



Charting the M&A Tax future

Strategies for 2026 compliance and provision planning



As we embark on 2026, corporate tax leaders are setting the tone for a new compliance cycle, balancing the finalization of year-end calculations with the demands of expanding operations, integrating acquisitions, and optimizing tax attributes for the road ahead. Whether your organization is focusing on earnings and profits (E&P), Section 382 ownership considerations, stock basis tracking, or state and local tax (SALT) nuances, these core pillars of merger and acquisition (M&A) tax can pave the way for more confident reporting and smoother transactions.

In a recent TaxWatch webcast, KPMG LLP professionals zeroed in on the primary year-end issues that surface immediately once the calendar flips, finalizing E&P positions, preparing time-sensitive information reporting, evaluating attribute limitations, and reconciling basis for both transactions and returns. With that holistic perspective, companies can better navigate compliance pressure, help reduce audit risk, and step into 2026's M&A environment with greater clarity and control.

Reimagining E&P beyond year-end

E&P is more than a mere year-end consideration. It reflects a corporation's economic capacity to pay dividends. Keeping E&P current throughout the year can facilitate vital planning, especially if distributions or redemptions might occur in early 2026 or midyear.

Key E&P principles

- **Not simply taxable income:** E&P starts with taxable income but adjusts for specific items, such as the use of alternative depreciation system instead of more accelerated methods, and permanent differences (e.g., fines, penalties).
- **Timing of losses:** In E&P computations, losses reduce E&P in the actual year they arise, even if those losses are carried forward for federal income tax purposes.

Distribution reporting requirements

- **Form 1099-DIV:** Must be provided to shareholders by January 31. If you cannot finalize E&P quickly (for instance, right after a distribution), then the portion that may be a dividend should be reported as such and then amended later if the final E&P calculation differs.
- **Form 8937:** Required if a distribution alters shareholders' basis (e.g., if a nondividend distribution is made). Must typically be filed within 45 days of the organizational action or by January 15 of the following year if the action occurs late in December.
- **Form 5452:** Required with a corporate tax return if distributions exceed E&P, classified as nondividend distributions.

Redemptions and withholding considerations

- **E&P decreases:** Redemptions reduce E&P by the lesser of the repurchase amount or the E&P allocable to the redeemed shares.
- **Escrow method:** Particularly relevant when a corporation has foreign shareholders and E&P is not yet computed. Funds are temporarily withheld to avoid underwithholding and minimize risk.

Leading practices



- **Annual rollforward:** Proactively track E&P throughout the year to sidestep frantic recalculations.
- **Integrate transaction data:** Mergers, spin-offs, or intercompany exchanges can significantly shift E&P, requiring diligent recordkeeping.

Harnessing Section 382 to manage tax attributes

Attribute preservation remains a hot topic as companies evolve ownership structures through equity transactions, funding rounds, or acquisitions. A 50-percentage-point or more jump in ownership by 5 percent shareholders triggers a new Section 382 limitation on net operating losses (NOLs), credit carryforwards, and disallowed interest deductions.

Defining an ownership change

- **Rolling three-year lookback:** Track each 5 percent shareholder's lowest ownership level within a three-year (36-month) window to see if an increase over 50 points has occurred.
- **Loss corporations:** Entities holding NOLs, capital loss carryovers, minimum tax credits, foreign tax credits, business credits, or significant built-in losses qualify as "loss corporations" subject to these rules.

Calculating the annual limitation

- **Base limitation:** Typically "equity value x the long-term tax-exempt rate."
- **Built-in gains versus losses:** If the corporation had net unrealized built-in gains at change date, then recognized gains during the next five years can boost the limitation. Conversely, net unrealized built-in loss means future built-in losses are only offsettable by any remaining limitation.

Leading practices



- **Annual equity tracking:** Keep detailed records of equity transactions, capitalization tables, 83(b) elections, and valuation remarks.
- **Timely documentation:** Required statement disclosures in the tax return must specify all change dates, the nature of attributes, and any elections (like closing the books on the ownership change date).

Illuminating Section 384: Protecting against blended gains

Section 384 further restricts corporations formed or reorganized in a manner that might blend a loss company with a built-in gain company.

- **5-Year Recognition Window:** Income from recognized built-in gains during this period cannot generally be offset with another corporation's pre-acquisition losses (unless they originally belonged to the gain corporation).
- **Planning Relevance:** Keep an eye on restructuring or asset reorganizations in 2026 to help ensure that built-in gains remain separate from legacy NOLs, unless structured under allowable exceptions.



Elevating stock basis tracking

Accurate stock basis propels strategic transactions. Whether disposing of a subsidiary or triggering a worthless stock deduction, a methodical approach is crucial.

Why basis matters?

1 Gain or loss on sale: Basis drives the ultimate tax result on stock dispositions. When planning an asset versus stock sale, modeling can clarify potential "tax leakage."

2 Basis adjustments: In a consolidated group, bracketed by the regulations under Sections 1.1502-32 and -36, stock basis is adjusted each year for subsidiary-level income/loss, tax-exempt income, noncapital nondeductible items, and distributions.

Unified loss rule

If you transfer "loss shares," three rules apply in order:

1. **Basis redetermination** – Possibly realigning multiple blocks of stock basis
2. **Basis reduction** – To remove noneconomic losses if outside basis exceeds inside basis
3. **Attribute reduction** – If stock loss remains, then the subsidiary's inside attributes may be reduced to prevent duplication of loss.

Worthless stock deductions

- **Capital versus ordinary:** Section 165(g)(3) can allow an ordinary deduction if you hold at least 80 percent vote/value and meet the "90 percent gross receipts from active sources" test over the subsidiary's entire existence.
- **Identifiable event:** For a worthless stock deduction, the stock must be genuinely worthless by year-end, with no liquidating or potential value.

Leading practices



- **Annual basis computing:** Maintain a running schedule, factoring in distributions, contributions, and intercompany transactions.
- **Monitor intercompany settlements:** Determine if they are made in cash or simply recorded in due-to/due-from accounts, as that can shift basis unexpectedly.

Considering SALT nuances

Many states diverge from the federal consolidated return regulations, meaning that E&P, NOL limitations, stock basis, or worthless stock deductions may be computed differently:

- **E&P at the state level** – Some states follow their own rules on depreciation or intercompany dividends, yielding different E&P numbers.
- **382-like limitations** – Certain states either fully adopt Section 382 or not at all; a separate-entity approach can lead to an ownership change test for each subsidiary individually.
- **Basis discrepancies** – Without a “1.1502-32 equivalent,” basis in a subsidiary could be far higher or lower than at the federal level, affecting the gain or loss in a state context.



The path forward: Strategy and readiness for 2026

Heading into a new year, especially one that promises fresh transaction activity, demands a proactive, far-reaching plan:

- **Roll E&P and stock basis early and often:**
Rather than waiting until December's close, periodic updates help ensure fewer surprises, especially if redemptions or distributions occur midyear.
- **Proactive ownership change analysis:**
Even if you do not anticipate a large equity shift, smaller steps (e.g., new investors or secondary offerings) can accumulate. Identifying a potential Section 382 trigger in real time avoids sudden limitations on your hard-earned NOLs or credits.
- **State-by-state evaluations:** Updating your approach to reflect each state's unique stance on consolidated reporting, combined returns, and NOL laws arms you with more reliable effective tax rate projections and compliance outcomes.
- **Documenting and disclosing properly:** Where required (e.g., Forms 1099-DIV, 8937, 5452, and 1042-S or the white-paper statement for Section 382), file within the prescribed deadlines. The same goes for worthless stock deductions above \$10 million, which may necessitate “reportable transaction” forms.

M&A tax considerations, ranging from E&P and distribution mechanics to Section 382 ownership-change analysis and the unified loss rule, are just as pertinent in January as they are in year-end planning. By treating these areas as ongoing processes, incorporating data from each acquisition, issuance, or reorganization, you can reduce compliance pressure, recognize potential pitfalls sooner, and seize planning opportunities for 2026 and beyond.

For questions about how these regulations affect your specific situation, consider reaching out to your trusted M&A tax adviser, especially if you confront complex transactions, multistate filings, or uncertain E&P thresholds.



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