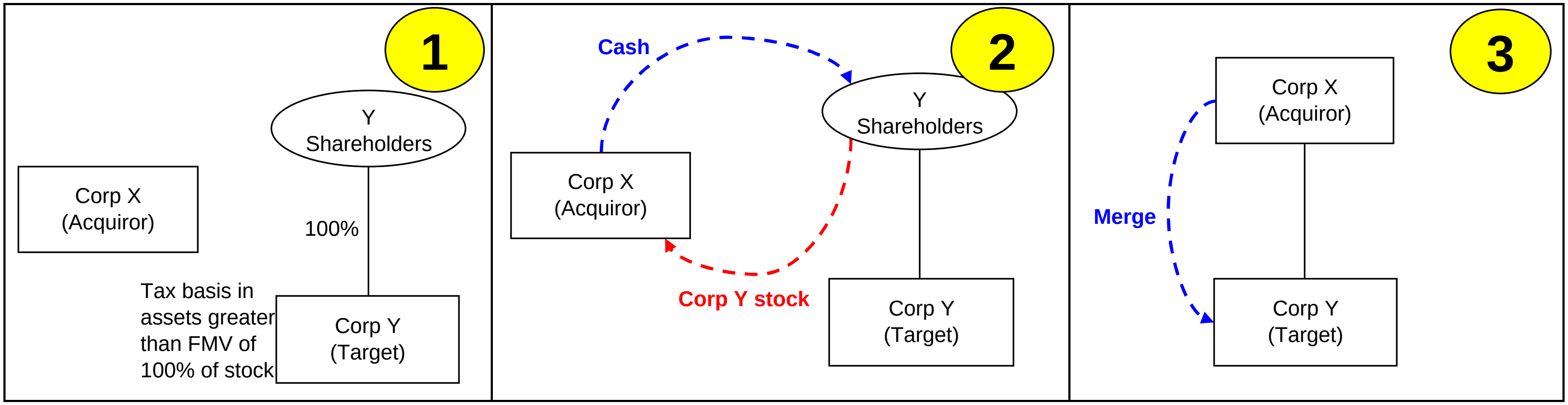
Revenue Ruling 70-223

Taxable Stock Acquisition & Downstream Merger

Initial Structure | **Stock Acquisition** | **Downstream Merger (within 2 years)**

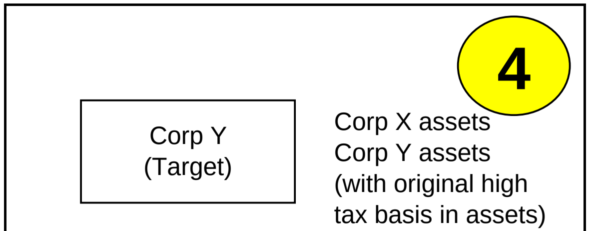


Corporation X purchased all of the outstanding stock of corporation Y within a 12-month period. Within two years of the last stock purchase X was merged into Y. Y's assets had an adjusted basis to Y greater than the cost of the Y stock to X.

There are good business reasons for combining the businesses of X and Y. In this case it was decided to merge X into Y rather than liquidate Y in order to obtain the more favorable tax treatment afforded by the reorganization provisions of the Code.

Section 368(a)(1)(A) defines a statutory merger or consolidation as a reorganization. Section 362 provides that the basis of property acquired by a corporation in connection with a reorganization, will be the same as the basis in the hands of the transferor. Since X may accomplish its desired objective of combining the two businesses by either liquidating Y or by merging into Y, it may choose whichever form it desires for the transaction.

Ending Point



Old section 334(b)(2) was created in 1954 to codify the princples of Kimbell-Diamond. Under section 334(b)(2), Corp X would have obtained a step-up (or step-down) in basis if Corp Y were liquidated into Corp X within 2 years of acquisition. In Corp X's case, there would have been a step-down in basis. To avoid this step-down, Corp X merged into Corp Y, rather than liquidating Corp Y. In 1982 Congress repealed old section 334(b)(2) and enacted section 338.