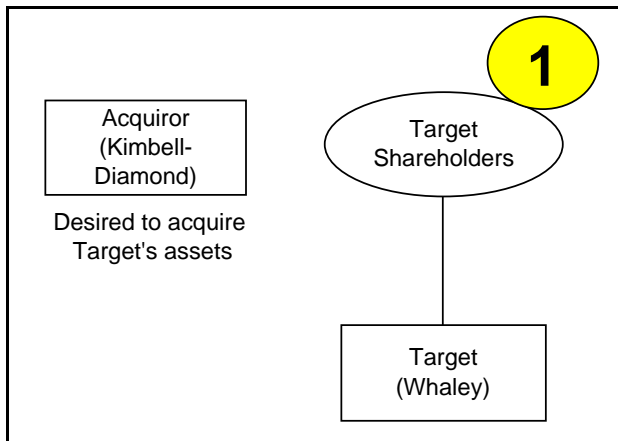


Kimbell-Diamond Milling Co. v. Commissioner
14 T.C. 74 (1950), 187 F.2d 718 (5th Cir. 1951)

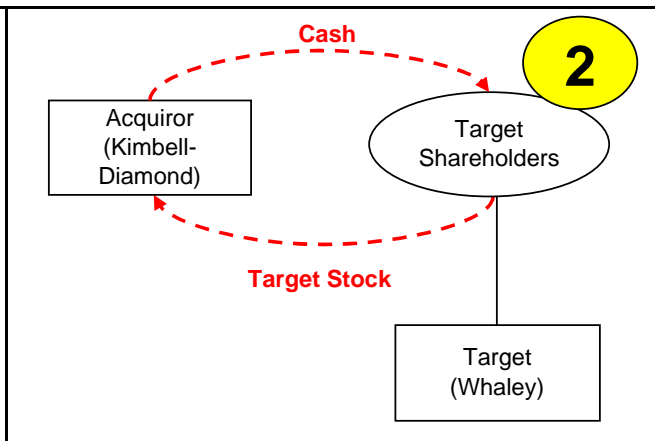
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**Stock Purchase & Target Liquidation
 Treated As Asset Acquisition**

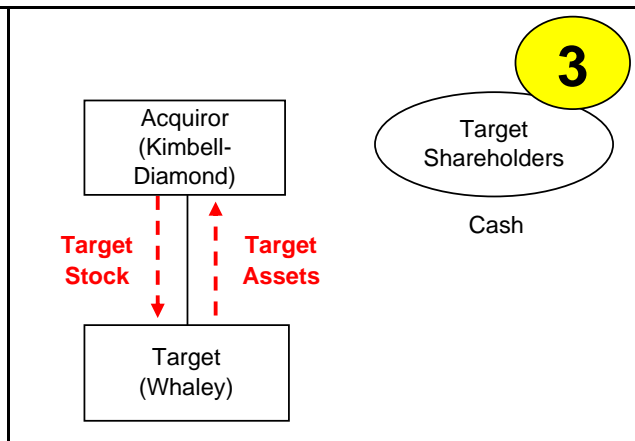
Initial Structure



Target Stock Acquisition



Target Liquidation



Kimbell-Diamond ("KD") had owned a mill which was destroyed by fire. If KD did not reinvest the insurance proceeds in similar replacement property, it would have been subject to gain recognition as a result of this involuntary conversion (predecessor to section 1033). KD acquired Target's mill and did not recognize gain, implying that it was taking advantage of the replacement property provisions. However, KD did not directly acquire the assets of Target. Rather, KD acquired the stock of Target and then liquidated Target.

Special basis rules apply to replacement property in involuntary conversions. However, KD argued that it should have a carryover basis for the assets from Target because KD acquired Target assets in a tax free liquidation. KD was trying to "have its cake and eat it too". KD wanted no gain recognition under section 1033 and it wanted the tax free liquidation carryover basis rules to apply.

The Fifth Circuit affirmed the Tax Court holding that KD was treated as directly acquiring the assets of Target and that KD had a cost basis in those assets (as modified by section 1033). Old section 334(b)(2) was added in 1954 to codify the principles of Kimbell-Diamond. In 1982 Congress repealed old section 334(b)(2) and enacted section 338. Section 338 was intended to replace the Kimbell-Diamond doctrine.

Ending Point

