

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

TSB-A-92 (7) C
Corporation Tax
March 30, 1992

STATE OF NEW YORK

COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. C911224A

On December 24, 1991, a Petition for Advisory Opinion was received from Columbia Federal Savings Bank, 93-22 Jamaica Avenue, Woodhaven, New York 11421.

The issue raised by Petitioner, Columbia Federal Savings Bank, is whether a transaction that is a reorganization that qualifies as a tax-free exchange under sections 368(a)(1)(A) and 368(a)(2)(D) of the Internal Revenue Code (hereinafter "IRC") is a tax-free exchange for purposes of Article 32 of the Tax Law.

With respect to such reorganization, Petitioner requests that the following conclusions be reached:

1. The Reorganization described herein qualifies as tax-free exchange.
2. Petitioner will recognize no gain or loss upon the transfer of substantially all its assets to its second tier subsidiary ("Stock Bank") solely in exchange for equity interests (voting and liquidation rights) in its first tier subsidiary ("Holding Company") and Stock Bank's assumption of Petitioner's liabilities.
3. Petitioner will recognize no recapture income as a result of the transfers to Stock Bank.
4. Neither Stock Bank nor Holding Company will recognize gain or loss upon the receipt by Stock Bank of substantially all of the assets of Petitioner in exchange for voting and liquidation rights in Holding Company and Stock Bank's assumption of Petitioner's liabilities.
5. Stock Bank's basis in the property received from Petitioner will be the same as the basis of such property in the hands of Petitioner immediately prior to the Reorganization.
6. Stock Bank's holding period for the property received from Petitioner will include the period during which such property was held by Petitioner.
7. Subject to the conditions and limitations set forth in sections 381, 382 and 383 of the IRC, and the Treasury regulations promulgated thereunder, Stock Bank will succeed to and take into account for purposes of Article 32 of the Tax Law the same items of Petitioner described in section 381(c) of the IRC taken into account for Federal income tax purposes.

8. Stock Bank will take into its accounts the dollar balances of those accounts of Petitioner that represent bad debt reserves with respect to which Petitioner has taken a deduction for taxable years ending on or before the date of the transfer that is treated as part of the merger. The bad debt reserves will have the same character in the hands of Stock Bank as they would have had in the hands of Petitioner if no transfer had occurred. Stock Bank will not include in gross income for its taxable year in which the Reorganization occurs the amount of Petitioner's bad debt reserves that Stock Bank will take into its accounts.
9. No gain or loss will be recognized to the depositors and borrower members of Petitioner on the receipt of liquidation and voting rights with respect to Holding Company in exchange for liquidation and voting rights with respect to Petitioner.
10. The basis of the equity interests in Holding Company (voting and liquidation rights) received by the depositors and borrower members of Petitioner will be the same as their basis in Petitioner equity interests (voting and liquidation rights) exchanged therefor.
11. The holding period of Holding Company equity interests received by the depositors and borrower members of Petitioner will include the period during which their Petitioner equity interests surrendered in exchange therefor were held.

On August 22, 1991, the board of directors of Petitioner adopted that certain Plan of Reorganization from Mutual Savings Bank to Mutual Holding Company (the "Plan of Reorganization"). In general, under the Plan of Reorganization, Petitioner will (i) incorporate an interim federal stock savings bank (the "Holding Company") as a first tier subsidiary of Petitioner, and capitalize Holding Company with \$100,000, (ii) incorporate a stock bank as a wholly-owned subsidiary of Holding Company and a second tier subsidiary of Petitioner (the "Stock, Bank") and (iii) merge with and into Stock Bank. Stock Bank, as the surviving entity, will acquire substantially all of Petitioner's assets and become liable for all of Petitioner's liabilities. Simultaneously with the merger, the shares of Holding Company stock will be cancelled and Holding Company will exchange its federal stock charter for a federal mutual holding company charter, and will become the mutual holding company of Stock Bank. As part of the Reorganization, all liquidation and voting rights held by each depositor and borrower member of Petitioner will be converted into and exchanged for identical liquidation and voting rights in Holding Company. Deposit accounts in Petitioner will be exchanged for identical deposit accounts in Stock Bank. The foregoing transactions are referred to herein as the "Reorganization." As of the date of the Reorganization, the common stock issued to Holding Company by Stock Bank will be the only issued shares of Stock Bank's capital stock.

Upon the transfer of assets and the assumption of liabilities, those persons who as of the date of the Reorganization held depository rights with respect to, or other rights as creditors of, Petitioner shall thereafter have such rights solely with respect to Stock Bank. Each deposit account in Petitioner at the time of the Reorganization will become a deposit account in Stock Bank in the same amount and upon the same terms and conditions, except that the holder of each such deposit account will have voting and liquidation rights with respect to Holding Company rather than Stock Bank. Similarly, borrowers of Petitioner will become borrowers of Stock Bank. The rights of the borrowers will not change by reason of the recognition and they will receive no benefits that they did not enjoy as borrowers of Petitioner. Persons who were borrowers of Petitioner on February 21, 1989 ("borrower members") will have voting and liquidation rights in Holding Company following the Reorganization.

Stock Bank will be formed to afford it access to capital sources not traditionally available to mutual savings banks. The mutual holding company will be authorized to borrow funds and to contribute the proceeds of such borrowings to Stock ... Bank. Formation of a mutual holding company also is expected to facilitate acquisitions and the diversification of Holding Company's activities. Following the consummation of the Reorganization, Holding Company is expected to borrow funds by issuing notes or debentures in a private placement or public offering. The notes or debentures may be convertible into common stock of Stock Bank and may be secured by part or all of the common stock of Stock Bank. The net proceeds of such borrowings will be contributed to Stock Bank in exchange for additional common stock of Stock Bank. At this time, there can be no assurance when, if ever, such a borrowing will occur, what the terms and conditions of such borrowing will be, whether the debt will be convertible into the stock of Stock Bank or whether any investors would elect to convert convertible debt into the stock of Stock Bank.

Subsequent to the approval of the Plan of Reorganization by the OTS (Office of Thrift Supervision), a special meeting of members of Petitioner to approve the ... Plan of Reorganization will be scheduled in accordance with Petitioner's Bylaws. An affirmative vote of not less than a majority of the total outstanding votes of the members of Petitioner is required for approval of the Plan of Reorganization.

Following the Reorganization, Stock Bank, which will then be known as Columbia Federal Savings Bank, will have the power to issue shares of capital stock (including common and preferred stock) to persons other than Petitioner. So long as Petitioner is in existence, however, it must own a majority of the voting stock of Stock Bank. Stock Bank may issue any amount of non-voting stock to persons other than Petitioner. No such stock will be issued as of the date of the Reorganization.

While an offering of the common stock of Stock Bank may be made at some time following the Reorganization, subject to the approval of the board of directors of Stock Bank and the OTS, the actual timing of a stock offering, including the type of security to be issued and whether the offering will be made to the public or in a private placement, will depend on market, regulatory and other conditions, and there can be no assurance when, if ever, such a stock offering will occur. Currently, such an offering is not contemplated.

For purposes of obtaining counsel's opinion concerning the Federal income tax consequences of the Reorganization, Petitioner has made certain representations in connection with the Reorganization. Such representations are required by Rev. Proc. 86-42, 1986-2 C.B. 722 in order for the Internal Revenue Service to issue an advance ruling concerning Federal income tax consequences of transactions such as the Reorganization. The representations are as follows:

1. The fair market value of the voting and liquidation rights in Holding Company received by each depositor and borrower will be approximately equal to the fair market value of the voting and liquidation rights surrendered in the exchange.

2. There is no plan or intention by the depositors and borrower members of Petitioner who own one percent or more of the voting and liquidation rights in Petitioner, and to the best of the knowledge of the management of Petitioner, there is no plan or intention on the part of the remaining depositors and borrowers of Petitioner to sell, exchange or otherwise dispose of a number of voting and liquidation rights received in the transaction that would reduce Petitioner depositors' and borrower members' ownership of voting and liquidation rights in Holding Company to a number of shares having a value, as of the date of the Reorganization, of less than 50 percent of the value of all of the formerly outstanding voting and liquidation rights of Petitioner as of the same date. For purposes of this representation, voting and liquidation rights in Petitioner exchanged for cash or other property, surrendered by dissenters or exchanged for cash in lieu of fractional shares of voting and liquidation rights in Holding Company will be treated as outstanding Petitioner voting and liquidation rights on the date of the Reorganization. Moreover, voting and liquidation rights of Petitioner and of Holding Company held by Petitioner depositors and borrowers and otherwise sold, redeemed, or disposed of prior or subsequent to the Reorganization will be considered in making this representation.

3. Stock Bank will acquire 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 held by Petitioner immediately prior to the Reorganization. For purposes of this representation, amounts paid by Petitioner to dissenters, amounts paid by Petitioner to depositors and borrower members who receive cash or other property, Petitioner assets used to pay its reorganization expenses, and all redemptions and distributions (except for regular, normal payments) made by Petitioner immediately preceding the transfer, will be included as assets of Petitioner held immediately prior to the Reorganization.

4. Prior to the Reorganization, Holding Company will be in control of Stock Bank

within the meaning of section 368(c) of the IRC.

5. Following the Reorganization, Stock Bank may issue additional stock to persons other than Holding Company. There is, however, no agreement or understanding under the Plan of Reorganization to issue additional capital. An offering will occur only if approved by both the board of directors of Stock Bank and the OTS and only if market, regulatory and other conditions are favorable. Currently, such an offering is not contemplated and there is no way of knowing any of the terms and conditions of issuance and how many, if any, shares of stock actually would be sold if additional stock is issued. No underwriting agreements will be entered into prior to the Reorganization and here are no agreements with other persons to purchase stock. No negotiations have been carried on with respect to the purchase of common stock of Stock Bank.

6. Following the Reorganization, Holding Company may issue notes and debentures convertible into common stock of Stock Bank in a private placement or in a public offering. There is, however, no binding commitment under the Plan of Reorganization to issue notes or debentures. Currently, there is no way of knowing any of the terms and conditions of issuance, how much debt will be issued, whether the debt will be convertible into the stock of Stock Bank and whether any investors would elect to convert their debt instruments into the stock of Stock Bank. No underwriting agreements will be entered into prior to the Reorganization and there are no agreements with other persons to purchase the debt. In addition, no negotiations have been carried on with respect to the purchase of the convertible debt.

7. Holding Company has no plan or intention to liquidate Stock Bank; to merge Stock Bank with and into another corporation; to sell or otherwise dispose of the stock of Stock Bank; or to cause Stock Bank to sell or otherwise dispose of any of the assets of Petitioner acquired in the Reorganization, except for dispositions made in the ordinary course of business or transfers described in section 368(a)(2)(C) of the IRC.

8. The liabilities of Petitioner assumed by Stock Bank and the liabilities to which the transferred assets of Petitioner are subject were incurred by Petitioner in the ordinary course of its business.

9. Following the Reorganization, Stock Bank will continue the historic business of Petitioner or use a significant portion of Petitioner's business assets in a business.

10. Holding Company, Stock Bank, Petitioner, and the depositors and borrower members of Petitioner will pay their respective expenses, if any, incurred in connection with the Reorganization.

11. There is no intercorporate indebtedness existing between Holding Company and Petitioner or between Stock Bank and Petitioner that was issued, acquired, or will be settled at discount.

12. No two parties to the Reorganization are investment companies as defined in section 368(a)(2)(F)(iii) and (iv) of the IRC.

13. Petitioner is not under the jurisdiction of a court in a Title 11 or similar case within the meaning of section 368(a)(3)(A) of the IRC.

14. The fair market value of the assets of Petitioner transferred to Stock Bank will equal or exceed the sum of the liabilities assumed by Stock Bank, plus the amount of liabilities, if any, to which the transferred assets are subject.

15. No stock of Stock Bank will be issued in the Reorganization.

16. Holding Company has no plan or intention to reacquire any of its voting and liquidation rights issued in the Reorganization.

17. No subscription rights are currently held by either depositors or borrower members of Petitioner.

Section 1451 of Article 32 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 nine 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 transaction where, for federal income tax purposes, a reorganization is treated as an exchange pursuant to section 368(a)(1)(A) and (a)(2)(D) of the IRC and results in no recognition of gain or loss for Federal income tax purposes. Therefore, for purposes of section 1453 of the Tax Law, such transaction would be treated the same as it is treated for Federal income tax purposes.

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Accordingly, if Petitioner's transaction described herein is treated as a Reorganization that is a tax-free exchange under sections 368(a)(1)(A) and (a)(2)(D) of the IRC, such exchange would be tax-free for New York State franchise tax purposes under Article 32 of the Tax Law, and as a result, conclusions 1 through 11 requested by Petitioner would be reached.

DATED: March 30, 1992

s/PAUL B. COBURN
Deputy Director
Taxpayer Services Division

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