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December 20, 2002

The Honorable Pamela F. Olson
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Washington, DC 20220

Robert E. Wenzel
Acting Commissioner
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Re: Report on Securitization Reform Measures

Ladies and Gentlemen:

I am pleased to submit New York State Bar Association Tax Section's Report No. 1024 on securitization reform measures. The report recommends that the IRS and Treasury issue rulings or regulations in a number of tax law areas as an alternative to further implementing the FASIT rules (sections 860H through 860L) and with a view to an eventual repeal of the FASIT sections.

The specific recommendations (16 in all) are summarized in Part III of the report. The recommendations fall into the following areas: withholding tax rules for interest income and swap payments under sections 871, 881, 1441 and 1442; the definition of a financial business in section 7704(d)(2); the definition of a trade of business under section 864 (specifically relating to the securities trading safe harbor in section 864(b)(2)(A)(ii)); the status of certificates issued by a credit card securitization trust as debt or equity; and the REMIC and taxable mortgage

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pool ("TMP") regulations. The report also includes recommendations on tax reporting by fixed investment trusts that are foreign trusts (which is relevant to pending proposed regulations under section 671 on reporting by widely-held fixed investment trusts).

The report was prepared by a new standing committee of the Tax Section on Securitizations and Structured Finance. The principal author and editor is James M. Peaslee.

The Tax Section has submitted two prior reports relating to regulations under the FASIT rules.[1] The first, in 1997, responded to an IRS notice asking for comments on topics to be addressed in regulations. Proposed regulations were issued in February 2002, and the second report commented on those regulations. We are not aware of any current plan to finalize these regulations, nor do we believe such an effort would be fruitful, for two reasons. First, the proposed regulations were widely criticized and revising them to respond to comments would be a major project. Second, from the perspective of market participants, the statute suffers from a number of important drawbacks, some of which likely cannot be fixed through regulations. Thus, even if regulations were adopted that responded favorably to taxpayer comments, FASITs likely would not be widely used.

The FASIT legislation was enacted in 1996 to address concerns of market participants relating to the tax treatment of securitizations of non-mortgage receivables and revolving pools of mortgages. The type of structure that was supposed to benefit most directly from the FASIT rules was a financing of credit card receivables through a master trust. Typically, the trust would issue trust certificates to investors that were intended to qualify as debt for tax purposes even though they took the legal form of beneficial interests in the trust. Market participants had substantive tax concerns related to the status of the trust certificates as debt and, in the event certificate classes were not characterized as debt, the classification of the trust as a corporation under the rules for publicly traded partnerships in section 7704, the application of withholding taxes to income paid to foreign investors, and whether income allocated to foreign investors was taxable as income effectively connected with a U.S. trade or business. It was hoped that FASIT legislation would resolve these issues. Perhaps as a result, during the

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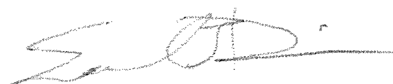
[1] See "Report on Suggested FASIT Regulations" (February 7, 1997), 97 *Tax Notes Today* 28-27 (February 11, 1997); "Report on Proposed Regulations Relating to Financial Asset Securitization Investment Trusts" (May 5, 2000), reprinted in 2000 *Tax Notes Today* 93-17 (May 12, 2000).

years since 1996 there has been no relevant guidance in these areas. The uncertainties that led to the FASIT legislation are still there.

After six years of experience with the FASIT statute, we believe the time has come to recognize that the legislation has not resolved the tax concerns that prompted its enactment and to consider other steps that can be taken in its place. The report recommends that the IRS and Treasury issue guidance in a number of areas as an alternative to the FASIT rules. If the recommended steps were taken, we believe the FASIT rules should be repealed.

The report includes recommendations for changes in the REMIC and TMP regulations. The changes are intended in part to compensate for the lack of a meaningful FASIT alternative. They also would update existing rules to accommodate securitizations of commercial mortgage loans and other changes in market practices since the regulations were issued.

Respectfully submitted,



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