



perspective  
**GAINED**

TAX UPDATE

**Impact of new accounting pronouncements**

**2019 WHAT'S NEW IN NEW ENGLAND BANKING WORKSHOP**



## **OBJECTIVES**

What you will gain:

- Knowledge about the tax implications of recent accounting pronouncements
- Tax strategies to implement now
- Planning opportunities for 2020

## ASU NO. 2016-02, LEASES (TOPIC 842) FINANCIAL REPORTING

- New standard is effective for public business entities in fiscal years beginning after 12/15/19 (1/1/20 for calendar year entity)
- For most other entities, it is deferred for one year, meaning that most calendar-year private companies will be required to adopt the new standard in 2021
- Early adoption is permitted for all entities
- Requires lessees to record all leases, except for short-term leases, on the balance sheet and recognize a right-of-use (ROU) asset and lease liability arising from the lease

### OLD RULES

Operating lease – off balance sheet

Capital lease – on balance sheet

### NEW RULES

Operating lease – on balance sheet

Finance lease – on balance sheet

## ASU NO. 2016-02, LEASES (TOPIC 842)

### TAX REPORTING

- Federal tax accounting method for leases has not changed
- What does this mean?
  - Still need to evaluate classification of lease for tax purposes
  - Tax lease or true lease vs. non-tax lease or financing lease

IRS revenue procedures 2001-28 and 2001-29, issued in May 2001, specify that a transaction must satisfy specific criteria to be classified as a true lease

- Tax lease – expense for lease payments
- Financing lease – capitalized fixed asset / depreciation / interest expense

## **ASU NO. 2016-02, LEASES (TOPIC 842)**

### **DEFERRED TAXES**

- New standard changes the way entities account for operating leases for financial reporting, which may create differences in methods of accounting for financial reporting and income tax purposes. Entities now record an ROU asset and a lease liability, effectively grossing up their balance sheets
- Federal tax accounting method for leases has not changed, and companies will not have any tax basis in the ROU asset and related lease liability
- Accordingly, a company must recognize a deferred tax liability for the excess of the GAAP basis in the ROU asset and a deferred tax asset for the GAAP basis in the related lease liability.

## **ASU NO. 2016-02, LEASES (TOPIC 842)**

### **OTHER TAX CONSIDERATIONS**

- State Apportionment
  - Property factor
  - Rent Expense
- Franchise, net worth, and similar taxes
- Personal Property / Real Estate Taxes



## **ASU NO. 2016-01, FINANCIAL INSTRUMENTS (SUBTOPIC 825) FINANCIAL REPORTING**

- Changes how certain financial assets and liabilities are recognized
- ASC 321, Investments – Equity Securities - requires entities to measure equity securities at FMV through income statement
- Pre-ASU 2016-01, OCI was used

# ASU NO. 2016-01, FINANCIAL INSTRUMENTS (SUBTOPIC 825) TAX REPORTING / DEFERRED TAXES

Initial recording:

- Reclassification of DTA / DTL from OCI to “regular deferred taxes”
- Beginning balance of DTA / DTL will be based on initial OCI reclassification difference between FMV and cost on initial date

Book-to-tax adjustments:

- Unrealized gain/loss generally not taxable income/tax deduction – will need new temporary difference item on tax provision since FMV adjustment is now booked through the income statement for financial reporting purposes
- Need to track by investment so the deferred market value adjustments can be recognized on the tax return when a specific investment is sold / disposed of



# ASU NO. 2016-01, FINANCIAL INSTRUMENTS (SUBTOPIC 825) TAX REPORTING / VALUATION ALLOWANCE

Valuation allowance:

- Needed if “more likely than not” test is not met for realization – ASC 740
- Pre-ASU 2016-01 – could separate analysis of realization of OCI DTA for AFS debt securities, based on intent to hold to maturity and fact that future taxable income was not needed to realize
- Under ASU 2016-01 – can no longer separate the analysis. Assessment of need for valuation allowance for AFS debt securities uses same rational, as other DTA’s
- Need may arise to record a valuation allowance when one wasn't needed pre-ASU 2016-01

## ASU NO. 2014-09, REVENUE FROM CONTRACTS WITH CUSTOMERS (TOPIC 606) FINANCIAL REPORTING

- FASB's intent is to provide a standardized approach for recognizing revenue across multiple industries
- Standard became effective for public business entities (PBEs) with annual reporting periods beginning after 12/15/17, and will be effective for non-PBEs for annual reporting periods beginning after 12/31/18
- Replaces a lot of industry - and transaction-specific guidance
- Guidance core principal - Recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services

### NOT WITHIN SCOPE

Interest income, dividend income, credit card fees, servicing income

### WITHIN SCOPE

Trust fees, asset management fees, deposit fees, sale of foreclosed property

# ASU NO. 2014-09, REVENUE FROM CONTRACTS WITH CUSTOMERS (TOPIC 606)

## TAX REPORTING

- Amendments to Tax Rules Under Section 451
- TCJA included some foundational changes under IRC §451 regarding when taxpayers recognize revenue for federal income tax purposes
- It's no surprise that we are seeing changes to IRC §451 around the same time that the ASC 606 standard is being adopted
- Section 451 “All-Events Test”: Accrual method taxpayer must include an item in gross income when all events have occurred that fix the right to receive the income. Meaning the required performance has occurred, payment is due or payment is made — whichever happens earlier — and the amount can be determined with reasonable accuracy
- TCJA incorporates into IRC §451 another “earlier of” provision: The right to income cannot be fixed any later than when that income is reported in an AFS

## **ASU NO. 2014-09, REVENUE FROM CONTRACTS WITH CUSTOMERS (TOPIC 606)**

### **TAX REPORTING**

- Both ASC 606 and the amendments to IRC §451 may result in a change in the timing of when revenue is recognized
- Generally, when a taxpayer changes the timing of an item of income for tax purposes, IRS consent is required to change the method of accounting
- Rev. Proc. 2018-29, as modified by Rev. Proc. 2018-49, allows taxpayers to obtain automatic consent from the IRS for a change in the tax reporting of revenue recognition, provided the change is made in the same year that the ASC 606 standard is adopted
- Rev. Proc. 2018-29 grants automatic consent where the taxpayer wants to change their method consistent with ASC 606 for the identification of the performance obligations, the allocation of the transaction price to those performance obligations, and/or considering the performance obligations satisfied

# BUSINESS INTEREST EXPENSE LIMITATION

## [Section 163(j)]

**Deductibility of net business interest expense limited to 30% of a taxpayers “adjusted taxable income”**

### **Issues**

1. Holding Companies with Subordinated Debt
2. Receipt of partnership K-1's (LIHTC, Rehab, etc.)
  - a. Deferred taxes and impact on tax basis in partnership investment

## AMT

### **TCJA eliminated the AMT for corporations**

Existing AMT credits can offset regular tax beginning in 2018. Any credit available after offsetting tax can be refunded:

- 50% in 2018, 2019, and 2020
- 100% in 2021

### **Tax accounting issue**

1. Should AMT credits remain a DTA or moved to a receivable
2. Impact on valuation allowance existing on AMT credit DTA
3. Does AMT credit asset need to be written down for government sequestration?



## **ACCELERATED TAX DEPRECIATION**

- Tax reform allows for 100% bonus depreciation on qualified property for year assets are placed in service before 12/31/22
- Bonus depreciation is set to phase out by 20% each year after 1/1/23 until it completely expires on 12/31/26
- Consider phase out in planning the timing of future capital purchases





## “PARKING TAX”

- Free parking for employees is not deductible by for-profit entities and is taxable as UBI for tax-exempt entities
- Parking expenses
  - “Any reasonable method” to calculate: 4-step approach (guidance exists)
- Planning opportunity: Re-evaluate parking arrangements or lease agreements. Eliminate reserved employee parking spots. Reduce parking expenses if possible.





## **SOLAR TAX CREDIT – Extended back in 2015**

- Sec. 25D(g) provides a credit of:
  - 30% if placed in service in a residence before 1/1/20
  - 26% if placed in service after 12/31/19 and before 1/1/21
  - 22% if placed in service after 12/31/20 and before 1/1/22
- Sec. 48(a)(2)(A) provides a 30% credit for solar energy equipment in commercial property if construction begins before 1/1/22



## Questions

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