

**IRS REVISES NOTICE RELATING TO LIQUIDITY-PROTECTED
PREFERRED STOCK ISSUED BY CLOSED-END FUNDS**

On June 25, 2008, the Internal Revenue Service revised Notice 2008-55, originally issued on June 13, 2008, relating to liquidity-protected preferred stock issued by closed-end funds.

In the original version of Notice 2008-55, the IRS had announced that if liquidity-protected preferred stock of such funds met certain criteria, the IRS would not challenge the characterization of the liquidity-protected preferred stock as equity for federal income tax purposes even if a put to the issuing fund, an affiliate, or a nonaffiliate were included in the structure. The IRS also noted that it would not challenge the equity status of interests in a liquidating partnership that aggregates auction-rate preferred stock if certain requirements set forth in the Notice were satisfied.

In revising Notice 2008-55, the IRS eased several important requirements of the minimum criteria that closed-end funds and liquidating partnerships must satisfy in order to obtain the protection of the Notice. The Notice's other requirements, and the effective date and grandfathering restrictions, remain in force in the revised version of the Notice.

The material changes to the terms of the original Notice include:

A. *Fund Must Invest "Predominantly" (Not "Exclusively") in Debt Instruments*

Under the revised Notice, a closed-end fund (operated as a regulated investment company) with liquidity-protected auction-rate preferred stock need only invest "predominantly" in debt instruments, with its other investments needing to be incidental to its business of investing in debt instruments. The original Notice had required that a closed-end fund invest "exclusively" in debt instruments to be within the scope of the Notice.

B. *Right to Require Repurchase by Fund After "Six Months" (Not "One Year")*

Under the revised Notice, the liquidity provider must hold auction-rate preferred stock purchased under a liquidity facility for a minimum continuous period of six months (rather than one year as required in the original Notice) before exercising a required redemption or repurchase by the fund or a related party.

C. *Triggering Event May Occur Two Auction Dates Prior to the "Termination Date" (Not "Stated Expiration Date") of Liquidity Facility*

The revised Notice describes liquidity facilities for auction-rate preferred stock that provide holders with a tender option to sell the preferred stock to a liquidity provider at a price equal to

the stock's liquidation preference, plus accrued but unpaid dividends, if one of two "trigger events" occurs: (1) a failed auction or remarketing; or (2) a failure to renew, replace, or extend an existing liquidity facility then in place with the same liquidity provider or another liquidity provider by a date that occurs at least two auction or remarketing dates before the "termination date" of the existing liquidity facility then in place. The original version of the Notice referred to the "stated expiration date" rather than the "termination date" of the relevant facility.

D. Liquidating Partnerships "Must Reasonably Expect" to (Not "Must") Be Invested 95 Percent in Auction-Rate Preferred Stock or in "Proceeds" from Dispositions Thereof

Regarding the use of liquidating partnerships to accumulate interests in closed-end fund auction-rate preferred stock, the revised Notice requires that such a partnership "must reasonably expect" that at least 95 percent of its assets will consist of auction-rate preferred stock meeting certain requirements as well as temporary investments of proceeds received from the disposition of such auction-rate preferred stock pending the redemption of partnership interests. In the original Notice, the 95 percent investment minimum had to be maintained, not just reasonably expected to be maintained. Also, the original Notice did not specifically include proceeds from dispositions of preferred stock as contributing toward the 95 percent minimum requirement.

As noted above, the other requirements of the original Notice, and the effective date and grandfathering restrictions, remain in force in the revised Notice.

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If you have any questions concerning the foregoing or would like additional information, please contact Rose DiMartino (212-728-8215, rdimartino@willkie.com), Margery K. Neale (212-728-8297, mneale@willkie.com), or P. Jay Spinola (212-728-8970, jspinola@willkie.com) on Investment Company Act issues; Thomas H. French (212-728-8124, tfrench@willkie.com) on liquidity provider issues; or James R. Brown (212-728-8287, jbrown@willkie.com), Richard L. Reinhold (212-728-8292, rreinhold@willkie.com), or Joseph A. Riley (212-728-8715, jriley@willkie.com) on tax matters. You may, of course, also contact the attorney with whom you regularly work.

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