

54:10A-4

LEGISLATIVE HISTORY CHECKLIST

NJSA: 54:10A-4 (Banking corporations-- domestic subsidiaries-- exempt debts owed to each other from taxation)

LAWS OF: 1985 **CHAPTER:** 468

BILL NO: S45

Sponsor(s): Weiss

Date Introduced: Pre-filed

Committee: Assembly: Revenue, Finance and Appropriations
Senate: Revenue, Finance and Appropriations

Amended during passage: Yes according to Governor's recommendations Amendments denoted by asterisks

Date of Passage: **Assembly:** January 3, 1985 Re-enacted 1-6-86
Senate: October 22, 1984 Re-enacted 11-18-85

Date of Approval: January 6, 1986

Following statements are attached if available:

Sponsor statement: Yes

Committee statement: **Assembly** Yes
Senate Yes

Fiscal Note: No

Veto Message: Yes

Message on Signing: No

Following were printed:

Reports: No

Hearings: No

468 85
1-6-86
[SECOND OFFICIAL COPY REPRINT]

SENATE, No. 45

STATE OF NEW JERSEY

PRE-FILED FOR INTRODUCTION IN THE 1984 SESSION

By Senator WEISS

AN ACT to amend the "Corporation Business Tax Act (1945)," approved April 13, 1945 (P. L. 1945, c. 162).

1 BE IT ENACTED *by the Senate and General Assembly of the State*
2 *of New Jersey:*

1 1. Section 4 of P. L. 1945, c. 162 (C. 54:10A-4) is amended to
2 read as follows:

3 4. For the purposes of this act, unless the context requires a
4 different meaning:

5 (a) "Commissioner" shall mean the Director of the Division of
6 Taxation of the State Department of the Treasury.

7 (b) "Allocation factor" shall mean the proportionate part of
8 a taxpayer's net worth or entire net income used to determine a
9 measure of its tax under this act.

10 (c) "Corporation" shall mean any corporation, joint-stock com-
11 pany or association and any business conducted by a trustee or
12 trustees wherein interest or ownership is ***[evidence]*** **evidenced**
13 by a certificate of interest or ownership or similar written instru-
13A ment.

14 (d) "Net worth" shall mean the aggregate of the values dis-
15 closed by the books of the corporation for (1) issued and outstand-
16 ing capital stock, (2) paid-in or capital surplus, (3) earned surplus
17 and undivided profits, and (4) surplus reserves which can reason-
18 ably be expected to accrue to holders or owners of equitable shares,
19 not including reasonable valuation reserves, such as reserves for
20 depreciation or obsolescence or depletion. Notwithstanding the
21 foregoing, net worth shall not include any deduction for the amount
22 of the excess depreciation described in paragraph (2) (F) of sub-

EXPLANATION—Matter enclosed in bold-faced brackets [thus] in the above bill is not enacted and is intended to be omitted in the law.

Matter printed in italics *thus* is new matter.

Matter enclosed in asterisks or stars has been adopted as follows:

*—Senate committee amendments adopted September 13, 1984.

**—Senate amendments adopted in accordance with Governor's recommendations November 18, 1985.

23 section (k) of this section. The foregoing aggregate of values shall
 24 be reduced by 50% of the amount disclosed by the books of the
 25 corporation for investment in the capital stock of one or more sub-
 26 sidiaries, which investment is defined as ownership (1) of at least
 27 80% of the total combined voting power of all classes of stock of
 28 the subsidiary entitled to vote and (2) of at least 80% of the total
 29 number of shares of all other classes of stock except nonvoting
 30 stock which is limited and preferred as to dividends. In the case of
 31 investment in an entity organized under the laws of a foreign coun-
 32 try, the foregoing requisite degree of ownership shall effect a like
 33 reduction of such investment from net worth of the taxpayer, if
 34 the foreign entity is considered a corporation for any purpose under
 35 the United States federal income tax laws, such as (but not by way
 36 of sole examples) for the purpose of supplying ***[deemed-paid]***
 37 **deemed paid** foreign tax credits or for the purpose of status as
 38 a controlled foreign corporation. In calculating the net worth of a
 39 taxpayer entitled to reduction for investment in subsidiaries, the
 40 amount of liabilities of the taxpayer shall be reduced by such
 41 proportion of the liabilities as corresponds to the ratio which the
 42 excluded portion of the subsidiary values bears to the total assets
 42A of the taxpayer.

42B **In the case of banking corporations which have international*
 42C *banking facilities as defined in subsection (n), the foregoing aggre-*
 42D *gate of values shall also be reduced by retained earnings of the*
 42E *international banking facility. Retained earnings means the earn-*
 42F *ings accumulated over the life of such facility and shall not include*
 42G *the pro rata share of dividends paid and federal income taxes paid*
 42H *or payable during the tax year.**

43 If in the opinion of the commissioner, the corporation's books
 44 do not disclose fair valuations the commissioner may make a rea-
 45 sonable determination of the net worth which, in his opinion, would
 46 reflect the fair value of the assets, exclusive of subsidiary invest-
 47 ments as defined aforesaid, carried on the books of the corporation,
 48 in accordance with sound accounting principles, and such determi-
 49 nation shall be used as net worth for the purpose of this act.

50 (e) "Indebtedness owing directly or indirectly" shall include,
 51 without limitation thereto, all indebtedness owing to any stock-
 52 holder or shareholder and to members of his immediate family
 53 where a stockholder and members of his immediate family together
 54 or in the aggregate own 10% or more of the aggregate outstanding
 55 shares of the taxpayer's capital stock of all classes.

56 (f) "Investment company" shall mean any corporation whose
 57 business during the period covered by its report consisted, to the

58 extent of at least 90% thereof of holding, investing and reinvesting
59 in stocks, bonds, notes, mortgages, debentures, patents, patent
60 rights and other securities for its own account, but this shall not
61 include any corporation which: (1) is a merchant or a dealer of
62 stocks, bonds and other securities, regularly engaged in buying the
63 same and selling the same to customers; or (2) had less than 90%
64 of its average gross assets in New Jersey, at cost, invested in
65 stocks, bonds, debentures, mortgages, notes, patents, patent rights
66 or other securities or consisting of cash on deposit during the period
67 covered by its report *;* or (3) is a banking corporation or a
68 financial business corporation as defined in the Corporation
69 Business Tax Act.

70 (g) "Regulated investment company" shall mean any corpora-
71 tion which for a period covered by its report, is registered and
72 regulated under the Investment Company Act of 1940 (54 Stat.
73 789), as amended.

74 (h) "Taxpayer" shall mean any corporation required to report
75 or to pay taxes, interest or penalties under this act.

76 (i) "Fiscal year" shall mean an accounting period ending on
77 any day other than the last day of December on the basis of which
78 the taxpayer is required to report for federal income tax purposes.

79 (j) Except as herein provided, "privilege period" shall mean
80 the calendar or fiscal accounting period for which a tax is payable
81 under this act.

82 (k) "Entire net income" shall mean total net income from all
83 sources, whether within or without the United States, and shall
84 include the gain derived from the employment of capital or labor,
85 or from both combined, as well as profit gained through a sale or
86 conversion of capital assets. For the purpose of this act, the
87 amount of a taxpayer's entire net income shall be deemed prima
88 facie to be equal in amount to the taxable income, before net
89 operating loss deduction and special deductions, which the taxpayer
90 is required to report to the United States Treasury Department
91 for the purpose of computing its federal income tax; provided,
92 however, that in the determination of such entire net income,

93 (1) Entire net income shall exclude 100% of dividends which
94 were included in computing such taxable income for federal income
95 tax purposes, paid to the taxpayer by one or more subsidiaries
96 owned by the taxpayer to the extent of the 80% or more owner-
97 ship of investment described in subsection (d) of this section. With
98 respect to other dividends, entire net income shall not include 50%
99 of the total included in computing such taxable income for federal
100 income tax purposes. Entire net income shall exclude for the

101 periods set forth in paragraph (2) (F) (i) of this subsection, any
 102 amount, except with respect to property described in section [168
 103 (f) (8) (D) (iii)] *168 (f) (8) (D) (v)* of the Internal Revenue Code
 104 **as in effect immediately prior to January 1, 1984**, which is
 105 included in a taxpayer's federal taxable income solely as a result of
 106 an election made pursuant to the provisions of paragraph (8) of
 106A that section.

107 (2) Entire net income shall be determined without the exclusion,
 108 deduction or credit of:

109 (A) The amount of any specific exemption or credit allowed in
 110 any law of the United States imposing any tax on or measured by
 111 the income of corporations;

112 (B) Any part of any income from dividends or interest on any
 113 kind of stock, securities or indebtedness, except as provided in
 114 subsection (k) (1) of this section;

115 (C) Taxes paid or accrued to the United States on or measured
 116 by profits or income, or the tax imposed by this act, or any tax
 117 paid or accrued with respect to subsidiary dividends excluded from
 118 entire net income as provided in subsection (k) (1) of this section;

119 (D) Net operating losses sustained during any year or period
 120 other than that covered by the report;

121 (E) 90% of interest on indebtedness owing directly or indirectly
 122 to holders of 10% or more of the aggregate outstanding shares of
 123 the taxpayer's capital stock of all classes; except that such interest
 124 may, in any event, be deducted

125 (i) Up to an amount not exceeding \$1,000.00;

126 (ii) In full to the extent that it relates to bonds or other
 127 evidences of indebtedness issued, with stock, pursuant to a
 128 bona fide plan of reorganization, to persons, who, prior to
 129 such reorganization, were bona fide creditors of the corpora-
 130 tion or its predecessors, but were not stockholders or share-
 131 holders thereof;

132 (iii) In full to the extent that it relates to debt of a financial
 133 business corporation owed to an affiliate corporation; provided
 134 that such interest rate does not exceed 2% over prime rate;
 135 the prime rate to be determined by the Commissioner of
 136 Banking;

137 (iv) In full to the extent that it relates to financing of motor
 138 vehicle inventory held for sale to customers providing said
 139 indebtedness is owed to a taxpayer customarily and routinely
 140 providing this type of financing;

141 (v) In full to the extent it relates to debt of a banking
 142 corporation to a bank holding company, [as defined in 12 U.S.C.

143 § 1841,] of which the banking corporation is a subsidiary, or
 144 to a debt of a banking corporation to another banking corpo-
 145 ration **with respect to federal funds transactions governed
 146 by Section 23A of the Federal Reserve Act, (12 U.S.C.
 147 § 371c.)** when both banking corporations are subsidiaries of
 147A the same bank holding **[corporation. A bank holding corpo-
 147B ration is a corporation]** ** company, as** defined in 12 U.S.C.
 147C § 1841.

148 (F) (i) The amount by which depreciation reported to the
 149 United States Treasury Department for property placed in service
 150 on and after January 1, 1981, for purposes of computing federal
 151 taxable income in accordance with section 168 of the Internal
 152 Revenue Code in effect after December 31, 1980, exceeds the amount
 153 of depreciation determined in accordance with the Internal Revenue
 154 Code provisions in effect prior to January 1, 1981, but only with
 155 respect to a taxpayer's accounting period ending after December
 156 31, 1981; provided, however, that where a taxpayer's accounting
 157 period begins in 1981 and ends in 1982, no modification shall be
 158 required with respect to this paragraph (F) for the report filed for
 159 such period with respect to property placed in service during that
 160 part of the accounting period which occurs in 1981.

161 (ii) For the periods set forth in subparagraph (F) (i) of this
 162 subsection, any amount, except with respect to property described
 163 in section [168 (f) (8) (D) (iii)] 168 (f) (8) (D) (v) of the
 164 Internal Revenue Code *as in effect immediately prior to January 1,
 165 1984*, which the taxpayer claimed as a deduction in computing
 166 federal income tax pursuant to a qualified lease agreement under
 166A paragraph (8) of that section.

167 The director shall promulgate rules and regulations necessary to
 168 carry out the provisions of this section, which rules shall provide,
 169 among others, the manner in which the remaining life of property
 170 shall be reported.

171 (3) The commissioner may, whenever necessary to properly
 172 reflect the entire net income of any taxpayer, determine the year or
 173 period in which any item of income or deduction shall be included,
 174 without being limited to the method of accounting employed by
 175 the taxpayer.

176 *(4) There shall be allowed as a deduction from entire net income
 177 of a banking corporation, to the extent not deductible in deter-
 178 mining federal taxable income, the eligible net income of an inter-
 179 national banking facility determined as follows:

180 (A) The eligible net income of an international banking facility
 181 shall be the amount remaining after subtracting from the eligible
 182 gross income the applicable expenses;

183 (B) *Eligible gross income shall be the gross income derived by*
 184 *an international banking facility, which shall include, but not be*
 185 *limited to, gross income derived from:*

186 (i) *Making, arranging for, placing or carrying loans to*
 187 *foreign persons, provided, however, that in the case of a foreign*
 188 *person which is an individual, or which is a foreign branch of*
 189 *a domestic corporation (other than a bank), or which is a*
 190 *foreign corporation or foreign partnership which is controlled,*
 191 *by one or more domestic corporations (other than banks),*
 192 *domestic partnerships or resident individuals, all the proceeds*
 193 *of the loan are for use outside of the United States;*

194 (ii) *Making or placing deposits with foreign persons which*
 195 *are banks or foreign branches of banks (including foreign sub-*
 196 *subsidiaries) or foreign branches of the taxpayers or with other*
 197 *international banking facilities; or*

198 (iii) *Entering into foreign exchange trading or hedging*
 199 *transactions related to any of the transactions described in this*
 200 *paragraph;*

201 (iv) *Such other activities of an international banking facil-*
 202 *ity may, from time to time, be authorized to engage in;*

203 (C) *Applicable expenses shall be any expense or other deduc-*
 204 *tions attributable, directly or indirectly, to the eligible gross*
 205 *income described in paragraph (B) of this subsection.**

206 (1) "Real estate investment trust" shall mean any unincorpo-
 207 rated trust or unincorporated association qualifying and electing
 208 to be taxed as a real estate investment trust under federal law.

209 (m) "Financial business corporation" shall mean any corporate
 210 enterprise which is (1) in substantial competition with the business
 211 of national banks and which (2) employs moneyed capital with the
 212 object of making profit by its use as money, through discounting and
 213 negotiating promissory notes, drafts, bills of exchange and other
 214 evidences of debt; buying and selling exchange; making of or deal-
 215 ing in secured or unsecured loans and discounts; dealing in securi-
 216 ties and shares of corporate stock by purchasing and selling such
 217 securities and stock without recourse, solely upon the order and for
 218 the account of customers; or investing and reinvesting in market-
 219 able obligations evidencing indebtedness of any person, copartner-
 220 ship, association or corporation in the form of bonds, notes or de-
 221 bentures commonly known as investment securities; or dealing in or
 222 underwriting obligations of the United States, any state or any
 223 political subdivision thereof, or of a corporate instrumentality of
 224 any of them. This shall include, without limitation of the foregoing,
 225 business commonly known as industrial banks, dealers in commer-

226 cial paper and acceptances, sales finance, personal finance, small
 227 loan and mortgage financing businesses, as well as any other enter-
 228 prise employing moneyed capital coming into competition with the
 229 business of national banks; provided, that the holding of bonds,
 230 notes, or other evidence of indebtedness by individual persons not
 231 employed or engaged in the banking or investment business and
 232 representing merely personal investments not made in competition
 233 with the business of national banks, shall not be deemed financial
 234 business. Nor shall "financial business" include national banks,
 235 production credit associations organized under the Farm Credit
 236 Act of 1933 *or the Farm Credit Act of 1971, Pub. L. 92-181
 237 (12 U. S. C. § 2091 et seq.)*, stock and mutual insurance companies
 238 duly authorized to transact business in this State, security brokers
 239 or dealers or investment companies or bankers not employing
 240 moneyed capital coming into competition with the business of
 241 national banks, real estate investment trusts, or any of the following
 242 entities organized under the laws of this State: credit unions,
 243 savings banks, savings and loan and building and loan associations,
 244 pawnbrokers, and State banks and trust companies.

245 *(n) "International banking facility" shall mean a set of asset
 246 and liability accounts segregated on the books and records of a
 247 depository institution, United States branch or agency of a foreign
 248 bank, or an Edge or Agreement Corporation that includes only
 249 international banking facility time deposits and international
 250 banking facility extensions of credit as such terms are defined in
 251 section 204.8(a)(2) and section 204.8(a)(3) of Regulation D of the
 252 board of governors of the Federal Reserve System, 12 CFR Part
 253 204, effective December 3, 1981. In the event that the United States
 254 enacts a law, or the board of governors of the Federal Reserve Sys-
 255 tem adopts a regulation which amends the present definition of
 256 international banking facility or of such facilities' time deposits or
 257 extensions of credit, the Commissioner of Banking shall forthwith
 258 adopt regulations defining such terms in the same manner as such
 259 terms are set forth in the laws of the United States or the regula-
 260 tions of the board of governors of the Federal Reserve System. The
 261 regulations of the Commissioner of Banking shall thereafter pro-
 262 vide the applicable definitions.*

1 2. This act shall take effect immediately *and shall be applicable
 2 with respect to accounting or privilege periods beginning on or
 3 after January 1, 1985*.

195 business commonly known as industrial banks, dealers in commer-
 196 cial paper and acceptances, sales finance, personal finance, small
 197 loan and mortgage financing businesses, as well as any other enter-
 198 prise employing moneyed capital coming into competition with the
 199 business of national banks; provided, that the holding of bonds,
 200 notes, or other evidences of indebtedness by individual persons not
 201 employed or engaged in the banking or investment business and
 202 representing merely personal investments not made in competition
 203 with the business of national banks, shall not be deemed financial
 204 business. Nor shall "financial business" include national banks,
 205 production credit associations organized under the Farm Credit
 206 Act of 1933, stock and mutual insurance companies duly autho-
 207 rized to transact business in this State, security brokers or dealers
 208 or investment companies or bankers not employing moneyed capital
 209 coming into competition with the business of national banks, real
 210 estate investment trusts, or any of the following entities organized
 211 under the laws of this State: credit unions, savings banks, savings
 212 and loan and building and loan associations, pawnbrokers, and
 213 State banks and trust companies.

- 1 2. This act shall take effect immediately.

STATEMENT

The purpose of this bill is to amend the Corporation Business Tax to exclude from taxation the debt of a banking corporation to another banking corporation when both corporations are subsidiaries of the *same* bankholding corporation in New Jersey. The bill is a logical extension of present State law which permits an exclusion of debt of a subsidiary banking corporation to its bank holding corporation.

Section 23A of the Federal Reserve Act was recently amended to allow banking corporations which are part of a consolidated group to buy and sell Federal Funds among themselves. The change permits New Jersey banks to buy and sell Federal Funds among themselves instead of requiring that they buy and sell such funds with other banks in New Jersey or another state. This bill would allow New Jersey based banking corporations to take advantage of the provisions of the federal law.

545(1985)

ASSEMBLY REVENUE, FINANCE AND APPROPRIATIONS
COMMITTEE

STATEMENT TO
SENATE, No. 45

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STATE OF NEW JERSEY

DATED: DECEMBER 13, 1984

PROVISIONS:

Senate Bill No. 45 (OCR) provides for an amendment to the Corporation Business Tax Act for the exclusion of interest on the indebtedness of a banking corporation to another banking corporation when both are subsidiaries of the same bank holding corporation in New Jersey.

BACKGROUND:

The current tax law permits an exclusion of interest on debt of a subsidiary banking corporation to its parent bank holding corporation but not between subsidiary corporations of the same parent.

FISCAL IMPACT:

Any cost estimate would be dependent upon the amount of business indebtedness between the subsidiaries and the applicable tax liability to the exclusion. There is no detailed information available on this concern.

The committee favorably reports this bill.

SENATE REVENUE, FINANCE AND APPROPRIATIONS
COMMITTEE

STATEMENT TO
SENATE, No. 45
with committee amendments

STATE OF NEW JERSEY

DATED: SEPTEMBER 13, 1984

Senate Bill No. 45 amends the Corporation Business Tax Act to exclude from taxation interest on the indebtedness of a banking corporation to another banking corporation when both corporations are subsidiaries of the same bankholding corporation in New Jersey. The bill extends present State law which permits an exclusion of interest on debt of a subsidiary banking corporation to its parent bankholding corporation.

COMMITTEE AMENDMENTS

The committee amended the bill to apply to tax accounting periods beginning on or after January 1, 1985. The bill was also amended to incorporate the previously enacted provisions of P. L. 1983, c. 422, pertaining to international banking facilities.

STATE OF NEW JERSEY
EXECUTIVE DEPARTMENT

February 23, 1985

SENATE BILL NO. 45 (OCR)

To the Senate:

Pursuant to Article V, Section 1, Paragraph 14 of the Constitution, I herewith return Senate Bill No. 45 (OCR) with my recommendations for reconsideration.

Senate Bill No. 45 (OCR) amends the definition of "entire net income" within the Corporation Business Tax Act to exempt from taxation the interest on indebtedness of a banking corporation to another banking corporation where both banking corporations are subsidiaries of the same bank holding corporation. The purpose of the bill is to enable banking corporations which are part of a consolidated group to take advantage of a recent amendment to Section 23A of the Federal Reserve Act.

The recent amendment to the Federal Reserve Act concerns the trading of Federal Funds. Federal Funds are reserves each member bank maintains at its regional Federal Reserve Bank. A bank with excess reserves can sell the excess to a bank with deficit reserves at an agreed upon interest rate. By allowing banking corporations within a consolidated group to engage in these transactions, they may control the interest rate charged. This results in a cost-savings to the borrower bank. By exempting the interest expense of such transactions to borrower banking corporations, Senate Bill No. 45 (OCR) will make Federal Funds transactions economically worthwhile for banking corporations within a consolidated group.

I must return Senate Bill No. 45 (OCR) to you with my recommendations for amendment for two reasons:

I am concerned that the enactment of Senate Bill No. 45 (OCR) will give subsidiary banking corporations a tax benefit that other corporate subsidiaries do not enjoy. Current case law exempts the interest on all intersubsidiary corporate debts that arise independently of the parent corporation. Current statutory law specifically exempts the interest on a debt owed by a subsidiary banking corporation directly to its parent bank holding corporation. The Division of Taxation, Department of the Treasury, advises that Senate Bill No. 45 (OCR) could be interpreted as also exempting the interest on debts between subsidiary banking corporations that are indirectly owed to the parent bank

STATE OF NEW JERSEY
EXECUTIVE DEPARTMENT

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holding corporation. As such, Senate Bill No. 45 (OCR) would represent an inadvertent extension of current law for subsidiary banking corporations, despite the fact that current statutory law exempts the interest on a debt owed by a subsidiary banking corporation directly to its parent bank holding corporation.

I recommend that Senate Bill No. 45 (OCR) be amended to limit its application to Federal Funds transactions. This amendment will ensure that subsidiary banking corporations will not receive a tax benefit that other corporate subsidiaries do not receive. Significantly, the amendment will coincide with the purpose of the bill as it will allow banking corporations to take advantage of the recent amendment to the Federal Reserve Act regarding Federal Funds transactions. In making this recommendation, it is not my intent to treat subsidiary banking corporations less favorably than other corporate subsidiaries.

I also recommend that Senate Bill No. 45 (OCR) be amended to correct a technical error in terminology. Senate Bill No. 45 (OCR) refers to a parent entity as a "bank holding corporation", as the term is defined within the Federal Bank Holding Company Act. The federal act, however, does not define the term "bank holding corporation." As such, Senate Bill No. 45 (OCR) refers to an entity that arguably does not exist.

I recommend that all reference to the term "bank holding corporation" be deleted, and that the term "bank holding company" be inserted. The latter term is defined within the federal Banking Holding Company Act and includes a bank holding corporation. This amendment will also enable Senate Bill No. 45 (OCR) to conform to current law.

Accordingly, for the aforementioned reasons, I herewith return Senate Bill No. 45 (OCR) and recommend that it be amended as follows:

Page 5, Section 1, Line 145: After "ration" insert "with respect to federal funds transactions governed by Section 23A of the Federal Reserve Act, (12 U.S.C. §371c.)"

STATE OF NEW JERSEY
EXECUTIVE DEPARTMENT

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Page 5, Section 1, Line 146-147: After "same bank holding" delete
"corporation. A bank holding corporation is a corporation" insert "company,
as"

Respectfully,
/s/ Thomas H. Kean
GOVERNOR

[seal]

Attest:
/s/ W. Cary Edwards
Chief Counsel