

NASD**notice to members**

July 21, 1983

I M P O R T A N T**OFFICERS, PARTNERS AND PROPRIETORS**

TO: All NASD Members and Other Interested Persons

RE: Final Reporting Regulations Under the Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA")

Although it appears at this writing that the provisions under TEFRA with respect to withholding on dividends and interest will be repealed, members should be aware that other provisions of the Act - primarily the expanded reporting requirements - are still effective for transactions occurring after July 1, 1983.

The key provisions of the final regulations which were published earlier this year are summarized below and the text of the expanded reporting rules are also included in this notice.

INFORMATION REPORTING REQUIREMENTS FOR BROKER-DEALERS**TRANSACTIONAL REPORTING**

The final regulations require members to make an information return to the Internal Revenue Service with respect to the following:

What to Report

For transactions occurring on or after July 1, 1983:

- On a transactional basis, the gross proceeds of customers' sales (including short sales) of securities, commodities, and on closing transactions in forward contracts;

- On a transactional basis for each such sale, the name, address and taxpayer identification number, a description of the property sold, the CUSIP number, and such other information as may be required by Form 1099;
- On a transactional basis for each sale of a bond, the amount of interest which is accrued and unpaid; and,
- A statement (Form 1099 or equivalent) must be furnished to customers setting forth information reported to the IRS.

For the purposes of the above reporting requirements, the following definitions would apply:

Sale The term "sale" means any disposition of securities, commodities, regulated futures contracts, or forward contracts for cash and includes:

- retirements of indebtedness
- short sales

Securities The regulations define "securities" as:

- a share of stock in a corporation (foreign or domestic);
- a debt obligation;
- An interest in or a right to purchase any of the foregoing in connection with the issuance thereof from the issuer, an agent of the issuer or an underwriter;
- an interest in a trust;
- an interest in a partnership.

The term "securities" does not include options.

Gross Proceeds The term "gross proceeds" means the total amount paid or credited to a customer's account as a result of the sale less the amount of any accrued interest (which is reportable separately) and increased by any amount not so paid or credited by reason of repayment of margin loans. The broker may but is not required to take commissions, and options premiums into account in determining gross proceeds, provided the method chosen is consistent.

Sale Date A broker may report a sale as of trade or settlement date provided the method of reporting is consistent. A short sale, however, must be reported as of the date the short sale is entered on the books of the broker, i.e., trade date.

How to Report

The regulations specify that all information returns must be filed on computer readable magnetic media authorized by the Commissioner of the IRS. However, upon application to the IRS, a broker may be permitted to file information returns on Form 1099 if undue hardship is demonstrated. Such application for exemption from magnetic media reporting must be made to the IRS on or before September 15, 1983.

The regulations allow a broker to group its customers' accounts by some logical operational classification such as:

- department
- branch
- office
- other.

When to Report

Brokers are permitted to elect a monthly, quarterly or annual reporting period. Brokers may also send statements to their customers on the same basis or on any other basis without regard to the reporting period elected provided that all statements required to be furnished for a calendar year must be furnished on or before January 31st of the following calendar year.

Information returns shall be filed after the last calendar day of the reporting period elected and on or before the end of the second calendar month following the close of the calendar year of such reporting period.

EXCEPTIONS TO REPORTING REQUIREMENTS

An information return is not required on sales by a customer who is described in the regulations on withholding as an "exempt recipient." These include:

- Corporations;
- Tax-exempt organizations;
- IRA's;
- The United States or a respective state;
- Foreign governments or international organizations;
- Real estate investment trusts;
- A foreign central bank of issue;
- Investment companies registered under the Investment Company Act of 1940;
- Common trust funds;
- Nominees and custodians;

- Financial institutions, brokers and other intermediaries which collect interest or dividends for a payee or otherwise acts as a middleman between the payor and payee; and,
- Charitable remainder trusts which are tax exempt.

Individuals who might otherwise be exempt from withholding regulations are not exempt from these reporting regulations. In addition, no return of information would be required on sales at the issue price of interests in regulated investment companies that compute their current price per share for purposes of distributions, redemptions, and purchases so as to stabilize the price per share at a constant amount that approximates its issue price or the price at which it was originally sold to the public.

No reporting is required on the following payments:

- Non-transferable obligations (example: savings accounts, checking accounts and NOW accounts);
- Retirement of short term original issue discount;
- Callable obligations (that have no premium or discount);
- Obligations as to which the gross proceeds are reportable under other provisions of the law;
- Sales of foreign currency (other than a sale on a forward contract or regulated futures contract); and,
- Sales of a fractional share of stock if the gross proceeds on the sale of the fractional share are less than \$20.

In the case of redemptions of stock or retirement of securities, only the broker responsible for paying the holder, or crediting the gross proceeds to the customer's account has to report the sale.

TRANSITIONAL RULE

For reporting periods ending before January 1, 1984, a member in lieu of the transaction reporting noted above may report for each customer account:

- Name of the customer;
- Address;
- Taxpayer Identification Number;
- Aggregate gross proceeds of all sales of the account during the reporting period for which a return of information is required; and,
- Any other information required by Form 1099.

Additionally, such information may be submitted on hard copy Form 1099's for periods that end before January 1, 1984, or begin before 30 days after the date on which a timely filed request to file information returns on Form 1099 is denied by the IRS.

EFFECTIVE DATE

The regulations apply with respect to transactions occurring on or after July 1, 1983.

EXPANDED INTEREST AND ORIGINAL ISSUE DISCOUNT REPORTING

What to Report

The regulations provide generally that anyone who pays interest and certain middlemen (including broker-dealers) who receive interest on behalf of other persons must make an information return if the amount of interest paid to, or received on behalf of, such person aggregates \$10 or more during the calendar year.

"Interest" is defined in the regulations to include, among other things:

- Interest on an obligation;
- Interest on deposits left with broker-dealers;
- Any payment made in lieu of interest to a person whose obligation has been borrowed in connection with a short sale or other similar transaction; and,
- Interest paid on amounts held by investment companies or other pooled funds or trusts.

Interest excluded from the reporting requirements includes:

- Interest on an obligation issued by a natural person; and,
- Interest on any obligation if such interest is exempt from taxation.

For payments of interest (other than original issue discount), an information return must be made for the calendar year on Forms 1096 and 1099 which show:

- Aggregate amount of the payments;
- Name;
- Address;
- Taxpayer Identification Number; and,
- Any other information required by the forms.

ORIGINAL ISSUE DISCOUNT

As was previously noted in Notice to Members 83-10, the provisions of the proposed regulations with respect to original issue discount were perhaps the most complex and troublesome for members due to the lack of reference data on these instruments. As a result of comments to the IRS on the proposed regulations in this area by the NASD, SIA, and others, the Treasury Department announced in a news release, dated December 30, 1982, that the lack of information as to original issue discount obligations would be considered reasonable cause for failure to comply with the reporting requirements until December 31, 1983.

In the final regulations, the IRS announced that they would publish a list of publicly traded original issue discount obligations that may be relied on in determining the amount of original issue discount which would be subject to reporting. Beginning January 1, 1984, members may rely on the IRS's publication to determine whether an obligation is issued with original issue discount and the amount of original issue discount subject to reporting. These actions by the IRS will serve to substantially lessen the burden of reporting in this area.

Long term discount obligations in registered form are not included in the delayed reporting period as reporting on these obligations was required prior to TEFRA. Savings bonds are also not included since they are not considered by the IRS to be original issue discount obligations. For obligations issued at a discount and paying stated periodic interest, reporting on such interest is required at all times after December 31, 1982.

How to Report

Information returns must be made for the calendar year and must be filed on Forms 1096 and 1099. The regulations provide that returns may be made on a transactional basis if the interest payment is made on a U.S. Savings Bond, an interest coupon, short term original issue discount obligations or any other similar obligation. Magnetic media filing is permitted; however, such submission must conform to rules governing the submission of data in this form.

When to Report

Information returns with respect to interest reporting must be filed after September 30th of the reporting year and no later than February 28th of the following year. Members electing transactional reporting may report at any time but in no event later than February 28th of the year following the calendar year in which interest was paid. Returns shall be filed with the appropriate IRS Center, the address of which is listed in the instructions for Form 1096.

* * *

While repeal of withholding is anticipated, members should bear in mind that any compromise proposal probably will include an even further extension of reporting requirements and back-up withholding at the source for incorrect reporting or a failure to report. For example, currently under Sections 316 and 317 of TEFRA, if a taxpayer fails to provide or provides an obviously incorrect Taxpayer identification number, the person required to make an information return would be

required to withhold 15% of any amount required to be reported under the regulations including interest, dividends and gross proceeds. Members should familiarize themselves with these and other withholding provisions which may ultimately be imposed and assess their impact on their own operations.

Members who utilize outside service bureaus for recordkeeping purposes are urged to make contact with these agencies to ensure that systems are being developed to comply with these reporting requirements. Members who clear on a fully-disclosed basis should make arrangements with their clearing firms to insure that their reporting obligations are also fulfilled.

Questions concerning these regulations should be directed to the appropriate IRS contact person listed in the attached notices. For information returns of brokers, contact:


Gregory A. Roth at (202) 566-3238

For expanded interest and OID reporting, contact:

Diane L. Kroupa at (202) 566-3828

Please direct any questions covering this notice to James M. Cangiano, Assistant Director, Department of Policy Research, at (202) 728-8273.

Sincerely,



Gordon S. Macklin
President

Attachments

REGISTRATION

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[T.D. 7873]

Income Tax; Taxable Years Beginning After December 31, 1953; Information Returns of Brokers.

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations relating to information returns of brokers. Changes to the applicable tax law were made by the Tax Equity and Fiscal Responsibility Act of 1982. The regulations require brokers to make returns of information on dispositions (including short sales) of securities commodities, regulated futures contracts, and forward contracts effected for customers. They also require barter exchanges to make returns of information with respect to exchanges of property or services through the barter exchange. The regulations affect brokers effecting dispositions (including short sales) of securities, commodities, regulated futures contracts, and forward contracts, and barter exchanges, providing them with the guidance needed to comply with the law.

DATES: Effective on March 3, 1983.

The regulations apply with respect to transactions occurring on or after July 1, 1983.

FOR FURTHER INFORMATION CONTACT: Gregory A. Roth of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, Attention: CC:LR:T, 202-566-3238 (not a toll-free call).

SUPPLEMENTARY INFORMATION:

Background

On November 15, 1982, the Federal Register published proposed amendments to the Income Tax Regulations (26 CFR Part 1) under section 6045 of the Internal Revenue Code of 1954 (47 FR 51415). The amendments were proposed to provide rules relating to returns of brokers under

section 6045 of the Internal Revenue Code of 1954. Section 311 of the Tax Equity and Fiscal Responsibility Act of 1982 (96 Stat. 600) amended section 6045.

A public hearing was held on January 27, 1983. After consideration of all comments regarding the proposed amendments, those amendments are adopted as revised by this Treasury decision.

Explanation of Provisions

The final regulations generally require brokers to make returns of information with respect to sales by customers. In addition, barter exchanges are required to file returns of information on exchanges of property or services through the barter exchange if there are at least 100 such exchanges during the calendar year. The rules in the final regulations are substantially the same as the rules in the notice of proposed rulemaking, which are summarized in the preamble of the notice of proposed rulemaking. Several rules have been changed, however, in response to public comments received. These changes are summarized below.

Comments and Changes Due to Comments

A number of comments suggested that the regulations should permit reporting on an aggregate rather than a transactional basis. For reasons set forth below, the Internal Revenue Service believes that transactional reporting is necessary. The Service recognizes, however, that brokers would benefit from additional time to implement a transactional reporting system. Accordingly, the final regulations permit brokers and barter exchanges to elect aggregate reporting for calendar year 1983 and should provide brokers and barter exchanges with sufficient time to implement a transactional reporting system in a cost-efficient manner.

Transactional reporting is necessary, as a general rule, so that the amount received in a sale of property can be matched with the basis of the property to determine gross income. The Service received numerous comments suggesting that aggregate reporting would reduce the burden on reporters and should be adequate for the Service's needs. These comments were given careful

consideration. In the case of broker reports that provide only gross proceeds information, however, the Service's planned uses of the reports (selecting returns for correction processing under the information returns processing program, selecting returns for audit, implementing audits, and monitoring taxpayer compliance) generally require transactional data. Transactional data facilitates thorough, accurate, and cost-efficient audits.

In the case of transactions in regulated futures contracts, however, the Service has concluded that aggregate reporting may provide adequate information since such reporting generally provides sufficiently accurate gross income information. Accordingly, the final regulations provide special aggregate reporting requirements for regulated futures contracts. A broker is required to separately report such contracts annually and on an account-by-account basis. As to regulated futures contracts in each customer account, the broker must report the realized profit or loss during the year, the unrealized profit or loss at the end of the preceding year, the unrealized profit or loss at the end of the year, and the unadjusted taxable gain or loss for the year. The reporting rules were formulated solely taking into consideration the optimal form of reporting of commodities transactions in general and without regard to considerations of the tax treatment of options on futures.

The Service intends to monitor taxpayer compliance with respect to regulated futures contracts to determine whether aggregate reporting hampers enforcement efforts to reduce avoidance of tax. If abuses are detected, the Service will reconsider these special reporting rules for regulated futures contracts.

Several comments objected to the requirement in the proposed regulations that brokers and barter exchanges file returns of information on magnetic media. In general, the comments requested additional time to implement magnetic media reporting and suggested that requiring the use of magnetic media would impose an undue burden on brokers and barter exchanges that lack the necessary data processing capacity. The comments also suggested that the exemption for brokers with fewer than 250 customers and barter exchanges with fewer than 250 members or clients is of limited applicability.

The final regulations require magnetic media reporting, but not until calendar year 1984. The final regulations provide, as did the proposed regulations, that the Commissioner may waive the magnetic

media requirement on a showing of undue hardship. Existing brokers and barter exchanges must file an application for waiver on or before September 15, 1983; new brokers and barter exchanges will have at least two full months after becoming a broker or barter exchange to file an application for waiver. It is anticipated that the waiver authority will be exercised liberally so as not to unduly burden brokers and barter exchanges that lack both the necessary data processing facilities and cost-efficient access to computer service bureaus. This waiver policy will effect the relief that the exemption in the proposed regulations was intended to provide. Accordingly, these regulations do not include that exemption.

The proposed regulations provided that, for purposes of section 6045, a sale occurs on the date the customer becomes entitled to the gross proceeds thereof (settlement date). Comments received indicate that many brokers do not treat the settlement date as the sale date, but instead consider that a sale occurs on the date it is entered on the books of the broker (trade date). The final regulations allow a broker to report using either the settlement date or the trade date.

The proposed regulations required brokers to report the cost of property used to cover a short sale in the year of cover. A number of comments objected to this requirement because such cost information frequently is not available to the broker. In addition, this requirement was inconsistent with provisions of the regulations that required gross proceeds information with respect to other types of sales. The final regulations require brokers to report the amount received on the entry into the short sale in the year of entry. The Service recognizes that in situations where a short sale is not covered in the year of entry, the report by the broker under section 6045 will be made with respect to a year preceding the year in which the customer reports the sale for tax purposes.

The proposed regulations required brokers to report in terms of United States dollars the proceeds of a sale paid in a foreign currency directly or indirectly convertible into United States dollars, with conversion of the foreign currency into United States dollars at the exchange rate on the day of sale. Some brokers commented that it is difficult for them to determine what currencies are indirectly convertible. Additionally, some comments observed that there is no single exchange rate on a given day. Some comments expressed concern that the proposed regulations,

in effect, required brokers to keep dual records for all affected accounts: one in the foreign currency and another in United States dollars.

The Service needs reports in United States dollars to audit returns effectively. However, the Service recognizes the need to provide some flexibility. Consequently, the regulations provide simplified rules for foreign currency conversion. Conversion is required as to any directly convertible foreign currencies and as to any indirectly convertible currencies specified in a notice published in the Federal Register. Conversion may be at the exchange rate on the day of sale or on the last day of the reporting period. A broker may use generally recognized financial publications as a source for exchange rates.

The Service received a number of comments on the exemption provided in the proposed regulations for obligor payments on short-term obligations and certain types of accounts at financial institutions. Many of the comments requested clarification of the scope of the exemption. Other comments noted that certain similar transactions that have no tax effect or are already subject to reporting under provisions of the Internal Revenue Code other than section 6045 were not exempt under the proposed regulations.

To clarify the proposed exemption and to extend the exemption to debt transactions otherwise adequately reported or not likely to have tax effect, the final regulations exempt obligor payments on nontransferable obligations (including savings bonds, savings accounts, checking accounts, and NOW accounts), obligations as to which the entire gross proceeds are reported by the broker under provisions of the Internal Revenue Code other than section 6045, retirement of short-term obligations that have original issue discount, and retirement of book entry or registered form obligations as to which no interim transfers have occurred.

Comments received from depository trusts, dividend reinvestment plans, and similarly situated brokers noted that they frequently purchase or redeem fractional shares for various reasons. It is possible that the cost of reporting such transactions would be disproportionate compared to the potential tax on such transactions. In response to these concerns, the regulations provide an exemption for redemptions and repurchases of fractional shares for less than \$20.

Some comments requested that barter exchanges be allowed to report

exchanges in terms of trade credits rather than the cash equivalent of such credits. The Service is unable to use information reported in terms other than cash. Moreover, barter exchanges are better situated to convert credits into their cash equivalent than is the Service. Accordingly, this suggestion was not adopted.

Special Analyses

The Commissioner of Internal Revenue has determined that this rule is not a major rule as defined in Executive Order 12291. Accordingly, a Regulatory Impact Analysis is not required.

The Secretary of the Treasury certifies that the regulations in this document do not have a significant impact on a substantial number of small entities. Accordingly, a regulatory flexibility analysis is not required. The Secretary's certification is based on a determination that the economic impact of the reporting requirements is primarily attributable to requirements imposed directly by the statute. The Service has significant discretion under the statute to require reporting of information other than information regarding gross proceeds. In general, however, the regulations require only gross proceeds information, the reporting of which is expressly contemplated by the statute. As to the manner of reporting, the regulations obtain the information contemplated by the statute in a usable form with the minimum possible impact on small entities and the economy in general. The regulations require reports with respect to each transaction and require the use of magnetic media because alternative methods of reporting provide information in an unusable form and would not result in the improved compliance contemplated by Congress. In an effort to minimize the burdens on brokers, the regulations permit brokers to elect a monthly, quarterly, or annual reporting period. Brokers also may send statements to their customers on the same basis. Although the Service believes year-end statements to customers would contribute to significant improvements in taxpayer compliance, it recognizes the possibility that such a requirement would increase the burden imposed by the regulations. Finally, the impact of the regulations on small entities is minimized by certain exemptions.

Drafting Information

The principal author of these regulations is Gregory A. Roth of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal

Revenue Service and Treasury Department participated in developing the regulations on matters of both substance and style.

List of Subjects in 26 CFR 1.6001-1—1.6109-2

Income taxes, Administration and procedure, Filing requirements.

PART 1—[AMENDED]

Amendments to the Regulations

The amendments to 26 CFR Part 1 are as follows:

Paragraph. New § 1.6045-1 is added immediately after § 1.6044-5. The new section is set forth below.

§ 1.6045-1 Returns of information of brokers and barter exchanges.

(a) *Meaning of terms.* The following definitions apply for purposes of this section:

(1) The term "broker" means a person that, in the ordinary course of a trade or business during the calendar year, stands ready to effect sales to be made by others. (2) The term "customer" means, with respect to a sale effected by a broker, the person (other than such broker) that makes the sale, if the broker acts as—

(i) An agent for such person in the sale;

(ii) A principal in the sale; or

(iii) The participant in the sale responsible for paying to such person or crediting to such person's account the gross proceeds on the sale.

(3) The term "security" means—

(i) A share of stock in a corporation (foreign or domestic);

(ii) An interest in a trust;

(iii) An interest in a partnership;

(iv) A debt obligation;

(v) An interest in or right to purchase any of the foregoing in connection with the issuance thereof from the issuer or an agent of the issuer or from an underwriter that purchases any of the foregoing from the issuer, or

(vi) An interest in a security described in paragraph (a)(3) (i) or (iv) (but not including options or executory contracts that require delivery of such type of security).

(4) The term "barter exchange" means any person with members or clients that contract either with each other or with such person to trade or barter property or services either directly or through such person. The term does not include arrangements that provide solely for the informal exchange of similar services on a noncommercial basis.

(5) The term "commodity" means—

(i) Any type of personal property or an interest therein (other than securities as

defined in paragraph (a)(3)) the trading of regulated futures contracts in which has been approved by the Commodity Futures Trading Commission;

(ii) Lead, palm oil, rapeseed, tea, tin, or an interest in any of the foregoing; or

(iii) Any other personal property or an interest therein that is of a type the Secretary determines is to be treated as a "commodity" under this section, from and after the date specified in a notice of such determination published in the Federal Register.

(6) The term "regulated futures contract" means a regulated futures contract within the meaning of section 1256(b).

(7) The term "forward contract" means—

(i) An executory contract that requires delivery of a commodity in exchange for cash and which contract is not a regulated futures contract; or

(ii) An executory contract that requires delivery of personal property or an interest therein in exchange for cash, or a cash settlement contract, if such executory contract or cash settlement contract is of a type the Secretary determines is to be treated as a "forward contract" under this section, from and after the date specified in a notice of such determination published in the Federal Register.

(8) The term "closing transaction" means any termination of an obligation under a forward contract or a regulated futures contract.

(9) The term "sale" means any disposition of securities, commodities, regulated futures contracts, or forward contracts for cash, and includes redemptions of stock, retirements of indebtedness, and enterings into short sales. In the case of a regulated futures contract or a forward contract, the term "sale" means any closing transaction. When a closing transaction in a regulated futures contract involves making or taking delivery, the profit or loss on the contract is a sale, and, if delivery is made, such delivery is a separate sale. When a closing transaction in a forward contract involves making or taking delivery, the delivery is a sale without separation of the profit or loss on the contract from the profit or loss on the delivery, except that taking delivery for United States dollars is not a sale. The term "sale" does not include grants or purchases of options, exercises of call options, or enterings into contracts that require delivery of personal property or an interest therein.

(10) The term "effect" means, with respect to a sale, to act as—

(i) An agent for a party in the sale wherein the nature of the agency is such

that the agent ordinarily would know the gross proceeds from the sale; or

(ii) A principal in such sale.

Acting as an agent or principal with respect to grants or purchases of options, exercises of call options, or enterings into contracts that require delivery of personal property or an interest therein is not of itself effecting a sale. A broker that has on its books a forward contract under which delivery is made effects such delivery.

(11) The term "foreign currency" means currency of a foreign country.

(12) The term "convertible foreign currency" means a foreign currency that is either:

(i) Readily convertible into United States dollars; or

(ii) Of a type the Secretary determines is to be treated as a "convertible foreign currency," from and after the date specified in a notice of such determination published in the Federal Register.

(13) The term "cash" means United States dollars or any convertible foreign currency.

(b) *Examples.* The following examples illustrate the definitions in paragraph (a):

Example (1). The following persons generally are brokers within the meaning of paragraph (a)(1):

(i) A mutual fund, an underwriter of the mutual fund, or an agent for the mutual fund, any of which stands ready to redeem or repurchase shares in such mutual fund.

(ii) An obligor that regularly issues and retires its own notes.

(iii) A professional custodian (such as a bank) that regularly arranges sales for custodial accounts pursuant to instructions from the owner of the property.

(iv) A depository trust or other person who regularly acts as an escrow agent in corporate acquisitions, if the nature of the activities of the agent is such that the agent ordinarily would know the gross proceeds from sales.

(v) A stock transfer agent for a corporation, which agent records transfers of stock in such corporation, if the nature of the activities of the agent is such that the agent ordinarily would know the gross proceeds from sales.

(vi) A dividend reinvestment agent for a corporation that stands ready to purchase or redeem shares.

Example (2). The following persons are not brokers within the meaning of paragraph (1)(a) in the absence of additional facts that indicate the person is a broker:

(i) A stock transfer agent for a corporation, which agent daily records transfers of stock in such corporation, if the nature of the activities of the agent is such that the agent ordinarily would not know the gross proceeds from sales.

(ii) A person (such as a stock exchange) that merely provides facilities in which others effect sales.

(iii) An escrow agent or nominee if such

agency is not in the ordinary course of a trade or business.

(iv) An escrow agent, otherwise a broker, which agent effects no sales other than such transactions as are incidental to the purpose of the escrow (such as sales to collect on collateral).

(v) A floor broker on a commodities exchange, which broker maintains no records with respect to the terms of sales.

(vi) A corporation that issues and retires long-term debt on an irregular basis.

(vii) A clearing organization.

Example (3). A, B, and C belong to a carpool in which they commute to and from work. Every third day, each member of the carpool provides transportation for the other two members. Because the carpool arrangement provides solely for the informal exchange of similar services on a noncommercial basis, the carpool is not a barter exchange within the meaning of paragraph (a)(4).

Example (4). X is an organization whose members include retail merchants, wholesale merchants, and persons in the trade or business of performing services. X's members exchange property and services among themselves using credits on the books of X as a medium of exchange. Each exchange through X is reflected on the books of X by crediting the account of the member providing property or services and debiting the account of the member receiving such property or services. X also provides information to its members concerning property and services available for exchange through X. X charges its members a commission on each transaction in which credits on its books are used as a medium of exchange. X is a barter exchange within the meaning of paragraph (a)(4) of this section.

Example (5). A warehouse receipt is an interest in personal property for purposes of paragraph (a). Consequently, a warehouse receipt for a quantity of lead is a commodity under paragraph (a)(5)(ii). Similarly an executory contract that requires delivery of a warehouse receipt for a quantity of lead is a forward contract under paragraph (a)(7)(ii).

Example (6). The only customers of a depository trust acting as an escrow agent in corporate acquisitions, which trust is a broker, are shareholders to whom the trust makes payments or shareholdings for whom the trust is acting as an agent.

Example (7). The only customers of a stock transfer agent, which agent is a broker are shareholders to whom the agent makes payments or shareholdings for whom the agent is acting as an agent.

Example (8). D, an individual not otherwise exempt from reporting, is the holder of an obligation issued by P, a corporation. R, a broker, acting as an agent for P, retires such obligation held by D. Such obligor payments from R represent obligor payments by P. (See paragraph (c)(3)(v)). D, the person to whom the gross proceeds are paid or credited by R, is the customer of R.

(c) *Reporting by brokers—(1) Requirement of reporting.* Any broker shall, except as otherwise provided, report in the manner prescribed in this section.

(2) *Sales required to be reported.* Except as provided in paragraphs (c)(3),

(c)(5), (g), and (p)(1), a broker shall make a return of information with respect to each sale by a customer of the broker effected by the broker in the ordinary course of a trade or business in which the broker stands ready to effect sales to be made by others.

(3) *Exceptions—(i) Sales for exempt recipients.* No return of information is required with respect to a sale by a customer that is an exempt recipient described in section 3452(c)(2) (A) through (E) or (G) through (I) (relating to exemptions from withholding) as determined under § 35.3452(c)-1.

(ii) *Multiple brokers.* In the case of a sale in which a broker is instructed to initiate the sale by a person that is an exempt recipient described in section 3452(c)(2) (F) or (K)(i) (relating to exemptions from withholding) as determined under § 35.3452(c)-1, no return of information is required with respect to the sale by the broker so instructed. In the case of a redemption of stock or retirement of securities, only the broker responsible for paying the holder redeemed or retired, or crediting the gross proceeds on the sale to such holder's account, is required to report the sale.

(iii) *Custodians and trustees.* No return of information is required with respect to a sale effected by a custodian or trustee in its capacity as such, provided the sale is otherwise reported by the custodian or trustee on a properly filed Form 1041 and all Schedule K-1 reporting requirements are satisfied.

(iv) *Sales at issue price.* No return of information is required with respect to a sale of an interest in a regulated investment company (within the meaning of section 851) that computes its current price per share for purposes of distributions, redemptions, and purchases so as to stabilize the price per share at a constant amount that approximates its issue price or the price at which it was originally sold to the public.

(v) *Obligor payment on certain obligations.* No return of information is required with respect to payments representing obligor payments on—

(a) Nontransferable obligations (including savings bonds, savings accounts, checking accounts, and Now accounts);

(b) Obligations as to which the entire gross proceeds are reported by the broker of Form 1099 under provisions of the Internal Revenue Code other than section 6045 (including stripped coupons issued prior to July 1, 1982); or

(c) Retirement of short-term obligations, as defined in § 35.3455(b)-1 (b)(1), that have original issue discount.

as defined in section 1232(b)(1).

(vi) *Callable obligations.* No return of information is required with respect to demand obligations that also are callable by the obligor and that have no premium or discount.

(vii) *Foreign currency.* No return of information is required with respect to a sale of foreign currency other than a sale pursuant to a forward contract or regulated futures contract that requires delivery of foreign currency.

(viii) *Fractional share.* No return of information is required with respect to a sale of a fractional share of stock if the gross proceeds on the sale of the fractional share are less than \$20.

(ix) *Certain retirements.* No return of information is required from an issuer or its agent with respect to the retirement of book entry or registered form obligations as to which the relevant books and records indicate that no interim transfers have occurred.

(4) *Examples.* The following examples illustrate the application of the reporting requirements:

Example (1). A, an individual, places an order with B, a person generally known in the investment community to be a federally registered broker/dealer, to sell A's stock in a publicly traded corporation. B, in turn, places an order to sell the stock with C, a second broker, who executes the sale. B discloses to C the identity of the customer placing the order. C is not required to make a return of information with respect to the sale because C was instructed by B, an exempt recipient described in section 3452(c)(2)(F) and § 35.3452(c)-1(j), to initiate the sale.

Example (2). The facts are the same as in Example (1) except that B has an omnibus account with C so that B does not disclose to C whether the transaction is for a customer of B or for B's own account. C is not required to make a return of information with respect to the sale because C was instructed by B, an exempt recipient described in section 3452(c)(2)(F) and § 35.3452(c)-1(j), to initiate the sale.

Example (3). D, an individual not otherwise exempt from reporting, owns bonds that are held by E, a broker/dealer, in an account for D with E designated as nominee for D. Upon retirement of the bonds, the gross proceeds are automatically credited to the account of D. E is required to make a return of information with respect to the redemption because E is the broker responsible for making payment of the gross proceeds to D.

(5) *Form of reporting for regulated futures contracts—(i) In general.* A broker effecting closing transactions in regulated futures contracts shall report information with respect to regulated futures contracts solely in the manner prescribed in this paragraph (c)(5). In the case of a sale that involves making delivery pursuant to a regulated futures contract, only the profit on loss on the contract is reported as a transactions with respect to regulated futures contracts under this paragraph

(c)(5); such sales are, however, subject to reporting under paragraph (d)(2). The information required under this paragraph (c)(5) must be reported on a calendar year basis, unless the broker is advised in writing by an account's owner that the owner's taxable year is other than a calendar year and the broker elects to report with respect to regulated futures contracts in such account on the basis of the owner's taxable year. The following information must be reported as required by Form 1099 with respect to regulated futures contracts held in a customer's account:

(a) The name, address, and taxpayer identification number of the customer.

(b) The net realized profit or loss from all regulated futures contracts closed during the calendar year.

(c) The net unrealized profit or loss in all open regulated futures contracts at the end of the preceding calendar year.

(d) The net unrealized profit or loss in all open regulated futures contracts at the end of the calendar year.

(e) The aggregate profit or loss from regulated futures contracts $((b) + (d) - (c))$.

(f) Any other information required by Form 1099. See 17 CFR 1.33. For this purpose, the end of a year is the close of business of the last business day of such year. In reporting under this paragraph (c)(5), the broker shall make such adjustments for commissions that have actually been paid and for option premiums as are consistent with the books of the broker. No additional returns of information with respect to regulated futures contracts so reported are required.

(ii) *Examples.* The following examples illustrate the application of the rules in this paragraph (c)(5):

Example (1). On October 30, 1984, A, an individual who is a calendar year taxpayer not otherwise exempt from reporting, buys one March 1985 put on Treasury Bond futures (i.e. A purchases an option to enter into a short regulated futures contract of \$100,000 face value U.S. Treasury bonds). A pays \$500 for the option. On December 19, 1984, A, through B, exercises the option and enters into the futures contract. On February 15, 1985, A, through B, enters into a closing transaction with respect to the futures contract. These are A's only transactions in the account. Since B's books list A's regulated futures contract on December 31, 1984, B must report for A, for 1984, the unrealized profit or loss in the contract as of December 31, 1984. For 1985, B will report the same amount for A as the unrealized profit or loss at the beginning of 1985. The return of information for 1985 will also include the gain or loss from the contract in the net realized profit or loss from all regulated futures contracts sales during 1985.

Example (2). The facts are the same as in Example (1) except that A does not enter into the closing transaction, but instead, on March

20, 1985, B informs A that A will make delivery under the contract. On March 22, 1985, A does so; consequently, A becomes entitled to the gross proceeds. B enters the closing transaction on its books on March 20, 1985. In addition to the returns of information required by paragraph (c)(5), as described in Example (1), B must report the March 22, 1985 delivery as a separate transaction. B may use as the sale date for the delivery either March 20, 1985, the date the transaction is entered on the books of B, or March 22, 1985, the date A becomes entitled to the gross proceeds. B may not deduct the \$500 premium from the gross proceeds with respect to the March 22, 1985 delivery.

Example (3). The facts are the same as in Example (2) except that A buys a call on Treasury bond futures and takes delivery. B will supply the returns of information required by paragraph (c)(5), as described in Example (1). B is not required to make a return of information with respect to A's taking delivery.

Example (4). C, an individual who is a calendar year taxpayer not otherwise exempt from reporting, has an account with D, a broker. C trades both regulated futures contracts and forward contracts through C's account with D. D must report C's regulated futures contracts on an annual basis as required by paragraph (c)(5). With respect to C's forward contracts, D may elect to use the calendar month, quarter, or year as D's reporting period as provided in paragraph (c)(6).

(6) *Reporting periods and filing groups—(i) Reporting period—(a) In general.* A broker may elect to use the calendar month, quarter, or year as the broker's reporting period. A broker may separately elect a reporting period for each filing group.

(b) *Election.* For each calendar year, a broker shall elect a reporting period by filing Forms 1096 and 1099 in the manner elected. A different reporting period may be subsequently elected by filing in the manner subsequently elected, provided no duplication of reported transactions results.

(ii) *Filing group—(a) In general.* A broker may elect to group customers or customer accounts by office, branch, department or other method of operational classification and separately file Forms 1096 and 1099 for each filing group.

(b) *Election.* For each calendar year, a broker shall elect filing groups by filing Forms 1096 and 1099 in the manner elected. Different filing groups may be subsequently elected by filing in the manner subsequently elected, provided no duplication of reported transactions results.

(iii) *Example.* The following example illustrates the rules of this paragraph (c)(6):

Example. The A department of C, a broker, files a separate report for each month of 1984, whereas the B department of C files one report for all of 1984. C makes no other

reports or returns of information under section 6045 for 1984. C had thereby elected two filing groups for 1984, the A department and the B department. The A department has the calendar month as its 1984 reporting period, whereas the B department has the calendar year as its 1984 reporting period. The same result would occur if A and B were offices or branches of C.

(d) *Information required.*—(1) *In general.* A broker that is required to make a return of information under paragraph (c) during a reporting period shall report on a separate Form 1096 for each filing group, showing such information as may be required by Form 1096, in the form, manner, and number of copies required by Form 1096.

(2) *Transactional reporting.* As to each sale with respect to which a broker is required to make a return of information under this section, the broker, except as provided in paragraphs (c)(5) and (p)(1), shall show on Form 1099 the name, address, and taxpayer identification number of the customer, the property sold, Committee on Uniform Security Identification Procedures (CUSIP) number of the security sold (if known), the gross proceeds, sale date, and such other information as may be required by Form 1099, in the form, manner, and number of copies required by Form 1099.

(3) *Bond sales between interest payment dates.* As to each sale of a debt obligation prior to maturity with respect to which a broker is required to make a return of information under this section, a broker shall show separately on Form 1099 the amount of accrued and unpaid interest as of the sale date that must be reported by the customer as interest income under § 1.61-7(d) (but not the amount of any original issue or market discount). Such interest information shall be shown in the manner and at the time required by Form 1099 and section 6049.

(4) *Sale date.*—(1) *In general.* Except as otherwise provided in this paragraph (d) (4), a broker may report a sale as occurring on the date the sale is entered on the books of the broker of the date the customer becomes entitled to the gross proceeds thereof. The method of reporting the date the sale occurs shall be consistently applied by the broker as to all reports with respect to a filing group during a calendar year.

(ii) *Exception.* For purposes of this section, a broker shall report a short sale as occurring on the date the short sale is entered on the books of the broker.

(iii) *Example.* The following example illustrates the application of the rules in this paragraph (d)(4):

Example. C, an individual not otherwise exempt from reporting, through J, a broker, enters into a short sale with respect to 100 shares of the stock of corporation B for \$50 per share on July 12, 1985. J is required to report the sale as occurring on July 12, 1985 with gross proceeds of \$5,000 dollars.

(5) *Gross proceeds.* The gross proceeds on a sale are the total amount paid to the customer or credited to the customer's account as a result of such sale reduced by the amount of any interest reported under paragraph (d)(3) and increased by any amount not so paid or credited by reason of repayment of margin loans. In the case of a closing transaction which results in a loss, gross proceeds are the amount debited from the customer's account. The broker may, but is not required to, take commissions and option premiums into account in determining gross proceeds, provided the treatment chosen is consistent with the books of the broker.

(6) *Conversion of proceeds paid in foreign currency.*—(i) *Convertible currency.* In the event the proceeds of a sale are paid in convertible foreign currency, the amount subject to reporting under this section shall be computed by converting such foreign currency into United States dollars at the exchange rate determined in the following manner. The broker may choose, with respect to a filing group, to use either the exchange rate on the date the sale occurs or the exchange rate at the close of business on the last business day of the reporting period in which the sale occurs. In either case, the broker may use as such exchange rate the rate at which the broker was able to purchase the foreign currency at the relevant time or, if there is no such rate, the exchange rate quote for such foreign currency at such time in any generally recognized financial publication, provided the broker consistently uses the same publication.

(ii) *Nonconvertible currency.* [Reserved.]

(e) *Reporting of barter exchanges.*—(1) *Requirement of reporting.* A barter exchange shall, except as otherwise provided, report in the manner prescribed in this section.

(2) *Exchanges required to be reported.*—(i) *In general.* Except as provided in paragraphs (e)(2)(ii), (g), and (p)(2), a barter exchange shall make a return of information with respect to exchanges of personal property or services through the barter exchange during the calendar year among its members or clients or between such persons and the barter exchange. For this purpose, property or services are exchanged through a barter exchange if payment for property or services is

made by means of a credit on the books of the barter exchange or scrip issued by the barter exchange or if the barter exchange arranges a direct exchange of property or services among its members or clients or exchanges property or services with a member or client.

(ii) *Exemption.* A barter exchange through which there are fewer than 100 exchanges during the calendar year is not required to report for, or make a return of information with respect to exchanges during, such calendar year. The Commissioner may require multiple barter exchanges to be combined for purposes of the preceding sentence upon a determination that a material purpose for the formation or continuation of one or more of the barter exchanges to be combined was to receive one or more exemptions pursuant to this subparagraph.

(f) *Information required.*—(1) *In general.* A person that is a barter exchange during a calendar year shall report on Form 1096 showing the information required thereon for such year.

(2) *Transactional reporting.* As to each exchange with respect to which a barter exchange is required to make a return of information under this section the barter exchange, except as provided in paragraph (p) (2), shall show on Form 1099 the name, address, and taxpayer identification number of each member or client providing property or services in the exchange, the property or services provided, the amount received by the member or client for such property or services, the date on which the exchange occurred, and such other information as may be required by Form 1099, in the form, manner, and number of copies required by Form 1099.

(3) *Exchange date.* For purposes of this section an exchange is considered to occur with respect to a member or client of a barter exchange on the date cash, property, a credit, or scrip is actually or constructively received by the member or client as a result of the exchange. (See § 1.451-2 for rules pertaining to constructive receipt.)

(4) *Amount received.* The amount received by a member or client in an exchange includes cash received, the fair market value of any property or services received, and the fair market value of any credits to the account of the member or client on the books of the barter exchange or scrip issued to the member or client by the barter exchange, but does not include any amount received by the member or client in a subsequent exchange of credits or scrip. For purposes of this section, the fair market value of a credit

or scrip is the value assigned to such credit or scrip by the issuing barter exchange for the purpose of exchanges unless the Commissioner requires the use of a different value that the Commissioner determines more accurately reflects fair market value.

(5) *Meaning of terms.* For purposes of this paragraph (f)—(i) A credit is an amount on the books of the barter exchange that is transferable from one member or client of the barter exchange to another such member or client, or to the barter exchange in payment for property or services;

(ii) Scrip is a token issued by the barter exchange that is transferable from one member or client, of the barter exchange to another such member or client, or to the barter exchange, in payment for property or services; and

(iii) Property does not include a credit or scrip.

(6) *Reporting period.* A barter exchange shall use the calendar year as the reporting period.

(g) *Exempt foreign persons—(1) In general.* No return of information is required with respect to the participation in any transaction during a calendar year of a person who furnishes during such calendar year (or who has furnished during any of the two preceding calendar years) to the broker or barter exchange (irrespective of whether the branch of the broker or barter exchange is within or without the United States) a statement, signed under penalty of perjury, that such person is an exempt foreign person, unless an employee or other agent of the broker or barter exchange who is responsible for receiving or reviewing such statement has actual knowledge that such statement is incorrect. However, the broker or barter exchange may, at its option, require the statement to be provided with respect to each separate transaction. The broker or barter exchange shall retain such statement for at least four years following the end of the last calendar year for which a return of information is not required by reason of such statement. See § 1.6001-1 (relating to records in general) for the requirements relating to the retention of statements provided under this paragraph (g). If, after providing such statement, the person ceases to be an exempt foreign person, such person shall so notify the broker or barter exchange in writing within 30 days of this change in status. For purposes of this paragraph (g), an exempt foreign person is a person who, during a calendar year in which such person participates in transactions with respect to which a return of information would otherwise be required under this section—

(i) Is neither a citizen of the United States, a resident of the United States, nor a person treated as a resident of the United States by reason of an election under section 6013 (g) or (h);

(ii) Is not subject to the provisions of section 877;

(iii) In the case of an individual, has not been, and at the time the statement is furnished reasonably expects not to be, present in the United States for a period aggregating 183 or more days (or is a beneficiary of a tax treaty to which the United States is a party and pursuant to which gains from such person's transactions are exempt from Federal income taxation); and

(iv) At the time the statement is furnished, is not, or reasonably expects not to be, engaged in a trade or business in the United States during such year (or is a beneficiary of a tax treaty to which the United States is a party and pursuant to which gains from such person's transactions are exempt from Federal income taxation).

(2) *Example.* The following example illustrates the application of the exception to the reporting requirements for exempt foreign persons:

Example. In March 1983, F, an individual, opens an account with G, a foreign branch of a brokerage firm incorporated in the United States. G requires new customers to complete a form signed under penalty of perjury that includes 4 questions corresponding to the 4 criteria for an exempt foreign person listed in paragraph (g)(1)(i) through (iv). F's responses to the 4 questions indicate that the 4 criteria are satisfied, and the sole employee of G responsible for receiving and reviewing such statement has no actual knowledge to the contrary. G does not require F to provide a statement that F is an exempt foreign person for each separate transaction it effects on F's behalf and does not require F to provide such a statement on a periodic basis. During 1984, 1985 and 1986, F does not furnish to G a statement that F is an exempt foreign person. If G is not notified by F that F has ceased to be an exempt foreign person, G is not required to make a return of information with respect to sales effected for F during 1983, 1984 and 1985. However, if no other exception applies, G is required to make a return of information with respect to sales effected for F during 1986. The same result would occur if G were a United States branch of either a United States or a foreign brokerage firm.

(h) *Identity of customer—(1) In general.* For purposes of this section, a broker or barter exchange shall treat the person who appears on the books and records of the broker or barter exchange with respect to property or services as the principals with respect thereto.

(2) *Examples.* The following examples illustrate the rule of this paragraph (h):

Example (1). The records of A, a broker, show an account in the name of "B". B is a

nominee for C. All reporting with respect to such account shall treat B as the customer.

Example (2). J, an individual, places an order with H, a broker, to sell J's stock that is held by P, a broker/dealer, in an account for J with P designated as nominee for J, and to credit the gross proceeds from the sale to J's account with P. The account is in the name of P, so that H's customer is P.

(i) [Reserved.]

(j) *Time and place for filing.* Forms 1096 and 1099 required under this section shall be filed after the last calendar day of the reporting period elected by the broker or barter exchange and on or before the end of the second calendar month following the close of the calendar year of such reporting period with the appropriate Internal Revenue Service Center, the address of which is listed in the instructions for Form 1096.

(k) *Requirement and time for furnishing statement—(1) Requirement for furnishing statements.* A broker or barter exchange making a return of information under this section with respect to a transaction shall furnish to the person whose identifying number is (or is required to be) shown on such return a written statement showing the information required by paragraph (c)(5), (d), (f), or (p) of this section and containing a legend stating that such information is being reported to the Internal Revenue Service if the return of information is not made on magnetic media, this requirement may be satisfied by furnishing to such person a copy of all Forms 1099 with respect to such person filed with the Internal Revenue Service Center. A statement shall be considered to be furnished to a person to whom a statement is required to be made under this paragraph (k) if it is mailed to such person at the last address of such person known to the broker or barter exchange.

(2) *Time for furnishing statements.* A broker or barter exchange may furnish the statements required by this paragraph (k) yearly, quarterly, monthly or on any other basis, without regard to the reporting period elected by the broker or barter exchange, provided that all statements required to be furnished under this paragraph (k) for a calendar year shall be furnished on or before January 31 of the following calendar year.

(l) *Use of magnetic media—(1) In general.* Except as otherwise provided by paragraph (1) (2) and (3), a broker or a barter exchange required to file returns of information under this section, shall, in lieu of filing Form 1099 for such year, file such returns of information on magnetic media

authorized by the Commissioner and shall follow the appropriate revenue procedures for such magnetic media filing in lieu of following Form 1099 instructions.

(2) *Exception for undue hardship.* (i) The Commissioner may authorize a broker or barter exchange to file returns of information on Form 1099 instead of on magnetic media if undue hardship is shown on an application filed with the appropriate Internal Revenue Service Center.

(ii) In the case of a person who is a broker or barter exchange on July 1, 1983, an application to file returns of information on Form 1099 must be filed on or before September 15, 1983. In the case of a person who becomes a broker or barter exchange after July 1, 1983, such application must be filed by the end of the second month following the month in which such person becomes a broker or barter exchange.

(3) *Transitional rule.* A broker or barter exchange may submit returns of information on Form 1099 for reporting periods that—

(i) End before January 1, 1984; or

(ii) Begin before 30 days after the date on which a timely filed request to file returns of information on Form 1099 is denied.

(m) *Reporting on options transactions.*

[Reserved]

(n) *Reporting on bond discounts.*

[Reserved]

(o) *Additional reporting by stock transfer agents.* [Reserved]

(p) *Transitional rules—(1)*

Information required from brokers. In the case of reporting periods ending before January 1, 1984, a broker may show the information required by this paragraph (p)(1) on Form 1099 in lieu of the information required under paragraph (d)(2). As to each customer account for which a return of information is required under this section with respect to sales, the broker must report the name, address, and taxpayer identification number of the customer, the aggregate gross proceeds of all sales of the account during the reporting period for which a return of information is required under this section, and such other information as may be required by Form 1099, in the form, manner, and number of copies required by Form 1099.

(2) *Information required from barter exchanges.* In the case of reporting periods ending before January 1, 1984, a barter exchange may show the information required by this paragraph (p)(2) on Form 1099 in lieu of the information required under paragraph (f)(2). As to each member or client providing property or services in an

exchange for which a return of information is required under this section, the barter exchange must report the name, address, and taxpayer identification number of the member or client, the aggregate amount received by the member or client during the reporting period for property or services provided by such member or client in exchanges for which a return of information is required, and such other information as may be required by Form 1099, in the form, manner, and number of copies required by Form 1099.

(q) *Effective date.* This section applies to calendar year 1983 and all succeeding calendar years, and, as to 1983, only to transactions occurring on or after July 1, 1983.

(Secs. 6011(e), 6045 and 7805 of the Internal Revenue Code of 1954, (96 Stat. 610, 68A Stat. 747, 917; 26 U.S.C. 6011(e), 6045, 7805)

James L. Owens,

Acting Commissioner of Internal Revenue.

Approved: March 3, 1983.

John E. Chapoton,

Assistant Secretary of the Treasury.

[FR Doc. 83-4878 Filed 3-3-83; 4:49 pm]

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26 CFR Parts 1 and 5f

(T.D. 7681)

Income Tax; Information Reporting Requirements With Respect to Interest and Original Issue Discount**AGENCY:** Internal Revenue Service, Treasury.**ACTION:** Final regulations.

SUMMARY: This document contains final regulations relating to information reporting requirements with respect to interest and original issue discount. Changes to the applicable tax law were made by the Tax Equity and Fiscal Responsibility Act of 1982. These regulations affect issuers of obligations, payors of interest, and certain recipients, and provide them with the guidance needed to comply with the law.

DATES: The regulations apply to payments of interest and original issue discount made after December 31, 1982.

FOR FURTHER INFORMATION CONTACT: Diane L. Kroupa of the Legislation and Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington, D.C. 20224 (Attention: CC: LR: T) (202-566-3828 or 3829).

SUPPLEMENTARY INFORMATION:**Background**

On November 15, 1982, the *Federal Register* published temporary regulations (47 FR 51364) and proposed amendments (47 FR 51412) to the Income Tax Regulations (26 CFR Part 1) under section 6049 of the Internal Revenue Code of 1954. These amendments were proposed to conform the regulations to section 309 of the Tax Equity and Fiscal Responsibility Act of 1982 (Pub. L. 97-248, 96 Stat. 591). Several written comments responding to this notice were received. A public hearing was held on January 25, 1983. After consideration of all comments regarding the proposed amendments, those amendments are adopted by this Treasury decision with several revisions in response to the comments. The revisions and the comments are discussed below.

Public Comments

The regulations provide generally that payors who pay interest and certain middlemen who receive interest on behalf of other persons must make an information return if the amount of interest paid to, or received on behalf of, such person aggregates \$10 or more during the calendar year. If an amount of tax is withheld under section 3451

with respect to a payment of interest, however, an information return is required to be made irrespective of the amount of interest paid. The regulations define the term interest for purposes of information reporting. Commentators requested clarification that amounts paid with respect to commercial paper, repurchase agreements, and banker's acceptances constitute interest subject to reporting under section 6049. The regulations are amended to state specifically that such amounts constitute interest subject to reporting.

The definition of interest is also amended, due to commentators' requests for clarification, to provide that amounts that a governmental entity pays with respect to a refund of tax are not interest subject to reporting under section 6049. Interest paid on amounts held as a security deposit or interest on amounts held in escrow to guarantee performance on a contract or to provide security is also not subject to information reporting under section 6049 unless the amount is deposited in a bank or savings institution.

Merchandise or property provided to a payee as interest (or in lieu of a cash payment of interest) is interest subject to reporting under section 6049. The amount subject to reporting is the fair market value of such property.

The proposed regulations require insurance companies to report under section 6049 any interest paid when proceeds of a policy are delayed, whether or not the policy provides for an interest payment under those circumstances. Based on the comments received, the regulations are amended to require reporting of such interest only if the policy specifically provides that such interest be paid. Rev. Rul. 74-369, 1974-2 C.B. 393, holds that if interest is not paid pursuant to the terms of the policy, such interest is subject to reporting under section 6041 if it equals or exceeds \$600.

Commentators also requested clarification as to whether an information return is required to be made with respect to payments made to individuals who are exempt from withholding under section 3451. The regulations are amended to clarify that information returns are required to be made with respect to interest paid to individuals who are exempt individuals for purposes of the withholding requirements. An individual who is exempt from withholding as a result to filing an exemption certificate under the withholding provisions is not thereby exempt from reporting. Thus, payors are required to make information returns reporting the amount of interest paid to such individuals.

The regulations provide that payments made to persons that are exempt recipients for purposes of the withholding requirements are not subject to reporting. Persons qualifying as exempt recipients are described in the regulations. If a recipient is exempt from withholding without filing an exemption certificate, payments made to the recipient are also exempt from reporting. Thus, in general, payments of interest made to a corporation are not subject to information reporting under section 6049.

The proposed regulations require an information return to be made to an exempt recipient, however, with respect to original issue discount. Commentators pointed out certain problems in connection with reporting original issue discount. The Treasury Department announced in a news release that the lack of information as to discount obligations would be considered reasonable cause for failure to comply until December 31, 1983, with the reporting requirements of original issue discount that were added by the Tax Equity and Fiscal Responsibility Act of 1982. The Service will publish a list of publicly traded original issue discount obligations that may be relied on in determining the amount of original issue discount subject to reporting. Beginning January 1, 1984, persons (other than the issuer of an obligation) will be able to rely on the Internal Revenue Service's publication to determine whether an obligation is issued with original issue discount and the amount of original issue discount subject to reporting. No information return is required to be made with respect to exempt recipients.

Comments received after the new release was published requested clarification of whether reporting on savings bonds and certain other discount obligations has been delayed. For long term discount obligations in registered form, information reporting was required prior to enactment of the Tax Equity and Fiscal Responsibility Act of 1982. Thus, these obligations are not within the scope of the deferred effective date for reporting on discount obligations. Savings bonds are not considered original issue discount obligations under section 1232A. Thus, reporting has not been delayed on savings bonds. For obligations issued at a discount and bearing stated interest, reporting is required on the stated interest at all times after December 31, 1982.

The proposed regulations provide that middlemen who pay interest on United States savings bonds, interest coupons, and short term discount obligations and

Federal agencies that pay interest on United States savings bonds may report on a transactional basis rather than on an annual aggregate basis. The proposed regulations require that the issuer's name, in addition to the middleman's name, be placed on the information return when an information return is made on a transactional basis. Certain commentators stated that this requirement complicated the processing of such transactions. The final regulations provide that only the middleman's name, and not the issuer's name, is required to be placed on the information return.

The proposed regulations provide that no information return is required with respect to tax exempt obligations. Commentators requested that payors be permitted to rely on their customer's written statement that an interest coupon is exempt and, therefore, not subject to information reporting. The regulations are amended to provide that a holder of a tax exempt obligation must provide written certification to the payor (other than the issuer of the obligation) that interest represented by the coupon is exempt from taxation. Payors may rely on such certifications in not making an information return with respect to such coupons. A statement that interest coupons are exempt from taxation on the envelope or "shell" commonly used by financial institutions to process such coupons, signed by the payee, will be sufficient for this purpose if the envelope is properly completed (*i.e.*, shows the payee's name, address, and taxpayer identification number). An issuer who receives the envelope or "shell" on which the payee has certified that the coupon is exempt from taxation when the obligation is not in fact tax exempt is required to make an information return.

Commentators also solicited guidance concerning the form to be used when reporting on short term discount obligations. The regulations are clarified to state that discount on short term discount obligations is treated as a payment of interest that should be reported on Form 1099-INT. This form should be used to report discount on short term government obligations as well as short term corporate obligations.

The proposed regulations provide that amounts paid to certain persons who are not United States persons will not be considered to be interest subject to reporting under section 6049. Under the proposed regulations, a payor may treat a payee as a foreign person for this purpose if the payor receives a statement, signed by the payee under penalties of perjury. In addition, if the

payee is an individual, he must establish that he holds a passport from a country other than the United States. Various comments have indicated that the passport requirement is unduly burdensome, as many foreign individuals do not have passports and as, with respect to transactions effected other than in person, it is difficult administratively to confirm the possession of a non-United States passport. In response to these comments, the passport procedure has been eliminated.

The regulations have been amended to expand upon the types of information that should be provided on the statement certifying the status of a payee as a non-United States person. Specifically, the statement must contain the name, address, and taxpayer identification number (if any) of the payee. In response to a request by various commentators that a special Internal Revenue Service form be provided for this statement, the regulations have been modified to indicate that an optional form (W-8) will be provided by the Internal Revenue Service for this purpose.

Commentators also have requested clarification of the situations in which the statement described above must be provided to a payor. The regulations have been clarified to indicate that, in order to avoid reporting, the statement generally must be provided to the payor in each instance in which an exception to the definition of interest is dependent on a payee's status as a person who is not a United States person. However, the regulations have been amended to provide that the statement will not be required with respect to a particular payment made in a calendar year if, with respect to that or any other payment made by the payor to the payee in that year, the payor has received a Form 1001, a Form 4224 or other appropriate documentation indicating either that the payment is subject to reduced rates of tax under a treaty or is effectively connected with a United States trade or business of the payee. Similarly, the statement certifying the status of the payee as a foreign person is not required with respect to a particular payment made to a payee in a calendar year if the payor has actually withheld tax under subchapter A of chapter 3 of the Code on that or on any other payment made to the payee during that year.

Certain exceptions to the definition of interest are provided in the proposed regulations for amounts paid by various enumerated foreign entities (*e.g.*, a foreign corporation not engaged in trade

or business in the United States during the calendar year). The regulations have been amended to provide more clearly that the exceptions apply only if one of the enumerated foreign entities is the obligor on an obligation with respect to which the amount in question is paid. Thus, the status of a paying agent or middleman as one of the enumerated foreign entities is not material to the issue of whether the amount paid by such paying agent or middleman is to be considered interest for purposes of reporting. Similarly, the fact that a paying agent or middleman is not one of such enumerated foreign entities will not cause an amount paid on an obligation issued by one of such entities to be recharacterized as interest subject to reporting.

Under the proposed regulations the person required to report is responsible for determining whether foreign currency, not readily convertible into United States dollars, is nevertheless indirectly convertible into United States dollars. The regulations have been amended to give the responsibility for making this determination to the Secretary.

Non-applicability of Executive Order 12291

The Commissioner has determined that this Treasury decision is not subject to review under Executive Order 12291 or the Treasury and OMB implementation of the Order dated April 28, 1982

Regulatory Flexibility Act

Pursuant to 5 U.S.C. 605(b), the Secretary of the Treasury has certified that the requirements of the Regulatory Flexibility Act do not apply to this regulation as it will not have a significant economic impact on a substantial number of small entities.

The impact of the requirement that information returns be made with respect to payments of interest and original issue discount is due to requirements imposed directly by the statute. In the areas in which the Service has been given significant discretion under the statute, the Service has exercised its discretion so as to minimize the potential impact of reporting while at the same time ensuring compliance with the statute.

For example, the statute permits regulations to be issued to require payors to furnish duplicate written statements to the payees of the amount of interest paid and the amount of tax withheld under section 3451, if any. The statute also permits regulations to be issued to require such payees to file this

duplicate copy of the information return with the payee's tax return. No regulations have been issued under this authority. Thus, payors are not required to furnish duplicate copies of the information return to the payee, and payees are not required to attach the information return to their tax return.

Drafting Information

The principal author of these regulations is Diane L. Kroupa of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. Personnel from other offices of the Internal Revenue Service and Treasury Department, however, participated in developing the regulations, both on matters of substance and style.

List of Subjects in 26 CFR 1.6001-1—1.6109-2

Income taxes, Administration and procedure, Filing requirements, Reporting and recordkeeping.

Adoption of Amendments to the Regulations

Accordingly, 26 CFR Part 5f is amended by removing §§ 5f.6049-1, 5f.6049-2, and 5f.6049-3, and 26 CFR Part 1 is amended as follows:

PART 1—[AMENDED]

Paragraph 1. The headings of §§ 1.6049-1, 1.6049-2, and 1.6049-3 are revised to read as follows:

§ 1.6049-1 Returns of information as to interest paid in calendar years before 1983 and original issue discount includible in gross income for calendar years before 1983

§ 1.6049-2 Interest and original issue discount subject to reporting in calendar years before 1983.

§ 1.6049-3 Statements to recipients of interest payments and holders of obligations to which there is attributed original issue discount in calendar years before 1983.

§ 1.6049-1 [Amended]

Par. 2. Section 1.6049-1 is amended—

1. By removing the phrase "calendar years after 1962" each place it appears in paragraph (a)(1)(i) and (iii) and inserting in lieu thereof the phrase "calendar year before 1983".

2. By removing the phrase "calendar year after 1970" each place it appears in paragraph (a)(1)(ii)(a), (iv), and in paragraph (a)(5), and inserting in lieu

thereof the phrase "calendar year before 1983", and

3. By adding the phrase "and on or before December 31, 1982" immediately after the phrase "issued after May 27, 1969 (other than an obligation issued by a corporation pursuant to a written commitment which was binding on May 27, 1969, and at all times thereafter)" the place it appears in paragraph (a)(1)(ii)(a).

§ 1.6049-2 [Amended]

Par. 3. Section 1.6049-2 is amended by adding the phrase "and on or before December 31, 1982" immediately after the phrase "issued after May 27, 1969 (other than an obligation issued pursuant to a written commitment which was binding on May 27, 1969, and at all times thereafter)" the place it appears in paragraph (c)(2).

§ 1.6049-3 [Amended]

Par. 4. Section 1.6049-3 is amended—

1. By removing the phrase "calendar year after 1962" the place it appears in paragraph (b)(1)(i) and inserting in lieu thereof the phrase "calendar year before 1983", and

2. By adding the phrase "and prior to calendar year 1983" immediately after the phrase "calendar year after 1970" the place it appears in paragraph (b)(1)(ii).

Par. 5. New §§ 1.6049-4, 1.6049-5, and 1.6049-6 are added immediately after § 1.6049-3 to read as follows:

§ 1.6049-4 Return of information as to interest paid and original issue discount includible in gross income after December 31, 1982.

(a) *Requirement of reporting*—(1) *In general.* Except as provided in paragraph (c) of this section, an information return shall be made by the persons described in paragraph (a)(2) of this section with respect to any payment of interest (as defined in § 1.6049-5) after December 31, 1982. Such return shall contain the information required in paragraph (b) of this section.

(2) *Persons required to make reports.* The persons required to make an information return under section 6049(a) and this section are—

(i) Every person who is required to deduct and withhold the tax imposed by section 3451;

(ii) Every person who makes a payment of interest aggregating \$10 or more to any other person during a calendar year; and

(iii) Every person who collects (or otherwise acts as a middleman (as defined in paragraph (f)(4) of this section) with respect to) payments of interest on behalf of another person

aggregating \$10 or more during a calendar year.

(b) *Information to be reported*—(1) *Interest payments.* Except as provided in paragraph (b)(3) of this section, in the case of a payment of interest other than original issue discount treated as interest under § 1.6049-5(c), an information return on Forms 1096 and 1099 shall be made for the calendar year showing the aggregate amount of the payments, the name, address, and taxpayer identification number of the person to whom paid, the amount of tax deducted and withheld under section 3451 from the payments, and such other information as is required by the forms. An information return is required if the aggregate amount of interest is \$10 or more unless the tax imposed by section 3451 is required to be withheld. In such event, the amount required to be shown is the amount subject to withholding even if such amount is less than \$10.

(2) *Original issue discount.* Except as provided in paragraph (b)(3) of this section, in the case of original issue discount, an information return on Forms 1096 and 1099 shall be made for each calendar year of any holder of an obligation as to which there is original issue discount includible in gross income aggregating \$10 or more (determined, if semiannual record date reporting is being used, under § 1.6049-1(a)(1)(ii)(b)(1)), by treating each holder as holding the obligation on every day it was outstanding during the calendar year). An information return shall be made, however, in any case in which an amount of tax is required to be deducted and withheld under section 3451. In such case, the amount required to be reported is the amount subject to withholding even if the amount of original issue discount includible in gross income is less than \$10. With respect to an obligation described in § 1.1232-3A (e) or (f) (relating respectively to deposits in banks and similar financial institutions and to face-amount certificates), § 1.6049-1(a)(1)(ii)(d) and the last sentence of § 1.6049-1(a)(1)(ii)(a)(2) shall apply. The information return shall show—

(i) The name, address, and taxpayer identification number of each record holder for whom an amount of original issue discount is includible in gross income;

(ii) The account, serial, or other identifying number of each obligation with respect to which a return is being made;

(iii) The aggregate amount of original issue discount includible in the gross income of each holder for the period during the calendar year for which the

return is made (or, if the aggregation rules of § 1.6049-1(a)(1)(ii)(b)(2) are being used, the aggregate amount or original issue discount for the period such holder held the obligations). If, however, the semiannual record date reporting rules are being used under § 1.6049-1(a)(1)(ii)(b)(1), the aggregate amount shall be determined by treating each record date holder as if he held each obligation on every day it was outstanding during the calendar year. For purposes of this section, an obligation shall be considered to be outstanding from the date of original issue (as defined in § 1.1232-3(b)(3));

(iv) The amount of tax withheld under section 3451, if any;

(v) The name and address of the person filing the return; and

(vi) Such other information as is required by the forms. Section § 1.6049-1(a)(1)(ii) (b) and (c) shall apply for purposes of this paragraph.

(3) *Returns made by middleman.* Every person acting as a middleman (as defined in paragraph (f)(4) of this section) shall make an information return on Forms 1096 and 1099 for the calendar year. In the case of interest payments (other than original issue discount), the return shall show the aggregate amount of such interest, the name, address, and taxpayer identification number of the person on whose behalf received, the amount of tax withheld under section 3451, if any, and such other information as is required by the forms. In the case of original issue discount, the return shall show the information required to be shown for the actual owner, as described in paragraph (b)(2) of this section. A middleman shall make an information return regardless of whether the middleman receives a Form 1099. A middleman shall not be required to make an information return if the payments of interest aggregate less than \$10 unless such amount is subject to withholding under section 3451. If an amount of tax is required to be deducted and withheld under section 3451, a return shall be made irrespective of the amount of the payment and irrespective of whether the payment is made to an exempt recipient described in paragraph (c)(1)(ii) of this section.

(4) *Returns made with respect to payments on certificates of deposit issued in bearer form.* Every person carrying on the banking business who makes payments of interest to another person (whether or not aggregating \$10 or more) during a calendar year with respect to a certificate of deposit issued in bearer form shall make an information return on Forms 1096 and 1099. The information return shall show

the information required in § 1.6049-1(a)(1)(vi) (a) through (e) inclusive and a statement as to the amount of tax withheld under section 3451, if any.

(c) *Information returns not required—*
(1) *Payment to exempt recipient.* (i) In the case of a payment to a person described in paragraph (c)(1)(ii) of this section, no return shall be required to be made unless such payment is made by a person required to make a return by paragraph (a)(2)(i) of this section (relating to persons required to withhold tax). Thus, a person who withholds tax under section 3451 is required to make an information return regardless of whether the payee is an exempt recipient described in paragraph (c)(1)(ii) of this section.

(ii) An information return shall not be required with respect to payments made to—

(A) A corporation as defined in section 7701(a)(3), whether domestic or foreign,

(B) An organization exempt from taxation under section 501(a) or an individual retirement plan,

(C) The United States or a State, the District of Columbia, a possession of the United States, or a political subdivision or a wholly-owned agency or instrumentality of any one or more of the foregoing,

(D) A foreign government, a political subdivision thereof, or an international organization,

(E) A foreign central bank of issue (as defined in § 1.895-1(b)(i) to be a bank which is by law or government sanction the principal authority, other than the government itself, issuing instruments intended to circulate as currency),

(F) A dealer in securities or commodities required to register as such under the laws of the United States or a State,

(G) A real estate investment trust (as defined in section 856),

(H) An entity registered at all times during the taxable year under the Investment Company Act of 1940.

(I) A common trust fund (as defined in section 584(a)),

(J) A nominee or custodian.

(K) A financial institution such as a mutual savings bank, savings and loan association, building and loan association, cooperative bank, homestead association, credit union, industrial loan association or bank, or other similar organization.

(L) A broker as defined in section 6045(c), or

(M) Any trust which—

(1) Is exempt from tax under section 664(c) (*i.e.*, a charitable remainder annuity trust or a charitable remainder unitrust), or

(2) Is described in section 4947(a)(1) (relating to a certain charitable trust).

A payor who may treat any person as an exempt recipient for withholding purposes as described in § 31.3452(c)-1 (b) through (p) without requiring such person to file an exemption certificate may treat the persons listed in this subdivision (ii)(A) through (M) as an exempt recipient for information reporting purposes. A payor shall make an information return with respect to an individual who files an exemption certificate to be exempt from withholding under section 3451. The individual is not exempt for reporting purposes. A payor shall make an information return with respect to a trust which is an exempt individual under section 3452(b)(4) and § 31.3452(b)-1(d). See § 1.6049-4(c)(2) providing that the trust satisfies the reporting requirements under section 6049 if the trust files a Form 1041 and furnishes a beneficiary a Form K-1 containing the information required to be shown on the form, including amounts withheld under section 3451.

(iii) The application of this paragraph (c) may be illustrated by the following examples:

Example (1). In 1980, Corporation Y issued 10-year debentures with 9 percent interest coupons payable semiannually on June 30 and December 31. Individual F, who is exempt from withholding under section 3451, presents a coupon for payment at Bank M on the interest payment date. Bank M transmits the coupon to Bank N, which in turn presents the coupon to Corporation Y for payment. Bank M is required to make an information return with respect to the payment to individual F under § 1.6049-4(a)(2)(iii). Bank N is not required to make an information return with respect to the payment to Bank M, and Corporation Y is not required to make an information return with respect to the payment to Bank N because Banks M and N are exempt recipients described in § 1.6049-4(c)(1)(ii)(K).

Example (2). Broker E acquires a bond issued in 1980 by the United States Treasury through the Bureau of Public Debt. Broker E sells interests in the bond to the public after December 31, 1982. A purchaser may acquire an interest in any interest payment falling due under the bond or an interest in the principal of the bond. The bond is held by Custodian H for the benefit of the persons acquiring these interests. Custodian H files an exemption certificate claiming exemption from withholding under § 31.3452(c)-1(n). On receipt of interest and principal payments under the bond, Custodian H transfers the amount received to the person whose ownership interest corresponds to the component giving rise to the payment. Under section 1232B, each bond component is treated as a bond issued with original issue discount equal to the excess of the stated redemption price at maturity over the

purchase price of the bond component. Accordingly, H is required to make an information return setting forth the information required in § 1.6049-4(b)(2) with respect to each holder of an interest in the bond. The Bureau of Public Debt is not required to make an information return since it made payment to Custodian H who is an exempt recipient described in § 1.6049-4(c)(1)(ii)(I).

Example (3). On January 1, 1984, the United States Treasury through the Bureau of Public Debt issues \$1 million of obligations with a maturity of 1 year or less. The obligations are represented by entries on records maintained through Federal Reserve banks and branches for the account of member banks of the Federal Reserve system. Bank O, which is a member bank of the Federal Reserve system, tenders an offer for \$100,000 of the obligations. The Federal Reserve opens an account for Bank O showing that it owns \$100,000 of the obligations. When Bank O sells any of these obligations to an investor, it maintains a book entry account showing such investor's ownership. Upon maturity, the United States Treasury credits the amount due the Federal Reserve bank holding an interest in the obligation. The Federal Reserve bank in turn credits the account of Bank O, which then credits the accounts of the persons owning the obligations. Bank O must make the information return required under section 6049 and this section with respect to the payments made by it to persons not described in § 1.6049-4(c)(1). Thus, if, at maturity of the obligation, Bank O held an obligation on its books for D, an individual, Bank O is required to make an information return with respect to the payment made to individual D. Neither the Bureau of Public Debt nor the Federal Reserve bank is required to make an information return since such payments were made to persons described in § 1.6049-4(c)(1)(ii).

Example (4). Assume the same facts as example (3) except a brokerage house buys the \$100,000 of obligations through the Federal Reserve bank. The Federal Reserve maintains a book entry account showing that a member bank holds \$100,000 of obligations for a brokerage house. The brokerage house sells these obligations to its customers. The brokerage house holds \$50,000 of the obligations for a pension trust, \$30,000 of the obligations for Corporation Z, and \$10,000 of the obligations each for Individuals I and J. The brokerage house is required to make an information return with respect to the payments of interest at maturity on the obligations it holds for its customers who are not described in § 1.6049-4(c)(1). Thus, the brokerage house is required to make an information return with respect to the payments made to Individuals I and J. No information return is required with respect to the payments made to the pension trust or Corporation Z because such persons are exempt recipients described in § 1.6049-4(c)(1)(ii). The Bureau of Public Debt and the Federal Reserve bank are not required to make an information return because they made payment to a person described in § 1.6049-4(c)(1)(ii).

(2) *Payments by certain middlemen.*

An information return shall not be required if—

(i) The record owner is required to file a fiduciary return on Form 1041 disclosing the name, address, and taxpayer identification number of the actual owner, and furnishes Form K-1 to each actual owner containing the information required to be shown on the form, including amounts withheld under section 3451;

(ii) The record owner is a nominee of a banking institution or trust company exercising trust powers, and such banking institution or trust company is required to file a fiduciary return on Form 1041 disclosing the name, address, and identifying number of the actual owner, and furnishes Form K-1 to each actual owner containing the information required to be shown on the form, including amounts withheld under section 3451;

(iii) The record owner is a banking institution or trust company exercising trust powers, or a nominee thereof, and actual owner is an organization exempt from taxation under section 501(a) for which such banking institution or trust company files an annual return, but only if the name, address, and taxpayer identification number of the record owner is included on or with the Form 1041 fiduciary return filed for the estate or trust or the annual return filed for the tax exempt organization.

(d) *Special rules—(1) Aggregation of payments.* For purposes of paragraph (b) of this section, until such time as the Commissioner determines that it is feasible to require aggregation of payments on two or more accounts, insurance contracts, or investment certificates, and, until this section is amended accordingly to provide for reporting on an aggregate basis, the requirement for filing Form 1099 under this section will be met if a person making payments of interest subject to reporting files a separate Form 1099 with respect to each account, insurance contract, or investment certificate. In the case of obligations described in section 6049(b)(1)(A), separate Forms 1099 may be filed as provided in the preceding sentence with respect to holdings in different issues.

(2) *Treatment of original issue discount.* The amount of original issue discount subject to reporting under section 6049 shall be the amount of original issue discount includible in the gross income of any holder that is treated as paid under § 1.6049-5(c).

(3) *Conversion of amounts paid in foreign currency into United States dollars—(i) Convertible foreign currency.* In the event that an amount of

interest or an amount of original issue discount on an obligation with a maturity of not more than 1 year is paid or credited in convertible foreign currency, the amount shall be converted into United States dollars, and the amount subject to reporting under section 6049 shall be computed on such United States dollar amount, on the date of the payment or crediting. For this purpose, the term "convertible foreign currency" means currency of a foreign country that either is readily convertible into United States dollars or is of a type the Secretary determines is to be treated as a convertible foreign currency from the date specified in a notice of such determination published in the Federal Register.

(ii) *Nonconvertible foreign currency.* [Reserved]

(iii) *Original issue discount on foreign currency obligations with a maturity of more than 1 year.* [Reserved]

(4) *Determination of person to whom interest or original issue discount is paid or for whom it is received.* Section 1.6049-1(a)(3) and (4) shall apply with respect to payments of interest and original issue discount after December 31, 1982.

(5) *Payments by governmental units.* In the case of payments made by any governmental unit or any agency or instrumentality thereof, the officer or employee having control of the payment of interest or original issue discount (or the person appropriately designated for purposes of this section) shall make the returns and statements required under section 6049.

(6) *When payment deemed made—(i) In general.* Except as provided in paragraph (d)(6)(ii) of this section, for purposes of section 6049, interest is deemed to have been paid when it is credited or set apart to a person without any substantial limitation or restriction as to the time or manner of payment or condition upon which payment is to be made, and is made available to him so that it may be drawn at any time, and its receipt brought within his own control and disposition.

(ii) *Instruments paid on presentment or demand.* In the case of a payment made on an obligation described in paragraph (e)(2) of this section (relating to transactional reporting), interest is deemed to have been paid at the time the obligation is presented for payment. For example, interest represented by a coupon detached from a bond is considered paid for purposes of section 6049 when the coupon is presented for payment.

(7) *Permission to submit information required by Form 1099 on magnetic tape,*

For rules relating to permission to submit the information required by Form 1099 on magnetic tape or other media, see § 1.9101-1.

(8) *Obligations that are not exempt from taxation.* When an issuer of an obligation that is not exempt from taxation receives an envelope or "shell", signed by the payee, stating that interest on the obligation is exempt from taxation under section 103(a) (as described in § 1.6049-5(b)(1)(ii)), the issuer shall make an information return under section 6049. The information return shall show the name, address, and taxpayer identification number of the person who signed the statement claiming that interest on the obligation is exempt from taxation, the amount of interest paid, and such other information as is required by the form. An information return is required regardless of the amount of interest. The issuer shall also furnish a written statement to such person showing the information required by § 1.6049-6(b).

(9) *Savings bonds—(i) In general.* A person who makes payment on a United States savings bond when the bond is presented for payment shall report the difference between the amount to be paid and the amount paid for the bond. The amount subject to reporting shall not be reduced to take into account—

(A) Amounts previously included in the income of a holder as a result of an election under section 454 to include annually the increase in the redemption price of the bond; or

(B) Amounts accrued prior to transfer of the bond where the bond has been reissued in the name of the person presenting the bond for payment.

With respect to a savings bond that is reissued in another person's name, the amount subject to reporting when the bond is reissued is the amount of interest that has accrued. With respect to a savings bond that is exchanged in a tax-deferred transaction (as described in section 1037), the amount subject to reporting is the amount of cash paid to the holder at the time of the transaction.

(ii) *Examples.* The application of the provisions of paragraph (d)(10)(i) of this section may be illustrated by the following examples:

Example (1). On June 10, 1943, A purchases a \$50 Series E savings bond. The amount paid for the savings bond is \$37.50. A elects under section 454 to include the increase in the redemption price of the bond annually in income. A presents the bond to Bank M to be cashed on July 1, 1983. The amount to be paid on the bond on that date is \$204.96. Bank M is required to make an information return under section 6049 showing that it paid \$167.46 (the difference between \$204.96 and \$37.50) of interest, without regard to A's election to

include annually the increase in the redemption price of the bond.

Example (2). On December 1, 1970, B purchases a \$500 Series E savings bond. The amount paid for the bond is \$375. On August 1, 1984, the bond is reissued by the Bureau of Public Debt by deleting B's name and inserting the name of B's child. At the time of reissue, the redemption value of the bond is \$1,015.80. The accrued interest is \$640.80 (the difference between \$1,015.80 and \$375). The reissue is a taxable transaction, and B must include in income the accrued interest at the time of reissue. The Bureau of Public Debt is required to make an information return under section 6049 showing that it paid \$640.80 of interest to B.

Example (3). Assume the same facts as in example (2) except that B exchanges the bond for a Series HH savings bond in the amount of \$1,000 issued in B's name. The exchange is tax-deferred under section 1037. The Bureau of Public Debt stamps a legend on the bond stating that interest of \$625 has been deferred. The amount of \$15.80 is paid to B. The Bureau of the Public Debt must make an information return showing that it paid \$15.80 of interest to B.

Example (4). Assume the same facts as in example (3) except that the exchange is not a tax-deferred exchange. The Bureau of the Public Debt must make an information return showing that it paid \$640.80 of interest to B.

(e) *Transactional reporting—(1) In general.* An information return required to be made under paragraph (b) of this section may be made on a transaction-by-transaction basis, rather than on an annual aggregation basis, if payment described in paragraph (e)(2) of this section is made by a person described in paragraph (e)(3) of this section.

(2) *Payments subject to transactional reporting.* An information return may be made on a transactional basis if payment is made on—

(i) A United States savings bond,
(ii) An interest coupon (but see § 1.6049-5(b) which provides that no information return is required to be made with respect to an interest coupon that is exempt from taxation),

(iii) A discount obligation having a maturity at issue of 1 year or less, including commercial paper and short-term government obligations defined in section 1232(a)(3), and

(iv) Any obligation similar to those described in subdivisions (i) through (iii). The information return with respect to payments on the types of obligations described in this paragraph shall be made on Form 1099-INT. A payor may include all interest paid in one transaction on one information return, irrespective of whether obligations of different issuers are paid as part of the transaction.

(3) *Persons subject to transactional reporting.* A person may make a return on a transactional basis if the person is—

(i) A middleman (as defined in paragraph (f)(4) of this section) who is required to make an information return under paragraph (b)(3) of this section with respect to any payment described in paragraph (e)(2) of this section, or

(ii) A federal agency making payments on a United States savings bond.

(4) *Transaction defined.* For purposes of this paragraph (e), a transaction means a payment at one time on one or more obligations. For example, if an individual who is exempt from withholding under section 3451 presents at one time five Series EE bonds on each of which \$3 of interest has accrued, \$15 of interest will be paid as part of the transaction. Accordingly, an information return is required under § 1.6049-4 (a)(2)(iii) because the interest paid in the transaction exceeds \$10. If only three of the savings bonds were presented, however, no return would be required even if the remaining two bonds were redeemed the following day. See paragraph (a)(2)(i) of this section for the requirement that an information return be made if any amount of tax is withheld under section 3451.

(5) *Information required.* The information return for any transaction under paragraph (e) of this section shall show the following:

(i) The name, address, and taxpayer identification number of the person to whom the interest is paid;

(ii) The name and address of the person filing the form;

(iii) The amount of interest paid;

(iv) The amount of tax withheld under section 3451 if any; and

(v) Such other information as is required by the form.

(f) *Definitions.* For purposes of section 6049, this section, and §§ 1.6049-5 and 1.6049-6—

(1) *Person.* The term "person" includes any governmental unit, international organization, and any agency or instrumentality thereof. Therefore, interest paid by one of these entities must be reported unless one of the exceptions under section 6049 applies.

(2) *Natural person.* The term "natural person" means any individual, but shall not include a partnership (whether or not composed entirely of individuals), a trust, or an estate.

(3) *Obligation.* The term "obligation" includes bonds, debentures, notes, certificates, and other evidences of indebtedness regardless of how denominated.

(4) *Middleman—(i) In general.* The term "middleman" means any person, including a financial institution as described in paragraph (c)(1)(K) of this

section, a broker as defined in section 6045(c), or a nominee, who makes payment of interest for, or collects interest on behalf of, another person, or otherwise acts in a capacity as intermediary between a payor and a payee. For example, a person (other than an issuer of an obligation) who makes payment on an interest coupon of the obligation to another person is a middleman, irrespective of whether such person purchases the coupon for his own account, accepts the coupon as agent for the payee, or otherwise deals with the coupon. The term "middleman" also includes a trustee, including a corporate trustee of a trust where the trust is the payee. See § 1.6049-4(c)(2) providing that the trustee does not have to make an information return on Form 1099 to a beneficiary if the trustee is required to file Form 1041 and furnishes Form-K-1 to the beneficiary showing the information required to be shown on the form, including amounts withheld under section 3451. A person shall not be considered to be a middleman as to any portion of an interest payment which is actually owned by another person whose name is also shown on the information return filed with respect to such interest payment. Thus, in the case of a savings account jointly owned by a husband and wife, the husband will not be considered as acting in the capacity of a middleman with respect to his wife if his wife's name is included on the information return filed by the payor with respect to the interest.

(ii) *Example.* The application of the provisions of paragraph (f)(4) of this section may be illustrated by the following example:

Example. In January, 1984, Broker B purchases on behalf of its customer, Individual A, an obligation issued by partnership RR in a public offering on that date. Broker B holds the obligation for A throughout 1984. The obligation bears no stated interest and matures in January 1986. Broker B is a middleman with respect to the obligation of RR that it holds for A. Broker B is required to make an information return showing the amount of original issue treated as paid to A during 1984 under § 1.6049-5(c).

(g) *Time and place for filing a return for the payment of interest—(1) Annual return.* Except as provided in paragraph (g)(2) of this section, the returns required under this section for any calendar year for the payment of interest shall be filed after September 30 of such year, but not before the payor's final payment to the payee for the year, and on or before February 28 of the following year. Such returns shall be filed with the appropriate Internal Revenue Service Center, the address of which is listed in the instructions for Form 1096. For

extensions of time for filing returns under this section, see § 1.6081-1.

(2) *Transactional return.* In the case of a return under paragraph (e) of this section, relating to returns on a transactional basis, such return shall be filed at any time but in no event later than February 28 of the year following the calendar year in which the interest was paid. The return shall be filed with the appropriate Internal Revenue Service Center, the address of which is listed in the instructions for Form 1096. For extensions of time for filing returns under this section, see § 1.6081-1

§ 1.6049-5 Interest and original issue discount subject to reporting after December 31, 1982

(a) *Interest subject to reporting requirement.* For purposes of §§ 1.6049-4, 1.6049-6 and this section, except as provided in paragraph (b) of this section, the term "interest" means—

(1) Interest on an obligation—

(i) In registered form (as defined in § 5f.103-1(c)), or

(ii) Of a type offered to the public. Principles consistent with § 5f.163-1 shall be applied to determine whether an obligation is of a type offered to the public.

(2) Interest on deposits with persons carrying on the banking business. Such term shall include deposits evidenced by time certificates of deposit issued in any amount whether negotiable or non-negotiable. The term "interest" includes payments to a mortgage escrow account and amounts paid with respect to repurchase agreements and banker's acceptances. Property which the payee receives from the payor as interest (or in lieu of a cash payment of interest) shall be interest for purposes of section 6049. The amount subject to reporting is the fair market value of such property.

(3) Amounts, whether or not designated as interest, paid or credited by mutual savings banks, savings and loan associations, building and loan associations, cooperative banks, homestead associations, credit unions, industrial loan associations or banks, or similar organizations, in respect of deposits, face amount certificates, investment certificates, or withdrawable or repurchasable shares. Thus, even though amounts paid or credited by such organizations with respect to deposits are designated as "dividends", such amounts are included in the definition of interest for purposes of section 6049. The term "interest" includes payments to a mortgage escrow account and amounts paid with respect to repurchase agreements. Property which the payee receives from the payor as interest (or in lieu of a cash payment of interest) is

"interest" for purposes of section 6049. The fair market value of such property is the amount subject to reporting.

(4) Interest on amounts held by insurance companies under an agreement to pay interest thereon. Any increment in value of "advance premiums" "prepaid premiums", or "premium deposit funds" which is applied to the payment of premiums due on insurance policies, or made available for withdrawal by the policyholder, shall be considered interest subject to reporting. Interest that an insurance company pays pursuant to an agreement with the policyholder to a beneficiary because the payment due has been delayed is interest subject to reporting. Interest subject to reporting also includes interest paid by insurance companies with respect to policy "dividend" accumulations (see sections 61 and 451 and the regulations thereunder for rules as to when such interest is considered paid), and interest paid with respect to the proceeds of insurance policies left with the insurer. The so-called "interest element" in the case of annuity or installment payments under life insurance or endowment contracts does not constitute interest for purposes of section 6049.

(5) Interest on deposits with brokers as defined in section 6045(c) and the regulations thereunder. Any payment made in lieu of interest to a person whose obligation has been borrowed in connection with a short sale or other similar transaction is subject to reporting under section 6049.

(6) Interest paid on amounts held by investment companies as defined in section 3 of the Investment Company Act of 1940 (15 U.S.C. section 80 a-3) and on amounts invested in other pooled funds or trusts. For purposes of section 6049, interest paid on amounts invested in pooled funds or trusts, such as mortgage pass-through certificates or mortgage participation certificates, shall be considered to be the interest paid as stated on the certificate, and shall not be the interest on any notes or obligations underlying such certificates. See § 1.6049-4(c)(2) providing that in the case of interest paid on amounts invested in such pooled funds or trusts, the reporting requirements of section 6049 shall be considered satisfied if the issuer files Form 1041 as the fiduciary of a grantor trust and furnishes Form K-1 to each beneficiary, containing the information required by the form, including amounts withheld under section 3451. See § 31.3454(a)-1(a)(7) for the provisions relating to withholding.

(b) *Interest excluded from reporting requirement*—(1) *In general.* The term "interest" does not include—

(i) Interest on any obligation issued by a natural person as defined in § 1.6049-4(f)(2) irrespective of whether such interest is collected on behalf of the holder of the obligation by a middleman.

(ii) Interest on any obligation if such interest is exempt from taxation under section 103(a), relating to certain governmental obligations, or interest which is exempt from taxation under any other provision of law without regard to the identity of the holder. The holder of a tax exempt obligation must provide written certification to the payor (other than the issuer of the obligation) that the obligation is exempt from taxation. A statement that interest coupons are tax exempt on the envelope or "shell" commonly used by financial institutions to process such coupons, signed by the payee, will be sufficient for this purpose if the envelope is properly completed (*i.e.*, shows the name, address, and taxpayer identification number of the payee). A payor may rely on such written certification in treating such interest as tax exempt for purposes of section 6049. See § 1.6049-4(d)(8) with respect to the requirement that the issuer of a taxable obligation shall make an information return if such issuer receives and envelope which improperly claims that the interest coupons contained therein are tax exempt.

(iii) Interest on amounts held in escrow to guarantee performance on a contract or to provide security. However, interest on amounts held in escrow with a person described in paragraph (a) (2) or (3) of this section is interest subject to reporting under section 6049.

(iv) Interest that a governmental unit pays with respect to tax refunds.

(v) Interest on deposits posted for security, such as deposits posted with a public utility company. However, interest on deposits posted for security with a person described in paragraph (a) (2) or (3) of this section is interest subject to reporting under section 6049.

(vi) Any amount paid to—

(A) Any nonresident alien or foreign corporation, if the amount paid is subject to withholding of tax under subchapter A of chapter 3 of the Code by the person paying such amount, or

(B) Any nonresident alien or foreign corporation, if the amount paid would be subject to withholding of tax under subchapter A of chapter 3 of the Code by the person paying such amount but for the fact that—

(1) Under section 862(a)(1) such amount is considered to be from sources outside the United States,

(2) The amount is exempt from withholding of tax by reason of the provisions of a tax treaty,

(3) The amount of tax is exempt from withholding of tax under section 1441(a) or 1442(a) by reason of the application of section 1441(c) and paragraph (a) or (f) of § 1.1441-4, or

(4) The amount is original issue discount (within the meaning of section 1232 (b)(1)),

(vii) Any amount paid with respect to an obligation of, or a deposit with, an issuer or other obligor which is—

(A) A foreign government or international organization or any agency or instrumentality thereof,

(B) A foreign central bank of issue,

(C) A foreign corporation not engaged in trade or business in the United States within the calendar year of the payment,

(D) A foreign corporation, the interest payments of which would be exempt from withholding under subchapter A of chapter 3 of the Code if such an amount were paid to a person who is not a United States person, or

(E) A partnership which is not engaged in a trade or business in the United States within the calendar year of the payment and which is composed in whole of nonresident alien individuals or persons described in paragraph (b)(1)(vii) (A) through (C) of this section.

(viii) Any amount on which the person making the payment is required to deduct and withhold a tax under section 1451 (relating to tax-free covenant bonds), or would be so required but for section 1451(d) (relating to benefit of personal exemptions).

(ix) Any amount not otherwise described in paragraph (b)(1) of this section which is paid outside the United States and which is income from sources outside the United States within the meaning of section 862(a)(1).

(2) *Amount paid to persons who are not United States persons.* (i) A payor may treat an amount as an amount described in paragraph (b)(1)(vi)(A) of this section if such payor in fact withholds tax on such amount under subchapter A of chapter 3 of the Code in accordance with the provisions of chapter 3.

(ii) Unless it has actual knowledge that the payee of an amount is a United States person, a payor may treat such amount as an amount described in paragraph (b)(1)(vi)(B)(2) of this section if with respect to such amount the payor is provided by the payee with a Form 1001 in accordance with § 1.1441-6 (b) or (c), or with a certificate or

corresponding letter in accordance with § 1.1441-6(c)(3).

(iii) Unless it has actual knowledge that the payee of an amount is a United States person, a payor may treat such amount as an amount described in paragraph (b)(1)(vi)(B)(3) of this section if with respect to such amount it has received a Form 4224 from the payee in accordance with § 1.1441-4(a) or has on file with respect to such amount a notice described in § 1.1441-4(f)(2)(ii).

(iv) Unless it has actual knowledge that the payee of an amount is a United States person, a payor may treat such amount as an amount described in paragraph (b)(1)(vi)(B) (1) or (4) of this section if it receives a statement, signed by the payee under penalties of perjury, certifying that the payee is not a United States person, or, in the case that the payee is an individual, that he is neither a citizen nor a resident of the United States. In addition to such certification, the statement shall contain the name of the payee, the address of the payee, and the taxpayer identification number (if any) of the payee. The address provided for an individual shall be that of his permanent residence; the address provided for a partnership or corporation shall be the address of its principal office; and the address provided for a trust or an estate shall be the address of the permanent residence or principal office of any fiduciary of the trust or estate. The statement may be made, at the option of the payor on a Form W-8 or on a form prepared by the payor which is substantially similar to Form W-8. Blank copies of Form W-8 will be supplied to payors upon request to the district director. The statement must be received by the payor in the calendar year in which the payment is made or collected or in either of the preceding 2 calendar years. The payor, however, may require the statement from the payee each time it makes a payment to, or collects an amount on behalf of, the payee. The payor shall retain the statement for at least 4 years following the end of the last calendar year during which the amount to which the statement relates, is paid or collected. If the person providing the statement becomes a United States citizen or resident during the period to which the statement relates such person shall notify the payor in writing within 30 days of such change in status. In the case of a trust or an estate, the statement shall be provided by a fiduciary, as defined in section 7701(a)(6), on behalf of the trust or estate; and in the case of a partnership, the statement shall be provided by any general partner on behalf of the

partnership. The payor need not receive the statement described in this paragraph (b)(2)(iv) with respect to an amount paid to a payee during a calendar year if, with respect to any other payment to such payee in that year, the payor has withheld tax under subchapter A of chapter 3 of the Code in accordance with the provisions of chapter 3 or if, with respect to any amount that is or may be paid to the payee during that year, the payor has received the documentation described in paragraph (b)(2) (ii) or (iii) of this section in accordance with the provisions of § 1.1441-4 or § 1.1441-6.

(3) *Amounts paid by certain foreign obligors and amounts from sources outside the United States.* (i) The provisions of this paragraph (b)(3)(i) apply with respect to determinations made by paying agents and middlemen as to whether an amount is paid with respect to an obligation or deposit of an entity described in paragraph (b)(1)(vii) of this section and as to whether an amount is income from sources outside the United States for purposes of paragraph (b)(1)(ix) of this section. Absent actual knowledge to the contrary, a paying agent or middleman may treat an entity as a foreign government, an international organization, or a foreign central bank of issue if the paying agent or middleman could treat such entity as an exempt recipient without requiring an exemption certificate as provided in § 31.3452(c)-1 (g), (h), or (i). Absent actual knowledge to the contrary, a middleman generally may treat a corporation as a foreign corporation if its name reasonably so indicates and may treat such corporation as a corporation either which is not engaged in trade or business within the United States or the interest payments of which would be exempt from withholding under subchapter A of chapter 3 of the Code if such payments were made to a person who is not a United States person. However, a paying agent or a middleman having a contractual relationship with, the foreign corporation with respect to the payment or collection of an amount must receive a statement, signed under penalties of perjury, from the secretary or other authorized representative of the foreign corporation either that the corporation is not, or does not expect during the calendar year of payment to be, engaged in trade or business in the United States or that the interest paid by the foreign corporation would be exempt from withholding under subchapter A of chapter 3 of the Code if such interest were paid to a person who is not a

United States person. Absent actual knowledge to the contrary, a middleman generally may treat a domestic corporation as a corporation the interest payments of which would not be subject to withholding under subchapter A of chapter 3 of the Code if such payments were made to a person who is not a United States person if an annual report, offering circular, or other standard source of financial information published by the corporation reasonably so indicates. However, a paying agent or, or middleman having a contractual relationship with, a domestic corporation with respect to the payment or collection of an amount may, absent actual knowledge to the contrary, treat a domestic corporation as such a corporation only if the secretary or other authorized representative of the corporation provides the paying agent or middleman with a statement, signed under penalties of perjury, that interest paid by such corporation would not be subject to withholding under subchapter A of chapter 3 of the Code if such interest were paid to a person who is not a United States person. A paying agent or middleman may, absent actual knowledge to the contrary, treat a partnership as a partnership which is not engaged in trade or business in the United States during the calendar year of payment and which is composed in whole of nonresident alien individuals or persons described in paragraph (b)(1)(vii) (A), (B), or (C) of this section if it receives a statement, signed under penalties of perjury, from any general partner of the partnership that the partnership is not, and is not expected during the calendar year of the payment to be, engaged in trade or business in the United States and that all of its partners are, and are expected during the calendar year of payment to be, nonresident alien individuals or persons described in paragraph (b)(1)(vii) (A), (B), or (C) of this section. A statement received by a paying agent or middleman in accordance with the provisions of this paragraph (b)(3) must be provided to such paying agent or middleman in the calendar year in which a payment is made or collected or in either of the 2 preceding calendar years. The paying agent or middleman may, however, require such a statement from the corporation or partnership each time it makes a payment for the corporation or partnership. The paying agent or middleman shall retain the statement for at least 4 years following the end of the last calendar year during which an amount to which the statement relates is paid or collected. If after providing such statement the status of the corporation

or partnership changes from that reflected in the statement, the corporation or partnership shall notify the paying agent or middleman within 30 days of such change in status.

(ii) Notwithstanding the provisions of paragraph (b)(1)(vii) of this section, amounts described in such paragraph are considered to be interest for purposes of this section when paid within the United States to a United States person. In such case, the person required to report under section 6049 is the payor which makes the payment within the United States. For purposes of this paragraph, the term "United States person" is defined in section 7701(a)(30).

(iii) Paragraph (b)(3)(ii) of this section shall not apply with respect to an international organization (as described in paragraph (b)(1)(vii)(A) of this section) which is paying interest within the United States if the international organization is an organization of which the United States is a member and which enjoys immunity with respect to the inviolability of its archives pursuant to an international agreement having full force and effect in the United States.

(iv) For purposes of paragraph (b)(3)(ii) of this section, a payor may, unless it has actual knowledge to the contrary, treat a person to whom it makes a payment within the United States as a person who is not a United States person if, during the calendar year of payment, it withholds tax on any amount paid to such person under subchapter A of chapter 3 of the Code in accordance with the provisions of chapter 3 or, if, with respect to any amount which is or may be paid to such person during that calendar year, it has received documentation described in paragraph (b)(2) (ii), (iii), or (iv) of this section in accordance with the provisions of such paragraphs and of § 1.1441-4 or § 1.1441-6.

(4) *Examples.* The application of paragraph (b) of this section may be illustrated by the following examples:

Example (1). Corporation X is a foreign corporation which is not engaged in trade or business in the United States during the calendar year. A, a United States citizen, holds bonds of Corporation X that were issued in a public offering. A collects the interest on such bonds by presenting the coupons to M, a paying agent of Corporation X whose office is in the United States. Amounts paid with respect to obligations of Corporation X are generally not considered to be interest for purposes of section 6049 since Corporation X is an entity described in paragraph (b)(1)(vii)(C) of this section. However, because M makes a payment of such amounts within the United States to a

United States person, the payment by M is considered to be a payment of interest for purposes of section 6049, and M is required to report under section 6049.

Example (2). The facts are the same as in example (1) except that A presents his coupons directly to Corporation X at its office in the United States. In accordance with paragraph (b)(3)(ii) of this section, the payment by Corporation X with respect to the coupons is considered to be a payment of interest for purposes of section 6049, and Corporation X is required to report.

Example (3). The facts are the same as in example (1) except that A is a non-resident alien individual. A provides M with the statement described in paragraph (b)(2)(iv) of this section, which certifies that A is not a United States citizen or resident. Unless M has actual knowledge that the statement provided by A is false, M may rely on such statement and is not required to report under section 6049.

Example (4). The facts are the same as in example (1) except that Corporation X is engaged in trade or business in the United States and 50 percent or more of its gross income for the preceding 3-year period described in section 861(a)(1)(C) has been income which is effectively connected to its United States trade or business. Corporation X is not a beneficiary of an income tax treaty to which the United States is a party. A presents its coupons for payment directly to Corporation X at its office outside the United States. The amount paid by Corporation X is not excluded from the definition of interest for purposes of section 6049 under either paragraph (b)(1)(vii) (C) or (D) of this section since Corporation X is engaged in trade or business in the United States and since all or a portion of the interest paid by it would be subject to withholding under subchapter A of chapter 3 of the Code if such interest were paid to a person who is not a United States person. Therefore, Corporation X is required to report the amount paid to A under section 6049.

Example (5). The facts are the same as in example (4) except that Corporation X is a resident of a country which has an income tax treaty with the United States that precludes the United States from imposing tax on interest paid by residents of that country to persons who are not United States persons. Under paragraph (b)(1)(vii)(D) of this section, the amount paid by Corporation X on its bonds is not considered to be interest for purposes of section 6049 since, by reason of the application of a treaty, interest paid by Corporation X would be exempt from withholding under subchapter A of chapter 3 of the Code if such interest were paid to a person other than a United States person. Corporation X is not required to report on the amounts paid to A under section 6049.

Example (6). The facts are the same as in example (5) except that A presents its coupons from the Corporation X bonds for payment to N, a paying agent of Corporation X in the United States. The payment by N to A is considered to be a payment of interest under paragraph (b)(3)(ii) of this section, and N is required to report the payment to A under section 6049.

Example (7). Corporation Y is a domestic corporation, all of the gross income of which

for the 3-year period described in section 861(a)(1)(B) has been from sources outside the United States. B, a United States citizen holds bonds issued by Corporation Y in a public offering. B presents the coupons from such bonds for payment to Corporation Y at an office maintained by Corporation Y outside the United States. Under paragraph (b)(1)(ix) of this section, the amounts paid by Corporation Y are not considered to be interest for purposes of section 6049 since such amounts are considered to be from sources outside the United States under sections 861(a)(1)(B) and 862(a)(1) and are paid outside the United States. Corporation Y is not required under section 6049 to report its payment to B.

Example (8). D has a deposit in an account maintained with a foreign branch of R, a domestic corporation which carries on a commercial banking business. R makes payment of amounts with respect to such deposit outside the United States. Such amounts are considered to be income from sources outside the United States under sections 861(a)(1)(F)(i) and 862(a)(1) and, in accordance with paragraph (b)(1)(ix) of this section, are not considered to be interest for purposes of section 6049. Therefore, R is not required to report under section 6049 regardless of whether D is or is not a United States person.

Example (9). The facts are the same as in example (8) except that D's deposit is in a Puerto Rican branch of a United States bank. The amounts paid with respect to such deposit are income from sources outside the United States within the meaning of sections 861(a)(1)(F)(i) and 862(a)(1). In accordance with the provisions of paragraph (b)(1)(ix) of this section, such amounts are not considered to be interest for purposes of section 6049, and R is not required by section 6049 to report the amounts paid to D regardless of whether D is or is not a United States person.

Example (10). E, a nonresident alien individual, maintains an account in the United States with Corporation S, a domestic corporation which carries on a commercial banking business. S receives the statement described in paragraph (b)(2)(iv) of this section from E with respect to the amount paid on the deposit in E's account with S. The amount paid by S to E with respect to E's deposit is considered to be from sources outside the United States under sections 861(a)(1)(A) and 862(a)(1) and is not subject to withholding under subchapter A of chapter 3 of the Code. In accordance with provisions of paragraph (b)(1)(vi)(B)(1) of this section, such amount is not considered to be interest for purposes of section 6049. Thus, S is not required to report.

Example (11). U is a domestic corporation which is engaged in a commercial banking business in the United States and outside the United States through a foreign branch. F, an alien individual resident of the United States, holds a non-deposit obligation of U which is a part of a public debt issuance. F makes a demand for payment of the interest due on such obligation at the foreign branch of U. The amount paid by U is considered to be income from sources within the United States under section 861(a)(1) and is considered to be interest under section 6049. U, therefore, is

required to report the payment to F under section 6049.

Example (12). The facts are the same as in example (11) except that the obligation held by F was issued by W, a wholly-owned foreign subsidiary of U. W is not engaged in trade or business in the United States during the calendar year. F makes a demand for payment at the office of W outside the United States. Under paragraph (b)(1)(vii)(C) of this section, the amounts paid by W to F are not considered to be interest for purposes of section 6049. Therefore, W is not required under section 6049 to report the payment to F, regardless of whether F is or is not a United States person.

Example (13). Q, a domestic corporation, acts within the United States as custodian for G with respect to obligations of Z that are owned by G. G is a nonresident alien individual who is a resident of a country with which the United States has an income tax treaty. Z is a foreign corporation the interest payments of which would not be subject to withholding under subchapter A of chapter 3 of the Code if such payments were made to a person who is not a United States person. During the preceding calendar year, Q received a Form 1001 from G in accordance with the provisions of § 1.1441-6(c) with respect to interest paid on other corporate obligations held by Q on G's behalf. During the present calendar year Q collects amounts paid on the Z obligations on behalf of G. G does not give Q the statement described in paragraphs (b)(2)(iv) and (b)(3)(iv) of this section with respect to such amounts. However, as the Form 1001 submitted by G in the preceding calendar year is effective during the present calendar year with respect to certain amounts that are or may be paid to G, Q is not required to report on the amounts collected on G's behalf with respect to the Z obligations.

(c) *Original issue discount treated as payment of interest.* In determining whether an obligation is one which was issued at a discount and the amount of discount which is includible in income of the holder, a payor (other than the issuer of the obligation) may rely on the Internal Revenue Service's publication of publicly traded original issue discount obligations. In the case of an obligation as to which there is during any calendar year an amount of original issue discount includible in the gross income of any holder (as determined under sections 1232 and 1232A and the regulations thereunder), the issuer of the obligation or a middleman (as defined in § 1.6049-4(f)(4)) shall be treated as having paid to such holder during such calendar year an amount of interest equal to the amount of original issue discount so includible without regard to any reduction by reason of a purchase allowance under section 1232(a)(2)(C)(ii), 1232A(a)(6) or (b)(4) or a purchase at a premium under 1232A(c)(4)(A) or paragraph (d)(2) of § 1.1232-3. Thus, the determination of

the amount of original issue discount includible in the gross income of any holder with respect to any obligation shall be determined as if any holder of the obligation were the original holder. In the case of (1) an obligation to which section 1232A does not apply (for example, a short-term government obligation as defined in section 1232(a)(3)) and (2) an obligation issued on or before December 31, 1982, in bearer form, the amount of original issue discount includible in gross income shall be treated as if paid in the calendar year in which the date of maturity occurs or in which the date of redemption occurs if redemption occurs before maturity. The amount subject to reporting on an obligation issued in bearer form with a maturity at the date of issue of more than 1 year (a long term obligation) is the amount of original issue discount includible in the gross income of the holder during the calendar year of maturity or redemption if redemption occurs before maturity. The amount of original issue discount subject to reporting on a long term obligation shall not be reduced to reflect any purchase allowance. Discount on short term government obligations as defined in section 1232(a)(3), such as Treasury bills, and discount on other obligations with a maturity at the date of issue of not more than 1 year (a short term obligation), including commercial paper, when paid at maturity or redemption if redemption occurs before maturity, shall constitute a payment of interest for purposes of section 6049. In general, the amount subject to reporting on short term obligations is the difference between the stated redemption price at maturity and the original issue price. The procedure set forth in section 3455(b)(2)(B) and § 31.3455(b)-1(b)(3) for establishing the price at which a holder purchased an obligation subsequent to the date of original issue shall apply for purposes of section 6049. Any original issue discount on an obligation (including an obligation with a maturity of not more than 6 months from the date of original issue) held by a nonresident alien individual or foreign corporation is interest described in § 1.6049-5(b)(1)(vi)(A) or (B) and, therefore, is not interest subject to reporting under section 5f.6049.

§ 1.6049-6 Statements to recipients of interest payments and holders of obligations as to which there is attributed original issue discount after December 31, 1982.

(a) *Requirement of furnishing statement to recipient.* Every person filing a Form 1099 under section 6049(a) and § 1.6049-4(e) shall furnish to the person whose identifying number is

required to be shown on the form a written statement showing the information required by paragraph (b) of this section. With respect to interest other than interest reported on a transactional basis under § 1.6049-4(e), no statement is required to be furnished under section 6049(c) and this section if the aggregate of the payments for the calendar year is less than \$10, unless such payment is subject to the tax imposed under section 3451. In the case of any payment that is subject to withholding under section 3451, a statement shall be furnished irrespective of the amount of the payment. With respect to payments which are reported on a transactional basis, no statement is required to be furnished under section 6049(c) and this section to a person if the payment of interest to (or received on behalf of) such person for the transaction is less than \$10 unless the payment is subject to withholding under section 3451. Again, in the case of any payment that is subject to withholding under section 3451, a statement shall be furnished irrespective of the amount of the payment.

(b) *Form of statement.* The written statement required to be furnished to a person under paragraph (a) of this section shall show the following information:

(1) With respect to payments of interest (other than original issue discount) to any person during a calendar year, the statement shall show—

(i) The aggregate amount of payments shown on Form 1099 as having been made to (or received on behalf of) such person;

(ii) The amount of tax withheld under section 3451, if any;

(iii) The name and address of the person filing the form; and

(iv) A legend stating that such amount is being reported to the Internal Revenue Service.

(2) With respect to original issue discount includible in the gross income of a holder of an obligation during a calendar year, the statement shall show—

(i) The aggregate amount of original issue discount includible in the gross income by (or on behalf of) such person for the calendar year with respect to the obligation (determined by applying the rules of paragraph (b)(2) of § 1.6049-4);

(ii) The amount of tax withheld under section 3451, if any;

(iii) The account, serial, or other identifying number of each obligation with respect to which a return is being made;

(iv) All other items shown on Form 1099 for such calendar year, and

(v) A legend stating that such amount and such items are being reported to the Internal Revenue Service.

(c) *Time for furnishing statements.* Each statement required by this section to be furnished to any person for a calendar year with respect to a payment of interest (other than interest where a middleman or a Federal agency makes a return on a transactional basis (as described in paragraph (e) of § 1.6049-4)) shall be furnished to such person after April 30 of the year of payment and on or before January 31 of the following year, but no statement may be furnished before the final interest payment for the calendar year. If a middleman or a Federal agency makes a return on a transactional basis, the statement shall be furnished at, or any time subsequent to, the time of payment, but in no event later than January 31 of the year following the calendar year of payment.

(d) *Special rule.* The requirements of this section for the furnishing of a statement to any person, including the legend requirement of paragraph (b)(1)(iv) and (2)(v) of this section, may be met by the furnishing to such person a copy of the Form 1099 filed pursuant to § 1.6049-4, or a reasonable facsimile thereof, in respect of such person. However, in the case of Form 1099 with respect to original issue discount on obligations subject to section 1232A, a copy of the instructions must also be sent to such person. A statement shall be considered to be furnished to a person within the meaning of this section if it is mailed to such person at his last known address.

PART 5f—[AMENDED]

§§ 5f.6049-1, 5f.6049-2 and 5f.6049-3
[Removed]

Par. 6. Sections 5f.6049-1, 5f.6049-2, and 5f.6049-3 of the Temporary Income Tax Regulations under the Tax Equity and Fiscal Responsibility Act of 1982 (26 CFR Part 5f) are hereby removed.

This Treasury decision is issued under authority contained in sections 6049 (a), (b), and (d) and 7805 of the Internal Revenue Code of 1954 (96 Stat. 592, 594; 26 U.S.C. 6049 (a), (b), and (d); 68A Stat. 917, 26 U.S.C. 7805), and in section 309 of the Tax Equity and Fiscal Responsibility Act of 1982 (96 Stat. 591).

Roscoe L. Egger, Jr.,

Commissioner of Internal Revenue.

Approved: March 16, 1983.

John E. Chapoton,

Assistant Secretary of the Treasury.

[FR Doc. 83-7716 Filed 3-22-83; 1:23 pm]

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NASD

National Association of Securities Dealers, Inc.
1735 K St., N.W. • Washington, D.C. 20006 • (202) 728-8000

notice to members 83-40

July 25, 1983

TO: All NASD Members and Other Interested Persons

RE: Quarterly Checklist of Notices to Members

Following is a list of NASD Notices to Members issued during the second quarter of 1983. Requests for copies of any notice should be accompanied by a self-addressed label and may be directed to: NASD Administrative Services, 1735 K Street, N.W., Washington, D.C. 20006.

| <u>Notice Number</u> | <u>Date</u> | <u>Topic</u> |
|----------------------|----------------|--|
| 83-15 | April 8, 1983 | Underwriting Compensation Received by Members in Public Corporate Offerings |
| 83-16 | April 8, 1983 | Applicability of SEC Rule 10b-6 to Controlled Accounts |
| 83-17 | April 14, 1983 | Amendments to Rules Governing Transactions Executed for Persons Associated with Another Member |
| 83-18 | April 22, 1983 | 43 Additional Securities Are Mandated Into National Market System |
| 83-19 | April 27, 1983 | Approval of Revisions to Qualification Requirements of Foreign Issues on NASDAQ |
| 83-20 | May 2, 1983 | Quarterly Checklist of Notices to Members |
| 83-21 | May 5, 1983 | Gerald Greenspan - Notification of Past Illegal Activities |

| <u>Notice Number</u> | <u>Date</u> | <u>Topic</u> |
|----------------------|---------------|---|
| 83-22 | May 11, 1983 | Real-Time Transaction Reporting in Additional 57 NASDAQ NMS Securities Effective May 24, 1983 |
| 83-23 | May 11, 1983 | Memorial Day Trade Date-Settlement Date Schedule |
| 83-24 | May 19, 1983 | Request for Vote on Proposed Corporate Financing Rule |
| 83-25 | May 27, 1983 | Request for Comments on Amendment to Corporate Financing Filing Requirements |
| 83-26 | June 1, 1983 | Adoption of Amendments to Interpretation on Free-Riding and Withholding |
| 83-27 | June 6, 1983 | Appointment of SIPC Trustee for Gibrasco, Inc. |
| 83-30 | June 27, 1983 | Independence Day Trade Date-Settlement Date Schedule |

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NASDNational Association of Securities Dealers, Inc.
1735 K St., N.W. • Washington, D.C. 20006 • (202) 728-8000**notice to members 83-41**

July 25, 1983

TO: All NASD Members and Other Interested Persons

RE: SEC Staff Issues No-Action Letter Providing Temporary Relief from Certain Provisions of Rules 15c3-1 and 15c3-3 Dealing with Municipal Securities

SUMMARY

Recently, in response to a request by the Association, the staff of the SEC's Division of Market Regulation issued a no-action letter concerning 17 C.F.R. 240.15c3-1 (the "net capital rule") and 17 C.F.R. 240.15c3-3 (the "customer protection rule"). The letter provides, until December 31, 1983, a temporary extension of certain time periods specified in the rules before which capital deductions and/or other actions are required to be taken for transactions involving registered municipal securities.

The Association's request was prompted by a concern on the part of its Capital and Margin Committee, and others, that the issuance of municipal securities in registered form, as required by the provisions of the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA), would have a deleterious effect on the clearance and settlement of municipal securities transactions which, in turn, would subject broker-dealers to increased capital and reserve requirements in accordance with the provisions of the net capital and customer protection rules. A brief discussion of the background concerning the Association's request, and the sections of the rules affected as a result thereof, follows. Also, a copy of the letter issued by the Division of Market Regulation is reprinted as part of this Notice.

BACKGROUND

The Tax Equity and Fiscal Responsibility Act of 1982, which was signed into law on September 3, 1982, contains a number of provisions affecting the broker-dealer community. The Association has taken an active role in attempting to assess the impact of the new law by identifying various areas of concern to its members. One such area is the issuance of municipal securities in registered form.

Under the provisions of TEFRA, municipal securities issued after July 1, 1983, must be issued solely in registered form, both as to principal and interest, in order to preserve their tax-exempt status. ^{1/} The registration requirement, however, does not change the status of municipal securities as exempt securities under the Securities Exchange Act of 1934 (the "1934 Act"). Therefore, issuing municipalities would not be required to use registered transfer agents who are subject to SEC rules regarding "turnaround" time for transfer items.

Municipal securities broker-dealers were concerned that the performance of the transfer function by issuers and unregistered transfer agents would increase the number of aged fails in the marketplace. The SEC's net capital and customer protection rules, which set forth methods of measuring the adequacy of a broker-dealer's capital and customer-related reserves, contain provisions, among others, which penalize the broker-dealer for: (1) transactions remaining uncompleted beyond specified dates after settlement; and, (2) transfer items which have not been returned from transfer after a specified time. If significant delays develop in the transfer process, causing clearance problems and an increase in the number of uncompleted transactions, broker-dealers would be subject to much higher capital penalties.

The Association believed that these were very real concerns on the part of municipal securities broker-dealers. In connection therewith, the NASD conducted a survey of selected municipal securities broker-dealers to gather data with respect to the aging of fails in municipal securities. Eight broker-dealers participated in the survey and supplied information regarding total aged fails and total mortgage revenue bond fails ^{2/} for the period September 1981 through January 1982 and correspondingly for the period September 1982 through January 1983. The findings of the survey supported the contention that the requirement to register previously unregistered securities results in an increase in total aged fails.

The Association was not alone in expressing concern over this situation. A number of industry groups including the Municipal Securities Rulemaking Board ("MSRB") and Public Securities Association ("PSA") have also undertaken actions with respect to the question of registration. On October 18, 1982, the PSA issued a white paper which, among other things, called for net capital relief for municipal securities in fail situations due to the action of transfer agents. Also, in October 1982, the MSRB conducted a two-day conference for all segments of the municipal industry on registered municipal securities in an effort to identify problems and to propose solutions. One of the many recommendations which came forth from the

^{1/} TEFRA exempts from this registration requirement securities with maturities of one year or less; securities which are not of a type offered to the public; and, securities which are sold to non-U.S. nationals and are payable outside the United States.

^{2/} So that an adequate comparison could be made, the Association requested information with respect to the impact that the registration of mortgage revenue bonds has had on the municipal marketplace. Mortgage revenue bonds were required to be issued in registered form as of January 31, 1982, a situation analogous to the overall registration requirement concerning municipal securities.

conference was the recommendation to liberalize certain of the provisions of the net capital and customer protection rules as they would apply to transactions in registered municipal securities.

In light of the above findings and discussions, the Association petitioned the Commission to extend by interpretation relevant time periods in the net capital and customer protection rules as applicable to registered municipal securities. The following is a summary of the Commission's no-action letter granting such relief.

SEC Rule 15c3-1

The no-action letter issued by the SEC's Division of Market Regulation provides relief in the following instances which would otherwise affect the capital requirements of a broker-dealer relative to its transactions in municipal securities in accordance with the provisions of SEC Rule 15c3-1.

- Subparagraph (c)(2)(ix) provides for a deduction from net capital for those municipal fails to deliver which are outstanding for 21 business days or longer. This time period has been extended to 30 business days for transactions involving registered municipal securities.
- Under subparagraph (c)(2)(iv)(B), an existing interpretation provides that broker-dealers must make appropriate deductions from net worth for deficits in cash accounts for C.O.D. transactions involving municipal securities 42 calendar days after trade date. This time period has been extended to 60 calendar days after trade date for such transactions involving registered municipal securities.
- Subparagraph (a)(8) permits a municipal securities broker's broker to compute its capital requirements in accordance with specified guidelines. In this regard, subparagraph (a)(8)(iv) requires such a broker to make a deduction from net worth equal to 1% of the market value of the underlying security for municipal securities fails to deliver which are outstanding for 21 business days or longer. This time period has been extended to 30 business days for fails to deliver involving registered municipal securities.

SEC Rule 15c3-3

In its no-action letter, the staff of the Division of Market Regulation provides an extension of the time period applicable to municipal securities fails to deliver as specified in the Reserve Formula computed in accordance with SEC Rule 15c3-3.

- In computing its reserve requirement, a broker-dealer is required to exclude from the debit side of the formula fails to deliver which are outstanding more than 30 calendar days. This time period has been extended to 45 calendar days for fails to deliver involving registered municipal securities.

Reporting Requirement

The SEC staff as a condition for granting relief in this area is requiring the designated examining authority to secure data from each broker-dealer who takes advantage of a temporary extension. A broker-dealer who determines to avail itself of such relief would be required to supply data concerning aged fail(s) on a monthly basis as of its FOCUS Part I filing date. The information would be submitted to the firm's designated examining authority which will then forward the information to the SEC.

In this regard, an Association member for whom the NASD is the designated examining authority is requested to complete the enclosed form and submit it to the Association along with its FOCUS Part I Report for each month in which the member relies on any of the extensions for aged fails permitted by the SEC's temporary no-action letter. This form must be submitted even if the member uses the interpretation in only one instance.

As you will note, the form has been designed to collect information on a cumulative basis; the member may use one form to record its data each month. In this regard, the member must furnish the following information for fails involving registered municipal securities when taking interpretive relief.

- the number of such fails which exceed 21 business days;
- the contract values of the fails;
- the age of the fails;
- the number of issuers and transfer agents responsible for the delays; and,
- the number of broker-dealers who have failed to deliver to the reporting broker-dealer.

Members are reminded that the relief provided by the no-action letter is available only for fails involving registered municipal securities and is effective only through December 31, 1983.

* * *

Questions concerning this Notice may be directed to James M. Cangiano, Assistant Director, Department of Policy Research, at (202) 728-8273. Questions regarding the filing and the completion of the attached form should be referred to your local NASD District office.

Sincerely,


Gordon S. Macklin
President

Attachments

**SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Division of Market Regulation**

July 7, 1983

Mr. Gordon S. Macklin
President
National Association of
Securities Dealers, Inc.
1735 K Street, N.W.
Washington, D.C. 20006

Dear Mr. Macklin:

In your letter of June 15, 1983, you describe the problems which might arise from the required registration of municipal securities issued after July 1, 1983. You state that municipal broker-dealers will encounter delays in transferring the securities after sale or resale. These delays you believe may result in unwarranted deductions under the net capital rule and the customer protection rule. You recommend that provisions of the net capital rule and Rule 15c3-3 which require deductions for aged municipal securities failed to deliver be altered, for these registered securities. The NASD is requesting for its members temporary interpretative relief only and not a permanent rule change.

You believe that these further delays will be caused because neither issuers which do their own transferring nor unregistered transfer agents are subject to regulatory restraints comparable to those of Rule 17Ad-2 of the Securities Exchange Act. In connection with its concerns, the NASD conducted a survey of selected municipal securities broker-dealers to gather data with respect to the aging of fails in municipal securities. So that an adequate comparison could be made, the NASD requested information with respect to the impact that the registration of mortgage revenue bonds has had on the municipal marketplace. Mortgage revenue bonds were required to be issued in registered form as of January 31, 1982. Eight broker-dealers supplied information regarding total aged fails and total mortgage revenue bond fails for the period September 1981 through January 1982 and correspondingly for the period September 1982 through January 1983.

The findings of the survey support the contention that the requirement to register previously unregistered securities results in an increase in total aged fails. From one year to the next, total aged fail items showed an increase of 93%, and there was a corresponding increase of 246% in the dollar amount represented by these items. However, the statistics indicate even greater increases when mortgage revenue bond fails are considered separately. The total number of mortgage revenue bond fails showed an increase of 525%, with a corresponding increase in

Mr. Gordon S. Macklin
Page Two

dollar amount of 2580%. In the period September 1981 through January 1982, mortgage revenue bond fails represented 3.1% of the total aged fails; for the period September 1982 through January 1983, they represented 10.0% of the total aged fails; however, they represented 17.4% of the total aged fails which constitute the increase from 1981/1982 to 1982/1983.

The Division shares your concerns that the present change in the form of registration should not result in unwarranted charges to broker-dealers in municipal securities. However, we are equally concerned that this change not be used as a mechanism to excuse delay in the completion of securities transactions. The Commission, as you are aware, in a recent release stressed the need for reduction in the aging period for fails in municipal securities.

In sum, we are sympathetic to the need for relief particularly as to the period for aging municipal securities fails to deliver. However, as a condition for granting relief in this area, the designated examining authority ("DEA") for each broker or dealer who takes advantage of any extension in the aging period must secure from that firm data on these fails which should be provided to the Commission in a report by the DEA. Specifically, we request data on the number of fails as to registered bonds which exceed 21 business days, their contract values, the age of the fails to deliver, the number of issuers and transfer agents responsible for the delays and the number of brokers who have failed to deliver to the reporting broker-dealer. This data should be obtained monthly as of the FOCUS filing date. It may be presented to the Commission in whatever form the DEA thinks most appropriate.

Based on the circumstances described above, the Division will raise no question nor recommend any action to the Commission until December 31, 1983 if (1) broker-dealers in computing net capital make required deductions under Rule 15c3-1(c)(2)(ix) from the contract value of fails to deliver of registered municipal securities only after the fails to deliver are outstanding 30 business days or longer; (2) broker-dealers in computing the reserve requirements under Rule 15c3-3 remove failed to deliver contracts of registered municipal securities only if older than 45 calendar days; and (3) broker-dealers in computing net capital make appropriate deductions from net worth under Rule 15c3-1(c)(2)(iv)(B) for C.O.D. transactions involving registered municipal securities only after 60 calendar days after trade date; and (4) those broker-dealers which have elected paragraph (a)(8) of the net capital rule make the required deduction as to fails to deliver contracts of registered municipal securities only after the fail is outstanding 30 business days or longer.

Sincerely,

/s/
Edward A. Kwalwasser
Associate Director

cc: Heather L. Ruth
Executive Director
Public Securities Association