Some Information to Consider
Regarding the Tax Treatment of S.Crow Collateral Corp.'s
Monetized Installment Sale Transactions

A competent analytical framework for determining what a seller's tax treatment should be upon entering into a monetized installment sale transaction with S.Crow Collateral Corp. has two general components, as follows:

1. As an intermediary installment sale transaction; and
2. As a monetized installment sale transaction.

S.Crow Collateral Corp.'s Role as a Qualified Intermediary

This analytical component is present, because S.Crow Collateral Corp. is an intermediary in the transaction; S.Crow Collateral Corp. purchases from the seller and simultaneously re-sells to a subsequent purchaser, who otherwise (in most instances) would have purchased directly from the seller. Upon execution of the installment agreement, S.Crow Collateral Corp. acquires equitable ownership rights to the asset. Upon the resale, those pass to the subsequent buyer.

Temp. Treas. Reg. 26 CFR 15a.453-1(b)(3)(i), explicitly provides that an installment seller to a qualified intermediary such as S.Crow Collateral Corp. is not deemed to be in constructive receipt of the sale proceeds which the intermediary receives. The Regulation—which applies only to installment sale situations—reads in pertinent part as follows:

> For a special rule regarding a transfer of property to a qualified intermediary followed by the sale of such property by the qualified intermediary, see § 1.1031(k)-1(j)(2)(ii) of this chapter.

That § 1.1031(k)-1(j)(2)(ii) states the following:

> **(ii) Qualified intermediaries.** Subject to the limitations of paragraphs (j)(2) (iv) and (v) of this section, in the case of a taxpayer's transfer of relinquished property involving a qualified intermediary, the determination of whether the taxpayer has received a payment for purposes of section 453 and § 15a.453-1(b)(3)(i) of this chapter is made as if the qualified intermediary is not the agent of the taxpayer.

So, the analysis turns to this question: Does S.Crow Collateral Corp. function as a qualified intermediary in its installment transaction with a seller?

Treas. Reg. 26 CFR 1.1031(k)-1(g)(4)(iii) provides the definition of a "qualified intermediary", which, according to that Regulation, has three components:

1. The intermediary is not the taxpayer or a disqualified person (such as a person who has acted as the taxpayer's employee, attorney, accountant, investment banker or broker, or real estate agent or broker within the previous two years), per Treas. Reg. 26 CFR 1.1031(k)-1(k)); and

2. The intermediary enters into a written agreement with the taxpayer under which the intermediary acquires the relinquished property from the taxpayer and transfers the relinquished property; and

3. The intermediary enters into a written agreement with the taxpayer under which the intermediary acquires replacement property and transfers the replacement property to the taxpayer.

Under Treas. Reg. 26 CFR 1.1031(k)-1(g), it is not necessary that the intermediary be the one who conveys legal title, if the taxpayer's rights are assigned to the intermediary and the transfers occur pursuant to an agreement to which the intermediary is a party or an agent of a party.

S.Crow Collateral Corp.'s transactions satisfy all three components. S.Crow Collateral Corp. is never the selling taxpayer and is never a disqualified person. Every installment contract provides for S.Crow Collateral Corp. to acquire the asset from the taxpayer and re-sell it. Each of S.Crow Collateral Corp.'s monetized installment transactions requires S.Crow Collateral Corp., at the seller's direction, to arrange for a replacement asset and its transfer to the seller, either (a) by explicit exchange language in the documents or (b) by arrangement for the funding for the acquisition and transfer, or both.

It is not our place to speak about whether our competitors satisfy the requirements of the Regulations.

S.Crow Collateral Corp.'s Monetized Installment Sale Transactions

Anyone who seeks to know whether a particular monetized installment sale transaction would permit the seller to defer the tax on the gain under Section 453 of the *Internal Revenue Code* must begin with Section 453A(d), which states in part as follows:

> **(d) Pledges, etc., of installment obligations**
> **(1) In general**
> For purposes of section 453, if any indebtedness (hereinafter in this subsection referred to as "secured indebtedness") is secured by an installment obligation to which this section applies, the net proceeds of the secured indebtedness shall be treated as a payment received on such installment obligation . . .
> **(4) Secured indebtedness**
> For purposes of this subsection indebtedness is secured by an installment obligation to the extent that payment of principal or interest on such indebtedness is directly secured (under the terms of the indebtedness or any underlying arrangements) by any interest in such installment obligation. A payment shall be treated as directly secured by an interest in an installment obligation to the extent an arrangement allows the taxpayer to satisfy all or a portion of the indebtedness with the installment obligation.

One's analysis then turns to how the most widely known monetization-loan transaction was treated. That was the one described in the 2012 Internal Revenue Service Chief Counsel Memorandum 20123401F, found at https://www.irs.gov/pub/irs-lafa/20123401F.pdf.

In that Chief Counsel Memorandum, the IRS based its analysis on Sections 453 and 453A. The IRS also considered the step-transaction and form-over-substance doctrines but found them not to be applicable, because the parties dealt at arms-length with one another, all parties considered the loan transaction to be a real transaction, and anyway tax deferral was permitted for a monetized installment sale which complied with Section 453A(d).

We cannot speak for others who do monetized installment sale transactions, but in the case of S.Crow Collateral Corp.'s monetized installment sale transactions the monetization lender has no right or interest whatever in, to or under the installment agreement or the installment obligation; the lender is given no pledge or security in the installment obligation; and the monetization lender is not allowed to use the installment obligation to satisfy all or any portion of the indebtedness to the lender. Further, S.Crow Collateral Corp. does not make any payment to the lender on the installment seller's debt to the lender; every payment to the monetization lender is made by the borrower (who is usually, but not always, the installment seller), and if the borrower does not do so, the monetization lender has no right to collect that money from S.Crow Collateral Corp.

The Chief Counsel Memorandum does not say whether the buyer in that monetized installment sale transaction was an intermediary, but it's highly likely that the buyer was indeed an intermediary; the Memorandum does not say that the buyer ever took or retained possession or title, and the buyer was free to re-sell the property immediately.

The installment sale in the Chief Counsel Memorandum situation was of agricultural property, but the only relevance of that fact was that with agricultural property Section 453A(b)(3)(B) makes it permissible (notwithstanding Section 453A(d)) for the seller to give the lender a lien on the installment contract without causing the seller to lose tax deferral. The Chief Counsel's analysis was that tax deferral for an installment seller's monetization loan that does not violate the "pledge rule" of Section 453A(d)—whether because of the Section 453A(b)(3)(B) exception for agricultural property or because of the lack of any pledge at all—was "a permitted result under I.R.C. §§ 453 and 453A".

Disclaimer

Nothing in this paper is intended to be, or may be taken to be, tax, legal or investment advice. Interested parties should consult their legal, tax and investment advisers before participating in any transaction.