

Part III

Administrative, Procedural, and Miscellaneous

26 CFR 601.601: Rules and regulations.
(Also Part I, § 1058)

Rev. Proc. 2008-63

SECTION 1. PURPOSE

This revenue procedure provides guidance with respect to the application of § 1058(a) of the Internal Revenue Code to situations in which securities are originally transferred pursuant to an agreement that meets the requirements of § 1058(b), the transferee subsequently defaults under the agreement as a direct or indirect result of its bankruptcy (or the bankruptcy of an affiliate), and as soon as is commercially practicable (but in no event more than 30 days following the default), the transferor uses collateral provided pursuant to the agreement to purchase identical securities.

SECTION 2. BACKGROUND

.01 Section 1058(a) provides that in the case of a taxpayer who transfers securities (as defined in § 1236(c)) pursuant to an agreement which meets the requirements of § 1058(b), no gain or loss shall be recognized on the exchange of such securities by the taxpayer for an obligation under such agreement, or on the exchange of rights under such agreement by that taxpayer for securities identical to the securities transferred by that taxpayer.

.02 In adding § 1058 to the Code, Congress intended to provide nonrecognition treatment to securities loans in which “the contractual obligation [to return identical securities] does not differ materially either in kind or in extent from the securities exchanged” S. Rep. No. 762, 95th Cong., 2d Sess. 7 (1978); 1978-2 C.B. 357, 361 (“Senate Report”). Congress also sought to encourage securities holders to make their securities available for loans. Congress explained:

Under present law, uncertainty has developed as to the correct income tax treatment of certain securities lending transactions. As a result, some owners of securities are reluctant to enter into such transactions.

Senate Report at 3; 1978-2 C.B. 359.

Because of time delays which a broker may face in obtaining securities (from the seller or transfer agent) to deliver to a purchaser, brokers are frequently required to borrow securities from organizations and individuals with investment portfolios for use in

completing these market transactions. It is generally thought to be desirable to encourage organizations and individuals with securities holdings to make the securities available for such loans since the greater the volume of securities available for loan the less frequently will brokers fail to deliver a security to a purchaser within the time required by the relevant market rules.

Senate Report at 5; 1978-2 C.B 360.

.03 Recently, a significant number of securities loans have terminated as a result of a default by the borrower of the securities. These defaults are often the direct or indirect result of the bankruptcy of the borrower (or an affiliate of the borrower). For example, the bankruptcy of the borrower might, by itself, constitute an event of default under the securities loan agreement. Likewise, the bankruptcy of an affiliate of the borrower might indirectly prevent the borrower from returning identical securities upon notice of termination by the lender, if, for example, such a bankruptcy affects the borrower's liquidity and practical ability to acquire identical securities in the secondary market. In many of these situations, the lender thereafter purchases identical securities and applies collateral provided by the borrower pursuant to the securities loan agreement against the purchase price (and the borrower's obligation to return identical securities is terminated).

SECTION 3. SCOPE

This revenue procedure applies to taxpayers ("Lenders") who have transferred securities to an unrelated person ("Borrower") in a securities loan in which—

.01 The securities loan agreement (“Agreement”) satisfies the requirements of § 1058(b);

.02 The Agreement requires that the Borrower transfer collateral to secure the Borrower’s obligations under the Agreement;

.03 The Borrower defaults under the Agreement as a direct or indirect result of its bankruptcy (or the bankruptcy of an affiliate); and

.04 As soon as is commercially practicable after the default (but in no event more than 30 days following the default), the Lender applies collateral provided under the Agreement (or cash generated by the sale of such collateral) to the purchase of identical securities.

SECTION 4. APPLICATION

For taxpayers within the scope of this revenue procedure, the Internal Revenue Service will treat the purchase described in section 3.04 of this revenue procedure as an exchange of rights under the Agreement for identical securities to which § 1058(a) applies.

SECTION 5. EFFECTIVE DATE

This revenue procedure is effective for taxable years ending on or after January 1, 2008.

SECTION 6. NO INFERENCE

This revenue procedure provides guidance with respect to certain federal income tax issues involving securities loans described in section 3 of this revenue procedure.

No inference should be drawn about whether similar consequences will obtain if a

securities loan falls outside the scope of this revenue procedure.

SECTION 7. DRAFTING INFORMATION

The principal author of this revenue procedure is Charles W. Culmer of the Office of Associate Chief Counsel (Financial Institutions & Products). For further information regarding this revenue procedure contact Mr. Culmer on (202) 622-3950 (not a toll free call).