

New York State Department of Taxation and Finance
Taxpayer Services Division
Technical Services Bureau

TSB-A-88 (15) C
Corporation Tax
TSB-A-88 (8) I
Income Tax
July 12, 1988

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. Z880323B

On March 23, 1988, a Petition for Advisory Opinion was received from North Side Savings Bank, 185 West 231st Street, Bronx, New York 10463.

The issue raised is whether the liquidation of Richmond Hill Savings Bank (hereinafter "Target") into Petitioner will constitute a tax-free transaction for purposes of Articles 22 and 32 of the Tax Law. To facilitate such transaction, Petitioner will incorporate North Side Interim Savings Bank (hereinafter "Sub") as a wholly-owned subsidiary.

Specifically, the questions are:

1. For purposes of Article 32, will "entire net income", as defined in section 1453 of the Tax Law, be recognized to Petitioner, Sub or Target as a result of the proposed transaction.
2. For purposes of Article 22, will income be taxed to the shareholders of Petitioner under section 611 and section 612 of the Tax Law, other than to those who perfect their dissenters' rights under section 6022 of the New York State Banking Law.
3. For purposes of any other provision of the Tax Law, will income be taxed to petitioner, Sub, Target or the shareholders of Petitioner.

Petitioner is a New York chartered stock savings bank. Effective April 15, 1986, Petitioner converted from a New York chartered mutual savings bank to a New York chartered stock savings bank in a transaction which qualified as a reorganization pursuant to section 368(a)(1)(F) of the Internal Revenue Code (hereinafter "IRC"). At that time, Petitioner established a liquidation account in an amount equal to the net worth of Petitioner prior to conversion for the benefit of its eligible account holders. The liquidation account has been maintained for those eligible account holders who have kept their savings accounts at Petitioner.

Petitioner is primarily engaged in attracting savings deposits from the general public and originating and investing in loans secured by first mortgage liens on residential dwellings and income-producing commercial real estate. As of December 31, 1987, Petitioner had outstanding 3,680,000 shares of common stock which is publicly held.

Sub will be incorporated under the laws of New York State. Sub will be created solely for the purpose of facilitating the consummation of the proposed acquisition of Target by Petitioner. The only activity to be conducted by Sub will be to enter into the Plan of Merger and to merge with and into Target. Except for activities related to the merger, Sub will not engage in any operations.

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Sub will have an authorized capital structure of up to 1000 shares of common stock, \$1.00 par value, all of which will, prior to the proposed transaction, be issued and outstanding and owned by Petitioner.

Target is a New York chartered stock savings bank. Effective July 21, 1986, Target converted from a New York chartered mutual savings bank to a New York chartered stock savings bank in a transaction which qualified as a reorganization pursuant to Section 368(a)(1)(F) of the IRC. At that time, Target established a liquidation account in an amount equal to the net worth of Target prior to conversion for the benefit of its eligible account holders. The liquidation account has been maintained for those eligible account holders who have kept their savings accounts at Target.

The business of Target consists primarily of attracting savings deposits from the general public and originating and investing in loans secured by first mortgage liens on residential dwellings and income-producing commercial real estate.

As of December 31, 1987, Target had outstanding 6,612,500 shares of common stock and stock options representing 228,000 shares of common stock which were granted pursuant to a 1986 stock option plan. Target's common stock is publicly traded.

In order to expand the geographical area in which the business activities of Petitioner are conducted and to otherwise complement Petitioner's business, the following plan is proposed:

- (1) Sub will be incorporated as a wholly-owned subsidiary of Petitioner solely in order to facilitate the acquisition by Petitioner of Target.
- (2) Petitioner was given on January 23, 1988, the right to acquire 726,500 shares of Target common stock pursuant to a stock option agreement to be entered into between the two parties.
- (3) Sub will be merged with and into Target pursuant to section 601 of the New York State Banking Law and 12 U.S.C. § 1828(c). Target will be the surviving corporation. Except with respect to stockholders who validly perfect their dissenters' rights under state law, each share of Target will be converted into the right to receive \$23.75 in cash from Petitioner. The holders of stock options representing 228,000 shares of stock will also receive cash in exchange for their stock options. Petitioner's right to acquire 726,500 shares of Target common stock will be canceled.
- (4) Subsequent to, but on the same day of, the merger of Sub into Target, Petitioner will adopt a plan of complete liquidation of Target. Target will be liquidated in a single liquidating distribution which will take the form of a merger of Target into Petitioner pursuant to section 601 of the New York State Banking Law. Target's assets will be transferred to, and its liabilities will be assumed by, Petitioner.

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For federal income tax purposes, the following has been held:

- (1) The formation of Sub and its merger with and into Target will be disregarded for federal income tax purposes, and the transaction will be treated as a purchase by Petitioner of the outstanding shares of Target (Rev. Rul. 73-427, 1973-2 C.B. 301). The purchase will be treated as a qualified stock purchase within the meaning of section 338(d)(3) of the IRC (section 338(h)(3)(A) of the IRC); see section 1.338-4T(d) (Question 3 and Answer 3.)
- (2) For federal income tax purposes, the merger of Target into Petitioner pursuant to applicable law will be treated as a distribution by Targeting complete liquidation within the meaning of section 332 of the IRC (section 1.332-2(d) of the Income Tax Regulations).
- (3) Provided that the requirements of section 332(b) of the IRC are met, no gain or loss will be recognized by Petitioner on its receipt of the assets of Target distributed in complete liquidation of Target (section 332(a) of the IRC).
- (4) No gain or loss will be recognized by Target on the distribution of its assets to Petitioner in complete liquidation (section 337(a) of the IRC).
- (5) The basis of the assets of Target in the hands of Petitioner will be the same as the basis of those assets in the hands of Target immediately preceding the respective liquidations (section 334(b)(1) of the IRC).
- (6) The holding period of the assets received by Petitioner in complete liquidation of Target will include the period during which such property was held by Target (section 1223(2) of the IRC).
- (7) The basis in the hands of Petitioner of the Target stock acquired in the proposed merger of Sub into Target will be equal to the amount of cash paid by Petitioner to the Target shareholders for their stock (section 1012 of the IRC; section 1.1012 of the Income Tax Regulations).
- (8) As provided in section 1001 of the IRC, gain or loss will be realized and recognized to each Target shareholder upon receipt of cash as a result of the merger of Sub into Target, measured by the difference between the amount of cash received and the Target shareholders adjusted basis (as determined under section 1011 of the IRC) in the stock surrendered. Provided section 341 of the IRC (relating to collapsible corporations) is not applicable and the stock of Target surrendered for cash qualifies as a capital asset in the shareholders' hands, the gain or loss will be capital gain or loss, subject to the provisions and limitations of Subchapter P of Chapter 1 of the IRC.

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- (9) As provided in section 381(c)(2) of the IRC and section 1.381(c)(2)-1 of the regulations, Petitioner will succeed to and take into account the earnings and profits, or deficit in earnings and profits, of Target as of the date of transfer. Any deficit in earnings and profits of Target will be used only to offset earnings and profits accumulated after the date of transfer.
- (10) Pursuant to section 381(a) of the IRC and section 1.381(a)-1 of the regulations, Petitioner will succeed to and take into account the items of Target described in section 381(c) of the IRC. These items will be taken into account by Petitioner subject to the provisions and limitations of sections 381, 382, and 383 of the IRC.
- (11) Since section 381 of the IRC is applicable to the transaction, the provisions of section 593(e) of the IRC will not apply to the distribution of the assets of Target to Petitioner.
- (12) Pursuant to sections 381(c)(16) and 591 of the IRC, in the event the effective date of the proposed transaction precedes the date interest is paid or credited to the savings accounts of depositors of Target, such interest paid or credited by Petitioner with respect to savings accounts of Target will be deductible by Petitioner when it is paid or credited, provided such amounts are withdrawable, subject only to customary notice of intent to withdraw, even though such interest is attributable to periods preceding the merger.
- (13) Except as otherwise provided by section 384 of the IRC, provided Target has a net unrealized built-in gain, any income of such corporation for any recognition period taxable year (to the extent attributable to recognized built-in gains) shall not be offset by any pre-acquisition loss of any other member of the affiliated group.

Question 1

Section 1451 of the Tax Law imposes, annually, a franchise tax on every banking corporation for the privilege of exercising its franchise or doing business in New York State in a corporate or organized capacity.

Section 1455(a) of the Tax Law provides that the basic tax is 9 percent of the taxpayer's entire net income, or portion thereof allocated to New York State, for the taxable year or part thereof.

Entire net income is defined in section 1453(a) of the Tax Law as "total net income from all sources which shall be the same as the entire taxable income (but not alternative minimum taxable income)..., which the taxpayer is required to report to the United States treasury department,.., subject to the modifications and adjustments hereinafter provided."

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Section 1453(b) through (k) of the Tax Law and sections 18-2.3, 18-2.4 and 18-2.5 of the Franchise Tax on Banking Corporations Regulations, promulgated thereunder, provide for the modifications and adjustments required by section 1453(a).

Herein, Sub's merger with and into Target is disregarded for federal income tax purposes and is treated as a qualified stock purchase by Petitioner of the outstanding shares of Target within section 338(d)(3) of the IRC. For purposes of section 1453 no modification or adjustment is required for such transaction. The transaction would be treated the same as it is treated for federal income tax purposes.

In addition, there is no modification or adjustment required when a transaction constitutes a tax-free liquidation for federal income tax purposes pursuant to section 332 of the IRC. Therefore, for purposes of section 1453 the tax-free liquidation of Target would be treated the same as it is treated for federal income tax purposes.

Question 2

Section 611(a) of the Tax Law provides: "[t]he New York taxable income of a resident individual shall be his New York adjusted gross income less his New York deduction and New York exemptions, as determined under this part."

Section 612(a) of the Tax Law provides: "[t]he New York adjusted gross income of a resident individual means his federal adjusted gross income as defined in the laws of the United States for the taxable year, with the modifications specified in this section."

Pursuant to section 612, no modification is required when a transaction is treated for federal income tax purposes as a qualified stock purchase by a corporation within section 338(d)(3) of the IRC. Therefore, such transaction would have the same affect on shareholders of the corporations for New York personal income purposes as it has for federal income tax purposes.

In addition, section 612 of the Tax Law does not contain any modification that affects the shareholders of corporations where a transaction constitutes a tax-free liquidation for federal income tax purposes pursuant to section 332 of the IRC.

Accordingly, for personal income tax purposes under Article 22, resident shareholders of Petitioner are not required to make any modifications pursuant to section 612 of the Tax Law as a result of the transaction described herein. Any capital gains or losses recognized for federal income tax purposes will be treated the same for New York personal income tax purposes.

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Question 3

There is no other provision of the Tax Law where income would be taxed to Petitioner, Sub, Target or the shareholders of Petitioner as a result of the tax-free transaction as described herein.

DATED: July 12, 1988

s/FRANK J. PUCCIA
Director
Technical Services Bureau

NOTE: The opinions expressed in Advisory Opinions
are limited to the facts set forth therein.