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2003 HOUSE FINANCE AND TAXATION

HB 1109

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2003 HOUSE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB1109

House Finance and Taxation Committee

Conference Committee

Hearing Date January 8, 2003

Tape Number	Side A	Side B	Meter #
1	X		20

Committee Clerk Signature *Janice Stein*

Minutes:

REP. WESLEY BELTER, CHAIRMAN Called the hearing to order.

MARY LOFTSGARD, SUPERVISOR, CORPORATE INCOME TAX SECTION,

OFFICE OF THE STATE TAX COMMISSIONER, Explained the proposed bill. See attached written testimony.

REP. BELTER Asked whether the financial institutions were involved in the process of developing this legislation.

MARY LOFTSGARD No

REP. WINRICH This bill would make the treatment of financial institutions and other kinds of S-corporations consistent?

MARY LOFTSGARD Yes

REP. GROSZ Asked if it was true of all types of assets, tangible and intangible?

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House Finance and Taxation Committee
Bill/Resolution Number HB 1109
Hearing Date January 8, 2003

MARY LOFTSGARD Stated she was not that familiar with the internal revenue, she stated she would get that information back to Rep. Grosz.

REP. GROSZ Questioned the effective dates, would the proposed bill be effective for prior periods?

MARY LOFTSGARD Yes.

With no further testimony, the hearing was closed.

COMMITTEE ACTION 1-21-03, Tape #2, Side A, Meter #0.3

REP. DROYDAL Made a motion for a **DO NOT PASS**.

REP. CLARK Second the motion. **MOTION CARRIED**

13 YES 0 NO 1 ABSENT

REP. WIKENHEISER Was give the floor assignment.

FISCAL NOTE
 Requested by Legislative Council
 01/03/2003

REVISION

Bill/Resolution No.: HB 1109

1A. State fiscal effect: Identify the state fiscal effect and the fiscal effect on agency appropriations compared to funding levels and appropriations anticipated under current law.

	2001-2003 Biennium		2003-2005 Biennium		2005-2007 Biennium	
	General Fund	Other Funds	General Fund	Other Funds	General Fund	Other Funds
Revenues						
Expenditures						
Appropriations						

1B. County, city, and school district fiscal effect: Identify the fiscal effect on the appropriate political subdivision.

2001-2003 Biennium			2003-2005 Biennium			2005-2007 Biennium		
Counties	Cities	School Districts	Counties	Cities	School Districts	Counties	Cities	School Districts

2. Narrative: Identify the aspects of the measure which cause fiscal impact and include any comments relevant to your analysis.

If enacted, HB 1109 will have a very small positive fiscal impact, the amount of which cannot be determined.

3. State fiscal effect detail: For information shown under state fiscal effect in 1A, please:

A. Revenues: Explain the revenue amounts. Provide detail, when appropriate, for each revenue type and fund affected and any amounts included in the executive budget.

B. Expenditures: Explain the expenditure amounts. Provide detail, when appropriate, for each agency, line item, and fund affected and the number of FTE positions affected.

C. Appropriations: Explain the appropriation amounts. Provide detail, when appropriate, of the effect on the biennial appropriation for each agency and fund affected and any amounts included in the executive budget. Indicate the relationship between the amounts shown for expenditures and appropriations.

Name:	Kathryn L. Strombeck	Agency:	Tax Dept.
Phone Number:	328-3402	Date Prepared:	01/03/2003

Kalosta Rickford
 Operator's Signature

10/2/03
 Date

FISCAL NOTE
 Requested by Legislative Council
 01/02/2003

Bill/Resolution No.: HB 1109

1A. State fiscal effect: Identify the state fiscal effect and the fiscal effect on agency appropriations compared to funding levels and appropriations anticipated under current law.

	2001-2003 Biennium		2003-2005 Biennium		2005-2007 Biennium	
	General Fund	Other Funds	General Fund	Other Funds	General Fund	Other Funds
Revenues						
Expenditures						
Appropriations						

1B. County, city, and school district fiscal effect: Identify the fiscal effect on the appropriate political subdivision.

2001-2003 Biennium			2003-2005 Biennium			2005-2007 Biennium		
Counties	Cities	School Districts	Counties	Cities	School Districts	Counties	Cities	School Districts

2. Narrative: Identify the aspects of the measure which cause fiscal impact and include any comments relevant to your analysis.

3. State fiscal effect detail: For information shown under state fiscal effect in 1A, please:

A. Revenues: Explain the revenue amounts. Provide detail, when appropriate, for each revenue type and fund affected and any amounts included in the executive budget.

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C. Appropriations: Explain the appropriation amounts. Provide detail, when appropriate, of the effect on the biennial appropriation for each agency and fund affected and any amounts included in the executive budget. Indicate the relationship between the amounts shown for expenditures and appropriations.

Name:	Kathryn L. Strombeck	Agency:	Tax Dept.
Phone Number:	328-3402	Date Prepared:	01/03/2003

Kathryn L. Strombeck
 Operator's Signature

10/2/03
 Date

Date: 1-21-03
Roll Call Vote #: 1

2003 HOUSE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. HB 1109

House FINANCE & TAXATION Committee

Check here for Conference Committee

Legislative Council Amendment Number _____

Action Taken Do Not Pass

Motion Made By Rep. Drovdal Seconded By Rep. Clark

Representatives	Yes	No	Representatives	Yes	No
BELTER, CHAIRMAN	✓				
DROVDAL, VICE-CHAIR	✓				
CLARK	✓				
FROELICH	✓				
GROSZ	✓				
HEADLAND	✓				
IVERSON	✓				
KELSH	✓				
KLEIN	✓				
NICHOLAS	✓				
SCHMIDT	✓				
WEILER	✓				
WIKENHEISER	✓				
WINRICH	✓				

Total (Yes) 13 No 0

Absent _____

Floor Assignment Rep. Wikenheiser

If the vote is on an amendment, briefly indicate intent:

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REPORT OF STANDING COMMITTEE (410)
January 21, 2003 3:17 p.m.

Module No: HR-11-0866
Carrier: Wikenheiser
Insert LC: . Title: .

REPORT OF STANDING COMMITTEE
HB 1109: Finance and Taxation Committee (Rep. Belter, Chairman) recommends DO NOT PASS (13 YEAS, 0 NAYS, 1 ABSENT AND NOT VOTING). HB 1109 was placed on the Eleventh order on the calendar.

(2) DESK, (3) COMM

Page No. 1

HR-11-0866

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2003 TESTIMONY

HB 1109

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**TESTIMONY BEFORE THE HOUSE
FINANCE AND TAXATION COMMITTEE**

HB 1109

MARY LOFTSGARD

JANUARY 8, 2003

Chairman Belter, members of the committee, my name is Mary Loftsgard. I am the supervisor of the Corporate Income Tax Section of the Office of State Tax Commissioner, and I am here to testify in support of HB 1109.

The Tax Commissioner proposes a change to N.D.C.C. Chapter 57-35.3, the Financial Institutions Tax. House Bill 1109 creates a new subdivision to N.D.C.C. Section 57-35.3-02(1). This subdivision defines items that must be added to federal taxable income in order to determine the North Dakota taxable income of a financial institution. As you see, the bill would require financial institutions to add: "The amount of any net recognized built-in gains calculated under section 1374(d)(2) of the Internal Revenue Code"

This proposed amendment to the statute deals with a specific federal tax treatment that occurs when there is a conversion from a regular corporation (C) to a sub-chapter S-corporation (S-corporation). If the C corporation holds property that has increased in value at the time of the conversion to an S-corporation, and sells or distributes the property within 10 years of the conversion, federal tax law requires a special gain to be recognized in the year of the sale. The special gain and the associated federal tax is computed at the entity

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(S-corporation) level. The S-corporation then offsets its ordinary income by the tax computed on the gain and reports that ordinary income to the shareholders based on their respective interests in the S-corporation. That is, the tax on the gain is treated as a deductible loss passed on to the shareholder.

For North Dakota tax purposes, if the S-corporation is not a financial institution, the gain (net of federal income tax) is reported and tax is paid at the entity level by the S-corporation (North Dakota Form 60). The S-corporation shareholders then report their respective shares of North Dakota ordinary income on their North Dakota returns (individual, corporate, etc.).

For North Dakota financial institutions tax, all tax is paid at the entity level. The starting point for computing North Dakota taxable income for S-corporation financial institutions is ordinary income computed for federal tax purposes. This means that the recognized gain is not included in North Dakota taxable income. However, the S-corporation which is a financial institution enjoys the benefit of the federal tax deduction computed on that gain because the federal tax was deducted in arriving at ordinary income.

The purpose of the proposed legislation is two-fold. It will ensure that all income for which a federal tax deduction is allowed is included in North Dakota taxable income of financial institutions. The proposed legislation will also provide consistency in treatment for S-corporations that are financial institutions with those that are not.

A fiscal note has been prepared for this bill. It indicates a small, but indeterminate increase in revenue to the state.

We are not able to readily identify how many of the 288 financial institutions that file in North Dakota are S-corporations. Nor are we readily able to identify how many converted to that status from C corporation status, or, of these, how many had gains of the type in question, or the amount of the gains. There also is no way to predict how many C corporations may convert to S-corporations in the future.

The Tax Commissioner recommends a "do-pass" on HB 1109. If there are any questions, I will be glad to respond.

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