

FHLBANK TOPEKA STOCK DIVIDENDS

TAX CONSIDERATIONS FOR YOUR INSTITUTION

FHLBank Topeka does not offer legal or tax advice. Members need to consult their own legal and tax advisers as to the proper treatment of stock dividends from FHLBank, including appropriate cost basis adjustments and implications of future sales and redemptions of FHLBank stock.

FHLBank stock dividends may qualify as tax-deferred stock dividends under the Internal Revenue Code and therefore may not be taxable at the time declared and credited to the member. Revenue Ruling 90-98, 1990-48 I.R.B. 4.

Calculating Stock Basis | When a member purchases FHLBank stock, the cost basis of the shares purchased is the \$100 paid for the stock. In contrast, when a member receives a stock dividend from the FHLBank, the cost basis of the shares then owned by the member may be reallocated across all the shares owned (i.e., including the stock received as a dividend) based on the fair market value of the shares (\$100). I.R.C. Section 307. This reallocation should generally be done by “lots” (i.e., a lot would be those shares acquired on a particular date and any stock dividends subsequently received on those shares). 26 CFR 1.1012-1(c)(1). Because of the reallocation, the purchase of shares after receipt of a stock dividend will result in the purchased shares having a different cost basis than the shares owned when the stock dividend was received.

Identification of Shares Redeemed | When FHLBank stock is redeemed for \$100 a share, the amount of capital gain on the sale of the shares will be determined by the difference between the sale price (\$100) and the cost basis of the shares sold. The shares may have a tax basis of \$100 (shares purchased after the payment of any stock dividends), or the shares may have a tax basis significantly less than \$100 due to repeated stock dividends from FHLBank. The higher the tax basis, the lower the capital gain that arises from the sale.

When FHLBank redeems FHLBank stock, a member may identify the shares being redeemed (e.g., by identifying the acquisition date of the shares being sold in the minutes of a member’s board meeting or in a communication to FHLBank). By choosing which stock will be redeemed, the member can potentially reduce the tax consequences of the redemption by identifying shares that have a higher cost basis. Adequate tracking of cost basis in FHLBank stock, and identification of the particular shares to be redeemed, is required to obtain this tax benefit. Inadequate tracking of shares will result in the application of an assumption that the shares being redeemed are those held the longest (first-in, first-out rule, also known as FIFO), typically the shares with the lowest cost basis. Revenue Ruling 71-350, 1971-2 C.B. 176.