a parent company acquires a subsidiary, the transaction's form alone does not dictate the tax outcome. Courts will examine the purpose of the transaction to ascertain whether the assets should receive a carryover or a stepped-up basis. This case emphasizes the importance of documenting the intent behind corporate transactions to support the desired tax treatment. Future cases involving similar fact patterns will hinge on the primary purpose of the acquiring corporation and whether the transaction was to acquire stock and continue the business, or if the primary purpose was asset acquisition.

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