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MEMORANDUM

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TO: IBANYS Board of Directors

FROM: William Y. Crowell, III

DATE: September 16, 2011

RE: Legislative Update – Corporate Tax Reform Proposal

IBANYS, together with Brian Flynn, its tax advisor, and several Chief Financial Officers met with the New York State Department of Taxation and Finance to discuss their Corporate Tax Reform Proposal (the "Proposal"). This Proposal merges the Bank Tax and the Corporate Franchise Tax. Our goal has been to advocate for an acceptable substitute deduction for the REIT which is eliminated in their Proposal. At the same time, IBANYS has focused on making any deduction available to all banks so that members who currently do not benefit from the REIT deduction would be able to take advantage of any new deduction.

IBANYS explained the community bank business model and its positive impacts on the New York State economy. The single factor apportionment formula used in the Proposal has negative impacts on the community bank business model. Changes to the Proposal are necessary to avoid negative consequences for community banks.

IBANYS advocated for elimination of the asset test in the qualified residential loan portfolio deduction, along with inclusion of not only residential but commercial loans. With respect to the small business loan subtraction, IBANYS urged that it be expanded to include residential mortgages and also that the definition of a small business loan be increased from $1 million to $2 million.

The Department of Taxation and Finance staff advised that our suggestions would be given consideration. They expect that a determination on a final Proposal will be made in a six week period, and very soon thereafter the Governor will decide whether the Proposal should be included in the 2012-2013 State budget proposal.

A copy of talking points prepared for the meeting is attached. If there are any questions, please don't hesitate to contact me.

CORPORATE TAX REFORM PROPOSAL

TALKING POINTS

Policy Objectives

- Provide a substitute deduction to replace the current REIT deduction which is repealed by the proposal.

- Encourage local investment in New York communities consisting both of residential mortgages for homeowners and commercial loans for small businesses.

- Encourage community banks to continue to retain residential and commercial mortgage loans in their loan portfolios with dual benefit of employment created through servicing of the loan portfolio by a community bank versus sale of mortgages, and interest income earned on the portfolio represents a continuing taxable revenue stream for the State.

- The community bank business model creates investment in New York State as community banks rely solely on their market areas for investment versus regional and money center banks which are able to shift their funding within their large market areas. The community bank business model should be encouraged because it is New York centric.

The single factor apportionment formula under the corporate tax reform proposal creates a disincentive for community banks to retain residential or commercial mortgages in their portfolio because of tax consequences. This proposal encourages community banks to sell their mortgages. Community banks do not operate on this approach currently. The strength of community banks is based in part upon their due diligence in making mortgages because those mortgages are retained as investments in their portfolios.

The two options in the proposal:

1. Qualified residential loan portfolio deduction.

2. Small business loan subtraction.

Issues with Above Options

1. Qualified residential loan portfolio deduction:

    - Balance sheet requirements with the 60% asset test as a qualification for the deduction should be replaced by simple requirement banks under $8 billion in assets – the distinctions between thrifts and community commercial banks are not relevant and the statute should be modernized.

    - This proposal should be broadened to include commercial loans and not limited to residential loans only, particularly in view of need for economic development of small businesses.

- The 32% of ENI for charge-offs should be increased to provide an equivalent deduction to the REIT.

2. Small business loan subtraction:

- Residential loans should be included in this formula, particularly in view of economic situation and these loans are a critical part of community bank deposit model.

- Principal for small business loan should be increased from $1 million to $2 million to capture the majority of small business loans. This amount falls within SBA limits. It is also important to encourage development of small business by encouraging loans and an increase in amount will avoid loan splitting to achieve a deduction.

- The percentage applied to this deduction should insure a tax benefit equivalent to the REIT.