

Memorandum

To: Ms. Lisa Thompson (MIC:64)
Principal Property Appraiser

Date: January 30, 2012

From: Daniel Paul (MIC:82)
Tax Counsel

Subject: *Filing Requirements for Statutory Mergers and Statutory Conversions
Assignment No. 11-101*

This memorandum is in response to your request for a legal opinion on whether legal entities undergoing statutory mergers or statutory conversions are required to file *Form BOE-100-B, Statement of Change in Control and Ownership of Legal Entities* (Form 100B) with the Board of Equalization (Board) pursuant to Revenue and Taxation Code¹ section 480.1 or 480.2 within 90² days of the event.

I. Background

Section 64, subdivision (a) provides that the purchase or transfer of ownership interests in legal entities does not constitute a transfer of the legal entity's real property. One exception to the general rule excluding transfers of legal entity interests from change in ownership is provided in section 64, subdivision (c)(1), and Property Tax Rule³ (Rule) 462.180, subdivision (d)(1), which provide that when a legal entity or other person obtains control through direct or indirect ownership or control of more than 50 percent of a corporation's voting stock, or obtains a majority ownership interest in any partnership, limited liability company (LLC), or other legal entity, through the purchase or transfer of that corporate stock or other interest, there is a change in ownership of the real property owned by that corporation or other legal entity in which the controlling interest is obtained. For partnerships and LLCs, the degree of ownership is determined by the direct or indirect ownership of the interests in the capital and profits. (See Rule 462.180, subdivision (d)(1)(B).)

Section 480.1, subdivision (a) provides that whenever there is a change in control of a corporation or other legal entity as defined in section 64, subdivision (c)(1), the person or legal entity acquiring control of the corporation or other legal entity must file Form 100B with the Board within 90 days from the date of the change in control.

Section 480.2, subdivision (a) requires a Form 100-B to be filed whenever there is a change in ownership of any corporation, partnership, limited liability company, or other legal entity, as defined in section 64, subdivision (d).

¹ All statutory references are to the Revenue and Taxation Code unless otherwise indicated.

² Increased to 90 days from 45 days, effective January 1, 2012 (SB 507).

³ Cal. Code Regs., tit. 18, § 462.180. All Rule references are sections to title 18 of the California Code of Regulations.

Rule 462.180, subdivision (d)(4) provides that transfers of legal entity interests that result solely in a change in the method of holding title, and in which proportional ownership interests in all real property represented by the transferred interests remain the same after the transfer, do not constitute a change in ownership. Whenever a transfer of ownership interests in a legal entity (transferred entity) is excluded from change in ownership under Rule 462.180, subdivision (d)(4), immediately after the transfer the holders of the interests in the legal entity to which the interests were transferred (transferee entity) become "original co-owners" with respect to the legal entity ownership interests of the transferee entity for purposes of determining the change in ownership consequences of any subsequent transfers of transferee entity interests. (See Rule 462.180, Example 10.)

Rule 462.180, subdivision (d)(4) further provides that statutory mergers and conversions involving partnerships and LLCs do not result in the owners of the converted or surviving entity becoming original co-owners when the law of the jurisdiction of the converted or surviving entity provides that such entity remains the same entity or succeeds to the assets of the converting or disappearing entity without other act or transfer and the partners or members of the converting or disappearing entity maintain the same ownership interest in profits and capital of the converted or surviving entity that they held in the converting or disappearing entity.

II. Mergers

Entity Merges into Another Entity

A statutory merger⁴ is a transaction pursuant to either Corporations Code section 1100, 15911.02, 16910, or 17550 whereby two or more entities combine into a single entity that was one of the constituent (pre-existing) entities. When two entities merge in a statutory merger, the entity that ceases to exist is called the disappearing entity and the other is called the surviving entity.

In a statutory merger, all of the assets of the disappearing entity transfer to the surviving entity by "operation of law." This means that the transfer happens automatically and without the disappearing entity having to deed the assets to the surviving entity. The language in the statutes generally says something like the following: the surviving entity "*shall succeed, without other transfer, act, or deed, to all the rights and property, whether real, personal, or mixed, of each of the disappearing*" entities. (Corp. Code, §1107, subd. (a).)

The following Corporations Code provisions govern this process:

- (a) *Corporations*: Corp. Code, § 1107;
- (b) *LLCs*: Corp. Code, § 17554;
- (c) *Limited Partnerships*: Corp. Code, § 15911.16; and
- (d) *General Partnerships*: Corp. Code, § 16914.

⁴ All mergers must comply with statutory requirements. (9 Witkin, Summary of Cal. Law (10th ed. 2010) Partnership, §§ 52, 57, 121MM, 121QQ, 181, 185.) If there is an attempt to merge legal entities that fails to meet the statutory requirements, then no merger has occurred. In such a case, no transfer of real property or legal entity interests has occurred and Form 100B is not required to be filed.

To effectuate a statutory merger, the parties file a certificate of merger with the Secretary of State (or other similar state agency or division, for example, the New York Department of Corporations), which stamps and certifies the certificate. (Corp. Code, §§ 1103, 15911.14, 16915, 17552.) The surviving entity then records this certified certificate of merger, or a certified merger agreement, with the county recorder to demonstrate the transfer of the disappearing entity's real property and to have the recorder re-title it in the name of the surviving entity. The language in the statutes generally states something like the following:

[T]he filing for record in the office of the county recorder of any county in this state in which any of the real property of that disappearing party to the merger is located of a copy of the agreement of merger or consolidation or certificate of ownership or certificate of merger, certified by the Secretary of State or an authorized public official of the state or place pursuant to the laws of which the merger or consolidation is effected, shall evidence record ownership in the surviving or consolidated party to the merger, of all interest of the disappearing party to the merger in and to the real property located in that county. (Corp. Code, § 1109.)

The following Corporation Code provisions govern this process:

- (a) *Corporations*: Corp. Code, § 1109;
- (b) *LLCs*: Corp. Code, § 17556;
- (c) *Limited Partnerships*: Corp. Code, § 15911.18; and
- (d) *General Partnerships*: Corp. Code, § 16916.

Thus, when the surviving entity records a certified certificate of merger or merger with the county recorder, the recorder re-titles the property in the name of the surviving entity. A deed need not be recorded, although in practice it often is.

Since a statutory merger results in a transfer of the real property of the disappearing entity under state law, a statutory merger causes a change in ownership of the real property of the disappearing entity pursuant to section 61, subdivision (j). Since the transfer is of real property interests, the surviving entity is subject to the filing requirements under sections 480 and 480.3, and therefore must file a Change in Ownership Statement (COS) and Preliminary Change in Ownership Report (PCOR) with the appropriate county assessors for each piece of real property.⁵ This is the case even if the statutory merger is proportional—the surviving entity is a transferee of the assets and has the same filing requirements, although it would claim the exclusion from change in ownership for proportionality. If a statutory merger qualifies as proportionate, the surviving entity would not need to file a Form 100B because there are no transfers of legal entity interests, as discussed in the next section below.

⁵ This is consistent with Property Tax Annotation (Annotation) 220.0066. In that Annotation, SM Bank was the disappearing entity and M was the surviving entity. We advised that the property held by SM Bank transferred to M by the terms of the merger and thus underwent a change in ownership pursuant to section 61, subdivision (j).

Since a statutory merger results in a transfer of *all* assets of the disappearing entity, any ownership interests in legal entities that the disappearing entity owns directly would also transfer to the surviving entity as a result of the merger, which could result in a change in control of such subsidiaries under section 64, subdivision (c)(1) (in which case the *surviving entity* must file a Form 100B), or a change in ownership under section 64, subdivision (d) (in which case the *entity whose ownership interests were transferred* must file a Form 100B).

No Transfer of Legal Entity Ownership Interests in a Statutory Merger

In a statutory merger, the owners of the interests in the disappearing entity do not transfer their interests to anyone; rather, the ownership interests in the disappearing entity are canceled and cease to exist. The language in the statutes generally state that *the separate existence of the disappearing entities cease*.

The following Corporations Code provisions govern this process:

- (a) *Corporations*: Corp. Code, § 1107;
- (b) *LLCs*: Corp. Code, § 17554;
- (c) *Limited Partnerships*: Corp. Code, § 15911.16; and
- (d) *General Partnerships*: Corp. Code, § 16914.

Potential Transfer of Legal Entity Ownership Interests of the Surviving Entity

A separate inquiry is whether any person or entity gains control of the surviving entity at the same time as the merger within the meaning of section 64, subdivision (c)(1), or whether, cumulatively, more than 50 percent of the interests in the surviving entity are transferred by original co-owners, as one of the steps in the overall transaction or reorganization, which includes the statutory merger as one of the steps. If that is the case, then Form 100B must be filed, either under section 480.1 or 480.2, as applicable.

We note that the parties may describe the transfer of legal entity ownership interests of the surviving entity as being part of the "merger." However, any transfers of ownership interests in the surviving entity must be analyzed independently for change in ownership purposes. Legal entity ownership interests in the surviving entity may be transferred as part of the overall reorganization as payment, or consideration, to the prior owners of the disappearing entity. Thus, the owners of the disappearing entity may obtain an ownership stake in the surviving entity in exchange for their ownership stake in the disappearing entity. Transfers of the ownership interests in the surviving entity must be analyzed for whether a change in ownership has occurred under either section 64, subdivisions (c)(1) or (d).

If a change in control has occurred under section 64, subdivision (c)(1), the party acquiring ownership control must file a Form 100B under section 480.1, and if there is a change in ownership under section 64, subdivision (d), the surviving entity must file a Form 100B under section 480.2.

III. Statutory Conversions

A statutory conversion is a transaction pursuant to either Corporation Code section 1151, 15911.09, 16902, or 17540.2 whereby an entity converts to another entity of a different type. The entity that undergoes the conversion is called the converting or disappearing entity and the resulting entity is called the converted or surviving entity. (Corp. Code, §§ 1150, 15911.01, 16901, 17540.1.) Unlike a statutory merger, where the surviving entity already exists, the converted entity does not legally come into existence until the conversion. The converting entity "becomes" the converted entity.

In a statutory conversion, all of the assets of the converting entity are vested in the converted entity by "operation of law". This means that the vesting happens automatically and without the converting entity having to transfer or deed the property to the converted entity. There is not even a "transfer" by operation of law, just a new vesting. The language in the statutes generally says something like the following: "*An entity that converts into another entity pursuant to this chapter is for all purposes the same entity that existed before the conversion,*" (Corp. Code, § 17540.9, subd. (a)), and "*All the rights and property, whether real, personal, or mixed, of the converting entity ... are vested in the converted entity.*" (Corp. Code, § 17540.9, subd. (b)(1).)

The following Corporations Code provisions govern this process:

- (a) *Corporations*: Corp. Code, § 1158;
- (b) *LLCs*: Corp. Code, § 17540.9;
- (c) *Limited Partnerships*: Corp. Code, § 15911.09; and
- (d) *General Partnerships*: Corp. Code, § 16909.

If a conversion involving partnerships and LLCs occurs pursuant to any of the above provisions of the Corporations Code, and the partners or members of the converting or disappearing entity maintain the same ownership interest in profits and capital of the converted or surviving entity that they held in the converting or disappearing entity, then no change in ownership occurs and the owners of the converted or surviving entity do not become original co-owners. (Rule 462.180, subd. (d)(4).)

To effectuate a statutory conversion, the parties file a statement of conversion with the Secretary of State (or other similar state agency or division, like the New York Department of Corporations). (Corp. Code, §§ 1155, 15911.06, 16906, 17540.6.) The parties must record either a statement of conversion, certified by the secretary of state, or formative documents for the converted entity in the counties wherein the converting entity owned real property.

The following Corporations Code provisions govern this process:

- (a) *Corporations*: Corp. Code, § 1156;
- (b) *LLCs*: Corp. Code, § 17540.7;
- (c) *Limited Partnerships*: Corp. Code, § 15911.07; and

(d) *General Partnerships*: Corp. Code, § 16907.

Because a statutory conversion does not involve a transfer of legal entity interests, or a transfer of real property, in our opinion the converted entity is not required to file a Form 100B with the Board, and is not required to file a PCOR and COS with any county assessor. The recording of a deed is not necessary for real property to be re-titled in the name of the converted entity because the vesting happens pursuant to the Corporations Code. The recording of either a statement of conversion, certified by the secretary of state, or formative documents for the converted entity, in the counties where the converting entity owned real property, is sufficient for the counties to re-title all real property in the name of the converted entity.

IV. Conversions and Mergers Involving Corporations

Because statutory conversions do not result in any transfers of real property under state law, there are no change in ownership consequences and a statutory conversion involving corporations is covered by the rules discussed in Section III, above.

A statutory merger where corporations are involved is governed by the same rules discussed in Section II, above. The only difference is that where such a merger is proportional and qualifies for the exclusion under Rule 462.180, subdivision (d)(4), the parties may not avoid original co-owner status under that subdivision. Original co-owner status may only be avoided for corporations under section 64, subdivision (b), for transfers of real property between two corporations that are members of an affiliated group.

V. Recommended Changes to the Legal Entity Ownership Program (LEOP) Webpage

Based on the foregoing, we recommend that the LEOP webpage be revised to reflect the above conclusions regarding statutory mergers and conversions. Please find the attached documents with proposed changes to the pages "Definition of Change in Control" and "Definition of Change in Ownership."

DMP:yg

J:/Prop/Prec/Legal Entities/2012/11-101.doc

Attachments

cc: Mr. David Gau MIC:63
Mr. Todd Gilman MIC:70