Guidance from Treasury regarding USD LIBOR Phase-Out

Hawkins Advisory

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The *Hawkins Advisory* discusses recently published Proposed Treasury Regulations that provide guidance as to the ability of parties to variable rate debt and other contracts that currently rely on LIBOR as an interest rate benchmark to alter the documents for these transactions for the purpose of incorporating interest rates reflective of other reference rates. The *Advisory* also reviews the status of other regulatory efforts to prepare the capital markets to transition from broad reliance upon LIBOR.

The Proposed Treasury Regulations generally provide that such changes will not be treated as "substantial" modifications of existing transactions that might otherwise result in a variety of federal tax consequences, including termination, if the new reference rate is a "qualified rate" and certain other requirements are met. This would create an exception from the current rules governing alterations.

- Qualified rates generally may include a reference rate selected, endorsed or recommended for this purpose by a governmental capital markets regulator (such as the Federal Reserve Bank of New York's Secured Overnight Financing Rate), a rate that is calculated on the basis of such a rate or a "qualified floating rate", defined, with certain variations, as in the existing variable rate debt instrument rules).
- To qualify for the proposed exception, the change to a qualified rate must result in an instrument that continues to have substantially the same fair market value as it did prior to the change. Safe harbor rules are provided for valuations that are based upon historic averages of the relevant reference rates and for new reference rates resulting from arm's length negotiations.

This proposed exception may extend to changes to "fallback rates" and to "associated alterations" that are reasonably necessary to implement the underlying reference rate changes.

The Proposed Regulation comment period expires on Saturday November 23, 2019. Taxpayers may rely upon the Proposed Regulations for permitted changes that occur prior to the Final Regulation publication date, provided that the taxpayer and its related parties consistently apply the proposed regulations prior to such date.

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