ALABAMA DEPARTMENT OF REVENUE
REVENUE RULING 97-004

This document may not be used or cited as precedent. Code of Alabama 1975, §40-2A-5(a).

TO:

SUBJECT: Treatment of Corporate Reorganization for Purposes of the Financial Institution Excise Tax, Code of Alabama 1975, §40-16-1, et seq.

DATE: April 24, 1997

FACTS

Holding Company, a Delaware corporation, Bank A, an Alabama state banking corporation, Bank B, an Alabama state banking corporation and other subsidiaries, file consolidated financial institution excise tax returns with the Alabama Department of Revenue. In addition, the Holding Company owns all of the authorized, issued and outstanding shares of the common capital stock of Bank C, Bank D and Bank E, which are chartered in three different southeastern states.

Interstate branching by merger of banks chartered in Alabama and the other three states will be permitted by Section 102 of the Riegle-Neal Interstate Banking and Branch Efficiency Act of 1994, effective on and after June 1, 1997. Additionally, the law of Alabama (Code of Alabama 1975, §5-13B-22) and the

other three states permit interstate merger of banks chartered in their respective states. Moreover, intrastate merger of banks chartered in Alabama is currently permitted by Code of Alabama 1975, §5-7A-1.

In light of such, the Holding Company and each of the banks wish to take advantage of the efficiencies in eliminating separate bank charters and operate one bank with interstate branches. To that end the Holding Company and each of the banks mentioned herein have filed an application with the Board of Governors of the Federal Reserve System to merge Bank C, Bank D, Bank E and Bank B (the "Disappearing Banks") into Bank A. A similar application has been filed with the Alabama banking department. Upon consummation of the merger, all assets of the Disappearing Banks will be owned by Bank A, which will then be known as Bank A.

Alabama imposes a financial institution excise tax under the provisions of Code of Alabama 1975, §40-16-1, et seq., on "financial institutions" doing business in Alabama. It is in lieu of the corporate income tax imposed pursuant to the provisions of Code of Alabama 1975, §40-18-1, et seq. Each of the Holding Company, Bank A and Bank B, have filed consolidated financial institution excise tax returns as permitted by §40-16-3(b).

ISSUES

1. Whether the mergers described herein, in and of themselves, will cause either Holding Company, Bank A, Bank B, or any other member of the group of financial institutions to recognize "gross income" for purposes of the financial institution excise tax.

2. Whether Bank A's basis in the assets acquired from the

Disappearing Banks will equal the basis of those entities in the assets immediately prior to the transfer to Bank A.

LAW AND ANALYSIS

Code of Alabama 1975, §40-16-4, requires every financial institution to pay to the state annually an excise tax for the privilege of engaging in this state in the business of banking and of conducting a financial institution, as such term is defined in Chapter 16 of Title 40, Code of Alabama, and of conducting a business employing moneyed capital coming into competition with the business of national banks measured by its net income for the preceding taxable year at the rate of six percent of such income.

"Financial institution" is defined in §40-16-1(1) as including any person, firm, corporation and any legal entity whatsoever doing business in this state as a national banking association, bank, banking association, trust company, industrial or other loan company or building and loan association, any other institution or person employing moneyed capital coming into competition with the business of national banks, regardless of what business form is used and whether or not incorporated and by whatsoever authority existing. The common parent corporation of a controlled group of corporations eligible to elect to file a consolidated excise tax return, in accordance with Section 40-16-3 also is considered to be a financial institution if such parent corporation is a registered bank holding company as defined by the Bank Holding Company Act of 1956, as amended. Holding Company is a "financial institution" because it is the common parent of a controlled group of corporations doing business as banks and having branches, offices, and other locations within Alabama.

"Net income" is defined under Code of Alabama 1975, §40-16-

1(2), as that income arising from the business the privilege to engage in which is taxed, computed by deducting from the gross income arising from such business, without any exclusions from or credit to such gross income, the total amount of certain deductions. However, there is no definition or explanation of the term "gross income arising from such business" in §40-16-1 through 40-16-8 Code of Alabama 1975.

As evidenced by the statutes' failure to define gross income, the financial institution excise tax statutes contain few details regarding the intended application of the tax to various situations. Accordingly, the Department of Revenue has made reference to the appropriate Alabama corporate income tax provisions to fill in such gaps.

For example, there are no less than four references to the Alabama income tax law and regulations in the Department's financial institution excise tax regulations. Specifically, i.e., Department of Revenue Regulation §810-9-1-.01(4)(d)2. provides, with respect to the deductibility of taxes, "[i]n the case of corporate taxpayers which are members of affiliated groups which file consolidated income tax returns, the deductible tax will be allocated and apportioned based on the regulations provided under the Alabama income tax law."

In addition, the Alabama Department of Revenue Administrative Law Judge sanctioned the Department's use of the income tax three-factor formula of property, payroll and sales (or gross receipts) in apportioning a foreign financial institution's income to Alabama. The Administrative Law Judge noted that "neither the financial institution excise tax statutes (Title 40, Chapter 16), nor the Department's regulations relating thereto dictate how a financial institution operating in Alabama should apportion or compute its percentage

of income earned in Alabama.... Rather, the Department as a matter of general policy requires all financial institutions to apportion net income to Alabama using the standard three-factor formula of property, payroll and sales." Navistar Financial Corporation v. State DOR, Docket No. INC. 93-249, 1994 WL 606208(Ala. Dept. of Rev.), Vol. 3, No. 1, Alabama Department of Revenue Administrative Law Quarterly, 3rd Quarter, 1994.

Clearly, both the Department and its administrative law division have made use of the Alabama corporate income tax laws and regulations in constructing and interpreting the provisions of the Alabama financial institution excise tax. As a consequence thereof, the Department should look to Alabama's income tax statutes in determining the tax consequences of the foregoing mergers.

Code of Alabama 1975, §40-18-8(g) provides in pertinent part:

> In the case of a reorganization defined in 26 U.S.C. §368 (relating to definitions applicable to corporate reorganizations) ... the amount of gain or loss recognized shall be determined in accordance with 26 U.S.C. §§354, 355, 356, 361, 371 and 374.

Internal Revenue Code ("IRC") §368(a)(1)(A) provides that "a statutory merger or consolidation" qualifies as a tax-free reorganization for federal income tax purposes.

Code of Alabama 1975, §40-18-6(a)(5) provides in pertinent part:

> . . . The basis of property acquired by a corporation in a transaction described in subsection (f) or (g) of Section 40-18-8 shall be determined in accordance with

26 U.S.C. §362.

IRC §362 provides generally that the basis in property acquired by a corporation in connection with a reorganization "shall be the same as it would be in the hands of the transferor, increased in the amount of gain recognized to the transferor on such transfer." However, special rules apply for certain contributions to capital, including money, and stock or securities in a corporation.

If the mergers of Bank C, Bank D, Bank E, and Bank B into Bank A qualify as tax-free reorganizations under IRC §368(a)(1)(A), then for Alabama corporate income tax purposes the mergers will constitute tax-free transactions which generate no taxable income for the group consisting of Holding Company, Bank A and Bank B, or any separate taxable income for any such member. The treatment of the mergers under the financial institution excise tax should follow the corporate income tax law of the state.

RULINGS

1. Assuming that the mergers qualify as tax-free reorganizations under IRC §368(a)(1)(A), the mergers described above will not, in and of themselves, cause either Holding Company, Bank A, Bank B, or any other member of the group of financial institutions to recognize "gross income" for purposes of the financial institution excise tax.

2. Bank A's basis in the assets acquired from the Disappearing Banks will be determined in accordance with IRC §362. Accordingly, the type of assets in question will determine Bank A's basis in those assets.

The Commissioner of Revenue has recused himself from issuing

this revenue ruling. In accordance with Code of Alabama 1975, §40-2-44, the Commissioner has assigned the Assistant Commissioner of Revenue the duty of issuing this ruling.

ALABAMA DEPARTMENT OF REVENUE

By: _____
GEORGE E. MINGLEDORFF III
Assistant Commissioner

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