Reeves v. Commissioner, 71 T. C. 727 (1979)

Prior cash purchases of stock by an acquiring corporation are irrelevant to the qualification of a subsequent stock-for-stock exchange as a tax-free reorganization under Section 368(a)(1)(B).

Summary

In Reeves v. Commissioner, the U. S. Tax Court ruled that International Telephone & Telegraph Corp. ‘s (ITT) acquisition of Hartford Fire Insurance Co. stock solely in exchange for ITT voting stock qualified as a tax-free reorganization under Section 368(a)(1)(B), despite ITT’s earlier cash purchases of Hartford stock. The court held that the prior cash acquisitions were irrelevant to the reorganization’s validity, as the 1970 stock-for-stock exchange alone met the statutory requirements. This decision clarifies that for a reorganization, the focus is on the transaction that meets the 80% control threshold, not on earlier acquisitions for different consideration.

Facts

ITT initially approached Hartford for a merger in 1968, which Hartford rejected. Subsequently, ITT purchased approximately 8% of Hartford’s stock for cash between November 1968 and March 1969. In 1970, ITT acquired over 80% of Hartford’s stock solely in exchange for ITT voting stock through a tender offer. More than 95% of Hartford’s shareholders, including the petitioners, tendered their shares in this exchange. The Internal Revenue Service had initially approved the transaction but later revoked its ruling due to misstatements in the ruling request.

Procedural History

The petitioners filed for summary judgment in the U. S. Tax Court, challenging the IRS’s determination that the exchange was taxable due to ITT’s prior cash purchases. The Tax Court granted summary judgment in favor of the petitioners, ruling that the 1970 exchange qualified as a reorganization under Section 368(a)(1)(B).

Issue(s)

1. Whether prior cash purchases of stock by the acquiring corporation disqualify a subsequent stock-for-stock exchange from being a tax-free reorganization under Section 368(a)(1)(B)?

Holding

1. No, because the 1970 exchange, standing alone, met the statutory requirements of a (B) reorganization, as it involved an acquisition of over 80% of the target corporation’s stock solely for voting stock.

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Court’s Reasoning

The court reasoned that the 1970 exchange satisfied the “solely for voting stock” requirement of Section 368(a)(1)(B) because it involved a single transaction where more than 80% of Hartford’s stock was exchanged for ITT voting stock. The court distinguished this case from prior cases by emphasizing that the 80% control was achieved in one transaction without any non-stock consideration. The court also noted that the legislative history and judicial precedents did not compel a different result. The court declined to address whether the prior cash purchases were part of the reorganization plan, deeming them irrelevant to the issue at hand. The decision included a concurring opinion and dissenting opinions, reflecting differing views on the interpretation of prior judicial decisions and the impact of the cash purchases.

Practical Implications

This decision clarifies that for a transaction to qualify as a (B) reorganization, the focus is on whether a single transaction meets the 80% control threshold with voting stock, regardless of prior cash acquisitions. Practitioners should ensure that the transaction achieving the 80% control is structured to meet the “solely for voting stock” requirement. The decision may influence how future reorganizations are structured, particularly in cases involving multiple acquisitions over time. It also highlights the importance of distinguishing between transactions for tax purposes, which could affect planning for acquisitions and reorganizations. Subsequent cases like *McDowell v. Commissioner* have cited Reeves in upholding similar reorganizations, emphasizing the need for clear separation between different types of acquisitions.

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