

**Internal Revenue Service**

Department of the Treasury  
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Refer Reply To:  
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March 17, 2009

Legend

Fund =

Dear :

This responds to a letter, submitted on behalf of Fund, requesting a ruling that the proposed transactions will be covered under Notice 2008-55, 2008-27 I.R.B. 11, issued June 13, 2008 (“the Notice”) and that the Service will not challenge the equity characterization of the auction rate preferred stock at issue. The material information is summarized below.

The Fund is a closed-end management company that has elected to be taxed as a regulated investment company (“RIC”), as defined under section 851 of the Internal Revenue Code. Assets of the Fund consist predominantly of debt instruments generating interest exempt from Federal income tax and other investments that are incidental to the Fund’s business of investing in such debt instruments.

There are two classes of Fund stock outstanding, a single class of auction rate preferred stock (“Current Preferred”) and a single class of common stock. It is Fund’s intention to redeem the Current Preferred using the net proceeds from the issuance of a new class of preferred stock referred to as “variable rate demand preferred” (“VRDP”). Unlike the Current Preferred, the VRDP will offer its holders the benefit of a liquidity

facility, which will make it more attractive to investors and in particular money market funds. Money market funds cannot hold the Current Preferred stock because it lacks the requisite liquidity features necessary to enable it to qualify as an eligible security for purchase by money market funds under the Securities and Exchange Commission's ("SEC") Rule 2a-7, 17 C.F.R. 270.2a-7, issued under the Investment Company Act of 1940.

A bank or other financial institution ("the Bank") will provide the liquidity facility. In order to engage the Bank to act as the liquidity provider for the VRDP, the Fund believes that it will need to make the modifications described below to the terms of the VRDP, as compared to the Current Preferred.

Currently, the Fund is required by the terms of its charter to redeem the Current Preferred if the "asset coverage ratio" (that is, the ratio of the value of the Fund's assets to the aggregate liquidation preference of the Current Preferred) falls below 200% and remains below 200% for longer than a designated cure period (in addition, issuers of auction rate preferred stock are required to maintain asset coverage requirements imposed by nationally recognized statistical rating organizations). The amount of Current Preferred that must be redeemed is at least the amount needed to restore the asset coverage ratio to 200%. Shares of Current Preferred that are redeemed for this purpose are selected randomly, by lot, by the Fund from among all the shares of Current Preferred outstanding.

The Bank negotiating with the Fund has asked for a higher asset coverage ratio (between 200% and 250%, inclusive, depending on market conditions at the time the VRDP is issued), with such provisions remaining in effect so long as the Bank acts as the liquidity provider. The Fund believes that other liquidity providers may also require the Fund to maintain an asset coverage ratio in that range, depending on market conditions at the time the VRDP is issued.

Section 3.6 of the Notice imposed certain conditions on any contractual rights of a liquidity provider to require redemption or repurchase of stock by the issuer, including a requirement that the liquidity provider must hold auction rate preferred stock purchased under a liquidity facility for a minimum continuous holding period of at least six months before any redemption or repurchase of such stock by the issuer or a related party to the issuer. As described in section 2.1 of the Notice, auction rate preferred stock, in general, is mandatorily redeemable in certain circumstances, including upon a failure to meet asset coverage requirements, and optionally redeemable by the issuer at any time. As a result of the increased asset coverage ratio required by the Bank, it will be more likely that the Bank, as the liquidity provider, will not hold the VRDP for six months. However, in this circumstance, any redemption would not be the result of the Bank exercising a contractual right to demand that the VRDP be redeemed, the Fund would make the determination when, and if, a redemption would be made. Also, since

any VRDP redeemed for the purpose of maintaining asset coverage ratios would be selected randomly, by lot, no holder of VRDP would necessarily have its shares redeemed. The requirement that the liquidity provider hold the auction rate preferred stock for six months applies to the situation where the liquidity provider has a contractual right to demand that the issuer redeem its shares and does not apply to redemptions that are made by the Fund in order to maintain asset coverage ratios or to optional redemptions (i.e., redemptions at the option of the Fund). An optional redemption will occur only in compliance with state law, which requires the board to determine that such redemption is in the best interest of the Fund, and the Investment Company Act, which, among other things, requires, pursuant to Rule 23c-2 adopted by the SEC, that any redemption by a registered closed-end investment company, such as the Fund, be made by lot, on a pro rata basis, or in such other manner as will not discriminate unfairly against any holder of the securities of the class or series.

It is expected that each share of VRDP will have a fixed liquidation preference, such as \$25,000 or \$100,000, and a dividend rate that will be reset periodically, ordinarily every seven days. VRDP shareholders will have the option at any time to tender their VRDP for remarketing at a price equal to the liquidation preference of the VRDP plus accumulated but unpaid dividends (the "Purchase Price") on a specified purchase date (the "Purchase Date"). The Purchase Date will be any business day that is not less than seven days after the VRDP shareholder delivers a notice of tender. In addition, the VRDP will be subject to mandatory tender for remarketing by the remarketing agent at the Purchase Price upon: (a) a failure by the Fund to make a scheduled payment of dividends on the VRDP; (b) a failure by the Bank to maintain short-term debt ratings in one of the two highest ratings categories; (c) a failure by the Fund to pay the Bank any liquidity fee due in advance by seven business days before the start of the month to which the fee relates; (d) the fifteenth day prior to the occurrence of an "extraordinary corporate event" with respect to the Bank; (e) the Fund having obtained a liquidity facility with a party other than the Bank, subject to the right of the VRDP holders to opt out; or (f) the Fund having provided notice of a proposed special rate period (that is, a rate period greater than seven days), subject to the right of the VRDP holders to opt out. An "extraordinary corporate event" with respect to the Bank means a dissolution of the Bank. It also means the consolidation or merger of the Bank into another entity or the transfer of all or substantially all of the assets of the Bank to another entity unless before the consolidation, merger or transfer the Bank confirms that the surviving entity or transferee (a) will assume all of the Bank's obligations under the liquidity facility and (b) have short-term debt ratings in one of the two highest categories.

Based on its experience and discussions with investors, the Fund believes that the mandatory tender events described above represent situations in which VRDP holders will want to dispose of their VRDP and will ordinarily do so through the remarketing mechanism. Based on market conditions and investment conditions, other mandatory tender events may be included in the terms of the VRDP at the time it is issued. By making these situations mandatory tender events, the Fund is assuring the investors that their shares will be remarketed in these situations whether or not the investors are

aware that situations have occurred. Investors are free to opt out of the mandatory tender in certain instances and are free to re-acquire the remarketed shares in others.

In each case, the remarketing agent will use its best efforts to remarket any VRDP shares tendered. A remarketing “fails” to the extent that any VRDP shares tendered for remarketing remain unsold on the Purchase Date, in which case the VRDP shares will be delivered to the Bank for purchase under the liquidity facility. In addition, all outstanding VRDP shares must be tendered to and purchased by the Bank upon a failure to renew, replace, or extend the liquidity facility either with the Bank or another liquidity provider at least 15 days before the liquidity facility is scheduled to terminate. All current and future holders of VRDP will be designated third-party beneficiaries of the liquidity facility and will have the right to enforce the liquidity facility directly against the Bank.

Even if the Bank purchases VRDP pursuant to the liquidity facility, efforts to remarket the VRDP (including both shares tendered by investors and shares purchased by the Bank) will continue. If the Bank holds any share of VRDP for a continuous period of six months, however, the Bank may require the Fund to redeem or repurchase that share of VRDP at a price equal to the Purchase Price. Redemptions and repurchases of the Bank’s VRDP by the Fund will be subject to the state law restrictions applicable to all stock redemptions and repurchases.

Fund has made the following representations in connection with its request for rulings:

- (a) Except for the special redemption right provided to the Bank to require the Fund to redeem or repurchase VRDP that it has held for a continuous period of six months, neither the Bank nor any subsequent holder of the VRDP will have any greater rights with respect to the VRDP than other holders of the VRDP under the terms of the liquidity facility, the terms of the VRDP, or state law.
- (b) Fund is an Eligible Issuer, as defined in § 2.1 of the Notice. The Current Preferred has been outstanding since before February 12, 2008.
- (c) The Fund may pay dividends on the VRDP only if the Fund duly declares the dividends and pays them out of legally available funds, as provided under applicable state law.
- (d) Before the Bank purchases any VRDP under the liquidity facility, it will not be related to the Fund such that any loss realized on a sale of property by the Bank to the Fund will not be disallowed under section 267(b) or section 707(b) of the Code.
- (e) The Bank provides the holders of VRDP a tender option or right to sell their stock to the Bank only if one of the following two trigger events occurs: (1) a

- failed auction or remarketing; or (2) a failure to renew, replace, or extend the existing liquidity facility then in place with the Bank or another liquidity provider by a date that occurs at least 15 days before the termination date of the existing liquidity facility.
- (f) The contractual rights that the Bank has to require the Fund to redeem or repurchase stock purchased by the Bank under the liquidity facility are limited by applicable state law restrictions on redemptions of stock that apply to any holder of the VRDP.
  - (g) The bank negotiating with the fund has asked for a higher asset coverage ratio (between 200% and 250%, inclusive, depending on market conditions at the time the VRDP is issued), with such provisions remaining in effect so long as the bank acts as the liquidity provider. Except for any redemption by the fund of VRDP held by the bank that is necessary to restore the specified asset coverage ratio, or otherwise to maintain asset coverage requirements imposed by nationally recognized statistical rating organizations, or in connection with an optional redemption (in the case of any of the foregoing, which redemption would be made from all outstanding VRDP, not just VRDP held by the bank), the bank will hold the VRDP for a minimum continuous holding period of at least six months.
  - (h) An optional redemption will occur only in compliance with state law, which requires the board to determine that such redemption is in the best interest of the Fund, and the Investment Company Act, which, among other things, requires, pursuant to Rule 23c-2 adopted by the SEC, that any redemption by a registered closed-end investment company, such as the Fund, be made by lot, on a pro rata basis, or in such other manner as will not discriminate unfairly against any holder of the securities of the class or series.
  - (i) Based on its experience and discussions with investors, the Fund believes that the mandatory tender events represent situations in which VRDP holders will want to dispose of their VRDP and will ordinarily do so through the remarketing mechanism. Based on market conditions and investment conditions, other mandatory tender events may be included in the terms of the VRDP at the time it is issued. By making these situations mandatory tender events, the Fund is assuring the investors that their shares will be remarketed in these situations whether or not the investors are aware that situations have occurred. Investors are free to opt out of the mandatory tender in certain instances and are free to re-acquire the remarketed shares in others.
  - (j) In each case, the remarketing agent will use its best efforts to remarket any VRDP shares tendered through the mandatory tender mechanism.

- (k) All current and future holders of VRDP will be designated third-party beneficiaries of the liquidity facility and will have the right to enforce the liquidity facility directly against the Bank.

Based on the information supplied and representations made by Fund, it is held as follows:

The requirement under section 3.6 of the Notice that the liquidity provider hold the auction rate preferred stock for six months before redemption only applies to redemptions that are made at the option of the liquidity provider pursuant to its contractual rights under the liquidity facility. The IRS will not challenge the equity characterization of the VRDP for Federal income tax purposes as a result of adding a liquidity facility, with the terms described herein if, otherwise, the conditions described in Notice 2008-55 are met.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. Specifically, no opinion is expressed regarding whether the Fund qualifies as a RIC.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Pursuant to the power of attorney on file in this office, a copy of this letter is being sent to your authorized representatives.

Sincerely,

*Alfred C. Bishop*  
Alfred C. Bishop, Jr.  
Branch Chief, Branch 6  
(Corporate)

cc: