Cabax Mills v. Commissioner, 59 T. C. 401 (1972)

A parent corporation can tack its holding period of a subsidiary's stock to the holding period of assets received upon the subsidiary's liquidation if the stock was purchased under specific conditions.

Summary

Cabax Mills purchased 98% of Snellstrom's stock in April 1964, liquidated it in April 1965, and received timber-cutting contracts. The IRS challenged Cabax's election to treat timber-cutting profits as long-term capital gains under section 631(a), arguing the holding period began at liquidation. The Tax Court held for Cabax, ruling that under section 334(b)(2), the holding period of the contracts began when Cabax acquired Snellstrom's stock, allowing it to tack this period onto the contracts' holding period for section 631(a) eligibility. This decision clarifies how holding periods can be tacked in corporate liquidations under specific conditions.

Facts

In April 1964, Cabax Mills acquired 98% of Snellstrom Lumber Co. 's stock, primarily to gain ownership of its plywood plant and timber-cutting rights. Despite initial attempts to purchase these assets directly, Cabax had to buy the stock due to the unwillingness of Snellstrom's owners to sell the assets separately. In April 1965, Snellstrom was liquidated, and Cabax received, among other assets, timber-cutting contracts that Snellstrom had owned for over six months prior to January 1, 1965. Cabax cut timber under these contracts from May to December 1965, electing to report the profits as long-term capital gains under section 631(a) of the Internal Revenue Code.

Procedural History

The IRS determined a deficiency in Cabax's corporate income tax for 1965, arguing that Cabax did not meet the six-month holding period requirement for the timber-cutting contracts under section 631(a). Cabax petitioned the Tax Court, which ruled in its favor, allowing it to tack its holding period of Snellstrom's stock onto the holding period of the timber-cutting contracts received in liquidation.

Issue(s)

1. Whether Cabax Mills can tack its holding period of Snellstrom's stock onto the holding period of the timber-cutting contracts received upon Snellstrom's liquidation under section 1223(1) of the Internal Revenue Code.

Holding

1. Yes, because under section 334(b)(2), Cabax's basis in the timber-cutting contracts was the same as its basis in Snellstrom's stock, and section 1223(1) allows

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for tacking of holding periods when the basis of the exchanged property is the same as the property received.

Court’s Reasoning

The Tax Court reasoned that Cabax’s purchase of Snellstrom’s stock and the subsequent liquidation met the conditions of section 334(b)(2), which requires a substituted basis for the assets received in liquidation equal to the parent corporation’s basis in the subsidiary’s stock. The court interpreted this to mean that the holding period of the timber-cutting contracts began when Cabax purchased the stock, allowing it to tack this period onto the contracts’ holding period under section 1223(1). The court rejected the IRS’s argument that the transaction should be treated as one continuous event from stock purchase to liquidation, asserting that the liquidation still constituted an exchange under sections 331(a) and 332. The court also noted that this interpretation was consistent with the purpose of section 334(b)(2), which codified the judicial principle established in Kimbell-Diamond Milling Co. cases, and did not preclude tacking under section 1223(1).

Practical Implications

This decision impacts how corporations can structure acquisitions and liquidations to achieve favorable tax treatment. It clarifies that under specific conditions, a parent corporation can tack the holding period of a subsidiary’s stock to the holding period of assets received in liquidation, potentially allowing for long-term capital gains treatment on those assets. This ruling influences how similar cases should be analyzed, particularly in determining the holding period for assets acquired through stock purchases and subsequent liquidations. It also affects legal practice in corporate tax planning, as attorneys must now consider the potential for tacking holding periods in structuring such transactions. The decision has implications for businesses seeking to optimize tax outcomes through corporate reorganizations and may influence future cases involving similar tax code provisions.

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