Far and Wide:
UNDERSTANDING YOUR FEDERAL AND STATE TAX LIABILITIES

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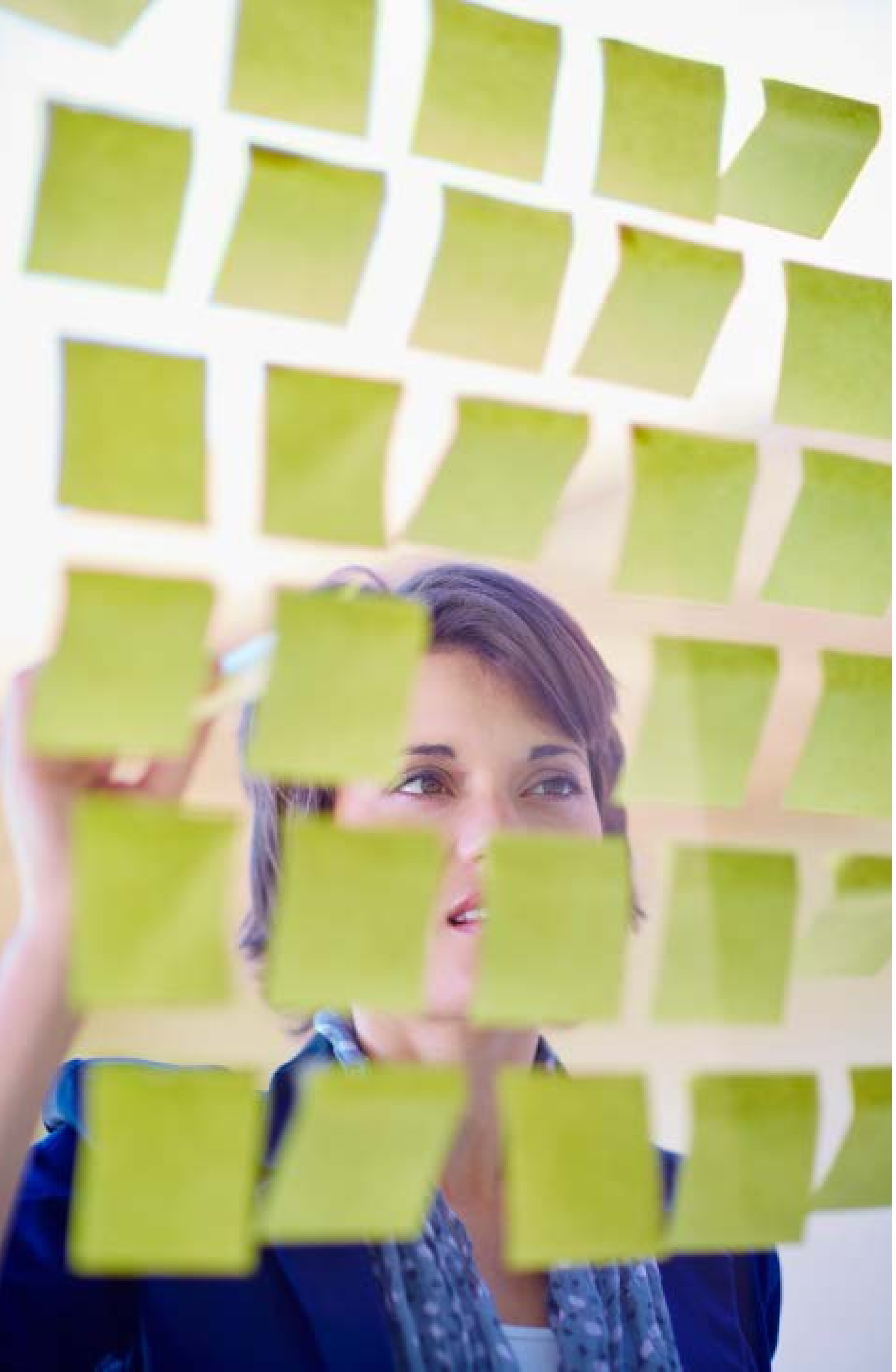


Agenda

- What is nexus?
- How is nexus determined for banks?
- Impact of filing versus not filing state returns
- Voluntary disclosure programs

What is Nexus?

Connection a potential taxpayer has with a state that permits the state to assess various types of taxes

Minimum physical presence required before a state taxing authority can subject a taxpayer to taxes within the state

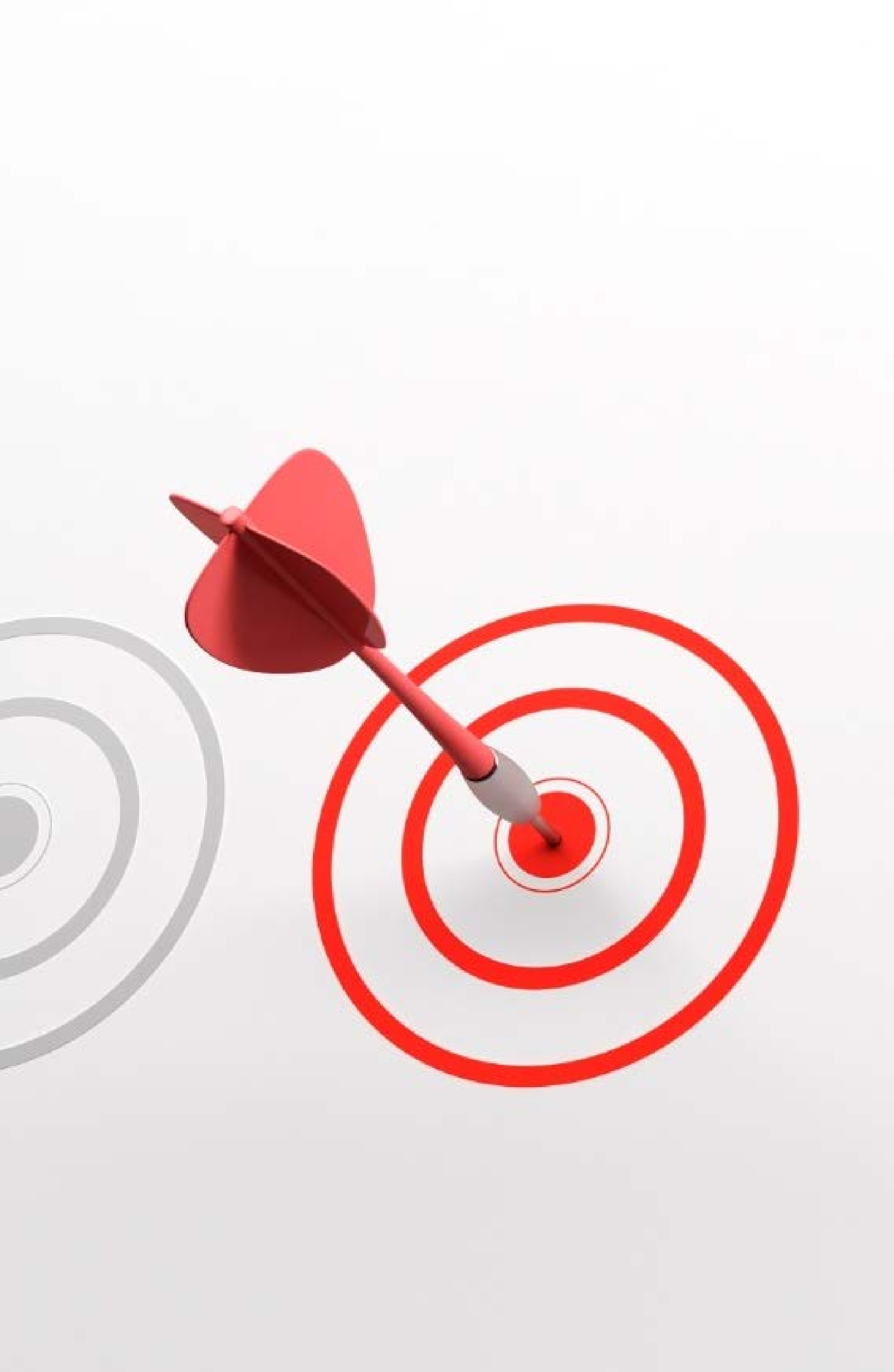
Nexus rules can vary from state to state

A business with nexus in a state is required to register, file and pay various taxes in that state

Nexus

QUILL CORP V. NORTH DAKOTA:

- U.S. Supreme Court Case
- Office supply retailer; no physical presence
- Licensed computer software program that ND customer used to check inventory and place orders.
- ND tried to impose sales tax on floppy disks located in the state
- Court ruled that Quill had nexus under Due Process Clause but not under Commerce Clause
- Court ruled that a state cannot require out-of-state seller to collect sales tax if seller has no physical presence



After the Quill Case

- States confined by the physical presence test from the Quill case
- States began looking for indirect physical presence
- Internet sales and changes in technology expand the range of nexus creating activities
- Pressure from in state retailers who were afraid of losing sales
- State budget deficits and revenue needs drive their approach to nexus

Common Activities that Create NEXUS

- Place of business: office, branch, warehouse, etc.
- Ownership of: equipment, land, property, inventory or other types of tangible personal property in state
- Employees residing in state
- Performing services in state
- Third party relationships such as agents, independent contractors, sales reps, etc.
- Frequent or recurring solicitation
- In-state affiliates

Agency NEXUS

- Nexus can be created through independent contractors and third parties
- Scripto, Inc. v. Carson – U.S. Supreme Court case
- Court held that, for nexus purposes, distinction between an employee and independent contractor was “without constitutional significance”
- In other words: nexus cannot be avoided by outsourcing activities to a third party that would otherwise create nexus

Affiliate/Attributional NEXUS

- Attributing nexus from an affiliate of a taxpayer if there is an overlap of selling or other shared activities
- Activities of one company may create nexus

EXAMPLES:

- Out of state seller owns in state seller and they sell the same or similar products
- In state taxpayer performs other services assisting, or on behalf of, out of state seller

Public Law 86-272

Prohibits state from imposing a “net income tax” on taxpayers whose only in state activity is solicitation of orders for tangible personal property

Protected if:

- Order approved outside of state, and
- Orders are shipped from outside the state

Public Law 86-272

- PL 86-272 does not apply to the following types of taxes:
- Capital or equity based taxes
- Franchise taxes not based on net income
- Business activity taxes
- Gross receipts taxes
- Minimum taxes

Factor-Based NEXUS

- Based on meeting certain thresholds such as:
  - Gross receipts exceed a certain amount
  - Payroll exceeds a certain amount
  - Property exceeds a certain amount
- Some states have adopted this model

Financial Institution NEXUS Standards

NEXUS CREATING ACTIVITIES:

- Loans secured by real or tangible personal property in state
- Deposits of a certain amount attributable to a state
- Loans of a certain amount attributable to a state
- Solicitation of, or activities with, a certain number of customers within a state
- Receipts of a certain amount derived from customers within a state
- Hire of in-state third party to close loans
- Purchased mortgages in secondary market on in-state property

Financial Institution NEXUS Standards

ADDITIONAL NEXUS CREATING ACTIVITIES:

- Solicitation of credit cards via mail or internet website
- Purchase of consumer loans on secondary market secured by tangible personal property
- Hire of unrelated, in-state, third party to service loans
- Foreclosure on in-state properties
- Resident of state holds institution's credit cards

NEXUS Example:

MASSACHUSETTS

- Activities conducted on a regular basis if:
- Conducted with 100 or more residents of MA during any taxable year, or
- Taxpayer has $10,000,000 or more of assets attributable to sources within MA, or
- Taxpayer has in excess of $500,000 of receipts attributable to MA
- This is a rebuttable presumption

We Have NEXUS – Now What?

- If you determine the institution has nexus generally you must file a tax return in that state
- Taxable income is typically apportioned using a three factor formula:
  1. Gross receipts
  2. Payroll
  3. Property (including rents paid)
- Taxable income is apportioned based on the state's formula
- Many states have minimum taxes and/or capital or asset based taxes

Determining When and Why to File

- State’s filing threshold versus management’s filing threshold?
- Is there a difference?

CONSIDERATIONS

- Impact on tax accrual, tax expense, deferred taxes and uncertain tax positions
- Risk of examination if return not filed
- Tax, penalty and interest exposure
- Apportionment for home state tax returns – is it different if we do/do not file in other states

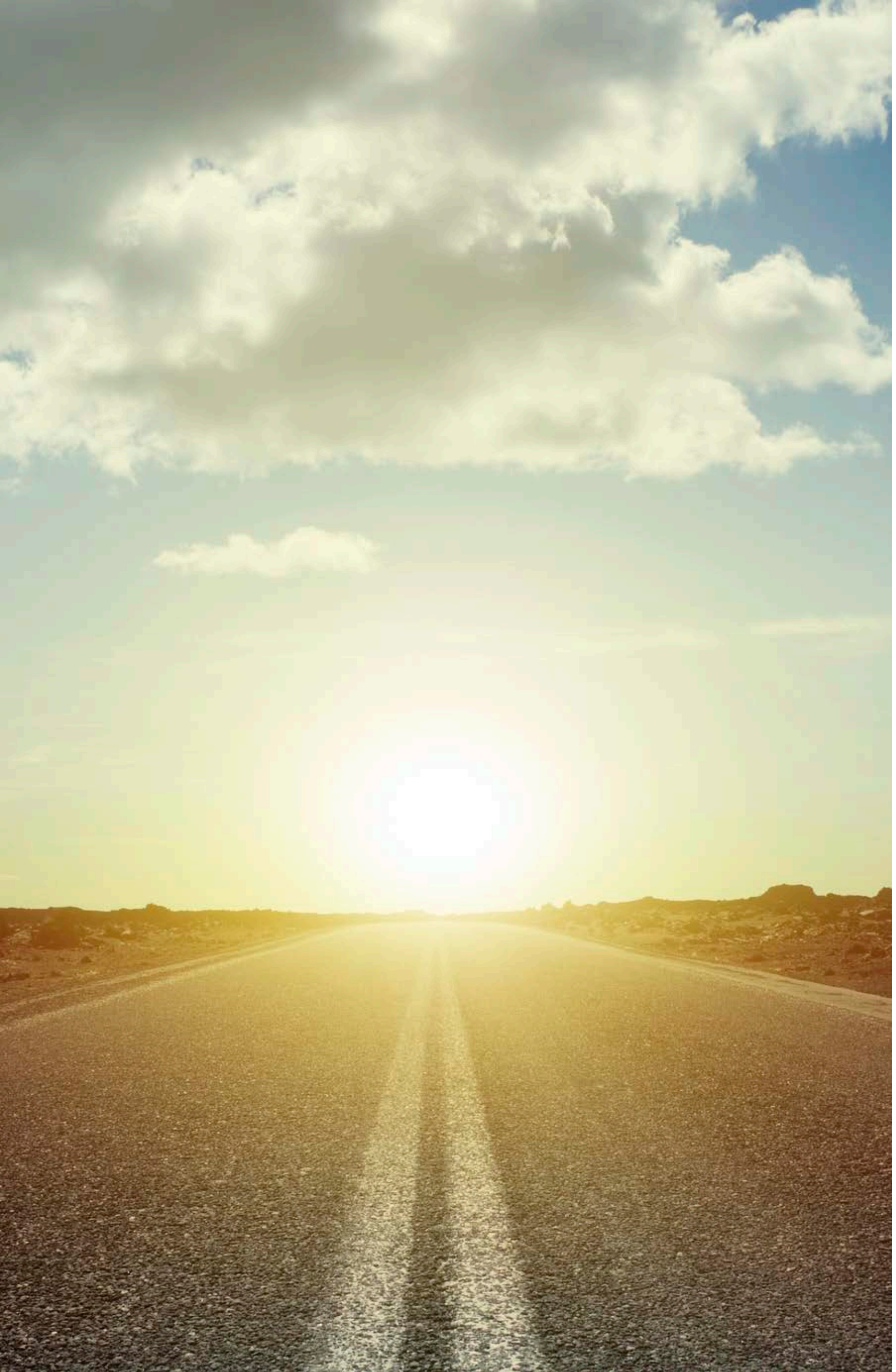
Coming Clean

VOLUNTARY DISCLOSURE PROGRAMS

PROGRAMS WHEREBY TAXPAYERS RECEIVE CERTAIN BENEFITS FROM PROACTIVELY DISCLOSING PRIOR PERIOD TAX LIABILITIES

- Limitation on look back period (usually three to six years)
- Abatement of penalties
- Full or partial interest: abate interest in full, lower rate or no benefit
- Brings closure to prior periods
- Protects buyers in case where sale may occur
- Will incur costs and compliance burden in utilizing these types of programs

NEXUS Related Questions?



2016 Update:
FEDERAL TAX LAWS

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On Track with Your Agenda

UNDERSTAND HOW THE **PROTECTING AMERICANS FROM TAX HIKES ACT OF 2015** AND OTHER TAX PROVISIONS FROM THE **CONSOLIDATED APPROPRIATES ACT OF 2016** IMPACT YOUR FEDERAL INCOME TAXES

- Business credits, deductions and other items
- Depreciation and expensing
- Energy Provisions including credits
- Tax compliance and reporting
- Procedure and administration

Research Credit

THE RESEARCH AND EXPERIMENTATION CREDIT WAS RESTORED FOR 2015 AND MADE PERMANENT.

R&E CREDIT

- Has expired eight times in 16 years
- Reinstated several times
- Permanent credit as of 2015

BASICS

- Credit available for qualified expenses
- Credit is 20% or 13% if an election is made
- Not just “lab research”
- Business improvement and technology also qualify

Technology

INTERNAL USE SOFTWARE:
Can qualify for the R&D credit

- New Regs issued in 2015
- Must meet three conditions
  1. Qual research (41(d))
  2. Not specifically excluded
  3. One of three conditions
     a. High threshold
     b. Dev – other research
     c. Use in production proc.

Technology

HIGH THRESHOLD TEST

INNOVATIVENESS:
Reduced cost or improved speed

ECONOMIC RISK:
Commit substantial resources and uncertainty in recovering resources

COMMERCIAL AVAILABILITY:
Not off shelf; modification of commercially available software qualify? Courts are split

Work Opportunity Tax credit

Restored and extended through 2019; two tiered credit

Credit is 40% of first year qualified wages; however

If hours worked at least 120 but less than 400; credit is 25%

Maximum credit per worker is $2,400

Certification is required by employment date

Work Opportunity Tax Credit

TARGETED GROUPS

- IV-A assistance (TANF)
- Veterans
- Ex-Felons
- Summer youth
- SSI – social security
- Designated community (e.g. empowerment zone)
- Long term family assistance
- **Long-term unemployment**
- Nutrition assistance

Fixed Assets and Depreciation

- Bonus depreciation extended through 2019, or 2020 for specific items.
- Deduction is 50% of cost
- AMT uses same method
- Phasedown of credit after 2017
- 2018 is 40%
- 2019 is 30%
- Long production period property may qualify for an extra year.

Fixed Assets and Depreciation

QUALIFYING PROPERTY

- Original use must be new
- Tangible personal property
- If ADS required, no bonus
- Timely placed in service
- Timely acquisition requirement

Depreciation

QUALIFIED LEASEHOLD IMPROVEMENTS

GENERAL RULE

- 39 year life for depreciation
- Straight line method
- AMT same as regular tax
- Improvement to realty
- Not tangible personal property such as teller work area

EXCEPTIONS TO PATH

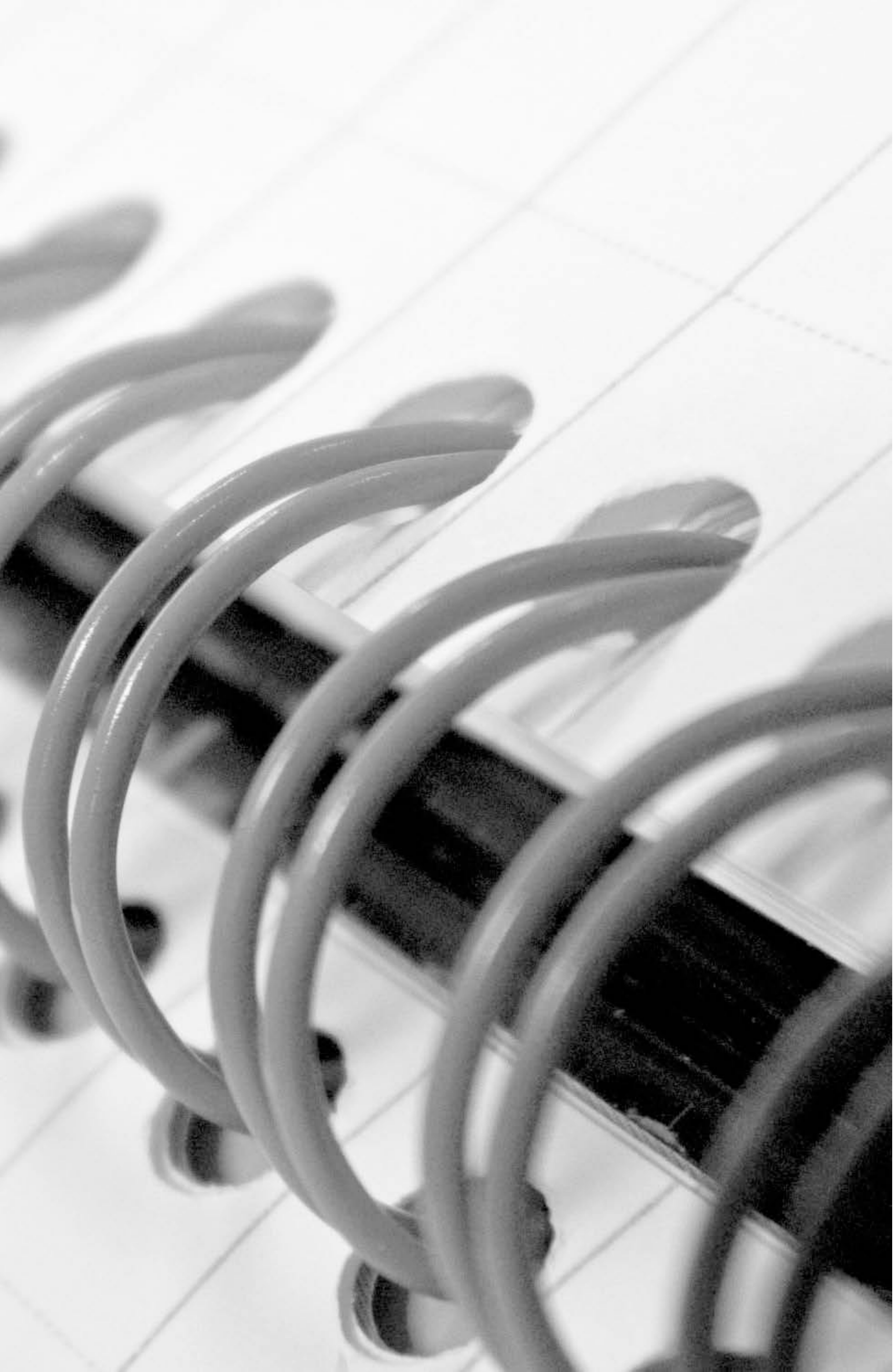
- Enlargements
- Elevators
- Structural framework

Depreciation

QUALIFIED LEASEHOLD IMPROVEMENTS

PATH RULE

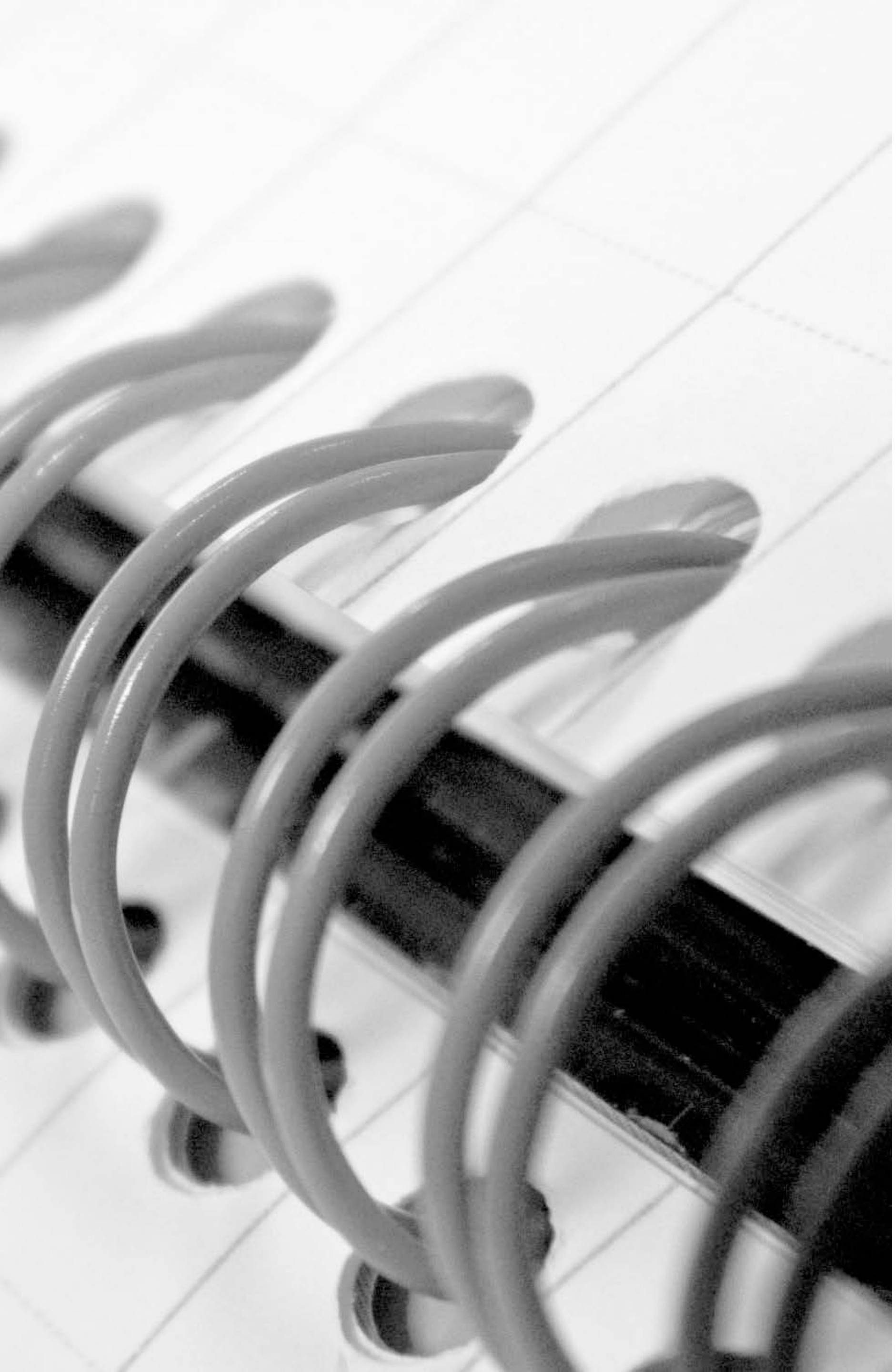
- 15 year life for depreciation
- 150 declining balance
- AMT same as regular tax
- Bonus depr permitted
- Improvement made pursuant to a lease
- Lease not between related parties
- Building in service at least 3 years



Depreciation Section 179 Expensing

GENERAL RULE

- Qualifying property can be immediately expensed
- Tangible personal property – used or new
- Same for AMT
- Ability to revoke election now permanent
- HVAC may now qualify – see next slide



Depreciation Section 179 Expensing

LIMITATIONS

- Allowable expense cannot exceed $500,000
- Phase-out if total additions exceed $2,000,000

OLD LAW

$25,000 deduction with phase-out at $200,000

Energy Credit for Solar Property

Credit extended

2016

Due to expire

Some phase-outs for construction start before 2021 and finish before 2023

2021

Extension ends

Energy Credit for Solar Property

CREDIT APPLICATION

- A percentage of qualified expenses – 30%
- Qualifying expenses are: equipment/ supplies that produce solar energy plus labor
- Basis reduction is 50% of the credit
- Credit can also be used against AMT

Tax Return Due Dates

OLD LAW

- Calendar year taxpayers – Due date of March 15
- Fiscal year-end due date was the 15th day of 3rd month after year-end. (2 ½ months)
- Could be extended another 6 months – to September 15 for calendar year taxpayers.

Tax Return Due Dates

NEW LAW

- C Corporations, for tax years beginning after 12/31/2015, will be due the 15th day of the 4th month.
- Calendar year will be April 15th.
- C corps with June 30 y/e still use 15th day of 3rd month until yrs beginning after 12/31/2025
- Extension still 6 months but until 2026 it is 5 months.

Tax Return Due Dates

- Partnerships will be due on the 15th day of the 3rd month – March 15
- Partnerships will be given 6 month extensions, instead of 5.
- Trusts returns are due the 15th day of 4th month – April 15. Extension will be 5 ½ months instead of 5. Extend due date will be September 30.
- Form 5500 extension remains 2 ½ months. Was 3 ½ months very briefly but law repealed.
- FBAR due April 15 with maximum extension of 6 months

Mortgage Interest Reporting

INFORMATION REQUIRED

- Name, address and TIN of borrower
- Amount of interest, other than points
- Amount of points and whether paid directly by borrower
- Name, address and TIN of lender
- Refund of overpaid interest

Mortgage Interest Reporting

NEW REQUIREMENTS

- Amount of outstanding principal on the loan
- Date of origination of loan
- Address of property which secures loan (description if no address)
- Applicable to Forms 1098 provided after 12/31/2016. See new Form 1098 for 2016.

Information Returns

DUE DATE CHANGES

OLD LAW

- Form W-3 and 1096/1099 were due to the IRS from the Employer by February 28.
- Information return penalty: maximum (3rd tier) of $100 per return and $1,500,000 per calendar year.
- Lower penalty (2nd tier) if by Aug 1 of $60 per return and a maximum of $500,000
- Lowest penalty (1st tier) if filed no less than 30 days late was $30 per return and a maximum of $250,000
- Lower maximums for small business

Information Returns

DUE DATE CHANGES

NEW LAW

- Form W-3 and 1096/1099 are now due to the IRS from the Employer by January 31. Effective for 2016.
- Information return penalty: maximum (3rd tier) of $250 per return and $3,000,000 per calendar year.
- Lower penalty (2nd tier) if by Aug 1 of $100 per return and a maximum of $1,500,000
- Lowest penalty (1st tier) if filed no less than 30 days late was $50 per return and a maximum of $500,000
- Max for small business also higher

Tax Exempts and Development Incentives

- Qualified Zone Academy Bonds (QZABS) have been extended through 2016. These are bonds that pay a tax credit rather than interest.
- New Markets Tax Credit: retroactively restored for 2015 and extended through 2019. Credit is 39% and claimed over 7 years.
- Empowerment zone designation retroactively restored and extended through 2016. (Boston, MA; Aroostook County, ME; New Haven, CT). Employment credits up to $3,000 per employee.

IRS LB&I

NEW EXAMINATION PROCEDURES

- IRS introduced new audit procedures for LB&I and issued Publication 5125.
- Procedures are intended to:
  - Issues based approach
  - Establish roles for IRS and Business
  - Examiners are to work transparently to understand business and share that issues have been identified for examination
  - Discuss IDR before issuing
  - Keep taxpayer informed regularly
  - Provide written documentation of facts and seek taxpayer acknowledgement.

IRS LB&I

NEW EXAMINATION PROCEDURES

- Procedures are intended to (cont.):
  - If issued unagreed, document disputed facts
  - Apply facts to the law in a fair & impartial manner
  - Prepare well-developed Notices of Proposed Adjustment
  - Taxpayer to respond timely on agreed upon schedule
  - Taxpayer to review and discuss IDRs before issued
  - Collaborate with IRS to agree on facts
  - IRS to provide audit plan with defined steps

Contact Us

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