

02.20.09

THE TAX GROUP

at Brownstein Hyatt Farber Schreck

Cancellation of Debt Relief in the American Recovery and Reinvestment Act of 2009

On February 17, 2009, in Denver, Colorado, President Obama signed into law the American Recovery and Reinvestment Act of 2009 (the "ARRA"). The ARRA is one of the largest pieces of legislation in U.S. history.

One of the most significant tax incentives for businesses is a deferral of cancellation of debt income ("CODI") from the reacquisition of a debt instrument. Members of the firm's Government Relations Group were instrumental in obtaining the CODI relief that was enacted as part of ARRA. It has been hailed by business leaders and chambers of commerce as a critical tool to the economic recovery.

Under prior law, if a taxpayer or a related party acquired debt of the taxpayer at a discount, the taxpayer would immediately recognize ordinary income equal to the amount of the debt discharged, absent a statutory exclusion. ARRA allows certain businesses to defer the recognition of income arising from discharge of indebtedness.

The deferral is available for any debt instrument issued by a corporation or issued by any other person in connection with the conduct of a trade or business by such person. For purposes of the provision, a "debt instrument" is broadly defined to include any bond, debenture, note, certificate or any other instrument or contractual arrangement constituting indebtedness.

The debt instrument must be reacquired in 2009 or 2010 by the debtor (or a related party) which issued (or otherwise is the obligor under) the debt instrument. The debt can be acquired for cash, in exchange for another debt instrument, in exchange for corporate stock or a partnership interest or the contribution of the debt instrument to capital. If acquired for another debt instrument which has original issue discount (OID), deductions with respect to the OID are generally deferred to the periods that the CODI is included in income.

If elected by the taxpayer the CODI is deferred until 2015 and then included in gross income ratably over the next 5 years. The election must be made by including a statement with the tax return for the year in which the debt was reacquired. In the case of a partnership, corporation or other pass through entity, the election is made at the entity level. If the election is made, other exclusions to CODI do not apply to the debt instrument.

CODI and any related deduction for OID that is deferred by an electing taxpayer (and has not previously been taken into account) generally is accelerated and taken into income in the

Always There

taxable year in which the taxpayer: (1) dies, (2) liquidates or sells substantially all of its assets (including a title 11 or similar case), (3) ceases to do business, or (4) is in similar circumstances. In the case of a pass thru entity, CODI is accelerated if the holder disposes of its interest in the entity.

There are special rules for partnerships prescribing how any income or deduction deferred under the provision is to be allocated among partners. Additionally, there is a special rule to shield partners from gain arising from a decrease in a partner's share of liabilities as a result of the discharge of debt. Any decrease in liabilities is taken into account by the partner at the same time, and to the same extent, as the CODI is recognized.

This document is intended to provide you with general information about the Emergency Economic Stabilization Act of 2008. The contents of this document are not intended to provide specific legal advice. If you have any questions about the contents of this document or if you need legal advice as to an issue, please contact the attorney listed below or your regular Brownstein Hyatt Farber Schreck, LLP attorney. This communication may be considered advertising in some jurisdictions.

Albuquerque Office 201 Third Street NW Suite 1700 Albuquerque, NM 87102 T 505.244.0770 Timothy R. Van Valen	Denver Office 410 Seventeenth Street Suite 2200 Denver, CO 80202 T 303.223.1100 Gregory W. Berger Andrew C. Elliott Irene F. Gallagher Neil M. Goff Marybeth K. Jones Nancy A. Strelau	Las Vegas Office 100 City Parkway Suite 1600 Las Vegas, NV 89106 T 702.382.2101 Andrew S. Brignone Jason S. Jeskey Adam P. Segal	Santa Barbara Office 21 East Carrillo Street Santa Barbara, CA 93101 T 805.963.7000 Steven Jung Michelle Lee Pickett Christine E. Ray George G. Short	Washington, DC Office 1350 I Street, NW Suite 510 Washington, DC 20005 T 202.296.7353 Michael B. Levy
--	---	--	---	--

©2009 Brownstein Hyatt Farber Schreck, LLP. All Rights Reserved.