

MEMO# 14191

November 29, 2001

DRAFT OUTLINE OF INSTITUTE COMMENTS ON TAXATION OF NOTIONAL PRINCIPAL CONTRACTS

BY EMAIL [14191] November 29, 2001 TO: TAX COMMITTEE No. 30-01 RE: DRAFT OUTLINE OF INSTITUTE COMMENTS ON TAXATION OF NOTIONAL PRINCIPAL CONTRACTS As we discussed at our recent Committee meetings, the Internal Revenue Service and Treasury Department are seeking comments on the taxation of notional principal contracts (commonly referred to as “swaps”) with contingent nonperiodic payments. In Notice 2001-44, four potential methods were identified for including contingent nonperiodic payments made under a swap in income – the (1) “noncontingent swap” method, (2) “full allocation” method, (3) “modified full allocation” method and (4) “mark-to-market” method.¹ Attached to this memorandum is a draft outline of the Institute’s comments on Notice 2001-44. In sum, the outline recommends that the “full allocation” method be adopted for short-term swaps and the “mark-to-market” method be available on an elective basis. The outline also identifies technical issues that must be addressed in order to implement a “mark-to-market” method for regulated investment companies. ACTION REQUESTED: In order to expedite the drafting of the Institute’s comment letter, please provide your comments on the attached outline to the undersigned (dflores@ici.org or 202/371-5436) as soon as possible and, preferably, by Friday, December 7th . As part of your comments, please generally describe the types of swaps with contingent nonperiodic payments presently utilized by your complex and the term of such swaps (e.g., credit default swaps with terms of 3 to 5 years). Please also indicate how a “short-term” or “long-term” swap should be defined and what approach, if any, the Institute should recommend for “long-term” swaps with contingent nonperiodic payments. Deanna J. Flores Associate Counsel Attachment Attachment (in .pdf format) 1 See Institute Memorandum to Tax Committee No. 21-01, dated July 26, 2001. 2