



TaxNewsFlash

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Rev. Proc. 2020-34: Relief for mortgage loans, lease arrangements of certain trusts (COVID-19)

The IRS today released an advance version of Rev. Proc. 2020-34 to provide temporary relief under a safe harbor for arrangements treated as trusts holding rental real property that may be subject to a mortgage loan and is leased to tenants who are experiencing financial hardship as a result of the coronavirus (COVID-19) pandemic.

Rev. Proc. 2020-34 [PDF 65 KB] allows eligible trusts to make certain modifications to their mortgages loans or lease agreements, or to accept certain additional cash contributions, without jeopardizing their tax status as grantor trusts. Modifications to the mortgage assets or lease agreements and cash contributions that meet the safe harbor criteria will not be deemed to create a “power to vary” that would jeopardize grantor trust treatment under Reg. section 301.7701-4(c) and Rev. Rul. 2004-86.

In addition, the safe harbor provided by Rev. Proc. 2020-34 states that a cash contribution from one or more new trust interest holders—to acquire a trust interest or a non-pro rata cash contribution from one or more current trust interest-holders—is to be treated as a purchase and sale under section 1001, of a portion of each non-contributing (or lesser contributing) trust interest-holder’s proportionate interest in the trust’s assets.

Rev. Proc. 2020-34

According to today’s release, the IRS and Treasury Department have received comments from trusts that hold rental real property, and that are experiencing financial difficulties from the COVID-19 situation. According to the comments, trustees report they may find it necessary to:

- Respond to the COVID-19 financial hardship of their tenants by modifying the trust’s real property leases with the tenants to defer or waive rent payments;
- Request relief under various forbearance programs with respect to debt service on the mortgage loan secured by the trust’s real property; and
- Accept additional cash contributions in order to avoid default on the trust’s loan obligations, to satisfy lender demands on which receiving a loan modification may be contingent, to pay trust expenses, or to bolster trust reserves for the payment of expenses and loan payments.

Depending on the circumstances for a particular trust, these contributions may come pro-rata from current trust interest-holders, non-pro rata from these current interest-holders, or from outside investors.

To afford temporary relief, Rev. Proc. 2020-34 provides a “safe harbor” for Delaware statutory trusts that hold real property subject to a lease and for other trusts formed under the equivalent law of other states or the District of Columbia. The safe harbor is stated as applying to arrangements that are fixed investment trusts holding rental real property that are treated as grantor trusts under Reg. section 301.7701-4(c) and Rev. Rul. 2004-86 and that engage in one or more of the safe harbor actions described in the following measures of Rev. Proc. 2020-34:

- Section 6.02 (defining the allowable mortgage loan modifications)
- Section 6.03 (defining the allowable lease modifications)
- Section 6.04 (defining the allowable cash contributions)

The safe harbor in Section 6.02 allows for a modification of one or more mortgage loans that secure the trust’s real property in certain forbearance actions. The allowable modifications must be performed either as: (1) an allowable modification following forbearance under Section 4022 or 4023 of the *Coronavirus Aid, Relief, and Economic Security Act of 2020* (CARES Act); or (2) an allowable modification following forbearance as described in Section 2.07 of Rev. Proc. 2020-26 that the trust requested or agreed to between March 27, 2020 (the date of enactment of the CARES Act) and December 31, 2020, and that were granted as a result of the trust experiencing financial hardship as a result of the COVID-19 emergency.

In addition, the safe harbor in Section 6.03 of Rev. Proc. 2020-34 allows for a modification of one or more real property leases (including modifications to the specific allocations of fixed rent in the lease agreements) for leases entered into by the trust on or before March 13, 2020, provided the modifications were requested and agreed to on or after March 27, 2020, and on or before December 31, 2020. The reason for the modifications must be to coordinate the lease cash flows with certain cash flows, or to defer or waive one or more tenants’ rental payments for any period between March 27, 2020, and December 31, 2020, because the tenants are experiencing a financial hardship due to the COVID-19 situation. Special considerations are defined for leases subject to section 467.

The safe harbor in Section 6.04 of Rev. Proc. 2020-34 is also available regarding cash contributions that are made between March 27, 2020, and December 31, 2020, as a result of the trust experiencing financial hardship due to the COVID-19 emergency, provided the contribution must be needed to increase permitted trust reserves, to maintain trust property, to fulfill obligations under mortgage loans, or to fulfill obligations under real property leases.

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