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Exploring the Flexibility Offered by the TBOC Merger Provisions

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I. Introduction.

The common conception of a merger is the combination of two entities into one surviving entity.[1] However, the Texas Business Organizations Code (the "**TBOC**")[2] provides that through the use of the merger provisions of the code, a Texas domestic entity (an organization formed under or the internal affairs of which are governed by the TBOC[3]) may be divided into two or more new domestic entities or other organizations or into a surviving domestic entity and one or more new domestic or foreign entities or non-code organizations.[4] This division through use of the merger statutes is sometimes called a divisive merger or a divisional merger.[5] These provisions remain unique to Texas, although Pennsylvania provides for a statutory division but does not deal with division in its merger statutes.[6]

Through an illustrative, fictitious case study, this paper will consider the possibilities presented by the Texas divisional merger provisions as a tool to accomplish client goals and will provide a checklist of steps required to accomplish a divisive merger of a Texas limited liability company or limited partnership (including presenting a form plan of merger). This paper will not examine the federal income tax implications of a divisive merger of a tax partnership, which will be covered in a companion paper.[7]

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[1] Steven A. Bank, *Taxing Divisive and Disregarded Mergers*, 34 Ga. L. Rev. 1523 (2000).

[2] TEX. BUS. ORG. CODE § 101.001 et seq.

[3] TBOC Sec. 1.002(18).

[4] TBOC Sec. 1.002(55)(A).

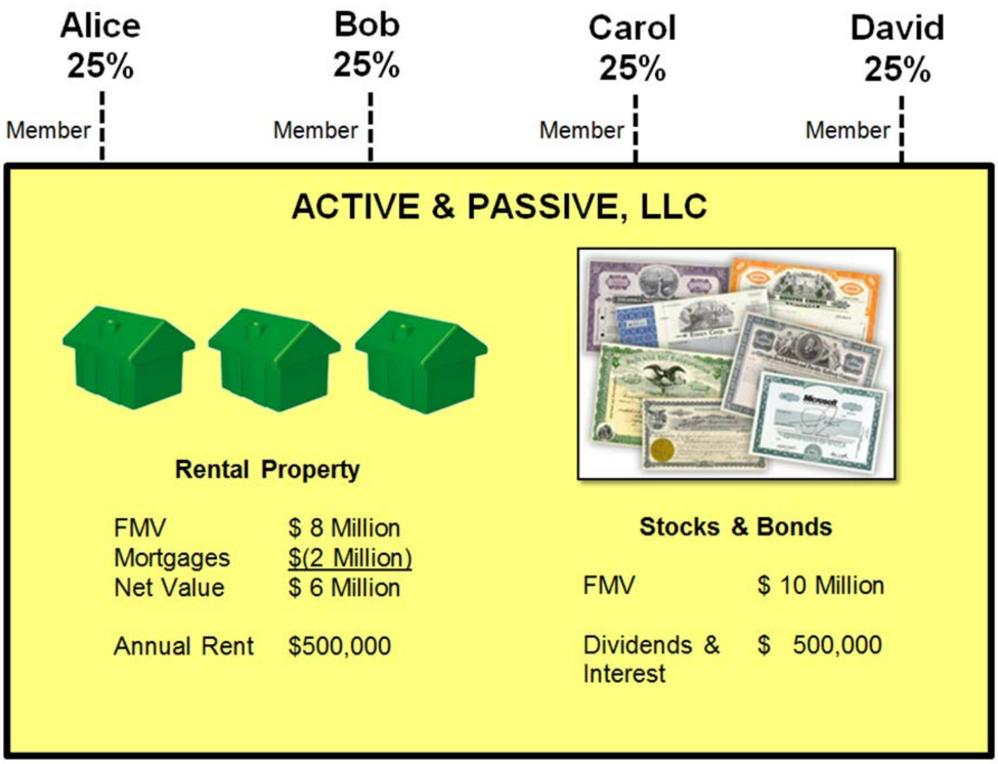
[5] The Texas divisional merger provisions came into existence when Texas adopted the revised Texas Business Corporation Act in 1989 and have since been expanded to cover not only corporations, but other forms of entities, as described above. Texas Business Corporation Act, 71st Leg., R.S., ch. 801, § 26, 1989 Tex. Gen. Laws 3610, 3629.

[6] 15 Pa. C.S.A. § 1951, et seq.

[7] See *Tax Consequences of Partnership Divisions* by Craig M. Bergez, presented at The University of Texas School of Law Continuing Legal Education Program on LLC's, LP's and Partnerships.

II. A Case Study.

A. Factual Assumptions. To illustrate how the flexible Texas merger statute could be used to solve problems for owners of an entity, let us consider a case study involving a fictitious entity that we will call "Active & Passive, LLC." Let's assume that Active & Passive, LLC is a Texas limited liability company with four individual owners, Alice, Bob, Carol and David, each whom own a 25% membership interest in the company. Let's further assume that Active & Passive, LLC has the following assets: rental real estate properties with an aggregate fair market value of $8,000,000 and a portfolio of stocks and bonds with an aggregate fair market value of $10,000,000. Let's assume that rental properties are encumbered by mortgages to secure debt aggregating $2,000,000 (so that the equity in the rental properties is $6,000,000) and that the stocks and bonds are owned free and clear. Let's assume that the rentals properties produce rental income each year of $500,000 and let's assume that the stock and bonds pay annual dividends and interest equaling $500,000. The diagram below illustrates these assumptions.



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