

MINNESOTA · REVENUE

CORPORATION FRANCHISE TAX 100% Dividend Received Deduction and AMT Provisions

March 27, 2002

| | Yes | No |
|---|-----|----|
| Separate Official Fiscal Note Requested | | X |
| Fiscal Impact | | |
| DOR Administrative Costs/Savings | | X |

Department of Revenue
Analysis of H.F 3270, Art. 14, Sections
Relating to the Dividend Received Deduction,
as amended 3/21/02 by Senate

| | Revenue Gain or (Loss) | | | |
|--------------------|-------------------------------|-------------------------|-------------------------|----------------------|
| | <u>F.Y. 2002</u> | <u>F.Y. 2003</u> | <u>F.Y. 2004</u> | <u>FY2005</u> |
| | | (000's) | | |
| General Fund Total | (\$0) | (\$4,400) | (\$2,100) | (\$2,200) |

Effective retroactive taxable years beginning after December 31, 2000.

EXPLANATION OF THE BILL

Current Law: If dividends are eliminated by federal consolidation regulations a taxpayer is allowed to claim a 100% dividend received deduction. However if the payor corporation is not subject to the corporate franchise tax, the maximum deduction is 80% of dividends received. Insurance companies domiciled in retaliatory states have been exempt from the corporate tax since 1991. The rest of the insurance companies were exempted in 2001.

For the computation of the alternative minimum tax (AMT), the deductions against Minnesota alternative minimum taxable income are limited to 90% of alternative minimum taxable income. The dividend received deduction is included in the 90% limitations. The only exception to these limitations is investment companies subject to tax under M.S. 290.36.

Proposed Law: The proposed law enlarges the group of corporations that may receive a 100% dividend received deduction. To be eligible for the deduction, the dividends must be from a company that is subject to the insurance gross premium tax, and the deduction is limited by the distributions paid by the holding company to another insurance company that is subject to the insurance gross premium tax.

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In addition, the dividends must be received from “another member of the affiliated group.” Due to the meaning of federal law term “another member of the affiliated group”, the 100% deduction can be taken by holding companies that own property and casualty companies. Under federal law, a life insurance company can not be a member of an affiliated group.

In general, reinsurance companies are not subject to the gross premium tax. Because the corporation paying the dividend must be subject to the gross premium tax, in most cases dividends from a reinsurance company are ineligible to receive the 100% dividend received deduction.

The bill allows an exception to what may be included in the AMT 90% limitations on deductions against Minnesota alternative minimum taxable income. The proposal allows the 90% limitations to be exceeded provided that the dividends were received from an insurance company that is subject to the gross premium tax.

The bill amends the definition of income used to calculate income for insurance regulatory purposes. It is unclear how the change in M.S. 60D will effect the calculation of income for franchise tax purposes.

REVENUE ANALYSIS DETAIL

- Banking and insurance companies are merging together to form very large financial services companies. This analysis is based on historical tax returns information recomputed under current law for AMT liabilities, and it assumes that a small number of holding companies will be able to make use of the expanded definition of the dividend received deduction and the lack of 90% limitations under the AMT.
- Due to the retroactive effective date, the revenue impact for F.Y. 2003 includes revenue losses from calendar years 2001, 2002 and part of 2003.

Number of Taxpayers Affected:

A small number of insurance holding companies.

ADMINISTRATIVE/OPERATIONAL IMPACT

There will be no significant administrative or operational costs or savings to DOR in administration of this bill.

Source: Minnesota Department of Revenue
Tax Research Division
<http://www.taxes.state.mn.us/polic.html#analyses>