

§ 1.1233-2

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on the date of the short sale, as part of an arbitrage operation, to purchase property by virtue of which he has the right to receive or acquire substantially identical property to that sold short, he will be deemed, for purposes of section 1233(f) (1) and (2), to hold such substantially identical property at the close of business on the date of the short sale. For purposes of this subparagraph, it is immaterial whether, on the basis of all the facts and circumstances, the preferred stock of X is substantially identical to the common stock of X. The short sale on November 1 does not affect the holding period of the 100 shares of X Corporation common stock purchased on August 13, 1957. Because of the operation of rule (2) of paragraph (c)(2) of this section, the holding period of the preferred stock acquired as the result of A's contract to purchase it as part of an arbitrage operation (or the common stock which A acquires by conversion of such preferred stock into common stock) will not begin until the short sale entered into in the arbitrage operation is closed.

(3) *Definition of arbitrage operations.* For the purpose of section 1233(f), arbitrage operations are transactions involving the purchase and sale of property entered into for the purpose of profiting from a current difference between the price of the property purchased and the price of the property sold. Assets acquired for arbitrage operations include only stocks and securities and rights to acquire stocks and securities. The property purchased may be either identical to the property sold or, if not so identical, such that its acquisition will entitle the taxpayer to acquire property which is so identical. Thus, the purchase of bonds or preferred stock convertible, at the holder's option, into common stock and the short sale of the common stock which may be acquired therefor, or the purchase of stock rights and the short sale of the stock to be acquired on the exercise of such rights, may qualify as arbitrage operations. A transaction will qualify as an arbitrage operation under section 1233(f) only if the taxpayer properly identifies the transaction as an arbitrage operation on his records as soon as he is able to do so. Such identification must ordinarily be entered in the taxpayer's records on the day of the transaction. Property acquired in a transaction properly identified as part of an arbitrage operation is the only property which will be deemed acquired for an arbitrage operation.

The provisions of section 1233(f) and this paragraph shall continue to apply to property acquired in a transaction properly identified as an arbitrage operation although, because of subsequent events, e.g., a change in the value of bonds so acquired or of stock into which such bonds may be converted, the taxpayer sells such property outright rather than using it to complete the arbitrage operation.

(4) *Effective date of section 1233(f).* Section 1233(f), relating to arbitrage operations involving short sales of property, is effective only with respect to taxable years ending after August 12, 1955, and only with respect to short sales made after such date.

[T.D. 6500, 25 FR 12011, Nov. 26, 1960, as amended by T.D. 6494, 25 FR 9372, Sept. 30, 1960; T.D. 6926, 32 FR 11468, Aug. 9, 1967; T.D. 7728, 45 FR 72650, Nov. 3, 1980]

§ 1.1233-2 Hedging transactions.

The character of gain or loss on a short sale that is (or is identified as being) part of a hedging transaction is determined under the rules of § 1.1221-2.

[T.D. 8555, 59 FR 36367, July 18, 1994]

§ 1.1234-1 Options to buy or sell.

(a) *Sale or exchange—(1) Capital assets.* Gain or loss from the sale or exchange of an option (or privilege) to buy or sell property which is (or if acquired would be) a capital asset in the hands of the taxpayer holding the option is considered as gain or loss from the sale or exchange of a capital asset (unless, under the provisions of subparagraph (2) of this paragraph, the gain or loss is subject to the provisions of section 1231). The period for which the taxpayer has held the option determines whether the capital gain or loss is short-term or long-term.

(2) *Section 1231 transactions.* Gain or loss from the sale or exchange of an option to buy or sell property is considered a gain or loss subject to the provisions of section 1231 if, had the sale or exchange been of the property subject to the option, held by the taxpayer for the length of time he held the option, the sale or exchange would have been subject to the provisions of section 1231.