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Route to: ☐ _____ ☐ _____ ☐ _____ ☐ _____
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Taxation of Financial Institutions—Second Edition

Publication 752

Release 69

November 2018

HIGHLIGHTS

RELEASE 69 IN BRIEF:

- This publication has been updated by KPMG LLP to keep the reader abreast of recent federal court decisions, income tax regulations, and IRS rulings affecting the taxation of financial institutions.

NOTE TO PRACTITIONERS: You can obtain a free PDF copy of our analysis of *The Tax Cuts & Jobs Act of 2017* [Public Law Number 115-97] via the LexisNexis Store at www.lexisnexis.com/store. It is an explanation of President Trump's tax legislation. Also in the LexisNexis Store are articles written by expert tax authors for LexisNexis offering personal commentary and insights into the new legislation.

History, Overview, and Definitions — Banks and Thrifts — Economic Growth, Regulatory Relief, and Consumer Protection Act. The Economic Growth, Regulatory Relief, and Consumer Protection Act (ERC) was signed into law on May 24, 2018 and amends the Dodd-Frank Act and

has far-reaching implications on the banking industry. *See* § 1.14.

Accounting Methods. Accounting method changes required to be filed under the automatic consent procedures are set forth in Revenue Procedure 2018-31 (which replaces Revenue Procedure 2017-30). *See* § 2.02, 2.03 and 2.06.

Accounting Methods — General Accounting Methods — Accrual Method. Public Law 115-97 set forth revisions to IRC Section 451 for tax years beginning after December 31, 2017. Until further guidance is issued, Notice 2018-35 provides that taxpayers may continue to rely on Revenue Procedure 2004-34 for the treatment of advance payments. *See* § 2.02[4].

Accounting Periods — Internal Revenue Code Requirements. Inclusion of Revenue Procedure 2018-17. *See* § 3.03[2].

Debt Instruments — Interest, OID, and Significant Modifications — Determination of OID — Qualified Stated Interest Accrual. Average annual gross

receipts was raised from \$5 million to \$25 million over 3 year period for purposes of determining eligibility to utilize cash method of accounting. *See* § 4.03[3].

Debt Instruments — Interest, OID, and Significant Modifications — Debt Instruments With Principal That is Subject to Acceleration — Loan Pools and the (a)(6) Method. For tax years beginning after December 31, 2018, interchange fees and merchant discount are required to be included in income under IRC Section 451. *See* § 4.07[4].

Debt Instruments — Interest, OID, and Significant Modifications — Tax Cuts and Jobs Act of 2017 and IRC Section 163(j) and the Limit on the Deduction for Business Interest. Notice 2018-28 addresses treatment of interest expense, interest income and business interest limitation for corporate taxpayers. *See* § 4.13[1].

Securities Investment and Derivative Transactions — Forward Contracts and IRC Section 1256 Contracts — IRC Section 1256 Contracts — Exceptions to IRC Section 1256 — IRC Section 988 Transactions. Proposed Regulation § 1.988-7 would provide an election for a taxpayer to use a mark-to-market method of accounting for foreign currency gain or loss attributable to IRC Section 988 Transactions. *See* § 5.04[2][d][ii].

Securities Investment and Derivative Transactions — Notional Principal Contracts — Timing Rules — Nonperiodic Payments — Noncontingent Nonperiodic Payments. Removal of discussion regarding Treasury Regulation § 1.446-3T(g)(4). *See* § 5.06[3][c][ii].

Municipal Obligations — Mortgage Revenue Bonds — Bonds Generally Issued After August 15, 1986. Inclusion of Revenue Procedure 2018-23 and 2018-33.

See § 6.08.

Leases — Introduction. Effective date of current rules and developments. *See* § 10.01.

Financial Institutions as Securities Dealers — Change in Method of Accounting — Change to Non-Dealer. Inclusion of Revenue Procedure 2018-31 which replaces Revenue Procedure 2017-30. *See* § 12.07[2] and § 12.10[1] and [2].

Net Investment Income — Final and Proposed Regulations — CFCs and PFICs. Public Law 115-97 provides for IRC Section 965(a) which addresses treatment of deferred foreign income as Subpart F income. *See* § 17.06[6].

International Taxation of U.S. Banks — Choice of Entity — Controlled Foreign Corporation (CFC) — Overview of Subpart F. Addition of new IRC Section 951A which requires a U.S. shareholder of a CFC to include in income its “global intangible low-taxed income” (“GILTI”) in a manner similar to Subpart F income. *See* § 20.02[2][a].

International Taxation of U.S. Banks — Choice of Entity — Foreign Currency Translation — Foreign Branches. Issued on June 13, 2018, Notice 2018-57 delays the applicability of the new 987 regulations by two years. *See* § 20.02[4][a].

International Taxation of U.S. Banks — Other Developments — Public Law 115-97: The Tax Cuts and Jobs Act — Limitations on the Deduction of Net Business Interest Expense. Issued on April 16, 2018, Notice 2018-28 provided important clarifications with respect to the application of IRC Section 163(j). *See* § 20.09[4][b].

International Taxation of U.S. Banks — Other Developments — Public Law 115-97: The Tax Cuts and Jobs Act —

Rules Related to Passive and Mobile Income — Global Intangible Low-Tax Income. Brief discussion of Revenue Procedure 2018-17 as it relates to Specified Foreign Corporations (SFC) with a December 31 year end. *See* § 20.09[4][d][i].

Information Reporting and Backup Withholding — Information Reporting — Certain Life Insurance Contracts. Addition of IRC Section 6050Y related to new information reporting requirements associated with certain life insurance contract transactions. *See* § 21.01[2][n].

Information Reporting and Backup Withholding — Tax Shelter Disclosures and Disclosures by Material Advisors. Requirements related to Form 8886, Reportable Transaction Disclosure Statement. *See* § 21.05.

State Taxation of Financial Institutions — Nexus — History of Nexus Standards — Physical Presence Requirement Overturned. U.S. Supreme Court decided in favor of the State in *South Dakota v. Wayfair, Inc.* overruling the long-standing rule that an out-of-state seller must have a physical presence in a state before the state can require the seller to collect sales and use taxes. *See* § 24.02[5].

State Taxation of Financial Institutions — Nexus — Sales and Use Tax Nexus Developments — Economic Nexus. Several states have adopted economic nexus standards applicable to sales and use taxes. *See* § 24.05[5].

Sales and Use Taxes — Introduction — Sales and Use Tax Nexus. Physical presence nexus standard may no longer be relied on resulting in many taxpayers to be required to collect sales or use taxes in states where they have not historically collected. *See* § 27.01[2].

Financial Institutions as S Corporations — S Corporation Considerations — Advantages of S Corporation Status. An S corporation may possibly continue to use the cash method of accounting even when gross receipts exceed \$25 million dollars (\$5 million for tax years beginning prior to January 1, 2018). *See* § 29.02[2].

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Publication 752 Release 69

November 2018

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Revision

<input type="checkbox"/>	Title page.	Title page
<input type="checkbox"/>	1-27 thru 1-33	1-27 thru 1-33
<input type="checkbox"/>	2-13 thru 2-21	2-13 thru 2-21
<input type="checkbox"/>	2-31 thru 2-32.1.	2-31 thru 2-32.1
<input type="checkbox"/>	2-43 thru 2-46.1.	2-43 thru 2-46.1
<input type="checkbox"/>	2-91 thru 2-103	2-91 thru 2-103
<input type="checkbox"/>	3-7.	3-7 thru 3-8.1
<input type="checkbox"/>	4-4.1 thru 4-15	4-5 thru 4-16.1
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<input type="checkbox"/>	4-39 thru 4-40.1.	4-39 thru 4-40.1
<input type="checkbox"/>	4-71 thru 4-75	4-71 thru 4-76.1
<input type="checkbox"/>	4-91 thru 4-95	4-91 thru 4-95
<input type="checkbox"/>	4-107.	4-107
<input type="checkbox"/>	4-117 thru 4-119	4-117 thru 4-119
<input type="checkbox"/>	5-24.1 thru 5-25.	5-25 thru 5-26.1
<input type="checkbox"/>	5-39 thru 5-41	5-39 thru 5-41
<input type="checkbox"/>	6-35 thru 6-36.1.	6-35 thru 6-36.1
<input type="checkbox"/>	9-1 thru 9-39	9-1 thru 9-39
<input type="checkbox"/>	10-1 thru 10-7	10-1 thru 10-8.1
<input type="checkbox"/>	12-21 thru 12-33	12-21 thru 12-33
<input type="checkbox"/>	15-5 thru 15-21	15-5 thru 15-22.1
<input type="checkbox"/>	15-31 thru 15-41	15-31 thru 15-42.1
<input type="checkbox"/>	15-51 thru 15-53	15-51 thru 15-54.1
<input type="checkbox"/>	15-65 thru 15-75	15-65 thru 15-75
<input type="checkbox"/>	17-1 thru 17-15	17-1 thru 17-17

VOLUME 2

Revision

<input type="checkbox"/>	Title page.	Title page
<input type="checkbox"/>	20-15 thru 20-19	20-15 thru 20-20.1
<input type="checkbox"/>	20-33.	20-33
<input type="checkbox"/>	20-86.1 thru 20-91	20-87 thru 20-92.1
<input type="checkbox"/>	20-109 thru 20-113	20-109 thru 20-114.1
<input type="checkbox"/>	21-1 thru 21-3	21-1 thru 21-3
<input type="checkbox"/>	21-34.1.	21-34.1 thru 21-34.3
<input type="checkbox"/>	21-43.	21-43 thru 21-44.1
<input type="checkbox"/>	21-67 thru 21-73	21-67 thru 21-73
<input type="checkbox"/>	24-1 thru 24-19	24-1 thru 24-19

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<input type="checkbox"/>	27-1 thru 27-3	27-1 thru 27-4.1
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<input type="checkbox"/>	29-23.	29-23
<input type="checkbox"/>	29-43 thru 29-57	29-43 thru 29-57
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<input type="checkbox"/>	TS-1 thru TS-59	TS-1 thru TS-61
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