

Stradley Ronon Stevens & Young, LLP
2005 Market Street
Suite 2600
Philadelphia, PA 19103-7018
215.564.8000 Telephone
215.564.8120 Facsimile
www.stradley.com

With other offices in:
Washington, D.C.
New York
New Jersey
Illinois
Delaware



www.meritas.org

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IRS Proposes Stepped-Up Basis Rule for Educational Institutions Subject to 1.4 Percent Excise Tax

The Department of the Treasury (the Treasury Department) and the IRS announced in Notice 2018-55 (<https://www.irs.gov/pub/irs-drop/n-18-55.pdf>) that they intend to issue proposed regulations providing clarification regarding the calculation of net investment income for purposes of Section 4968(c). (Section references are to the Internal Revenue Code of 1986, as amended.) Similar to the rules found in Section 4940(c) (which provides for an excise tax on private foundations), the Treasury Department and the IRS intend to propose regulations stating that, in the case of property held by an applicable educational institution on Dec. 31, 2017, and continuously thereafter to the date of its disposition, basis of such property for determining gain shall be deemed to be not less than the fair market value of such property on Dec. 31, 2017, plus or minus all adjustments after Dec. 31, 2017, and before the date of disposition consistent with the regulations under Section 4940(c). In addition, for purposes of determining loss, basis rules that are consistent with the regulations under Section 4940(c) will apply.

Emailed Advice Concludes Mitigation May Apply to Allow Taxpayers to Carryback NOLs

In emailed advice (<https://www.irs.gov/pub/irs-wd/201823004.pdf>), the IRS concluded that mitigation applies to allow taxpayers to claim refunds by carrying back certain net operating losses (NOLs) to closed years when examination of an open year leads to the disallowance of a carryforward of a different NOL and revealed the taxpayers' errors in carrying forward the NOLs without making the election to waive the carryback period. The amount subject to recovery using mitigation is limited to the amount of the double disallowance, in this case, the amount of the NOL.

Proposed Regulations Issued on Arbitrage Investment Restrictions on Tax-Exempt Bonds

The IRS released proposed regulations (<https://www.federalregister.gov/documents/2018/06/12/2018-12565/arbitrage-investment-restrictions-on-tax-exempt-bonds>) regarding the arbitrage investment restrictions under Section 148 applicable to tax-exempt bonds and other tax-advantaged bonds issued by state and local governments. The proposed regulations would clarify existing regulations regarding the definition of "investment-type property" covered by arbitrage restrictions by expressly providing an exception for investments in capital projects that are used in furtherance of the public purposes of the bonds. The proposed regulations affect state and local governmental issuers of these bonds and potential investors in capital projects financed with these bonds.

Colorado and Rhode Island Announce Guidance on Deferred Foreign Income for C Corporations

The Rhode Island Division of Taxation proposed a regulation (http://www.tax.ri.gov/Advisory/ADV_2018_23.pdf) that would provide guidance to C corporations and their advisors on how to report deferred foreign income ("Section 965 income") for Rhode Island tax purposes for the 2017 tax year. Section 965 income, in its entirety, is recognized and must be included on a taxpayer's federal return for its last taxable year beginning before Jan. 1, 2018.

Colorado released guidance (<https://www.colorado.gov/pacific/sites/default/files/CDOR%20Supplemental%20Instructions%20for%20Repatriation.pdf>) on the Section 965 income stating that any amount a Colorado taxpayer must include in income as a result of Section 965 must also be included in the federal taxable income reported on the taxpayer's Colorado return. Further, if a taxpayer subject to Colorado corporate income tax apportionment and allocation properly claims a federal deduction or federal credit for foreign taxes paid on Section 965 income, a corresponding portion of the Section 965 income will be eligible for the foreign source income exclusion on the taxpayer's Colorado return.

U.S. Supreme Court Declined Review of Pennsylvania *Nextel* Case

The Supreme Court denied certiorari in *Nextel Communications of the Mid-Atlantic Inc. v. Department of Revenue*, keeping in place the Pennsylvania Supreme Court's decision that the \$3 million cap on the NOL deduction violated the Uniformity

Clause of the Pennsylvania Constitution, but the 12.5 percent of taxable income limitation on the NOL deduction was permitted. See our prior coverage here (<https://www.stradley.com/insights/publications/2017/10/tax-insights-october-25-2017>).



Christopher C. Scarpa



Kristin M. McKenna

For more information, contact Christopher C. Scarpa at 215.564.8106 or cscarpa@stradley.com or Kristin M. McKenna at 215.564.8145 or kmckenna@stradley.com.

Stradley Ronon's Tax Practice Group

Todd C. Vanett, Chair.....	215.564.8070	.....	tvanett@stradley.com
Zachary P. Alexander	215.564.8043	.....	zalexander@stradley.com
Jacquelyn Gordon	215.564.8176	.....	jgordon@stradley.com
Kristin M. McKenna	215.564.8145	.....	kmckenna@stradley.com
William R. Sasso.....	215.564.8045	.....	wsasso@stradley.com
Christopher C. Scarpa	215.564.8106	.....	cscarpa@stradley.com