MEMO# 32830

October 14, 2020

IRS Issues Additional Guidance on Transition from LIBOR

[32830]

October 14, 2020 TO: ICI Members
LIBOR Transition Working Group
Tax Committee SUBJECTS: Tax RE: IRS Issues Additional Guidance on Transition from LIBOR

The Treasury Department and the Internal Revenue Service (IRS) have issued additional guidance on the tax consequences of transitioning from the London Interbank Offered Rate (LIBOR) or other interbank offered rates (IBORs) to alternative reference rates. Revenue Procedure 2020-44 clarifies that certain modifications to contracts adopting fallback language recommended by the Alternative Reference Rates Committee (ARRC) or the International Swaps and Derivatives Association (ISDA) will not be treated as a material exchange of property for purposes of Treas. Reg. § 1.1001-1(a) and therefore will not result in a taxable event to the holders of the contracts. The revenue procedure also provides that such modifications will not be treated as legging out of an integrated transaction, a termination of a qualified hedge, or as a disposition or termination of either leg of a hedging transaction.

The Treasury Department and the IRS issued proposed regulations in October 2019, addressing guidance on the tax consequences of modifying debt instruments, derivative contracts, and other contracts to replace IBORs or add fallback provisions to IBORs.[1] In response to comments from ARRC, the revenue procedure specifically addresses modifications adopting ARRC or ISDA fallback language, with reference to the relevant sections of the ARRC recommendations and the ISDA Protocol.

Scope

The revenue procedure applies to any contract (including but not limited to a derivative contract, debt instrument, stock, insurance contract and lease agreement) that is modified to incorporate ISDA or ARRC fallback language. The revenue procedure permits certain deviations from such language:

1. Deviations that are reasonably necessary to make the terms incorporated into the contract legally enforceable in a relevant jurisdiction or to satisfy legal requirements of that jurisdiction;
2. Deviations from the terms of ISDA fallback language that are reasonably necessary to incorporate the ISDA fallback into a contract that is not a Protocol Covered Document

(as defined in the ISDA Protocol);

3. Deviations to omit terms that cannot under any circumstances affect the operation of the modified contract; or
4. Deviations to add, revise or remove technical, administrative or operational terms, provided that the addition, revision or removal is reasonably necessary to adopt or to implement the ARRC or ISDA fallback language. This category of deviations does not apply to the addition of a term that obligates one party to make a one-time payment (or similar payments) as a substitute for any portion of an ARRC or ISDA fallback language or as consideration for the modification.

Effective Date

The revenue procedure is effective for modifications to contracts occurring on or after October 9, 2020, and before January 1, 2023, though taxpayers may rely on this guidance for modifications to contracts occurring before October 9, 2020.

Additional Guidance

The Treasury Department and IRS may provide additional relief as necessary to address developments in the transition from IBORs, including changes to the ARRC or ISDA fallback language. The government requests comments on the list of permissible deviations to the ARRC and ISDA fallback language, including the need for additional categories of deviations.

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endnotes

[1] *See* Institute Memorandum No. 32002, dated October 10, 2019, which can be found at: https://www.ici.org/my_ici/memorandum/memo32002.
