

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

TSB-A-88 (14) C  
Corporation Tax  
TSB-A-88 (7) I  
Income Tax  
June 15, 1988

STATE OF NEW YORK  
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. Z880323A

On March 23, 1988, a Petition for Advisory Opinion was received from Binghamton Savings Bank, 58-68 Exchange Street, Binghamton, New York 13902.

The issue raised is whether the merger of Binghamton Interim Savings Bank (hereinafter "Sub"), a subsidiary of BSB Bancorp, Inc. (hereinafter "Parent"), into Petitioner will constitute a tax-free reorganization for purposes of Articles 22 and 32 of the Tax Law.

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 Parent, Sub or Petitioner as a result of the reorganization.
2. For purposes of Article 22, will income be taxed to the shareholders of Parent or 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 Parent, Sub, Petitioner or the shareholders of Parent or Petitioner.

Petitioner is a New York State stock savings bank. On September 26, 1985, Petitioner converted from a New York State mutual savings bank to a New York State stock savings bank in a transaction intended to qualify as a reorganization within the meaning of section 368(a)(1)(F) of the Internal Revenue Code (hereinafter "IRC"). At that time, Petitioner established a liquidation account for the benefit of its eligible account holders in recognition of their proprietary interests in an amount equal to the net worth of Petitioner prior to the conversion. Petitioner has outstanding 3,123,182 shares of common stock. The present directors and officers of Petitioner beneficially own approximately 7.63 percent of the outstanding Petitioner stock.

Parent is a Delaware corporation recently organized by Petitioner to engage in business as a bank holding company under the Bank Holding Company Act of 1956, as amended. Parent will not engage in any business activity prior to consummation of the proposed transaction. Parent has authorized 5,000,000 shares of \$0.01 par value common stock and 2,500,000 shares of \$0.01 par value preferred stock.

Sub will be formed by Parent as a New York State stock savings bank solely to effect the proposed transaction. Sub will issue its common stock to Parent.

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The Board of Directors of Petitioner believes that a holding company structure will provide Petitioner with greater operational flexibility and opportunity for expansion and diversification. Accordingly, pursuant to an Agreement and Plan of Merger and Reorganization, the following transaction has been proposed:

- (1) Pursuant to applicable law, Sub will merge with and into Petitioner. The separate corporate existence of Sub will terminate upon the effective date of the merger, and Petitioner will acquire all of the assets of Sub.
- (2) Each share of Petitioner common stock outstanding on the effective date of the merger, except those held by dissenting shareholders, will be exchanged for one share of Parent common stock. Accordingly, no fractional shares of Parent common stock will be issued.
- (3) Petitioner shareholders who dissent to the transaction, if any, will receive cash from Petitioner for their shares under section 6022 of the New York State Banking Law.
- (4) On the effective date of the merger, each share of Parent stock held by Petitioner will be canceled and each share of Sub common stock outstanding will be automatically exchanged for one share of Petitioner common stock. As a result of the merger, Parent will own all of the issued and outstanding stock of Petitioner.

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

- (1) Provided that (a) the proposed merger of Sub with and into Petitioner qualifies as a statutory merger under applicable law, (b) after the transaction Petitioner will hold substantially all of its assets and substantially all of the assets of Sub, and (c) in the transaction, the shareholders of Petitioner exchange an amount of Petitioner common stock representing control of Petitioner within the meaning of section 368(c) of the IRC solely for Parent common stock, but prior recipients of Petitioner liquidation account interests (i.e. pre-conversion Petitioner deposit account holders) will retain such interests, the transaction will qualify as a reorganization within the meaning of section 368(a)(1)(A) of the IRC. The reorganization will not be disqualified by reason of the fact that stock of Parent is used in the transaction (section 368(a)(2)(E) of the IRC and Rev. Rul. 77-428, 1977-2 C.B. 117). The Internal Revenue Service has determined that Petitioner's deposits with liquidation account interests do not constitute stock for purposes of section 368(c) of the IRC. A liquidation account interest is a mere component of the deposit and is not divisible from the deposit. While the Internal Revenue Service rules that a conversion may qualify for tax free reorganization treatment based on a finding that there is sufficient proprietary interest for continuity of interest purposes found in the liquidation

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account interest due to the unique nature of the financial structure and control of regulated mutual savings banks (Rev. Rul. 80-105, 1980-1 C.B. 78), the Internal Revenue Service believes that the entire deposit with liquidation rights in a stock bank is virtually cash equivalent in light of the United States Supreme Court decision in Paulsen v. Commissioner, 469 U.S. 131 (1985), 1985-1 C.B. 127. (But see Rev. Ruls. 69-3, 1969-1 C.B. 103, and 69-646, 1969-2 C.B. 54, the interest received rises to the level of "stock" and thus, section 354 of the IRC applies). The Court held that the debt characteristics of a mutual deposit represented by its withdrawal value are so predominant that the deposit is virtually a cash equivalent. It is the Internal Revenue Service's view that a stock bank deposit represents even less proprietary interest than a mutual deposit because depositors of a stock bank have no voting rights and their only proprietary right is a liquidation account that does not increase in value even if the net worth of the bank increases. [Cf. Helvering v. Southwest Consolidated Corp., 315 U.S. 194, 202 (1942) (a creditor's interest can constitute a proprietary interest in an insolvent corporation for continuity of interest purposes, yet not constitute stock for control purposes)].

- (2) For purposes of ruling (1), "substantially all" means at least 90 percent of the fair market value of the net assets and at least 70 percent of the fair market value of the gross assets of each of Petitioner and Sub. Parent, Sub, and Petitioner will each be "a party to a reorganization" within the meaning of section 368(b) of the IRC.
- (3) No gain or loss will be recognized to Sub on the transfer of its assets to Petitioner in exchange for Petitioner common stock (section 361(a) of the IRC).
- (4) No gain or loss will be recognized to Petitioner upon the receipt of the assets of Sub in exchange for Petitioner common stock (section 1032(a) of the IRC).
- (5) The basis of the assets of Sub acquired by Petitioner will be the same in the hands of Petitioner as the basis of such assets in the hands of Sub immediately prior to the exchange (section 362(b) of the IRC).
- (6) No gain or loss will be recognized to Parent upon the receipt of stock of Petitioner solely in exchange for stock of Sub (section 354(a) (1) of the IRC).
- (7) The holding period of the assets of Sub in the hands of Petitioner will, in each instance, include the holding period during which such assets were held by Sub (section 1223(2) of the IRC).
- (8) No gain or loss will be recognized to the shareholders of Petitioner upon the exchange of their Petitioner stock solely for Parent common stock (section 354(a) (1) of the IRC).

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- (9) The basis of the Parent common stock received by the shareholders of Petitioner will be the same as the basis of Petitioner stock surrendered in exchange therefor (section 358(a)(1) of the IRC).
- (10) The holding period of the Parent common stock received by the shareholders of Petitioner will include the period during which Petitioner stock surrendered therefor was held, provided the stock of Petitioner is a capital asset in the hands of the shareholders of Petitioner on the date of the exchange (section 1.223(1) of the IRC).
- (11) Where cash is received by a dissenting Petitioner shareholder from Petitioner, that cash will be treated as received by that shareholder in redemption of his Petitioner stock subject to the provisions and limitations of section 302 of the IRC.

#### 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."

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). However, there is no modification or adjustment applicable to a tax-free reorganization where, for federal income tax purposes, the transaction constitutes a statutory merger pursuant to section 368(a)(1)(A) of the IRC, and pursuant to section 368(a)(2)(E) of the IRC, stock of a corporation which before the merger was in control of the merged corporation is used in the transaction. Therefore, for purposes of section 1453 of Article 32 of the Tax Law, such reorganization would be treated the same as it is treated for federal income tax purposes.

Accordingly, since Sub's merger into Petitioner is a tax-free statutory merger under section 368(a)(1)(A) of the IRC, such merger would be a tax-free transaction for both Sub and Petitioner under Article 32 of the Tax Law. Also, since Petitioner and Parent are each "a party to a reorganization" within section 368(b) of the IRC and the stock of Parent is used in the transaction pursuant to section 368(a)(2)(E) of the IRC, and no gain or loss is recognized for the

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exchange of stock for federal income tax purposes pursuant to section 354(a) (1) of the IRC, no gain or loss from such exchange would be recognized for New York State franchise tax purposes under Article 32.

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."

Section 612 of the Tax Law does not contain any modification that affects the shareholders of the corporations that are each a party to a tax-free reorganization, where for federal income tax purposes the transaction constitutes a statutory merger pursuant to section 368(a) (1) (A) of the IRC and, pursuant to section 368(a) (2) (E) of the IRC, stock of a corporation which before the merger was in control of the merged corporation is used in the transaction.

Accordingly, if no taxable income will be realized by shareholders of Petitioner or Parent for federal income tax purposes as a result of a tax-free reorganization treated as a statutory merger of Sub into Petitioner pursuant to section 368(a) (1) (A) of the IRC including the exchange of stock pursuant to section 368(a) (2) (E) of the IRC, no taxable income will be realized for New York State personal income tax purposes. Where shareholders perfect their dissenters' rights under section 6022 of the Banking Law, such transaction, for New York State personal income tax purpose, will be accorded the same treatment as the transaction receives for federal income tax purposes.

Question 3

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

DATED: June 15, 1988

s/FRANK J. PUCCIA  
Director  
Technical Services Bureau

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