TAXATION OF FINANCIAL INSTRUMENTS
Spring 2015
Omri Marian

General Information, Class Policies, First Day Assignments

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Class schedule and location: Wednesdays, 1:00 pm – 3:10 pm, room 355C.
Office hours: Mondays and Wednesdays, 3:10 pm – 4:30 pm, and by appointment.

Course objectives and structure

Financial instruments are present in our everyday lives (in our student loans, home-mortgage, car-leases and bank deposits, to name a few), and are an integral part of any commercial transaction (such as stock-purchase agreements, commercial loans, compensation plans, and securities offerings). The course is aimed at providing an overview of U.S. federal income taxation of financial instruments, including debt instruments, options, futures, forward, swaps and structured derivatives.

It is assumed that students have no prior knowledge in finance. We will therefore start with an Introductory Unit discussing the basic building blocks of financial instruments, their basic tax treatments, as well as the tax considerations at play. We will also practice basic Microsoft Excel skills, necessary for lawyers who practice taxation of financial instruments. No prior knowledge of Excel is necessary.

In Unit 1 we will explore the tax treatment of debt instruments. We will discuss the distinction between debt and non-debt instruments, concepts related to the time value of money such as original issue discount, market discount and bond premium. We will also discuss the tax treatment of certain types of structured debt instruments, such as contingent payment debt instruments and variable rate debt instruments.

Unit 2 will be dedicated to the tax treatment of financial derivatives such as options, forwards, futures, swaps and certain common types hybrid financial instruments that combine both equity and debt characteristics.

Unit 3 will address taxpayers’ use financial innovation to their advantage, as well as Congress’s and Treasury’s attempt to battle schemes that are perceived abusive. In this context we will explore issues relating to wash sales, short sales, constructive sales, straddles and hedging transactions.
Grading and Exam

90 percent of your grade in the course will be based on anonymously graded two and a half hour final examination. The exam will include 20 multiple choice questions; five of the questions will require you to briefly explain your choice of answer.

The exam will be open-book. You will be allowed to bring in any book (printed-form only!) as well as any self-prepared notes. Code and Treasury Regulations are also recommended (you will be allowed online access to the Code and Regulation thru Lexis, Westlaw, CCH IntelliConnect or RIA Checkpoint). Some of the questions may require the use of Microsoft Excel or a financial calculator (you may use which ever you prefer).

10 percent of your grade will be based on class participation, accorded at my discretion. Class participation grade must be earned. If you did not participate at all throughout the semester you should expect to get zero points for the participation component.

The College of Law grading policies can be found at: http://www.law.ufl.edu/student-affairs/current-students/academic-policies#9.

Texts

No textbook is required for this course. I will assign readings from two treatises that are available online (do not purchase these texts):

- Bittker & Lokken, Federal Taxation of Income, Estates & Gifts (B&L). This treatise is available online at RIA CheckPoint.
- Garlock, Federal Income Taxation of Debt Instruments (Garlock). This treatise is available online at CCH Intellicconnect.

Other course materials, TWEN access

Problem sets and additional reading materials will be provided through the course website on TWEN. It is essential that you register to the course website on TWEN as soon as possible. The password for the course website will be posted on the message board outside my office.

Class materials; Laptop/Tablet policy

Laptops are recommended. You are expected to have access to Microsoft Excel during class sessions. If you do not own a laptop, make sure you sit in class next to someone who does, so you can observe how Microsoft Excel is used. Please bring to each class the reading materials assigned. You should also have in-class access to the full set of the Code and Treasury Regulations.
Problems sets: Class preparation

Assignments may be discussed over the course of more than one class. The review of the assigned problems will, in most cases, be integrated with the lecture. Students are expected to discuss their proposed answers in class voluntarily, but I will cold-call to the extent necessary.

In case you are unprepared for class, and you are being called-on in class, you may pass the question. You are allowed a maximum of two passes during the semester without affecting your final grade. In case you are unprepared for class and prefer not to pass in the presence of your classmates, you may elect in advance to pass cold-calls by letting me know you are passing (by e-mail or in person) the morning of the day of the class. There is no need to provide an excuse. In such a case, I will not call you in class (such a pass will be counted, however, towards your two-pass limit). Passing more than two times during the semester will harm your class-participation component of the grade (meaning, in will reduce your earned participation grade). Wrong, yet at least minimally thoughtful answers will not harm your participation grade (but it is also likely they will not increase your participation grade). Wrong but thoughtful answers will be viewed favorably for purposes of the participation component.

Attendance

Attendance is mandatory. I will not verify attendance in class. However, if I notice your absence, it will be counted towards your two-pass limit. I will generally approve additional absences (that won’t be counted towards the two-pass limit) only in cases of job-interviews, confirmed sick days, or non-frivolous personal reasons. Advance notice will be appreciated.

Accommodations for students with disabilities

Students requesting classroom accommodation must first register with the Office of Disability Resources. The UF Office of Disability Resources will provide documentation to the student who must then provide such documentation to the Law School Office of Student Affairs when requesting accommodation.

First Day Assignment

Assignment 1 – this assignment will probably be discussed over the course of the first two to three classes

Topics covered:

- Introduction to the building blocks of financial instruments: debt, equity, forwards, futures, options and swaps.
- Introduction to basic tax considerations relating to financial instruments.
Class preparation:

- Code: (Skim all) §§ 163, 243, 385, 1271 – 1275; 1234; 1234A; 1234B; 1256(a), (b), (g)(1) & (7); 475(a), (b)(1)(A), (b)(2) & (c)(1).
- Regulations: (Skim all) § 1.1234-1 & -3. Skim §§ 1.446-3(c)(1)-(3);
- Problem Set A1 (will be posted on TWEN)

Future Assignments

Each assignment will be posted on TWEN at least a week prior to class discussion of the subject matter. However, for purposes of the completeness of the topics covered in the course, the tentative list of the assignments is as follows:

**Introductory Unit**

1. Assignment 1 (see supra) – The building block of financial instruments and their tax treatment in general.

**Unit 1**

2. Assignment 2 – Plain vanilla debt instruments: the debt/equity conundrum, interest, original issue discount (OID), acquisition premium, and how it all relates to the time value of money.
3. Assignment 3 – Structured-interest debt instruments: step-up notes; contingent payment debt instruments (CPDIs); variable rate debt instruments (VRDIs).
4. Assignment 4 – Secondary market transactions in debt instruments: sale and exchange of debt instruments; market discount; bond-premium; debt modifications.

**Unit 2**

5. Assignment 5 – Hybrid Instruments I: the combination of debt and options: options; investment units, convertible debt, reverse-convertible debt.
6. Assignment 6 – Hybrid Instruments II: the combination of debt and forwards: prepaid forwards, reveres convertibles and other structured instruments.

**Unit 3**

7. Assignment 7 – Anti abuse rules: wash sales, short sales, constructive sales and straddles.
8. Assignment 8 (time permitting) – Hedging transactions
9. Assignment 9 (time permitting) – Foreign currency transactions.