

Proposed Guidance with Respect to LIBOR Transition – 1001 and 863

----1.1001-6----

- (a) **IBOR-related modifications.** For purposes of §1.1001-1(a), modifications of a contract (including, but not limited to, a debt instrument, a derivative contract, stock, an insurance contract or a lease agreement) described in paragraphs (b) and (c) are not treated as the exchange of the contract for a modified contract differing materially in kind or extent. Any other modifications to the contract that are made contemporaneously with any modifications described in paragraphs (b) or (c) are subject to §1001 and any applicable regulations for purposes of determining whether such a deemed exchange has occurred, without taking into account any modification described in the preceding sentence.
- (b) **Certain modifications to a reference rate.** This paragraph (b) applies to a modification to the terms of a contract that—
- (1) changes a reference rate of the contract from an IBOR rate to a qualified replacement rate;
 - (2) may provide for one or more compensating adjustments; and
 - (3) may provide for transition administrative changes.
- (c) **Certain modifications to a fallback reference rate.** This paragraph (c) applies to a modification to the terms of a contract that is intended to provide for an alternative to an IBOR rate referenced by such contract in the event that such IBOR rate becomes unavailable, unreliable or otherwise may no longer be used under the terms of the contract, provided that such modification is reasonably expected to result in consequences consistent with those resulting from a modification described in paragraph (b) of this section.
- (d) **Definitions.**
- (1) *Reference rate.* A reference rate is a rate by reference to which payments on a contract are determined under the terms of the contract.
 - (2) *IBOR rate.* An IBOR rate includes the London Interbank Offered Rate (LIBOR), the Euro Interbank Offered Rate (EURIBOR), the Tokyo Interbank Offered Rate (TIBOR), the Bank Bill Swap Rate (BBSW), the Canadian Dollar Offered Rate (CDOR), the Hong Kong Interbank Offered Rate (HIBOR), the Interbank Equilibrium Interest Rate (TIIE), the Singapore Interbank Offered Rate (SIBOR), the Singapore Swap Offer Rate (SOR), and any other interbank offered rate.
 - (3) *Qualified replacement rate.* A qualified replacement rate includes—
 - (i) a qualified floating rate (within the meaning of §1.1275-5(b), without regard to the limitations on multiples contained in §§1.1275-5(b)(2)(i)-(ii));

- (ii) a rate recommended by the Alternative Reference Rates Committee (e.g., Secured Overnight Financing Rate (SOFR)) or a comparable non-U.S. organization or non-U.S. regulator; or
 - (iii) a rate otherwise identified by the Commissioner in a notice or revenue procedure as a suitable replacement rate.
- (4) *Compensating adjustment*. A compensating adjustment means a compensating spread adjustment or a compensating contemporaneous payment, and may include both, provided that such compensating adjustments are intended by the parties to offset the change in value of the contract to the parties that would result solely from the change to the reference rate. The compensating adjustments may be determined using any reasonable methodology to account for the difference in values between the modified contract and the unmodified contract, including differences between the historic averages of the relevant reference rates. A compensating adjustment will be conclusively presumed to be determined using a reasonable methodology if it is determined using a methodology based on the principles of:
 - (i) a method for calculating or determining such adjustments that has been recommended by the Alternative Reference Rates Committee or a comparable non-U.S. organization or non-U.S. regulator; or
 - (ii) a method for calculating or determining such adjustments that is used in fallback provisions implemented in the relevant “Rate Options” for the relevant IBOR rates in the interest rate definitions published by the International Swaps and Derivatives Association or that is described in the consultation on “Interbank Offered Rate (IBOR) Fallbacks for 2006 ISDA Definitions” published on July 12, 2018 by the International Swaps and Derivatives Association.¹
- (5) *Compensating spread adjustment*. A compensating spread adjustment is a fixed rate by which a qualified reference rate that replaces an IBOR rate in a contract is increased or decreased.
- (6) *Compensating contemporaneous payment*. A compensating contemporaneous payment is a payment between parties to a contract made in connection with the modification of the contract to replace the IBOR rate referenced by such contract with a qualified replacement rate.
- (7) *Transition administrative changes*. Transition administrative changes means, with respect to any qualified replacement rate, any technical, administrative or operational changes (including, but not limited to, changes to the definition of interest period and the timing and frequency of determining rates and making payments of interest)

¹ The consultation is available here - <http://assets.isda.org/media/f253b540-193/42c13663-pdf/>

intended to facilitate the adoption and implementation of such qualified replacement rate and to permit the administration thereof in a manner substantially consistent with market practice (or, if such market practice is not administratively feasible or no market practice for the administration of the qualified replacement rate exists, in such other manner of administration as is reasonably necessary in connection with the administration of the contract). Changes will be conclusively presumed to meet the requirements of this definition of transition administrative changes if they meet the definition of “Benchmark Replacement Conforming Changes” as published by the Alternative Reference Rates Committee or are consistent with changes required for fallback provisions implemented in the relevant “Rate Options” for the relevant IBOR rates in the interest rate definitions published by the International Swaps and Derivatives Association.

- (e) **Additional modifications.** In addition to specifying additional qualified replacement rates, the Commissioner may by notice or revenue procedure treat other modifications to contracts as subject to [§1.1001-6] upon the determination that such treatment is necessary or desirable in order to facilitate the replacement of IBOR rates generally or within specific financial markets.
- (f) **Effective date.** This section applies to modifications to a contract occurring on or after July 27, 2017.²

----1.863-7(a)----

- (3) Notwithstanding any limitation set forth in paragraph (a)(1) or (2) above, the source of any compensating contemporaneous payment (as defined in [§1.1001-6(d)(6)]) made pursuant to a modification described in [§1.1001-6(a)] with respect to any derivative contract (as defined in §1.1001-4(b)(3)) shall be determined in accordance with paragraph (b) of this section, whether or not such derivative contract is a notional principal contract.

² This is the date on which the U.K. Financial Conduct Authority announced it would not persuade or compel banks to contribute to LIBOR after 2021.

Proposed Guidance with Respect to LIBOR Transition – REMICs & Other Securitization Vehicles

If one or more modifications of qualified mortgages held by a REMIC or of regular interests in a REMIC are made in accordance with Section [] of this [revenue procedure][notice]—

.01 The Service will not challenge a securitization vehicle's qualification as a REMIC on the grounds that the modifications to any of the qualified mortgages are not among the exceptions listed in §1.860G-2(b)(3).

.02 The Service will not contend that the modifications to any of the qualified mortgages are prohibited transactions under section 860F(a)(2) on the grounds that the modifications result in one or more dispositions of qualified mortgages and that the dispositions are not among the exceptions listed in section 860F(a)(2)(A)(i)-(iv).

.03 The Service will not challenge a securitization vehicle's qualification as a REMIC on the grounds that the modifications to any regular interest held by the REMIC cause the regular interest to be transferred to the REMIC on a date not permitted by Section 860G(a)(3).

.04 The Service will not challenge a securitization vehicle's qualification as a REMIC on the grounds that the modifications to any regular interest in the REMIC cause the terms of the regular interest to be subject to a contingency that is not among the exceptions listed in §1.860G-1(b)(3).

.05 The Service will not challenge a securitization vehicle's qualification as a REMIC on the grounds that the modifications to the interest rate of any regular interest in the REMIC that are described in Section [] of this [revenue procedure][notice] cause the regular interest to bear interest at rate other than a variable rate described in §1.860G-1(a)(3), including for purposes of computing any weighted average rate or specified portion, which in either case takes into account the interest rate of such regular interest.

.06 The Service will not challenge a securitization vehicle's qualification as a REMIC on the grounds that any expenses reasonably incurred by the REMIC in connection with any modifications to any qualified mortgages held by the REMIC or regular interests in the REMIC that result in reduced payments on a regular interest in the REMIC cause the terms of the regular interest to be subject to a contingency that is not among the exceptions listed in §1.860G-1(b)(3).

.07 The Service will not contend that any payment by a party other than the REMIC of expenses reasonably incurred in connection with any modifications to any qualified mortgages held by the REMIC or regular interests in the REMIC is subject to a tax under Section 860G(d) on the grounds that such payment is a contribution that is not among the exceptions listed in Section 860G(d)(2).

If a modification of a stripped coupon or stripped bond issued by a fixed investment trust is made in accordance with Section [] of this [revenue procedure][notice]—

.01 The Service will not treat the modification of the stripped coupon or stripped bond as a newly issued debt instrument under section 1286.

.02 The Service will not treat the modification of the stripped coupon or stripped bond issued by a fixed investment trust as a “power to vary” under §301.7701-4(c).