

ST 18-0002-PLR 01/31/2018 WATERCRAFT USE TAX

Watercraft whose change in ownership is due to the merger of corporations into a limited liability company is not subject to Watercraft Use Tax. See 86 Ill. Adm. Code 153.105 and 805 ILCS 5/11.39 and 11.50. (This is a PLR.)

January 31, 2018

Re: Private Letter Ruling Request on Watercraft Use Tax

Dear Xxxxx:

This letter is in response to your letter dated November 16, 2017, in which you requested information. The Department issues two types of letter rulings. Private Letter Rulings (“PLRs”) are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. Persons seeking PLRs must comply with the procedures for PLRs found in the Department’s regulations at 2 Ill. Adm. Code 1200.110. The purpose of a General Information Letter (“GIL”) is to direct taxpayers to Department regulations or other sources of information regarding the topic about which they have inquired. A GIL is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120. You may access our website at www.tax.illinois.gov to review regulations, letter rulings and other types of information relevant to your inquiry.

Review of your request disclosed that all the information described in paragraphs 1 through 8 of Section 1200.110 appears to be contained in your request. This Private Letter Ruling will bind the Department only with respect to PARENT COMPANY and its affiliate entities COMPANY, COMPANY 1 (d/b/a COMPANY 2), COMPANY 3, and COMPANY 4 (the “Affiliate Entities”), for the issue or issues presented in this ruling, and is subject to the provisions of subsection (e) of Section 1200.110 governing expiration of Private Letter Rulings. Issuance of this ruling is conditioned upon the understanding that neither PARENT COMPANY, any of its Affiliated Entities, nor a related taxpayer is currently under audit or involved in litigation concerning the issues that are the subject of this ruling request. In your letter you have stated and made inquiry as follows:

Please view this letter as a private letter ruling request to the Illinois Department of Revenue (“Department”) that seeks the Department’s guidance on the application of the Watercraft Use Tax (35 ILCS 158/15-1 *et.seq.*) to the merger of PARENT COMPANY’s affiliate entities, COMPANY, COMPANY 1 (d/b/a COMPANY 2), COMPANY 3, and COMPANY 4 (the “Affiliate Entities”). This ruling requests a determination of whether watercrafts owned by these Affiliate Entities, which are used for dinner cruises, sightseeing and other cruises, would be taxed on the merger of these companies. Such a private letter ruling request is proper under 86 [sic] Ill. Admin. Code § 1200.110.

There are no regulations that are clearly dispositive of the issues in this request. And, there are no authorities that we are aware of that are contrary to the ruling request made herein.

To the best of our knowledge, the Department has not previously ruled on the same or a similar issue for the Affiliate Entities or a predecessor. Neither the Affiliate Entities nor their representative has previously submitted the same or a similar issue to the Department, but withdrew it before a letter ruling was issued. Moreover, the issues in this request are not part of any current audit with the Department, nor part of any pending litigation matter between the Department and the Affiliate Entities or any related company of the Affiliate Entities. Powers of Attorney for the Affiliate Entities are enclosed with this private letter ruling request.

BACKGROUND AND RELEVANT FACTS

The Affiliate Entities are engaged in the providing of dinner cruises, sightseeing cruises and other cruises in Illinois. Each of the Affiliate Entities own and operate watercraft to provide such services. To streamline its operating structure, PARENT COMPANY, the ultimate parent of the Affiliate Entities plans to merge these companies together, the surviving company will be COMPANY. ("COMPANY"), a Delaware LLC. This will result in COMPANY being the lone surviving operating company. This merger will be done and recognized under Delaware law (8 DE Code §252 *et. seq.*, and 2 DE Code §18-209) and Illinois law (805 ILCS 5/11.39). It will also be considered a tax-free merger for Federal Income Tax purposes under I.R.C. 368(a)(1)(A). A copy of the before and after chart of the company structure is enclosed.

APPLICABLE LAW

Under both Delaware and Illinois law, a merger of corporations and limited liability companies is allowed by law. See, 805 ILCS 5/11.39; 8 DE Code §264; 2 DE Code § 18-209. In Delaware (like Illinois), by operation of law, the merged entities "become part of" the surviving entity. 8 DE Code §259; 2 DE Code § 18-209. The assets of these merged companies thereafter become "vested" in the surviving entity. 8 DE Code §259; 2 DE Code §18-209. As stated in Section 259 of the Delaware General Corporate Law:

"the separate existence of all the constituent corporations . . . except the one into which the others . . . have been merged, as the case may be, shall cease and the constituent corporations shall become the new corporation. . . . and all property, real, personal and mixed . . . shall be vested in the corporation surviving..."

Likewise, Section 18-209 of the Delaware Limited Liability Act provides:

"all property, real, personal and mixed and all debts due to any said such domestic limited liability companies and other business entities . . . shall be

vested in the surviving or resulting domestic limited liability company or other business entity...”

As a result, upon the merger of the companies there is no actual transfer of the assets of the merged companies, rather the merged companies and their assets, as a matter of law, merely become part of the surviving entity. *Id.*

Similarly, as noted above, the Illinois Business Corporation Act treats merged companies in the same manner as Delaware law. See, §11.50 of the Illinois Business Corporation Act of 1983 (805 ILCS 5/11.50). In essence, Section 11.39 of the Illinois Business Corporation Act expressly recognizes the merger of foreign and domestic corporations and limited liability companies, and applies Section 11.50 of this Act to such mergers. See, 805 ILCS 5/11.39(f). Under Section 11.50 of the Illinois Business Corporation Act, such mergers are treated as the continuation of the merged companies as part of the surviving company, and the assets and liabilities of the merged companies simply become part of the surviving company by operation of law, just like under Delaware law. 805 ILCS 5/11.50.

The Watercraft Use Tax imposes a tax on the privilege of using watercraft acquired in a gift, transfer or purchase of such watercraft, not otherwise subject to the Illinois Use Tax. 35 ILCS 158/15-10. The Watercraft Use Tax is virtually identical to the Aircraft Use Tax. 35 ILCS 157/10-15. Like the Aircraft Use Tax, the Watercraft Use Tax does not have a specific exemption for transfers between related parties. However, as the Department recognized in ST 10-0007 PLR (10/13/2010), “if ownership of an aircraft changes as a result of a merger or consolidation, then no tax is due.” The reason for this is that in a merger there is no actual gift, transfer or purchase of the assets. *Id.* So, too, the same rationale would apply to mergers of entities owning watercraft, since no gift, transfer or purchase of the watercraft is occurring in such a merger.

ISSUE

Is a Watercraft Use Tax due on the merger of the Affiliate Entities with respect to the watercraft that becomes vested in COMPANY, the surviving Affiliate Entity.

ANALYSIS

The Watercraft Use Tax is designed to tax the privilege of using watercraft acquired by gift, transfer or purchase. 35 ILCS 158/15-10. By its very nature, the tax only applies if some transfer of watercraft occurs, similar to the Aircraft Use Tax. 35 ILCS 157/10-15. However, when no actual transfer occurs, but rather watercraft merely become vested by operation of law in a surviving entity as a result of a conversion or merger of entities into that entity, then no tax should be due. See, e.g., ST 10-0007 PLR (10/13/2010).

Unlike a gift, transfer or purchase of a watercraft, in a merger the constituent entities simply become part of the surviving entity, and by operation of law, the watercraft owned by those entities are now owned by that surviving entity. Since there is no

transfer of the watercraft to a new entity but merely a continuation of same ownership of the watercraft as part of the consolidated surviving entity, no Watercraft Use Tax is owed. See, 805 ILCS 5/11.50; 8 DE Code §259; 2 DE Code §18-209.

In Private Letter Ruling ST 10-0007 PLR, the Department addressed a virtually identical issue as presented in this private letter ruling request. The issue in Private Letter Ruling ST 10-0007 was whether the Illinois Aircraft Use Tax applied to an aircraft in a merger or consolidation under the Illinois Business Corporation Act. The Department concluded that the Aircraft Use Tax did not apply to mergers or consolidations, since “there is not a transfer between two separate legal entities, rather one entity become [sic] another entity, or is consolidated into a separate entity, while the original entity ceases to exist.” *Id.* Private Letter Ruling ST 10-0007 relied on Illinois law and stated that it was being consistent with how Illinois law treats such mergers. 805 ILCS 5/11.39 and 5/11.50. Notably, both the Department’s position and Illinois law is likewise consistent with how Delaware law treats such mergers. 8 DE Code §259; 2 DE Code §18-209.

In the matter at hand, the Affiliate Entities are merged into the surviving entity, COMPANY. No transfer, gift or purchase of the watercraft owned by the Affiliate Entities is occurring, rather the entities are simply being consolidated into the surviving entity. So, for the same legal and logical reasons that the Department concluded that the Aircraft Use Tax did not apply in Private Letter Ruling ST 10-0007, the Watercraft Use Tax should not apply here. Therefore, we request a private letter ruling be issued confirming that Watercraft Use Tax shall not apply to the watercraft owned by the Affiliate Entities in the merger of the Affiliate Entities into the surviving entity, COMPANY.

If you have any questions, need any additional documents or facts, or contemplate issuing a private letter ruling different from that requested above, please call.

DEPARTMENT’S RESPONSE:

Under the Watercraft Use Tax Law, a tax is imposed on the privilege of using, in this State, any watercraft acquired by gift, transfer, or purchase after September 1, 2004. This tax does not apply if the use of the watercraft is otherwise taxed under the Use Tax Act. 35 ILCS 158/15-10. The tax is imposed on the use of watercraft in this State regardless of whether the watercraft is actually registered under the Boat Registration and Safety Act. See 86 Ill. Adm. Code 153.105.

There is no exemption under the Watercraft Use Tax Law for watercraft transferred between related parties. Any transfer of watercraft between separate legal entities, even related entities, that is not otherwise exempt under the Law, is subject to Watercraft Use Tax. For a list of nontaxable transactions see 86 Ill. Adm. Code 153.115.

While a transfer of watercraft between related entities is taxable under the Watercraft Use Tax Law, if ownership of the watercraft changes as a result of a merger or consolidation, then no tax is

due. That result is in accordance with the provisions of Section 11.50 of the Business Corporation Act of 1983 related to the merger or consolidation of corporations, which reads in part:

“(a) When such merger or consolidation has been effected:

* * *

(2) The separate existence of all corporation parties to the plan of merger or consolidation, except the surviving or new corporation, shall cease.

* * *

(4) Such surviving or new corporation shall thereupon and thereafter possess all the rights, privileges, immunities, and franchises, as of a public or a private nature, of each of the merging or consolidating corporations; and all property, real, personal, and mixed, and all debts due on whatever account, including subscriptions to shares, and all other choses in action, and all and every other interest, of or belonging to or due to each of the corporations so merged or consolidated, shall be taken and deemed to be transferred to and vested in such single corporation without further act or deed; and the title to any real estate, or any interest therein, vested in any of such corporations shall not revert or be in any way impaired by reason of such merger or consolidation.

(5) Such surviving or new corporation shall thenceforth be responsible and liable for all the liabilities and obligations of each of the corporations so merged or consolidated; and any claim existing or action or proceeding pending by or against any of such corporations may be prosecuted to judgment as if such merger or consolidation had not taken place, or such surviving or new corporation may be substituted in its place. Neither the rights of creditors nor any liens upon the property of any such corporations shall be impaired by such merger or consolidation.

* * * ” 805 ILCS 5/11.50.

When corporations are merged or consolidated, as a matter of law, the new corporation takes over the prior corporation’s assets and liabilities as if it were the prior corporation. The assumption of the assets and liabilities by the surviving corporation or new company takes place as a matter of law. There is not a “transfer” between two separate legal entities, rather, one entity becomes another entity, or is consolidated into a separate entity, while the original entity ceases to exist. A transfer that is taxable under the Watercraft Use Tax does not occur in these instances.

This reasoning applies to a merger between a corporation and a limited liability company as well. Section 11.39 of the Business Corporation Act governs mergers between a corporation and a limited liability company. Subsection (f) of Section 11.39 states that “Section 11.50 of this Act shall, insofar as it is applicable, apply to mergers between domestic corporations and limited liability companies.” 805 ILCS 5/11.39(f).

The merger described in this letter ruling request occurs under the laws of Delaware. As demonstrated in this letter, the relevant provisions of Delaware law are comparable to the provisions of the Business Corporation Act of 1983 discussed above. For Watercraft Use Tax purposes Illinois

treats these Delaware mergers in the same manner as an Illinois merger. As described in the letter request, the change in ownership of the watercraft from each of the Affiliate Entities to COMPANY as a result of the merger of the Affiliate Entities into COMPANY under the Delaware Code provisions that are comparable to the relevant provisions of the Business Corporation Act is not subject to Watercraft Use Tax.

The factual representations upon which this ruling is based are subject to review by the Department during the course of any audit, investigation, or hearing and this ruling shall bind the Department only if the factual representations recited in this ruling are correct and complete. This Private Letter Ruling is revoked and will cease to bind the Department 10 years after the date of this letter under the provisions of 2 Ill. Adm. Code 1200.110(e) or earlier if there is a pertinent change in statutory law, case law, rules or in the factual representations recited in this ruling.

I hope this information is helpful. If you have further questions concerning this Private Letter Ruling, you may contact me at (217) 782-2844. If you have further questions related to the Illinois sales tax laws, please visit our website at www.tax.illinois.gov or contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

Richard S. Wolters
Chairman, Private Letter Ruling Committee

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