

IBANYS' Special Tax & State Budget Edition: April 1, 2014

**STATE BUDGET APPROVED:
IBANYS' EFFORTS PRODUCE MAJOR TAX SAVINGS FOR
NEW YORK COMMUNITY BANKS!**

An Important Message from IBANYS President & CEO John Witkowski:

Yesterday, the New York State Legislature approved the 2014-15 State Budget. It will result in tax savings for all New York community banks, and represents a major victory for the IBANYS membership.

The budget includes proposals made by the IBANYS Board of Directors and Government Relations team to protect community banks in the face of extensive tax reform which would have increased taxes for some community banks.

IBANYS retained former KPMG tax partner Brian Flynn as a consultant to analyze the tax consequences of the proposed budget to New York community banks. A number of recommendations were made by IBANYS to the Legislature and the Governor to prevent tax increases to banks. Key recommendations were the grandfathering of the REIT and an increase in the net interest deduction for residential and small business loans.

The budget adopted IBANYS' proposals, and makes fundamental changes in the way banks and thrifts are taxed in New York State. Among these changes are the merging of the bank tax into the commercial company tax, the adoption of combined unitary reporting and the adoption of economic nexus which will require out-of-state banks doing a banking business in the state but having no physical presence here to pay NYS taxes.

It also adopts a single factor apportionment concept based on the location of the borrower or the location of the property securing a loan, and eliminates the 3% tax calculated on minimum taxable income.

These changes are effective for tax years beginning in 2015. Further, there is a reduction in the corporate tax rate from 7.1% to 6.5% beginning in 2016.

Most importantly for community banks and small thrifts (for purposes of the law, institutions that have combined assets of \$8 billion or less) one of three deductions is available under the new law. They are the REIT deduction, which many community banks have utilized over the years; the residential and business loan deduction, and the subtraction modification for qualified residential loan portfolios. A summary of each deduction follows.

- The REIT deduction - When the governor proposed his budget, this deduction was not included. In fact, language specifically disallowing the deduction was included in the original bill. Due to the efforts of IBANYS the REIT deduction was restored. It must be used by banks or thrifts that maintained a REIT on April 1, 2014 for any year in which the REIT is still in existence. With the repeal of the minimum tax banks and thrifts may want to revisit the amount of mortgage loans in the REIT.
- Residential/small business loan deduction - A 50% net interest income deduction (i.e., interest income less interest expense deemed incurred to carry such loan) is provided for loans made to NYS borrowers or where the property securing the loan is located in the state. In order for a loan to qualify for this treatment it must be \$5,000,000 or less. When the Governor introduced the bill the deduction was 40% and the maximum amount of the loan to which the deduction would apply was \$1,000,000. As the result of suggestions made by IBANYS the amounts were raised to 50% and \$5,000,000.
- Subtraction modification for qualified residential loan portfolios - This deduction has been in the NYS bank tax law in the past, but could only be used by institutions with a thrift charter. This change was previously recommended to the New York State Tax Department by IBANYS. If 60% of a thrift or a community bank's assets fit within defined categories, then a deduction is available that consists of the amount by which 32% of the institution's Entire Net Income exceeds the bad debt deduction allowed for federal income tax purposes. Although this deduction was in the bill as originally presented, at IBANYS' request changes were made in the definitions of the asset categories which should make it easier for more banks and thrifts to qualify for this deduction.

The single factor formula for apportioning income to New York may also provide planning opportunities. This newsletter is intended a broad overview of the new law. Your tax advisor should be contacted for the details and specifics of how this law may impact your institution.

In short, as New York revamps its tax structure, the specific proposals that IBANYS developed and advocated will mean a much-improved tax situation for all eligible community banks and thrifts. This is a win/win situation that will produce tax savings both to institutions that currently have REITS, and those that do not.

While IBANYS was not alone in working to affect the original tax reform provisions, we began the process many months ago. The strong leadership from our officers, Board of Directors and CFO Peer Council (with particular thanks to Canandaigua National Bank & Trust EVP and CFO Larry Heilbronner) was a determining factor for this positive outcome. Many IBANYS member banks devoted their time and efforts, and played an important role in this accomplishment. IBANYS' Government Relations staff and

legislative counsel Bill Crowell then formulated and executed the action plan that contributed to today's success.

The end result -- significant bottom line savings for community banks -- is just one example of how IBANYS provides value to our membership, and to all of New York's community banks.

Together, IBANYS member banks have made a real difference in the economic condition, viability and future of New York's community banks, and ultimately to the communities we serve.

As our membership increases, so does the strength of our collective voice, and the value we are able to provide to all New York community banks becomes even more meaningful.

Thank you for your continued participation and support. IBANYS is already formulating programs to assist member banks in fully understanding the opportunities presented by these new tax changes, and will continue to keep you informed.

New York community banks play a vital role in our state and local economies. Tell your customers, business and elected leaders and media.

[Click here for quotes from Governor Cuomo and DFS Superintendent Lawsby extolling the performance and value of New York community banks.](#)

[Click here for the full NYS Study on community banking.](#)

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