HB 211

Department of Legislative Services

Maryland General Assembly
2009 Session

FISCAL AND POLICY NOTE

House Bill 211 (Delegate Frick, *et al.*)
Ways and Means

Income Tax - Banks - Treatment of Losses on Loans and Bad Debts After Change of Ownership

This bill decouples the Maryland income tax from Notice 2008-83 issued by the Internal Revenue Service.

The bill takes effect July 1, 2009 and applies to any taxable year to which Notice 2008-83 is applicable.

Fiscal Summary

State Effect: Income tax revenues may increase significantly beginning in FY 2010. Federal legislation passed by the U.S. Congress but not yet signed by the President will significantly limit the impact of the bill. General fund expenditures increase by $20,700 in FY 2010 for one-time tax form changes and computer programming modifications at the Comptroller's Office.

Local Effect: Local income tax revenues and local highway user revenues may increase significantly beginning in FY 2010. Local expenditures are not affected.

Small Business Effect: None.

Analysis

Current Law/ Background: Section 382 of the Internal Revenue Code (IRC) was enacted in 1986 to prevent companies from acquiring other companies solely for tax-motivated purposes. Section 382 imposes an annual limitation on the use of net operating losses (NOLs) and other tax attributes following a change of ownership in the loss corporation of more than 50 percentage points by one or more 5% shareholders within a three-year period. Under Section 382, the corporation's NOLs incurred prior to the change of ownership can be utilized each year in an amount equal to the "IRC Section 382 limitation." IRC Section 382 limitation is equal to the fair market value of the loss corporation's stock immediately before the ownership change multiplied by the federal long-term tax-exempt rate.

In 2008, the IRS issued Notice 2008-83, which interpreted Section 382 of IRC to allow banks and other financial institutions pursuing acquisitions to write off acquired losses stemming from takeovers of other banks to offset future income. Notice 2008-83 effectively removed the limit on how much taxable income a purchasing bank, thrift, industrial loan company, and trust company can deduct postacquisition. The notice was designed to help the struggling banking sector recover by allowing acquiring banks the ability to deduct the built-in tax losses of any banks they acquire that possesses a portfolio of loans that have deteriorated in value.

According to several published news reports, several members of Congress and tax analysts questioned the authority of the U.S. Department of the Treasury to issue the notice and the timing and manner in which the notice was issued. In response to these concerns, the economic stimulus bill passed by the U.S. Congress, the American Recovery and Reinvestment Act of 2009 (H.R. 1), includes a repeal of Notice 2008-83. Any banks that already have binding agreements to purchase other banks on or before January 16, 2009, would be able to use the Treasury-created exemption, but all deals after that date would be subject to the standard tax code Section 382 rules.

The provision states that Congress finds that the delegation of authority to the Treasury Department under Section 382(m) does not authorize the Secretary to provide exemptions or special rules that are restricted to particular industries or classes of taxpayers. Also, the statute says that IRS Notice 2008-83 is inconsistent with the congressional intent in enacting Section 382(m) and that the legal authority to prescribe Notice 2008-83 is doubtful.

With two exceptions, H.R. 1 states that Notice 2008-83 will not have any effect for any ownership changes after January 16, 2009. One exception is for ownership changes pursuant to a binding contract entered into on or before January 16, 2009. The second exception applies to changes made pursuant to an agreement entered into on or before January 16, 2009, that are described in a public announcement or in a filing with the U.S. Securities and Exchange Commission. The provision is expected to increase federal revenues by $7.0 billion over 10 years.

State Revenues: The bill decouples the State income tax from Notice 2008-83 issued by IRS for any tax year in which the notice is in effect. Businesses are required for State income tax purposes to calculate deductions and losses without regard to the provisions available under Notice 2008-83. As a result, general fund revenues and Transportation Trust Fund revenues may increase significantly beginning in fiscal 2010. The amount of the revenue gain cannot be reliably predicted and depends on the amount of related acquisitions that occur in each, the amount of losses, and extent to which the losses and income are apportioned to Maryland.

President Obama has announced that he intends to sign the economic stimulus bill February 17, 2009. The stimulus bill repeals Notice 2008-83 for any ownership changes after January 16, 2009. If the economic stimulus bill becomes law, the extent of any revenue gain under HB 211 will be limited to ownership changes before January 16, 2009 and to any exceptions specified in the economic stimulus bill.

State Expenditures: The Comptroller's Office reports that it will incur a one-time expenditure increase of $20,700 in fiscal 2010 to add the subtraction modification to the personal income tax form. This amount includes data processing changes to the SMART income tax return processing and imaging systems and systems testing.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): Office of the Comptroller, CCH Incorporated, Department of Legislative Services

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Analysis by: Robert J. Rehrmann

Direct Inquiries to:
(410) 946-5510
(301) 970-5510