

- (i) Calculation of gross income from a matched book.
- (j) Income earned by qualified securities affiliates.
- (1) General rule.
- (2) Affiliate income requirement.
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- (4) Related group.
- (5) Example.
- (k) Income from nonsecurities activities.
- (l) Effective date.

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Par. 4. Section 1.1296-4 is added to read as follows:

§ 1.1296-4 Characterization of certain banking income of foreign banks as nonpassive.

(a) *General rule.* For purposes of section 1296, banking income earned by an active bank, as defined in either paragraph (b) (1) or (2) of this section, or by a qualified bank affiliate, as defined in paragraph (i) of this section, is nonpassive income.

(b) *Active bank*—(1) *U.S. licensed banks.* A corporation (whether domestic or foreign) is an active bank if it is licensed by federal or state bank regulatory authorities to do business as a bank in the United States. A foreign corporation will not satisfy the requirements of this paragraph (b)(1) if, under its federal or state license or licenses, the foreign corporation is permitted to maintain only an office, such as a representative office, that is prohibited by federal or state law from taking deposits or making loans.

(2) *Other foreign banks.* A foreign corporation is an active bank if it meets the licensing requirement of paragraph (c) of this section and it actively conducts, within the meaning of § 1.367(a)-2T(b)(3), a banking business that is a trade or business within the meaning of § 1.367(a)-2T(b)(2). In order for the business conducted by a foreign corporation to be considered a banking business, the foreign corporation must also meet the deposit-taking requirements of paragraph (d) of this section and the lending requirements of paragraph (e) of this section.

(c) *Licensing requirements.* To be an active bank under paragraph (b)(2) of this section, a foreign corporation must be licensed or authorized to accept deposits from residents of the country in which it is chartered or incorporated and to conduct, in that country, one or more of the banking activities described in paragraph (f)(2) of this section. However, in no case will a foreign corporation satisfy the requirements of this paragraph (c) if one of the principal purposes for its obtaining a license or authorization was to satisfy the requirements of this section.

(d) *Deposit-taking requirements*—(1) *General rule.* To be an active bank under paragraph (b)(2) of this section—

(i) A foreign corporation must, in the ordinary course of the corporation's trade or business, regularly accept deposits from customers who are residents of the country in which it is licensed or authorized; and

(ii) The amount of deposits shown on the corporation's balance sheet must be substantial.

(2) *Deposit.* Whether a liability constitutes a deposit for purposes of this paragraph (d) is determined by reference to the characteristics of the relevant instrument and does not depend solely on whether the instrument is designated as a deposit.

(3) *Substantiality of deposits.* Whether the amount of deposits (including interbank deposits) shown on a corporation's balance sheet is substantial depends on all the facts and circumstances, including whether the corporation's capital structure and funding sources as a whole are similar to that of banking institutions engaged in the same types of activities and subject to the jurisdiction of the same bank regulatory authorities.

(e) *Lending activities test.* To be an active bank under paragraph (b)(2) of this section, a corporation must regularly make loans to customers in the ordinary course of its trade or business. A note, bond, debenture or other evidence of indebtedness will be treated as a loan for purposes of this section only if the debt instrument is received by the corporation on an extension of credit made pursuant to a loan agreement entered into in the ordinary course of the corporation's banking business. Such debt instruments generally will not be considered loans for purposes of this section if the instruments are not treated as loans (but are classified as securities or other investment assets, for example) for purposes of the foreign corporation's financial statements.

(f) *Banking income*—(1) *General rule.* Banking income is the gross income derived from the active conduct (within the meaning of § 1.367(a)-2T(b)(3)) of any banking activity described in paragraph (f)(2) of this section.

(2) *Banking activities.* For purposes of this section, the following are banking activities—

(i) Lending activities described in paragraph (e) of this section;

(ii) Factoring evidences of indebtedness for customers;

(iii) Purchasing, selling, discounting, or negotiating for customers notes, drafts, checks, bills of exchange,

acceptances, or other evidences of indebtedness;

(iv) Issuing letters of credit and negotiating drafts drawn thereunder for customers;

(v) Performing trust services, including activities as a fiduciary, agent or custodian, for customers, provided such trust activities are not performed in connection with services provided by a dealer in stock, securities or similar financial instruments;

(vi) Arranging foreign exchange transactions (including any section 988 transaction within the meaning of section 988(c)(1)) for, or engaging in foreign exchange transactions with, customers;

(vii) Arranging interest rate or currency futures, forwards, options or notional principal contracts for, or entering into such transactions with, customers;

(viii) Underwriting issues of stock, debt instruments or other securities under best efforts or firm commitment agreements for customers;

(ix) Engaging in finance leases, as defined in § 1.904-4(e)(2)(i)(V);

(x) Providing charge and credit card services for customers or factoring receivables obtained in the course of providing such services;

(xi) Providing traveler's check and money order services for customers;

(xii) Providing correspondent bank services for customers;

(xiii) Providing paying agency and collection agency services for customers;

(xiv) Maintaining restricted reserves (including money or securities) as described in paragraph (g) of this section; and

(xv) Any other activity that the Commissioner determines, through a revenue ruling or other formal published guidance (see § 601.601(d)(2) of this chapter), to be a banking activity generally conducted by active banks in the ordinary course of their banking business.

(g) *Certain restricted reserves.* A deposit of assets in a reserve is, for purposes of this section, a banking activity if the deposit is maintained in a segregated account in order to satisfy a capital or reserve requirement under the laws of a jurisdiction in which the corporation actively conducts (within the meaning of § 1.367(a)-2T(b)(3)) a banking business that is a trade or business (within the meaning of § 1.367(a)-2T(b)(2)). A deposit of assets into a reserve qualifies under this paragraph (g) if and only to the extent that the assets are not available for use in connection with the corporation's banking business because of significant