

January 6, 2004

New Tax Regulations Affect Confidentiality Agreements

In a March 7, 2003 memo, we recommended that the confidentiality provisions of most agreements be modified to exclude certain tax-related matters. This recommendation was prompted by regulations issued by the Internal Revenue Service as part of its efforts to eliminate abusive tax shelters. Under those regulations, participation in a "confidential transaction" resulted in reporting and record-keeping requirements, and we suggested that most parties would choose to avoid these burdens by expressly authorizing disclosure of tax treatment and tax structure.

Good news!! On December 29, 2003, the IRS issued new regulations that significantly change what is considered to be a "confidential transaction" for these purposes. Under the new regulations, the definition of a "confidential transaction" is limited to transactions in which an advisor who is paid a significant fee places a limitation on disclosure of the tax treatment or tax structure of the transaction. Confidentiality obligations that are imposed solely by the parties to a transaction will not cause a transaction to be a "confidential transaction" for purposes of these regulations. There is some uncertainty about how these new rules will be applied to transactions in which a participant is both an advisor and a principal, such as certain financial transactions in which a commercial bank or investment bank is both an advisor and a party to the transaction.

These new regulations are effective for transactions entered into on or after December 29, 2003, and they may also be relied on for transactions entered into on or after January 1, 2003 and before December 29, 2003. Accordingly, the tax confidentiality carve-out language that had become standard in commercial agreements is generally not needed. In addition, the failure to include the language (or the inclusion of ineffective language) in prior agreements should not have any adverse consequences.

If you have any questions concerning these new regulations, please contact Rick Bronstein or Peter Rothenberg.

1285 Avenue of the Americas
New York, New York 10019-6064
(212) 373-3000

1615 L Street, NW
Washington, DC 20036-5694
(202) 223-7300

Alder Castle, 10 Noble Street
London EC2V 7JU England
(44-20) 7367 1600

2, rue du Faubourg Saint-Honoré
75008 Paris, France
(33-1) 53.43.14.14

Fukoku Seimei Building 2nd Floor
2-2, Uchisawaicho 2-chome
Chiyoda-ku, Tokyo 100, Japan
(81-3) 3597-8120

Oriental Plaza, Tower E3, Suite 1205
No. 1 East Chang An Ave., Dong Cheng District
Beijing 100738, People's Republic of China
(86-10) 8518-2766

12th Fl., Hong Kong Club Building
3A Chater Road, Central
Hong Kong
(852) 2536-9933