



# FEDERAL and STATE TAX UPDATE

FMS NJ/NY Half-Day Seminar  
Stony Hill Inn

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# Agenda

- ▶ Deferred Tax Asset Call Report Adjustments (Basel III)
- ▶ Accounting for Low Income Housing Credit Investments
- ▶ Bad Debt Charge-offs
- ▶ Cancellation of Indebtedness Income
- ▶ Loss Company Valuation for 382
- ▶ Pennsylvania Bank Shares Tax Update
- ▶ New York Bank Tax Reform for 2015
- ▶ Tax Reform Outlook



# Deferred Tax Asset Call Report Adjustments (Basel III)

## SIX PRINCIPLES

1. Netting DTL against related disallowed intangible asset
2. Netting DTA/DTL against related AOCI item opt out
3. NOL/credit carryforward DTA disallowed entirely
4. Residual DTL netted against NOL/credit carryforward DTA and Temporary Difference DTA proportionately
5. DTA determined net of valuation allowance
6. Future-income-dependent Temporary Difference DTA limited to 10% of CET 1 capital

# Deferred Tax Asset Call Report Adjustments (Basel III)- continued

Example	
Net DTA from income tax note (assumed)	\$20,000
Add back DTL (assumed)	<u>5,000</u>
Gross DTA <u>after</u> valuation allowance	\$25,000
Divide by NOL carryforward DTA (assumed)	<u>6,000</u>
Equals NOL carryforward DTA ratio	<u>24%</u>

# Deferred Tax Asset Call Report Adjustments (Basel III)- continued

Example - cont'd	
DTL (from prior slide)	\$5,000
Less DTL related to goodwill (assumed)	-1,000
Less DTL related to unrealized gains (assumed)	<u>-2,000</u>
Residual DTL	\$2,000
NOL carryforward DTA ratio (from prior slide)	<u>24%</u>
DTL apportioned to NOL carryforward DTA	<u>\$480</u>
Disallowed NOL carryforward DTA	<u>\$5,520</u>

# Deferred Tax Asset Call Report Adjustments (Basel III)- continued

Example - cont'd	
DTL apportioned to Temp Diff DTA	\$1,520
Net Temp Diff DTA	\$17,480
Temp Diff DTA recoverable in carryback	<u>10,000</u>
Temp Diff DTA future-income-dependent	\$7,480
10% of CET 1 capital before adjustment	<u>7,000</u>
Disallowed Temp Diff DTA	<u>\$480</u>

# Deferred Tax Asset Call Report Adjustments (Basel III)- continued

## Determine carryback refund potential at quarter-end

- Few states allow carrybacks
- 2-year federal carrybacks - real issue

Example - cont'd	
Regular federal income tax before credits	\$12,000
Less credits	-1,000
Less 10% Tentative AMT (assumed)	<u>-1,000</u>
Refund recoverable in carryback of Temp Diff.	<u>\$10,000</u>



# Deferred Tax Asset Call Report Adjustments (Basel III)- continued

- Capital loss carryforward treatment not clear
- Minimum tax credit carryforward treatment not differentiated
- Mind the phase-ins



# Low Income Housing Credit Investments

## ASU 2014-01

- Proportional amortization method of accounting for LIHC investments
  - Based on tax benefits realized in current year to total tax benefits expected over life of investment
- Current methods are Effective Yield Method, Equity Method and Cost Method
- An accounting policy election for all investments
- Most investments should qualify
- Loans made to project don't affect qualification
- Impairment = MLTN carrying amount will not be realized
  - Charge down to fair value
- Effective for years beginning after 15 December 2014
- Early adoption allowed and old investments grandfathered

# Low Income Housing Credit Investments

Example		Dr	Cr
Investment in LIH Project	\$90,000		
LIHTC	\$100,000		
Credit per year	\$10,000		
Tax loss per year	\$3,500		
<u>INVESTMENT</u>			
Investment in LIH Project		\$90,000	
Cash			\$90,000

# Low Income Housing Credit Investments

Example - continued	Dr	Cr
<u>Annual entry</u>		
Accrued income tax payable	\$13,500	
Investment in LIH Project		\$9,000
Cash		4,500

## LB&I Directive 04-1014-008

- Not applicable to bad debt reserve method
- Compelling case for making bad debt conformity election -Treas. Reg. sec. 1.166-2(d)(3)
  - enables deduction for :
    - Non-accrual interest
    - Non-credit impairment of debt securities - thus all of OTTI is deductible
- Automatic change of accounting method

## LB&I Directive 04-1014-008

- Relieves banks from obtaining subsequent express determination letters
- Implementing Directive will enable banks to:
  - Immediately deduct any remaining book charge-offs deferred for tax
  - Immediately deduct estimated costs to sell OREO capitalized into tax basis
  - Deduct credit-impairment of debt securities
- Make conformity election for 2014
- Need express determination letter from regulator relative to last examination

# Cancellation of Indebtedness Income

- IRS proposed regulations eliminate 36-month non-payment as an event requiring Form 1099-C
- Treas. Reg. 1.6050P-1(b)(2)(H)
- Remaining 7 identifiable events essentially predicated upon discharge of debt by operation of law or agreement between creditor and debtor

# Loss Company Valuation for 382

- Change of ownership of more than 50 percentage points triggers limitation on use of target loss company NOL and credit carryovers
- Annual limitation = AFLTTE \* “Value” of Loss Corporation immediately prior to change
- Many changes in ownership are “distressed” situations
  - Price is not “fair market value” - not a “willing seller”
- Deal price is low - annual 382 limit is low

# Loss Company Valuation for 382

- Valuation “finesse” project is available to raise annual limit by creating net “built-in gains”
- Start with target book value and add for:
  - Loan value mark-up
  - Charter in place
  - Core Deposit Intangible



# Pennsylvania Bank Shares Tax Notices - 2014

- New Jersey and New York Banks receiving notices from PA Dept. of Revenue
- PA law now defines nexus for Bank Shares Tax to include \$100,000 of receipts from loans to PA borrowers or loans secured by PA property
- Governor's tax proposal would eliminate the \$100,000 threshold
- Tax is typically not substantial
- Can avoid by moving PA loans to non-bank subsidiary
  - Different PA nexus rule for non-bank corporations

# New York City Tax Reform for 2015

- New York City Code Amended effective 1 January 2015 to “follow” NYS Tax Reform
- Rates reduced from 9% to 8.85% for community banks
- Single receipts factor apportionment phased in over 4 years to 2018
- NYC Code changes do not encompass a “receipts-sourced-in-city” nexus standard

# Tax Reform Outlook

## Federal

Senate -Class III up for re-election

	Republican	Democrat	Independent	Total
Now	54	44	2	100
2016 election	24	10	-0-	34
Safe seats	10	7	-	17
Other	14	3	-	17



# Tax Reform Outlook

## New Jersey

Republican governor till January of 2018

Senate                    24 Democrats        16 Republicans

Gen Assembly        48 Democrats        32 Republicans

Next election        November 2015 - only Assembly up for election

Veto override        54 Gen Assembly 27 Senate

\$1.75 billion budget shortfall

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Glenn is the practice leader for the financial institutions industry tax group at BDO. A partner in our Philadelphia office with more than 25 years of experience, Glenn provides tax consultancy to financial institution clients. Glenn lectures and writes widely in relation to financial institution taxation. He is a former member of the advisory board of the Bank Tax Institute and continues to serve that body periodically as a faculty member. He is a regular speaker at the annual PICPA Financial Institutions Conference.

His work includes counseling clients on accounting for income taxes under ASC 740; executive compensation; Pennsylvania, New Jersey, Delaware and New York state taxation of banks and thrifts; and financial transactions taxation. He also represents financial institution clients before the Internal Revenue Service, the New York State Department of Tax and Finance, the New York City Finance Department and the New Jersey Division of Revenue.

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