

HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 96-24, page 5.

Federal rates; adjusted federal rates; adjusted federal long-term rate, and the long-term exempt rate. For purposes of sections 1274, 1288, 382, and other sections of the Code, tables set forth the rates for May 1996.

Rev. Rul. 96-25, page 4.

Fringe benefits aircraft valuation formula. For purposes of section 1.61-21(g) of the regulations, relating to the rule for valuing non-commercial flights on employer-provided aircraft, the Standard Industry Fare Level (SIFL), cents-per-mile rates, and terminal charges in effect for 1996 are set forth. Rev. Rul. 95-66 modified.

**INTL-062-90; INTL-0032-93; INTL-52-86;
INTL-52-94, page 26.**

General revision of regulations under Chapter 3 of the Code relating to withholding of tax on U.S. source income paid to foreign persons and related collection, refunds, and credits; revision of information reporting regulations under subpart B of Chapter 61 and backup withholding regulations under section 3406; and removal of regulations under part 35a and certain regulations under income tax treaties.

EXEMPT ORGANIZATIONS

Announcement 96-39, page 84.

Families for Children, Golden Valley, MN, no longer qualifies as an organization to which contributions are deductible under section 170 of the Code.

EXCISE TAX

Notice 96-28, page 7.

A determination has been made to add butyl benzyl phthalate to the list of taxable substances in section 4672(a)(3) of the Code.

ADMINISTRATIVE

Notice 96-29, page 7.

Credit for producing fuel from a nonconventional source, section 29 inflation adjustment factor, and section 29 reference price. This notice publishes the section 29 inflation adjustment factor, nonconventional source fuel credit, and the section 29 reference price for calendar year 1995. These data are used to determine the credit allowable on fuel produced from a nonconventional source under section 29 of the Code.

Rev. Proc. 96-30, page 8.

Section 355 checklist questionnaire. This procedure sets forth in a checklist questionnaire the information that must be included in a request for rulings under section 355.

Announcement 96-38, page 84.

The instructions for Schedule SSA (Form 5500), Annual Registration Statement Identifying Separated Participants With Deferred Vested Benefits, are corrected.

Announcement 96-40, page 85.

T.D. 8653, 1996-12 I.R.B. 4, relating to the character and timing of gain or loss from certain hedging transactions entered into by members of a consolidated group, is corrected.

Finding Lists begin on page 87.

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenue at the least cost; serve the public by continually improving the

quality of our products and services; and perform in a manner warranting the highest degree of public confidence in our integrity, efficiency and fairness.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1986 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1986.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts. Also included in this part are Bank Secrecy Act Administrative Rulings. Bank Secrecy Act Administrative Rulings are issued by the Department of the Treasury's Office of the Assistant Secretary (Enforcement).

Part IV.—Items of General Interest.

With the exception of the Notice of Proposed Rulemaking and the disbarment and suspension list included in this part, none of these announcements are consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provides (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

The contents of this publication are not copyrighted and may be reprinted freely. A citation of the Internal Revenue Bulletin as the source would be appropriate.

For sale by the Superintendent of Documents U.S. Government Printing Office, Washington, D.C. 20402.

Part I. Rulings and Decisions Under the Internal Revenue Code of 1986

Section 61.—Gross Income Defined

26 CFR 1.61-21: Taxation of fringe benefits.

Fringe benefits aircraft valuation formula. For purposes of section 1.61-21(g) of the regulations, relating to the rule for valuing non-commercial flights on employer-provided aircraft, the Standard Industry Fare Level (SIFL), cents-per-mile rates and terminal charges in effect for 1996 are set forth. Rev. Rul. 95-66 modified.

Rev. Rul. 96-25

For purposes of the taxation of fringe benefits under section 61 of the Internal Revenue Code, section 1.61-21(g) of the Income Tax Regulations provides a rule for valuing noncommercial flights on employer-provided aircraft. Section 1.61-21(g)(5) of the Income Tax Regulations provides an aircraft valuation formula to determine the value of such flights. The value of a flight is determined under the base aircraft valuation formula (also known as the Standard

Industry Fare Level formula or SIFL) by multiplying the SIFL cents-per-mile rates applicable for the period during which the flight was taken by the appropriate aircraft multiple provided in section 1.61-21(g)(7) and then adding the applicable terminal charge. The SIFL cents-per-mile rates in the formula and the terminal charge are calculated by the Department of Transportation and are revised semi-annually.

The following chart sets forth the terminal charges and SIFL mileage rates:

Period During Which the Flight Was Taken

1/1/96-6/30/96

Terminal Charge

\$32.20

SIFL Mileage Rates

Up to 500 miles = \$.1761 per mile

501-1500 miles = \$.1343

Over 1500 miles = \$.1291

EFFECT ON OTHER REVENUE RULING

Rev. Rul. 95-66, 1995-40 I.R.B. 4, is modified.

DRAFTING INFORMATION

The principal author of this Revenue ruling is Thomas R. Foley of the Office of the Associate Chief Counsel (Employee Benefits and Exempt Organizations). For further information regarding this revenue ruling contact Mr. Foley on (202) 622-6050 (not a toll-free call).

Section 42.—Low-Income Housing Credit

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of May 1996. See Rev. Rul. 96-24, page 5.

Section 280G.—Golden Parachute Payments

Federal short-term, mid-term, and long-term rates are set forth for the month of May 1996. See Rev. Rul. 96-24, page 5.

Section 355.—Distribution of stock and securities of a controlled corporation

25 CFR 1.355-1: Distribution of stock and securities of a controlled corporation.

The revenue procedure sets forth in a checklist questionnaire the information that must be included in a request for rulings under § 355. See Rev. Proc. 96-30, page 8.

Section 382.—Limitation on Net Operating Loss Carryforwards and Certain Built-In Losses Following Ownership Change

The adjusted federal long-term rate is set forth for the month of May 1996. See Rev. Rul. 96-24, page 5.

Section 412.—Minimum Funding Standards

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of May 1996. See Rev. Rul. 96-24, page 5.

Section 467.—Certain Payments for the Use of Property or Services

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of May 1996. See Rev. Rul. 96-24, page 5.

Section 468.—Special Rules for Mining and Solid Waste Reclamation and Closing Costs

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of May 1996. See Rev. Rul. 96-24, page 5.

Section 483.—Interest on Certain Deferred Payments

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of May 1996. See Rev. Rul. 96-24, page 5.

Section 807.—Rules for Certain Reserves

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of May 1996. See Rev. Rul. 96-24, page 5.

Section 846.—Discounted Unpaid Losses Defined

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of May 1996. See Rev. Rul. 96-24, page 5.

Section 1274.—Determination of Issue Price in the Case of Certain Debt Instruments Issued for Property

(Also Sections 42, 280G, 382, 412, 467, 468, 482, 483, 807, 846, 1288, 7520, 7872.)

Federal rates; adjusted federal rates; adjusted federal long-term rate, and the long-term exempt rate. For purposes of sections 1274, 1288, 382, and other sections of the Code, tables set forth the rates for May 1996.

Rev. Rul. 96-24

This revenue ruling provides various prescribed rates for federal income tax purposes for May 1996 (the current month.) Table 1 contains the short-term, mid-term, and long-term applicable federal rates (AFR) for the current month for purposes of section 1274(d) of the Internal Revenue Code. Table 2 contains the short-term, mid-term, and long-term adjusted applicable federal rates (adjusted AFR) for the current month for purposes of section 1288(b).

Table 3 sets forth the adjusted federal long-term rate and the long-term tax-exempt rate described in section 382(f). Table 4 contains the appropriate percentages for determining the low-income housing credit described in section 42(b)(2) for buildings placed in service during the current month. Finally, Table 5 contains the federal rate for determining the present value of an annuity, an interest for life or for a term of years, or a remainder or a reversionary interest for purposes of section 7520.

REV. RUL. 96-24 TABLE 1				
Applicable Federal Rates (AFR) for May 1996				
	<i>Period for Compounding</i>			
	<i>Annual</i>	<i>Semiannual</i>	<i>Quarterly</i>	<i>Monthly</i>
<i>Short-Term</i>				
AFR	5.76%	5.68%	5.64%	5.61%
110 AFR	6.35%	6.25%	6.20%	6.17%
120 AFR	6.94%	6.82%	6.76%	6.73%
130 AFR	7.52%	7.38%	7.31%	7.27%
<i>Mid-Term</i>				
AFR	6.36%	6.26%	6.21%	6.18%
110 AFR	7.01%	6.89%	6.83%	6.79%
120 AFR	7.65%	7.51%	7.44%	7.40%
130 AFR	8.31%	8.14%	8.06%	8.01%
150 AFR	9.61%	9.39%	9.28%	9.21%
175 AFR	11.26%	10.96%	10.81%	10.72%
<i>Long-Term</i>				
AFR	6.83%	6.72%	6.66%	6.63%
110 AFR	7.53%	7.39%	7.32%	7.28%
120 AFR	8.22%	8.06%	7.98%	7.93%
130 AFR	8.93%	8.74%	8.65%	8.58%

REV. RUL. 96-24 TABLE 2				
Adjusted AFR for May 1996				
	<i>Period for Compounding</i>			
	<i>Annual</i>	<i>Semiannual</i>	<i>Quarterly</i>	<i>Monthly</i>
Short-term adjusted AFR	3.75%	3.72%	3.70%	3.69%
Mid-term adjusted AFR	4.69%	4.64%	4.61%	4.60%
Long-term adjusted AFR	5.68%	5.60%	5.56%	5.54%

REV. RUL. 96-24 TABLE 3

Rates Under Section 382 for May 1996

Adjusted federal long-term rate for the current month	5.68%
Long-term tax-exempt rate for ownership changes during the current month (the highest of the adjusted federal long-term rates for the current month and the prior two months.)	5.68%

REV. RUL. 96-24 TABLE 4

Appropriate Percentages Under Section 42(b)(2) for May 1996

Appropriate percentage for the 70% present value low-income housing credit	8.55%
Appropriate percentage for the 30% present value low-income housing credit	3.66%

REV. RUL. 96-24 TABLE 5

Rate Under Section 7520 for May 1996

Applicable federal rate for determining the present value of an annuity, an interest for life or a term of years, or a remainder or reversionary interest	7.6%
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Section 1288.—Treatment of Original Issue Discount on Tax-Exempt Obligations

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of May 1996. See Rev. Rul. 96-24, page 5.

Section 7520.—Valuation Tables

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of May 1996. See Rev. Rul. 96-24, page 5.

Section 7872.—Treatment of Loans with Below-Market Interest Rates

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of May 1996. See Rev. Rul. 96-24, page 5.

Part III. Administrative, Procedural, and Miscellaneous

Tax on Certain Imported Substances; Notice of Determination

Notice 96-28

This notice announces a determination, under Notice 89-61, 1989-1 C.B. 717, that the list of taxable substances in § 4672(a)(3) will be modified to include butyl benzyl phthalate. This modification is effective April 1, 1991.

Background

Under § 4672(a), an importer or exporter of any substance may request that the Secretary determine whether that substance should be listed as a taxable substance. The Secretary shall add the substance to the list of taxable substances in § 4672(a)(3) if the Secretary determines that taxable chemicals constitute more than 50 percent of the weight, or more than 50 percent of the value, of the materials used to produce the substance. This determination is to be made on the basis of the predominant method of production. Notice 89-61, sets forth the rules relating to the determination process.

Determination

On March 22, 1996, the Secretary determined that butyl benzyl phthalate should be added to the list of taxable substances in § 4672(a)(3), effective April 1, 1991.

The rate of tax prescribed for butyl benzyl phthalate, under § 4671(b)(3), is \$5.54 per ton. This is based upon a conversion factor for methane of 0.05, a conversion factor for propylene of 0.17, a conversion factor for xylene of 0.47, a conversion factor for toluene of 0.32, and a conversion factor for chlorine of 0.26.

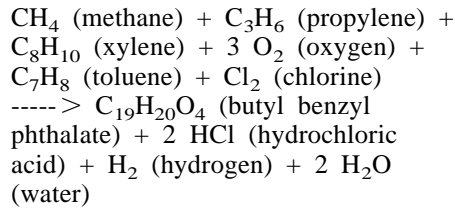
The petitioner is Monsanto Company, a manufacturer and exporter of this substance. No material comments were received on this petition. The following information is the basis for the determination.

HTS number: 2917.39.2000
CAS number: 85-68-7

Butyl benzyl phthalate is derived from the taxable chemicals methane, propylene, xylene, toluene, and chlo-

rine and is a liquid produced predominantly by the reaction of n-butanol and phthalic anhydride, followed by a reaction with benzyl chloride in the presence of a catalyst. n-butanol is manufactured by the hydrogenation of n-butyraldehyde, which is derived from propylene and synthesis gas (hydrogen and synthesis gas are derived from natural gas). Benzyl chloride is produced by direct photochemical chlorination of toluene. Phthalic anhydride is produced by the reaction of o-xylene with air in the presence of a catalyst.

The stoichiometric material consumption formula for this substance is:



Butyl benzyl phthalate has been determined to be a taxable substance because a review of its stoichiometric material consumption formula shows that, based on the predominant method of production, taxable chemicals constitute 77.25 percent by weight of the materials used in its production.

The principal author of this notice is Ruth Hoffman, Office of Assistant Chief Counsel (Passthroughs and Special Industries). For further information regarding this notice contact Ruth Hoffman on (202) 622-3130 (not a toll-free number).

Credit for Producing Fuel From a Nonconventional Source, Section 29 Inflation Adjustment Factor, and Section 29 Reference Price

Notice 96-29

This notice publishes the § 29 inflation adjustment factor, the nonconventional source fuel credit, and the § 29 reference price for calendar year 1995. These are used to determine the credit allowable on fuel produced from a nonconventional source under § 29 of the Internal Revenue Code. The calendar year 1995 inflation-adjusted credit applies to the sales of barrel-of-oil equivalent of qualified fuels sold by a taxpayer to an unrelated person during

the 1995 calendar year, the domestic production of which is attributable to the taxpayer.

BACKGROUND

Section 29(a) provides for a credit for producing fuel from a nonconventional source, measured in barrel-of-oil equivalent of qualified fuels, the production of which is attributable to the taxpayer and sold by the taxpayer to an unrelated person during the tax year. The credit is equal to the product of \$3.00 and the appropriate inflation adjustment factor.

Section 29(b)(1) and (2) provides for a phaseout of the credit. The credit allowable under § 29(a) must be reduced by an amount which bears the same ratio to the amount of the credit (determined without regard to § 29(b)(1)) as the amount by which the reference price for the calendar year in which the sale occurs exceeds \$23.50 bears to \$6.00. The \$3.00 in § 29(a) and the \$23.50 and \$6.00 must each be adjusted by multiplying these amounts by the 1995 inflation adjustment factor. In the case of gas from a tight formation, the \$3.00 amount in § 29(a) must not be adjusted.

Section 29(c)(1) defines the term "qualified fuels" to include oil produced from shale and tar sands; gas produced from geopressurized brine, Devonian shale, coal seams, or a tight formation, or biomass; and liquid, gaseous, or solid synthetic fuels produced from coal (including lignite), including such fuels when used as feedstocks.

Section 29(d)(1) provides that the credit is to be applied only for sale of qualified fuels the production of which is within the United States (within the meaning of § 638(1)) or a possession of the United States (within the meaning of § 638(2)).

Section 29(d)(2)(A) requires that the Secretary, not later than April 1 of each calendar year, determine and publish in the Federal Register the inflation adjustment factor and the reference price for the preceding calendar year.

Section 29(d)(2)(B) defines "inflation adjustment factor" for a calendar year as the fraction the numerator of which is the GNP implicit price deflator for the calendar year and the

denominator of which is the GNP implicit price deflator for calendar year 1979. The term "GNP implicit price deflator" means the first version of the implicit price deflator for the gross national product as computed and published by the Department of Commerce.

Section 29(d)(2)(C) defines "reference price" to mean with respect to a calendar year the Secretary's estimate of the annual average wellhead price per barrel of all domestic crude oil the price of which is not subject to regulation by the United States.

Section 29(d)(3) provides that in the case of a property or facility in which more than one person has an interest, except to the extent provided by regulations prepared by the Secretary, production from the property or facility (as the case may be) must be allocated among the persons in proportion to their respective interests in the gross sales from the property or facility.

Section 29(d)(5) and (6) provides that the term "barrel-of-oil equivalent" with respect to any fuel generally means that amount of the fuel which has a Btu content of 5.8 million.

INFLATION ADJUSTMENT FACTOR AND REFERENCE PRICE

The inflation adjustment factor for calendar year 1995 is 1.9439. The reference price for calendar year 1995 is \$14.62. As required by § 29(d)-(2)(A), the inflation adjustment factor and reference price for calendar year 1995 where published in the Federal Register on April 10, 1996 (61 Fed. Reg. 16031).

PHASE-OUT CALCULATION

Because the calendar year 1995 reference price does not exceed \$23.50 multiplied by the inflation adjustment factor, the phaseout of the credit

provided for in § 29(b)(1) does not occur for any qualified fuel sold in calendar year 1995.

CREDIT AMOUNT

The nonconventional source fuel credit under § 29(a) is \$5.83 per barrel-of-oil equivalent of qualified fuels ($\$3.00 \times 1.9439$). This amount was published in the Federal Register on April 10, 1996 (61 Fed. Reg. 16031).

DRAFTING INFORMATION CONTACT

The principal author of this notice is David G. McMunn of the Office of Assistant Chief Counsel (Passthroughs and Special Industries). For further information regarding this notice contact Mr. McMunn on (202)622-3110 (not a toll-free call).

26 CFR 601.201: Rulings and determination letters.
(Also Part I, § 355; 1.355-1.)

Rev. Proc. 96-30

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SECTION 1. PURPOSE

This revenue procedure updates Rev. Proc. 86-41, 1986-2 C.B. 716, which sets forth in a checklist questionnaire the information that must be included in a request for rulings under § 355, relating to the nonrecognition of gain or loss on distributions of stock and securities of controlled corporations.

SECTION 2. BACKGROUND

This checklist is intended to facilitate the filing and processing of ruling requests under § 355. It specifies information and representations to be included so that the requests will be as complete as possible when initially filed. Nevertheless, because the information and representations necessary to rule on a particular transaction depend upon all the facts and circumstances, the Service may require information or representations in addition to those set forth in this revenue procedure.

The general procedures of the Internal Revenue Service with respect to the issuance of letter rulings and determination letters by the National Office are outlined in the first revenue procedure published each year (the “**annual revenue procedure**”). *See, e.g.*, Rev. Proc. 96–1, 1996–1 I.R.B. 8. The Service also publishes a revenue procedure, generally in the first Internal Revenue Bulletin of the year, which provides a list of those areas of the Code under the jurisdiction of the Associate Chief Counsel (Domestic) for which the Service will not issue advance letter rulings. *See, e.g.*, Rev. Proc. 96–3, 1996–1 I.R.B. 82. The Service periodically updates these revenue procedures, along with this checklist questionnaire.

Careful attention to all requirements of the most recent revenue procedures, including this checklist questionnaire, will aid in the timely processing of ruling requests. Failure to submit the requisite information and representations will often delay consideration of the transaction and the issuance of a letter ruling.

This revenue procedure substantially modifies Rev. Proc. 86–41. The principal changes are to add to, delete, or modify the information and representations requested, and to add an appendix that provides guidelines with respect to ruling requests involving certain corporate business purposes. This document also revokes section 3.01(23) of Rev. Proc. 96–3, which sets forth “no rule” positions regarding certain corporate business purposes.

This section describes the information and representations to be provided in a § 355 ruling request. The presentation of the information and representations in the ruling request should follow the organization of this section and use appropriate descriptive headings. Taxpayers are welcome to provide a narrative description of the transaction to supplement (but not substitute for) the presentation requested in this section.

A ruling request should address each item in this section and provide all facts relevant to the transaction. If an item is not applicable, so state and briefly explain why.

Standard representations are set forth throughout this section and are highlighted by the word “representation” in boldface type. The representations are necessary to ensure that specific statutory and judicial requirements, and administrative ruling guidelines relating thereto, are satisfied. Each representation should be submitted in the language requested. If a representation cannot be submitted exactly as requested, an explanation must be given. Deviation from the language of the representations should be avoided, except as required by the facts being described. Unnecessary variations may delay processing the ruling request and will not be accepted unless reasons satisfactory to the Service are submitted.

The terms “**Distributing**” and “**Controlled**” in this document refer to the “**distributing corporation**” and “**controlled corporation**” as described in § 355(a)(1)(A). References to the term “**distribution**” include a distribution of stock or securities of Controlled with respect to Distributing stock, an exchange of Distributing stock or securities for Controlled stock or securities, or some combination thereof, as the context requires.

Requests for information and representations regarding Distributing or Controlled include, as the context requires, a request for information (or representations) regarding a successor of Distributing or Controlled. For example, if Distributing will merge with an acquiring corporation after the distribution, the representation requested in section 4.03(8) of this revenue procedure (that is, Distributing will continue to conduct its business) should be modified to include a similar representation under penalties of perjury by the acquiring corporation regarding the continuing conduct of Distributing’s business after the merger, in addition to Distributing’s representation. Similarly, the representation requested in section 4.05(1) of this revenue procedure (that is, there is no plan or intention by the Distributing shareholders to dispose of their shares in Distributing), should be modified to include a similar representation regarding dispositions of acquiring corporation shares by the Distributing shareholders. If a taxpayer believes that information regarding, or a representation by, a successor is inappropriate or should be modified, the taxpayer must explain why.

.01

(1) **Identification.** State the name, employer identification number, and place and date of incorporation of Distributing and Controlled. If Controlled is not in existence, state its proposed name and place of incorporation. If Distributing joins in the filing of a consolidated federal income tax return, provide the name and employer identification number of the common parent corporation of the affiliated group.

(2) **Jurisdiction.** Identify the District Office that has or will have examination jurisdiction over the return of Distributing (sometimes referred to below as the “**taxpayer**”) and of Controlled.

(3) **Taxable year.** State the last day of the taxable year of Distributing and Controlled.

.02

(1) **Capital structure of Distributing and Controlled immediately prior to the distribution.**

SECTION 3. CHANGES

SECTION 4. INFORMATION TO BE INCLUDED IN REQUESTS FOR RULINGS UNDER § 355

Distribution includes exchanges

Successors of Distributing or Controlled

Information regarding Distributing and Controlled

Ownership of interests in Distributing and Controlled

Under a separate heading for each corporation, provide the following information with respect to the stock and securities of Distributing and Controlled that will be outstanding immediately prior to the distribution:

Description of stock

(a) A complete description of each class of stock, setting forth the rights and privileges of each class, including voting or nonvoting rights, dividend and liquidation preferences or limitations, and whether classified as common or preferred stock.

Shareholdings

(b) A list of the number of shares and the percentage of each class of stock owned by each shareholder prior to the distribution. However, if the corporation has more than 100 shareholders, the taxpayer need only list those shareholders owning 5 percent or more of any class of stock, and state the total number of other shareholders together with the total number of shares and the percentage that these other shareholders own of each class of stock.

Description of agreements

(c) A description of any existing, planned, or intended agreements, such as a voting trust, affecting the rights of any shareholder. However, if the corporation has more than 100 shareholders, the taxpayer need only describe agreements affecting shareholders owning directly, or as a result of the agreement, controlling, 5 percent or more of any class of stock.

Description of securities

(d) A description of any securities and all other outstanding interests (bonds, debentures, notes, warrants, options, puts, etc.) and a brief explanation as to whether any of these items should be considered a stock interest.

Foreign shareholders

(2) Foreign shareholders. If Distributing has any foreign shareholders, state whether: (i) Distributing or Controlled was a United States real property holding corporation (as defined in § 897(c)(2)) at any time during the 5-year period ending on the date of the distribution, and (ii) Distributing or Controlled will be a United States real property holding corporation immediately after the distribution. *See* § 367(e)(1) and § 897. In addition, if Distributing is publicly traded, provide a list of all foreign persons owning 5 percent or more of Distributing stock either before or after the distribution. If Distributing is not publicly traded, provide a list of all foreign persons owning stock of Distributing either before or after the distribution. *See* section 4.08(7) of this revenue procedure for additional information regarding foreign parties.

Stock, securities, and property being distributed

(3) Description of stock, securities, and other property being distributed.

(a) **Stock.** State the number of shares and percentage of each class of stock of Controlled being distributed. In addition, if preferred stock is being distributed and it is contended that this stock is not “section 306 stock,” within the meaning of § 306(c), fully explain the reasons for this contention.

(b) **Securities.** State the principal amount of each series of securities of Controlled being distributed.

(c) **Other property.** Provide complete details as to any property, other than stock and securities of Controlled, to be distributed or received in the transaction including, but not limited to, cash, stock rights, warrants, or the payment of expenses incurred in connection with the transaction (*see* § 356).

Date of distribution

(d) **Timing.** State the date of the distribution and whether all the stock, securities, and other property will be distributed on that date. If all the stock, securities, and other property are not being distributed on the same date, state the approximate length of, and the reasons for, the delay in the distribution.

Control

(e) **Planned stock issuance, etc.** Describe any planned or intended stock issuances, redemptions, or dispositions of Controlled shares. Explain the effect of any of these transactions on the distribution-of-control requirement of § 355(a)(1)(D), and if property is being transferred from Distributing to Controlled, the effect on the control-immediately-after requirement of § 368(a)(1)(D).

Obtaining control

(f) **Obtaining control.** State whether Distributing has modified or will modify its ownership of Controlled stock, such as in a recapitalization, within the 5-year period preceding the distribution with the result that Distributing obtained or will obtain control of Controlled, as defined in § 368(c). Provide complete details, including the information requested in section 4.08(8) of this revenue procedure, with respect to such modifications.

(4) Ownership of stock and securities in Controlled immediately after the distribution.

Post-distribution ownership of interests in Controlled by Distributing

(a) **Interests in Controlled to be held by Distributing** (*see* § 1.355-2(e) of the Income Tax Regulations).

(i) **Retention of stock, securities, or options.** State the number of shares and percentage of each class of stock in, and the principal amount of each series of securities of, Controlled to be held by Distributing after the distribution and the length of time Distributing will hold this interest. Describe any options that Distributing will hold after the distribution to acquire stock in Controlled and the length of time Distributing will hold these options.

Post-distribution ownership of interests in Controlled by shareholders of Distributing

Post-distribution ownership of interests in Controlled by security holders of Distributing

Information concerning the businesses of Distributing and Controlled (see generally § 1.355-3)

Distributing's Active Businesses

(ii) **Retention of debt.** If Controlled will be indebted to Distributing after the distribution of Controlled stock, submit the following **REPRESENTATION**: *The indebtedness owed by the controlled corporation to the distributing corporation after the distribution of the controlled corporation stock will not constitute stock or securities.*

(iii) **Purpose for Distributing holding stock, securities, or options in Controlled.** If Distributing will hold stock, securities, or options in Controlled after the distribution, explain the reasons therefor and why this should not be viewed as in pursuance of a plan having as one of its principal purposes avoiding federal income tax. See Appendix B of this revenue procedure regarding favorable rulings with respect to the retention of stock, securities, or options. State whether a distribution of all the stock or securities of Controlled would be treated to any extent as a distribution of "other property" under § 356.

(b) **Interests in Controlled to be held by shareholders of Distributing.**

(i) **Distribution or exchange.** State whether the distribution of Controlled stock will be pro rata or non pro rata with respect to the shareholders of Distributing. Fully describe the transaction between Distributing and its shareholders.

(ii) **Stock ownership.** State the number of shares and the percentage of each class of stock outstanding in Distributing and Controlled that will be owned by each shareholder immediately after the distribution. However, if there will be more than 100 shareholders immediately after the distribution, the taxpayer need only list those shareholders who will own 5 percent or more of any class of stock, and state the expected total number of other shareholders together with the expected total number of shares and the expected percentage that these other shareholders will own of each class of stock.

(iii) **Securities.** Identify any shareholders of Distributing receiving securities of Controlled and state the principal amount of each series of securities to be received in the transaction. With respect to each shareholder, state the principal amount of each series of Distributing securities to be surrendered in the transaction, or, if no securities are being exchanged, so state. See § 1.355-2(f)(1).

(iv) **Surrender of stock.** If one or more Distributing shareholders will surrender Distributing stock in the transaction, submit the following **REPRESENTATION**: *The fair market value of the controlled corporation stock and other consideration to be received by each shareholder of the distributing corporation will be approximately equal to the fair market value of the distributing corporation stock surrendered by the shareholder in the exchange.*

(c) **Interests in Controlled to be held by security holders of Distributing.** Identify those security holders of Distributing receiving Controlled stock, the total number of shares of each class of stock being received, and the principal amount of the securities of Distributing being exchanged. Identify those security holders of Distributing receiving securities of Controlled, the principal amount being received by each holder, and the principal amount of the securities of Distributing being exchanged. See § 1.355-2(f)(1). If no securities are being exchanged, so state. If the securities are, or, immediately after the distribution, will be, held by more than 100 security holders, identify only those security holders that will own 5 percent or more of the outstanding shares of any class of Controlled stock or of any outstanding series of Controlled securities immediately after the distribution.

(d) **Receipt of consideration other than with respect to stock or securities.**

(i) **Shareholder in dual capacity.** Submit the following **REPRESENTATION**: *No part of the consideration to be distributed by the distributing corporation will be received by a shareholder as a creditor, employee, or in any capacity other than that of a shareholder of the corporation.*

(ii) **Security holder in dual capacity.** If consideration will be distributed to security holders, submit the following **REPRESENTATION**: *No part of the consideration to be distributed by the distributing corporation will be received by a security holder as an employee or in any capacity other than that of a security holder of the corporation.*

(iii) **Other transfers.** State whether the shareholders or security holders of Distributing will transfer or surrender any property in the transaction other than stock or securities of Distributing. If so, provide full details.

.03

(1) **Description of businesses.** Describe each line of business engaged in by Distributing, Controlled, and their respective subsidiaries, whether or not the business will be relied upon to meet the requirements of § 355(b). Note which corporations are engaged in each line of business.

(2) **Distributing's Active Businesses.** Submit a complete description of each trade or business that will be relied upon to meet the requirements of § 355(b) (an "Active Business"), that is conducted directly by Distributing, and that will be retained by Distributing. Provide the following information with respect to each such Active Business:

	<p>(a) Active conduct during the preceding 5-year period. Provide all information necessary to establish that the Active Business is a trade or business that has been actively conducted for the entire 5-year period ending on the date of the distribution (within the meaning of § 1.355-3(b)(2) and (3)). In general, the description should conclusively show that substantial managerial and operational activities have been directly carried on by the Active Business during each of the past 5 years.</p>
Employee information	<p>(b) Employee information. If the Active Business employed fewer than 50 full-time employees during any of the past 5 years, submit separate lists for each of the past 5 years showing the job titles of the Active Business' employees, the function (managerial, operational, or other) of each position, and the number of persons employed in each position. Include a brief description of the type of duties performed by each category of employee during each of these years.</p>
Nonemployee information	<p>(c) Nonemployee information. If Distributing is required to submit the employee information specified in section 4.03(2)(b) of this revenue procedure with respect to an Active Business, also state whether Distributing uses persons who are not employees, such as independent contractors. If so, include a brief description of the duties they perform, and the percentage of the activities they perform for the Active Business.</p>
Continuous ownership of Active Businesses conducted during 5-year period	<p>(d) Continuous ownership of an Active Business during the preceding 5-year period. State whether the Active Business has been continuously conducted, within the meaning of § 1.355-3(b), by Distributing for the 5-year period ending on the date of distribution. Give the date Distributing commenced conduct of the Active Business or acquired the Active Business. If an Active Business has not been continuously conducted by Distributing for such 5-year period, <i>see</i> section 4.03(6) of this revenue procedure.</p>
Change in business during 5-year period	<p>(e) Change in business. Describe any substantial change during the preceding 5-year period in the type of business activity conducted or the method of conducting business, such as substantial changes in: products or services offered, production capacity, assets owned or used, technology employed, sales or distribution channels, or locations. If the preceding 5-year period includes any time during which there was no business activity, or a significant amount of time during which there was a substantial reduction in business activity, identify the period of time, the type and amount of business activity during this period, and the reasons for the cessation or reduction in activity.</p>
Separation of real property, intellectual property, or other intangible property from user	<p>(f) Separation of real property, intellectual property, or other intangible property from user. State whether all or a portion of any real property, intellectual property, or other intangible property historically occupied or used by one business will be separated in the transaction from that business. If so, describe the property. State whether the business formerly using the property will continue to use the property after the transaction, and the terms upon which it will be allowed to use the property. Describe any other planned use of the property after the transaction. Explain the reason for separating the ownership of the property from its historic user.</p>
Balance sheets	<p>(g) Balance sheets. Provide a copy of the most recent balance sheet of Distributing (including all applicable notes). The balance sheet should not be limited to assets and liabilities of Distributing's Active Businesses. Also submit any consolidated balance sheets prepared for financial accounting purposes that include Distributing.</p>
Profit and loss statements	<p>(h) Profit and loss statements. Submit separate unconsolidated profit and loss statements (including all applicable notes) for each of the past 5 years for each Active Business. The statements must show that each business has had gross receipts and operating expenses (including employee expenses such as payroll withholding taxes) representative of the active conduct of a trade or business for each of the past 5 years. Submit the following REPRESENTATION: <i>The 5 years of financial information submitted on behalf of the distributing corporation is representative of the corporation's present operation, and with regard to such corporation, there have been no substantial operational changes since the date of the last financial statements submitted.</i></p>
Description of Active Businesses transferred to Controlled	<p>(3) Description of Active Businesses being transferred by Distributing to Controlled. If, in connection with the plan, Distributing transfers all or part of the assets of one or more of its Active Businesses (<i>see</i> § 1.355-3(c), example (4)) to either a newly formed or pre-existing Controlled, identify and submit a complete description of each Active Business or part of an Active Business being transferred. Submit the information and representation required by section 4.03(2)(a) through (h) of this revenue procedure for each such Active Business, or part of an Active Business, being transferred. If property will be transferred from Distributing to Controlled, submit a pro forma balance sheet for Controlled reflecting the transfer of assets to Controlled and all liabilities to be assumed or to which the property transferred will be subject.</p>
Description of pre-existing Controlled's Active Businesses	<p>(4) Pre-existing Controlled's Active Businesses. If Controlled is a pre-existing corporation, submit a complete description of each Active Business conducted directly by Controlled.</p>

Submit the information and representation required by section 4.03(2)(a) through (h) of this revenue procedure with respect to each such Active Business, treating references to Distributing as references to Controlled, as appropriate.

Indirect conduct of trade or business

(5) **Indirect conduct of trade or business through ownership of stock in other corporations.** If either Distributing or Controlled is not directly engaged in an Active Business but will be so engaged indirectly through ownership of stock and securities in one or more corporations controlled by it (“**Other Corporations**”) immediately after the distribution, submit the information and representation required by sections 4.03(2)(a) through (h) of this revenue procedure (treating, for this purpose, each Other Corporation as Distributing or Controlled, as appropriate). In addition, if Distributing or Controlled is not directly engaged in an Active Business, submit the following **REPRESENTATION: Immediately after the distribution, at least 90 percent of the fair market value of the gross assets of [insert the name of the corporation so indirectly engaged] will consist of the stock and securities of controlled corporations that are engaged in the active conduct of a trade or business as defined in § 355(b)(2). See section 3.04 of Rev. Proc. 77-37, 1977-2 C.B. 568, 570.**

Active Businesses acquired during 5-year period

(6) **Changes in ownership of an Active Business during the 5-year period ending on the date of distribution.** If an Active Business that is directly conducted by Distributing, Controlled, or an Other Corporation has been acquired by that corporation during the 5-year period ending on the date of distribution, identify the Active Business that was acquired and provide the following information with respect to that Active Business:

(a) **Identity.** Identify the party from whom the business was acquired, and the transferor’s relationship, if any, to Distributing or its shareholders.

(b) **Date.** State the date the business was acquired and the period of time the business had been previously conducted by Distributing’s, Controlled’s, or Other Corporation’s predecessor in interest.

(c) **Transaction.** Describe the transaction in which the business was acquired. For example, was the business acquired in a reorganization under § 368(a)(1), by purchase, or by some other means? If a letter ruling was issued with respect to the transaction, attach a copy.

(d) **Consideration.** State the consideration given in the acquisition.

(e) **Gain or loss.** State whether gain or loss was recognized, in whole or in part, to any party to the transaction and whether the basis of the assets acquired was determined, in whole or in part, by reference to the transferor’s basis.

(7) **Stock ownership during the preceding 5-year period (see § 355(b)(2)(D)).**

Stock continuously owned during 5-year period

(a) **Stock of Controlled or Other Corporations continuously owned during the preceding 5-year period.** Identify Controlled and Other Corporations whose shares have been continuously held by Distributing or Controlled for the 5-year period ending on the date of distribution.

(b) **Stock of Controlled or Other Corporations acquired by Distributing, Controlled, or Other Corporations during the preceding 5-year period.** If the stock of Controlled or Other Corporations has been acquired by Distributing, Controlled, or Other Corporations during the 5-year period ending on the date of the distribution, identify the stock that was acquired and provide the following information with respect to that stock:

(i) **Identity.** Identify the party from whom the stock was acquired and the transferor’s relationship, if any, to Distributing or its shareholders.

(ii) **Date and consideration.** State the date the stock was acquired and the consideration given in the acquisition.

(iii) **Transaction.** Describe the transaction in which the stock was acquired. For example, was the stock acquired in a § 368(a)(1) reorganization, by purchase, or by some other means? State whether control was acquired in a transaction in which Distributing transferred cash or other liquid or inactive assets to Controlled. See section 4.01(31) of Rev. Proc. 96-3. If a letter ruling was issued with respect to the transaction, attach a copy.

(iv) **Gain or loss.** State whether gain or loss was recognized, in whole or in part, to any party to the transaction and whether the basis of the stock acquired was determined, in whole or in part, by reference to the transferor’s basis.

Other changes in ownership during 5-year period

(c) **Other changes in ownership.** Provide complete details concerning any change in ownership of the stock of Distributing, Controlled, or Other Corporations during the 5-year period ending on the date of the distribution that is not fully described under section 4.03(7)(b) of this revenue procedure. For this purpose, a change of ownership includes, but is not limited to, acquisitions, redemptions, recapitalizations, stock dividends, and sales. Information regarding sales of stock to which the issuing corporation was not a party need not be provided if: (i) the sale occurred on a recognized stock exchange or in an established market; and (ii) both the purchaser and the seller held less than 5 percent of the corporation’s stock both before and after the sale.

Continuation of business

(8) **Continuation of business.** If the transaction involves the vertical division of a single Active Business, submit the following **REPRESENTATION:** *Following the transaction, the distributing and controlled corporations will each continue, independently and with its separate employees, the active conduct of its share of all the integrated activities of the business conducted by the distributing corporation prior to consummation of the transaction.* If the transaction involves the separation of two or more Active Businesses, submit the following **REPRESENTATION:** *Following the transaction, the distributing and controlled corporations will each continue the active conduct of its business, independently and with its separate employees.* Additionally, if, following the transaction, Distributing and Controlled will share the services of any employees, identify these employees, specify the services to be performed, the length of time the employees will be shared, the compensation arrangements, and explain why the services of these employees will be shared.

In addition, describe any planned or intended substantial reduction in business activity for any Active Business. Generally, a substantial reduction in business activity does not include a vertical division of a single Active Business where Distributing and Controlled together continue all of the integrated activities of the Active Business.

Business purpose (see generally § 1.355-2(b))

.04

(1) **Detailed Description.** Describe in detail each purpose (whether or not a corporate business purpose) for the distribution of the stock of Controlled.

(2) **Corporate Business Purposes.** Explain which purposes described in section 4.04(1) of this revenue procedure are corporate business purposes within the meaning of § 1.355-2(b)(2) (“**Corporate Business Purposes**”). Describe how each Corporate Business Purpose is a real and substantial nonfederal tax purpose germane to the business of Distributing, Controlled, or the affiliated group (as defined in § 1.355-3(b)(4)(iv)) to which Distributing belongs. In addition, explain the business exigencies that require the distribution at this time. Submit the following **REPRESENTATION:** *The distribution of the stock, or stock and securities, of the controlled corporation is carried out for the following corporate business purposes: [list these Corporate Business Purposes]. The distribution of the stock, or stock and securities, of the controlled corporation is motivated, in whole or substantial part, by one or more of these corporate business purposes.*

Alternative transactions

(3) **Alternative transactions.** Explain why each Corporate Business Purpose cannot be achieved through a nontaxable transaction that does not involve the distribution of stock of Controlled and which is neither impractical nor unduly expensive. For example, in appropriate cases, possible alternative transactions might include the transfer of assets to a partnership or limited liability company. If a Corporate Business Purpose can be achieved through a nontaxable alternative transaction that would be impractical or unduly expensive, fully describe the reason the alternative transaction would be impractical or the additional expense that would be incurred by using the alternative transaction instead of the proposed transaction. An alternative transaction that will cause the loss of a favorable special tax status, such as an existing S corporation election, will ordinarily be viewed as unduly expensive.

Appendix A

(4) **Cross reference to Appendix A.** Appendix A of this revenue procedure provides guidelines that the Service will use, for ruling purposes, in evaluating whether a distribution satisfies the corporate business purpose requirement in certain situations and specifies information to be submitted with respect to the following business purposes: key employee, stock offering, borrowing, cost savings, fit and focus, competition, facilitating an acquisition of Distributing, facilitating an acquisition by Distributing or Controlled, and risk reduction. The business purposes described in Appendix A of this revenue procedure are not an exclusive list of Corporate Business Purposes for which the Service will issue a favorable ruling. If a purpose for the transaction is not described in Appendix A of this revenue procedure, the taxpayer should follow section 4.04 of this revenue procedure to establish that the distribution satisfies the corporate business purpose requirement.

Non-Corporate Business Purposes

(5) **Non-Corporate Business Purposes.**

(a) **General.** If the transaction will enable Distributing, Controlled, or Other Corporations to effect a reduction in federal taxes, or if it appears that the transaction will achieve one or more other non-Corporate Business Purposes, the taxpayer must convince the Service by clear and convincing evidence that the distribution is motivated in whole or substantial part by one or more Corporate Business Purposes in order to obtain a favorable ruling.

Shareholder planning

(b) **Shareholder planning.** State whether a purpose for the distribution is to facilitate the personal planning (such as estate planning or gifts) of any shareholder. If the answer is in the affirmative, provide the details.

Special tax status

(c) **Special tax status.** State whether Distributing, Controlled, or any Other Corporation is, plans to become, will cease to be, or will become eligible to become an S corporation, real estate investment trust, insurance company, bank, savings and loan, controlled foreign corporation, or other corporation with a special federal tax status. If so, describe the special tax status and the date it was or will become effective, will cease to be effective, or when the

Description of any reduction in federal taxes	<p>corporation will become eligible. If either Distributing or Controlled will be eligible to elect S corporation status after the distribution, <i>see</i> Appendix C.</p> <p>(d) Reduction in federal taxes. Describe any reduction in federal taxes of Distributing, Controlled, or any Other Corporations that can reasonably be expected to result from the transaction. For this purpose, nonrecognition of income or gain to the shareholders or corporation resulting from the application of § 355 or § 361 is disregarded.</p>
Representation regarding potential non-Corporate Business Purpose	<p>(e) Representation. In order to lessen the Service's concern about a potential non-Corporate Business Purpose, the taxpayer, in appropriate cases, may wish to represent that it will engage in a specific course of action (such as making or not making an election) that obviates the potential avoidance of federal taxes or other non-Corporate Business Purpose.</p>
Substantiation	<p>(6) Substantiation of business purpose.</p> <p>(a) Documentation. The taxpayer must provide substantiation of one or more Corporate Business Purposes that motivate the transaction in whole or substantial part. The type and extent of the substantiation will necessarily vary depending on the described business purpose and facts of the particular case. Accordingly, the taxpayer should submit documentation that provides factual support for the Corporate Business Purposes. The Service recognizes that a particular transaction may be undertaken for more than one Corporate Business Purpose. Generally, satisfying the requirements of this section 4.04(6) of this revenue procedure with respect to one Corporate Business Purpose that motivates the transaction, in substantial part, will suffice in such cases.</p>
Third party documentation	<p>(b) Third party documentation. If the transaction is being undertaken at the request of, or pursuant to the advice or analysis of, persons other than Controlled or Distributing, explain fully. Provide documentation of such third party requests, advice, or analysis to substantiate the business purpose for the distribution. Such documentation should include an explanation of the third party's qualifications to speak to the matter.</p> <p>Business purposes for which third party documentation may be necessary include, for example, risk reduction, cost savings, facilitating a stock offering or borrowing, obtaining regulatory relief, improving credit, and preserving a franchise. Third party documentation prepared specifically for submission with the taxpayer's ruling request must contain an acknowledgement that the documentation will be submitted to the Internal Revenue Service for use in determining the federal tax consequences of the transaction.</p>
Regulatory filings	<p>(7) Additional documents.</p> <p>(a) Regulatory filings. Provide copies of any proxy statements, information statements, or prospectuses filed or prepared in connection with the distribution or any related transaction. List and briefly describe any other documents that have been or will be filed with (or prepared for) any federal, state, local, or foreign regulatory body (such as the Securities and Exchange Commission) by the taxpayer in connection with the distribution. The Service may request copies of some or all such documents in the course of analyzing the ruling request.</p>
Material prepared for directors	<p>(b) Material prepared for directors. Attach a copy of any materials that relate to the purpose for the distribution and were prepared for or presented to the taxpayer's board of directors, and any relevant portions of the board's minutes.</p>
Communications to shareholders and employees	<p>(c) Communications to shareholders and employees. Attach a copy of any press releases relating to the distribution. Attach copies of any letters or memoranda relating to the distribution that the taxpayer or its officers sent to the taxpayer's shareholders. In addition, attach copies of the taxpayer's written statements to its employees that discuss any purpose for the distribution.</p>
Device (<i>see generally</i> § 1.355-(2)(d))	<p>.05</p> <p>(1) Dispositions of stock or securities.</p> <p>(a) Representation. Submit the following REPRESENTATION: <i>There is no plan or intention by the shareholders or security holders of the distributing corporation to sell, exchange, transfer by gift, or otherwise dispose of any of their stock in, or securities of, either the distributing or controlled corporation after the transaction.</i> For publicly traded companies, the taxpayer may instead submit the following REPRESENTATION: <i>There is no plan or intention by any shareholder who owns 5 percent or more of the stock of the distributing corporation, and the management of the distributing corporation, to its best knowledge, is not aware of any plan or intention on the part of any particular remaining shareholder or security holder of the distributing corporation to sell, exchange, transfer by gift, or otherwise dispose of any stock in, or securities of, either the distributing or controlled corporation after the transaction.</i></p>
Purchases of stock by Distributing or Controlled	<p>(b) Permitted purchases. For ruling purposes, the Service will treat purchases by either Distributing or Controlled of its stock after the transaction as not violating the device requirement of § 355(a)(1)(B) provided that:</p> <p>(i) there is a sufficient business purpose for the stock purchase;</p>

- (ii) the stock to be purchased is widely held;
- (iii) the stock purchases will be made in the open market; and
- (iv) there is no plan or intention that the aggregate amount of stock purchases will equal or exceed 20 percent of the outstanding stock of the corporation.

Submit the following **REPRESENTATION**: *There is no plan or intention by either the distributing corporation or the controlled corporation, directly or through any subsidiary corporation, to purchase any of its outstanding stock after the transaction, other than through stock purchases meeting the requirements of section 4.05(1)(b) of Rev. Proc. 96-30.*

If the stock purchases do not meet the requirements of this paragraph (b), the Service will consider ruling on whether the purchases violate the device requirement of § 355(a)(1)(B) after considering all of the facts and circumstances of each case.

(c) **Other dispositions.** If a plan or intent to dispose exists (including stock purchases that meet the requirements of section 4.05(1)(b) of this revenue procedure), provide the following information:

(i) **Detailed description.** Give complete details concerning the transaction, including any agreements existing between the parties and the number of shares of each class of stock or the amount of each series of securities that will be disposed of by each shareholder or security holder.

(ii) **Consideration.** State the consideration to be received by each shareholder or security holder.

(iii) **Evidence of nondevice.** Explain any special circumstances indicating why the disposition should not be viewed as a device, such as proportionate sales of Distributing and Controlled stock by the shareholder.

(2) **Absence of earnings and profits.** If the taxpayer contends that the distribution should not be considered to be a device because of an absence of earnings and profits (*see* § 1.355-2(d)(5)(ii)), submit the following **REPRESENTATIONS**:

(a) *The distributing corporation and the controlled corporation have no accumulated earnings and profits at the beginning of their respective taxable years;*

(b) *The distributing corporation and the controlled corporation will have no current earnings and profits as of the date of the distribution;*

(c) *No distribution of property by the distributing corporation immediately before the transaction would require recognition of gain resulting in current earnings and profits for the taxable year of the distribution; and*

(d) *The distributing corporation is not aware of, nor is the distributing corporation planning or intending, any event that will result in the distributing corporation or the controlled corporation having positive current or accumulated earnings and profits after the distribution.*

(3) **Non pro rata distribution.** State whether all or any part of the distribution, if considered taxable, would qualify as an exchange under § 302(a) or § 303(a).

(4) **Investment and inactive assets.** Under a separate heading for each corporation, provide the following information with respect to Distributing, Controlled, or Other Corporations:

(a) **Detailed description.** Provide a description and valuation of the investment assets, and other assets that are not related to the reasonable needs of the Active Businesses of Distributing, Controlled, or Other Corporations; and

(b) **Explanation.** Explain why Distributing, Controlled, or Other Corporations will hold these assets.

(5) **Liquidation or sale of assets.** Submit the following **REPRESENTATION**: *There is no plan or intention to liquidate either the distributing or controlled corporation, to merge either corporation with any other corporation, or to sell or otherwise dispose of the assets of either corporation after the transaction, except in the ordinary course of business.* Alternatively, describe the subsequent transaction.

.06 The taxpayer must explain how the continuity of interest requirement will be satisfied. Generally, the Service will view this requirement as satisfied if one or more persons who, directly or indirectly, were the owners of the enterprise prior to the distribution own, in the aggregate, 50 percent or more of the stock in each of the modified corporate forms in which the enterprise is conducted after the separation. In appropriate cases, the Service may require a continuity of interest representation from the taxpayer.

.07 Explain in detail why the distribution of Controlled stock, or of Controlled stock and securities, will not be a disqualified distribution within the meaning of § 355(d)(2). Generally, the explanation should set forth facts establishing that, taking into account the application of § 355(d)(6), (7), and (8), immediately after the distribution: (i) no person holds disqualified stock in Distributing that constitutes a 50 percent or greater interest in Distributing; and (ii) no person holds disqualified stock in Controlled that constitutes a 50 percent or greater

Information regarding planned dispositions of stock or securities

Absence of earnings and profits

Distribution qualifying as an exchange
Investment assets

Liquidation or sale of assets

Continuity of shareholder interest (*see generally* § 1.355-2(c))

Disqualified distribution

interest in Controlled. It is not necessary for the taxpayer to submit information accounting for all of the stock of Distributing or Controlled if, by providing information with respect to a smaller amount of stock, it can establish that the distribution will not be a disqualified distribution.

.08

(1) Transfers and transactions between Distributing and Controlled.

Miscellaneous

Contributions to capital

(a) Contributions to capital. Provide complete details concerning any transfers of property by Distributing to Controlled in anticipation of or in connection with the transaction. For ruling purposes, such transfers ordinarily will be treated as occurring in connection with a reorganization pursuant to § 368(a)(1)(D). If a transfer of property from Distributing to Controlled will not qualify as a reorganization pursuant to § 368(a)(1)(D), and the taxpayer contends that § 351 applies to the transaction, submit the information and representations specified in Rev. Proc. 83-59, 1983-2 C.B. 575, as modified or superseded, or explain why an item is not being submitted.

Section 351

Liabilities

(b) Liabilities. If Controlled is assuming liabilities or receiving assets subject to liabilities, submit the following **REPRESENTATIONS**:

(i) *The total adjusted bases and the fair market value of the assets transferred to the controlled corporation by the distributing corporation each equals or exceeds the sum of the liabilities assumed by the controlled corporation plus any liabilities to which the transferred assets are subject; and*

(ii) *The liabilities assumed in the transaction and the liabilities to which the transferred assets are subject were incurred in the ordinary course of business and are associated with the assets being transferred.*

Investment credit

recapture representation

(c) Investment credit property. If any property is being transferred between Distributing and Controlled, state whether any investment credit determined under § 46 has been (or will be) claimed with respect to any of such property. If the answer is in the affirmative, submit the following **REPRESENTATION**: *The income tax liability for the taxable year in which investment credit property (including any building to which § 47(d) applies) is transferred will be adjusted pursuant to § 50(a)(1) or (a)(2) (or § 47, as in effect before amendment by Public Law 101-508, Title 11, 104 Stat. 1388, 536 (1990), if applicable) to reflect an early disposition of the property.* Alternatively, explain why no increase in tax will be required under § 50 (or § 47, as in effect before such amendment) as a result of the transaction.

Matching of income and deductions

(d) Matching of income and deductions. State the overall method of accounting of Distributing and Controlled. Further, state whether the transaction involves or will result in a situation in which one party recognizes income but another party recognizes the deductions associated with such income or one party owns property but another party recognizes the income associated with such property. *See, for example*, Notice 95-53, 1995-44 I.R.B. 21. If one or more parties use the cash method of accounting, explain the extent to which any actions have been or will be taken that are not in the ordinary course of business and that might affect the timing or the amount of any income or deduction to be recognized by a cash basis party to the transaction. *See, for example*, Rev. Rul. 80-198, 1980-2 C.B. 113. In addition, submit a statement as to whether any income items, such as accounts receivable, or any items resulting from a sale, exchange or disposition that would have resulted in income to Distributing, or any items of expense, will be transferred to Controlled. If any of these items are being transferred, fully explain. Further, submit the following **REPRESENTATION**: *The distributing corporation neither accumulated its receivables nor made extraordinary payment of its payables in anticipation of the transaction.* If Distributing uses the cash method of accounting or a similar method and Controlled uses the accrual method or a similar method, a closing agreement will be required unless the taxpayer submits the following **REPRESENTATION**: *No income items, including accounts receivable or any item resulting from a sale, exchange or disposition of property, that would have resulted in income to the distributing corporation, and no items of expense will be transferred to the controlled corporation if the distributing corporation has earned the right to receive the income or could claim a deduction for the expense under the accrual or similar method of accounting.*

(2) Indebtedness.

Debt cancellation

(a) Cancellation of indebtedness. If any indebtedness has been or will be cancelled in connection with the transaction, give complete details concerning the principal amount of the indebtedness, the circumstances under which it arose, and the date and method under which the indebtedness will be discharged.

Intercorporate indebtedness

(b) Continuing indebtedness. Submit the following **REPRESENTATION**: *No intercorporate debt will exist between the distributing corporation and the controlled corporation at the time of, or subsequent to, the distribution of the controlled corporation stock.* Alternatively, submit a full description of all existing, planned, or intended debt between Distributing and

Controlled, including complete details as to principal amounts, terms, and reasons for the issuance. Include copies of any instruments evidencing the intercorporate indebtedness. If any debt exists between Controlled, as debtor, and Distributing, as creditor, state whether such debt arose in connection with a transfer of assets by Distributing to Controlled. If so, explain the circumstances.

Consolidated transactions

(3) **Consolidated transactions.** If Distributing joins in the filing of a consolidated federal income tax return, submit the following **REPRESENTATION**: *Immediately before the distribution, items of income, gain, loss, deduction, and credit will be taken into account as required by the applicable intercompany transaction regulations (See § 1.1502-13 and § 1.1502-14 as in effect before the publication of T.D. 8597, 1995-32 I.R.B. 6, and as currently in effect; § 1.1502-13 as published by T.D. 8597). Further, Distributing's excess loss account with respect to the Controlled stock will be included in income immediately before the distribution (See § 1.1502-19).*

Future intercorporate transactions

(4) **Continuing transactions between Distributing and Controlled (or two or more controlled corporations).** Describe in detail any continuing, planned, or intended transactions between Distributing and Controlled following the distribution, either directly or indirectly (such as through a partnership), or between an Other Corporation and a corporation from which it will be separated. In addition, submit the following **REPRESENTATION**: *Payments made in connection with all continuing transactions, if any, between the distributing and controlled corporations, will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.*

Investment company

(5) **Investment company.** If assets are transferred by Distributing to Controlled, or if liabilities owed by Controlled to Distributing are cancelled, submit the following **REPRESENTATION**: *No two parties to the transaction are investment companies as defined in § 368(a)(2)(F)(iii) and (iv).*

Consideration received by Distributing

(6) **Transfers of money or property to Distributing.** Set forth all consideration received by Distributing, including distributions by Controlled to Distributing, in connection with the transaction. Describe any receipt of money or property by Distributing from Controlled in contemplation of the distribution (other than in the ordinary course of business).

Foreign corporation

(7) **Foreign corporation.** State whether Distributing, Controlled, or any Other Corporation is a foreign corporation and whether any such foreign corporation is a passive foreign investment corporation (as defined in § 1296(a)), or a controlled foreign corporation (as defined in § 957) both before and after the distribution. See §§ 367(b), 367(e)(1), 897, and 1248(f).

Other transactions

(8) **Other transactions.** State whether there have been, or will be, any related transactions, and, if so, describe these other transactions and fully explain their relationship to, and impact on, the present transaction. Even if the transaction is thought to be unrelated, provide full details if it is contemplated that any stock is to be issued or redeemed by Distributing, Controlled, or Other Corporations, other than that already described as being distributed pursuant to the plan. Provide a description of any plan or intention to issue, redeem, or alter any rights in, such as voting rights, shares of stock of Distributing, Controlled, or Other Corporations.

Plan of reorganization and other relevant documents

(9) **Plan of reorganization and other relevant documents.** Submit a copy of the plan of reorganization or distribution. Alternatively, state why a copy is not available. In addition, submit a copy of any indemnification and tax sharing agreements to which Distributing or Controlled is a party.

If these or any other documents requested in this revenue procedure become available after filing the ruling request, submit copies as soon as possible.

Requested rulings

(10) **Requested rulings.** List the rulings being requested in the exact wording desired, and provide statutory, regulatory, or other authority for their issuance.

Presubmission conference

(11) **Presubmission conference.** Prior to submitting a § 355 ruling request, the taxpayer may request a conference with the Office of Assistant Chief Counsel (Corporate). A presubmission conference is particularly recommended if the transaction does not satisfy all of the requirements or relevant guidelines of this revenue procedure. The taxpayer must submit a description of the transaction, including the name of the taxpayer, and a memorandum of the issues to be discussed at the conference, at least three business days before the conference. The taxpayer must provide a power of attorney for each representative attending the conference. In appropriate cases, the Service will consider conducting the presubmission conference by telephone. For additional information regarding presubmission conferences, see the annual revenue procedure referred to in section 2 of this revenue procedure and contact the Office of the Assistant Chief Counsel (Corporate) at (202) 622-7710 (not a toll-free call).

SECTION 5. EFFECT ON OTHER DOCUMENTS

.01 Rev. Procs. 91–63, 91–62, and 86–41 are superseded. Section 3.01(23) of Rev. Proc. 96–3 is revoked.

.02 The item relating to the § 355 Checklist Questionnaire in section 9.01 of Rev. Proc. 96–1 is amended to read as follows: Rev. Proc. 96–30, 1996–19 I.R.B. 8.

.03 Section 9.02 of Rev. Proc. 96–1 is modified to replace the reference to Rev. Proc. 91–63 with a reference to section 4.05(1)(b) of Rev. Proc. 96–30.

SECTION 6. EFFECTIVE DATE

This revenue procedure will apply to all ruling requests postmarked, or, if not mailed, received, on or after June 5, 1996. However, the Service may ask the taxpayer to submit information specified in this revenue procedure for any ruling requests submitted prior to that date. The revocation of section 3.01(23) of Rev. Proc. 96–3 is effective on date May 6, 1996. The Service will entertain ruling requests on the business purposes listed in Appendix A of this revenue procedure whether the ruling request arrives before, on, or after the publication date of this revenue procedure.

DRAFTING INFORMATION

The principal author of this revenue procedure is Dean P. Lekos of the Office of Assistant Chief Counsel (Corporate). For further information regarding this revenue procedure, contact Mr. Lekos on (202) 622-7550 or Mr. Howard W. Staiman on (202) 622-7750 (not toll-free calls).

APPENDIX A

SECTION 1. BUSINESS PURPOSE GUIDELINES

Appendix A provides guidelines that the Service will use, for ruling purposes, in evaluating whether a distribution satisfies the corporate business purpose requirement in certain situations. These guidelines apply in addition to the requirements specified in section 4.04 of this revenue procedure.

The business purposes described in this Appendix A are not an exclusive list of Corporate Business Purposes for which the Service will issue a favorable ruling. If a purpose for the transaction is not described in Appendix A of this revenue procedure, the taxpayer should follow section 4.04 of this revenue procedure to establish that the distribution satisfies the corporate business purpose requirement. The failure of a transaction to meet the guidelines in this Appendix A does not, in and of itself, mean that the distribution is not carried out for a Corporate Business Purpose. Moreover, the Service will consider requests for rulings that do not satisfy the guidelines in this Appendix A and may rule favorably in appropriate circumstances. Conversely, although a transaction may fall within the literal language of these guidelines, the Service will not issue a favorable ruling unless it is satisfied that the transaction is motivated, in whole or substantial part, by a real and substantial nonfederal tax purpose germane to the business of Distributing, Controlled, or the affiliated group to which Distributing belongs, and that the purpose cannot be achieved through a nontaxable transaction that does not involve the distribution of Controlled stock and which is neither impractical nor unduly expensive. The Service will continue to evaluate the guidelines in this Appendix A and may modify them when appropriate.

The Service recognizes that a particular transaction may be motivated, in whole or substantial part, by more than one business purpose described in this Appendix A. Generally, in such cases, satisfying the guidelines for one Corporate Business Purpose that motivates the transaction, in substantial part, will suffice.

A reference to Distributing or Controlled includes, as the context requires, a reference to Other Corporations (as defined in section 4.03(5) of this revenue procedure), or to a corporation that will be formed as part of the transaction.

SECTION 2. SPECIFIC CORPORATE BUSINESS PURPOSES

.01 Key Employee.

(1) General. To establish that a Corporate Business Purpose for the distribution is to provide an equity interest in a business of Distributing or Controlled to a current or prospective employee, or employees, ordinarily, the taxpayer must demonstrate to the satisfaction of the Service that:

(a) The transfer of Distributing or Controlled stock to this employee, or these employees, will accomplish a real and substantial purpose germane to the business of Distributing, Controlled or the affiliated group (as defined in § 1.355–3(b)(4)(iv)) to which Distributing belongs. Among other things, the taxpayer must explain why the individual, or each individual, is considered a key employee, and why it is necessary to give the individual, or each individual, an equity interest of the type and amount proposed in the transaction.

(b) Generally within one year of the distribution, the employee, or the employees as a group, will receive a significant amount, in terms of percentage and value, of voting stock of either Distributing or Controlled. (An acquisition of a significant percentage of stock may not be required, however, if it would be prohibitively expensive for the employee,

or employees, to acquire a significant percentage of stock.) The taxpayer must state when the employee, or employees, will acquire the stock and fully describe the terms and method of acquisition (for example, purchase, compensation, or exercise of an option).

(c) The objective to be accomplished by transferring stock to the employee, or employees, cannot be accomplished by an alternative nontaxable transaction that does not involve the distribution of Controlled stock and which is neither impractical nor unduly expensive. (For example, the Service generally will consider that it is unduly expensive to create a controlled corporation that would terminate an existing S corporation election. In such cases, however, the taxpayer must demonstrate why another nontaxable transaction, such as the transfer of assets to a partnership or limited liability company, is neither impractical nor unduly expensive.) Where the taxpayer contends that a transaction involving a distribution will provide the employee, or employees, voting power representing a meaningful voice in the governance of their employer's business that is not available through an alternative transaction, the Service will consider such cases on a case-by-case basis, taking into account factors such as the distribution of voting power among the shareholders, family relationships, and competing economic interests.

(2) Options and restricted stock. The Service will scrutinize closely situations in which stock issued to the employee, or employees is subject to an option or restriction.

(3) Stock ownership plans. The principles of section 2.01(1) and (2) of this Appendix A also apply if a business purpose is to transfer Distributing or Controlled stock to an employee stock ownership plan described in § 4975(e)(7) (an "ESOP"), treating the ESOP as a group of key employees. Other plans relating to employee stock ownership will be considered on a case-by-case basis.

.02 Stock offering. To establish that a Corporate Business Purpose for the distribution is to facilitate a stock offering, ordinarily, the taxpayer must demonstrate to the satisfaction of the Service that:

(1) The issuing corporation needs to raise a substantial amount of capital in the near future to fund operations, capital expenditures, acquisitions, the retirement of indebtedness, or other business needs.

(2) The stock offering will raise significantly more funds per share (net of transaction costs of the distribution), or is otherwise more advantageous, if Distributing and Controlled are separated in connection with the offering. The taxpayer ordinarily must submit substantiation in the form of an analysis based on the professional judgment of persons qualified to speak to such matters. The analysis should be supported by data involving comparable corporations, businesses, and stock offerings and should compare the expected results of an offering, taking into account the proposed distribution, with the expected results of an offering by Distributing or Controlled without the distribution. Generally, the Service will acknowledge (without extensive substantiation) that an offering of publicly traded stock by a widely held corporation with no significant shareholders will raise more funds per share than an offering by the same corporation in the position of a controlled subsidiary.

(3) The funds raised in the stock offering will, under all circumstances, be used for the business needs of Distributing, Controlled, or the affiliated group (as defined in § 1.355-3(b)(4)(iv)) to which Distributing belongs. The taxpayer should explain when and how the funds will be used in satisfying such business needs.

(4) The stock offering will be completed within one year of the distribution.

(5) If the stock of a corporation with one or more significant shareholders will be purchased by a limited number of investors who require the distribution as a condition of their participation, the Service may require appropriate substantiation from these investors.

.03 Borrowing. To establish that a Corporate Business Purpose for the distribution is to facilitate borrowing, ordinarily, the taxpayer must demonstrate to the satisfaction of the Service that:

(1) Distributing or Controlled needs to raise a substantial amount of capital in the near future to fund operations, capital expenditures, acquisitions, or other business needs.

(2) The separation will enable Distributing or Controlled to borrow significantly more money or borrow on significantly better nonfinancial terms. The taxpayer ordinarily must submit substantiation, such as an analysis based on the professional judgment of persons qualified to speak to such matters.

(3) The funds raised in the borrowing will, under all circumstances, be used for the business needs of Distributing, Controlled, or the affiliated group (as defined in § 1.355-3(b)(4)(iv)) to which Distributing belongs. The taxpayer should explain when and how the funds will be used in satisfying such business needs.

(4) The borrowing will be completed within one year after the distribution.

If the distribution will enable Distributing or Controlled to borrow money at a lower cost, see section 2.04 of this Appendix A, relating to cost savings.

.04 Cost savings. To establish that a Corporate Business Purpose for the distribution is cost savings, ordinarily, the taxpayer must demonstrate to the satisfaction of the Service that the distribution will produce significant cost savings. Ordinarily, the taxpayer's submission should include analysis based on the professional judgment of persons qualified to speak to this matter (such as the taxpayer's insurer for insurance savings, an investment banker for lower borrowing costs, or, in appropriate cases, the taxpayer's employees). The analysis must explain the savings and why the savings cannot be achieved through a nontaxable transaction that does not involve the distribution of stock of Controlled and which is neither impractical nor unduly expensive.

Significant cost savings generally are projection period cost savings equal to at least one percent of the base period net income of Distributing's affiliated group. Projection period cost savings are the total anticipated future cost savings to

Distributing, Controlled, and their affiliated group for the 3-year period following the distribution, reduced by the transaction costs of the distribution and any anticipated additional direct or indirect costs to Distributing, Controlled and their affiliated group, all of which are computed on an after-tax basis. For this purpose, all savings (whether or not from the same source) and all additional costs to Distributing, Controlled, and their affiliated group are aggregated. Base period net income is the total net consolidated financial income of Distributing's affiliated group for the 3-year period preceding the distribution, all of which is computed on an after-tax basis, using generally accepted accounting principles. The taxpayer may choose to use the 5-year periods preceding and following the distribution for the base period and projection period instead of 3-year periods. Members of an affiliated group are determined in accordance with § 1.355-3(b)(4)(iv). In the case of foreign tax savings, explain the extent to which the foreign tax that is expected to be saved would have resulted in foreign tax credits or foreign tax credit carryovers for federal tax purposes.

The Service may apply different guidelines in various situations, including the following:

- (1) Projection period cost savings will not equal one percent of base period net income.
- (2) Net income for one or more of the 3 (or 5) years preceding the distribution is nominal or is affected by extraordinary or nonrecurring items of gain, loss, income or deduction, or there is a loss for any year.
- (3) Controlled stock will be distributed to a member of Distributing's affiliated group.
- (4) There are cost savings from the reduction of both federal and nonfederal taxes. In certain situations, a purpose of reducing nonfederal taxes is not a Corporate Business Purpose. *See* § 1.355-2(b)(2).

.05 Fit and Focus.

(1) **General.** This section 2.05 of Appendix A provides guidelines for a ruling request in which a Corporate Business Purpose for the distribution is that the separation will enhance the success of the businesses by enabling the corporations to resolve management, systemic, or other problems that arise (or are exacerbated) by the taxpayer's operation of different businesses within a single corporation or affiliated group. Except as provided in section 2.05(2) of this Appendix A, the Service ordinarily will rule with respect to pro rata as well as non pro rata distributions.

(2) **Significant shareholder or nonpublicly traded.** If Distributing is not publicly traded (or is publicly traded, but has a significant shareholder), the Service ordinarily will not rule unless the distribution:

- (a) is a non pro rata distribution to enable a significant shareholder or shareholder group to concentrate on a particular business (*see* example (2) of § 1.355-2(b)(5)), or
- (b) effects an internal restructuring within an affiliated group (members of an affiliated group are determined in accordance with § 1.355-3(b)(4)(iv)).

(3) **Significant shareholder defined.** A significant shareholder is any person who is directly or indirectly, or together with related persons, the owner of 5 percent or more of any class of stock of Distributing or Controlled and who actively participates in the management or operation of Distributing or Controlled. If the taxpayer contends that a person meeting or exceeding this 5 percent threshold does not actively participate in management or operations, the taxpayer should submit details supporting the taxpayer's contention.

(4) **Substantiation.** Documentary substantiation satisfactory to the Service is essential. The documentation should describe in detail the problems associated with the current corporate structure and demonstrate why the distribution will lessen or eliminate these problems. Internal reports and studies, and analyses based upon the professional judgment of persons qualified to speak to such matters (such as investment bankers or management consultants), are examples of documentation that may provide adequate substantiation. Reports by securities analysts or similar materials may also be helpful. However, in the case of a non pro rata distribution made to enable a significant shareholder or shareholder group to concentrate on a particular business, the Service ordinarily will not require third party documentation or detailed studies.

(5) **Special scrutiny.** In evaluating the ruling request, the Service will scrutinize closely the following situations:

(a) **Continuing relationship.** Any continuing relationship between Distributing and Controlled to determine if such relationship is consistent with the stated business purpose. Examples of continuing relationships include common directors, officers, or key employees, the provision of goods or services to the other company, or commonly-owned property.

(b) **Cross ownership.** Except for cases involving an internal restructuring of an affiliated group, any direct or indirect continuing interest in both Distributing and Controlled by a significant shareholder or, in the case of a nonpublicly traded corporation, any other shareholder. For example, if the purpose of the distribution is to allow a significant shareholder to concentrate on a particular business, the Service ordinarily will require, as a condition of ruling, that the separating shareholders not maintain interests (including interests as employees or directors) in both Distributing and Controlled after the distribution. Exceptions will be made on a case-by-case basis, taking into account the extent and nature of the interest in each corporation.

(c) **Certain internal restructurings.** Any internal restructuring in which the distributee is not entitled to eliminate, exclude, or receive a 100 percent dividends-received deduction with respect to, a distribution from Distributing, such as a transaction involving a foreign corporation.

.06 Competition.

(1) **General.** To establish that a Corporate Business Purpose for the distribution is to resolve the taxpayer's problems with customers or suppliers who object to Distributing or Controlled being associated with a business that competes with the customer or supplier, ordinarily, the taxpayer must demonstrate to the satisfaction of the Service that:

(a) One or more customers or suppliers have significantly reduced (or will significantly reduce) their purchases from, or sales to (or, for potential customers or suppliers, have not made any purchases from, or sales to), Distributing or Controlled because of the competing business.

(b) Because of the distribution, these customers or suppliers will significantly increase (or not implement a planned significant reduction in) their purchases from, or sales to, Distributing or Controlled after the distribution.

(c) These customers or suppliers do not object to the Distributing shareholders' ownership of stock of Controlled after the distribution.

(d) Sales to these customers, or purchases from these suppliers, will represent a meaningful amount of sales or purchases by Distributing or Controlled after the distribution.

(2) Substantiation. The taxpayer must submit substantiating evidence. In most cases, corroboration from customers or suppliers will be required.

.07 Facilitating an acquisition of Distributing. To establish that a Corporate Business Purpose for the distribution is to tailor Distributing's assets to facilitate a subsequent tax-free acquisition of Distributing by another corporation (the "acquiring corporation"), ordinarily, the taxpayer must demonstrate to the satisfaction of the Service that:

(1) The acquisition will not be completed unless Distributing and Controlled are separated.

(2) The acquisition cannot be accomplished by an alternative nontaxable transaction that does not involve the distribution of Controlled stock and is neither impractical nor unduly expensive.

(3) The acquiring corporation is not related to Distributing or Controlled. If the taxpayer contends that the Service should rule favorably, notwithstanding the fact that the acquiring corporation is related to Distributing or Controlled, explain the relationship and why the Service should disregard the relationship.

(4) The acquisition will be completed, and, except in unusual circumstances, will be completed within one year of the distribution.

.08 Facilitating an acquisition by Distributing or Controlled. To establish that a Corporate Business Purpose for the distribution is to tailor Distributing's assets or Controlled's corporate structure to facilitate a subsequent tax-free acquisition of another corporation (the "target corporation") by Distributing or Controlled, ordinarily, the taxpayer must demonstrate to the satisfaction of the Service that:

(1) The combination of the target corporation with Distributing or Controlled will not be undertaken unless Distributing and Controlled are separated.

(2) The acquisition cannot be accomplished by an alternative nontaxable transaction that does not involve the distribution of Controlled stock and is neither impractical nor unduly expensive.

(3) The target corporation is not related to Distributing or Controlled. If the taxpayer contends that the Service should rule favorably, notwithstanding the fact that the target corporation is related to Distributing or Controlled, explain the relationship and why the Service should disregard the relationship.

(4) The acquisition will be completed, and, except in unusual circumstances, will be completed within one year of the distribution.

.09 Risk Reduction. If a Corporate Business Purpose for the distribution is to significantly enhance the protection of one or more businesses (the "other businesses") from the risks of another business (the "risky business"), the factors the Service will consider, and the taxpayer should address, include:

(1) The nature and magnitude of the risks faced by the risky business. The taxpayer must submit information regarding the claims history of the risky business, or of the typical risk experience of similar businesses in that industry.

(2) Whether the assets and insurance associated with the risky business are sufficient to meet reasonably expected claims arising from the conduct of the risky business. The taxpayer must submit the book value and approximate fair market value of the net assets, including intangibles, of the risky business. Describe any other factors, such as liabilities that are not included on the taxpayer's balance sheet, that affect the value of the net assets of the risky business. The taxpayer must submit information as to the taxpayer's current insurance coverage and discuss the availability and cost of additional insurance. Facts regarding the cost and availability of insurance generally will require third party substantiation. If affordable insurance is available, but a separation of the businesses would reduce the cost, see section 2.04 of this Appendix A, relating to cost savings.

(3) Whether, under applicable law, the distribution will significantly enhance the protection of the other businesses from the risks of the risky business and, whether, under applicable law, an alternative nontaxable transaction that does not involve the distribution of Controlled stock and which is neither impractical nor unduly expensive (for example, creating a parent/subsidiary or holding company structure) would provide similar protection. See example (3) of § 1.355-2(b)(5). The taxpayer's submission should include an analysis of the law and the application of the law to the relevant facts of the proposed transaction. An opinion of counsel may be required. It is not necessary for the taxpayer to establish conclusively that, under applicable law, the proposed transaction will afford adequate protection or that an alternative transaction would not afford adequate protection. However, the taxpayer must convince the Service that, based on objective analysis of the law and its application to the facts, risk reduction is a real and substantial purpose for the transaction.

APPENDIX B

SECTION 1. RULING REQUESTS INVOLVING RETENTION OF STOCK OR OPTIONS BY DISTRIBUTING

.01 The Service will issue favorable rulings regarding the application of § 355(a)(1)(D)(ii), relating to the retention by Distributing of stock or options in Controlled, to transactions in which Controlled stock will be widely held if Distributing establishes that the following requirements are satisfied:

(1) A sufficient business purpose exists for the retention of the stock, options, and any stock acquired on the exercise of the options.

(2) None of Distributing's directors or officers will serve as directors or officers of Controlled as long as Distributing retains the stock, options, or any stock acquired on the exercise of the options. Under appropriate facts and circumstances, the Service may issue a favorable ruling in cases in which the directors or officers of Distributing will serve as directors or officers of Controlled. For example, the Service may issue a favorable ruling if a director or officer of Distributing serves as a director or officer of Controlled solely to accommodate Controlled's business needs.

(3) The retained stock, options, and any stock acquired upon exercise of the options will be disposed of as soon as a disposition is warranted consistent with the business purpose specified in section 1.01(1) of this Appendix B, but in any event, not later than 5 years after the distribution.

(4) Distributing will vote the retained stock and any stock acquired on exercise of the options in proportion to the votes cast by Controlled's other shareholders. For example, if after the distribution the other shareholders of Controlled vote 70 percent in favor of a matter and 30 percent against, Distributing would be required to vote the stock 70 percent in favor and 30 percent against the matter.

.02 In other cases, the Service may issue favorable rulings, based upon all relevant facts and circumstances, regarding the application of § 355(a)(1)(D)(ii). For example, the Service will rule favorably if the transaction is covered by Rev. Rul. 75-321, 1975-2 C.B. 123.

APPENDIX C

SECTION 1. REPRESENTATIONS REGARDING S CORPORATION STATUS

.01 This Appendix C contains representations regarding S corporation status that the taxpayer may submit to lessen the Service's concerns about the potential avoidance of federal taxes. These representations may be submitted if either Distributing or Controlled will be eligible to elect S corporation status after the distribution. If either Distributing or Controlled will be eligible to elect S corporation status after the distribution, but the taxpayer does not submit any of the representations in this Appendix C, please explain. The taxpayer's failure to submit any of the representations will not prevent the Service from issuing a favorable ruling if it is satisfied that the distribution is motivated in whole or substantial part by one or more Corporate Business Purposes. On the other hand, there may be cases where the submission of one of the representations will not conclusively establish that the transaction does not have the potential for the avoidance of federal taxes.

(1) **No S elections.** *REPRESENTATION: The distributing corporation is not an S corporation (within the meaning of § 1361(a)), and there is no plan or intention by the distributing or controlled corporation to make an S corporation election pursuant to § 1362(a).*

(2) **Distributing and Controlled will elect S corporation status.** *REPRESENTATION: The distributing corporation is not an S corporation (within the meaning of § 1361(a)), but immediately before the distribution, the distributing corporation will be eligible to make an S corporation election pursuant to § 1362(a). The distributing and controlled corporations will elect to be an S corporation pursuant to § 1362(a) on the first available date after the distribution, and there is no plan or intent to revoke or otherwise terminate the S corporation election of either the distributing or controlled corporation.*

(3) **Distributing is an S corporation.** *REPRESENTATION: The distributing corporation is an S corporation (within the meaning of § 1361(a)). The controlled corporation will elect to be an S corporation pursuant to § 1362(a) on the first available date after the distribution and there is no plan or intent to revoke or otherwise terminate the S corporation election of either the distributing or controlled corporation.*

Part IV. Items of General Interest

Notice of Proposed Rulemaking and Withdrawal of Notice of Proposed Rulemaking

General Revision of Regulations Relating to Withholding of Tax on Certain U.S. Source Income Paid to Foreign Persons and Related Collection, Refunds, and Credits; Revision of Information Reporting and Backup Withholding Regulations; and Removal of Regulations Under Part 35a and of Certain Regulations Under Income Tax Treaties

INTL-062-90; INTL-0032-93;
INTL-52-86; INTL-52-94

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking and withdrawal of notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations relating to the withholding of income tax under sections 1441 and 1442 on certain U.S. source income paid to foreign persons, the related tax deposit and reporting requirements under section 1461, and the related collection, refunds, and credits of withheld tax under sections 1461 through 1463 and section 6402. Additionally, this document contains proposed regulations relating to the statutory exemption under sections 871(h) and 881(c) for portfolio interest. This document proposes to remove certain temporary employment tax regulations under the Interest and Dividend Compliance Act of 1983 and to amend existing regulations under sections 6041A and 6050N. This document also proposes changes to proposed regulations contained in project number INTL-52-86 [1988-1 C.B. 892], published on February 29, 1988 (53 FR 5991) under sections 6041, 6042, 6045, and 6049. This document proposes related changes to the regulations under sections 163(f), 165(j), 3401, 3406, 6114, and 6413 and proposes further changes to the proposed regulations under section 6109 contained in project number IL-0024-94 [1995-27 I.R.B. 33] published on June 8, 1995 (60 FR 30211). This document proposes to remove certain regulations under income tax treaties.

The IRS and Treasury have reviewed current withholding and reporting procedures applicable to cross-border flows of income and have concluded that changes are necessary in view of the substantial growth in such flows over the past 15 years. This document also removes proposed regulations published on July 12, 1976 (41 FR 28517) and September 10, 1984 (49 FR 355110), respectively.

DATES: Written comments and requests for a public hearing must be received by July 22, 1996.

ADDRESSES: Send submissions to: CC:DOM:CORP:R ([INTL-0032-93]), Room 5228, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. In the alternative, submissions may be hand delivered between the hours of 8 a.m. and 5 p.m. to: CC:DOM:CORP:R ([INTL-0032-93]), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue NW., Washington, DC.

FOR FURTHER INFORMATION CONTACT: Philip Garlett, telephone (202) 622-3880 (not a toll-free number), for questions on proposed regulations under sections 1441, 1442, 1461, 1462, 1463, 3401, 6402, and 6413; Gwendolyn A. Stanley, telephone (202) 622-3860 (not a toll-free number) for questions on payments to partnerships; Carl Cooper, telephone (202) 622-3840 (not a toll-free number) for questions on proposed regulations under sections 163(f), 165(j), 871(h) and 881(c) and on withholding agreements; Teresa Burrige Hughes, telephone (202) 622-3880 (not a toll-free number), for questions on proposed regulations under sections 6041 through 6049, 6050N; Teresa Burrige Hughes, telephone (202) 622-3880 and Renay France, telephone (202) 622-4910, for questions on proposed regulations under section 3406; Elissa Shendalman (202) 622-3870 on proposed regulations under section 6045 and 6049 relating to the reporting of payments made in a currency other than the U.S. dollar or transactions subject to section 988; Lilo Hester, telephone (202) 874-1490 (not a toll-free number), for questions on proposed regulations under section 6109; David F. Bergkuist, telephone (202) 622-3860 (not a toll-

free number), for questions on proposed regulations under section 6114.

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

The collections of information contained in this notice of proposed rulemaking have been submitted to the Office of Management and Budget for review in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507).

Comments on the collection of information should be sent to the Office of Management and Budget, Attn: Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Washington, DC 20503, with copies to the Internal Revenue Service, Attn: IRS Reports Clearance Officer, T:FP, Washington, DC 20224. Comments on the collections of information should be received by June 21, 1996.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid control number.

The collections of information relating to foreign persons that receive payments subject to withholding under sections 1441 or 1442 of the Internal Revenue Code are in §§1.1441-1(e), 1.1441-4(a)(2), 1.1441-4(b) (1) and (2), 1.1441-4(c), (d) and (e), 1.1441-5(a)(2)(ii), 1.1441-5(b), 1.1441-6(b) and (c), 1.1441-8(b), 1.1441-9(b), 1.1461-1(b) and (c), 301.6114-1, and 301.6402-3(e), 31.3401(a)(6)-1(e). This information is required by the IRS to identify and verify the status of persons to whom payments of U.S. source income is made. This information will be used to claim foreign person status and, in appropriate cases, to claim residence in a country with which the United States has an income tax treaty in effect, so that withholding at a reduced rate of tax may be obtained at source. The likely respondents and recordkeepers are individuals, state or local governments, farms, business or other for-profit institutions, federal agencies, nonprofit institutions, and small business or organizations. Responses to this collection of information are mandatory.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential, as required by 26 U.S.C. 6103.

The burden for the reporting requirement contained in §§1.1441-1(e)(2), 1.1441-4(a)(2), 1.1441-4(b)(2), 1.1441-4(c)(2), 1.1441-4(d), 1.1441-4(e)(1), (2) and (3), 1.1441-6(b), 1.1441-8(b), 1.1441-9(a)(2), 301.6114-1(b)(4), and 301.6402-3(e) will be reflected in the burden of Form W-8, Form 8833, Form 8233, and the income tax return of a foreign person filed for purposes of claiming a refund of tax.

The collection of information requirement for corporations contained in §1.6049-4(c) will be reflected in the burden of Form W-8.

The requirement for the recordkeeping requirement in §1.6049-5(c)(1)(ii) and (iii) is in an existing regulation, appearing in TD 7966 that was approved under OMB number 1545-0112.

Background

This document contains proposed amendments to the Income Tax Regulations (CFR parts 1, 31, 35a and 301) under sections 163(f), 165(j), 871, 881, 1441, 1442, 1461, 1462, 1463, 3401, 3406, 6041, 6041A, 6042, 6045, 6049, 6050N, 6109, 6114, 6402, and 6413 of the Internal Revenue Code (Code). This document also proposes to remove certain regulations under income tax treaties.

Explanation of Provisions

A. Current rules

These proposed regulations deal with the withholding of tax under section 1441, 1442, or 1443 on amounts paid to foreign persons, procedures for claiming foreign status to avoid backup withholding under section 3406 on certain payments, and the reporting to the IRS of payments to foreign persons. Reporting to the IRS may be required under sections 6011 and 1461 or under the reporting provisions of chapter 61 of the Code, such as sections 6041, 6041A, 6042, 6044, 6045, 6049, 6050H, and 6050N, (the 1099 reporting provisions).

1. U.S. income tax on U.S. source income of foreign persons.

Under sections 871(a) and 881(a) of the Code, non-resident alien individuals and foreign corporations are subject to a 30 percent tax on most items of income they receive from sources within the United States that are not effectively connected with the conduct of a trade or business in the United States. Income taxable under these provisions includes interest, dividends, royalties, compensation, and other fixed or determinable annual or periodical income. The tax liability imposed under section 871(a) and 881(a) is generally collected by way of withholding at source under section 1441(a) (for payments to non-resident alien individuals and foreign partnerships) or under section 1442(a) (for payments to foreign corporations). Special withholding provisions apply under section 1443 to payments of certain income to foreign tax-exempt entities.

The 30 percent rate is often reduced under the Code or an income tax treaty. Under current regulations, a withholding agent may generally rely on a statement furnished by, or on behalf of, the beneficial owner certifying entitlement to a reduced rate. For example, the portfolio interest exception under section 871(h) and 881(c) is conditioned upon the beneficial owner of the interest providing a statement of foreign status to the U.S. withholding agent, which can be provided on a Form W-8. See §35a.9999-5(b), A-9. If a reduction is claimed under an income tax treaty, the withholding agent may generally rely on a Form 1001 provided by, or on behalf of, the beneficial owner claiming residence in a treaty country. For dividends, however, no certification is required and the withholding agent may generally rely on the address of the payee in the treaty country. The procedural requirements for claiming a reduced rate of withholding may vary depending upon the type of income, the taxpayer, or whether a treaty is involved.

A withholding agent is generally required to file an annual income tax return on Form 1042 to report amounts upon which a tax was actually withheld under chapter 3 of the Code or would have been required to be withheld but for an exemption under the Code, the regulations, or an income tax treaty. An information return on a Form 1042-S

must be attached to the Form 1042 and report each recipient's name and address, amounts paid, and taxes withheld, if any. Section 1.1461-2(b) and (c).

2. Backup withholding

Under chapter 61 of the Code and section 3406, a reportable payment, as defined in section 3406(b), is subject to backup withholding at the rate of 31 percent unless the payor receives a taxpayer identifying number (TIN), generally on a Form W-9, and, for reportable interest and dividends, a certification that the payee is not subject to notified payee underreporting. The payor of a reportable payment is also generally required to file Form 1099 with the IRS showing the name, address, and TIN of the payee; the amount of the payment; and the amount that was withheld, if any. The payor must also provide a copy of Form 1099 to the payee, who must report the payment on an income tax return to the extent the payment constitutes gross income. A payor that fails to obtain a TIN or other required information or to backup withhold when required under section 3406 may also be liable under section 3403 for the amount that should have been withheld. Information reporting by payors is critical to a matching system that allows the IRS to match information provided by payors with income reported on a payee's return.

The information reporting provisions of chapter 61 provide guidance to help payors determine when payments are made to a foreign person and, therefore, exempt from 1099 reporting and backup withholding. Generally, depending upon the type of payment involved, a payor may rely on a certification of foreign status made on Form W-8, Form 1001, Form 4224, or on documentary evidence. Therefore, even though an amount is exempt from withholding under chapter 3 of the Code if earned by a foreign person (e.g., gain from the sale of securities), a payor must nevertheless comply with specified certification procedures in order to avoid being subject to backup withholding. Only amounts subject to reporting under the 1099 reporting provisions can be subject to backup withholding under section 3406. Therefore, payments to foreign persons that are exempt from reporting are also exempt from backup withholding.

B. Need for reform

The IRS and Treasury have reviewed the current withholding and reporting procedures applicable to cross-border flows of income and have concluded that changes are necessary in view of the substantial growth in such flows over the past 15 years. The IRS and Treasury have concluded that allowing the benefit of the reduced rate at source continues to be desirable. A system that reduces withholding at source permits an investor to receive its full income without the administrative costs and delays that can occur when applying for a refund of withheld taxes. This advantage, however, is necessarily accompanied by the need to rely, in part, on withholding agents. Withholding agents perform an important compliance function as recipients of the necessary documentation substantiating claims of foreign status and of reduced rates of withholding and as providers of information to the IRS.

One of the important objectives of the proposed revisions is to eliminate unnecessary burdens that the lack of standardization and coordination of current procedures imposes on withholding agents. For example, under current rules, different forms must be used for different purposes; different standards of proof apply for establishing foreign status for purposes of the 1099 reporting provisions (and the related backup withholding provisions) and of the Chapter 3 withholding provisions. Also, the revisions seek to facilitate compliance by clarifying many of the uncertainties under current procedures (*e.g.*, the scope of due diligence standards imposed on withholding agents). This proposal also addresses the important issue of payments to intermediaries (nominees, agents, etc.) and whether, in the case of interest, dividends, and gross proceeds from publicly traded or widely held obligations or stocks, intermediaries should certify status on behalf of beneficial owners and, if so, how. Under current rules, nominee procedures work differently for different types of income. For example, a U.S. broker redeeming a short-term obligation held by a foreign financial institution as an agent may exempt the payment from 1099 reporting and backup withholding and grant the exemption from the 30 percent tax under section 871(a) without having to obtain certificates or documentation. If the foreign financial institution makes a payment to another person offshore then

no certification or documentation is required. On the other hand if, for example, the foreign financial institution, remitted the amount to a person in the United States through a U.S. office, it might have to obtain a Form W-8 or a Form W-9. In contrast, interest on registered obligations may not qualify as portfolio interest under sections 871(h) and 881(c) unless the U.S. withholding agent receives a statement that the beneficial owner of the obligation is not a U.S. person (see section 871(h)(2)-(B)(ii)). Current regulations implement this condition by requiring that a beneficial owner certification be passed up through a chain of intermediaries to the U.S. withholding agent. These procedures have proved difficult to implement in a number of cases and these proposed regulations offer alternative procedures. The proposed revisions, therefore, respond to the concerns expressed by various representatives of the financial community regarding the cost of complying with current procedures and potential harm to the competitiveness of U.S. financial institutions in handling investment transactions in the United States and abroad.

These proposed regulations are also responsive to the Congressional mandate in section 342 of the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA) that Treasury consider a range of options for replacing the address/self-certification method of administering income tax treaty benefits. Since 1982, the IRS and Treasury have studied several options for improving the withholding tax procedures, including a system of certification of residence in a treaty country and refund systems. At hearings held in February of 1985 on proposed regulations issued in 1984 under section 1441, comments from the public and several U.S. treaty partners made it apparent that certification requirements, as proposed, would create too many administrative problems for payments made through nominees. The proposed revisions take these comments into account and propose to rely on procedures essentially identical to the procedures proposed for portfolio interest on registered obligations.

The streamlining of current procedures and the implementation of workable nominee certification procedures represent a substantial simplification and reduction of burden. The IRS and Treasury expect that this, in turn, should result in greater compliance and

improve the ability by withholding agents and the IRS to detect abusive claims under U.S. income tax treaties or under the Code.

C. Summary of proposal

1. Changes affecting portfolio-type investments

The proposed regulations under section 1441 and related Code provisions would substantially revise some aspects of the current system for withholding on, and reporting of, amounts paid to foreign persons. Current certification procedures (*i.e.*, Forms W-8, 1001, 4224, etc.) would be unified and reliance standards would be clarified in an effort to streamline the processing of cross-border payments, particularly by banks and other financial institutions. Most forms (W-8, 1001, 4224, 8709) are proposed to be combined into a single form (Form W-8). In addition, taxpayer identifying numbers are not required to be stated on withholding certificates, with certain limited exceptions that do not affect market-based transactions. These changes are important steps toward reducing the burden on withholding agents and assisting taxpayer compliance.

The address rule for claiming tax treaty benefits for dividends is proposed to be eliminated. Instead, dividends would be made subject to the same beneficial owner and intermediary certification procedures as are proposed for portfolio interest on registered obligations. It is also proposed to apply the same procedures to bank deposit interest (as described in section 871(i)(2)(A)). On the other hand, the documentary evidence procedures currently in effect for bank deposit interest on accounts held with foreign branches would be continued and would be applied as well to offshore payments of dividends on publicly traded stocks and portfolio interest on registered obligations. Therefore, documentary evidence would become the general rule for dividends and interest earned on accounts held with foreign branches. These proposed changes illustrate the effort by the IRS and Treasury to eliminate unnecessary procedural differences in order to reduce the burden on withholding agents.

The proposal does not generally affect other important classes of investment transactions. Thus, current port-

folio interest rules for bearer obligations (including commercial paper), convertible obligations, pass-through certificates, as well as rules for broker proceeds and short term obligations would be retained. In order to further simplify compliance, the regulations under section 165(j) (§1.165-12) are proposed to be revised to eliminate the requirements that, in connection with delivery of bearer obligations, holders receive statements and send confirmations. Provisions regarding foreign-targeted registered obligations are to be retained. However, because these special procedures have been rarely used, comments are solicited on their usefulness and whether they should be retained.

Foreign intermediary procedures as currently applicable to portfolio interest (which are proposed to become applicable to dividends and bank deposit interest as well) are substantially revised by providing several options, allowing different taxpayers to comply in different ways. These options recognize that it is appropriate to adapt withholding requirements to accommodate different types of transactions and should provide substantial relief from current requirements.

In order to allow sufficient time for transition, the regulations are proposed to be generally effective for payments made after 1997. In addition, withholding agents would be allowed to continue to rely on existing certificates after that date until their validity expires as determined under current rules. Comments are solicited on whether these proposed effective dates leave adequate time to implement necessary system changes.

The regulations proposed in 1988 regarding the reporting by U.S. banks of bank deposit interest paid to Canadian residents are finalized, effective for payments made on or after January 1, 1997 with respect to Forms W-8 furnished on or after that date. See the Rules and Regulations section of this issue of the Bulletin.

2. Intermediary procedures options for portfolio interest, dividends on publicly traded stock, and bank deposit interest.

The proposed regulations offer intermediary certification options designed to simplify compliance by withholding agents. These procedures would be

mostly relevant to portfolio interest on registered obligations, dividends on publicly traded stocks (eliminating the address rule), and interest paid on bank deposits (as described in section 871(i)(2)(A)). First, for portfolio interest on registered obligations, the current certification procedures would be retained, as an option and are not repropoed. See §35a.9999-5(b), A-9. These rules will be included in final regulations in proposed §1.871-14(c)-(2)(iii) and, accordingly, that section of the proposed regulations is reserved. Preserving the existing regulations is designed to accommodate those taxpayers and withholding agents for whom the current rules work appropriately.

The regulations propose to add two new procedures. First, a withholding agent would be allowed to rely on an intermediary Form W-8 furnished on behalf of one or more beneficial owners (or other intermediaries) without having to obtain beneficial owner documentation if the intermediary has entered into a withholding agreement with the IRS and, thus, is a "qualified intermediary." In a chain of intermediaries, an intermediary would be allowed to rely on the intermediary Form W-8 of another qualified intermediary. If the other intermediary is not qualified, the qualified intermediary would generally be required to obtain beneficial owner documentation from the other non-qualified intermediary. The qualified intermediary would then pass such documentation up the chain or rely on such documentation when issuing its intermediary Form W-8.

Under the withholding agreement procedure, a qualified intermediary would agree with the IRS to obtain such documentation or certifications as the agreement would specify. It is contemplated that institutions that are subject to bona fide "know-your-customer" procedures under their domestic laws will generally be permitted to rely on such procedures. The withholding agreement will generally include provisions for beneficial owner information to be reported or made available to the IRS and for the IRS to audit such information. In appropriate cases, the reporting and audit may be limited to the beneficial ownership information pertaining to U.S. source income (other than gross proceeds) of U.S. customers or to an audit of the reports prepared by, and the methodology employed by,

the approved external auditors of the qualified intermediary.

The regulations propose a second intermediary procedure permitting a foreign agent of a U.S. withholding agent to act on behalf of the withholding agent. While the U.S. withholding agent would remain liable for the acts (or failures to act) of its agent, the proposed procedure streamlines the withholding process as the foreign agent would collect the appropriate documentation on behalf of the U.S. withholding agent and report beneficial owner information to the IRS without having to furnish the documentation to the U.S. withholding agent. The documentation requirements under this procedure would be the same as those normally applicable to withholding agents.

Lastly, the proposed regulations provide that the U.S. competent authority may agree to special withholding procedures with a foreign competent authority under an income tax treaty. The United States intends to consult with its tax treaty partners before implementing changes that would affect its relationship with its treaty partners.

3. Use of taxpayer identifying number.

A taxpayer identifying number (TIN) is not required to be shown on withholding documents provided for income on portfolio-type investments.

A TIN continues to be required for claims of effectively connected income. A TIN would also be required to support claims of benefits under an income tax treaty (other than dividends on publicly traded stocks). Therefore, for example, payments of dividends on non-publicly traded stocks, royalties, or related party interest would require a TIN to be shown on the withholding certificate in order for a withholding agent to rely on a claim of a reduced rate under a tax treaty.

In the case of an individual, a TIN would generally be an IRS individual taxpayer identifying number (ITIN) issued by the IRS to a nonresident alien individual who is not otherwise eligible for a Social Security Number. In the case of a non-individual, a TIN would be an Employer Identification Number (EIN). Over time, the IRS will issue EIN's to foreign persons that begin with the two digits "98" to permit instant recognition of foreign status. See regulations proposed under

section 6109 contained in project number INTL-0024-94, published on June 8, 1995 (60 FR 302111), describing the types of taxpayer identifying numbers issued to nonresident alien individuals and the manner in which a number can be obtained. Further revisions to the regulations under section 6109 are proposed in order to require the statement of a TIN in appropriate cases.

4. Other proposed changes

The regulations propose to clarify the extent of due diligence expected from certain withholding agents, such as banks and other financial institutions. Thus, for payments of portfolio-type income, the withholding agent's due diligence would be limited to an examination of the address stated on the withholding certificate. If the address on the certificate were a U.S. address or did not match the address information in its records, the withholding agent would have to seek further proof of a claim of foreign status. This change would not affect the current requirement that a withholding agent cannot ignore what it actually knows when determining the extent to which it may rely on a withholding certificate. However, in the case of financial institutions, knowledge would be limited to information that can be associated with the account under the same procedures as apply for purposes of the backup withholding provisions.

As a further burden reduction, the regulations propose to eliminate the requirement to attach withholding certificates to Forms 1042 and 1042-S. The current reporting requirements are otherwise unchanged except for clarification of how these requirements apply in the case of payments to intermediaries. Therefore, even though certification procedures are proposed to be modified for bank deposit interest, such interest continues to be exempt from reporting (except for certain interest on bank deposits paid to Canadian residents).

The period of validity of a certificate of foreign status (Form W-8) is limited to three years as under current law. However, a Form W-8 stating a beneficial owner's TIN is proposed to be valid indefinitely if it relates to income required to be reported to the IRS (or if the TIN is actually reported even though not otherwise required). The validity period for certificates used to

claim a reduced rate for effectively connected income is proposed to be extended from one year to three years.

The regulations propose new procedures dealing with payments to foreign partnerships. These procedures generally would allow looking through to the partners and reliance on a certification provided for each partner. Alternatively, in order to facilitate certification for partnerships with many partners or for tiered partnerships, the regulations would also allow a foreign partnership to be a qualified intermediary under an agreement with the IRS. In that case, the partnership would be allowed to furnish an intermediary certificate for the partnership. The partnership would be required to withhold under section 1441 in the same manner as a domestic partnership. In addition, the regulations would clarify the manner in which a foreign entity and its interest holders can determine entitlement to benefits under an income tax treaty with a particular country based upon the principles in effect under the laws of that country.

The proposed regulations also address the practical difficulties that exist under current rules due to the lack of clear guidelines on determining the status of a payee as a U.S. or a foreign person in the absence of documentation. While some guidelines exist in limited cases (e.g., §35a.9999-5(b) A-10), guidance is incomplete. The proposed regulations offer a comprehensive and uniform set of presumptions to assist withholding agents with these determinations.

5. Changes to reporting rules under chapter 61 of the Internal Revenue Code

On February 29, 1988, the IRS and Treasury published in project number INTL-52-86 (53 FR 5991) proposed amendments to the 1099 information reporting regulations (the 1988 proposed regulations) modifying the reporting requirements and the procedures for presenting a claim of foreign status. The provisions in the 1988 proposed regulations concerning information reporting of bank deposit interest paid to persons resident in Canada are finalized. See §1.6049-5(e)(2) of the 1988 proposed regulations and the Rules and Regulations section of this issue of the Bulletin. The 1988 proposed regulations are not otherwise

amended. In order to standardize procedures, changes are proposed to the procedures for certifying foreign status that were proposed in 1988 so as to conform them to those proposed under section 1441. The IRS and Treasury are considering finalizing the 1988 proposed regulations at the same time that the proposed regulations under section 1441 are finalized.

Proposed effective dates

Unless otherwise provided in the regulations, the regulations are proposed to be effective for payments made after December 31, 1997. The regulations contain a number of transition rules designed to phase out currently outstanding withholding certificates (e.g., Forms W-8 and 1001).

Section-by-section analysis

§1.163-5 Denial of interest deduction on certain obligations issued after December 31, 1982, unless issued in registered form

Section 1.163-5(c) contains foreign targeting procedures applicable to certain obligations issued in bearer form. Section 1.163-5(c)(2)(i)(B)(5) would be revised to modify the cross-reference to the documentary evidence rules since the Q&A regulations under part 35a are proposed to be eliminated.

§1.165-12 Denial of deduction for losses on registration-required obligations not in registered form

Section 165(j)(1) and §1.165-12(a) deny a loss deduction to a holder of a registration-required obligation that is not in registered form unless the holder meets certain exceptions. Under §1.165-12(c)(1)(iii) and (iv), the loss disallowance rule does not apply to a holder that delivers a registration-required obligation that is in bearer form and that is offered or sold in the United States if the holder delivers the obligation to a financial institution, and the financial institution provides a statement that it is a financial institution within the meaning of §1.165-12(c)(1)(v), it is purchasing the obligation for its own account, the account of another financial institution, or an exempt organization, that will comply with section 165(j)(3)(A), (B), or (C). The loss disallowance rule also does not apply if a holder delivers a

registration-required obligation in bearer form that is offered or sold outside the United States if it is delivered to a financial institution and the holder gives the financial institution a confirmation stating that any U.S. taxpayer that holds the obligation in bearer form and that is not exempt under section 165(j)(3)(A), (B), or (C) will be denied a deduction for any loss or capital gain treatment with respect to the obligation. A holder may deliver a registration-required obligation in bearer form that is offered and sold outside the United States to a person other than a financial institution only if the holder has documentary evidence, as described in §35a.9999-4T, A-5 that the person is not a U.S. person.

These proposed regulations would revise §1.165-12(c)(1)(iv) to eliminate the requirement that the holder receive a statement from a financial institution for bearer obligations offered or sold in the United States. The proposed regulations would also eliminate the requirement that the holder deliver a confirmation to a financial institution for obligations offered or sold outside the United States. These changes are proposed to reduce the documentation burden associated with secondary market transactions. The documentary evidence requirement for delivery outside the United States to a foreign person other than a financial institution is retained. The proposed regulations would clarify that the holder may receive such evidence electronically.

§1.871-14 Rules for portfolio interest.

Under section 871(h) and 881(c), interest that qualifies as portfolio interest is generally exempt from tax and is exempt from withholding at source under section 1441(b)(9). Section 1.871-14 proposes procedures governing whether interest (including original issue discount) qualifies as portfolio interest described in section 871(h)(2). Section 1.1441-2(d) provides the exemption from withholding.

For interest on bearer obligations, the existing provisions in §35a.9999-5(a), A-1 (dealing with portfolio interest on bearer obligations) and in §35a.9999-5(c) (dealing with convertible obligations) will be incorporated in §1.871-14(b) without substantive changes and are not repropoed. These rules will be restated in proposed §1.871-14(b)(1) and (b)(2) that are currently shown as reserved.

For interest on registered obligations, section 871(h)(2)(B)(ii) provides that such interest qualifies as portfolio interest only if the U.S. withholding agent receives a statement that the beneficial owner is not a United States person. Paragraph (c)(2)(i) provides that the statement requirement would be satisfied if the beneficial owner furnishes the type of documents described in proposed §1.1441-1(e)(1)(i) for a withholding agent to rely on a claim of foreign status. Thus, in the case of a payment to a beneficial owner, the beneficial owner must provide a beneficial owner withholding certificate described in proposed §1.1441-1(e)(2) or, if the payment is made on an account held at a foreign branch, documentary evidence may be substituted (see paragraph (c)(2)(ii)). The ability to use documentary evidence on foreign branch accounts is a significant change from current law and one that intends to reduce the burden on transactions outside the United States. Further, as under current regulations, the withholding certificate would not have to state a taxpayer identifying number (although one may be provided, if desired). See §35a.9999-5(b), A-9.

In the case of a payment to a foreign person that acts as an intermediary (e.g., an agent, representative, nominee, etc.), the proposed procedures under section 1441 would require either that the intermediary furnish an intermediary withholding certificate or, if the intermediary acts as the agent of the withholding agent, that the intermediary be an authorized foreign agent. Under proposed §1.1441-1(e)(3)(iv) or proposed §1.871-14(c)(2)(iii), the certificate could be, as under current rules, a certificate to which the beneficial owner documentation is attached (see §35a.9999-5(b), A-9). Alternatively, under proposed §1.1441-1(e)(3)(ii), it could be a certificate by which the intermediary certifies for the beneficial owner (or other intermediaries) without being required to attach beneficial owner documentation. The latter certificate could be issued only by a qualified intermediary, i.e., a person that has an agreement with the IRS. The qualified intermediary certificate would be issued based upon certifications or documentation obtained by the qualified intermediary. The same standards would apply to these documents as are proposed to be applied to documents that a U.S. withholding agent is required to

obtain when paying directly to a beneficial owner. Therefore, a taxpayer identifying number is not required to be shown on a beneficial owner withholding certificate provided to the qualified intermediary. Alternatively, the qualified intermediary could rely on documentary evidence for accounts held at foreign branches. In addition, different procedures may apply under the terms of a qualified intermediary's agreement with the IRS.

Where a withholding agent acts through an authorized foreign agent, certificates received by the agent would be deemed to be received by the withholding agent. In that case, no certificate would be required from the authorized agent. See proposed §1.1441-7(c)(2) for the description of an authorized foreign agent and proposed §1.1461-1(b)(2)(iii) and (c)(4)-(iii) for the filing of returns by the withholding agent and its authorized foreign agent. Paragraph (c)(2)(iv) specifies that other procedures may apply under a competent authority agreement with a country with which the United States has an income tax treaty.

The regulations clarify the consequences of a late-received Form W-8 or other documentation. Paragraph (c)(3) provides that the withholding certificate may be received by the withholding agent at any time before expiration of the beneficial owner's period of limitation for claiming a refund of tax with respect to the interest. The applicable period is described in section 6511(a). Under this rule, a foreign person would be allowed, for example, to provide the required certificate to a U.S. withholding agent (or its authorized foreign agent) at any time prior to filing an income tax return and still be able to qualify the interest as portfolio interest. However, a withholding agent that does not hold a valid certificate (or other valid documentation) when paying the interest would be required to withhold. Failure to do so would make the withholding agent liable for the tax if the required certification or documentation procedures are not complied with prior to the expiration of the beneficial owner's period of limitation. If a withholding agent fails to withhold although it does not hold a valid certificate, but the documentation procedures are ultimately complied with, a withholding agent would be liable for

interest pursuant to section 1463 even though there is no underlying tax liability. In addition, the withholding agent may be subject to penalties for failure to withhold tax. See proposed §1.1441-1(f)(5).

Paragraphs (d) and (e) are reserved. Paragraph (d) will reflect the rules in §35a.9999-5(e), regarding pass-through certificates. Paragraph (e) will reflect the rules in 35a.9999-5(b) A-12 through A-15 regarding foreign-targeted registered obligations. These rules are not repropounded. Under §1.871-14(g), the rules contained in proposed regulation §1.871-14 are proposed to be effective for payments of interest after December 31, 1997. However, withholding agents may continue to rely on valid Forms W-8 that they hold on the date that is 60 days after the regulations become final until the forms expire under the rules as in effect on April 22, 1996.

§1.1441-1 Requirement for the withholding of tax on payments to foreign persons.

This section states the general rules concerning withholding on payments to foreign persons. Paragraph (a) provides the general purpose and scope of the section. Paragraph (b) states the general rule that a withholding agent must withhold 30 percent of the gross amount of income subject to withholding if paid to a foreign person unless the beneficial owner of the income is a U.S. person or is a foreign person entitled to a reduced rate of tax. A withholding agent may grant a reduced rate at source in the case of a payment to a foreign person only if, before payment, it can associate the appropriate documentation with the payment. Therefore, actual knowledge that the beneficial owner is a foreign person would not excuse the obligation to obtain appropriate documentation. A withholding agent failing to act in accordance with these rules may ultimately be relieved from the liability for the tax under section 1461, but would, in any event, be liable for interest, and possibly, penalties. See paragraph (f)(5). For this purpose, payment to a foreign person includes a payment to a U.S. person if the withholding agent has actual knowledge or reason to know that the U.S. person is acting as the agent of a foreign person. These rules restate current law. See §§1.1441-1 and

1.1441-7(a)(1) of the existing regulations.

Paragraph (c) defines terms, including payee and beneficial owner. Paragraph (c)(3) defines a payee as the person to whom the payment is made. This definition has significance for purposes of coordinating the section 1441 withholding provisions with the 1099 reporting and backup withholding rules under chapter 61 of the Code and section 3406, respectively (the 1099 reporting and backup withholding provisions determine consequences of payments based on payees; in contrast, the section 1441 withholding provisions determine consequences of payments based on beneficial owner). In the case of a payment to a foreign partnership, paragraph (c)(3)(ii) provides that the partners, and not the partnership, are considered to be the payees. However, a foreign partnership could be considered a payee if it certified to the withholding agent that it is a qualified intermediary (see paragraph (e)(5) regarding qualified intermediaries) or if it certified that the income is effectively connected with a U.S. trade or business (in which case, the partnership must itself withhold the tax required under section 1446). The provisions specify how these rules would apply on a look-through basis to tiered partnership structures.

Under paragraph (c)(6), a beneficial owner is defined as the person who, under U.S. tax principles, would be required to include the amount paid in gross income. Therefore, under these principles, partners, and not partnerships, are the beneficial owners (unless the partner is itself a partnership, in which case, one looks through to the partners of the highest tier foreign partnership). Therefore, the identification of a beneficial owner is influenced by the classification of the entity to which the payment is made. This proposed rule revises §1.1441-3(f) of the existing regulations that, in effect, treats a partnership as a beneficial owner for purposes of the withholding provisions. This provision has created difficulties for partners of a foreign partnership who wish to claim the benefit of a reduced rate at source based on their status, but may not do so because the entity does not qualify for the reduced rate. The proposed regulations would alleviate these difficulties by permitting beneficial owner information to be passed to the with-

holding agent or by permitting the partnership to be a qualified intermediary.

The IRS and Treasury are aware that some large investment partnerships hold significant amounts of U.S. portfolio type investments. The IRS and Treasury understand that generally these entities are treated as corporations under the provisions of section 7704(c)(3) and the regulations under that section. Therefore, the proposed revisions requiring beneficial owner documentation for partners would not adversely affect these entities. The IRS and Treasury solicit comments on this point.

Generally, the determination of the classification of an entity, including an entity organized in a foreign country, is made under U.S. tax rules. Because U.S. and foreign laws may differ on classification principles, the U.S. tax classification of an entity as a partnership or a corporation may differ from the tax treatment of that entity under the laws of a foreign country. Therefore, in the case of income paid to a foreign entity, the entity might be considered the beneficial owner under U.S. tax principles (because it is classified as an association taxable as a corporation under U.S. tax principles), but, if foreign tax principles are applied, its interest holders, rather than the entity, might be considered the beneficial owners. This dual characterization may give rise to difficulties in the application of income tax treaties. In order to alleviate these difficulties, paragraph (c)(6)(ii)(B) proposes that foreign tax principles, rather than U.S. tax principles, apply to identify the beneficial owner of income for which a claim of a reduced rate of withholding is made based upon a tax treaty. Under this proposed rule, when a benefit is claimed under a tax treaty with a particular country, the tax principles that govern the determination of who the beneficial owner is for purposes of obtaining benefits under that treaty would be the principles in effect under the laws of that country. This clarification is intended to address the significant uncertainties resulting from the current lack of guidance on these issues. The IRS and Treasury intend to consult with treaty partners in order to promote uniformity in this area. Paragraph (c)(6)(iii) provides that the beneficial owner rules in the proposed regulations would not apply to trusts.

Until further guidance is provided, the rules in the current regulations would continue to apply trusts. See §1.1441-3(f) and (g) of the existing regulations.

While different procedures would apply depending upon whether a payment is made to a corporation or a partnership, a withholding agent would not be required to determine the classification of an entity when making a payment to a foreign person. Rather, a withholding agent would be allowed to rely on the classification claimed by the entity, unless it had actual knowledge or reason to know otherwise.

Paragraph (d) deals with procedures that would enable a withholding agent to determine the circumstances in which it could consider that the payment is made to a U.S. person and is, therefore, exempt from section 1441 withholding. This paragraph replaces §1.1441-5 of the existing regulations and proposes to replace Form 1078 with Form W-9, consistent with the manner in which a U.S. payee must generally provide a taxpayer identifying number under section 3406. In the case of a payment to an exempt recipient or a payment of scholarship, grant, pension, or annuities, for which no Form W-9 is required under section 3406, a person also would be permitted to use a Form W-9 to establish its U.S. status. The regulations specify the information that must be stated on such a certificate, which parallels that required under §31.3406(h)-3(e)(2) in order for a payor to reasonably rely on a Form W-9. If no, or insufficient, documentation is provided, the presumptions in §1.1441-1(f) would apply to determine whether the beneficial owner should be treated as a foreign or U.S. person.

In the case of a payment to a foreign person acting as an intermediary (e.g., agent, representative, or nominee) for a U.S. person, paragraph (d)(3) provides that the intermediary may transmit a Form W-9 for the U.S. person to claim U.S. status and avoid section 1441 withholding. If the U.S. person is not an exempt recipient, the withholding agent would then have to comply with the 1099 reporting requirements under chapter 61 of the Code, because, under these rules, the U.S. person would be treated as a payee. Similarly, as a result of the payee rules set forth in paragraph (c)(3)(ii) dealing with payments to foreign partnerships, a withholding agent may treat a payment to a foreign partnership as a payment made to a

U.S. person to the extent of the U.S. partner's distributive share of that payment. Similarly, the withholding agent would have to comply with the 1099 reporting requirements.

Paragraph (e) describes the conditions for a withholding agent to rely upon a beneficial owner's claim of foreign status. Paragraph (e)(1) provides that a withholding agent may rely upon a claim of foreign status if, prior to making the payment, the withholding agent (1) holds a beneficial owner withholding certificate or an intermediary withholding certificate, (2) complies with on-line confirmation procedures when prescribed by the IRS, and (3) has not received a notification from the IRS that the withholding certificate is incorrect or unreliable. The withholding agent's reliance on the withholding certificate is subject to the withholding agent's actual knowledge or reason to know otherwise. See standards of knowledge in proposed §1.1441-7(b).

Paragraph (e)(2) sets forth the requirements for a beneficial owner withholding certificate. Generally, a withholding certificate would be a Form W-8 or, in the case of certain compensation for personal services, a Form 8233 (or an acceptable substitute) that is signed under penalties of perjury by the beneficial owner and contains certain required information. The certificate serves as a representation that the beneficial owner is not a U.S. person and that the conditions for claiming a reduced rate of withholding tax are satisfied. These conditions may vary depending upon the nature of the income or the type of exemption claimed.

Required information on a beneficial owner Form W-8 would include the beneficial owner's name, permanent residence address, the type of income to be received, and the basis for any reduced rate claimed. Generally, the Form W-8 would not be required to state the beneficial owner's taxpayer identifying number ("TIN"), except in limited cases (see paragraph (e)(4)(vii), below). Paragraph (e)(3) sets forth the requirements for an intermediary withholding certificate. Intermediary withholding certificates may be provided by one of three types of persons: (1) a qualified intermediary, (2) a foreign partnership, or (3) an agent, nominee, or other representative that is not a qualified intermediary.

Information required from a qualified intermediary on a Form W-8 would include similar information as that required for the beneficial owner Form W-8 except that the information would relate to the intermediary. In addition, the Form W-8 would have to state a TIN and certify that the issuer is a qualified intermediary and has obtained the appropriate certificates or documentation with respect to the account holders covered by the Form W-8. A foreign partnership that is not a withholding agent (because it is not a qualified intermediary or acting for the account of others) would have to provide the same information about itself, and attach the partners' withholding certificates. In addition, the partnership would be required to state an EIN on the withholding certificate. See proposed §1.1441-5(b) for the certificates required to be attached in the case of tiered partnerships. See also, proposed §1.1461-1(c)(4)(v) for Form 1042-S filing requirements for the withholding agent.

An agent, nominee, or representative furnishing an intermediary certificate would have to provide information about itself, state an EIN for the intermediary (or an SSN or ITIN in the case of an individual) and certify that it is not acting for its own account and is using the Form W-8 to transmit beneficial owner certification for the payment to which the Form W-8 relates. These procedures are essentially similar to those in effect for portfolio interest on registered obligations under §1.9999-5(b), A9 and that are proposed to be retained in proposed §1.871-14(c)(2)(iii).

Paragraph (e)(4)(i) requires that, in the case of joint owners, each owner provide a withholding certificate. This rule would parallel the requirements for backup withholding purposes. See §31.3406(h)-2(a).

Paragraph (e)(4)(ii)(A) provides the general rule that a withholding certificate would be valid for a period of three years or until the circumstances of the beneficial owner changed, making an item of information on the certificate incorrect. However, under paragraph (e)(4)(ii)(B), a withholding certificate that includes a TIN would be valid indefinitely if the income (or, under special procedures, the TIN) with

which the certificate is associated were reported to the IRS. For example, a bank may rely on a claim of foreign status by an account holder if it holds a Form W-8 for the account holder even without a TIN. In that case, the certificate would be valid for a period of three years only. If, however, the account holder were to state a TIN on the form and the bank adopted procedures by which it reports the TIN to the IRS as provided in proposed §1.1461-1(d), the certificate would be valid indefinitely until a change in circumstances of the account holder made the information on the form incorrect.

Second, certificates furnished to claim a reduced rate of withholding on income that is effectively connected with the conduct of a trade of business within the United States would also be limited to three years in all circumstances. This is a change from existing regulations under §1.1441-4(a)(2) that require that a new certificate be filed each year. This change would relieve the burden associated with annual renewal of these certificates and simplify compliance by providing uniform validity period rules. The 3-year period of validity for this certificate would extend from the date it is signed to the last day of the third succeeding calendar year. This change would insure a full 3-year validity period in all cases (and up to four years where the certificate is furnished at the beginning of the calendar year).

Under paragraph (e)(4)(iii), withholding certificates must be retained for as long as they are relevant for the determination of the withholding agent's liability under proposed §1.1461-1. This rule would replace the 4-year retention period under current law and conform the rules under section 1441 to the retention period required for Forms W-9 under section 3406. This change is necessary because the Form W-8, like Form W-9, is proposed to be made valid indefinitely in certain circumstances. Paragraph (e)(4)(iv) anticipates the possibility that, in the future, a withholding agent may rely on electronically transmitted information otherwise required to be stated on a withholding certificate.

Paragraph (e)(4)(v) provides for on-line confirmation procedures for TIN's required to be stated on withholding certificates in order to verify their correctness and the claim that it be-

longs to a foreign person. Such procedures are being developed by the IRS and, when the system becomes operational, the IRS may require certain categories of withholding agents handling large volumes of payments to foreign persons (such as certain teaching institutions) to perform on-line confirmation of such TIN's. These procedures would be similar to those currently in use under section 3406 in order to notify payors of an incorrect TIN.

Paragraph (e)(4)(vi) defines an acceptable substitute form. As under section 3406, these regulations would permit the use of substitute forms provided the information furnished is the same as is required under the regulations and is certified to be correct under penalties of perjury. See §31.3406(h)-3(c)(1).

Paragraph (e)(4)(vii) provides all of the circumstances in which a taxpayer is required to furnish a TIN on a withholding certificate for purposes of the regulations under sections 1441, 1442, and 1443. Taxpayers would be required to furnish a TIN when claiming the benefit of a reduced rate under an income tax treaty (other than with respect to dividends on publicly traded stocks) or because income is effectively connected with a U.S. trade or business. In addition, intermediaries, partnerships, foreign organizations claiming to be tax-exempt under section 501(c), and private foundations would be required to furnish a TIN. A TIN would be an IRS Individual Taxpayer Identification Number (ITIN), a Social Security Number (SSN), or an Employer Identification Number (EIN). A non-resident alien individual not eligible for a social security number would be able to obtain an ITIN from the IRS. See proposed regulations under section 6109 describing procedures for obtaining an ITIN.

Paragraph (e)(5)(i) provides that a qualified intermediary may furnish a single intermediary withholding certificate to a withholding agent on behalf of beneficial owners, other intermediaries, and U.S. payees. The qualified intermediary would have to obtain certification or documentation from these persons on whose behalf the intermediary withholding certificate is provided. Generally, the certification and documentation would be the same as that which a withholding agent is required to obtain, subject to such

modifications as the intermediary's agreement with the IRS would provide. It is anticipated that the terms of the agreement would be flexible enough to accommodate the individual circumstances of a particular qualified intermediary, including any locally applicable know-your-customer rules or practices. Therefore, the agreement might acknowledge certain documentary evidence procedures already in place and not require additional documentation. Paragraph (e)(5)(ii) provides that a qualified intermediary is a foreign person that is a party to a withholding agreement with the IRS and is a clearing organization as defined in §1.163-5(c)(2)(i)(D)(8), a financial institution as defined in §1.165-12(c)(1)(iv), a partnership, or any other person acceptable within the discretion of the IRS. A qualified intermediary would be able to either assume primary responsibility for withholding and reporting to the IRS (if so permitted under its agreement with the IRS) or leave that responsibility to the withholding agent. A qualified intermediary that assumes primary withholding responsibility would present an intermediary withholding certificate to the withholding agent or another qualified intermediary representing that it will withhold all appropriate amounts and comply with all applicable reporting requirements. The withholding agent or other qualified intermediary would be allowed to rely on such a certificate and not withhold. However, the withholding agent would have to file Forms 1042 and 1042-S under section 1461 to report the payment to the qualified intermediary and the qualified intermediary's EIN. See proposed §1.1461-1(b)(2)(ii) and (c)(4)(ii).

A qualified intermediary that does not assume primary withholding responsibility would present an intermediary withholding certificate to a U.S. withholding agent or another qualified intermediary representing that beneficial owners of U.S. income payments (other than gross proceeds) are not U.S. persons and, if applicable, qualify for a reduced rate of withholding. It is anticipated that a qualified intermediary would establish separate accounts for income subject to different withholding rates. A single intermediary withholding certificate should serve as documentation for all these separate accounts. In addition, the qualified intermediary would provide a Form W-9 for each beneficial owner that is a

U.S. person to whom payments of income otherwise subject to withholding are made and for whom reporting is required under chapter 61 of the Code.

A qualified intermediary would generally have to agree to be subject to the same reporting requirements as apply to withholding agents under proposed §1.1461-1(b) and (c), to allow periodic inspection of its records, and to pay any amount of tax liability determined to be due. The IRS intends to agree to arrangements with the qualified intermediary so that, for example, inspection of records may be minimized where the IRS otherwise gets sufficient access to beneficial ownership information, through annual reporting of TIN's, review of know-your-customer rules, and selection of appropriate account information, or through an exchange of information program under a tax treaty. In appropriate cases, the IRS may rely on audits performed by an institution's approved external auditors where, for example, under an income tax treaty or local laws, the IRS would be given access to appropriate auditor's records to verify compliance. Records may include workpapers of, reports prepared by, and methodology employed by, the approved external auditors. A proposed revenue procedure providing guidance with respect to withholding agreements has been published as Announcement 96-23, 1996-18 I.R.B. 7.

Paragraph (e)(5)(v) specifies that a foreign partnership that is a qualified intermediary acting for its partners is a withholding agent with respect to its partners' distributive shares of income paid to the partnership. In that case, the partnership is subject to the same withholding and reporting procedures as would apply to a domestic partnership. Thus, any arrangement whereby the partnership would seek to shift primary withholding responsibility to the withholding agent under the provisions of paragraph (e)(5)(iv)(B) would not be recognized.

Paragraph (f) contains a set of presumptions upon which a withholding agent (for purposes of section 1441) and a payor (for purposes of the 1099 reporting provisions) would rely to determine whether to treat a person as U.S. or foreign if, at the time of payment, the withholding agent or payor does not have actual knowledge of the status of the person to whom the payment is made and lacks the required documentation or knows or has reason

to know that the documentation it holds is incorrect or unreliable. A presumption under this paragraph (f) could be rebutted by providing or correcting the required documentation to the withholding agent or payor. Thus, these presumptions would assist the payor in determining whether the income paid is subject to the 1099 reporting and backup withholding regime (if paid to a U.S. person that is not an exempt recipient) or to the section 1441 withholding regime (if paid to a foreign person).

Presumptions of foreign status resulting from the application of these provisions would, when applied for purposes of section 1441, only affect whether the withholding agent should withhold 30 percent from the payment on the ground that the payment may, under the provisions, be treated as made to a foreign beneficial owner. However, the presumptions could not operate to deem the payee as having established proof of foreign status for purposes of claiming a reduced rate of tax under the Code or an income tax treaty.

Paragraph (f)(2)(i) addresses reportable payments to a non-exempt recipient (a non-exempt recipient is a person for whom the payor must file a Form 1099; see proposed §1.6049-4(c)(1)(ii) for a list of exempt recipients). Where a withholding agent lacks the required documentation, it would presume that the payee is a U.S. individual. Accordingly, the withholding agent would withhold 31 percent under section 3406. Paragraph (f)(2)(ii) incorporates the concept of the 30-day grace period under §31.3406(d)-3(a) for a payee to furnish a Form W-9 to the payor. Because it may take longer to obtain the required documentation from a foreign person than from a U.S. person, the proposed regulations allow a withholding agent to treat a payee as a beneficial owner that is a foreign person for up to 90 days from the date the agent credits the payee's account (or until the end of the calendar year if earlier) if the withholding agent has the name and a foreign address for the account holder or a facsimile copy or an electronic transmission of the information on a withholding certificate. This special rule would defer the obligation to backup withhold under section 3406 because there are sufficient indicia of foreign status, but does not defer the obligation to withhold

under section 1441, if applicable. If the required documentation were provided or corrected within the 90-day grace period, the amount withheld may be refunded to the payee under the adjustment procedures described in proposed §1.1461-2. The 90-day grace period would be terminated if any part of the proceeds in the account that are subject to the grace period were withdrawn (other than for purposes of withholding an amount of tax). If the required documentation were not provided or corrected by the expiration of the grace period, the payee would be presumed to be a U.S. payee for purposes of section 3406 and chapter 61 of the Code from the date the account was first credited.

A special rule for joint owners or payees is provided in paragraph (f)(2)(iii) that would permit a withholding agent to presume that a payment made to joint owners or payees for whom it does not hold the required documentation is made to U.S. payees. The grace period would apply to joint payees if each payee qualified for its application. If any one of them withdrew any portion of the funds in the account, then additional withholding under paragraph (f)(2)(ii)(A) would be required.

Paragraph (f)(2)(iv) addresses reportable payments to an exempt recipient. In that case, the withholding agent could presume that the payee is a foreign person if it knew the payee's TIN and the TIN began with the two digits "98." The withholding agent also could presume that the payee is a foreign person if the payee had a foreign mailing address or the payment were made outside of the United States (as defined in proposed §1.6049-5(e)). In other cases, the withholding agent could presume that the exempt recipient is a U.S. person. Thus, for example, a U.S. withholding agent making a payment of interest on a registered obligation to a corporation with an EIN beginning with the digits "98" would not have to backup withhold under section 3406 (because the corporation is an exempt recipient). However, it should withhold a 30 percent tax under section 1442 because the condition under §1.871-14(c)(1)(iii) that a certificate of foreign status be received by the U.S. withholding agent for the interest to qualify as portfolio interest would not be satisfied. Thus, the withholding agent should treat the

interest as not qualified for the portfolio interest exemption for purposes of section 1441(b)(9). Adjustments to the tax may be made at a later time in accordance with proposed §1.1461-2 if the required documentation described in proposed §1.871-14(c)(2) is later furnished. See proposed §§1.871-14(c)(3) and 1.1441-1(f)(5) for rules addressing late received documentation.

Paragraph (f)(3) contains special presumption provisions for certain payments that are not subject to backup withholding: scholarship and pension income. In the case of scholarship and grant income, the withholding agent or payor may generally treat the payee as a U.S. person unless it has U.S. visa information in its records concerning the payee. For pension and annuities, the payment would be presumed to be made to a U.S. person if the payor had the payee's Social Security number and the payment were made either to a U.S. mailing address or to a mailing address in a foreign country with which the United States has an income tax treaty in effect that exempts residents of the country from U.S. tax on that income. In all other cases, the payor could presume that the payee is a foreign person. A withholding agent may use these presumptions as a safe harbor or may, at its option, choose to withhold at a higher rate if it were unsure of the application of the presumption in a particular case.

Paragraph (f)(4) provides special rules for pass-through entities. Paragraph (f)(4)(i) provides rules for determining whether to treat a partnership as foreign or domestic. The withholding agent or payor could presume that the partnership is a foreign partnership if the withholding agent or payor actually knows that the partnership's EIN begins with the digits "98," if the mailing address of the partnership is in a foreign country, if the payment is made outside of the United States (as defined in proposed §1.6049-5(e)), or if the withholding agent or payor knows or had reason to know that the partnership is foreign.

Under paragraph (f)(4)(ii), a withholding agent or payor that makes a reportable payment to a person determined to be a foreign partnership could presume that any partner for which it does not hold the required documentation is a U.S. individual. In that case, the payee would be treated as a U.S. payee that is not an exempt recipient

and the payment would be subject to reporting under chapter 61 of the Code and to backup withholding under section 3406.

Paragraph (f)(4)(iii) provides rules for partners' distributive shares. A domestic partnership could treat a partner as a U.S. payee if, at the time it is required to withhold on a reportable payment, it did not hold all of the required documentation for that partner. A foreign partnership that is a qualified intermediary under proposed §1.1441-1(e)(5)(ii) could treat a partner as a foreign payee if, at the time it were required to withhold on a reportable payment, it could not associate the payment with the required documentation.

Paragraph (f)(5) clarifies that a withholding agent that does not act in accordance with the presumptions and fails to withhold the required amount may be liable under section 1461 or 3403 for the tax that should have been withheld based upon the presumptions in paragraph (f), unless the withholding agent can demonstrate either that the correct amount of tax was, in fact, withheld or that the beneficial owner paid the tax due. Proof of payment of tax could be established on the basis of a Form 4669 furnished by the beneficial owner certifying the amount of tax paid to the IRS. Proof that the correct amount of tax was, in fact, withheld, could be based upon obtaining the required documentation. Late-received documentation could be accepted as proof of status and entitlement to a reduced rate of tax. However, if the delays involved in obtaining this documentation affected its reliability, the IRS could require further proof of status or entitlement to a reduced rate. Further, pursuant to section 1463 or section 3403, the withholding agent would be liable for interest under section 6601, even though, ultimately, there is no underlying tax liability. Penalties may also apply.

Under paragraph (f)(6), a reportable payment is an amount reportable under section 3406(b) (without regard to any exception to reporting under section 6041, 6041A, 6042, 6045, 6049, 6050A, or 6050N).

Paragraph (f)(7) provides that if overwithholding occurs under section 1441 as a result of application of the presumptions in paragraph (f), adjustments may be made in accordance with proposed §1.1461-2(a). Appropriate refunds and credits may be claimed under

section 1464 or 6414. Amounts overwithheld under section 3406 are subject to adjustments pursuant to §31.6413-(a)-3(a)(1).

Paragraph (g) provides that these rules are effective for payments made after December 31, 1997. However, transition rules are provided so that valid certificates (as determined under current rules) that are outstanding on the date that is 60 days after these regulations are published as final regulations may continue to be relied upon for their period of validity. In addition, dividends on publicly traded stocks are given special transition relief. See proposed §1.1441-6(b)(2).

§1.1441-2 Income subject to withholding

Paragraph (a) restates the rules in §§1.1441-1 and -3(a) of the existing regulations limiting withholding to items of income from sources within the United States. Paragraph (b) simplifies §1.1441-2(a) of the existing regulations by providing that, for purposes of chapter 3 of the Code, fixed or determinable, annual or periodical (FDAP) income is any income includable in income under section 61, subject to enumerated exceptions in paragraph (b)(2) (including certain exceptions for original issue discount and capital gains, including option premiums). Under these proposed rules, income paid under a notional principal contract would be FDAP, but see proposed §1.1441-4(a)(3) for an exemption from withholding.

Paragraph (b)(3) reflects the position adopted by the IRS in TIR-877 (December 27, 1966) and in Rev. Rul. 68-333, 1968-1 C.B. 390 that FDAP includes original issue discount paid by an original issuer of bonds or other obligations with original issue discount. However, under the authority of section 1441(c)(8), only certain items of original issue discount are currently subject to withholding of tax under Chapter 3. The lack of rules in this area in the past reflects the difficulties in determining the amount of OID upon which withholding should be applied. These proposed regulations, however, identify transactions in which information about the amount of original issue discount would generally be known or available to the withholding agent. Therefore, the proposed regulations require withholding on amounts paid upon sale by an

obligor that is related to the original issuer. In addition, amounts that fail to qualify for the portfolio interest exemption under section 871(h) or 881(c) (because, for example, the statement described in section 871(h)(5) has not been furnished to the U.S. withholding agent) would also be subject to withholding, regardless of whether it is possible for the withholding agent to determine precisely the amount of OID. See proposed §1.871-14(c)(2). If the required documentation were not furnished, the amounts could be treated as paid to a U.S. or foreign payee based upon the presumptions in proposed §1.1441-1(f). If the amounts are presumed paid to a U.S. payee, backup withholding under section 3406 might apply. See §31.3406(b)(2)-(2). If the amounts are presumed paid to a foreign payee, withholding under section 1441 would apply (unless the OID instrument had a maturity not exceeding 183 days from the date of issue).

Under these rules, the entire amount of OID (as determined on the date of issue) would have to be reported as taxable if the exact amount of OID were not known. Any amount of over-withholding may be adjusted or refunded in accordance with the procedures in proposed §1.1461-2(a) or §1.1464-1.

The proposed changes to the OID rules would be effective for OID on obligations issued after a date that is 60 days after these regulations are published as final regulations.

Paragraph (c) restates §1.1441-2(b) of the existing regulations to eliminate the reference to pre-1967 payments. It also eliminates the reference to items of income under section 402(a)(2) and 403(a)(2), relating to payments from certain employees trusts or under employee annuities, in order to conform to the amendment made to sections 1441(b) and (c)(5) by Public Law 102-318 that deleted these sections from the requirement of withholding under section 1441.

Paragraph (d) lists exemptions from withholding for certain items that otherwise constitute FDAP income. Paragraph (d)(1) lists the exceptions that are not conditioned upon furnishing documentation (e.g., interest on bearer or foreign targeted registered obligations, short-term obligations). However, documentation may be required under the 1099 reporting provisions in order to avoid reporting under

sections 6041 or 6049 and backup withholding under section 3406. Paragraph (d)(2) lists two other exceptions, but those exceptions are conditioned upon furnishing documentation described in proposed §1.871-14(c)(2). The exceptions are portfolio interest on registered obligations described in section 871(h)(2)(B) or 881(c)(2)(B) (other than foreign targeted obligations) and bank deposit interest described in section 871(i)(2)(A). Because bank deposit interest is not subject to beneficial owner documentation requirements under current rules, the regulations propose a transition rule that would allow interest paid on accounts in existence on or before a date that is 60 days after these regulations are published as final regulations to continue to be subject to current rules until December 31, 1999.

Paragraph (e) clarifies the meaning of *payment* for purposes of withholding. An amount would be considered paid when it is includable in income under the cash basis method of accounting. Under paragraph (e)(2), income reallocated under section 482 from a U.S. person to a related foreign person would be considered a payment for withholding tax purposes. A payment would also be considered to be made if income arose as a result of a secondary adjustment made after income is allocated under section 482, unless the taxpayer entered into a repatriation agreement that eliminated the liability for withholding. Paragraph (e)(3) provides that income is not considered paid if it is blocked under certain executive authority, but is considered paid on the date the blocking restriction is removed and, therefore, subject to withholding as of that date. Paragraph (e)(4) provides special payment rules for dividends. These rules are similar to those in effect for purposes of backup withholding. See §31.3406(b)(2)-4. Paragraph (e)(5) coordinates the payment election for branch interest tax under §1.884-4(c)(1) with section 6049 and the withholding provisions under section 1441.

§1.1441-3 Amounts subject to withholding

Paragraph (a) restates the rule in §1.1441-2(a)(1) of the existing regulations that withholding is generally imposed on the gross amount of income. Paragraph (b) provides for special withholding rules for interest. Paragraph (b)(1) restates the rule in

§1.1441-3(c)(3) of the existing regulations that requires withholding on the entire amount of stated interest owed on an interest-bearing obligation, regardless of the character of the amounts paid. The heading is modified to eliminate any inference that this rule is limited to payments on defaulted interest coupons. Paragraph (b)(2) restates the exemption from withholding in §1.1441-4(h) of the existing regulations regarding sales of obligations between interest payment dates. An anti-abuse rule is added that would require withholding where the withholding agent knew or had reason to know that the sale transaction was part of a plan the principal purpose of which was to avoid withholding through a pattern of sales and repurchases.

Paragraph (c) provides rules relating to corporate distributions and substantially relieves the withholding burden imposed under §1.1441-3(b) of the existing regulations on these distributions. Under the proposed regulations, a corporation could determine the amount of a distribution subject to withholding based on a reasonable estimate of available earnings and profits for the taxable year. A corporation that made a reasonable estimate, but nonetheless underwithheld, would remain liable for the amount of tax underwithheld (and interest), but not penalties. These proposed regulations adopt the same “reasonable estimate” standard as is provided under §31.3406(b)(2)-4(c)(2). Under paragraph (c)(2)(ii), an intermediary could rely on a reasonable estimate represented by the distributing corporation. The distributing corporation would be made liable for any amount of underwithholding where the withholding agent had relied on the representation and the estimate had not been reasonably determined.

Paragraph (c)(3) proposes special procedures for withholding on certain distributions made by a Regulated Investment Company (RIC). In order to determine whether a withholding obligation arises in that case, a RIC would benefit from the same exceptions that would apply to other corporations for distributions payable in stock or stock rights or distributions treated in part or in full as in exchange for stock. In addition, the proposed regulations provide that no withholding is required for a distribution that is a capital gain dividend defined in section 852(b)-

(3)(C) or an exempt interest dividend defined in section 852(b)(5)(A). Special procedures are proposed for implementing these exemptions, however, because a RIC must specifically designate the extent to which a distribution falls under one of these provisions. Under applicable rules, the designation may be made as late as 60 days after the close of the RIC's taxable year, and after making the designation, the RIC may find that the amount so designated exceeds what the Code and the regulations allow. This presents special difficulties under section 1441, which assumes that the amounts subject to withholding are fixed at the time they are paid.

To address these special difficulties, paragraph (c)(3) would allow a RIC to designate interim distributions as being subject to section 852(b)(3)(C) or 852(b)(5)(A). If it later determined that the designation was in excess of what was permitted and, as a result, had underwithheld, the RIC would have to satisfy the tax liability and could adjust the withholding pursuant to proposed §1.1461-2(b). A RIC would not be subject to penalties for failure to withhold timely, provided the designation was based upon a reasonable estimate when made. However, interest would apply under section 6601. In addition, the RIC might be liable for penalties if the IRS determined that the estimates were not reasonably determined.

Paragraph (d) restates, without significant changes, the rule in §1.1441-3(d) of the existing regulations regarding withholding on the full amount realized from the sale of property where the withholding agent does not know the amount of gain subject to withholding. A withholding agent may, however, determine gain based on the beneficial owner's withholding certificate if it indicates the beneficial owner's basis in the property sold. This rule is of limited application as most capital gains are exempt from withholding under section 1441.

Paragraph (e) restates the rule in §1.1441-7(c) of the existing regulations pertaining to payments in kind. The property conversion requirement under current rules would be made optional. Instead, the withholding agent could choose to obtain payment from another source. The regulations further propose to clarify that the amount of a payment in kind is measured by the fair market

value of the property transferred or of the services provided. Payments made in foreign currency require a conversion of the amount of tax using the spot rate (as defined in §1.988-1(d)(1)) or a reasonable spot rate convention. Paragraph (e)(3) provides guidance where the withholding agent's satisfaction of the beneficial owner's tax liability constitutes additional income to the beneficial owner that is subject to withholding. In that case, the final withholding tax liability would be calculated under a gross-up formula.

The provisions currently stated under §1.1441-3(j), relating to conduit financing arrangements, are proposed to be incorporated without change into a new paragraph (f). These provisions are not repropoed.

The address rule in §1.1441-3(b)(3) of the existing regulations would be eliminated and replaced by requirements to furnish appropriate documentation or to establish foreign status and, if applicable, residence in a treaty country. See proposed §1.1441-1(e) and 1.1441-6. Section §1.1441-3(c)(1) requiring withholding in the case of interest paid on obligations issued by the U.S. government would be deleted as unnecessary given the provisions in §1.1441-2(a) describing income subject to withholding. Section §1.1441-3(c)(4) addressing unknown owners would also be deleted because the presumption provisions in §1.1441-1(f) provide guidance. The special rules for tax-free covenant bonds issued prior to 1934 are proposed to be deleted. Comments are solicited as to whether these rules are still necessary.

§1.1441-4 Certain exemptions from withholding

Paragraph (a)(1) restates, without significant change, the provisions in §1.1441-4(a) of the existing regulations regarding the exemption from withholding for certain income effectively connected with the conduct of a trade or business within the United States. The regulations clarify that the exemption under this section does not apply to claim an exemption under an income tax treaty (*i.e.*, income not attributable to a permanent establishment). Claims of treaty benefit must be made under the procedures described in proposed §1.1441-6.

Under paragraph (a)(2)(i), a withholding agent could rely on a claim

that income is effectively connected with the conduct of a trade or business within the United States if it held a withholding certificate so stating. The regulations do not permit a withholding agent to rely on a qualified intermediary withholding certificate to grant a reduced rate of withholding for income claimed to be effectively connected, except in the case of a qualified intermediary that is a partnership acting for its own account. A partnership that does not claim to be a qualified intermediary could also furnish an intermediary withholding certificate described in proposed §1.1441-1(e)(3)(iii) (*i.e.*, the transmittal certificate normally required from a partnership transmitting its partners' documentation under the procedures described in proposed §1.1441-5(b)). For purposes of claiming an effectively connected income exemption, it would not be necessary to attach the partners' documentation to the certificate since the exemption is available regardless of the status of the partners and, under section 1446, the partnership is required to withhold. The validity period of a withholding certificate used to claim an effectively connected exemption is proposed to be extended from one year to three years (subject to amendment if a change in circumstances affected the character of the income that the beneficial owner anticipated would be effectively connected). This rule should significantly ease the burden on continuing transactions that generate effectively connected income every year.

The regulations propose to eliminate the requirement that the certificate be attached to the Form 1042-S; the withholding agent would be required to state the beneficial owner's TIN on the Form 1042-S. See proposed §1.1461-1(c)(1)(i). If the withholding certificate were silent as to whether the income is effectively connected or if the required documentation were lacking, incorrect, or unreliable, the withholding agent should presume that the income is not effectively connected.

The rules provided in §1.1441-4(f) of the existing regulations are proposed to be restated in a new paragraph (a)(2)(ii) and are not repropoed. Paragraph (a)(2)(iii) provides for special rules for payments made to joint owners that would require each joint owner to provide a withholding certificate certifying that the income is effectively connected with a trade or

business in the United States. These rules are consistent with the joint owners rules provided under the section 3406 regulation. See §31.3406(h)-2(a).

Paragraph (a)(3) provides that no withholding is required on income from notional principal contracts regardless of whether a withholding certificate is provided. However, such income would have to be reported on a Form 1042 and 1042-S. This rule would significantly simplify the paper flows currently associated with these transactions.

Paragraph (a)(4) parallels the rule in proposed §1.1441-1(f)(5) regarding the consequences of acting in a manner contrary to prescribed presumptions. Late received documentation could relieve the withholding agent from the tax liability. However, an interest charge would apply under section 6601 on the amount that should have been withheld even if, ultimately, there is no underlying tax liability. In addition, penalties might apply.

Paragraph (b) of the existing regulations concerning compensation for personal services of an individual is substantially unchanged. A new paragraph (b)(1)(ii) is added to require that withholding on distributions from certain qualified pension plans and annuities occur under section 1441 rather than under section 3405 as was required under §1.1441-4T(b)(ii) (which expired on February, 1993). A new paragraph (b)(1)(vi) is also added that would allow employers to wage withhold on compensation that is otherwise exempt from wage withholding by reason of section 3402(e). This rule provides relief for employers of non-resident alien individuals who derive income from sources partly within and partly without the United States on a regular basis (e.g., crew members working on cruise ships). Without this rule, employers would have to withhold at the 30 percent rate instead of the lower wage withholding rate.

The provisions under paragraph (b)(2) of the existing regulations (dealing with a claim of reduced rate of withholding on personal service income under an income tax treaty) are unchanged with one exception. The 10-day review rule in paragraphs (b)(2)(i) and (iv) would be extended to 20 days. This extension is necessary because of the increase in the number of Forms 8233 that the IRS receives.

Paragraph (b)(6) is added to eliminate the requirement in §1.1441-3(e) of

the existing regulations to pro-rate the personal exemption based on the period during which a nonresident alien individual is present in the United States during the taxable year. Therefore, the entire personal exemption amount could be taken into account to determine the base amount on which to withhold.

Paragraph (c) incorporates the provisions in §1.1441-2(c) of the existing regulations dealing with participants in certain exchange or training programs and provides additional guidance with respect to payments of scholarship or fellowship grants to nonresident alien individuals. It reflects 1988 and 1994 statutory amendments to section 1441 concerning certain visa holders. Such income is subject to a lower withholding rate of 14 percent under section 871(c). The regulations propose an alternate withholding election so that taxpayers may choose to be subject to the withholding rates applicable to wages, which in many cases are likely to result in a lower rate. Also, individuals who receive both scholarship or grants and compensation income from the same withholding agent could choose to combine all income on Form 8233 to claim a reduced rate under a tax treaty for both types of income.

Paragraphs (d) (dealing with annuities) and (e) (dealing with central banks of issue and the Bank of International Settlement) merely reflect conforming changes regarding the proposed documentation requirements.

§1.1441-5 Withholding on payments to pass-through entities

The existing regulations in §1.1441-5 address claims of U.S. status. These provisions are restated, with modifications, in proposed §1.1441-1(d).

This section, as revised, would provide special withholding procedures for payments to partnerships. Paragraph (a) deals with domestic partnerships. As under current regulations, payments to domestic partnerships would not require withholding, even if the partners were foreign persons. A domestic partnership is the withholding agent for items of income included in the distributive share of a partner that is a foreign person. Paragraph (b) proposes to modify the current rules for payments to foreign partnerships to permit a look-through approach, so that claims of reduced rate could be presented by

the partnership on behalf of the partners (including partners that are U.S. persons). The look-through approach would apply through tiers of foreign partnerships. In the alternative, a foreign partnership could, under an agreement with the IRS, become a qualified intermediary so that the partners' documentation would not have to be furnished to the withholding agent. See proposed §1.1441-1(e)(5) for rules applicable to qualified intermediaries. Paragraph (b)(2) clarifies how the look-through approach would operate in the case of a tiered partnership. Generally, the partnership would have to look through tiers until it reached the beneficial owner (as determined under proposed §1.1441-1(c)(6)). However, it could stop at any level in the chain that constitutes a payee (as defined in proposed §1.1441-1(c)(3)).

§1.1441-6 Claim of a reduced rate under an income tax treaty

The proposed regulations eliminate the "address" rule in §1.1441-6(c)(1) of the existing regulations and in regulations under several income tax treaties, which permits a withholding agent to grant a reduced rate of tax under a treaty based upon the address of the payee (including a nominee). Paragraph (b)(1) provides general procedures for reliance by a withholding agent on a claim for a reduced rate of withholding under a treaty based upon the documentation requirements described in proposed §1.1441-1(e)(1)(i). A withholding agent could rely upon a beneficial owner withholding certificate described in proposed §1.1441-1(e)(2) as establishing both foreign status and residence in the treaty country provided a TIN is stated on the certificate. In addition, in the case of dividends with respect to which an advance ruling is required in order to secure the reduced rate of tax under the tax treaty, the withholding certificate would have to state that the beneficial owner has obtained such a ruling. Such rulings are currently required under a very limited number of tax treaties: Austria, Denmark, Ireland, and Switzerland. See paragraph (e) regarding the procedures for obtaining such a ruling. Further, for amounts exceeding \$500,000 in the aggregate for the taxable year paid to a beneficial owner related to the withholding agent, the beneficial owner would have to indicate on the certificate that it will file a Form 8833 under

section 6114. The regulations under section 6114 are proposed to be modified accordingly. Claims of treaty benefit could also be made on the basis of an intermediary withholding certificate described in proposed §1.1441-1(e)(3). Further, a U.S. withholding agent could act through an authorized foreign agent described in proposed §1.1441-7(c)(2).

Paragraph (b)(2) provides special rules for certain dividends paid on stock that is traded on a U.S. established market. For these dividends, the withholding agent could grant treaty benefits based upon the same documentation procedures as are proposed to apply to portfolio interest on registered obligations (*e.g.*, no TIN is required on a beneficial owner withholding certificate). See proposed §1.871-14(c)(2). Paragraph (b)(3) provides that the competent authorities may agree to different certification procedures under an applicable tax treaty.

Paragraph (b)(4) clarifies the manner in which beneficial owners could claim benefits under a tax treaty where foreign law principles apply to identify the beneficial owner of a payment made to a foreign entity. Under proposed §1.1441-1(c)(6)(ii)(B), the beneficial owner would be determined based upon the laws of the country whose tax treaty with the United States is invoked to claim a reduced rate of tax.

These procedures are intended to apply in a reciprocal manner. Therefore, paragraph (b)(4)(iv) provides that, if the IRS determined that a treaty partner is not identifying beneficial owners in a similar manner and, as a result, denies benefits under an otherwise applicable treaty to an entity organized in the United States or to interest holders residing in the United States, the benefits of these procedures could be suspended for entities organized, or interest holders residing, in that country until the competent authorities reached a reciprocal agreement on the application of treaty benefits in such cases. Suspension of benefits under this provision would be effective on a prospective basis only.

Paragraph (c) states the rules regarding certification of a TIN by the IRS. These procedures would apply to payments for which a Form W-8 is furnished with a TIN. They are directed to beneficial owners (or their agents) and are designed to ensure that the IRS

can verify the beneficial owner's status as a resident of a treaty country based upon the information return later filed by the withholding agent on Form 1042-S. If the IRS determined that the TIN does not support the beneficial owner's claim of residence in the treaty country, it would so notify the withholding agent. The IRS could waive the requirement that a taxpayer certify its TIN with the IRS when it implements procedures to verify a taxpayer's status directly with a foreign competent authority. The IRS could also certify a TIN based upon representations made by a qualified intermediary.

The IRS would certify a TIN based upon a certificate of residence or documentary evidence. Paragraph (c)(3) describes a certificate of residence as a certificate issued by the tax authorities of the treaty country certifying that the taxpayer files income tax returns as a resident of that country and is current on his filing obligations. Paragraph (c)(4) describes documentary evidence as a document that is no more than three-years old and sufficiently identifies the person and the residence of that person in the treaty country.

Paragraph (e) incorporates the provisions in existing regulations that condition the benefit of the reduced five-percent rate on related party dividends to an advance ruling from the IRS determining that the parent-subsidiary relationship is not established or maintained with the principal purpose to secure the reduced rate. The ruling would be required only if so required under an applicable treaty. It must be requested prior to the payment of the dividend. While a request made after payment would not disqualify the dividend from the benefit of the reduced rate if a favorable ruling is later obtained, the withholding agent would nevertheless withhold. Failure to do so would subject the withholding agent to an interest charge under section 6601. Also, the withholding agent would be liable for the tax and related penalties if a favorable ruling were not issued. See proposed §1.1441-1(f)(5) regarding the consequences to the withholding agent when it does not withhold the full amount even though it does not hold the required documentation prior to payment.

The regulations are proposed to be effective for payments made after December 31, 1997. However, certificates issued on or before the date that

is 60 days after these regulations are published as final regulations will continue to be valid until they expire, based upon existing regulations. In addition, because no documentation is currently required for dividends, the regulations propose a transition rule that would allow dividends paid on publicly-traded stock to accounts in existence on or before a date that is 60 days after these regulations are published as final regulations to continue to be subject to the current address rule until December 31, 1999.

§1.1441-7 General provisions relating to withholding agents.

This section modifies §1.1441-7 of the existing regulations dealing with withholding agents. Paragraph (a) clarifies that a withholding agent is any person that has the control, receipt, custody, disposal, or payment of an item of income and not merely a person that pays or causes an amount to be paid. If there are several withholding agents with respect to one payment, only one tax should be withheld and only one return should be filed.

Paragraph (b) restates the "actual knowledge or reason to know" standards applicable to a withholding agent as in effect under current law. The IRS and Treasury are aware that the application of a "reason to know" standard without limitation may be impractical in the case of financial institutions handling large volumes of transactions for many customers. Therefore, the regulations propose to limit the due diligence expected from withholding agents paying portfolio interest, deposit interest, or dividends on publicly traded stock. Under paragraph (b)(2)(ii), a withholding agent's due diligence regarding a beneficial owner certificate would be limited to examining the address stated on the certificate. If this information indicated that the beneficial owner might be a U.S. taxpayer or conflicted with information that the withholding agent otherwise had in its records for that account, the withholding agent would have to obtain specified documentation to verify the beneficial owner's claim of foreign status or residence. Paragraph (b)(3) proposes to incorporate rules consistent with those under section 3406 dealing with universal accounts. Therefore, if the withholding agent used a system of universal accounts, it would be required to use

that system to determine the scope of its due diligence under the regulations.

Paragraph (c) restates and expands the provisions in §1.1441-7(b) of the existing regulations pertaining to authorized agents and adds provisions regarding an authorized foreign agent. This new concept is intended to facilitate compliance by U.S. withholding agents that make payments through their agent abroad. By imputing the acts of a foreign agent to a U.S. withholding agent, the required documentation could remain with the foreign agent and would not have to be provided to the U.S. withholding agent. However, the regulations require that the agent be “authorized” in order to insure that the IRS can verify the foreign agent’s compliance with the withholding procedures, which, in turn, would determine whether the U.S. withholding agent has itself complied. See proposed §1.1461-1(b)(2)(iii) and (c)(4)(iii) regarding corresponding filing requirements.

Section §1.1441-7(b)(3) of the existing regulations is proposed to be deleted, pending comments on the continuing necessity of providing guidance on tax-free covenant bonds.

Paragraph (d) restates without changes the provisions in §1.1441-7(a)(2) of the existing regulations dealing with the United States as a withholding agent. Paragraph (e) restates without changes the provisions in §1.1441-3(c)(2) of the existing regulations dealing with assumed obligations. Section §1.1441-7(c) of existing regulations dealing with payments other than money would be deleted and restated in proposed §1.1441-3(f) dealing with withholding procedures for payments in kind.

§1.1441-8T Foreign government and international organization exemption from withholding

This section exempts from withholding certain types of income excluded from gross income under section 892 that are paid to foreign governments and international organizations. Revisions are proposed to paragraph (b) of the existing regulations to conform the certification procedures to the proposed withholding certificate procedures described in proposed §1.1441-1(e)(1)(i). Therefore, Form 8709 would be replaced by the standard withholding certificate (Form W-8), meaning that

foreign governments and international organizations would be relieved from the requirement to furnish annual certification. A foreign government or an international organization would not be required to furnish a tax identifying number. However, if it did, the certificate would be valid indefinitely for income required to be reported on Form 1042 or for which the withholding agent reports the TIN to the IRS. See proposed §1.1441-1(e)(4)(ii).

§1.1441-9 Exemption from withholding on exempt income of foreign tax-exempt corporations and foreign private foundations

This new section provides that income paid to a foreign organization described in section 501(c) would not be subject to withholding under section 1442 if the income were not subject to tax as unrelated business income under section 511 and the entity were exempt from tax under section 501(a). For purposes of granting a reduced rate, a withholding agent could rely on a withholding certificate satisfying the requirements of proposed §1.1441-1(e)-(1). A beneficial owner certificate must include a taxpayer identifying number and must certify that it will not be subject to tax under section 511, and that the IRS has issued a determination letter. In the absence of such a letter, the beneficial owner should provide an opinion of counsel stating that the organization meets the conditions for a tax exemption under section 501(c). Since the affidavit requirement for foreign foundations is proposed to be eliminated, foreign tax-exempt organizations would be subject to the same documentation requirements as would apply to foreign foundations under proposed §1.1443-1(b).

§1.1461-1 Deposit and return of tax withheld

The provisions in §1.1461-1 of the existing regulations pertaining to ownership certificates for bond interest are proposed to be deleted. Interest on bonds described in this section would be subject to the regular procedures provided in the regulations under sections 1441 and 1443. The special rules would no longer be necessary in view of the substitute procedures provided in the proposed regulations. Comments are solicited as to the continuing need for provisions governing tax-free covenant bonds.

Section 1.1461-1 contains proposed procedures for withholding agents to pay the withheld tax and file the annual income tax return and information returns with respect to payments of income subject to section 1441 withholding. Paragraph (a) restates §1.1461-3 of the existing regulations regarding the payment of amounts withheld. The provisions regarding pre-1973 years are proposed to be deleted as obsolete. Paragraph (b) revises §1.1461-2(b) of the existing regulations on the filing of returns of amounts withheld. Paragraph (b)(1) clarifies that the Form 1042 must include the total amount of income paid during the preceding calendar year. Also, the filing date is changed from March 15 to February 28 in order to conform with the filing dates for Form 1099. The proposed regulations would eliminate the requirement to attach the Forms 1042-S to the return. Instead, the Forms 1042-S would have to be filed separately with a transmittal form. See paragraph (c)(1)(i).

Paragraph (b)(2) describes applicable return requirements for multiple withholding agents. Generally, as under current rules, only one Form 1042 would have to be filed for an item of income. Exceptions to this general rule are provided for payments to qualified intermediaries where the U.S. withholding agent would have to file a return, regardless of whether the qualified intermediary assumed primary withholding responsibility for the payment and regardless of whether the qualified intermediary were also required to file a return under its agreement with the IRS. Another exception would be provided for payments to an authorized foreign agent. In that case, the U.S. withholding agent and the authorized foreign agent would each be required to make a return. The return of the withholding agent would report amounts paid to the authorized foreign agent. The return of the authorized foreign agent would report amounts paid to the beneficial owner or its intermediaries.

Paragraph (b)(3) requires that changes to the originally filed Form 1042 be filed on an amended return on a new Form 1042X. This change is designed to facilitate the processing of returns by the IRS and would be consistent with the procedures for filing other amended returns.

Paragraph (c) revises the provisions in §1.1461-2(c) of the existing regula-

tions regarding the filing of information returns on Form 1042-S. As under existing regulations, any income subject to withholding must be reported on an information return on Form 1042-S and a return would be due irrespective of the fact that no tax was withheld (e.g., the beneficial owner claimed an exemption or the withholding agent failed to withhold).

The provisions of §1.1461-2(c)(3) of the existing regulations requiring that the name of the beneficial owner be reported on Form 1042-S would be retained. However, more detailed guidance is provided regarding reporting of income paid to intermediaries. See paragraph (c)(4) below dealing with multiple agents. The proposed regulations eliminate as unnecessary the requirements under existing regulations to attach any certificate, form, or statement to the return.

Paragraph (c)(1)(ii) proposes new rules pertaining to joint owners. A single Form 1042-S may be provided to one of the joint owners. In that case, the withholding agent should provide the Form 1042-S to the joint owner whose status determines the tax withheld. Further, any one owner may request a separate Form 1042-S, but the total amounts of income and tax reported paid and withheld on all the forms 1042-S may not exceed the total amount of income actually paid and tax actually withheld.

Paragraph (c)(2) replaces §1.1461-2(c)(1) of the existing regulations and states that the items of income that are subject to reporting on Form 1042-S are those items of income subject to withholding, income from a notional principal contract, and amounts described in sections 6041 through 6050P that are paid to a foreign person and are not exempt from reporting under those sections or the corresponding regulations. This provision is intended to standardize reports of payments to foreign persons to the IRS and should simplify compliance by withholding agents. Paragraph (c)(2)(ii) lists the exceptions to reporting on a Form 1042-S. As under current regulations, items of income exempt from reporting include portfolio interest on a bearer obligation and original issue discount on short-term obligations. An explicit exception for reporting on deposits described in section 871(i)(2)(A) would be added. However, bank deposit interest that is subject to withholding under

section 1441 (because, for example, documentation was not furnished but payments were made to a foreign address; see special grace period provisions under proposed §1.1441-1(f)(2)-(i)(B)) would have to be reported. Also, interest on bank deposit interest paid to Canadian residents would have to be reported based upon provisions under final regulations under section 6049 published in the Rules and Regulations section of this issue of the Bulletin. In addition to the items excepted from reporting under existing §1.1461-1(c)(1), other items are added that prevent duplicative reporting. Finally, the proposed regulations would clarify that to the extent group-term life insurance and other items of income required to be reported pursuant to the provisions in §§1.6041-2 and 1.6052-1 can be associated with wages required to be reported on a Form W-2, then such items may also be reported on a Form W-2 instead of a Form 1042-S.

Paragraph (c)(3) restates the provisions of §1.1461-2(c)(2) of the existing regulations regarding the types of information to be included on Form 1042-S. It clarifies that the information could be based on the information furnished by or on behalf of the beneficial owner, as corrected based on the withholding agent's actual knowledge if necessary. In addition, the Form 1042-S would have to include the TIN of the beneficial owner if required to be shown on the withholding certificate. Also, a beneficial owner's TIN that the beneficial owner is not required to furnish but which is actually known to the withholding agent would have to be reported on Form 1042-S.

Paragraph (c)(4) is added to provide rules for filing Form 1042-S where there are multiple withholding agents. Generally, as with the Form 1042, only one Form 1042-S must be filed with respect to an item of income. Current rules requiring the withholding agent to identify the beneficial owners of payments made to agents, nominees, or representatives, if known, would be eliminated for payments to an intermediary that either claims to be a qualified intermediary or is an authorized foreign agent. In all other cases, the information on a Form 1042-S must be reported for each beneficial owner. This would modify §1.1461-2(c)(3)(i) of the existing regulations providing that beneficial owner information be reported only if known. For

payments made to a person claiming to be a qualified intermediary or is an authorized foreign agent, each withholding agent in the chain would be permitted to report on one Form 1042-S reflecting the payment made to the next qualified intermediary or authorized foreign agent in the chain. In the case of a payment to an authorized foreign agent, however, the withholding agent would be excused from the requirement to report the beneficial owner information only to the extent that the authorized foreign agent actually complies with the filing requirements under paragraph (c)(4)(iv).

Paragraph (c)(5) is added to cross-reference the magnetic media filing requirements applicable to Forms 1042-S under §1.6011-1(c). Generally, a filer of 250 or more Forms 1042-S must file on magnetic media, unless a waiver is granted.

Paragraph (d) would allow a withholding agent to provide a list of taxpayer identifying numbers furnished by or on behalf of beneficial owners to the extent the agent has relied upon such number to grant a reduced rate of withholding tax. This is a special filing procedure under which the reporting of the associated amount of income would not be have to be reported.

Finally, paragraph (e) clarifies the provisions regarding indemnification of withholding agents. Section 1461 indemnifies a withholding agent from the claim of any person for the amount of any payments made in accordance with the provisions of chapter 3 of the Code. Some commentators and withholding agents have expressed concerns that section 1461 could be interpreted to limit indemnification to amounts that were required to be withheld. The proposed regulations clarify that a withholding agent that withheld based upon a reasonable belief that such amount was withheld in accordance with chapter 3 of the Code would be treated for purposes of section 1461 as having withheld in accordance with chapter 3 (even though it is later determined that the withholding agent's application of the rules was incorrect). Additionally, a withholding agent would be indemnified against any claim of any person for the amount of any withholding made in accordance with the grace period provisions under proposed §1.1441-1(f)(2)(ii).

Paragraph (f) restates without changes §1.1461-2(f) of the existing

regulations dealing with amounts that may not constitute gross income, in whole or in part. This rule would apply to amounts subject to withholding under proposed §§1.1441-3(b)(1) or 1.1441-3(d).

Paragraph (g) is added to provide guidance on requests of extensions of time to file Form 1042, Forms 1042-S, and to furnish Forms 1042-S to recipients. The rules with respect to such requests would parallel those under section 6081. A change would be made, however, to the form to be used for making a request for an extension of time to file Forms 1042-S. Currently, these requests are made on Form 2758; the proposed regulations require such a request to be made on Form 8809.

§1.1461-2 Adjustments for overwithholding and underwithholding of tax

This section has also been renumbered and, although the rules are the same as those of the current regulations in §1.1461-4, it has been redrafted to simplify the language and to update the examples. Specifically, the rule for reimbursements remains the same, but the rule in proposed §1.1461-4(b) with respect to the adjustment of tax payments or deposits is now titled “set-offs,” which more accurately describes the adjustment process.

§1.1462-1 Withheld tax as credit to recipient of income

Section 1.1462-1(a) is clarified by stating that the amount of income from which the tax is required to be withheld includes the amount calculated under the gross-up formula in proposed §1.1441-3(e)(3).

§1.1463-1 Tax paid by recipient of income

This section provides that if the income tax for which the beneficial owner and the withholding agent have joint liability under section 1461 has been paid by either one of them, the IRS may not collect from the other, regardless of the original liability for the tax. This section has been changed to reflect the 1989 statutory amendment (Public Law 101, 239, Sec. 7743(a)) that provides for the imposition of interest and penalties on the party that fails to withhold.

Prior proposed regulations under section 871 and chapter 3 of the Code

In 1976, proposed regulations were published relating primarily to withholding and original issue discount. In 1984, proposed regulations were published relating primarily to claims of benefits under income tax treaties. These proposed regulations were contained in project number LR-2043, published on July 12, 1976 (41 FR 28517) and project number LR-271-83, published on September 10, 1984 (49 FR 35511). Both proposed regulations are being withdrawn on April 22, 1996.

Regulations under sections 6041, 6041A, 6042, 6045, 6049, and 6050N

These proposed regulations provide exceptions from information reporting and backup withholding under sections 3406, 6041, 6041A, 6042, 6045, 6049, and 6050N for payments to foreign beneficial owners and for income paid by certain foreign payors or middlemen.

Generally the regulations clarify and simplify the regulations under sections 3406, 6041, 6042, 6045, and 6049 that were proposed on February 29, 1988, at 53 FR 5991 (1988) (the 1988 proposed regulations). In addition, the regulations under these sections are proposed to be revised. The regulations also would add new exceptions from reporting (including the addition of middleman rules) to sections 6041, 6041A, and 6050N. These proposed revisions and new exceptions from reporting parallel the exceptions under these proposed regulations under sections 6042 and 6049. Further, parallel provisions are found in each section for: definitions of terms (such as non-U.S. payor or non-U.S. middleman); presumptions as to whether a payee is U.S. or foreign where the required documentation is lacking, incorrect, or unreliable; rules for payments to joint owners; and rules for converting into U.S. dollars amounts paid in foreign currency. In addition, the proposed regulations specify that the standard of knowledge applicable to payors and middlemen would be actual knowledge. Thus, the “reason to know” standard would not apply for purposes of the reporting provisions.

The subparagraphs under proposed §1.6042-3(a) (dealing with the defini-

tion of dividends for purposes of information reporting under that section) are proposed to be restated with changes in drafting only. The substantive rules in that paragraph would be unchanged and are, therefore, not re-proposed. Also, §1.6042-3(b)(3) and (4) of the 1988 proposed regulations (relating to capital gain dividends from regulated investment companies and payments to exempt recipients) would be redesignated as subparagraphs (vii) and (viii), respectively, of proposed §1.6042-3(b)(1). These rules are not re-proposed.

This document also proposes to revise the definition of an exempt recipient in the case of a corporation. Section §1.6049-4(c)(1)(ii)(A) of the 1988 proposed regulations provides that a person would be treated as a corporation, and therefore as an exempt recipient not subject to information reporting, if the name of the payee or a corporate resolution provided to the payor clearly indicates corporate status (the eyeball test). These proposed regulations retain the eyeball test of the 1988 proposed regulations for payments (i) other than interest, dividends and broker proceeds paid to accounts established after a date that is 60 days after the date that these regulations are published as final regulations in the Federal Register and (2) other than interest, dividends and broker proceeds that are not paid to a person to whom the payor has an account relationship. For interest and dividends paid to a new account, the entity would be required to provide either a corporate resolution or similar document that clearly indicates corporate status, a Form W-9 with an EIN, or a Form W-8. For interest and dividends paid where an account relationship does not exist, the payor may continue to rely on the eyeball test if the payor also has a mailing address of the payee in the United States. The IRS and Treasury understand that financial institutions routinely request a corporate resolution when opening accounts for entities. Therefore, requiring such a document would not significantly increase burden and would improve compliance. This proposed rule is reflected in paragraph (c)(1)(ii)(A). In addition, the list of international organizations under paragraph (c)(1)(ii)(G) is proposed to be eliminated as a simplification measure.

In addition, the 1988 proposed regulations under §1.6049-5 are proposed

to be substantially redrafted, although without significant substantive changes. Paragraph (b)(6) provides an exception from reporting for amounts from sources outside the United States paid outside the United States by a non-U.S. payor or non-U.S. middleman. This provision duplicates that found in the 1988 proposed regulations at proposed §§1.6049-5(b)(8) and 1.6049-5(d)(3)-(i), (ii), and the foreign source portion of proposed §1.6049-5(d)(3)(iii).

Paragraph (b)(7) (which corresponds to §1.6049-5(c)(6) of the 1988 proposed regulations) would except portfolio interest paid on bearer obligations if paid outside the United States. In these proposed regulations, this exception would not apply where a U.S. middleman acts as a custodian, nominee, or other agent of the payee and collects the amount for, or on behalf of, the payee, whether or not the middleman is also acting as agent of the payor. Paragraph (b)(8) (which corresponds to §1.6049-5(c)(6) of the 1988 proposed regulations) provides an exception for portfolio interest paid on registered obligations.

The provisions of §1.6049-5(b)(9) of the 1988 proposed regulations, which excepted from reporting amounts paid by an international organization (or its agent) on an obligation issued by the international organization are proposed to be incorporated in paragraph (b)(9) of these new proposed regulations. These rules are not reposed.

Paragraph (b)(10) (which corresponds to §1.6049-5(c)(5)(ii) of the 1988 proposed regulations) provides an exception for certain short-term foreign targeted obligations. Paragraph (b)(11) (which corresponds to §1.6049-5(e)(1) (the parenthetical language) and §1.6049-5(e)(2)(i) and (ii) of the proposed 1988 proposed regulations) provides an exception for certain foreign-targeted obligations issued by persons engaged in the banking business. Although the 1988 proposed regulations limited the exceptions at §1.6049-5(e)(2)(i) and (ii) to Canadians, these proposed regulations expand the scope of the exceptions to apply to all beneficial owners. However, as under the 1988 proposed regulations, the exception would not apply where a U.S. middleman acts as an agent of the payee.

Paragraph (b)(12) (which corresponds to §§1.6049-5(b)(7) and (c)(1), (2), and (3) of the 1988 proposed

regulations) would except any amount of U.S. source interest subject to withholding under section 1441. Such interest would be required to be reported on a Form 1042-S under proposed §1.1461-1(c). This exception would replace §1.6049-5(b)(1)(vi), (b)(1)(vi)(B)(1) and (b)(2)(iv) of the existing regulations, which provide an exception for reporting for bank deposit interest paid to a foreign person, but only if a Form W-8 (or documentary evidence in appropriate cases) is provided to the payor. The withholding certificate requirement for bank deposit interest is now found at proposed §1.1441-2(d)(2).

Paragraph (b)(13) provides a new exception for assets blocked pursuant to an executive order.

Paragraph (b)(14) provides the general rule for exempting any other amount of otherwise reportable interest based on specified documentation furnished to the payor or middleman. The standards of documentation are described in paragraph (c) and would generally parallel the documentation standards proposed for purposes of claiming a reduced rate of withholding under section 1441. Therefore, the payor could rely on a beneficial owner or intermediary withholding certificate described in proposed §1.1441-1(e)(1)-(i) provided it complied with the procedures described in proposed §1.1441-1(e)(4)(iv) and (v) (dealing with on-line confirmation and notification procedures). No taxpayer identifying number is required to be stated on a beneficial owner withholding certificate. These proposed regulations retain the permission under current regulations to furnish documentary evidence instead of a certificate for payments made to an off-shore account. The on-shore and off-shore distinction is similar to that found in the 1988 proposed regulations. The provisions of the 1988 proposed regulations contained in paragraphs (d), (e), (f), (g), (h), (i), and (l) are withdrawn. Proposed paragraphs (j) (relating to payments outside the United States) and (k) (dealing with original issue discount) of the 1988 proposed regulations would be renumbered as paragraphs (e) and (f), respectively. The provisions in these paragraphs are not restated.

§31.3401(a)(6)-1(e) Income exempt from income tax

This section is amended to reflect the new certification procedures under proposed §§1.1441-1(e).

Backup withholding regulations under section 3406

Several changes to the backup withholding regulations under section 3406 are proposed to conform those regulations to the proposed information reporting and chapter 3 withholding regulations. Section 31.3406(d)-3 (c) would be amended to extend to 90 days the current 30-day grace period applicable to readily tradeable instruments acquired directly from a payor if the payment were made to a person for whom indicia of foreign status existed, as described in proposed §1.1441-1(f)(2)(i)(B).

Section 31.3406(g)-1(e) would revise the proposed regulations contained in project number IA-224-82 published in the Federal Register on September 27, 1990 (55 FR 39427) to restate the principles that no backup withholding applies under section 3406 to reportable payments made outside the United States even though documentary evidence of non-U.S. status may be required in order to exempt the payment from 1099 reporting, unless the payor has actual knowledge that the payee is a United States person. The regulations propose to add an exception for notional principal contract payments that are made outside the United States.

Amendments to §31.6413(a)-3

The regulations under §31.6413(a)-3 are proposed to be amended in order to allow payers to refund backup withholding in certain circumstances. Those regulations currently prohibit a refund of backup withholding except when erroneous withholding has occurred. It is proposed to expand the definition of erroneous withholding to a situation where the withholding agent backup withholds because the payee fails to provide sufficient documentation as required under section 3406 and 1441 and the regulations under these sections. Where an appropriate withholding certificate is later provided, the withholding agent could treat the earlier withholding as erroneous withholding. However, the withholding certificate should be received prior to the end of the calendar year in which the payment is made and prior to the time the payor furnishes a Form 1099 to the payee with respect to the payment for which the withholding erroneously occurred. The amount refunded would be the amount actually

withheld less the amount required to be withheld, if any, under chapter 3 of the Code.

Removal of Q&A regulations

The existing regulations under part 35a are proposed to be removed in order to reflect the proposed revisions in this document.

Amendments to §301.6109-1

Amendments to the regulations under this section are currently pending to authorize the IRS to issue taxpayer identifying numbers to certain foreign persons and to require a taxpayer to state a TIN on any tax return filed (other than an information return). These regulations are proposed to be further amended to require that a TIN be stated on withholding certificates as may be required under the regulations proposed under sections 1441, 1442, and 1443.

Amendments to §301.6114-1

The regulations under section 6114 are proposed to be amended to require certain foreign entities to file a Form 8833 if they are claiming to be qualified under a limitation of benefits provision under an income tax treaty, even though the income is also reported on a Form 1042 by the withholding agent. The filing requirement would be limited to payments between related parties that exceed \$500,000 for the taxable year. See proposed §1.1441-6(b)(1).

Amendments to §301.6402-3(e)

Paragraph (e) of the regulations under §301.6402-3 is proposed to be amended to require that returns filed to claim a refund of tax include the taxpayer's TIN. In addition, the Form 1042-S would have to be attached to the return and also show the taxpayer's TIN.

Removal of Certain Regulations Under Tax Conventions

This document proposes to remove certain regulations issued under income tax conventions between the United States and Greece, Germany, Switzerland, Ireland, France, Austria, Pakistan, Sweden and Denmark. Removal of these regulations will be done in

consultation with the competent authorities of these countries.

Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in EO 12866. Therefore, a regulatory assessment is not required. It has also been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) and the Regulatory Flexibility Act (5 U.S.C. chapter 6) do not apply to these regulations, and, therefore, a Regulatory Flexibility Analysis is not required. Pursuant to section 7805(f) of the Internal Revenue Code, these regulations will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact on small business.

Comments and Requests for a Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written comments (a signed original and eight (8) copies) that are submitted timely to the IRS. All comments will be available for public inspection and copying. A public hearing will be scheduled on a date, time, and place as will be published in the Federal Register.

* * * * *

Proposed Amendment to the Regulations

Accordingly, under the authority of 26 U.S.C. 7805, 26 CFR chapter I is proposed to be amended as follows:

PART 1—INCOME TAXES

Paragraph 1. The authority citation for part 1 is amended by adding entries in numerical order and removing the entry for §1.1441-4T to read as follows:

Authority: 26 U.S.C. 7805 * * *

Section 1.1441-2 also issued under 26 U.S.C. 1441(c)(4) and 26 U.S.C. 3401(a)(6).

Section 1.1441-3 also issued under 26 U.S.C. 1441(c)(4) and 26 U.S.C. 3401(a)(6). * * *

Section 1.1441-6 also issued under 26 U.S.C. 1441(c)(4) and 26 U.S.C. 3401(a)(6).

Section 1.1441-7 also issued under 26 U.S.C. 1441(c)(4) and 26 U.S.C. 3401(a)(6). * * *

§1.163-5 [Amended]

Par. 2. In §1.163-5 paragraph (c)(2)-(i)(B)(5) is amended by removing the language "subdivision (iii) of A-5 of §35a.9999-4T" in the last sentence and adding "§1.6049-5(c)(2)(ii)" in its place.

Par. 3. Section 1.165-12(c) is amended by:

- 1. Removing paragraph (c)(1)(iii).
- 2. Redesignating paragraphs (c)(1)-(iv) and (c)(1)(v) as paragraphs (c)(1)-(iii) and (c)(1)(iv), respectively.
- 3. Amending paragraphs (c)(1)(i) and (c)(1)(ii) by removing the language "(c)(1)(v)" and adding "(c)(1)(iv)" in its place.
- 4. Revising newly designated paragraph (c)(1)(iii).

The revision reads as follows:

§1.165-12 Denial of deduction for losses on registration-required obligations not in registered form.

* * * * *

(c) * * *

(1) * * *

(iii) The holder may deliver an obligation in bearer form that is offered or sold inside the United States only if the holder delivers it to a financial institution that is purchasing for its own account, the account of another foreign institution, or an exempt organization that will comply with the requirements of section 165(j)(3)(A), (B), or (C). The holder may deliver a registration-required obligation in bearer form that is offered and sold outside the United States to a person other than a financial institution only if the holder has evidence in its records that such person is not a U.S. citizen or resident and does not have actual knowledge that such evidence is false. Such evidence may include a statement by that person that is delivered electronically. For purposes of this paragraph (c), the term *deliver* includes a transfer of an obligation evidenced by a book entry including a book entry notation by a clearing organization evidencing transfer of the obligation from one member of the organization to another member. For purposes of

this paragraph (c), the term *deliver* does not include a transfer of an obligation to the issuer or its agent for cancellation or extinguishment.

* * * * *

Par. 4. Section 1.871-14 is added to read as follows:

§1.871-14 Rules relating to repeal of tax on interest of nonresident alien individuals and foreign corporations received from certain portfolio debt investments.

(a) *General rule.* No tax shall be imposed under sections 871(a)(1)(A), 871(a)(1)(C), 881(a)(1) or 881(a)(3) on any portfolio interest as defined in sections 871(h)(2) and 881(c)(2) received by a foreign person. But see section 871(h) or 882(a) if such interest is effectively connected with the conduct of a trade or business within the United States.

(b) *Rules concerning obligations not in registered form—(1) In general.* [Reserved] For further guidance, see §35a.9999-5(a), Answer 1.

(2) *Convertible obligations.* [Reserved] For further guidance, see §35a.9999-5(c), Answers 18 and 19.

(3) *Coordination with withholding and reporting rules.* See §1.1441-2(d)(1)(i) for an exception from documentation requirements otherwise applicable for purposes of section 1441. See section 6049 and §1.6049-5(b)(7) for rules relating to an exemption from Form 1099 reporting and backup withholding under section 3406.

(c) *Rules concerning obligations in registered form—(1) In general.* In the case of interest paid on an obligation that is in registered form, the term *portfolio interest* means any interest (including original issue discount)—

(i) That is paid on an obligation issued after July 18, 1984;

(ii) That would be subject to tax under section 871(a)(1)(A), 871(a)(1)(C), 881(a)(1) or 881(a)(3) but for section 871(h) or 881(c); and

(iii) With respect to which a United States (U.S.) person otherwise required to deduct and withhold tax under section 1441(a) or 1442(a) receives a statement that meets the requirements of section 871(h)(5) that the beneficial owner of the obligation is not a U.S. person.

(2) *Required statement.* A U.S. person will be considered to have received

a statement that meets the requirements of section 871(h)(5) if either it complies with one of the procedures described in this paragraph and does not have actual knowledge or reason to know that the beneficial owner is a U.S. person or it complies with the procedures described in paragraph (d) or (e) of this section.

(i) The U.S. person (or its authorized foreign agent described in §1.1441-7(c)(2)) complies with the withholding certificate procedures described in §1.1441-1(e)(1).

(ii) The U.S. person complies with the documentary evidence procedures described in §1.6049-5(c)(2)(ii) (but only if payments are made outside the United States with respect to offshore accounts). See §1.6049-5(e) for determining the place of payment and §1.6049-5(d)(3) for a definition of offshore accounts.

(iii) [Reserved] For further guidance, see §35a.9999-5(b), Answer 9, sentences 5 through 13.

(iv) The U.S. person complies with procedures that the U.S. competent authority may agree to with the competent authority of a country with which the United States has an income tax treaty in effect.

(3) *Time for providing certificate or documentary evidence.* Interest on a registered obligation shall qualify as portfolio interest if the withholding certificate or documentary evidence that must be provided is furnished before expiration of the beneficial owner's period of limitation for claiming a refund of tax with respect to such interest. See, however, §1.1441-1(f)(5) for consequences to a withholding agent that makes a payment without withholding even though it cannot associate the payment with the required documentation prior to the payment.

(4) *Coordination with withholding and reporting rules.* For an exemption from withholding under section 1441 with respect to obligations described in this paragraph (c), see §1.1441-2(d)(2). For rules applicable to withholding certificates, see §1.1441-1(e)(4). For application of presumptions when the U.S. person cannot associate the payment with the required documentation, see §1.1441-1(f). For standards of knowledge applicable to withholding agents, see §1.1441-7(b). For rules relating to an exemption from Form 1099 reporting and backup withholding under section 3406, see section 6049

and §1.6049-5(b)(8). For rules relating to reporting on Forms 1042 and 1042-S, see §1.1461-1(b) and (c).

(d) *Application of repeal of 30 percent withholding to pass-through certificates.* [Reserved] For further guidance, see §35a.9999-5(e), Answers 21 and 22.

(e) *Foreign-targeted registered obligations.* [Reserved] For further guidance, see §35a.9999-5(b), Answers 12 through 15.

(f) *Definitions.* For purposes of this section, the terms *foreign person* and *beneficial owner* have the meaning set forth in §1.1441-1(c)(2) and (c)(6), respectively; the term *withholding agent* has the meaning set forth in §1.1441-7(a); and the term *payment* has the meaning set forth in §1.1441-2(e).

(g) *Effective date—(1) In general.* This section shall apply to payments of interest made after December 31, 1997.

(2) *Transition rule.* For purposes of paragraph (c)(2)(i) of this section, a withholding agent that holds a valid Form W-8 on a date that is 60 days after these regulations are published as final regulations in the Federal Register may treat it as a valid withholding certificate until its validity expires under applicable provisions as in effect on April 22, 1996.

Par. 5. Section 1.1441-0 is added to read as follows:

§1.1441-0 Outline of regulation provisions for section 1441.

This section lists captions contained in §§1.1441-1, 1.1441-2, 1.1441-3, 1.1441-4, 1.1441-5, 1.1441-6, 1.1441-7, 1.1441-8T, and 1.1441-9.

§1.1441-1 Requirement for the deduction and withholding of tax on payments to foreign persons.

- (a) Purpose and scope.
- (b) General rule of withholding.
- (c) Definitions.
 - (1) Withholding.
 - (2) Foreign person.
 - (3) Payee.
 - (4) Individual
 - (5) Foreign corporations.
 - (6) Beneficial owner.
 - (7) Chapter 3 of the Internal Revenue Code.

- (d) Claim of U.S. status by payee or beneficial owner.
 - (1) In general.
 - (2) Payments to a payee that is a U.S. person.
 - (3) Payments to a foreign person acting for a U.S. payee.
- (e) Beneficial owner's claim of foreign status.
 - (1) Withholding agent's reliance.
 - (2) Beneficial owner withholding certificate.
 - (3) Intermediary withholding certificate.
 - (4) Applicable rules.
 - (5) Qualified intermediaries.
- (f) Presumptions.
 - (1) In general.
 - (2) Reportable payments to non-exempt recipients.
 - (3) Special rules for scholarships, grants, pensions, annuities, etc.
 - (4) Special rules for pass-through entities.
 - (5) Failure to act in accordance with presumptions.
 - (6) Reportable payment.
 - (7) Adjustment, refund, or credit of overwithheld tax.
- (g) Effective date.
 - (1) In general.
 - (2) Transition rules.

§1.1441-2 Income subject to withholding.

- (a) In general.
- (b) Fixed or determinable annual or periodical income.
 - (1) In general.
 - (2) Exceptions.
 - (3) Original issue discount.
 - (4) Securities lending transactions.
- (c) Other income subject to withholding.
- (d) Items of income not subject to withholding under section 1441.
 - (1) Exemptions for which no withholding certificate or documentation is required.
 - (2) Exemptions for portfolio interest and income on bank, etc. deposits requiring a withholding certificate or documentation.
- (e) Payment.
 - (1) General rule.
 - (2) Income allocated under section 482.
 - (3) Blocked income.
 - (4) Special rules for dividends.
 - (5) Certain interest accrued by a foreign corporation.
 - (6) Payments other than in U.S. dollars.

- (f) Effective date.
 - §1.1441-3 Amounts subject to withholding.*

- (a) Withholding on gross amount.
- (b) Withholding on payments on certain obligations.
 - (1) Withholding at time of payment of interest.
 - (2) No withholding between interest payment dates.
- (c) Corporate distributions.
 - (1) General rule.
 - (2) Determination of accumulated and current earnings and profits on the date of payment.
 - (3) Special rules in the case of distributions from a regulated investment company.
 - (4) Overwithholding of tax.
- (d) Withholding on certain gains.
- (e) Payments other than in U.S. dollars.
 - (1) In general.
 - (2) Payments in foreign currency.
 - (3) Tax liability of beneficial owner satisfied by withholding agent.
- (f) Conduit financing arrangements.
- (g) Effective date.

§1.1441-4 Certain exemptions from withholding.

- (a) Certain income connected with a U.S. trade or business.
 - (1) In general.
 - (2) Withholding agent's reliance on a claim of effectively connected income.
 - (3) Income on notional principal contracts.
 - (4) Failure to act in accordance with presumption.
- (b) Compensation for personal services of an individual.
 - (1) Exemption from withholding.
 - (2) Manner of obtaining withholding exemption under tax treaty.
 - (6) Personal exemption.
- (c) Special rules for scholarship and fellowship income.
 - (1) In general
 - (2) Alternate withholding election
- (d) Annuities received under qualified plans.
- (e) Income of foreign central bank of issue or the Bank for International Settlements.
- (f) Effective date.
 - (1) General rule.

- (2) Transition rules.

§1.1441-5 Withholding on payments to pass-through entities.

- (a) Domestic partnerships.
 - (1) Exemption from withholding on payment to domestic partnerships.
 - (2) Withholding by a domestic partnership.
- (b) Foreign partnerships.
 - (1) In general.
 - (2) Special rules in the case of tiered partnerships.
 - (3) Presumptions.
 - (4) Example.
- (c) Trusts and estates. [Reserved]
- (d) Effective date.
 - (1) General rule.
 - (2) Transition rules.

§1.1441-6 Claim of a reduced rate of tax under an income tax treaty.

- (a) In general.
- (b) Reliance on claim of treaty benefits.
 - (1) In general.
 - (2) Special rules for certain dividends.
 - (3) Competent authorities agreement.
 - (4) Special rules for payments to certain foreign entities.
- (c) Proof of tax residence in a treaty country.
 - (1) In general.
 - (2) Certification of taxpayer identifying number.
 - (3) Certificate of residence.
 - (4) Documentary evidence establishing residence in the treaty country.
- (d) Joint owners.
- (e) Related party dividends under certain treaties.
- (f) Effective date.
 - (1) General rule.
 - (2) Transition rules.

§1.1441-7 General provisions relating to withholding agents.

- (a) Withholding agent defined.
- (b) Standards of knowledge.
 - (1) In general.
 - (2) Reason to know.
 - (3) Universal accounts.
- (c) Authorized agent.
 - (1) In general.
 - (2) Authorized foreign agent.

- (3) Notification.
- (4) Liability of U.S. withholding agent.
- (5) Filing of returns.
- (d) United States obligations.
- (e) Assumed obligations.
- (f) Conduit financing arrangements. [Reserved]
- (g) Effective date.

§1.1441-8T Foreign government and international organization exemption from withholding (temporary).

- (a) Foreign governments.
- (b) Statement claiming exemption.
- (c) Effective date.
 - (1) In general.
 - (2) Transition rules.

§1.1441-9 Exemption from withholding on exempt income of a foreign tax-exempt organization and foreign private foundations.

- (a) Income not subject to tax under section 511.
- (b) Statement claiming exemption.
- (c) Effective date.
 - (1) In general.
 - (2) Transition rules.

Par. 6. Section 1.1441-1 is revised to read as follows:

§1.1441-1 Requirement for the deduction and withholding of tax on payments to foreign persons.

(a) *Purpose and scope.* This section and §§1.1441-2 through 1.1441-9 provide rules for withholding under section 1441 when a payment is made to a foreign person. This section provides definitions of terms used in chapter 3 of the Internal Revenue Code and regulations under that chapter. It prescribes procedures to determine whether a tax must be withheld under chapter 3 of the Internal Revenue Code, including presumptions for determining whether a withholding agent should treat a payee as a United States (U.S.) person or a foreign person. Special procedures regarding payments to foreign persons that act as intermediaries are also provided. Section 1.1441-2 describes the income subject to withholding under section 1441. Section 1.1441-3 provides rules regarding the amount subject to withholding. Section 1.1441-4 provides exemptions from withholding for certain income effectively connected with the conduct

of a trade or business in the United States, including certain compensation for the personal services of an individual. Section 1.1441-5 provides rules regarding withholding on payments made to pass-through entities. Section 1.1441-6 provides rules regarding claiming a reduced rate of withholding under an income tax treaty. Section 1.1441-7 defines the term withholding agent and provides rules regarding withholding agents' obligations to withhold. Section 1.1441-8T provides rules for income received by a foreign government that is excluded from gross income under section 892. Section 1.1441-9 provides rules for payments to foreign tax exempt organizations and foreign private foundations.

(b) *General rule of withholding.* A withholding agent (as defined in §1.1441-7(a)) must withhold 30 percent of the gross amount of a payment (as defined in §1.1441-2(e)) of income subject to withholding made to a payee that is a foreign person unless the beneficial owner of the income is a foreign person entitled to a reduced rate of tax and for the withholding agent holds an appropriate withholding certificate or documentation or unless the beneficial owner of the income is a U.S. person. For this purpose, a payment to the U.S. agent of a foreign person is treated as a payment to a foreign person if the withholding agent has actual knowledge or reason to know of the agency relationship. For the documentation upon which a withholding agent may rely in order to treat a payee or beneficial owner as a U.S. person, see paragraph (d) of this section. For the documentation upon which a withholding agent may rely in order to treat a payee or a beneficial owner as a foreign person, see paragraph (e) of this section. For applicable presumptions if the withholding agent cannot associate the payment with the required documentation at the time of payment, see paragraph (f) of this section. For definitions of foreign person, payee, and beneficial owner, see paragraphs (c)(2), (3), and (6) of this section, respectively. For the determination of income subject to withholding, see §1.1441-2(a). For a definition of an offshore account, see §1.6049-5(d)(3). For withholding procedures applicable to payments to U.S. and foreign partnerships, respectively, see §1.1441-5(a) and (b). For withholding procedures applicable to payments to U.S. and foreign trusts and estates, see §1.1441-5(c).

(c) *Definitions*—(1) *Withholding.* The term *withholding* means the deduction and withholding of tax at the applicable rate from the payment of income.

(2) *Foreign person.* The term *foreign person* means a nonresident alien individual, a foreign corporation, a foreign partnership, a foreign trust, a foreign estate, and any other person that is not a United States person for purposes of chapter 3 of the Internal Revenue Code. A United States person is a person described in section 7701(a)(30), the U.S. government (including an agency or instrumentality thereof), or a State and the District of Columbia (including an agency or instrumentality thereof).

(3) *Payee*—(i) *General rule.* Except as otherwise provided in paragraph (c)(3)(ii) of this section, a payee is the person to whom a payment is made. See §1.1441-2(e) for the determination of when a payment is considered made. Treatment of a person as a payee has consequences for purposes of withholding under chapter 3 of the Internal Revenue Code (see paragraph (b) of this section (relating to the general rule of withholding)) as well as for purposes of reporting income under the provisions of chapter 61 of the Internal Revenue Code and backup withholding under section 3406. See paragraph (d)(3) of this section for when a withholding agent may treat a payment to a foreign person as a payment made to a payee that is a U.S. person if the foreign person is acting for or representing the U.S. person.

(ii) *Payments to a foreign partnership.* For purposes of chapter 3 of the Internal Revenue Code, section 3406, and chapter 61 of the Internal Revenue Code, a payment made to a foreign partnership shall be treated as a payment made to the partners rather than to the partnership. A withholding agent may, however, treat a payment to a foreign partnership as made to the partnership (rather than to its partners) if, with respect to the partnership, it holds an intermediary withholding certificate described in paragraph (e)(3)(ii) of this section (relating to a certificate from a qualified intermediary) or an intermediary withholding certificate described in paragraph (e)(3)(iii) of this section (relating to a certificate from a foreign partnership) representing that the income to which the certificate relates is effectively connected with the

conduct of a trade or business in the United States. In addition, if the withholding agent holds an intermediary withholding certificate described in paragraph (e)(3)(iv) of this section (relating to a certificate from an agent, nominee, representative, etc.), then the payee shall be the person on whose behalf the partnership is receiving the payment. In the case of tiered foreign partnerships that are not treated as payees under the provisions of this paragraph (c)(3)(ii), the payees shall be the partners of the next higher-tier foreign partnership. Thus, the rules of this paragraph (c)(3) shall apply through any number of tiers of foreign partnerships in order to determine which partner is treated as the payee. For example, if a payment is made to a foreign partnership (second tier) and one of the partners of the second tier partnership is another foreign partnership (first tier) with two individual partners, the payment to the second tier is treated as made to the individual partners of the first tier (unless the second tier partnership has furnished one of the intermediary withholding certificates referred to in this paragraph (c)(3)(ii)). If one of the partners in the first tier is a domestic partnership, the domestic partnership is treated as the payee under the provisions of paragraph (c)(3)(i) of this section, even though one of the partners of the domestic partnership might be a foreign partnership. If the first tier foreign partnership is a nominee and furnishes an intermediary withholding certificate described in paragraph (e)(3)(iv) of this section, the person on whose behalf the first tier partnership receives the payment is treated as the payee. See §1.1441-5(b) for rules regarding procedures applicable to beneficial owners' claims of reduced rate of withholding under chapter 3 of the Internal Revenue Code.

(4) *Individual*—(i) *Alien individual*. The term *alien individual* means an individual who is not a citizen or a national of the United States. See §1.1-1(c).

(ii) *Nonresident alien individual*. The term *nonresident alien individual* means a person described in section 7701(b)(1)(B), an alien individual who is a resident of a foreign country under the residence article of an income tax treaty and §301.7701(b)-7(a)(1) of this chapter, or an alien individual who is a resident of Puerto Rico, Guam, the

Commonwealth of Northern Mariana Islands, the U.S. Virgin Islands, or American Samoa as determined under §301.7701(b)-1(d) of this chapter. An alien individual who has made an election under section 6013(g) or (h) to be treated as a resident of the United States is nevertheless treated as a nonresident alien individual for purposes of withholding under chapter 3 of the Internal Revenue Code.

(5) *Foreign corporations*. For purposes of this section, a corporation created or organized in Guam, the Commonwealth of Northern Mariana Islands, the U.S. Virgin Islands, and American Samoa, is not treated as a foreign corporation if the requirements of subparagraphs (A), (B), and (C) of section 881(b)(1) are met for such corporation. Further, a payment made to a foreign government or an international organization shall be treated as a payment made to a foreign corporation for purposes of withholding under chapter 3 of the Internal Revenue Code.

(6) *Beneficial owner*—(i) *General rule*. In the case of a payment of income, the term *beneficial owner* means the person required under U.S. tax principles to include the amount paid in gross income under section 61 (determined without regard to an exclusion or exemption from gross income under the Internal Revenue Code). Thus, a nominee, agent, custodian, or any person acting in a similar capacity is not the beneficial owner. In the case of a scholarship, the student receiving the scholarship is the beneficial owner of that scholarship.

(ii) *Special rules for certain entities*—(A) *General rule*. The beneficial owners of income paid to a partnership are those persons that, under U.S. tax principles, are the taxpayers with respect to that income in their separate or individual capacities. For example, a partnership (first tier) that is a partner in another partnership (second tier) is not the beneficial owner of income paid to the second tier partnership since the first tier partnership is not liable for income tax under U.S. tax principles. See, however, §1.1441-5(a) for applicable withholding procedures for payments to a domestic partnership. See also §1.1441-5(b)(2) for applicable withholding procedures for payments to a foreign partnership where one of the partners (at any level in the chain of tiers) is a domestic partnership.

(B) *Special rules when an income tax treaty applies*. For purposes of claiming a reduction in the rate of withholding on income paid to a foreign entity based on an income tax treaty between the United States and a foreign country, the tax principles in effect under the laws of that foreign country shall apply to determine whether the entity or the persons holding an interest in that entity are required to include the amounts in income and, therefore, whether, under the principles of this paragraph (c)(6), the entity or the interest holders in the entity are the beneficial owners of the income. See §1.1441-6(b)(4)(iii) permitting a withholding agent to treat, at its option, payments made to a single foreign entity as beneficially owned in part by the entity and, in part, by any one or more persons holding an interest in the entity. The possibility of dual treatment may also occur if a reduced rate of tax is claimed under the Internal Revenue Code for certain types of income and under a U.S. income tax treaty for other types of income or if reduced rates are claimed under different tax treaties. For purposes of this paragraph (c)(6)(ii)(B), the term *foreign entity* does not include a trust or an estate. See §1.1441-6(b)(4) for procedures governing claims of benefits under an income tax treaty.

(C) *Trusts*. The provisions of paragraphs (c)(6)(i) and (c)(6)(ii)(A) of this section shall not apply to a trust, whether domestic or foreign. The beneficial owner of income paid to a trust shall be determined under the provisions of §1.1441-3(f) and (g), as in effect on the date preceding the date on which this document is published as a final regulation in the Federal Register.

(7) *Chapter 3 of the Internal Revenue Code*. For purposes of the regulations under sections 1441, 1442, and 1443, any reference to chapter 3 of the Internal Revenue Code shall not include references to sections 1445 and 1446, unless the context indicates otherwise.

(d) *Claim of U.S. status by payee or beneficial owner*—(1) *In general*. Payments made to a U.S. person are not subject to the withholding of tax under section 1441, absent actual knowledge or reason to know that the U.S. person may be acting as an agent for a foreign person. See paragraph (b) of this section. Absent actual knowledge or reason to know otherwise, a withholding

agent may apply the provisions of this paragraph (d) to a payment of income otherwise subject to withholding to determine whether to treat the payment as made to a U.S. person. See paragraph (f) of this section for applicable presumptions if the withholding agent cannot associate the payment with the required documentation prior to the time of payment.

(2) *Payments to a payee that is a U.S. person*—(i) *Reportable payments.* If a reportable payment (as defined in section 3406(b)) is made to a payee that is not an exempt recipient (as defined under the applicable information reporting provisions of chapter 61 of the Internal Revenue Code), the withholding agent may treat the payment as made to a U.S. person if the payee complies with the procedures described in §§31.3406(d)–1 through 31.3406(d)–5 of this chapter (including requiring a payee to furnish its taxpayer identifying number) and the withholding agent meets all the requirements described in §31.3406(h)–3(e) of this chapter regarding reliance by a payor on a Form W–9).

(ii) *Payments to exempt recipients and certain other payments.* If a reportable payment is made to a payee that is an exempt recipient (as defined under the applicable information reporting provisions of chapter 61 of the Internal Revenue Code) or is a scholarship, grant, pension, or annuity, a withholding agent may treat the payment as made to a U.S. person if the payee provides a certificate of U.S. status. For purposes of this paragraph (d)(2)(ii), a certificate of U.S. status is a Form W–9 (or such other form as the Internal Revenue Service may prescribe) that is signed under penalties of perjury by the payee and contains all required information. For purposes of this paragraph (d)(2)(ii), required information consists of the payee’s name, permanent residence address, and taxpayer identifying number. The procedures described in §31.3406(h)–3(a) of this chapter shall apply to payments to joint payees. A withholding agent that receives a Form W–9 in order to satisfy this paragraph (d)(2)(ii) must retain the form in accordance with the provisions of paragraph (e)(4)(iii) of this section relating to the retention of withholding certificates. The rules of this paragraph (d)(2)(ii) are only intended to provide a method by which a withholding agent may determine that a payee is not a

foreign person and do not otherwise impose a requirement that documentation be furnished by an exempt recipient or for payments subject to this paragraph (d)(2)(ii).

(3) *Payments to a foreign person acting for a U.S. payee.* Absent actual knowledge or reason to know otherwise, for purposes of chapter 3 of the Internal Revenue Code, section 3406, and chapter 61 of the Internal Revenue Code, a withholding agent may treat a payment to a foreign person as a payment made to a payee that is a U.S. person if it receives an intermediary withholding certificate described in paragraph (e)(3)(iv) of this section regarding the foreign person to which is attached the applicable certification described in paragraph (d)(2) of this section concerning the U.S. payee on whose behalf the foreign person is receiving the payment. See paragraph (e)(5) of this section for applicable procedures in the case of a payment to a foreign person acting as a qualified intermediary. See also, §1.1441–5(b)(1) for applicable procedures in the case of a payment to a foreign partnership that is not a qualified intermediary.

(e) *Beneficial owner’s claim of foreign status*—(1) *Withholding agent’s reliance.* Absent actual knowledge or reason to know otherwise, a withholding agent may rely on a claim that the beneficial owner of income is a foreign person, if, prior to the payment, it complies with the requirements described in paragraphs (e)(1)(i), (ii), and (iii) of this section. For this purpose, a withholding agent acting through an authorized foreign agent is deemed to comply with such requirements to the extent its authorized foreign agent so complies. See §1.1441–7(c)(2) for the description of an authorized foreign agent. In the case of a payment to a person other than an individual, a withholding agent may rely on the claim of entity classification made on the basis of the certification (or documentation, if applicable) furnished to the withholding agent, unless it has actual knowledge or reason to know that the classification claimed is incorrect.

(i) The withholding agent holds a beneficial owner withholding certificate described in paragraph (e)(2)(i) of this section or an intermediary withholding certificate described in paragraph (e)(3)(i) of this section.

(ii) The withholding agent complies with the electronic confirmation proce-

dures described in paragraph (e)(4)(v) of this section, if required.

(iii) The withholding agent has not been notified by the Internal Revenue Service that any of the information on the withholding certificate is incorrect or unreliable.

(2) *Beneficial owner withholding certificate*—(i) *In general.* A beneficial owner withholding certificate is a statement by which the beneficial owner of the income paid represents that it is a foreign person and, if applicable, claims a reduced rate of withholding under section 1441. A separate withholding certificate must be submitted to each withholding agent. If the beneficial owner receives more than one type of income from a single payor, the beneficial owner may submit one withholding certificate to the single payor for the different types of income. See paragraph (c)(6)(ii)(B) of this section and §1.1441–6(b)(4)(i) for the determination of beneficial owner when a benefit is claimed under an income tax treaty. A beneficial owner of an interest in a mutual fund that has a common investment advisor or common principal underwriter with other mutual funds (within the same family of funds) may, in the discretion of the mutual fund, provide one withholding certificate for shares acquired or owned in any of the funds. See §31.3406(h)–3(a)(2) of this chapter.

(ii) *Requirements for validity of certificate.* A beneficial owner withholding certificate is valid only if it is provided on a Form W–8 (or, in the case of personal services income described in §1.1441–4(b), a Form 8233), its validity period has not expired, it is signed under penalties of perjury by the beneficial owner and it contains all of the information described in this paragraph (e)(2)(ii). The required information is the name, permanent residence address, and taxpayer identifying number (TIN) of the beneficial owner (if required), the basis for the reduced rate of withholding claimed, if applicable, (including any applicable tax treaty provisions), and any other information as may be required (in addition to, or in lieu of, the information described in this paragraph (e)(2)(ii)) by the regulations under section 1441 or by a form or accompanying instructions. A permanent residence address is the address in the country where the person claims to be a resident for purposes of that country’s income tax. The address of a

financial institution with which the beneficial owner maintains an account, a post office box, or an address used solely for mailing purposes is not a residence address for this purpose. If the beneficial owner is an individual who does not to have a tax residence in any country, the address is where the beneficial owner normally resides. If the beneficial owner is a corporation, then the address is where the corporation maintains its principal office in its country of incorporation. Instead of the Form W-8 (or the Form 8233, if applicable), the withholding agent may rely on an acceptable substitute form or such other form as the Internal Revenue Service may prescribe. See paragraph (g)(2) of this section for continued validity of certificates during the transition period. See paragraph (e)(4)-(vii) of this section for circumstances in which a taxpayer identifying number is required on a beneficial owner withholding certificate.

(3) *Intermediary withholding certificate*—(i) *In general.* An intermediary withholding certificate is a statement by which a foreign payee represents that it is not the beneficial owner of the income paid or is a statement furnished by a partnership for its partners. It is used either to make representations regarding the status of beneficial owners of the income or to transmit appropriate documentation to the withholding agent. This paragraph (e)(3) describes the requirements for the validity of an intermediary withholding certificate issued either by a qualified intermediary, by a foreign partnership that is not a qualified intermediary, or by any other person that is neither a qualified intermediary nor a foreign partnership.

(ii) *Intermediary withholding certificate from a qualified intermediary.* In the case of an intermediary withholding certificate issued by a qualified intermediary (described in paragraph (e)(5)-(ii) of this section), the certificate is valid only if it is furnished on a Form W-8 (or an acceptable substitute form or such other form as the Internal Revenue Service may prescribe), it is signed under penalties of perjury by an officer or partner of the qualified intermediary with authority to sign for the intermediary, and it contains the information and certifications described in this paragraph (e)(3)(ii).

(A) The name, permanent residence address (as described in paragraph

(e)(2)(ii) of this section), and the employer identification number of the qualified intermediary.

(B) A certification that the issuer is a qualified intermediary.

(C) A certification that the issuer has obtained, as required in the withholding agreement with the Internal Revenue Service, the appropriate certificates (such as Forms W-8 or W-9) or any other documentation regarding its account holders or partners.

(D) A statement whether the qualified intermediary is assuming primary withholding responsibility for the amounts to which the certificate relates.

(E) If the information is not assuming primary withholding responsibility, the information and certificates required under paragraph (e)(5)(iv)(B) of this section regarding the basis for any reduced rate of withholding tax claimed.

(F) Any other information or certification as may be required (in addition to, or in lieu of, the information and certifications described in this paragraph (e)(3)(ii)) by the form or accompanying instructions.

(iii) *Intermediary withholding certificate from a foreign partnership.* In the case of an intermediary withholding certificate issued under the provisions of §1.1441-5(b) by a foreign partnership that is not a qualified intermediary, the certificate is valid only if it is furnished on a Form W-8 (or an acceptable substitute form or such other form as the Internal Revenue Service may prescribe), it is signed under penalties of perjury by a partner with authority to sign for the partnership, and it contains the information and certifications described in this paragraph (e)(3)(iii).

(A) The name, permanent residence address (as described in paragraph (e)(2)(ii) of this section), and the employer identification number of the partnership.

(B) The basis for the reduced rate of withholding claimed, expressed in relation to the distributive share of each partner to which the certificate relates.

(C) The appropriate withholding certificates for the partners as required under §1.1441-5(b)(1) (except for an intermediary withholding certificate furnished in order to claim a reduced rate for income effectively connected with the conduct of a trade or business in the United States).

(D) A statement that the income is effectively connected with the conduct of a trade or business in the United States, if applicable.

(E) Any other information or certification as may be required (in addition to, or in lieu of, the information described in this paragraph (e)(3)(iii)) by the form or accompanying instructions.

(iv) *Intermediary withholding certificate from an agent, nominee, representative, etc.* In the case of an intermediary withholding certificate issued by a person that is not a qualified intermediary and is not acting for its own account, the certificate is valid if it is described in this paragraph (e)(3)(iv). In addition, a certificate furnished to qualify interest as portfolio interest for purposes of sections 871(h) and 881(c) or to qualify dividends on publicly traded stock (as defined in §1.1441-6(b)(2)) is valid if it is described in §1.871-14(c)(2)(iii). A certificate is described in this paragraph (e)(3)(iv) if it is furnished on a Form W-8 (or an acceptable substitute form, or such other form as the Internal Revenue Service may prescribe), it is signed under penalties of perjury by a person authorized to sign for the issuer of the certificate, and it contains the information and certifications described in this paragraph (e)(3)(iv).

(A) The name, permanent resident address (as described in paragraph (e)(2)(ii) of this section) and the taxpayer identifying number of the issuer of the certificate.

(B) A certification that the issuer is not acting for its own account and is using the certificate as a form to transmit beneficial owner documentation for the payment to which the certificate relates (or other applicable documentation concerning the person for whom the intermediary is receiving the payment).

(C) If furnishing an intermediary certificate to transmit more than one withholding certificate, the certificate may indicate the basis for the reduced rate of withholding claimed, based upon the attached withholding certificates.

(D) Any other information or certification as may be required (in addition to, or in lieu of the information and certification described in this paragraph (e)(3)(iv)) by the form or accompanying instructions.

(4) *Applicable rules*—(i) *Joint owners*. In the case of a payment to joint owners, a withholding certificate must be provided by each owner claiming to be a foreign person.

(ii) *Period of validity*—(A) *Three year period*. Except as otherwise provided in paragraph (e)(4)(ii)(B) of this section, a beneficial owner withholding certificate or an intermediary withholding certificate shall remain valid for three years or until such time as a change in circumstances makes any information on the certificate incorrect.

(B) *Validity period where TIN provided*. A withholding certificate furnished with a taxpayer identifying number shall remain valid until such time as a change in circumstances makes any information on the certificate incorrect but only if the income for which such certificate is furnished is required to be reported under §1.1461-1(c)(2)(ii) or the taxpayer identifying number furnished on the certificate is reported to the Internal Revenue Service under the procedures described in §1.1461-1(d).

(C) *Withholding certificate for effectively connected income*. Notwithstanding paragraph (e)(4)(ii)(B) of this section, the period of validity of a withholding certificate furnished to a withholding agent to claim a reduced rate of tax for income that is effectively connected with the conduct of a trade or business within the United States shall be limited to three years.

(D) *Computation of three-year period*. The three-year validity period shall start from the date that the certificate is signed until the last day of the third succeeding calendar year. For example, a certificate signed on September 30, 1998 remains valid through December 31, 2001.

(E) *Change in circumstances*. If a change in circumstances makes any information on the certificate incorrect, then the issuer of the certificate must inform the withholding agent within 30 days of the change and issue a new certificate. If a beneficial owner withholding certificate is used to claim foreign status only (and not, also, residence in a particular foreign country for purposes of an income tax treaty), a change of address is a change in circumstances for purposes of this paragraph (e)(4)(ii)(E) only if it changes to an address in the United States. Further, a change of address

within a foreign country is not a change in circumstances for purposes of this paragraph (e)(4)(ii)(E). A withholding agent may require a new certificate at any time prior to a payment, even though the withholding agent has no actual knowledge or reason to know that any information stated on the certificate has changed.

(iii) *Retention of withholding certificate*. A withholding agent must retain each withholding certificate for as long as it may be relevant to the determination of the withholding agent's tax liability under section 1461 and §1.1461-1.

(iv) *Electronic transmission of information*. Under procedures issued by the Internal Revenue Service, a withholding agent may be permitted to receive in electronic form the information required to be included on a withholding certificate or a certificate of U.S. status.

(v) *Electronic confirmation of information on withholding certificate*. Under procedures issued by the Internal Revenue Service, a withholding agent may be required to use an electronic on-line system to confirm with the Internal Revenue Service information concerning any taxpayer identifying number stated on a withholding certificate or a certificate of U.S. status.

(vi) *Acceptable substitute form*. For purposes of the regulations under section 1441, 1442, and 1443, the term *acceptable substitute* in the case of a Form W-8 or Form 8233 described in paragraph (e)(2) or (e)(3) of this section is a document prepared and furnished based on the rules set forth in §31.3406(h)-3(c)(1) of this chapter (relating to substitutes for a Form W-9).

(vii) *Requirement of taxpayer identifying number*. A taxpayer identifying number must be stated on a withholding certificate when required by this paragraph (e)(4)(vii). A taxpayer identifying number is required to be stated on a beneficial owner certificate if the beneficial owner is claiming the benefit of a reduced rate under an income tax treaty (other than with respect to dividends on stock traded on a U.S. established financial market), an exemption from withholding because income is effectively connected with a U.S. trade or business, an exemption under section 871(f) for certain annuities received under qualified plans, or an exemption based on a foreign organization's tax exempt status under

section 501(c) or private foundation status. In addition, a taxpayer identifying number is required to be stated on all intermediary withholding certificates. A taxpayer identifying number is an IRS individual tax identification number, an employer identification number, or a social security number as described in section 6109 and §301.6109-1 of this chapter, or any other identifier the Commissioner may designate.

(5) *Qualified intermediaries*—(i) *General rule*. A qualified intermediary, as defined in paragraph (e)(5)(ii) of this section, may furnish an intermediary withholding certificate to a withholding agent for purposes of certifying on behalf of beneficial owners, intermediaries (such as agents or nominees acting for the accounts of others), other qualified intermediaries or U.S. payees for the purpose of claiming reduced rates of withholding tax under section 1441, 1442, or 1443. Such certificate is in lieu of transmitting withholding certificates or other required documentation to a withholding agent. While the qualified intermediary is generally required to obtain withholding certificates or other appropriate documentary evidence from beneficial owners or payees pursuant to its agreement with the Internal Revenue Service, it is not required to attach such documentation to the intermediary withholding certificate.

(ii) *Definition of qualified intermediary*. The term *qualified intermediary* means a foreign person that is a party to a withholding agreement with the Internal Revenue Service and that is—

(A) A financial institution (as defined in §1.165-12(c)(1)(iv)) or a clearing organization (as defined in §1.163-5(c)(2)(i)(D)(8));

(B) A partnership; or

(C) Any other person acceptable to the Internal Revenue Service.

(iii) *Withholding agreement*—(A) *In general*. The Internal Revenue Service may, upon request, enter into a withholding agreement with a foreign person described in paragraph (e)(5)(ii) of this section pursuant to such procedures as the Internal Revenue Service may prescribe. The withholding agreement shall include the terms, conditions and procedures that the Internal Revenue Service shall deem appropriate to insure the collection of the tax due and reporting of information under sections 1441, 1461, 3406 and chapter 61 of the Internal Revenue Code.

(B) *Terms of the withholding agreement.* Generally, the agreement must include provisions dealing with defining, obtaining, and maintaining appropriate certification and documentation upon which the foreign person may rely to ascertain the nationality and residence of beneficial owners and U.S. payees, reporting account information to the Internal Revenue Service or otherwise making the account information available to the Internal Revenue Service, and, if applicable, acting as an acceptance agent to perform the duties described in §301.6109-1(d)(3)(iv)(A) of this chapter (as proposed in project number INTL-0024-94, published on June 8, 1995 (60 FR 30211)). In addition the agreement must specify the manner in which the Internal Revenue Service will verify compliance with the agreement. In appropriate cases, the Internal Revenue Service may agree to rely on audits performed by an intermediary's approved external auditor's records (including workpapers of the auditor and reports prepared by the auditor indicating the methodology employed to verify the entity's compliance with the agreement). For this purpose, the agreement shall specify which auditor or class of auditors is approved. An external auditor may not be approved unless it is subject to regulatory supervision under the laws of the country in which a significant part of the intermediary activities under the agreement are expected to occur, its internal procedures require it to verify that the intermediary complies with the terms of the withholding agreement and to report non-compliance findings under the agreement in the same manner as it is required to report other findings of non-compliance with applicable local laws and regulatory requirements, and the auditor's relevant records (*i.e.*, workpapers and reports) are available to the Internal Revenue Service. The agreement must include provisions for the assessment and collection of tax in the event that failure to comply with the terms of the agreement result in the failure by the withholding agent or the qualified intermediary to withhold and deposit the required amount of tax. Further, the agreement shall provide that a qualified intermediary that withholds any amount of tax must make deposits of the tax as required under §1.1461-1(a). The Internal Revenue Service may require the posting of a bond conforming to the requirements of §301.7101-1 of this chapter as to form

of bond or surety required. The agreement shall specify the scope of the agreement in the case of a foreign person with branches or relevant intermediary activities in more than one country. To determine the terms of any particular withholding agreement, the Internal Revenue Service will consider appropriate factors including whether or not the foreign person agrees to assume primary responsibility as a withholding agent, the type of local "know-your-customer" laws and practices to which it is subject, the extent and nature of supervisory and regulatory control exercised under the laws of the foreign country over the foreign person, the volume of investments in U.S. securities (determined in dollar amounts and number of account holders), and financial condition of the foreign person.

(iv) *Assignment of primary withholding responsibility—(A) In general.* A partnership that is a qualified intermediary acting for its own account must assume primary withholding responsibility. Any other qualified intermediary may assume primary withholding responsibility only if it is permitted to do so under its agreement with the Internal Revenue Service. A withholding agent and a qualified intermediary may arrange on who of the withholding agent or the qualified intermediary shall have primary responsibility for any amount required to be withheld under this section and section 3406 for any one or more classes of beneficial owners or payees and for any or more types of income expected to be paid to the intermediary. In a relationship between a withholding agent and a qualified intermediary, the qualified intermediary may agree to assume primary withholding responsibility for some types of income and not others. However, unless otherwise specified in the agreement, primary withholding responsibility for a type of income must be assumed for all beneficial owners and payees of that income or for none of them.

(B) *Applicable procedures when a qualified intermediary does not assume primary withholding responsibility.* When a qualified intermediary does not assume primary withholding responsibility, the intermediary withholding certificate must contain the information described in this paragraph (e)(5)(iv)-(B) or in any agreement between the qualified intermediary and the Service.

The certificate must separately identify the assets that are associated with each U.S. payee to which the certificate relates and that generate the type of income described in §1.1441-2(a) (*i.e.*, income that would be subject to withholding if paid to a foreign person). The qualified intermediary must furnish a Form W-9 for each U.S. payee that is not an exempt recipient and the name and address of each U.S. payee that is an exempt recipient. The intermediary withholding certificate must also separately identify the assets associated with non-U.S. payees to which the certificate relates and the applicable withholding tax rate or rates. If different withholding tax rates apply, the intermediary withholding certificate must indicate the applicable rate for each class of non-U.S. payees to which different withholding rates apply and the assets associated with each class. For payments that the intermediary withholding certificate states are made to U.S. payees, a withholding agent dealing with a qualified intermediary that has not assumed primary withholding responsibility must comply with applicable reporting requirements under chapter 61 of the Internal Revenue Code in the same manner as if it had received a Form W-9 (or acceptable substitute form) directly from the U.S. payee. The withholding agent must also comply with the return requirements under section 1461 and §1.1461-1(b)(2)(ii) and (c)(4)(ii) for payments made to non-U.S. payees.

(C) *Applicable procedures when qualified intermediary assumes primary withholding responsibility.* A withholding agent relying on an intermediary withholding certificate from a qualified intermediary representing that the qualified intermediary assumes primary withholding responsibility as permitted under its agreement with the Internal Revenue Service is relieved from the obligation to withhold on payments made to the intermediary. The withholding agent must comply with the return requirements under section 1461 and §1.1461-1(b)(2)(ii) and (c)(4)(ii) for payments made to the qualified intermediary.

(v) *Special rules for qualified intermediaries that are foreign partnerships.* A foreign partnership that is a qualified intermediary shall be a withholding agent with respect to its partner's distributive share of income subject to withholding that is paid to the part-

nership. Therefore, it shall withhold under the same procedures and at the same time as is prescribed for withholding by a domestic partnership. See §1.1441-5(a)(2) for withholding procedures applicable to domestic partnerships. In addition, the partnership shall not be relieved from its obligation to make a return on Form 1065 as required under section 6031 and the regulations under that section and to furnish the statements required under section 6031(b) and the regulations under that section.

(f) *Presumptions*—(1) *In general*—(i) *Reliance*. Absent actual knowledge or reason to know otherwise, a withholding agent or a payor described in §31.3406(a)-2 of this chapter may rely on the presumptions of this paragraph (f) to determine whether to treat a beneficial owner or a payee as a U.S. or a foreign person when, before making a payment of income subject to withholding, or a payment subject to reporting under chapter 61 of the Internal Revenue Code, the withholding agent or payor cannot associate the payment with the required documentation. When applying the provisions of this section, any presumption of foreign status pursuant to this paragraph (f) shall have effect only for purposes of applying the provisions of paragraph (b) of this section (regarding the rules of withholding) and may not be relied upon for purposes of granting a reduced rate of withholding under the Internal Revenue Code (e.g. section 1441(c)(9) or (c)(10)) or under an income tax treaty.

(ii) *Required documentation*. For purposes of this paragraph (f), the term *required documentation* means the applicable documentation that is required to be furnished in connection with the payment under this section, under §1.871-14(c)(2), or under chapter 61 of the Internal Revenue Code. A withholding agent or payor is not able to associate a payment with required documentation if, for that payment, it lacks documentation, the documentation it holds lacks information, or the withholding agent or payor knows or has reason to know that information associated with the required documentation is incorrect or unreliable. For purposes of this paragraph (f)(1), a withholding agent or payor has reason to know that information is incorrect or unreliable if the withholding agent or payor would have reason to know

under the rules of §1.1441-7(b)(2) or cannot reasonably rely on a Form W-9 (or an acceptable substitute) under §31.3406(h)-3(e) of this chapter. For purposes of this paragraph (f)(1), a Form W-9 (or an acceptable substitute) must contain the information described in §31.3406(h)-3(e)(2)(i) through (iv) of this chapter in order for a payor to reasonably rely on the Form W-9. In the case of other documentation, the required information shall include only the name, permanent residence address, taxpayer identifying number (when required), and signature under penalties of perjury (when required).

(2) *Reportable payments to non-exempt recipients*—(i) *In general*. Except as otherwise provided in paragraphs (f)(2)(ii) and (f)(4) of this section, a reportable payment (as defined in paragraph (f)(6) of this section) made to a payee who is an individual or other non-exempt recipient is presumed made to a U.S. payee for purposes of chapter 61 of the Internal Revenue Code, section 3406, and this section if, before payment, the withholding agent or payor cannot associate the payment with the required documentation (as determined under paragraph (f)(1)(i) of this section). In such a case, the withholding agent or payor must treat the payment as a payment that may be subject to reporting under chapter 61 of the Internal Revenue Code and the regulations under that chapter and to backup withholding under section 3406 and the regulations under that section.

(ii) *Special grace period for certain reportable payments in the case of indicia of a foreign payee*—(A) *General rule*. This paragraph (f)(2)(ii)(A) applies to payments of dividends, interest, original issue discount, broker proceeds described in §1.6045-1(d)(5), and exchanges of personal property or services through barter exchanges described in §1.6045-1(e)(2). A withholding agent or payor may treat the payee as a beneficial owner that is a foreign person for the grace period described in this paragraph (f)(2)(ii)(A) if, at the time a payment is first credited to an account, the withholding agent or payor has the name and an address in a foreign country for the account holder or a facsimile copy or an electronic transmission of the information contained in a withholding certificate described in paragraph (e)(2) or (e)(3) of this section. The grace period is 90

days from the date that the withholding agent or payor first credits the account or, if shorter, until the end of the calendar year. If this paragraph (f)(2)(ii)(A) applies, the withholding agent may then treat the payee as a beneficial owner that is a foreign person and is, therefore, required to withhold under section 1441 on the basis of this presumption from the time that the amounts are credited to the account.

(B) *Additional withholding in the event of payments or withdrawals*. If, at any time before provision or correction of the required documentation within the grace period specified in paragraph (f)(2)(ii)(A) of this section, the withholding agent loses control over any part or all of the amounts in an account described in paragraph (f)(2)(ii)(A) of this section (such as by making an actual payment from the account or allowing withdrawal of any part or all of the amounts in the account, other than for purposes of withholding an amount of tax), then the withholding agent or payor must treat the payee as a U.S. person for all amounts credited to the account during the grace period. Accordingly, the payor must withhold to the extent required under section 3406 on all reportable payments made to the account during the period to which the grace period applies and thereafter. The amount of backup withholding is equal to 31 percent of the reportable payments reduced by any amount previously withheld from the amounts credited to the account.

(C) *Application of withholding upon expiration of grace period*. If, upon the termination of the grace period described under paragraph (f)(2)(ii)(A) of this section, the required documentation has not been furnished or corrected, the payee is then presumed to be a U.S. person for purposes of section 3406 and chapter 61 of the Internal Revenue Code. Accordingly, the payor must withhold to the extent required under section 3406 on all reportable payments credited to the account during the grace period and thereafter (until appropriate documentation has been furnished or corrected). Any amount withheld from the payments subject to the grace period may be credited toward any amount of backup withholding due under section 3406. If the required documentation is furnished or corrected on or before the expiration of the grace period described in paragraph (f)(2)(ii)(A) of this section and establishes

that the beneficial owner is a foreign person, then any amount withheld on any payment made during the grace period will be treated as having been withheld under section 1441. To the extent such amount exceeds the amount of tax ultimately determined to be owed under section 1441, the excess shall be treated as an amount of overwithholding subject to adjustment under §1.1461-2(a), or refund or credit under §1.1464-1. If, on the other hand, U.S. status is established by required documentation on or before expiration of the grace period, then any amount withheld from the payments made during the grace period may be credited towards any amount of backup withholding due under section 3406. To the extent such tax exceeds the amount required to be withheld under section 3406, the excess shall be treated as erroneously withheld from the payee and shall be subject to adjustments as provided in §31.6413(a)-3 of this chapter.

(iii) *Joint owners or payees.* A withholding agent or payor may presume that a payment made to joint owners or payees for whom it cannot associate the required documentation for all payees is made to U.S. individuals. For purposes of applying this paragraph (f)(2)(iii), the grace period rules in paragraph (f)(2)(ii)(A) of this section shall apply only if each payee qualifies for it. In that case, the rules of paragraph (f)(2)(ii)(B) of this section would apply when any one of the joint account holders receives a payment, makes a withdrawal, or reinvests any portion of the funds in the account that are subject to the grace period.

(iv) *Special rules for exempt recipients.* If the payee is an exempt recipient described in §1.6049-4(c)-(1)(ii) and the withholding agent or payor has actual knowledge of the payee's employer identification number, then the withholding agent or payor may presume that the payee is a foreign person if the employer identification number begins with the two digits "98." The withholding agent or payor may also presume that the payee is foreign if the withholding agent's or payor's communications with the payee are mailed to an address in a foreign country, or if the payment is made outside the United States (as defined in §1.6049-5(e)). In other cases, the withholding agent or payor may presume that the exempt recipient is a U.S.

person and, therefore, subject to section 3406 and chapter 61 of the Internal Revenue Code and the regulations under those provisions. If a withholding agent or payor treats a payee as a foreign person pursuant to the presumption of this paragraph (f)(2)(iv), it must treat the payee as the beneficial owner and apply the provisions of section 1441, §1.871-14, and chapter 61 of the Internal Revenue Code accordingly. If the withholding agent treats the payee as a foreign person, it is subject to the return requirements of §1.1461-1(b) and (c). The presumption of this paragraph (f)(2)(iv) may be rebutted by providing the required documentation to the withholding agent or payor.

(3) *Special rules for scholarships, grants, pensions, annuities, etc.—(i) Scholarships and grants.* A payment representing scholarship or fellowship grant income (as defined in section 117) is presumed made to a U.S. person if the withholding agent or payor has a record of the payee's U.S. visa status in its records. In that case, the withholding agent or payor has reason to know that such individual is a foreign person and, therefore, the presumption of this paragraph (f)(3)(i) shall not apply.

(ii) *Pensions, annuities, etc..* A withholding agent or payor may presume that a payment from a trust described in section 401(a), an annuity plan described in section 403(a), or a payment with respect to any annuity, custodial account, or retirement income account described in section 403(b) is made to a U.S. or foreign person under the rules of this paragraph (f)(3)(ii).

(A) Such payment is presumed made to a U.S. person, if the withholding agent or payor has a Social Security number for the payee and a mailing address as described in this paragraph (f)(3)(ii)(A). A mailing address is an address used for purposes of information reporting or otherwise communicating with the payee that is an address in the United States or in certain foreign countries with which the United States has an income tax treaty. For this purpose, a income tax treaty must provide that the payee, if an individual resident in that country, would be entitled to an exemption from U.S. tax on amounts described in this paragraph (f)(3)(ii).

(B) Such payment is presumed made to a foreign person in all cases not

described in paragraph (f)(3)(ii)(A) of this section.

(4) *Special rules for pass-through entities—(i) Payments to partnerships.* In the case of a payment to a partnership, the presumptions of this paragraph (f)(4)(i) shall apply to determine whether to treat the partnership as a domestic or foreign partnership. This determination must be made before determining who are the payees under paragraph (c)(3) of this section. If the withholding agent or payor has actual knowledge of the partnership's employer identification number, then the withholding agent or payor may presume that the partnership is a foreign partnership if the employer identification number begins with the two digits "98." The withholding agent or payor may also presume that the partnership is foreign if the withholding agent's or payor's communications with the partnership are mailed to an address in a foreign country, or if the payment is made outside the United States (as defined in §1.6049-5(e)). In all other cases, the withholding agent or payor may presume that the partnership is domestic. The presumptions in this paragraph (f)(4)(i) may be rebutted by providing the required documentation to the withholding agent or payor.

(ii) *Payments to a foreign partnership.* A withholding agent or payor that makes a reportable payment to a partnership that it treats as a foreign partnership may presume that a partner is a U.S. payee that is not an exempt recipient if, before payment, the withholding agent cannot associate the payment with the required documentation for the partner. See paragraph (c)(3)(ii) of this section treating partners of a foreign partnership as payees. In such case, the withholding agent or payor must treat the portion of the payment allocable to the partner as made to a U.S. payee who is not an exempt recipient. Thus, the payment may be subject to reporting under chapter 61 of the Internal Revenue Code and the regulations under that chapter and to backup withholding under section 3406 and the regulations under that section. The portion of a payment allocable to a partner shall be determined based on the distributive shares of the partnership income allocable to each partner.

(iii) *Partners' distributive shares—(A) Domestic partnership.* For purposes

of this paragraph (f)(4)(iii)(A), a domestic partnership may presume that a partner is a U.S. payee that is not an exempt recipient if, at the time it is required to withhold on the amount, the partnership cannot associate the payment with the required documentation for that partner and the amount relates to a reportable payment made to the partnership.

(B) *Foreign partnership.* For purposes of this paragraph (f)(4)(iii)(B), a foreign partnership that is a qualified intermediary may treat a partner as a foreign payee if, at the time it is required to withhold on the amount, it cannot associate the amount with the required documentation for that partner.

(5) *Failure to act in accordance with presumptions.* A withholding agent that, contrary to the presumptions in this paragraph (f), grants a claim of reduced rate of withholding under section 1441 on income subject to withholding will be liable under section 1461 for the tax required to be withheld under section 1441, without the benefit of a reduced rate unless the withholding agent can demonstrate to the satisfaction of the District Director or the Assistant Commissioner (International) that the proper amount of tax, if any, was in fact paid to the Internal Revenue Service. Proof of payment of tax may be established on the basis of a Form 4669 (or such other form as the Internal Revenue Service may prescribe), establishing the amount of tax, if any, actually paid by the beneficial owner on the income. Proof that a reduced rate of withholding was appropriate may also be established on the basis of the required documentation described in paragraph (f)(1)(ii) of this section. However, if the required documentation was not received by the withholding agent before the time the payment was made or within the grace period specified in paragraph (f)(2)-(ii)(A) of this section, then the Commissioner, or his or her delegate, may require additional proof if it determines that the delays in obtaining the required documentation affect its reliability. The withholding agent will be liable for interest under section 6601 regardless of whether the underlying tax liability is due. In addition, the withholding agent may be subject to penalties.

(6) *Reportable payment.* Solely for purposes of the presumptions in this paragraph (f), a reportable payment is any payment of income subject to

withholding (as defined in §1.1441-2(a)) or any payment described in section 3406(b), notwithstanding the provisions in sections 6041, 6041A, 6042, 6044, 6045, 6049, 6050A, 6050N and the regulations under those sections that provide exemptions from reporting based upon the status of the payee as a foreign person. For example, a payment of interest described in §1.6049-5(b)-(14) as a non-reportable payment if paid to a foreign person is treated as a reportable payment for purposes of this paragraph (f). Accordingly, the withholding agent or payor must determine under the presumptions described in this paragraph (f) whether to treat the beneficial owner or payee as a foreign or U.S. person. See sections 6041 through 6049 and sections 6050A and 6050N and the regulations under those sections for reporting requirements for amounts treated as reportable payments for purposes of this paragraph (f).

(7) *Adjustment, refund, or credit of overwithheld tax.* If, as a result of the presumption rules of paragraph (f) of this section, the amount withheld under section 1441 is greater than the tax due, adjustments may be made in accordance with the procedures described in §1.1461-2(a). Alternatively, refunds or credits may be claimed in accordance with the procedures described in §1.1464-1, relating to refunds or credits claimed by the beneficial owner, or §1.6414-1, relating to refunds or credits claimed by the withholding agent. If an amount was withheld under section 3406, see §31.6413(a)-3(a)(1) of this chapter.

(g) *Effective date*—(1) *In general.* This section applies to payments of income made after December 31, 1997.

(2) *Transition rules.* For purposes of paragraph (e)(2)(i) and (d)(2)(ii) of this section, a withholding agent that holds a valid Form W-8, 1001, 4224, 1078, or a statement described in §1.1441-5(b) (as contained in 26 CFR Part 1, edition revised April 1, 1995) on the date that is 60 days after these regulations are published as final regulations in the Federal Register may treat it as a valid withholding certificate until its validity expires under applicable provisions as in effect on April 22, 1996. In addition, the documentation requirements for dividends on stock traded on a U.S. established financial market described in §1.1441-6(b)(2) shall apply only to accounts established after the date that is 60

days after these regulations are published as final regulations in the Federal Register. For accounts established on or before that date, the documentation requirements under this section shall apply to payments made after December 31, 1999.

Par. 7. Section 1.1441-2 is revised to read as follows:

§1.1441-2 Income subject to withholding.

(a) *In general.* For purposes of the regulations under section 1441, the term *income subject to withholding* means items of income from sources within the United States (not including items listed in paragraph (d)(1) of this section) that constitute either fixed or determinable annual or periodical income described in paragraph (b) of this section or other income subject to withholding described in paragraph (c) of this section. Withholding applies to the gross amount of the payment made to a foreign person. See part I (section 861 and following), subchapter N, chapter 1 of the Internal Revenue Code, and the regulations under such part for rules governing the determination of the source of income. See section 884(f) and the regulations thereunder to determine the circumstances under which interest paid by a foreign corporation is U.S. source income.

(b) *Fixed or determinable annual or periodical income*—(1) *In general.* For purposes of chapter 3 of the Internal Revenue Code, fixed or determinable annual or periodical income is all income included in gross income under section 61 (including original issue discount), except for the items listed in paragraph (b)(2) of this section.

(2) *Exceptions.* For purposes of chapter 3 of the Internal Revenue Code, the items of income described in this paragraph (b)(2) are not fixed or determinable annual or periodical income—

(i) Gains derived from the sale of property (including market discount and option premiums), except for gains described in paragraph (b)(3) or (c) of this section;

(ii) Insurance premiums within the meaning of section 4372 paid to a foreign insurer or reinsurer;

(iii) Items of U.S. source income that are excluded from gross income

under any provision of law without regard to the identity of the holder, such as interest excluded from gross income under section 103(a); and

(iv) Any other income that the Internal Revenue Service may determine, in published guidance, is not fixed or determinable annual or periodical income.

(3) *Original issue discount.* Amounts of original issue discount are fixed or determinable annual or periodical income. However, based on the authority of section 1441(c)(8), only the original issue discount described in this paragraph (b)(3) may be subject to withholding.

(i) *Amounts paid by original issuer.* Amounts paid by the original issuer (or its paying agent) to the beneficial owner on any obligation issued after March 31, 1972 and payable more than 6 months from the date of original issue that represent original issue discount realized by the beneficial owner upon the retirement of the obligation, or upon payment by the issuer on the obligation, to the extent that the amount is subject to tax under section 871(a)(1)(C) or under section 881(a)(3). This paragraph (b)(3)(i) only applies to original issue discount as defined in section 1273(a)(1). Therefore, it does not apply to market discount as defined in section 1278(a)(2).

(ii) *Amounts paid by related obligor.* Amounts paid by the obligor (or its paying agent) on obligations issued after the date that is 60 days after these regulations are published as final regulations in the Federal Register and payable more than 6 months from the date of original issue representing an amount of original issue discount if the obligor is related to the original issuer (within the meaning of section 163(e)(3)), to the extent such accrued amount is subject to tax under section 871(a)(1)(C)(ii) or under section 881(a)(3)(B).

(iii) *Amounts paid in a sale between related parties.* Amounts paid on the sale or exchange of obligations issued after the date that is 60 days after these regulations are published as final regulations in the Federal Register and payable more than 6 months from the date of original issue representing an amount of original issue discount if the seller is related to the purchaser within the meaning of section 163(e)(3), to the extent such accrued amount is subject

to tax under section 871(a)(1)(C)(i) or under section 881(a)(3)(A).

(iv) *Amounts actually known to be taxable original issue discount.* Amounts paid on obligations issued after the date that is 60 days after these regulations are published as final regulations in the Federal Register and payable more than 6 months from the date of original issue representing an amount of original issue discount if the obligor (or the seller in the case of a sale or exchange of obligations) has actual knowledge of the amount subject to tax under section 871(a)(1)(C) or under section 881(a)(3).

(v) *Amounts for which required documentation is not furnished.* Any amount of original issue discount paid on obligations issued after the date that is 60 days after the publication of these regulations as final regulations in the Federal Register and payable more than 6 months from the date of original issue representing an amount that fails to qualify as portfolio interest under section 871(h) or 881(c) (because of the failure to furnish the statement described in section 871(h)(5) and §1.871-14(c)(2)), to the extent the amount is subject to tax under section 871(a)(1)(C)(ii) or under section 881(a)(3)(B). The applicable rate of withholding tax shall be applied to the entire amount of stated interest, if any, and original issue discount on the obligation as determined on the date of original issue if the withholding agent does not know what proportion of the payment on the obligation represents taxable income. Adjustments to any amount of overwithheld tax may be made in compliance with the procedures described in §1.1461-2(a). Alternatively, refunds may be claimed in compliance with the procedures in §1.1464-1.

(4) *Securities lending transactions.* [Reserved]

(c) *Other income subject to withholding.* Withholding is also required on the gross amount of the following items of income:

(1) Gains described in sections 631(b) or (c), relating to treatment of gain on disposal of timber, coal, or domestic iron ore with a retained economic interest.

(2) Gains subject to the 30 percent tax under section 871(a)(1)(D) or section 881(a)(4), relating to contingent payments received from the sale or exchange of patents, copyrights, and similar intangible property.

(d) *Items of income not subject to withholding under section 1441—(1) Exemptions for which no withholding certificate or documentation is required.* The items of income described in this paragraph (d)(1) are not subject to withholding of tax under section 1441 regardless of the fact that no withholding certificate or other documentation has been furnished to establish foreign or U.S. status.

(i) Portfolio interest paid on bearer obligations that are described in section 871(h)(2)(A) or 881(c)(2)(A) and §1.871-14(b). See §1.6049-5(b)(7) regarding exemption from reporting under section 6049, and thus, from backup withholding under section 3406.

(ii) Original issue discount on any obligation payable less than 6 months from the date of original issue described in section 871(g)(1)(B)(i). See §1.6049-5(b)(10), (11), and (14) for exemptions from reporting under section 6049, and thus, from backup withholding under section 3406.

(iii) Any amount of original issue discount not described in paragraph (b)(3) of this section. See §1.6049-5(b)(10) and (11) for exemptions from reporting under section 6049, and thus, from backup withholding under section 3406.

(iv) Proceeds from a wager placed by a nonresident alien individual in the games of blackjack, baccarat, craps, roulette, or big-6 wheel.

(2) *Exemptions for portfolio interest and income on bank, etc. deposits requiring a withholding certificate or documentation—(i) In general.* No withholding is required under sections 1441(c)(9) and (c)(10) on interest and original issue discount that either qualifies as portfolio interest on an obligation in registered form described in section 871(h)(2)(B) or 881(c)(2)(B) (including interest on a foreign-targeted registered obligation described in §1.871-14(e)) or is paid on deposits described in section 871(i)(2)(A). A withholding agent may exempt from withholding an amount of interest and original issue discount paid on deposits described in section 871(i)(2)(A) only if, prior to the payment, the withholding agent complies with the procedures described in §1.871-14(c). The preceding sentence does not apply to amounts of original issue discount described in paragraph (d)(1)(ii) of this section or in §1.6049-5(b)(10) or (11).

(ii) *Transition rule.* The documentation requirements for interest on de-

posits described in section 871(i)(2)(A) shall apply to payments made after December 31, 1997 with respect to accounts established after the date that is 60 days after these regulations are published as final regulations in the Federal Register. For accounts established on or before that date, the documentation requirements under this section shall apply to payments made after December 31, 1999.

(e) *Payment*—(1) *General rule.* A payment is considered made when the amount would be includible in the income of the beneficial owner under the U.S. tax principles governing the cash basis method of accounting. A payment is considered made whether it is made directly to the beneficial owner or paid to another person for the benefit of the beneficial owner (e.g., to the agent of the beneficial owner). Thus, a payment of income is considered made to a beneficial owner if it is paid in complete or partial satisfaction of the beneficial owner's debt to a creditor.

(2) *Income allocated under section 482.* A payment is considered made to the extent income subject to withholding is allocated under section 482. Further, income arising as a result of a secondary adjustment made in conjunction with a reallocation of income under section 482 from a foreign person to a related U.S. person is considered paid to a foreign person unless the taxpayer to whom the income is reallocated has entered into a repatriation agreement with the Internal Revenue Service and the agreement eliminates the liability for the withholding tax. For purposes of determining the liability for withholding tax, the payment of income is deemed to have occurred on the dates of the transactions that give rise to the allocation of income and the secondary adjustments, if any.

(3) *Blocked income.* Income is not considered paid if it is blocked under executive authority, such as the President's exercise of emergency power under the Trading with the Enemy Act, 50 U.S.C. App. 5, or the International Emergency Economic Powers Act, 50 U.S.C. 1701 et seq. However, on the date that the blocking restrictions are removed, the income that was blocked is considered constructively received by the beneficial owner (and therefore paid for purposes of this section) and subject to withholding under §1.1441-1.

(4) *Special rules for dividends.* For purposes of sections 1441 and 6042, in

the case of stock for which the record date is earlier than the payment date, dividends are considered paid on the payment date. In the case of a corporate reorganization, if a beneficial owner is required to exchange stock held in a former corporation for stock in a new corporation before dividends that are to be paid with respect to the stock in the new corporation will be paid on such stock, the dividend is considered paid on the date that the payee or beneficial owner actually exchanges the stock and receives the dividend. See §31.3406(a)-4(a)(2) of this chapter.

(5) *Certain interest accrued by a foreign corporation.* For purposes of sections 1441 and 6049, a foreign corporation shall be treated as having made a payment of interest as of the last day of the taxable year if it has made an election under §1.884-4(c)(1) to treat accrued interest as if it were paid in that taxable year.

(6) *Payments other than in U.S. dollars.* For purposes of section 1441, a payment includes amounts paid in a medium other than U.S. dollars. See §1.1441-3(e) for rules regarding the amount subject to withholding in the case of such payments.

(f) *Effective date.* This section applies to payments of income made after December 31, 1997.

Par. 8. Section 1.1441-3 is amended by:

1. Revising the heading of the section.
2. Revising paragraphs (a) through (e).
3. Removing paragraph (f).
4. Redesignating paragraph (j) as paragraph (f).
5. Revising paragraph (g).
6. Removing paragraphs (h) and (i).
7. Removing the OMB parenthetical and the authority citation at the end of the section.

The revisions read as follows:

§1.1441-3 Amounts subject to withholding.

(a) *Withholding on gross amount.* Except as otherwise provided in regulations under section 1441, the amount subject to withholding under §1.1441-1 is the gross amount of income subject to withholding. The gross amount of income subject to withholding may not

be reduced by any deductions, except to the extent that one or more personal exemption is allowed as provided under §1.1441-4(b)(6).

(b) *Withholding on payments on certain obligations*—(1) *Withholding at time of payment of interest.* When making a payment on an interest-bearing obligation, a withholding agent must withhold under §1.1441-1 upon the gross amount of stated interest payable on the interest payment date, regardless of whether the payment constitutes a return of capital or the payment of income within the meaning of section 61. To the extent an amount was withheld on an amount of capital rather than interest, adjustments to any amount of overwithheld tax may be made under the procedures described in §1.1461-2(a). Alternatively, refunds or credits may be claimed by the beneficial owner under the procedures described in §301.6402-2 of this chapter.

(2) *No withholding between interest payment dates*—(i) *In general.* A withholding agent is not required to withhold tax under §1.1441-1 upon interest accrued on the date of a sale of debt obligations when that sale occurs between two interest payment dates, even though the interest is subject to tax under section 871 or section 881. See §1.6045-1(c) for reporting requirements by brokers with respect to sale proceeds. The exemption from withholding granted by this paragraph (b)(2) is not subject to the withholding certificate procedures described in §1.1441-1(e)(1). However, the exception is not a determination that the accrued interest is not fixed or determinable annual or periodical income.

(ii) *Anti-abuse rule.* The exemption in paragraph (b)(2)(i) of this section does not apply if the sale of securities is part of a plan the principal purpose of which is to avoid tax by selling and repurchasing securities and the withholding agent has actual knowledge or reason to know of such plan.

(c) *Corporate distributions*—(1) *General rule.* Subject to the provisions of this paragraph (c), a corporation making a distribution with respect to its stock is not required to withhold under section 1441, 1442, or 1443 on the portion of the distribution—

(i) That is treated as a nontaxable distribution payable in stock or stock rights;

(ii) That is treated as a distribution in part or full payment in exchange for stock;

(iii) That is not paid out of accumulated earnings and profits or current earnings and profits;

(iv) That is paid by a regulated investment company and is a capital gain dividend (as defined in section 852(b)(3)(C)) or an exempt interest dividend (as defined in section 852(b)(5)(A)); or

(v) That is paid by a real property holding corporation (defined in section 897(c)(2)) or a real estate investment trust (defined in section 856) and is subject to withholding under section 1445 and the regulations under that section.

(2) *Determination of accumulated and current earnings and profits on the date of payment*—(i) *General rule.* In order for a corporation to determine the amount of withholding tax due on any distribution with respect to stock, the distributing corporation may, at its option, either treat the entire distribution as a dividend as defined in section 316 or may treat only a portion of the distribution as a dividend if, prior to, and at a time reasonably close to the date of payment, the distributing corporation makes a reasonable estimate of the portion of the distribution that is not a dividend based upon expected earnings and profits as relevant facts and circumstances shall indicate. A reasonable estimate may be made based on the procedures described in §31.3406(b)(2)–4(c)(2) of this chapter.

(ii) *Procedures in case of underwithholding.* A distributing corporation that determines at the end of the taxable year of the distribution that it underwithheld under section 1441 shall be liable under section 1461 for the amount underwithheld. No penalties shall be imposed for failure to withhold and deposit tax if—

(A) The corporation made a reasonable estimate as provided in paragraph (c)(2)(i) of this section; and

(B) Either—

(1) The corporation pays over the underwithheld amount on or before the date that it is required to file a return on Form 1042 for the calendar year of the distribution pursuant to §1.1461–2(b); or

(2) The corporation is not a calendar year taxpayer and it files an amended return on Form 1042X (or such other form as the Commissioner may prescribe) for the calendar year in which the distribution is made and pays the

additional amount of tax and interest within 60 days of the close of the taxable year of the distribution.

(iii) *Reliance on reasonable estimate by intermediary.* For purposes of determining whether the payment of a corporate distribution is a dividend, a withholding agent that is not the distributing corporation may rely on representations made by the distributing corporation regarding the reasonable estimate of expected earnings and profits made pursuant to paragraph (c)(2)(i) of this section. Failure by the withholding agent to withhold the required amount due to an erroneous estimate that the Internal Revenue Service has determined was not reasonably made shall be imputed to the distributing corporation. Therefore, the Internal Revenue Service may collect any additional amount from the distributing corporation and subject the corporation to applicable interest and penalties as a withholding agent.

(3) *Special rules in the case of distributions from a regulated investment company.* If the amount of distributions designated as subject to section 852(b)(3)(C) or 852(b)(5)(A) exceeds the amount permitted to be designated under those sections for the taxable year, then no penalties will be asserted for any resulting underwithholding provided the designations were based on a reasonable estimate (made pursuant to paragraph (c)(2)(i) of this section) and adjustments to the amount withheld are made within the time period described in paragraph (c)(2)(ii)(B) of this section. Any adjustment to the amount of tax due and paid to the Internal Revenue Service by the withholding agent as a result of underwithholding shall not be treated as a distribution for purposes of section 562(c) and the regulations thereunder. Any amount of U.S. tax that a foreign shareholder is treated as having paid on the undistributed capital gain of a regulated investment company under section 852(b)(3)(D) may be claimed by the foreign shareholder as a credit or refund under §1.1464–1. The procedures described in paragraph (c)(2)(iii) of this section shall apply in the case of distributions made to an intermediary.

(4) *Overwithholding of tax.* If the tax on any distribution has been overwithheld, adjustments may be made in accordance with the procedures described in §1.1461–2(a). Alternatively, refunds or credits may be claimed in accordance with §1.1464–1,

relating to refunds or credits claimed by the beneficial owner, or §1.6414–1, relating to refunds or credits claimed by the withholding agent.

(d) *Withholding on certain gains.* Absent actual knowledge or reason to know otherwise, a withholding agent may rely on a claim regarding the amount of gain described in §1.1441–2(c) if the beneficial owner withholding certificate, or other appropriate withholding certificate, states the beneficial owner's basis in the property giving rise to the gain. In the absence of a withholding certificate, the withholding agent may withhold an amount under §1.1441–1 that is necessary to assure that the tax withheld is not less than 30 percent of the recognized gain. For this purpose, the recognized gain is determined without regard to any deduction allowed by the Internal Revenue Code from the gains. The amount so withheld shall not exceed 30 percent of the amount payable by reason of the transaction giving rise to the recognized gain. Adjustments to any amount of overwithheld tax may be made in accordance with the procedures described in §1.1461–2(a). Alternatively, refunds or credits may be claimed in accordance with §1.1464–1, relating to refunds or credits claimed by the beneficial owner, or §1.6414–1, relating to refunds or credits claimed by the withholding agent.

(e) *Payments other than in U.S. dollars*—(1) *In general.* The amount of a payment made in a medium other than U.S. dollars is measured by the fair market value of the property or services provided in lieu of U.S. dollars. The withholding agent may liquidate the property prior to payment in order to withhold the required amount of tax under section 1441 or obtain payment of the tax from an alternative source. However, the obligation to withhold under section 1441 is not deferred even if no alternative source can be located. Thus, for purposes of withholding under chapter 3 of the Internal Revenue Code, the provisions of §31.3406(h)–2(b)(2)(ii) of this chapter (relating to backup withholding from another source) shall not apply. If the withholding agent satisfies the tax liability related to such payments, the rules of paragraph (e)(3) of this section apply.

(2) *Payments in foreign currency.* If the amount subject to withholding tax is paid in a currency other than the

U.S. dollar, the amount of withholding tax under section 1441 shall be determined by applying the applicable rate of withholding to the foreign currency amount and converting the amount withheld into U.S. dollars on the date of payment at the spot rate (as defined in §1.988-1(d)(1)) or pursuant to a reasonable spot rate convention. For example, a withholding agent may use a month-end spot rate or a monthly average spot rate. A spot rate conven-

tion must be used consistently for all non-dollar amounts withheld and from year to year. Such convention cannot be changed without the consent of the Commissioner. The U.S. dollar amount so determined shall be treated by the beneficial owner as the amount of tax paid on the income for purposes of determining the final U.S. tax liability and, if applicable, claiming a refund or credit of tax.

(3) *Tax liability of beneficial owner*

satisfied by withholding agent—(i) General rule. In the event the satisfaction of a tax liability of a beneficial owner by a withholding agent constitutes income to the beneficial owner and such income is of a type that is subject to withholding, the amount of the payment deemed made by the withholding agent for purposes of this paragraph (e)(3) shall be determined under the following gross-up formula:

$$\text{Payment} = \frac{\text{Gross payment without withholding}}{1 - (\text{tax rate})}$$

(ii) *Example.* The following example illustrates the provisions of this paragraph (e)(3):

Example. College X awards a qualified scholarship within the meaning of section 117(b) to foreign student, FS, who is in the United States on an F visa. FS is a resident of a country that does not have an income tax treaty with the United States. The scholarship is \$20,000 to be applied to tuition, mandatory fees and books, plus benefits in kind consisting of room and board and roundtrip air transportation. College X agrees to pay any U.S. income tax owed by FS with respect to the scholarship. The fair market value of the room and board measured by the amount College X charges non-scholarship students is \$6,000. The cost of the roundtrip air transportation is \$2,600. Therefore, the total fair market value of the scholarship received by FS is \$28,600. However, the amount taxable is limited to the fair market value of the benefits in kind (\$8,600) because the portion of the scholarship amount for tuition, fees, and books is not included in gross income under section 117. Under the gross-up formula, College X is deemed to make a payment of \$10,000 (\$8,600 divided by 1-.14). The U.S. tax that must be deducted and withheld from the payment under section 1441(b) is \$1,400 (.14 × \$10,000). College X reports scholarship income of \$30,000 and \$1,400 of U.S. tax withheld on Forms 1042 and 1042-S.

* * * * *

(g) *Effective date.* This section applies to payments of income made after December 31, 1997.

Par. 9. Section 1.1441-4 is amended by:

1. Revising the section heading.
2. Revising paragraphs (a) and (b)(1)(ii).
3. Adding paragraph (b)(1)(vi).
4. Revising the last sentence of paragraph (b)(2)(i).
5. Revising the introductory text of paragraph (b)(2)(ii).
6. Paragraph (b)(2)(ii) is amended by:

- a. Revising paragraph (b)(2)(ii)(A).
- b. Redesignating paragraph (b)(2)-(ii)(H) as paragraph (b)(2)(ii)(J) and amending newly designated paragraph (b)(2)(ii)(J) by removing the period and adding “; and” in its place.
- c. Redesignating paragraphs (b)(2)-(ii)(B), (C), (D), (E), (F) and (G) as paragraphs (b)(2)(ii)(D), (E), (F), (G), (H) and (I), respectively.
- d. Adding new paragraphs (b)(2)(ii)-(B), (C), and (K).
- e. Amending newly designated paragraph (b)(2)(ii)(I) by removing the language “, and” and adding a semicolon in its place.
- f. Amending newly designated paragraphs (b)(2)(ii)(D), (E), (F), (G), and (H) by removing the comma at the end of the paragraphs and adding a semicolon in its place.

7. The concluding text of paragraph (b)(2)(iv) is amended by:

- a. Removing the language “ten” and adding “20” in its place.
- b. Removing the language “Director of Foreign Operations” and adding “Assistant Commissioner (International)” in its place.
8. Revising paragraph (b)(2)(v).
9. Adding paragraph (b)(2)(vi).
10. Adding paragraph (b)(6).
11. Revising paragraphs (c), (d), (e), and (f).
12. Removing paragraphs (g), (h), and (i).
13. Removing the OMB parenthetical and the authority citation at the end of the section.

The revisions and additions read as follows:

§1.1441-4 Certain exemptions from withholding.

(a) *Certain income connected with a U.S. trade or business—(1) In general.* No withholding is required under section 1441 on income otherwise subject to withholding if the income is (or is deemed to be) effectively connected with the conduct of a trade or business within the United States and is includible in the beneficial owner’s gross income for the taxable year. For purposes of this paragraph (a), an amount is not deemed to be includible in gross income if the amount is (or is deemed to be) effectively connected with the conduct of a trade or business within the United States and the beneficial owner claims an exemption from tax under an income tax treaty because the income is not attributable to a permanent establishment in the United States. To claim a reduced rate of withholding because the income is not attributable to a permanent establishment, see §1.1441-6(b)(1). This paragraph (a) does not apply to income of a foreign corporation to which section 543(a)(7) applies for the taxable year or to compensation for personal services performed by an individual. See paragraph (b) of this section for compensation for personal services performed by an individual.

(2) *Withholding agent’s reliance on a claim of effectively connected income—(i) In general.* Absent actual knowledge or reason to know otherwise, a withholding agent may rely on a claim of exemption based upon paragraph (a)(1) of this section if, prior to the payment to the foreign person, the withholding agent complies with the requirements of §1.1441-1(e)(1) and is

furnished either a beneficial owner withholding certificate (including one that is transmitted with an intermediary withholding certificate described in §1.1441-1(e)(3)(iv)), or an intermediary withholding certificate described in §1.1441-1(e)(3)(ii) from a partnership acting for its own account (regardless of whether the distributive share information is stated on the certificate and whether the certificates described in §1.1441-1(e)(3)(iii)(C) are attached). For purposes of this paragraph (a), a withholding certificate is not valid unless it includes a taxpayer identifying number. A statement on the withholding certificate that the income is effectively connected with the conduct of a trade or business in the United States and that the income will be reported by the beneficial owner on an income tax return will satisfy the requirement of §1.1441-1(e)(2)(ii) or (e)(3)(iii) that the certificate describe the basis for the claim of reduced rate. A withholding agent may presume that the income is not effectively connected with the conduct of a trade or business in the United States if the withholding certificate is silent or if the withholding agent cannot associate the payment with the required documentation (as defined in §1.1441-1(f)(1)). See §1.1441-1(e)(4)(ii)(B)(2) for the period of validity applicable to a certificate provided under this section. A withholding certificate shall be effective only for the item or items of income specified therein. In compliance with §1.1441-1(e)(3)(ii)(A), the validity of the certificate expires when subsequent circumstances arising during the taxable year indicate that the income to which the certificate relates is not, or is no longer expected to be, effectively connected with the conduct of a trade or business within the United States.

(ii) *Exemption of certain foreign partnerships and foreign corporations.* [Reserved] For guidance prior to the date these regulations are published as final regulations in the Federal Register, see §1.1441-4(f) as contained in the 26 CFR Part 1, edition revised April 1, 1995.

(iii) *Payment to joint owners.* In the case of payments to joint owners, a withholding certificate must be provided by each beneficial owner claiming a reduced rate certifying that the income is effectively connected with the conduct of a trade or business within the United States.

(3) *Income on notional principal contracts.* A withholding agent that pays income attributable to a notional principal contract described in §1.863-7(a) shall have no obligation to withhold on the amounts paid under the terms of the notional principal contract regardless of whether a withholding certificate is provided. For rules regarding the obligation to file a return, see §§1.1461-1(c)(1)(i) and 1.6041-1(d)(5).

(4) *Failure to act in accordance with presumption.* A withholding agent that does not withhold, contrary to the presumption set forth in paragraph (a)(2) of this section that income is not effectively connected with the conduct of a trade or business within the United States, shall be liable for the tax imposed under section 1461, without the benefit of a reduced rate, unless the withholding agent can demonstrate to the satisfaction of the District Director or the Assistant Commissioner (International) that the income is effectively connected and was included in the Federal income tax return of the beneficial owner and that the proper amount of tax, if any, has been paid to the Internal Revenue Service. Proof of payment of tax may be established on the basis of a Form 4669 (or such other form as the Internal Revenue Service may prescribe) establishing the amount of tax, if any, actually paid by the beneficial owner on the income. Proof that a reduced rate of withholding was appropriate may be established by an appropriate withholding certificate described in §1.1441-1(e)(1)(i). However, if the required documentation was not received by the withholding agent before the time the payment was made or within the period specified in §1.1441-1(f)(2)(i)(B)(J), then the District Director or the Assistant Commissioner (International) may require additional proof if it determines that the delays in obtaining the required documentation affect its reliability. The withholding agent will be liable for interest under section 6601 regardless of whether the underlying tax liability is due. In addition, the withholding agent may be subject to penalties.

(b) *Compensation for personal services of an individual—(1) Exemption from withholding.* * * *

* * * * *

(ii) Such compensation that would be subject to withholding under section

3402 but for the provisions of section 3401(a) (not including paragraph (a)(6) of that section) and the regulations under that section. This paragraph (b)(1)(ii) does not apply to payments to a nonresident alien individual from any trust described in section 401(a), any annuity plan described in section 403(a), or any annuity, custodial account, or retirement income account described in section 403(b). Thus, for example, payments to a nonresident alien individual from a trust described in section 401(a) are subject to withholding under section 1441 and not under section 3405 or 3406.

* * * * *

(vi) Compensation that is exempt from withholding under section 3402 by reason of section 3402(e), provided that the employee and his employer enter into an agreement under section 3402(p) to provide for the withholding of income tax upon payments of amounts described in §31.3401(a)-3(b)(1) of this chapter. An employee who desires to enter into such an agreement should furnish his employer with Form W-4 (withholding exemption certificate) (or such other form as the Internal Revenue Service may prescribe). See section 3402(f) and the regulations thereunder and §31.3402(p)-1 of this chapter.

(2) *Manner of obtaining withholding exemption under tax treaty—(i) In general.* * * * The exemption from withholding becomes effective for payments made at least 20 days after a copy of the accepted statement is forwarded to the Assistant Commissioner (International).

(ii) *Statement claiming withholding exemption.* The statement claiming an exemption from withholding shall be made on Form 8233 (or an acceptable substitute). Form 8233 shall be dated, signed by the beneficial owner under the penalties of perjury, and contain the following information:

(A) The individual's name, permanent residence address, taxpayer identifying number, and the U.S. visa number, if any;

(B) The individual's current immigration status and visa type;

(C) The individual's original date of entry into the United States;

* * * * *

(K) Any other information as the form may require.

(v) *Copies of Form 8233.* The withholding agent shall forward one copy of each Form 8233 that is accepted under paragraph (b)(2)(iv) of this section to the Assistant Commissioner (International), within five days of his or her acceptance. The Assistant Commissioner (International) may review the forms so submitted. The withholding agent shall retain a copy of Form 8233.

(vi) *Electronic filing.* Under procedures published by the Internal Revenue Service, Forms 8233 may be filed electronically with the Internal Revenue Service.

(6) *Personal exemption*—(i) *In general.* To determine the tax to be withheld at source under §1.1441-1 from remuneration paid for personal services performed within the United States by a nonresident alien individual and from scholarship and fellowship income described in paragraph (c) of this section, a withholding agent may take into account one personal exemption pursuant to sections 873(b)(3) and 151 regardless of whether the income is effectively connected. The exemption does not need to be prorated for purposes of withholding under section 1441.

(ii) *Multiple exemptions.* More than one personal exemption may be claimed in the case of a resident of a contiguous country or a national of the United States under section 873(b)(3). In addition, residents of a country with which the United States has an income tax treaty in effect may be eligible to claim more than one personal exemption if the treaty so provides. Claims for more than one personal exemption shall be made on the withholding certificate furnished to the withholding agent. The exemptions do not need to be prorated for purposes of withholding under section 1441.

(iii) *Special rule where both scholarship and compensation income is received.* The fact that both scholarship income and compensation income are received during the taxable year does not entitle the taxpayer to claim more than one personal exemption amount (or more than the additional amounts permitted under paragraph (b)(6)(ii) of this section). Thus, if a nonresident alien student receives taxable scholar-

ship amounts from one payor and compensation income from another payor, no more than the total personal exemption amount permitted under the Internal Revenue Code or under an income tax treaty may be taken into account by both payors.

(c) *Special rules for scholarship and fellowship income*—(1) *In general.* Under section 871(c), certain amounts paid as a scholarship or fellowship for study, training, or research in the United States to a nonresident alien individual temporarily present in the United States as a nonimmigrant under subparagraph (F), (J), (M), or (Q) of section 101(a)(15) of the Immigration and Nationality Act are treated as income effectively connected with the conduct of a trade or business within the United States. Such amounts (as described in the second sentence of section 1441(b)) are subject to withholding tax under section 1441, but at the lower rate of 14 percent. That rate may be reduced under the provisions of an income tax treaty. Claims of a reduced rate under an income tax treaty shall be made under the procedures described in §1.1441-6(b)(1). Therefore, claims for amounts described in this paragraph (c)(1) may not be shown on a Form 8233. However, if the payee is receiving both compensation for personal services and income described in this paragraph (c)(1) from the same withholding agent, claims for both types of income may be shown on Form 8233.

(2) *Alternate withholding election.* A withholding agent may elect to withhold on the amounts described in paragraph (c)(1) of this section at the rates applicable under section 3402, as if the income were wages. Such election shall be made by obtaining a Form W-4 (or an acceptable substitute or such other form as the Internal Revenue Service may prescribe) from the beneficial owner. Such Form W-4 shall also serve as notice to the beneficial owner that the income is being treated as wages for purposes of withholding tax under section 1441.

(d) *Annuities received under qualified plans.* Withholding is not required under section §1.1441-1 in the case of any amount received as an annuity if the amount is exempt from tax under section 871(f) and the regulations under that section. A statement on the beneficial owner withholding certificate that the annuity is

excluded from gross income by reason of section 871(f) and the basis for that exclusion satisfies the requirement of §1.1441-1(e)(2)(ii) that the beneficial owner state the basis for the claim of reduced rate. A beneficial owner withholding certificate furnished for purposes of claiming the benefits of the exemption under this paragraph (d) is not valid unless it includes a taxpayer identifying number. See §1.1441-1(f)(3)(ii) regarding applicable presumptions if the withholding agent does not hold the required documentation prior to payment.

(e) *Income of a foreign central bank of issue or the Bank for International Settlements.* Section 895 provides for the exclusion from gross income of certain income derived by a foreign central bank of issue, or by the Bank for International Settlements, from obligations of the United States or of any agency or instrumentality thereof or from bank deposits. Absent actual knowledge or reason to know that a foreign central bank of issue, or the Bank for International Settlements, is operating outside the scope of the exclusion granted by section 895, the withholding agent may rely on a claim of exemption if, prior to making the payment, the withholding agent complies with the requirements of §1.1441-1(e)(1). The following statement on a beneficial owner withholding certificate satisfies the requirement in §1.1441-1(e)(2)(ii) that the beneficial owner state the basis for the claim of reduced rate:

(1) The bank is a foreign central bank of issue, or the Bank for International Settlements; and

(2) The bank does not, and will not, hold the obligations or the bank deposits covered by the withholding agreement for, or use them in connection with, the conduct of a commercial banking function or other commercial activity.

(f) *Effective date*—(1) *General rule.* This section applies to payments of income made after December 31, 1997.

(2) *Transition rules.* A withholding agent that holds a valid Form 4224 on a date that is 60 days after the date these regulations are published as final regulations in the Federal Register may treat it as a valid withholding certificate until its validity expires under applicable provisions as in effect on April 22, 1996.

§1.1441-4T [Removed]

Par. 10. Section 1.1441-4T is removed.

Par. 11. Section 1.1441-5 is revised to read as follows:

§1.1441-5 Withholding on payments to pass-through entities.

(a) *Domestic partnerships*—(1) *Exemption from withholding on payment to domestic partnerships.* A payment of income to a domestic partnership is not subject to withholding of tax under section 1441 even though it may have partners that are foreign persons. A payor (within the meaning of section 3406) may rely, in accordance with the procedures under §1.1441-1(d), on a Form W-9 furnished by the partnership.

(2) *Withholding by a domestic partnership*—(i) *In general.* A domestic partnership is required to withhold tax under §1.1441-1 as a withholding agent on the gross amount of items of income subject to withholding that are includible in the distributive share of income of a partner that is a foreign person. Pursuant to the authority provided under section 702(a), each partner shall take into account separately its distributive share of items of income subject to withholding, and thus the partnership, pursuant to section 703(a)(1), shall separately state these items of gross income when computing its taxable income. A partnership shall withhold when any distributions that include items of income subject to withholding are made. To the extent a foreign partner's distributive share of an item of income subject to withholding has not been actually distributed, the partnership is required to withhold on the partner's distributive share of that item of income on the earlier of the date that the statement required under section 6031(b) and §1.6031-1(b) to be provided to that partner is mailed or otherwise furnished to the partner or the due date for furnishing that statement as provided under §1.6031-1(b)(1). If a partnership withholds on a distributive share before the income is actually distributed to the partner, then withholding is not required when the income is subsequently distributed.

(ii) *Reliance on a partner's claim for reduced withholding.* Absent actual knowledge or reason to know other-

wise, a domestic partnership may rely on a claim for reduced withholding by a partner, if prior to the time the partnership is required to withhold, the partnership complies with the requirements of §1.1441-1(d) or (e)(1), whichever is applicable, with respect to the partner. See the presumptions described in §1.1441-1(f)(4)(iii)(A) applicable to a domestic partnership in determining the U.S. or foreign status of its partners.

(b) *Foreign partnerships*—(1) *In general.* A withholding agent must treat a payment to a foreign partnership as a payment to its partners, except to the extent the partnership is treated as a payee under §1.1441-1(c)(3)(ii). See §1.1441-1(e)(5)(v) for payments to a foreign partnership that claims to be a qualified intermediary. If the partnership is not treated as a payee, a withholding agent may, absent actual knowledge or reason to know otherwise, rely on a claim for a reduced rate of withholding by a partner if, prior to the payment, the withholding agent holds an intermediary withholding certificate described in §1.1441-1(e)(3)-(iii) pertaining to the partner. The certificate will be considered to pertain to the partner if the appropriate withholding certificate for the partner is attached to the intermediary withholding certificate. The appropriate withholding certificate for the partner may be a beneficial owner withholding certificate described in §1.1441-1(e)(2) (for a partner claiming to be a foreign person and a beneficial owner, determined under the provisions of §1.1441-1(c)(6)), the applicable certificates described in §1.1441-1(d)(2) (for a partner claiming to be a U.S. payee), an intermediary withholding certificate described in §1.1441-1(e)(3)(ii) or (iv) (for a partner that is a qualified intermediary or not otherwise acting for its own account), or an intermediary withholding certificate described in §1.1441-1(e)(3)(iii) representing that the income to which the certificate relates is effectively connected with the conduct of a trade or business in the United States. A claim must be presented for each portion of the payment that represents an item of income includible in the distributive share of the partner. When making a claim for several partners, the partnership may present a single intermediary withholding certificate to which the partners' certificates are attached.

(2) *Special rules in the case of tiered partnerships.* If a foreign or domestic partnership is a partner of a foreign partnership, the rules of this paragraph (b)(2) shall apply.

(i) A withholding agent may treat any portion of a payment made to a foreign partnership that represents an item of income includible in the distributive share of a partner (at any level in the chain of tiers) that is a domestic partnership as a payment to a U.S. person if the domestic partnership complies with the procedures described in §1.1441-1(d) (relating to the claim of U.S. status by a payee or beneficial owner).

(ii) A withholding agent may treat any portion of a payment made to a foreign partnership that represents an item of income includible in the distributive share of a partner (at any level in the chain of tiers) that is a foreign partnership as a payment to a foreign person if the withholding agent may treat the foreign partnership as the payee pursuant to the provisions in §1.1441-1(c)(3)(ii).

(iii) Where the partner in the foreign partnership to whom the payment is made (second tier) is a foreign partnership (first tier), the appropriate withholding certificate for the partner is an intermediary withholding certificate described in §1.1441-1(e)(3)(iii) issued by the second tier, and an intermediary withholding certificate described in §1.1441-1(e)(3)(iii) issued by the first tier to which is attached an appropriate withholding certificate for each of the partners of the first tier. The rules of this paragraph (b)(2)(iii) shall apply to any number of tiers of foreign partnerships.

(3) *Presumptions.* A withholding agent may apply the presumption described in §1.1441-1(f)(4)(ii) to any portion of a payment for which the withholding agent does not receive the required documentation (as defined in §1.1441-1(f)(1)(ii)).

(4) *Example.* The rules of this paragraph (b) may be illustrated by the following example:

Example. (i) *Facts.* FP is a foreign partnership organized under the laws of Country X deriving interest that would qualify as portfolio interest described in section 871(h)(2)(B) if the statement described in section 871(h)(5) is furnished. FP has three partners, A, B, and C. FP furnishes to the withholding agent an intermediary withholding certificate described in §1.1441-1(e)(3)(iii) to which it attaches a Form W-9 for A and a

beneficial owner withholding certificate for B. No documentation is attached for C.

(ii) *Analysis.* Absent actual knowledge or reason to know otherwise, the withholding agent may rely on A's Form W-9 to treat A as a U.S. person and, therefore, does not withhold on A's share of the payment. The withholding agent must comply with any information reporting obligations under sections 6042 (i.e., issue a Form 1099) with respect to A. Absent actual knowledge or reason to know otherwise, the withholding agent may also rely on B's claim for portfolio interest treatment for its share of the payment. The withholding agent must report the payment to B on Forms 1042 and 1042-S. Because the withholding agent cannot associate the required documentation (as defined §1.1441-1(f)(1)) for C's share of the interest income, the withholding agent may, for purposes of section 3406, treat that amount as a reportable payment made to a U.S. payee that is not an exempt recipient. See §1.1441-1(f)(4)(ii).

(c) *Trusts and estates.* [Reserved]

(d) *Effective date*—(1) *General rule.* This section applies to payments of income made after December 31, 1997.

(2) *Transition rules.* A withholding agent that holds a valid withholding certificate on the date that is 60 days after the date these regulations are published as final regulations in the Federal Register may treat it as a valid withholding certificate until its validity expires under applicable provisions as in effect on April 22, 1996.

Par. 12. Section 1.1441-6 is revised to read as follows:

§1.1441-6 Claim of a reduced rate of tax under an income tax treaty.

(a) *In general.* Under an income tax treaty in effect between the United States and a foreign country, the rate of tax to be withheld on a payment of income subject to withholding may be reduced if the beneficial owner of the income is a resident of the foreign country. Other requirements or conditions of the treaty, or revenue procedures issued thereunder, for claiming treaty benefits must also be satisfied, such as a limitation of benefits provision. If the requirements of this section are met, the amount withheld from the payment may be reduced at source to account for the treaty benefit. See also §1.1441-4(b)(2) for rules regarding claims of reduced rate of withholding under an income tax treaty in the case of compensation from personal services.

(b) *Reliance on claim of treaty benefits*—(1) *In general.* Absent actual knowledge or reason to know other-

wise, a withholding agent may rely on a claim that a beneficial owner is entitled to a reduced rate of withholding based upon an income tax treaty if, prior to the payment, the withholding agent complies with the requirements of §1.1441-1(e)(1). Except as otherwise provided in paragraph (b)(2) or (b)(3) of this section, for purposes of this paragraph (b)(1), a beneficial owner withholding certificate mentioned in §1.1441-1(e)(1) means a beneficial owner withholding certificate described in §1.1441-1(e)(2), that includes the beneficial owner's taxpayer identifying number and states that the taxpayer has complied with the advance ruling requirements described in paragraph (e) of this section (if applicable), and, if the beneficial owner is a person related to the withholding agent within the meaning of section 267(b) and 707(b), that the beneficial owner will file the statement required under §1.6114-1(b) (if applicable). The requirement to file an information return under section 6114 for income subject to withholding applies only to amounts paid during the calendar year that, in the aggregate, exceed \$500,000. See §301.6114-1(b) of this chapter. See paragraph (d) of this section for circumstances under which the withholding agent may be notified by the Internal Revenue Service that the certificate cannot be relied upon to grant benefits under an income tax treaty. A beneficial owner's taxpayer identifying number on a withholding certificate is valid for purposes of establishing proof of residence in a treaty country only if the taxpayer identifying number is certified by the Internal Revenue Service. However, absent actual knowledge or reason to know otherwise, a withholding agent may rely on a taxpayer identifying number that appears correct on its face, without having to inquire as to whether the taxpayer identifying number is certified, if the permanent residence address on the certificate is in the country whose tax treaty with the United States is invoked. See the confirmation and notification procedures described in §1.1441-1(e)(4)(iv) and (v).

(2) *Special rules for certain dividends.* In the case of dividends on stock traded on a U.S. established financial market, a withholding agent may rely on a beneficial owner withholding certificate described in §1.1441-1(e)(2). For this purpose, a U.S. established financial market is a

national securities exchange that is registered under section 6 of the Securities Exchange Act of 1934 (15 U.S.C. 78F), or an interdealer quotation system sponsored by a national securities association registered under section 15A of the Securities Exchange Act of 1934. In the case of payments made outside the United States (as defined in §1.6049-5(e)) with respect to an offshore account (as defined in §1.6049-5(d)(3)), a withholding agent may also consider that it holds a withholding certificate if it holds a certificate of residence described in paragraph (c)(3) of this section or documentary evidence described in paragraph (c)(4) of this section that the withholding agent has reviewed and maintains in its records. The withholding agent maintains the reviewed documents by retaining either the documents viewed or a photocopy thereof and noting in its records the date on which, and by whom, the documents were received and reviewed. This paragraph (b)(2) shall not apply to dividends that are exempt from withholding based on a claim that the dividends are effectively connected with the conduct of a trade or business in the United States.

(3) *Competent authorities agreement.* The procedures described in this section may be modified to the extent the U.S. competent authority may agree with the competent authority of a country with which the United States has an income tax treaty in effect.

(4) *Special rules for payments to certain foreign entities*—(i) *Determination of beneficial owner.* Under §1.1441-1(c)(6)(ii)(B), the tax principles in effect under the laws of the country whose tax treaty with the United States is invoked apply in certain cases to determine the beneficial owner of income entitled to claim a reduced rate of withholding under that income tax treaty. Thus, if a beneficial owner, as determined under §1.1441-1(c)(6)(ii)(B), is not a resident of the country whose law has been applied to determine beneficial owner status, then a payment to a foreign entity will not qualify for a reduced rate under that country's tax treaty with the United States even if the foreign entity receiving the payment is organized in that foreign country. Conversely, if a beneficial owner, as determined under §1.1441-1(c)(6)(ii)(B), is a resident of the country

whose law has been applied to determine beneficial owner status, then the beneficial owner's share of a payment to a foreign entity will qualify for a reduced rate under the applicable income tax treaty (provided other requirements for qualification are met) even if the foreign entity receiving the payment is not organized in, or is not a resident of, the foreign country in which the beneficial owner is resident.

(ii) *Withholding certificates.* The person claiming a reduced rate of tax under an income tax treaty shall apply the rules of §1.1441-1(c)(6)(ii)(B) and paragraph (b)(4)(i) of this section to determine the beneficial owner of income and entitlement to a reduced rate under an income tax treaty. The beneficial owner so determined may provide, as appropriate, a beneficial owner withholding certificate described in paragraph (b)(1) or (b)(2) of this section. Thus, for example, if the beneficial owner, as determined under §1.1441-1(c)(6)(ii)(B), is the interest holder rather than the entity, then the entity shall be treated as a foreign partnership for purposes of determining which withholding certificate is appropriate. If, conversely, the beneficial owner, as determined under §1.1441-1(c)(6)(ii)(B), is the entity rather than the interest holders, then the entity shall be treated as a corporation for purposes of determining which withholding certificate is appropriate.

(iii) *Request for dual treatment.* As set forth in §1.1441-1(c)(6)(ii)(B), a withholding agent may make payments to a foreign entity that is simultaneously claiming a reduced rate of tax on its own behalf and a reduced rate on behalf of persons in their capacity as interest holders in that entity. In such a case, the withholding agent may, at its option, accept such dual claims based, as appropriate, on beneficial owner withholding certificates described in paragraph (b)(1) or (2) of this section or documentary evidence described in §1.6049-5(c)(2)-(ii) furnished by such persons with respect to their respective share of such payments, even though the withholding agent holds different withholding certificates that requires it to treat the entity inconsistently with respect to different payments or with respect to different portions of the same payment. See paragraph (b)(4)(v) *Example 2* of this section.

(iv) *Reciprocal application by treaty partners.* Paragraph (b)(4) of this sec-

tion and the principles of §1.1441-1(c)(6)(ii)(B) will not apply if the U.S. competent authority determines that a treaty partner is not reciprocally applying the principles of §1.1441-1(c)(6)(ii)(B) to entities organized under the laws of the United States or to interest holders residing in the United States. In such case, the rules set forth in §1.1441-1(c)(6) shall apply without regard to the rules in §1.1441-1(c)(6)(ii)(B). This determination shall be effective upon publication of relevant guidance by the Service and shall apply prospectively only.

(v) *Examples.* This paragraph (b)(4) is illustrated by the following examples:

Example 1—(i) Facts. Entity A is a business organization formed under the laws of country Y that has an income tax treaty with the United States. Under the laws of country Y, A is subject to tax at the entity level and, therefore, is treated as the beneficial owner of income it receives and as a resident of country Y for purposes of the U.S.-Y tax treaty. A receives U.S. source royalties from withholding agent R and claims a reduced rate of withholding under the U.S.-Y tax treaty on its own behalf (rather than on behalf of its interest holders). A furnishes a beneficial owner withholding certificate described in paragraph (b)(1) of this section claiming to be the beneficial owner of the royalties.

(ii) *Analysis.* For purposes of claiming treaty benefits under the U.S.-Y treaty, A is treated as the beneficial owner of the royalties under §1.1441-1(c)(6)(ii)(B) since, under the tax law of country Y, A is required to include the royalties in income. R may treat A as the beneficial owner of the income for purposes of granting the benefit of a reduced rate under the U.S.-Y tax treaty.

Example 2—(i) Facts. The facts are the same as under *Example 1*, except that one of A's interest holders, T, is a corporation residing in country X. The U.S.-X tax treaty reduces the rate on royalties to zero whereas the rate on royalties under the U.S.-Y tax treaty is only reduced to 5 percent. Under the laws of country X, A is taxable on a flow-through basis and not at the entity level and T is required to include in income its distributive share of A's income. T claims to be the beneficial owner of its share of the royalty income paid to A and provides a beneficial owner certificate to A claiming the benefit of a zero rate under the U.S.-X tax treaty. A furnishes to R a beneficial owner withholding certificate for itself for the portion of the payment for which A alone claims to be the beneficial owner. In addition, it furnishes to R an intermediary withholding certificate described in §1.1441-1(e)(3)(iii) to which it attaches T's beneficial owner withholding certificate for the portion of the payment for which T claims to be the beneficial owner.

(ii) *Analysis.* For purposes of claiming treaty benefits under the U.S.-Y treaty, A is treated as the beneficial owner of all of the royalty income received from R under §1.1441-1(c)(6)(ii)(B), since, under the tax law of country Y (*i.e.*, under the laws of the country whose treaty benefits are claimed), A is subject to tax on that income.

However, for purposes of claiming benefits under the U.S.-X treaty, T may also be treated as the beneficial owner of its share of the royalty income under §1.1441-1(c)(6)(ii)(B), since, under the tax law of country X (*i.e.*, the laws of the country whose treaty benefits are claimed), T is required to include in income its share of A's income. Therefore, R may treat the royalty payment to a single foreign entity (A) as beneficially owned by different persons as a result of claims presented under different treaties. R may, at its option, grant dual treatment, that is, a reduced rate of zero percent under the U.S.-X treaty on the portion of the royalty payment for which T claims to be the beneficial owner and a reduced rate of 5 percent under the U.S.-Y treaty for the balance. However, under paragraph (b)(4)(iii) of this section, the withholding agent may, at its option, treat A as the sole beneficial owner of the royalty and grant benefits under the U.S.-Y treaty only.

Example 3. (i) Entity A is a business organization formed under the laws of country Y. A receives from withholding agent R U.S. source royalties and U.S. source interest income that is potentially eligible for the portfolio interest exemption under section 871(h) and 881(c) of the Internal Revenue Code. A's interest holders are S, an individual who resides in country Y, T, an individual who resides in country X, and U, an individual resident in the United States. The United States has a tax treaty with both country Y and country X. The U.S.-Y tax treaty reduces the rate on royalties to 5 percent, and the U.S.-X tax treaty reduces the rate to zero. A is classified as a partnership under U.S. tax principles. Under the tax laws of country Y, A is taxable on a flow-through basis, and S is required to include in income her distributive share of A's income. Under the tax laws of country X, A is taxable on a flow-through basis and T is required to include in income her distributive share of A's income. A furnishes R an intermediary withholding certificate described in §1.1441-1(e)(3)(iii) to which it attaches—

(A) A Form W-9 for U; and

(B) Beneficial owner withholding certificates for S and T that claim the portfolio interest exemption and a reduced rate of withholding under the U.S. treaties with Y and X, respectively.

(ii) *Analysis.* For purposes of claiming benefits under the U.S.-Y treaty, S is treated as the beneficial owner of his distributive share of royalty income received from R under §1.1441-1(c)(6)(ii)(B) since, under the tax law of country Y (*i.e.*, the laws of the country whose treaty benefits are claimed in the case of S), S is the person required to include in income her distributive share of the royalty. Therefore, R may withhold on S's proportionate share of the royalty income paid to A at the 5 percent rate under the U.S.-Y tax treaty. For purposes of claiming benefits under the U.S.-X tax treaty, T is treated as the beneficial owner of her distributive share of royalty income under §1.1441-1(c)(6)(ii)(B), since, under the laws of country X (*i.e.*, the laws of the country whose treaty benefits are claimed in the case of T), T is the person required to include in income her distributive share of the royalty. Therefore, R may withhold on T's proportionate share of the royalty income paid to A at the zero rate under the U.S.-X treaty, even though A is not organized in, or a resident of, country X. R may rely on U's Form W-9 to treat U as a U.S. person. Therefore, R does not withhold on U's

share of the royalty payment. R also does not withhold on any portion of the interest paid to A because S and T have furnished beneficial owner certificates and U has furnished a Form W-9.

(c) *Proof of tax residence in a treaty country*—(1) *In general.* A beneficial owner establishes proof of its tax residence in a treaty country for purposes of its claim to the withholding agent that a reduced rate of tax applies under an income tax treaty by complying with the procedures described in this paragraph (c) or with such other procedures as the Internal Revenue Service may prescribe in published guidance. For purposes of this section, the residence of a beneficial owner must be determined in accordance with the provisions of the applicable U.S. income tax treaty as may be clarified by any applicable regulations thereunder or technical explanations thereof, and any procedures issued by the Internal Revenue Service on the determination or proper method of certifying residence under particular income tax treaties.

(2) *Certification of taxpayer identifying number*—(i) *In general.* A taxpayer may certify its taxpayer identifying number as required under paragraph (b)(1) of this section by having the taxpayer identifying number certified by the Internal Revenue Service either directly as provided under paragraph (c)(2)(ii) of this section or through a qualified intermediary as provided in paragraph (c)(2)(iii) of this section.

(ii) *IRS-certified TIN.* The Internal Revenue Service may certify a taxpayer identifying number based upon a certificate of residence described in paragraph (c)(3) of this section or documentary evidence described in paragraph (c)(4) of this section. The certificate or documentary evidence must be furnished to the Internal Revenue Service by or on behalf of the beneficial owner upon application for the taxpayer identifying number or at any other time, as permitted under such procedures as the Internal Revenue Service may prescribe. If the tax residence of the beneficial owner changes, the beneficial owner shall promptly notify the Internal Revenue Service of that change. In addition, the Internal Revenue Service may exchange information for the purpose of confirming with the appropriate tax authority of the other country that the beneficial owner continues to be a tax resident of that country. The Internal

Revenue Service may from time to time, in its discretion, request that the beneficial owner reconfirm its residence in the treaty country.

(iii) *Special rules for qualified intermediaries.* The Internal Revenue Service may certify a taxpayer identifying number based upon the certification of a qualified intermediary described in §1.1441-1(e)(5)(ii) regarding the tax residence of any of its account holders, or persons owning an interest in the qualified intermediary, under procedures agreed upon with the Internal Revenue Service. If a new account or interest holder has a taxpayer identifying number at the time it opens an account or acquires an interest, the qualified intermediary may rely on a statement by the account or interest holder that appropriate proof of tax residence in the treaty jurisdiction was previously provided to the Internal Revenue Service. In such case, the qualified intermediary must notify the Internal Revenue Service each time the account or interest holder's address changes to another country or when the account or interest holder terminates its relationship with the qualified intermediary.

(3) *Certificate of residence.* A certificate of residence is generally a certificate issued by the competent authority (or another appropriate tax authority) of the treaty country of which the taxpayer claims to be a resident that certifies that the taxpayer has filed its most recent income tax return as a resident of that country. A certificate of residence is valid for a period of three years or such longer period as the Internal Revenue Service may prescribe. The competent authorities may agree to a different procedure for certifying residence, in which case such procedure shall govern for payments made to a person claiming to be a resident of the country with which such an agreement is in effect.

(4) *Documentary evidence establishing residence in the treaty country.* Generally, documentary evidence used to establish residence in a treaty country must include the name, address, and photograph of the person seeking to prove residence, must be an official document issued by an authorized governmental body (*i.e.*, a government or agency thereof, or a municipality), and must have been issued no more than three years prior to presentation to the withholding

agent. A document older than three years may be relied upon as proof of residence only if it is accompanied by additional evidence of the person's residence in the treaty country (*i.e.*, a bank statement, utility or medical bills). Documentary evidence must be in the form of original documents or a certified copy thereof.

(d) *Joint owners.* In the case of a payment to joint owners, all owners must furnish a withholding certificate or, if applicable, documentary evidence or a certificate of residence. The applicable rate of tax on a payment of income to joint owners shall be the highest applicable rate.

(e) *Related party dividends under certain treaties.* Income tax treaties between the United States and Austria, Denmark, Ireland, and Switzerland reduce the rate of tax on dividends between related corporations to 5 percent subject to the condition that the relationship between the domestic and foreign corporations was not arranged or maintained for the purpose of securing the reduced rate. A domestic corporation that makes a distribution to a resident of one of these countries may treat this condition as satisfied if, prior to the payment, a request has been made to the Internal Revenue Service for a private letter ruling determining that the relationship between the corporation and the shareholder was not arranged or maintained for such purpose and the Service has either issued a favorable ruling (and the ruling has not been revoked) or is considering the ruling request.

(f) *Effective date*—(1) *General rule.* This section applies to payments of income made after December 31, 1997.

(2) *Transition rules.* For purposes of this section, a withholding agent that holds a valid Form 1001 or 8233 on the date that is 60 days after these regulations are published as final regulations in the Federal Register may treat it as a valid withholding certificate until its validity expires under applicable provisions as in effect on April 22, 1996. In addition, the documentation requirements for dividends on stock traded on a U.S. established financial market described in paragraph (b)(2) of this section shall apply only to accounts established after the date that is 60 days after these regulations are published as final regulations in the Federal Register. For accounts established on or before that date, the

documentation requirements under this section shall apply to payments made after December 31, 1999.

Par. 13. Section 1.1441-7 is revised to read as follows:

§1.1441-7 General provisions relating to withholding agents.

(a) *Withholding agent defined.* For purposes of chapter 3 of the Internal Revenue Code, the term *withholding agent* means any person, U.S. or foreign, that has the control, receipt, custody, disposal, or payment of an item of income of a foreign person subject to withholding. See §1.1441-1(b) (dealing with general rules of withholding) and §1.1441-1(f) (dealing with presumptions of U.S. or foreign status in the absence of required documentation) for determining whether a payment is considered made to a foreign person. Any person who meets the definition of a withholding agent is required to deposit any tax withheld under §1.1461-1(a) and to make the returns prescribed by §1.1461-1(b) and (c). When several persons qualify as withholding agents with respect to a single payment, only one tax is required to be withheld and only one return (on Form 1042, as required under §1.1461-1(b)), is required to be made.

(b) *Standards of knowledge*—(1) *In general.* If a withholding agent does not withhold the full amount even though it has actual knowledge or reason to know that a claim of U.S. status or of a reduced rate of tax under section 1441 is incorrect, the withholding agent may be liable for tax, interest, and penalties under sections 1461 and 1463 and the regulations under those sections. A withholding agent that has received notification by the Internal Revenue Service that a claim of U.S. status or of a reduced rate is incorrect has actual knowledge beginning on the date that is 30 calendar days after the date the notice is received. A withholding agent that fails to act in accordance with the presumptions set forth in §1.1441-1(f) may be liable for tax, interest, and penalties. See §1.1441-1(f)(5).

(2) *Reason to know*—(i) *In general.* A withholding agent will be considered to have reason to know if it has sufficient knowledge of the underlying facts such that a reasonably prudent person in the position of the withhold-

ing agent would question the claim made or if the withholding agent has actual knowledge of sufficient facts to put it on notice that the claim is false.

(ii) *Limits on duty to inquire in certain cases.* In the case of portfolio interest, interest on deposits described in section 871(i)(2)(A), and dividends described in §1.1441-6(b)(2), a withholding agent's duty to inquire with respect to a beneficial owner withholding certificate is limited to the circumstances listed in this paragraph (b)(2)(ii). Where one or more of the circumstances described in this paragraph (b)(2)(ii) exist for a withholding certificate, the withholding agent may rely on the withholding certificate only after documentation is provided in support of the claim of foreign status, or reduced rate of tax under a tax treaty, and the certificate is corrected, if appropriate.

(A) The permanent residence address on the withholding certificate is an address in the United States.

(B) The payment is directed to a P.O. Box, an in-care-of address, a U.S. address, or an account with a financial institution in the United States.

(C) In the case of income for which benefits are claimed under an income tax treaty, the permanent residence address or mailing address is not in the corresponding treaty country.

(D) The beneficial owner notifies the withholding agent of an address for mailing purposes and that address is—

(1) Different from the permanent residence or mailing address stated on the withholding certificate provided to the withholding agent by or for the beneficial owner; and

(2) The address is one that is described in paragraph (b)(2)(ii)(A), (B), or (C) of this section.

(E) Such other circumstances as the Internal Revenue Service may prescribe in published guidance.

(3) *Universal accounts.* A withholding agent that is a financial institution dealing with the public and with which a customer may open an account shall apply the rules of this paragraph (b) on an account-by-account basis, except to the extent it uses a universal account system that uses a customer identifier that can be used to retrieve systematically any other accounts of the customer. See §31.3406(c)-1(c)(3)(ii) and (c)(3)(iii)(C) of this chapter.

(c) *Authorized agent*—(1) *In general.* The acts of an agent of a

withholding agent (including the receipt of withholding certificates, the payment of amounts of income subject to withholding, and the deposit of tax withheld) shall be imputed to the withholding agent on whose behalf it is acting. However, if the agent is a foreign person, a withholding agent that is a U.S. person may treat the acts of the foreign agent as its own for purposes of determining whether it has complied with the provisions of this section, but only if the agent is an authorized foreign agent, as defined in paragraph (c)(2) of this section.

(2) *Authorized foreign agent.* An agent is an authorized foreign agent only if—

(i) There is a written agreement between the withholding agent and the foreign person acting as agent;

(ii) The notification procedures described in paragraph (c)(3) of this section have been complied with;

(iii) Books and records and relevant personnel of the foreign agent are available for examination by the Internal Revenue Service in order to evaluate the withholding agent's compliance with the provisions of chapter 3, section 3406, and chapter 61 of the Internal Revenue Code, and the regulations under those provisions; for this purpose, the foreign agent's actual knowledge or reason to know shall be imputed to the U.S. withholding agent; and

(iv) The U.S. withholding agent remains fully liable for the acts of its agent and does not assert any of the defenses that may otherwise be available under common law principles of agency in order to avoid tax liability under the Internal Revenue Code.

(3) *Notification.* A withholding agent that appoints an authorized agent to act on its behalf for purposes of §1.871-14(c)(2), for the withholding provisions of chapter 3 of the Internal Revenue Code, or for the reporting provisions of chapter 61 of the Internal Revenue Code, is required to file notice of such appointment with the Office of the Assistant Commissioner (International). Such notice shall be filed before the first payment for which the authorized agent acts as such.

(4) *Liability of U.S. withholding agent.* A withholding agent acting through an authorized foreign agent is liable for any failure of the agent, such as failure to withhold an amount or

make payment of tax, in the same manner and to the same extent as if the agent's failure had been the failure of the U.S. withholding agent. Such liability shall exist irrespective of the fact that the authorized foreign agent is also a withholding agent and is itself separately liable for failure to comply with the provisions of the regulations under sections 1441, 1442, or 1443. However, liability for tax, interest, and penalties shall not be collected more than once.

(5) *Filing of returns.* See §1.1461-1(b)(2)(iii) and (c)(4)(iii) regarding returns required to be made where a U.S. withholding agent acts through an authorized foreign agent.

(d) *United States obligations.* If the United States is a withholding agent for an item of interest, including original issue discount, on obligations of the United States or of any agency or instrumentality thereof, the withholding obligation of the United States is assumed and discharged by—

(1) The Commissioner of the Public Debt, for interest paid by checks issued through the Bureau of the Public Debt;

(2) The Treasurer of the United States, for interest paid by him or her, whether by check or otherwise;

(3) Each Federal Reserve Bank, for interest paid by it, whether by check or otherwise; or

(4) Such other person as may be designated by the Internal Revenue Service.

(e) *Assumed obligations.* If, in connection with the sale of a corporation's property, payment of the bonds or other obligations of the corporation is assumed by the assignee, the assignee, whether an individual, partnership, or corporation, shall be a withholding agent to the extent amounts subject to withholding tax are paid to a foreign person. Thus, the assignee shall deduct and withhold such taxes under §1.1441-1 as would be required to be withheld by the assignor had no such sale or transfer been made.

(f) *Conduit financing arrangements.* [Reserved]

(g) *Effective date.* This section applies to payments of income made after December 31, 1997.

Par. 14. Section 1.1441-8T is amended as follows:

1. The section heading is revised.
2. Paragraph (b) is revised.

3. Paragraph (c) is added.

The revisions and addition read as follows:

§1.1441-8T Foreign government and international organization exemption from withholding (temporary).

* * * * *

(b) *Statement claiming exemption.* Absent actual knowledge or reason to know otherwise, the withholding agent may rely upon a claim of exemption made by the foreign government or international organization, if, prior to making the payment, the withholding agent satisfies the requirements of §1.1441-1(e)(1). For purposes of this paragraph (b), a beneficial owner withholding certificate means a certificate described in §1.1441-1(e)(2). A statement on the withholding certificate that the income is, or will be, exempt from taxation under section 892 and the regulations under that section will satisfy the requirement in §1.1441-1(e)(2)(ii) that the beneficial owner state on the certificate the basis for the claim of reduced rate.

(c) *Effective date—(1) In general.* This section applies to payments of income made after December 31, 1997.

(2) *Transition rules.* For purposes of this section, a withholding agent that holds a valid Form 8709 on the date that is 60 days after these regulations are published as final regulations in the Federal Register may treat it as a valid withholding certificate until its validity expires under applicable provisions as in effect on April 22, 1996.

Par. 15. Section 1.1441-9 is added to read as follows.

§1.1441-9 Exemption from withholding on exempt income of a foreign tax-exempt organization and foreign private foundations.

(a) *Income not subject to tax under section 511.* No withholding of tax is required under §1.1441-1 on income of a foreign organization described in section 501(c) of the Internal Revenue Code that is not subject to the tax imposed by section 511 of the Internal Revenue Code and is exempt from tax under section 501(a). See §1.1443-1 for withholding rules applicable to foreign private foundations.

(b) *Statement claiming exemption.* Absent actual knowledge or reason to

know otherwise, a withholding agent may rely upon a claim of exemption by the foreign tax-exempt organization if, prior to making the payment, the withholding agent meets the requirements of §1.1441-1(e)(1) (except that the certificate must contain a taxpayer identifying number). The requirement in §1.1441-1(e)(2)(ii) that the beneficial owner state on the certificate the basis for the claim of reduced rate shall be satisfied by the beneficial owner certifying that the income is not, or will not be, subject to tax under section 511 and that the Internal Revenue Service has issued a determination letter (and the date thereof). If the organization cannot certify that it has been issued such a letter, it must provide an opinion of counsel that it is tax exempt under section 501(c).

(c) *Effective date—(1) In general.* This section applies to payments of income made after December 31, 1997.

(2) *Transition rules.* For purposes of this section, a withholding agent that holds a valid Form W-8, 1001 or 4224 on the date that is 60 days after the date these regulations are published as final regulations in the Federal Register may treat it as a valid withholding certificate until its validity expires under applicable provisions as in effect on April 22, 1996.

Par. 16. Sections 1.1442-1 and 1.1442-2 are revised to read as follows:

§1.1442-1 Withholding of tax on foreign corporations.

For regulations concerning the withholding of tax at source under section 1442 in the case of foreign corporations, see §§1.1441-1 through 1.1441-7 and 1.1441-9.

§1.1442-2 Exemption under a tax treaty.

For regulations providing for a claim of reduced withholding tax under section 1442 by certain foreign corporations pursuant to the provisions of an income tax treaty, see §1.1441-6.

Par. 17. Section 1.1442-3 is added to read as follows:

§1.1442-3 Tax exempt income of a foreign tax-exempt corporation.

For regulations providing for a claim of exemption for income exempt from

tax under section 501(a) of a foreign tax-exempt corporation, see §1.1441-9. See §1.1443-1 for withholding rules applicable to foreign foundations.

§1.1443-1 [Amended]

Par. 18. Section 1.1443-1 is amended by:

1. Amending the second sentence of paragraph (b)(4)(i) by removing the words “an affidavit of the foreign organization or”.

2. Amending the third sentence in paragraph (b)(4)(i) by removing the words “an affidavit or”.

Par. 19. Section 1.1461-1 is revised to read as follows:

§1.1461-1 *Payment and returns of tax withheld.*

(a) *Payment of withheld tax—(1) Deposits of tax.* Every withholding agent who withholds tax pursuant to chapter 3 of the Internal Revenue Code shall deposit such amount of tax with a Federal reserve bank or authorized financial institution as provided in §1.6302-2(a). If for any reason the total amount of tax required to be returned for any calendar year pursuant to paragraph (b) of this section has not been deposited pursuant to §1.6302-2, the withholding agent shall pay the balance of tax due for such year at such place as the Internal Revenue Service shall specify. The tax shall be paid when filing the return required under paragraph (b)(2) of this section for such year, unless the Internal Revenue Service specifies otherwise. See paragraph (b)(2) of this section when there are multiple withholding agents.

(2) *Penalties for failure to pay tax.* For penalties and additions to the tax for failure to timely pay the tax required to be withheld under chapter 3 of the Internal Revenue Code, see sections 6656, 6672, and 7202 and the regulations under those sections.

(b) *Income tax return—(1) General rule.* A withholding agent shall make an income tax return on Form 1042 (or such other form as the Internal Revenue Service may prescribe) for income paid during the preceding calendar year that the withholding agent is required to report on an information return on Form 1042-S (or such other form as the Internal Revenue Service may

prescribe) under paragraph (c)(1) of this section. See section 6011 and §1.6011-1(c). The withholding agent must file the return on or before February 28 of the calendar year following the year in which the income was paid. The return must show the aggregate amount of income paid and tax withheld required to be reported on all the Forms 1042-S for the preceding calendar year by the withholding agent, in addition to such information as is required by the form and accompanying instructions. Withholding certificates or other statements or information provided to a withholding agent are not required to be attached to the return. A return must be filed under this paragraph (b)(1) even though no tax was required to be withheld during the preceding calendar year. The withholding agent must retain a copy of Form 1042 for the applicable statute of limitations on assessments and collection with respect to the items of income required to be reported on the Form 1042. See section 6501 and the regulations thereunder for the applicable statute of limitations. Adjustments to the total amount of tax withheld, as described in §1.1461-2, shall be stated on the return as prescribed by the form and accompanying instructions.

(2) *Multiple withholding agents—(i) General rule.* Except as otherwise provided in paragraph (b)(2)(ii) and (iii) of this section, no Form 1042 is required to be filed under paragraph (b)(1) of this section if a return is filed by another withholding agent reporting the same income in compliance with the provisions of this paragraph (b) and any remaining tax due is paid with the return as required under paragraph (a) of this section.

(ii) *Payment to a qualified intermediary.* A U.S. withholding agent making a payment to a qualified intermediary (as defined in §1.1441-1(e)(5)(ii)) must file a return under paragraph (b)(1) of this section, regardless of whether the qualified intermediary assumes primary withholding responsibility for the payment, as described in §1.1441-1(e)(5)(iv) and regardless of whether the qualified intermediary is also required to file a return under the terms of its agreement with the Internal Revenue Service. A qualified intermediary's agreement with the Internal Revenue Service shall specify the extent, if any, to which the intermediary is subject to filing requirements under this section.

(iii) *Payment to or through an authorized foreign agent.* Both the U.S. withholding agent making a payment to or through an authorized foreign agent (defined in §1.1441-7(c)) and the authorized foreign agent are required to file a return under paragraph (b)(1) of this section.

(3) *Amended returns.* An amended return may be filed on a Form 1042X or such other form as the Internal Revenue Service may prescribe. An amended return must include such information as the form and accompanying instructions shall require, including, with respect to any information that has changed from the time of the filing of the return, the information that was shown on the original return and the corrected information.

(c) *Information returns—(1) Filing requirement—(i) In general.* A withholding agent must make an information return on Form 1042-S (or such other form as the Internal Revenue Service may prescribe) to report the items of income specified in paragraph (c)(2) of this section that were paid during the preceding calendar year. One Form 1042-S shall be prepared for each beneficial owner (except as otherwise provided in paragraph (c)(4) of this section regarding multiple withholding agents). The Form 1042-S shall be prepared in such manner as the form and accompanying instructions prescribe. One copy of the Form 1042-S shall be filed with the Internal Revenue Service on or before February 28 of the calendar year following the year in which the item of income was paid. It shall be filed with a transmittal form as provided in the instructions to the Form 1042-S and the transmittal form. Withholding certificates or other statements or documentation provided to a withholding agent are not required to be attached to the information return. Another copy of the Form 1042-S shall be furnished to the payee on or before February 28 of the calendar year following the year in which the item of income was paid after the calendar year of payment. The withholding agent shall retain a copy of each Form 1042-S for the statute of limitations on assessment and collection applicable to the Form 1042 to which the Form 1042-S relates.

(ii) *Joint owners.* In the case of joint owners, a single Form 1042-S may be prepared. However, any one of the

owners may request that it be furnished its own Form 1042-S. Where more than one Form 1042-S is issued with respect to a single payment to joint owners, the aggregate amount of income and tax withheld reported on the Forms 1042-S cannot exceed the amount of income to the joint owners and tax withheld thereon. If a single Form 1042-S is prepared, the form shall state the name of only one owner and that name shall be that of the person whose status the withholding agent relied upon to determine the applicable rate of withholding tax.

(2) *Income subject to reporting*—(i) *In general.* Subject to the exceptions in paragraph (c)(2)(ii) of this section, the items of income required to be reported on a Form 1042-S are income subject to withholding (as defined in §1.1441-2(a)), income on a notional principal contract described in §1.1441-4(a)(3), and amounts described in sections 6041 through 6050P that are paid to a foreign person and are not exempt from reporting under sections 6041 through 6050P or the regulations under those sections.

(ii) *Exceptions to reporting.* The items of income listed in this paragraph (c)(2)(ii) are not required to be reported on a Form 1042-S.

(A) Any item of income paid by a partnership, trust or estate to the extent the item of income is required to be reported by the partnership, trust or estate under section 6031 or 6034.

(B) Any item required to be reported on a Form W-2, including an item required to be shown on Form W-2 solely by reason of §1.6041-2 (relating to return of information as to payments to employees) or §1.6052-1 (relating to information regarding payment of wages in the form of group-term life insurance).

(C) Any item of income required to be reported on Form 1099, and such other forms prescribed under sections 6041 through 6050P and the regulations under these sections.

(D) Any item of income paid to foreign governments, international organizations, and foreign central banks of issue that are exempt from tax under section 892 or section 895.

(E) Income required to be reported on Form 8288 (U.S. Withholding Tax Return for Dispositions by Foreign Persons of U.S. Real Property Interests) or Form 8804 (Annual Return for

Partnership Withholding Tax (Section 1446)).

(F) Income on deposits described in section 871(i)(2)(A), unless actually subject to withholding or specifically subject to reporting under section 6049 and the regulations under that section.

(G) Interest on a foreign-targeted registered obligation described in §1.871-14(e), except as otherwise provided in §1.871-14(e)(4)(ii)(A).

(3) *Required information.* Form 1042-S shall include such information as is required by the form and accompanying instructions. The information shall be based upon the information provided by or on behalf of the beneficial owner (e.g., a beneficial owner withholding certificate or documentary evidence), as corrected and supplemented based on the agent's actual knowledge or reason to know. In particular, the Form 1042-S must include the information described in this paragraph (c)(3), if applicable.

(i) The name, address, and taxpayer identifying number of the withholding agent.

(ii) A description of each category of income paid (e.g., interest, dividends, royalties, etc.) and the aggregate amount in each category expressed in U.S. dollars.

(iii) The rate of withholding applied and, if applicable, the basis for withholding at a reduced rate.

(iv) The name, permanent residence address, and taxpayer identifying number (if required under §1.1441-1(e)(4)-(vii) to be shown on a beneficial owner withholding certificate or actually known to the withholding agent making the return) of the beneficial owner.

(4) *Multiple withholding agents*—(i) *In general.* Except as otherwise provided in paragraph (c)(4)(ii), (iii), and (v) of this section, no information return is required to be filed under paragraph (c)(1)(i) of this section if a return is filed by another withholding agent reporting the same income in compliance with the provisions of this paragraph (c).

(ii) *Payment to a qualified intermediary.* A withholding agent making a payment to a qualified intermediary (defined in §1.1441-1(e)(5)(ii)) must report the payment but may do so on a single Form 1042-S.

(iii) *Payment to an authorized foreign agent*—(A) *Filing obligation of foreign authorized agent.* An author-

ized foreign agent (as described in §1.1441-7(c)(2)) is subject to the filing requirements described in paragraph (c)(1)(i) of this section because it is a withholding agent. Therefore, to the extent the U.S. withholding agent for which it is acting is not reporting the information required under this paragraph (c), it must report the information required to be reported under paragraph (c)(3) or (c)(4)(vi) of this section.

(B) *Filing obligations of the U.S. withholding agent.* A U.S. withholding agent making a payment to an authorized foreign agent is exempted from the requirement under paragraph (c)(4)-(iv) of this section to make a return on Form 1042-S for each beneficial owner and may, instead, make a single Form 1042-S to report the payment made to the authorized foreign agent. The exemption in this paragraph (c)(4)(iii)(B) shall apply only to the extent the authorized foreign agent complies with the filing requirements under paragraph (c)(4)(iii)(A) of this section.

(iv) *Payment to other foreign person not acting for its own account.* Payment of an item of income to an agent, nominee or representative for the benefit of other persons in respect of whom Forms 1042-S are required may not be shown on a single Form 1042-S but must be identified on separate Forms 1042-S for each beneficial owner if such agent, nominee, or representative is a foreign person and is not a qualified intermediary or an authorized foreign agent.

(v) *Payment to a foreign partnership.* Payment of an item of income to a foreign partnership that is not a qualified intermediary and acts for its own account may not be shown on a single Form 1042-S but must be identified on separate Forms 1042-S for each beneficial owner (or partner that is a qualified intermediary or authorized foreign agent).

(vi) *Required information.* An information return on a Form 1042-S by a withholding agent reporting payments to an intermediary or to a foreign partnership described in paragraph (c)(4)(v) of this section must contain the information contained in this paragraph (c)(4)(vi). The information on the Form 1042-S must be based upon the withholding certificates furnished by the payee, as corrected and supplemented by the withholding agent's actual knowledge or reason to know.

(A) The name, address, and taxpayer identifying number of the withholding agent.

(B) A description of each category of income paid (e.g., interest, dividends, royalties, etc.) and the aggregate amount in each category expressed in U.S. dollars.

(C) The rate of withholding applied.

(D) The basis for not withholding or withholding at a reduced rate.

(E) The name, address, and taxpayer identifying number of the payee.

(F) In the case of a payment to a partnership acting for its own account, the name, address, and taxpayer identifying number (if required under §1.1441-1(e)(4)(vii) to be stated on the withholding certificates or actually known to the withholding agent) of the person for whom a Form 1042-S is required to be prepared pursuant to the provisions of paragraph (c)(4)(v) of this section.

(5) *Magnetic media reporting.* A withholding agent that makes 250 or more Form 1042-S information returns for a taxable year must file Form 1042-S returns on magnetic media. See §301.6011-2 of this chapter for requirements applicable to a withholding agent that files Forms 1042-S on magnetic media and publications of the Internal Revenue Service relating to magnetic media filing.

(d) *Report of taxpayer identifying numbers.* When so required or permitted under procedures issued by the Internal Revenue Service, a withholding agent may attach to the Form 1042 a list of all the taxpayer identifying numbers that have been furnished to the withholding agent and upon which the withholding agent has relied to grant a reduced rate of withholding and that are not otherwise required to be reported on a Form 1042-S under the provisions of this section.

(e) *Indemnification of withholding agent.* A withholding agent is indemnified against the claims and demands of any person for the amount of any tax it deducts and withholds in accordance with the provisions of chapter 3 of the Internal Revenue Code and the regulations under that chapter. A withholding agent that withholds based on a reasonable belief that such withholding is required under chapter 3 of the Internal Revenue Code is treated for purposes of section 1461 and this paragraph (e) as having withheld tax in

accordance with the provisions of chapter 3 of the Internal Revenue Code and the regulations under that chapter. In addition, a withholding agent is indemnified against the claims and demands of any person for the amount of any payments made in accordance with the grace period provisions set forth in §1.1441-1(f)(2)(ii)(A). This paragraph (e) does not apply to relieve a withholding agent from tax liability under chapter 3 of the Internal Revenue Code.

(f) *Amounts paid not constituting gross income.* Any amount withheld in accordance with §§1.1441-3(b)(1) and 1.1441-3(d) shall be returned and paid in accordance with this section, even though the item or amount paid to the beneficial owner may not constitute gross income in whole or in part. For this purpose, a reference in this section to an item or amount of income shall, where appropriate, be deemed to refer to the amount subject to withholding under §§1.1441-3(b)(1) and 1.1441-3(d).

(g) *Extensions of time for requests made for calendar year beginning after the date of publication of these regulations as final regulations in the Federal Register—(1) Extension of time to file Form 1042.* The Internal Revenue Service may grant an extension of time in which to file a Form 1042. Form 2758, Application for Extension of Time to File Certain Excise, Income, Information, and Other Returns, or such other form as the Internal Revenue Service may prescribe, must be used to request an extension of time. The request must contain a statement of the reasons for requesting the extension. The request must be mailed or delivered not later than February 28 of the year following the end of the calendar year for which the return will be filed.

(2) *Extension of time to file Form 1042-S.* The Internal Revenue Service may grant an extension of time in which to file Form 1042-S. Form 8809, Request for Extension of Time to File Information Returns, or such other form as the Internal Revenue Service may prescribe, must be used to request an extension of time. The request must contain a statement of the reasons for requesting the extension. The request must be mailed or delivered not later than February 28 of the year following the calendar year for which the return will be filed.

(3) *Extension of time to furnish Forms 1042-S.* The Internal Revenue

Service may grant an extension of time in which to furnish Forms 1042-S to beneficial owners or intermediaries. Form 8809, request for Extension of Time to File Information Returns, or such other form as the Internal Revenue Service may prescribe, must be used to request an extension of time. The request must contain the withholding agent's name and address, the withholding agent's taxpayer identifying number, the type of statement and a statement of the reasons for requesting the extension. The request must be signed by the withholding agent or a person who is duly authorized to sign a return, statement, or other document. The request must be mailed or delivered not later than February 28 of the year following the end of the calendar year for which the statement will be furnished.

(h) *Penalties.* For penalties and additions to the tax for failure to file returns in accordance with this section, see sections 6651, 6662, 6663, 6721, 6722, 6723, 6724(c), 7201, 7203, and the regulations under those sections.

(i) *Effective date.* This section shall apply to returns required for payments made after December 31, 1997.

Par. 20. Section 1.1461-2 is revised to read as follows:

§1.1461-2 Adjustments for overwithholding or underwithholding of tax.

(a) *Adjustments of overwithheld tax—(1) In general.* A withholding agent that has overwithheld under chapter 3 of the Internal Revenue Code and made a deposit of that tax as provided in §1.6302-2(a) may adjust the overwithheld amount either pursuant to the reimbursement procedure described in paragraph (a)(2) of this section or pursuant to the set-off procedure described in paragraph (a)(3) of this section. Adjustments under this paragraph (a) may only be made within the time prescribed under paragraph (a)(2) or (3) of this section. After such time, an adjustment to the amount overwithheld can only be claimed by the beneficial owner with the Internal Revenue Service pursuant to the procedures described in chapter 65 of the Internal Revenue Code. For purposes of this section, the term *overwithholding* means any amount actually withheld (determined before application of the adjustment procedures under this sec-

tion) from an item of income pursuant to chapter 3 of the Internal Revenue Code in excess of the actual tax liability due, regardless of whether such overwithholding was in error or appeared correct at the time it occurred.

(2) *Reimbursement of tax*—(i) *General rule.* Under the reimbursement procedure, the withholding agent may repay the beneficial owner for the amount overwithheld by reducing, by the amount of tax actually repaid, the amount of any deposit of tax made by the withholding agent under §1.6302-2(a)(1)(iii) for any subsequent payment period occurring before the end of the calendar year following the calendar year of overwithholding. Any such reduction that occurs for a payment period in the calendar year following the calendar year of overwithholding shall be allowed only if—

(A) The withholding agent states, on a timely filed (not including extensions) Form 1042-S for the calendar year of overwithholding, the amount of tax withheld and the amount of any actual repayment; and

(B) The withholding agent states on a timely filed (not including extensions) Form 1042 for the calendar year of overwithholding, that the filing of the Form 1042 constitutes a claim for credit in accordance with §1.6414-1.

(ii) *Record maintenance.* If the beneficial owner is repaid an amount of withholding tax under the provisions of this paragraph (a)(2), the withholding agent shall keep as part of its records a receipt showing the date and amount of repayment and the withholding agent must provide a copy or such receipt to the beneficial owner. For this purpose, a canceled check or an entry in a statement is sufficient provided that the check or statement contains a specific notation that it is a refund of tax overwithheld.

(3) *Set-offs.* Under the set-off procedure, the withholding agent may repay the beneficial owner by applying the amount overwithheld against any amount which otherwise would be required under chapter 3 of the Internal Revenue Code to be withheld from income paid by the withholding agent to such person before the earlier of the due date for filing the Form 1042-S for the calendar year of overwithholding or the date that the Form 1042-S is actually filed with the Internal Revenue Service. For purposes of making a

return on Form 1042 or 1042-S (or an amended form) for the calendar year of overwithholding and for purposes of making a deposit of the amount withheld, the reduced amount shall be considered the amount required to be withheld from such income under chapter 3 of the Internal Revenue Code.

(4) *Examples.* The principles of this paragraph (a) are illustrated by the following examples:

Example 1. (i) N is a nonresident alien individual who is a resident of the United Kingdom. In December 1997, a domestic corporation C pays a dividend of \$100 to N, at which time C Corporation withholds \$30 and remits the balance of \$70 to N. On February 10, 1998, prior to the time that C files its Form 1042, N advises C Corporation that, pursuant to the income tax convention with the United Kingdom, only \$15 tax should have been withheld from the \$100 dividend and requests reimbursement of the \$15 that was erroneously withheld. Although C Corporation has already deposited the \$30 that was withheld, as required by §1.6302-2(a)(1)(iv), such corporation repays N in the amount of \$15.

(ii) During 1997, C Corporation makes no other payments upon which tax is required to be withheld under chapter 3 of the Internal Revenue Code; accordingly, its return on Form 1042 for such year, which is filed on February 28, 1998, shows total tax withheld of \$30, an adjusted total tax withheld of \$15, and \$30 previously paid for such year. Pursuant to §1.6414-1(b), C Corporation claims credit for the overpayment of \$15 shown on the Form 1042 for 1997. Accordingly, it is permitted to reduce by \$15 any deposit required by §1.6302-2 to be made of tax withheld during the calendar year 1998. The Form 1042-S required to be filed by C Corporation with respect to the dividend of \$100 paid to N in 1997 is required to show tax withheld of \$30 and tax released of \$15.

(iii) During 1998, C Corporation is required to withhold \$200 under chapter 3 of the Internal Revenue Code, all of which is withheld in June of that year. Pursuant to §1.6302-2(a)(1)(iii), C Corporation deposits the amount of \$185 on July 15, 1998, that is, \$200 less the \$15 for which credit is claimed on the Form 1042 for 1997. On February 28, 1999, C Corporation files its return on Form 1042 for calendar year 1998, which shows total tax withheld of \$200, \$185 previously deposited by C Corporation, and \$15 allowable credit.

Example 2. The facts are the same as in *Example 1* except that paragraph (iii) of *Example 1* does not apply and C Corporation is required to deposit on a quarter-monthly basis the tax withheld under chapter 3 of the Internal Revenue Code. C Corporation withholds tax of \$100 between February 8 and February 15, 1998, and complies with the quarter-monthly deposit requirement of §1.6302-2(a)(1)(ii) by depositing \$75 [(\$100 × 90 percent) less \$15] of the withheld tax within 3 banking days after February 15, 1998, and by depositing \$10 [(\$100 - \$15) less \$75] within 3 banking days after March 15, 1998.

(b) *Withholding of additional tax when underwithholding occurs.* A with-

holding agent may withhold the tax that should have been withheld from previous payments from future payments made to a beneficial owner. Such additional withholding of tax may only be made from payments made before the date that the Form 1042 is required to be filed (not including extensions). See §1.6302-2 for making deposits of tax or §1.1461-1(a) for making payment of the balance of tax due for a calendar year.

(c) *Definition.* For purposes of this section, the term *payment period* means the period for which the withholding agent is required by §1.6302-2(a)(1) to make a deposit of tax withheld under chapter 3 of the Internal Revenue Code.

(d) *Effective date.* This section applies to payments of income made after December 31, 1997.

§§1.1461-3 and 1.1461-4 [Removed]

Par. 21. Sections 1.1461-3 and 1.1461-4 are removed.

Par. 22. Section 1.1462-1 is amended by:

1. Revising paragraph (a).
2. Adding paragraph (c).
3. Removing the OMB parenthetical and the authority citation at the end of the section.

The revision and addition read as follows:

§1.1462-1 Withheld tax as credit to recipient of income.

(a) *Creditable tax.* The entire amount of the income from which the tax is required to be withheld (including amounts calculated under the gross-up formula in §1.1441-3(e)(3)) shall be included in gross income in the return required to be made by the beneficial owner of the income, without deduction for the amount required to be withheld, but the tax so withheld shall be allowed as a credit against the total income tax computed in the beneficial owner's return.

* * * * *

(c) *Effective date.* This section applies to payments of income made after December 31, 1997.

Par. 23. Section 1.1463-1 is revised to read as follows:

§1.1463-1 Tax paid by recipient of income.

(a) *Tax paid.* If the tax required to be withheld under chapter 3 of the Internal Revenue Code is paid by the beneficial owner of the income or by the withholding agent, it shall not be re-collected from the other, regardless of the original liability therefor. However, this section does not relieve the person that did not withhold tax from liability for interest or any penalties or additions to tax otherwise applicable.

(b) *Effective date.* This section applies to failures to withhold occurring after December 31, 1989.

Par. 24. Section 1.6041-1, the amendments to paragraph (a)(1) as proposed in project number INTL-52-86 published on February 29, 1988, at 53 FR 5993, are withdrawn.

Par. 25. Section 1.6041-1 is amended by:

1. Removing paragraph (a)(1)(iii).
2. Redesignating paragraphs (a)(1) introductory text and (a)(1)(i) as paragraphs (a)(1)(i) introductory text and (a)(1)(i)(A).
3. Adding a heading for paragraph (a)(1).
4. Amending newly designated paragraph (a)(1)(i)(A) by adding the word "or" at the end of the paragraph.
5. Redesignating paragraph (a)(1)(ii) as paragraph (a)(1)(i)(B) and removing the language "; or" at the end of the paragraph and adding a period in its place.
6. Designating the concluding text immediately following newly designated paragraph (a)(1)(i)(B) as paragraph (a)(1)(ii).
7. Removing the first sentence of newly designated paragraph (a)(1)(ii) and adding two new sentences in its place.
8. Adding paragraph (d)(5).

The revisions and additions read as follows:

§1.6041-1 Return of information as to payments of \$600 or more

(a) *General rule*—(1) *Information returns required*—(i) * * *

(ii) The payments described in paragraphs (a)(1)(i)(A) and (B) of this section shall not include any payments with respect to which a statement is required by, or may be required under

authority of section 6042(a) (relating to dividends); section 6043(a)(2) (relating to distributions in liquidation); section 6044(a) (relating to patronage dividends); section 6045 (relating to brokers' transactions with customers); section 6049(a)(1) and (a)(2) (relating to interest); section 6050N(a) (relating to royalties); or section 6050P(a) or (b) (relating to cancellation of indebtedness). In addition, the payments described in paragraphs (a)(1)(i)(A) and (B) of this section shall not include amounts excepted from the definition of dividends under section 6042(b)(2) and §1.6042-3(b)(1), amounts described in section 6044(b), amounts excepted from reporting under §1.6045-1(g)(1), amounts excepted from the definition of interest under section 6049(b)(2)(C) or (D), §1.6049-4(c), or §1.6049-5(b)(6) through (14). * * *

* * * * *

(d) * * *
(5) Amounts paid after December 31, 1997, with respect to notional principal contracts referred to in §1.1441-4(a)(3) that the payor or middleman may treat as paid to a beneficial owner that is a foreign person and that are not described in §1.6041-4(a)(2) or (4) shall be reported on a Form 1042 and 1042-S in accordance with §1.1461-1(b) and (c), whether or not effectively connected with the conduct of a trade or business in the United States. Although reportable, amounts described in this paragraph (d)(5) are not subject to backup withholding under section 3406 if paid outside the United States. See 31.3406(g)-(1)(e) of this chapter.

* * * * *

Par. 26. In §1.6041-3, paragraph (q), as proposed to be added in project number LR-3-87 on June 9, 1988, at 53 FR 21694, is withdrawn.

Par. 27. Section 1.6041-3 is amended by:

1. Revising the introductory text of the section.
2. Revising paragraph (a).
3. Adding paragraph (q).

The addition and revisions read as follows:

§1.6041-3 Payments for which no return of information is required under section 6041.

Returns of information are not required under section 6041 and

§§1.6041-1 and 1.6041-2 for payments described in paragraphs (a) through (q) of this section. See §1.6041-4 for reporting exemptions regarding foreign-related items.

(a) Payments of income required to be reported on Forms 1120-S, 941, W-2, and W-3, (however, see §1.6041-2 with respect to Forms W-2 and W-3);

* * * * *

(q) Payments to individuals as scholarships or fellowship grants, as defined in §1.117-6(c)(3). This exception does not apply to any amount of a scholarship or fellowship grant that represents payment for services, as defined in §1.117-6(d)(2). See §1.1461-1(c) for applicable reporting requirements with respect to amounts paid to foreign persons.

Par. 28. Section 1.6041-4 is revised to read as follows:

§1.6041-4 Foreign-related items.

(a) *Exempted foreign-related items.* Returns of information are not required under section 6041 and §§1.6041-1 and 1.6041-2 for payments of the items described in paragraphs (a)(1) through (4) of this section.

(1) Returns of information are not required for payments that a payor or middleman, as defined in paragraph (b)(1) of this section, may treat as made to a beneficial owner that is a foreign person pursuant to §1.1441-1(e)(1) and from which the payor or middleman is either required to withhold tax under section 1441 or the regulations under that section or would be so required but for exceptions in the regulations under section 1441 (such as, for example, under §1.1441-4 (dealing with effectively connected income) or §1.1441-6 (dealing with a reduction of rate of tax under an income tax treaty)). See §1.1441-1(e)(4)(i) in the case of payments to joint owners.

(2) Returns of information are not required for payments of amounts from sources outside the United States made by a non-U.S. payor or non-U.S. middleman (as defined in paragraph (b)(2) of this section) outside the United States. See §1.6049-5(e) for circumstances in which a payment is considered to be made outside the United States.

(3) Returns of information are not required for payments of amounts from

sources outside the United States that a payor or middleman may treat as paid to a beneficial owner that is a foreign person (because such person has furnished a certificate described in §1.6049-5(c)(1)). For purposes of this paragraph (a)(3), the provisions in §1.6049-5(c)(3) through (c)(6) (regarding operating rules related to the certificate of foreign status) shall apply.

(4) Returns of information are not required for the period that the amounts paid represent assets blocked as described in §1.1441-2(e)(3). The exemption in this paragraph (a)(4) shall terminate when payment is deemed to occur in accordance with the provisions of §1.1441-2(e)(3).

(b) *Definitions*—(1) *Payor and middleman*. For purposes of this section, the term *payor* means any person who is required to make an information return with respect to any reportable payment, as described in section 3406(b), including any middleman. The term *middleman* means any person whose legal relationship to the payor or payee (including any other middleman) is of a kind described in §1.6049-4(f)-(4) (as proposed in project number INTL-52-86 published in 1988-1 C.B. 892).

(2) *Non-U.S. payor and non-U.S. middleman*. For purposes of this section, the term *non-U.S. payor* or *non-U.S. middleman* means a payor or middleman other than—

(i) A person described in section 7701(a)(30);

(ii) The government of the United States, the government of any State or political subdivision thereof (or any agency or instrumentality of any of the foregoing);

(iii) A controlled foreign corporation within the meaning of section 957(a); or

(iv) A foreign person 50 percent or more of the gross income of which, from all sources for the three-year period ending with the close of its taxable year preceding the collection or payment (or such part of such period as the person has been in existence), was effectively connected with the conduct of trade or business within the United States.

(c) *Applicable presumptions*. The presumptions of §1.1441-1(f) shall apply for determining the payee's status where the required documentation is lacking, incorrect, or unreliable.

(d) *Joint owners*. In the case of amounts paid to joint owners for which a certificate or documentation is required as a condition for being exempt from reporting under this paragraph (d), a payor or middleman must receive from each joint owner the required certification or documentation. Where any one of the joint owners has not furnished such certification or documentation, the payment is not exempt from reporting under this section.

(e) *Payee*. For determination of payee, see §1.1441-1(c)(3).

(f) *Conversion into United States dollars of amounts paid in foreign currency*. For rules concerning foreign currency conversion, see §1.6049-4(d)-(3)(i).

(g) *Effective date*—(1) *General rule*. The provisions of this section apply to payments made after December 31, 1997.

(2) *Transition rules*. A payor that holds a valid Form W-8 on the date that is 60 days after these regulations are published as final regulations in the Federal Register may treat it as a valid certificate until its validity expires under applicable provisions as in effect on April 22, 1996.

Par. 29. Section 1.6041A-1 as proposed to be added in project number LR-214-82, published on January 7, 1986, at 51 FR 626, is amended by adding a new paragraph (d)(3), to read as follows:

§1.6041A-1 Returns regarding payments of remuneration for services and certain direct sales.

* * * * *

(d) *Exceptions to return requirement.* * * *

* * * * *

(3) *Foreign transactions*—(i) *In general*. No return shall be required under paragraph (a) of this section with respect to payments described in this paragraph (d)(3).

(A) Returns of information are not required for payments of remuneration for services that a payor or middleman, as defined in paragraph (d)(3)(ii)(A) of this section, may treat as made to a beneficial owner that is a foreign person pursuant to §1.1441-1(e)(1) and from which the payor or middleman is either required to withhold tax under section 1441 or the regulations under

that section or would be so required but for exceptions in the regulations under section 1441 (such as, for example, under §1.1441-4 (dealing with effectively connected income) or §1.1441-6 (dealing with a reduction of rate of tax under an income tax treaty)). See §1.1441-1(e)(4)(i) in the case of payments to joint owners.

(B) Returns of information are not required for payments of remuneration for services and certain direct sales from sources outside the United States made outside the United States by a non-U.S. payor or non-U.S. middleman (as defined in paragraph (d)(3)(ii)(B) of this section). See §1.6049-5(e) for circumstances in which a payment is considered to be made outside the United States.

(C) Payments of services and certain direct sales from sources outside the United States that a payor or middleman may treat as paid to a beneficial owner that is a foreign person (because such person has furnished a certificate described in §1.6049-5(c)(1)). For purposes of this paragraph (d)(3)(i)(C), the provisions in §1.6049-5(c)(3) through (c)(6) (regarding operating rules related to the certificate of foreign status) shall apply. See §1.6041-1(d)(5) for reportable payments made to foreign persons.

(D) Amounts paid for services and certain direct sales for the period that they represent assets blocked as described in §1.1441-2(e)(3). The exemption in this paragraph (d)(3)(i)(D) shall terminate when payment is deemed to occur in accordance with the provisions of §1.1441-2(e)(3).

(ii) *Definitions*—(A) *Payor and middleman*. For purposes of this section, the term *payor* means any person who is required to make an information return with respect to any reportable payment, as described in section 3406(b), including any middleman and the term *middleman* means any person whose legal relationship to the payor or payee (including any other middleman) is of a kind described in §1.6049-4(f)-(4) (as proposed in project number INTL-52-86 published in 1988-1 C.B. 892).

(B) *Non-U.S. payor and non-U.S. middleman*. For purposes of this section, the term *non-U.S. payor* or *non-U.S. middleman* means a payor or middleman other than—

(1) A person described in section 7701(a)(30);

(2) The government of the United States, the government of any State or political subdivision thereof (or any agency or instrumentality of any of the foregoing);

(3) A controlled foreign corporation within the meaning of section 957(a); or

(4) A foreign person 50 percent or more of the gross income of which, from all sources for the three-year period ending with the close of its taxable year preceding the collection or payment (or such part of such period as the person has been in existence), was effectively connected with the conduct of trade or business within the United States.

(C) *Applicable presumptions.* The presumptions of §1.1441-1(f) shall apply for determining the payee's status where the required documentation is lacking, incorrect, or unreliable.

(D) *Joint owners.* In the case of amounts paid to joint owners for which a certificate of documentation is required as a condition for being exempt from reporting under this paragraph (d)(3), the payor or middleman must receive from each joint owner the certification described in paragraph (d)(3)(i)(A) or (C) of this section. Where any one of the joint owners has not furnished such certification, the payment is not exempt from reporting under this section unless described in paragraph (d)(3)(i)(B) or (D) of this section.

(E) *Payee.* For determination of payee, see §1.1441-1(c)(3).

(iii) *Effective date*—(A) *General rule.* The provisions of this paragraph (d)(3) apply to payments made after December 31, 1997.

(B) *Transition rules.* A payor that holds a valid Form W-8 on a date that is 60 days after these regulations are published as final regulations in the Federal Register may treat it as a valid certificate until its validity expires under applicable provisions as in effect on April 22, 1996.

* * * * *

Par. 30. In §1.6042-3, paragraph (b), as proposed to be revised in project number INTL-52-86, published on February 29, 1988 (53 FR 5995) is amended by:

1. Removing paragraphs (b)(1) and (b)(2).

2. Redesignating paragraphs (b)(3) and (b)(4) as paragraphs (b)(1)(vii) and (b)(1)(viii), respectively.

Par. 31. Section 1.6042-3 is amended by:

1. Revising paragraph (a) introductory text.

2. Removing paragraph (b) introductory text.

3. Adding paragraph (b)(1) heading.

4. Revising paragraph (b)(1) introductory text.

5. Adding paragraphs (b)(1)(i) through (b)(1)(vi).

6. Revising paragraphs (b)(2) through (b)(4).

7. Adding paragraphs (b)(5) through (b)(7).

The additions and revisions read as follows:

§1.6042-3 Dividends subject to reporting.

(a) *In general.* Except as provided in paragraph (b) of this section, the term *dividend* for purposes of this section and §§1.6042-2 and 1.6042-4 means the amounts described in paragraphs (a)(1) and (2) of this section.

* * * * *

(b) *Exceptions*—(1) *In general.* Returns of information are not required under section 6042 and §§1.6042-2 and 1.6042-4 for amounts described in paragraphs (b)(1)(i) through (viii) of this section.

(i) Amounts paid by an insurance company to a policyholder, other than a dividend upon its capital stock.

(ii) Payments (however denominated) by a mutual savings bank, savings and loan association, or similar organization, in respect of deposits, investment certificates, or withdrawable or repurchasable shares. See, however, section 6049 and the regulations under that section for provisions requiring reporting of these payments.

(iii) Distributions or payments from sources within the United States that a payor or middleman (as defined in paragraph (b)(2) of this section) may treat as made to a beneficial owner that is a foreign person pursuant to §1.1441-1(e)(1) or, in the case of dividends paid on stock traded on a U.S. established financial market (as defined in §1.1441-6(b)(2)), pursuant to §1.1441-6(b)(2) or (3), or §1.6049-5(c).

(iv) Distributions or payments from sources outside the United States paid

outside the United States by a non-U.S. payor or a non-U.S. middleman (as defined in paragraph (b)(2)(ii) of this section). See §1.6049-5(e) for circumstances in which a payment is considered to be made outside the United States.

(v) Distributions or payments from sources outside the United States that a payor or middleman may treat as paid to a beneficial owner that is a foreign person (because such person has furnished a certificate or documentary evidence as required under §1.6049-5(c)(1) or (2)). For purposes of this paragraph (b)(1)(v), the provisions in §1.6049-5(c)(3) through (c)(6) (regarding operating rules related to the certificate of foreign status) shall apply.

(vi) Distributions or payments for the period that the amounts represent assets blocked as described in §1.1441-2(e)(3). The exemption in this paragraph (b)(1)(vi) shall terminate when payment is deemed to occur in accordance with the rules of §1.1441-2(e)(3).

* * * * *

(2) *Definitions*—(i) *Payor and middleman.* For purposes of this section, the term *payor* means any person who is required to make an information return with respect to any reportable payment, as described in section 3406(b) (including any middleman), and the term *middleman* means any person whose legal relationship to the payor or payee (including any other middleman) is of a kind described in §1.6049-4(f)(4) (as proposed in project number INTL-52-86 published in 1988-1 C.B. 892).

(ii) *Non-U.S. payor and non-U.S. middleman.* For purposes of this section, the term *non-U.S. payor* or *non-U.S. middleman* means a payor or middleman other than—

(A) A person described in section 7701(a)(30);

(B) The government of the United States, the government of any State or political subdivision thereof (or any agency or instrumentality of any of the foregoing);

(C) A controlled foreign corporation within the meaning of section 957(a); or

(D) A foreign person 50 percent or more of the gross income of which, from all sources for the three-year period ending with the close of its taxable year preceding the collection or

payment (or such part of such period as the person has been in existence), was effectively connected with the conduct of trade or business within the United States.

(3) *Applicable presumptions.* The presumptions of §1.1441-1(f) shall apply for determining the payee's status under §1.6042-3 where the required documentation is lacking, incomplete, incorrect, or unreliable.

(4) *Joint owners.* In the case of amounts paid to joint owners for which a certificate or documentation is required as a condition for being exempt from reporting under this paragraph (b), the payor or middleman must receive from each joint owner the required certification or documentation. Where any one of the joint owners has not furnished the required certification or documentation, the payment is not exempt from reporting under this section.

(5) *Payee.* For determination of payee, see §1.1441-1(c)(3).

(6) *Conversion into United States dollars of amounts paid in foreign currency.* For rules concerning foreign currency conversion, see §1.6049-4(d)-(3)(i).

(7) *Effective date—(i) General rule.* The provisions of this paragraph (b) apply to payments made after December 31, 1997.

(ii) *Transition rules.* A payor that holds a valid Form W-8 on the date that is 60 days after these regulations are published as final regulations in the Federal Register may treat it as a valid certificate until its validity expires under applicable provisions as in effect on April 22, 1996.

Par. 32. Section 1.6045-1 as proposed to be amended in project number INTL-52-86, published on February 29, 1988, at 53 FR 5996, is amended by:

1. Removing paragraph (a)(1).
2. Removing paragraphs (g)(1)(i), (g)(1)(ii), (g)(1)(iii) heading, (g)(1)(iii)(A), (g)(2), (g)(3), and (g)(4).
3. Redesignating paragraph (g)(1)-(iii)(B) as follows:

Paragraph	Redesignated as paragraph
(g)(1)(iii)(B)	(g)(1)(ii)
(g)(1)(iii)(B)(I)	(g)(1)(ii)(A)
introductory text	introductory text
(g)(1)(iii)(B)(I)(i)	(g)(1)(ii)(A)(I)

(g)(1)(iii)(B)(I)(ii)	(g)(1)(ii)(A)(2)
(g)(1)(iii)(B)(2)	(g)(1)(ii)(B)
introductory text	introductory text
(g)(1)(iii)(B)(2)(i)	(g)(1)(ii)(B)(I)
(g)(1)(iii)(B)(2)(ii)	(g)(1)(ii)(B)(2)
(g)(1)(iii)(B)(2)(iii)	(g)(1)(ii)(B)(3)
(g)(1)(iii)(B)(2)(iv)	(g)(1)(ii)(B)(4)
(g)(1)(iii)(B)(2)(v)	(g)(1)(ii)(B)(5)

4. Removing in newly designated paragraph (g)(1)(ii)(A) introductory text the language "subdivision 2 of this paragraph (g)(1)(iii)(B)" and adding "paragraph (g)(1)(ii)(B) introductory text of this section" in its place.

5. Removing in newly designated paragraph (g)(1)(ii)(B) introductory text the language "subdivision (1) of this paragraph (g)(1)(iii)(B)" and adding "paragraph (g)(1)(ii)(A)" in its place.

6. Removing in newly designated paragraph (g)(1)(ii)(B)(3) the language "§1.6049-5(j)(4)" and adding "§1.6049-5(e)" in its place.

Par. 33. Section 1.6045-1(d)(6)(iii) as proposed to be added in project number INTL-0015-91, published on March 17, 1992, at 57 FR 9224, is withdrawn.

Par. 34. Section 1.6045-1 is amended by:

1. Revising the heading of paragraph (a) and republishing paragraph (a) introductory text.
2. Revising paragraph (a)(1).
3. Revising paragraph (d)(6).
4. Revising paragraph (g)(1) heading; removing paragraph (g)(i) introductory text; and revising paragraphs (g)(1)(i) and (g)(2) through (g)(4).

The revisions read as follows:

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

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

(1) The term *broker* means any person (other than a person who is required to report a transaction under section 6043), U.S. or foreign, that, in the ordinary course of a trade or business during the calendar year, stands ready to effect sales to be made by others. A *broker* includes an obligor that regularly issues and retires its own debt obligations or a corporation that regularly redeems its own stock. However, with respect to a sale (including a redemption or retirement) effected at an office outside the United States, a *broker* includes only a person described

as a U.S. payor or U.S. middleman in §1.6049-5(d)(1). In addition, a *broker* does not include an international organization described in §1.6049-4(c)(1)-(ii)(G) that redeems or retires an obligation of which it is the issuer.

* * * * *

(d) * * *

(6) *Conversion into United States dollars of proceeds paid in foreign currency—(i) Conversion rules.* When the amount subject to reporting is paid in a currency other than the U.S. dollar, the amount subject to reporting under this section shall be determined by converting such foreign currency into U.S. dollars on the date of payment at the spot rate (as defined in §1.988-1(d)(1)) or pursuant to a reasonable spot rate convention. For example, a withholding agent may use a month-end spot rate or a monthly average spot rate. A spot rate convention must be used consistently with respect to all non-dollar amounts withheld and from year to year. Such convention cannot be changed without the consent of the Commissioner or his or her delegate.

(ii) *Effect of identification under §1.988-5(a), (b), or (c) where the taxpayer effects a sale and a hedge through the same broker—(A) In general.* In lieu of the amount reportable under paragraph (d)(6)(i) of this section, the amount subject to reporting shall be the integrated amount computed under §1.988-5(a), (b) or (c) if—

(1) A taxpayer effects through a broker a sale in exchange for nonfunctional currency (as defined in §1.988-1(c)) and hedges all or a part of such sale as provided in §1.988-5(a), (b) or (c) with the same broker; and

(2) The taxpayer complies with the requirements of §1.988-5(a), (b) or (c) and so notifies the broker prior to the end of the calendar year in which the sale occurs.

(B) *Effective date.* The provisions of this paragraph (d)(6)(ii) apply to transactions entered into on or after the date that is 60 days after these regulations are published as final regulations in the Federal Register.

* * * * *

(g) *Exempt foreign persons—(1) Brokers—(i) In general.* No return of information is required by a broker with respect to a customer who is considered to be an exempt foreign

person under this paragraph (g)(1)(i). Unless it has actual knowledge or reason to know otherwise, a broker may treat a customer as an exempt foreign person under the circumstances described in paragraph (g)(1)(i)(A) through (D) of this section. See §1.6045-1(c)(2)(ii) for reportable proceeds paid to foreign persons.

(A) With respect to a sale effected at an office of a broker inside the United States, the broker may treat the customer as an exempt foreign person if the broker complies with the procedures described in paragraph (g)(3) of this section.

(B) With respect to a sale effected at an office of a broker outside the United States, the broker may treat the customer as an exempt foreign person if the broker complies with the procedures described in paragraph (g)(3) of this section or §1.6049-5(c)(2).

(C) With respect to a redemption or retirement of stock or an obligation (the interest or original issue discount on which is described in §1.6049-5(b)-(6), (7), (10), or (11)) or the dividends on which are described in §1.6042-3(b)(1)(iv)) that is effected at an office of a broker outside the United States by the issuer (or its paying or transfer agent), the broker may treat the customer as an exempt foreign person if the broker is not also acting in its capacity as a custodian, nominee, or other agent of the payee.

(D) With respect to a sale effected by a broker at an office of the broker either inside or outside the United States, the broker may treat the customer as an exempt foreign person for the period that those proceeds are assets blocked as described in §1.1441-2(e)(3). For purposes of this paragraph (g)(1)(i)(D) and section 3406, a payment is deemed to occur in accordance with §1.1441-2(e)(3).

* * * * *

(2) *Barter exchange.* No return of information is required by a barter exchange with respect to a client or a member that the barter exchange may treat as a foreign person pursuant to the procedures described in paragraph (g)(3) of this section.

(3) *Certificate of foreign status—(i) In general.* For purposes of this paragraph (g), a broker may treat a customer as an exempt foreign person if the broker complies with the requirements of §1.1441-1(e)(1) (dealing with

reliance by a withholding agent on a beneficial owner's claim of foreign status). For purposes of this paragraph (g)(3)(i), the broker may rely on a beneficial owner withholding certificate described in §1.1441-1(e)(2). For purposes of this paragraph (g)(3)(i), in the case of an individual beneficial owner, the certificate shall include a certification that the beneficial owner has not been, and at the time the certificate is furnished, reasonably expects not to be present in the United States for a period aggregating 183 days or more during the calendar year.

(ii) *Applicable presumptions.* Absent actual knowledge or reason to know otherwise, the presumptions under §1.1441-1(f) shall apply in determining the payee's status where the required documentation is lacking, incorrect, or unreliable.

(iii) *Joint owners.* In the case of amounts paid to joint owners for which a certificate or documentation is required as a condition for being exempt from reporting under paragraph (g)(1)-(i) of this section, a broker or barter exchange must receive from each joint owner the required certification or documentation. Where any one of the joint owners has not furnished the required certification or documentation, the transaction is not exempt from reporting under paragraph (g)(1)(i) of this section.

(iv) *Payee.* For a determination of payee, see §1.1441-1(c)(3).

(v) *Operating rules.* For purposes of this paragraph (g), the provisions in §1.6049-5(c)(3) through (6) (regarding operating rules related to the certificate of foreign status) shall apply.

(4) *Effective date—(i) General rule.* The provisions of this paragraph (g) apply to payments made after December 31, 1997.

(ii) *Transition rules.* A payor that holds a valid Form W-8 on a date that is 60 days after these regulations are published as final regulations in the Federal Register may treat it as a valid certificate until its validity expires under applicable provisions as in effect on April 22, 1996.

* * * * *

Par. 35. In §1.6049-4, paragraphs (c)(1)(ii)(A) and (c)(1)(ii)(G), as proposed in project number INTL-52-86, published on February 29, 1988, at 53 FR 6000, are revised 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.*

* * * * *

(c) * * * (1) * * *

(ii) * * *

(A) *Corporation.* A corporation, as defined in section 7701(a)(3), whether domestic or foreign, is an exempt recipient. In addition, for purposes of this paragraph (c)(1), the term *corporation* includes a partnership all of whose members are corporations described in this paragraph (c)(1)(ii)(A), but only if the partnership files with the payor a certificate meeting the certification requirements set out below. Absent actual knowledge or reason to know otherwise, a payor may treat a payee as a corporation (and, therefore, as an exempt recipient) if one of the requirements of paragraph (c)(1)(ii)(A)(I), (2), (3), (4), (5), or (6) of this section are met before a payment is made.

(I) For payments other than interest, dividends, or broker proceeds, the name of the payee contains an unambiguous expression of corporate status that is "Incorporated," "Inc.," "Corporation," "Corp.," "P.C.," (but not "Company" or "Co.") or contains the term *indemnity company*, *reinsurance company*, or *assurance company*.

(2) For payments of interest, dividends or broker proceeds that are paid to a person with whom the payor does not have an account relationship, the payor may rely on the test of paragraph (c)(1)(ii)(A)(I) of this section if the payor also has a mailing address of the payee in the United States.

(3) The payor has on file a corporate resolution or similar document clearly indicating corporate status.

(4) The payor receives a Form W-9 which includes an EIN and a statement from the payee that it is a domestic corporation.

(5) The payor receives a withholding certificate described in §1.1441-1(e)-(2), that includes an employer identification number and a statement from the payee that it is a foreign corporation.

(6) The payor maintains an account for an entity claiming to be a corporation and the account was established on or before a date that is 60 days after these regulations are published as final regulations in the Federal Register and

the name of the payee contains an unambiguous expression of corporate status that is "Incorporated," "Inc.," "Corporation," "Corp.," or "P.C." (but not Company or Co.), or contains the term *insurance company, indemnity company, reinsurance company, or assurance company.*

* * * * *

(G) *International organization.* An international organization and any wholly owned agency or instrumentality thereof are exempt recipients. The term *international organization* shall have the meaning ascribed to it in section 7701(a)(18). Without requiring a certificate, a payor may treat a payee as an international organization if the payee is designated as an international organization by executive order (pursuant to 22 U.S.C. 288 through 288(f)).

* * * * *

Par. 36. Section 1.6049-4 is amended by revising paragraph (d)(3) to read as follows:

* * * * *

(d) * * *

(3) *Conversion into United States dollars of amounts paid in foreign currency—(i) Conversion rules.* When the amount subject to reporting is paid in a currency other than the U.S. dollar, the amount subject to reporting under this section shall be determined by converting such foreign currency into U.S. dollars on the date of payment at the spot rate (as defined in §1.988-1(d)(1)) or pursuant to a reasonable spot rate convention. For example, a withholding agent may use a month-end spot rate or a monthly average spot rate. A spot rate convention must be used consistently with respect to all non-dollar amounts withheld and from year to year. Such convention cannot be changed without the consent of the Commissioner or delegate.

(ii) *Special rule for §1.988-5(a) transactions where the payor on both components of a qualified hedging transaction is the same person—(A) In general.* Interest or original issue discount on a qualified debt instrument that is part of a qualified hedging transaction under §1.988-5(a) shall be computed for section 6049 reporting purposes under the rules described in §1.988-5(a)(9)(ii) if—

(I) The payor on the qualified debt instrument and the counterparty to the

§1.988-5(a) hedge are the same person; and

(2) The payee complies with the requirements of §1.988-5(a) and so notifies its payor prior to the date required for filing Form 1099 as required by this section.

(B) *Effective date.* The provisions of this paragraph (d)(3)(ii) apply to transactions entered into on or after December 31, 1997.

* * * * *

Par. 37. Section 1.6049-5, as proposed to be amended in project number INTL-52-86, published on February 29, 1988, at 53 FR 6003, is amended as follows:

1. Revising paragraphs (b) introductory text and (b)(6) through (b)(8).
2. Adding paragraphs (b)(10) through (b)(14).
3. Revising paragraphs (c) and (d).
4. Removing paragraph (e) and redesignating paragraph (j) as new paragraph (e).
5. Removing and reserving paragraph (f).
6. Revising paragraph (g).
7. Removing paragraphs (h) and (i).
8. Redesignating paragraph (k) as paragraph (f) and removing the last sentence.
9. Removing paragraph (l).

The revisions and additions read as follows:

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

* * * * *

(b) *Interest excluded from reporting requirement.* The term *interest or original issue discount* (OID) does not include—

* * * * *

(6) Amounts from sources outside the United States paid outside the United States by a non-U.S. payor or a non-U.S. middleman (as defined in paragraph (d)(2) of this section).

(7) Portfolio interest, as defined in §1.871-14(b)(1), paid with respect to bearer obligations described in section 871(h)(2)(A) or 881(c)(2)(A) or with respect to a foreign-targeted registered obligation defined in §1.6049-5(j)(4) (as proposed in project number INTL-

52-86 (1988-1 C.B. 892)) (other than by a U.S. middleman (as defined in paragraph (d)(1) of this section) that, as a custodian or nominee of the payee, collects the amount for, or on behalf of, the payee, regardless of whether the middleman is also acting as agent of the payor).

(8) Portfolio interest, as defined in §1.871-14(c)(1), paid with respect to registered obligations described in section 871(h)(2)(B) or 881(c)(2)(B).

* * * * *

(10) Amounts paid outside the United States (other than by a U.S. middleman (as defined in paragraph (d)(1) of this section) that, as a custodian or nominee or other agent of the payee, collects the amount for, or on behalf of, the payee, regardless of whether the middleman is also acting as agent of the payor) with respect to an obligation that: has a face amount or principal amount of not less than \$500,000; has a maturity (at issue) of 183 days or less; satisfies the requirements of sections 163(f)(2)(B)(i) and (ii)(I) (as if it were a registration-required obligation within the meaning of section 163(f)(2)(A)) and is issued in accordance with the procedures of §1.163-5(c)(2)(i)(D); and has on its face the following statement (or a similar statement having the same effect)—“By accepting this obligation, the holder represents and warrants that it is not a United States person (other than an exempt recipient described in section 6049(b)(4) of the Internal Revenue Code and regulations thereunder) and that it is not acting for or on behalf of a United States person (other than an exempt recipient described in section 6049(b)(4) of the Internal Revenue Code and the regulations thereunder).”

If the obligation is in registered form, it must be registered in the name of an exempt recipient described in §1.6049-4(c)(1)(ii). For purposes of this paragraph (b)(10), a middleman may treat an obligation as described in section 163(f)(2)(B)(i) and (ii)(I) and the regulations under that section if the obligation, or coupons detached therefrom, whichever is presented for payment, contains the statement described in this paragraph (b)(10).

(11) Amounts paid with respect to an account or deposit with a U.S. or foreign branch of a domestic or foreign corporation or partnership that is paid with respect to an obligation described

in paragraph (b)(11)(i) or (ii) of this section, if the branch is engaged in the commercial banking business; and the interest or OID is paid outside the United States (other than by a U.S. middleman (as defined in paragraph (d)(1) of this section) that acts as a custodian, nominee, or other agent of the payee, and collects the amount for, or on behalf of, the payee, regardless of whether the middleman is also acting as agent of the payor).

(i) An obligation is described in this paragraph (b)(11)(i) if it is not in registered form (within the meaning of section 163(f) and the regulations under that section), is described in section 163(f)(2)(B) and issued in accordance with the procedures of §1.163-5(c)(2)-(i)(C) or (D), and, in the case of a U.S. branch, is part of a larger single public offering of securities. For purposes of this paragraph (b)(11)(i), a middleman may treat an obligation as described in section 163(f)(2)(B) if the obligation, and any detachable coupons, contains the statement described in section 163(f)(2)(B)(ii)(II) and the regulations under that section.

(ii) An obligation is described in this paragraph (b)(11)(ii) if it produces income described in section 871(i)(2)-(A); has a face amount or principal amount of not less than \$500,000; satisfies the requirements of sections 163(f)(2)(B)(i) and (ii)(I) (as if it were a registration-required obligation within the meaning of section 163(f)(2)(A)) and is issued in accordance with the procedures of §1.163-5(c)(2)(i)(C) or (D); has on its face, and on any detachable coupons, the following statement (or a similar statement having the same effect)—“By accepting this obligation, the holder represents and warrants that it is not a United States person (other than an exempt recipient described in section 6049(b)(4) of the Internal Revenue Code and regulations thereunder) and that it is not acting for or on behalf of a United States person (other than an exempt recipient described in section 6049(b)(4) of the Internal Revenue Code and the regulations thereunder).” If the obligation is in registered form, it must be registered in the name of an exempt recipient described in §1.6049-4(c)(1)(ii). For purposes of this paragraph (b)(11)(ii), a middleman may treat an obligation as described in sections 163(f)(2)(B)(i) and (ii)(I) and the regulations under that section if the

obligation, or any detachable coupon, contains the statement described in this paragraph (b)(11)(ii).

(12) Amounts that the payor may treat as paid to a beneficial owner that is a foreign person pursuant to §1.1441-1(e)(1) and from which the payor or middleman is either required to withhold tax under section 1441 or the regulations under that section or would be so required but for exceptions in the regulations under section 1441 (such as, for example, under §1.1441-4 (dealing with effectively connected income) or §1.1441-6 (dealing with a reduction of rate of tax under an income tax treaty)).

(13) Amounts for the period that they represent an asset blocked as described in §1.1441-2(e)(3)). Payment of such amounts, including interest that is past due and OID on obligations that mature on or before the date that the assets are no longer blocked, is deemed to occur in accordance with the rules of §1.1441-2(e)(3).

(14) Amounts that are from sources outside the United States or original issue discount on any obligation payable less than 6 months from the date of original issue described in section 871(g)(1)(B)(i) and that a payor or middleman may treat as paid to a beneficial owner that is a foreign person (because such person has furnished a certificate or documentary evidence as required under paragraph (c) of this section).

(c) *Treatment of payee as a foreign person*—(1) *On-shore accounts or payments inside the U.S.* A payor or middleman making a payment with respect to an on-shore account, as defined in paragraph (d)(3) of this section, or making a payment inside the United States, as defined in paragraph (e) of this section, may treat the payment as made to a beneficial owner that is a foreign person if it complies with the requirements under §1.1441-1(e)(1) (dealing with reliance by a withholding agent on a beneficial owner's claim of foreign status). For purposes of this section, beneficial owner shall be as defined in §1.1441-1(c)(6)(ii)(A).

(2) *Payments made outside the United States with respect to off-shore accounts*—(i) *In general.* In the case of a payment made outside the United States with respect to an offshore account, as defined in paragraph (d)(3) of this section, a payor or middleman

may treat a payment as made to a beneficial owner (as described in §1.1441-1(b)(6)) that is a foreign person if it complies with the procedures described in paragraph (c)(1) of this section or complies with the documentary evidence procedures described in paragraph (c)(2)(ii) of this section.

(ii) *Documentary evidence.* A payor or middleman complies with the documentary evidence procedures if, prior to the payment, the payor or middleman has established procedures to obtain, review, and maintain documentary evidence sufficient to establish the identity of the beneficial owner and the status of that person as a foreign person; and the payor or middleman obtains, reviews, and maintains such documentary evidence in accordance with those procedures. A payor or middleman maintains the documents reviewed by retaining the original, certified copy, or a photocopy of the documents reviewed and noting in its records the date on which and by whom the document was received and reviewed.

(3) *Presumptions.* The presumptions of §1.1441-1(f) shall apply for determining the payee's status where the required documentation is lacking, incorrect, or unreliable.

(4) *Validity of certificates and documentary evidence.* For rules regarding the period of validity of a withholding certificate, see §1.1441-1(e)(4)(ii). Documentary evidence or a certificate that does not include a taxpayer identifying number shall be valid for a period of three years from the date received by the payor or middleman. The three-year validity period shall start from the date that the certificate is signed (or the documentation is received) until the last day of the third succeeding calendar year. For example, a withholding certificate signed on September 10, 1998, remains valid through December 31, 2001. A beneficial owner that becomes a U.S. person must, however, inform a payor or middleman within 30 days of change of status.

(5) *Retention of withholding certificate.* A payor or middleman must retain each withholding certificate, any applicable documentary evidence, and any information obtained in lieu of the withholding certificate as long as it may be relevant to the determination of the payor's or middleman's liability under the reporting provisions of this chapter and related provisions.

(6) *Standard of knowledge.* A payor or middleman may not rely on a certificate or documentary evidence described in paragraph (c)(1) or (c)(2)(ii) of this section if it has actual knowledge that the representations made therein or on the basis thereof are incorrect or if any of the required information or certifications described in §1.1441-1(f)(1)(ii) are lacking from the certificate or documentary evidence.

(7) *Joint owners.* In the case of amounts paid to joint owners and for which a certificate or documentation is required as a condition for being exempt from reporting under this paragraph (c), a payor or middleman must receive from each joint owner the required certification or documentation. Where any one of the joint owners has not furnished the required certification or documentation, the payment is not exempt from reporting under this paragraph (c).

(8) *Payee.* For determination of payee, see §1.1441-1(c)(3).

(d) *Definitions*—(1) *Payor or middleman and U.S. payor or U.S. middleman.* For purposes of this section, the term *payor* means any person who is required to make an information return with respect to any reportable payment, as described in section 3406(b) (including any middleman). For purposes of this section, the term *middleman* means any person whose legal relationship to the payor or payee (including any other middleman) is of a kind described in §1.6049-4(f)(4) (as proposed in project number INTL-52-86 published in 1988-1 C.B. 892). Thus, a person who, from within the United States, forwards an interest coupon or discount obligation on behalf of a payee for presentation, collection or payment outside the United States is also a middleman for purposes of this section (but the transfer, although subject to information reporting under this section, does not make the payment subject to backup withholding under section 3406). For purposes of this section, the term *U.S. payor* or *U.S. middleman* means a payor or middleman that is—

(i) A person described in section 7701(a)(30);

(ii) The government of the United States, the government of any State or political subdivision thereof (or any agency or instrumentality of any of the foregoing);

(iii) A controlled foreign corporation within the meaning of section 957(a); or

(iv) A foreign person 50 percent or more of the gross income of which, from all sources for the three-year period ending with the close of its taxable year preceding the collection or payment (or such part of such period as the person has been in existence), was effectively connected with the conduct of trade or business within the United States.

(2) *Non-U.S. payor or non-U.S. middleman.* A *non-U.S. payor* or a *non-U.S. middleman* is a payor or middleman that is not a U.S. payor or a U.S. middleman.

(3) *On-shore and off-shore accounts.* An *on-shore account* means an account maintained at an office or branch of a payor or middleman in the United States. An *off-shore account* means an account that is not an on-shore account.

* * * * *

(g) *Effective date*—(1) *General rule.* The provisions of paragraphs (b)(6) through (b)(14), (c), (d), and (e) of this section apply to payments made after December 31, 1997.

(2) *Transition rules.* A payor that holds a valid Form W-8 on a date that is 60 days after these regulations are published as final regulations in the Federal Register may treat it as a valid certificate until its validity expires under applicable provisions as in effect on April 22, 1996.

Par. 38. Section 1.6050N-1 is amended by:

1. Revising the section heading.
2. Redesignating paragraphs (c) and (d) as paragraphs (d) and (e), respectively.
3. Adding a new paragraph (c).
4. Revising newly designated paragraph (e).

The addition and revisions read as follows:

§1.6050N-1 Statement to recipients of royalties paid after December 31, 1986.

* * * * *

(c) *Exempted foreign-related items*—(1) *In general.* No return shall be required under paragraph (a) of this section for payments of the items described in paragraphs (c)(1)(i) through (iii) of this section.

(i) Returns of information are not required for payments of royalties that

a payor or middleman, as defined in paragraph (c)(2)(i) of this section, may treat as made to a beneficial owner that is a foreign person pursuant to §1.1441-1(e)(1) and from which the payor or middleman is either required to withhold tax under section 1441 or the regulations under that section or would be so required but for exceptions in the regulations under section 1441 (such as, for example, under §1.1441-4 (dealing with effectively connected income) or §1.1441-6 (dealing with a reduction of rate of tax under an income tax treaty)). See §1.1441-1(e)-(4)(i) in the case of payments to joint owners.

(ii) Returns of information are not required for payments of royalties from sources outside the United States made outside the United States by a non-U.S. payor or non-U.S. middleman (as defined in paragraph (c)(2)(ii) of this section). See §1.6049-5(e) for circumstances in which a payment is considered to be made outside the United States.

(iii) Returns of information are not required for payments of royalties from sources outside the United States that a payor or middleman may treat as paid to a beneficial owner that is a foreign person (because such person has furnished a certificate described in §1.6049-5(c)(1)). For purposes of this paragraph (c)(1)(iii), the presumptions in §1.6049-5(c)(3) through (6) (regarding operating rules related to the certificate of foreign status) shall apply.

(2) *Definitions*—(i) *Payor and middleman.* For purposes of this section, the term *payor* means any person who is required to make an information return with respect to any reportable payment, as described in section 3406(b), including any middleman. For purposes of this section, the term *middleman* means any person whose legal relationship to the payor or payee (including any other middleman) is of a kind described in §1.6049-4(f)(4) (as proposed in project number INTL-52-86 published in 1988-1 C.B. 892).

(ii) *Non-U.S. payor and non-U.S. middleman.* The term *non-U.S. payor* or *non-U.S. middleman* means a payor or middleman other than—

(A) A person described in section 7701(a)(30);

(B) The government of the United States, the government of any State or political subdivision thereof (or any agency or instrumentality of any of the foregoing);

(C) A controlled foreign corporation within the meaning of section 957(a); or

(D) A foreign person 50 percent or more of the gross income of which, from all sources for the three-year period ending with the close of its taxable year preceding the collection or payment (or such part of such period as the person has been in existence), was effectively connected with the conduct of trade or business within the United States.

(iii) *Applicable presumptions.* The presumptions of §1.1441-1(f) shall apply for determining the payee's status where the required documentation is lacking, incorrect, or unreliable.

(iv) *Joint owners.* In the case of amounts paid to joint owners and requiring a certificate or documentation as a condition for being exempt from reporting under this paragraph (c), the payor or middleman must receive from each joint owner the required certification. Where any one of the joint owners has not furnished the required certification, the payment is not exempt from reporting under this section.

(v) *Payee.* For determination of payee, see §1.1441-1(c)(3).

* * * * *

(e) *Effective date—(1) General rule.* The provisions of paragraph (c) of this section apply to payments made after December 31, 1997.

(2) *Transition rules.* A payor that holds a valid Form W-8 on a date that is 60 days after these regulations are published as final regulations in the Federal Register may treat it as a valid certificate until its validity expires under applicable provisions as in effect on April 22, 1996.

PART 31—EMPLOYMENT TAXES AND COLLECTION OF INCOME TAX AT SOURCE

Par. 39. The authority for part 31 continues to read in part as follows:

Authority: 26 U.S.C. 7805 * * *

Par. 40. Section 31.3401(a)(6)-1 is amended by:

- 1. Revising the section heading.
2. Revising the heading and first sentence of paragraph (e).
3. Adding paragraph (f).
4. Removing the authority citation at the end of the section.

The addition and revisions read as follows:

§31.3401(a)(6)-1 Remuneration for services of nonresident alien individuals.

* * * * *

(e) *Exemption from income tax for remuneration paid for services performed before January 1, 1998.* Remuneration paid for services performed within the United States by a nonresident alien individual before January 1, 1998 is excepted from wages and hence is not subject to withholding if such remuneration is, or will be, exempt from income tax imposed by chapter 1 of the Internal Revenue Code by reason of a provision of the Internal Revenue Code or an income tax convention to which the United States is a party.* * *

(f) *Exemption from income tax for remuneration paid for services performed after December 31, 1997.* Remuneration paid for services performed within the United States by a nonresident alien individual after December 31, 1997 is excepted from wages and hence is not subject to withholding if such remuneration is, or will be, exempt from the income tax imposed by chapter 1 of the Internal Revenue Code by reason of a provision of the Internal Revenue Code or an income tax convention to which the United States is a party. An employer may rely on a claim that the employee is entitled to an exemption from tax if it complies with the requirements of §1.1441-1(e)(1) of this chapter (for a claim based on a provision of the Internal Revenue Code) or §1.1441-4(b)(2) of this chapter (for a claim based on an income tax convention).

Par. 41. In §31.3406(d)-3, paragraph (c) is revised to read as follows:

§31.3406(d)-3 Special 30-day rules for certain reportable payments.

* * * * *

(c) *Application to foreign payees.* The rules of paragraphs (a) and (b) of this section also apply to a payee from whom the payor is required to obtain a Form W-8 (or an acceptable substitute) or is to obtain other evidence of foreign status (pursuant to relevant regulations under an applicable Internal Revenue Code section), provided the

payee represents orally or otherwise, before or at the time of the acquisition or sale of the instrument or the establishment of the account, that the payee is not a United States citizen or resident. In the case of a payment made after December 31, 1997, to a person with respect to whom indicia of foreign ownership exists, as described in §1.1441-1(f)(2)(ii)(A) of this chapter, at any time before expiration of the 30-day grace period described in this paragraph (c), the procedures described in that section shall apply, including the special grace period. The 30-day and 90-day grace periods shall run concurrently. Therefore, for example, if indicia of foreign ownership were provided on the 28th day after a payment is credited to an account, the 30-day grace period would convert to a 90-day grace period under §1.1441-1(f)(2)(ii)(A) of this chapter, of which 28 days would have already elapsed.

Par. 42. In §31.3406(g)-1, paragraph (e) is added to read as follows:

§31.3406(g)-1 Exception for payments to certain payees and certain other payments.

* * * * *

(e) *Certain reportable payments made outside the United States by foreign persons, foreign offices of United States banks and brokers, and others.* A payor of a reportable payment or transfer is not required to backup withhold under section 3406 if such reportable payment or transfer is of a kind that is exempt from reporting if documentary evidence described in §1.6049-5(2)(ii) of this chapter is provided to the payor, unless the payor has actual knowledge that the payee is a United States person. In addition, amounts paid with respect to notional principal contracts described in §1.6041-1(d)(5) of this chapter are not subject to backup withholding if they are paid outside the United States, unless the payor has actual knowledge that the payee is a United States person.

Par. 43. Section 31.3406(h)-2 is amended by:

- 1. Removing the heading of paragraph (e)(1).
2. Removing the paragraph designation (e)(1).
3. Removing paragraph (e)(2).

4. Revising paragraph (a)(3)(i) to read as follows:

§31.3406(h)-2 *Special rules.*

(a) * * *

(3) *Joint foreign payees*—(i) *In general.* If the relevant payee listed on an account or instrument provides the penalties of perjury statement regarding its foreign status, withholding under section 3406 applies unless—

(A) Every joint payee provides the statement regarding foreign status (under the provisions of chapter 3 and chapter 61 of the Internal Revenue Code and the regulations under those provisions); or

(B) Any one of the joint owners who has not established foreign status provides a taxpayer identifying number to the payor in the manner required in §31.3406(d)-1.

* * * * *

Par. 44. Section 31.6413(a)-3 is amended as follows:

1. In paragraph (a)(1)(iii), the language “(including the certification relating to foreign status described in §1.6049-5(b)(2)(iv) of this chapter or §1.6045-1(g)(1) of this chapter)” is removed and “(including the documentation required under §§1.1441-1(e)(1), 1.6045-1(g)(3), and 1.6049-5(c) of this chapter)” is added in its place.

2. Paragraph (a)(1)(ii) is amended by removing “or” at the end of the paragraph and paragraph (a)(1)(iii) is amended by removing the period at the end of the paragraph and adding “; or” in its place.

3. Paragraph (a)(1)(iv) is added.

4. Paragraphs (a)(2) and (b)(2) are revised.

The addition and revisions read as follows:

§31.6413(a)-3 *Repayment by payor of tax erroneously collected from payee.*

(a) * * * (1) * * *

(iv) The amount is withheld because a payor imposed backup withholding on a payment made to a person because the payee failed to furnish the required documentation described in §§1.1441-1(e)(1), 1.6045-1(g)(3), and 1.6049-5(c) of this chapter and the payee subsequently furnishes, completes, or

corrects the required documentation. The required documentation must be furnished, completed, or corrected prior to the end of the calendar year in which the payment is made and prior to the time the payor furnishes a Form 1099 to the payee with respect to the payment for which the withholding erroneously occurred.

(2) For purposes of paragraph (a)(1) of this section (other than erroneous withholding occurring under the circumstances described in paragraph (a)(1)(iv) of this section), if a payor or broker withholds because the payor or broker has not received a taxpayer identifying number or required certification and the payee subsequently provides a taxpayer identifying number or a required certification to the payor, the payor or broker may not refund the amount to the payee.

(b) * * *

(2) *Adjustment after the deposit of the tax*—(i) *In general.* Except as provided in paragraph (b)(2)(ii) of this section, if the amount erroneously withheld has been deposited prior to the time that the refund is made to the payee, the payor or broker may adjust any subsequent deposit of the tax collected under chapter 24 of the Internal Revenue Code that the payor or broker is required to make in the amount of the tax that has been refunded to the payee.

(ii) *Erroneous withholding from a payee that is a foreign person.* Where a payor withholds in error from a payee that is a nonresident alien or foreign person, as described in paragraph (b)(1) of this section, the payor may refund some or all of the amount subject to backup withholding under section 3406. A refund may be paid in accordance with the requirements of this paragraph (b)(2)(ii) where the required documentation is furnished, completed, or corrected prior to the end of the calendar year in which the payment is made and prior to the time the payor furnishes a Form 1099 to the payee with respect to the payment for which the withholding erroneously occurred. The amount of the refund will be the amount erroneously withheld less the amount of tax required to be withheld, if any, under chapter 3 of the Internal Revenue Code. With respect to the amount of the payment to the foreign person and the amount of tax required to be withheld under chapter 3 of the Internal Revenue Code, returns must be made

in accordance with the requirements of §1.1461-1(b) and (c) of this chapter.

PART 35a—TEMPORARY EMPLOYMENT TAX REGULATIONS UNDER THE INTEREST AND DIVIDEND TAX COMPLIANCE ACT OF 1983

Par. 45. The authority for part 35a is amended by removing the entries for §35a.9999-3, §35a.9999-3A and §35a.9999-4T to read in part as follows:

Authority: 26 U.S.C. 7805 * * *

§§35a.9999-1 through 35a.9999-3A, and 35a.9999-4T [Removed]

Par. 46. Sections 35a.9999-1 through 35a.9999-3A, and 35a.9999-4T are removed.

PART 301—PROCEDURE AND ADMINISTRATION

Par. 47. The authority citation for part 301 continues to read in part as follows:

Authority: 26 U.S.C. 7805. * * *

Par. 48. Section 301.6109-1 as proposed to be amended in project number INTL-0024-94, published on June 8, 1995, at 60 FR 30214, is amended as follows:

1. Paragraph (b)(2)(iii) is amended by removing “and” at the end of the paragraph.

2. Paragraph (b)(2)(iv) is revised.

3. Paragraph (b)(2)(v) is added.

4. Paragraph (c) is revised.

The revisions and additions read as follows:

§301.6109-1 *Identifying numbers.*

* * * * *

(b) * * *

(2) * * *

(iv) A foreign person that makes a return of tax under this title (including income, estate, and gift tax returns) but excluding information returns, statements, or documents;

(v) A foreign person that furnishes a withholding certificate described in §1.1441-1(e)(2) or (e)(3) of this chapter to the extent required under §1.1441-1(e)(4)(vii) of this chapter.

(c) *Requirement to furnish another’s number.* Every person required under

this title to make a return, statement, or other document must furnish such taxpayer identifying numbers of other U.S. persons and foreign persons that are described in paragraph (b)(2)(i), (ii), (iii), or (v) of this section as required by the forms and the accompanying instructions. The taxpayer identifying number of any person furnishing a withholding certificate referred to in paragraph (b)(2)(v) of this section shall also be furnished if it is actually known to the person making a return, statement, or other document described in this paragraph (c). If the person making the return, statement, or other document does not know the taxpayer identifying number of the other person, and such other person is one that is described in paragraph (b)(2)(i), (ii), (iii), or (v) of this section, such person must request the other person's number. The request should state that the identifying number is required to be furnished under authority of law. When the person making the return, statement, or other document does not know the number of the other person, and has complied with the request provision of this paragraph (c), such person must sign an affidavit on the transmittal document forwarding such returns, statements, or other documents to the Internal Revenue Service, so stating. A person required to file a taxpayer identifying number shall correct any errors in such filing when such person's attention has been drawn to them.

* * * * *

Par. 49. Section 301.6114-1 is amended by:

1. Revising paragraph (a)(1)(ii).
2. Revising paragraph (b)(4)(ii) introductory text, and adding paragraphs (b)(4)(ii)(C) and (b)(4)(ii)(D)
3. Revising paragraphs (c)(1) and (d)(4)(v):

The revisions read as follows:

§301.6114-1 Treaty-based return positions.

(a) * * * (1) * * *

(ii) If a return of tax would not otherwise be required to be filed, a return must nevertheless be filed for purposes of making the disclosure required by this section. For this purpose, such return need include only the taxpayer's name, address, taxpayer identifying number, and be signed

under the penalties of perjury (as well as the subject disclosure). Also, the taxpayer's taxable year shall be deemed to be the calendar year (unless the taxpayer has previously established, or timely chooses for this purpose to establish, a different taxable year). In the case of a disclosable return position relating solely to income subject to withholding (as defined in §1.1441-2(a) of this chapter), however, the statement required to be filed in paragraph (d) of this section must instead be filed at times and in accordance with procedures to be published by the Internal Revenue Service.

* * * * *

(b) * * *

(4) * * *

(ii) A treaty exempts from tax, or reduces the rate of tax on, fixed or determinable annual or periodical income subject to withholding under sections 1441 or 1442 that a foreign person receives from a U.S. person, but only if described in paragraphs (b)(4)-(ii)(A) and (B) of this section, or paragraph (b)(4)(ii)(C) or (D) of this section.

* * * * *

(C) For payments made after December 31, 1997, with respect to a treaty that contains a limitation on benefits article, that—

(1) The treaty exempts from tax, or reduces the rate of tax on income subject to withholding (as defined in §1.1441-2(a) of this chapter) that is paid to a foreign person (other than a State, including a political subdivision or local authority) that is the beneficial owner of the income and the beneficial owner is related to the person obligated to pay the income within the meaning of sections 267(b) and 707(b), and the income exceeds \$500,000; and

(2) A foreign person (other than an individual or a State, including a political subdivision or local authority) meets the requirements of the limitation on benefits article of the treaty; or

(D) For payments made after December 31, 1997, with respect to a treaty that imposes any other conditions for the entitlement of treaty benefits, for example as a part of the interest, dividends, or royalty article, that such conditions are met;

* * * * *

(c) *Reporting requirement waived.*
* * *

(1) Notwithstanding paragraph (b)(4) or (5) of this section, that a treaty has reduced the rate of withholding tax otherwise applicable to a particular type of fixed or determinable annual or periodical income subject to withholding under section 1441 or 1442, such as dividends, interest, rents, or royalties to the extent such income is beneficially owned by an individual or a State (including a political subdivision or local authority);

* * * * *

(d) * * *

(4) * * *

(v) The provision(s) of the limitation on benefits article (if any) in the treaty that the taxpayer relies upon to meet the requirements of that article and a statement of the relevant facts in support of the taxpayer's claim.

* * * * *

Par. 50. Section 301.6402-3 is amended as follows:

1. Paragraph (e) is revised as set forth below.

2. Removing the OMB parenthetical and the authority citation at the end of the section.

§301.6402-3 Special rules applicable to income tax.

* * * * *

(e) In the case of a nonresident alien individual or foreign corporation, the appropriate income tax return on which the claim for refund or credit is made must contain the tax identification number of the taxpayer required pursuant to section 6109 and the entire amount of income of the taxpayer subject to tax, even if the tax liability for that income was fully satisfied at source through withholding under chapter 3 of the Internal Revenue Code. Also, if the overpayment of tax resulted from the withholding of tax at source under chapter 3 of the Internal Revenue Code, a copy of the Form 1042-S required to be provided to the beneficial owner pursuant to §1.1461-1(c)(1)-(i) of this chapter must be attached to the return. For purposes of claiming a refund, the Form 1042-S must include the taxpayer identifying number of the beneficial owner even if not otherwise

required. No claim of refund or credit under chapter 65 may be made by the taxpayer for any amount that the withholding agent has repaid to the taxpayer pursuant to §1.1461-2(a)(2) of this chapter or that was subject to a set-off pursuant to §1.1461-2(a)(3) of this chapter. Upon request, a taxpayer must also submit such documentation as the Commissioner (or delegate), the District Director, or the Assistant Commissioner (International), may require establishing that the taxpayer is the beneficial owner of the income for which a claim of refund or credit is being made.

PART 502—[REMOVED]

Par. 51. Part 502 is removed.

PART 503—[REMOVED]

Par. 52. Part 503 is removed.

PART 509—[AMENDED]

Par. 53. The authority citation for part 509 is revised and the authority citation for “Subpart—General Income Tax” removed, to read as follows:

Authority: 26 U.S.C. 62, 3791 and 7805.

Par. 54. Part 509 is amended as follows:

1. Subpart—Withholding of Tax consisting of §§509.1 through 509.10 is removed.

2. In §509.103, paragraph (e) is removed and reserved.

3. In §509.117, paragraph (a) is removed and reserved.

4. Sections 509.119 and 509.122 are removed.

PART 513—[AMENDED]

Par. 55. The authority citation for part 513 is revised to read as follows:

Authority: 26 U.S.C. 62.

Par. 56. Part 513 is amended as follows:

1. Section 513.1 is removed.

2. Section 513.2 is amended as follows:

a. Paragraphs (a)(1) and (a)(2) are removed and reserved.

b. Paragraph (a)(4) is removed.

c. Paragraph (b) is removed and reserved.

d. Paragraphs (c) and (d) are removed.

3. Section 513.3 is amended as follows:

a. Paragraph (a)(1) is removed and reserved.

b. Paragraphs (b) and (c) are removed.

4. Section 513.4 is amended as follows:

a. Paragraph (a) is removed and reserved.

b. Paragraphs (c) and (d) are removed.

5. Section 513.5 is amended as follows:

a. Paragraph (a) is removed and reserved.

b. Paragraphs (c) and (d) are removed.

PART 514—[AMENDED]

Par. 57. The authority citation for part 514 is revised to read as follows:

Authority: 26 U.S.C. 7805.

Par. 58. Part 514 is amended as follows:

1. The undesignated centerheading preceding §514.1 and §§514.1 through 514.10 are removed.

2. Sections 514.20 through 514.21 are removed.

3. In §514.22, paragraph (c) is removed.

4. Sections 514.23 through 514.32 are removed.

5. Sections 514.101 through 514.117 are removed.

PART 516—[REMOVED]

Par. 59. Part 516 is removed.

PART 517—[REMOVED]

Par. 60. Part 517 is removed.

PART 520—[REMOVED]

Par. 61. Part 520 is removed.

PART 521—[AMENDED]

Par. 62. The authority citation for part 521 is revised to read as follows:

Authority: 26 U.S.C. 62, 143, 144, 211, and 231.

Par. 63. Part 521 is amended as follows:

1. Subpart—Withholding of Tax consisting of §§521.1 through 521.8 is removed.

2. In §521.103, paragraph (d) is removed and reserved.

Margaret Milner Richardson,
Commissioner of Internal Revenue.

(Filed by the Office of the Federal Register on April 15, 1996, 8:45 a.m., and published in the issue of the Federal Register for April 22, 1996, 61 F.R. 17614)

Correction of 1995 Instructions for Schedule SSA (Form 5500), Annual Registration Statement Identifying Separated Participants With Deferred Vested Benefits

Announcement 96-38

The Schedule SSA (Form 5500) instructions for when to file for single employer plans, incorrectly states that a separated plan participant with deferred vested benefits must be reported no later than the due date (including extensions) of the Schedule SSA filed for the plan year during which the separation occurred.

The instructions should state that a separated plan participant with deferred vested benefits must be reported no later than the due date (including extensions) of the Schedule SSA filed for the plan year following the plan year in which the separation occurred.

Deletions from Cumulative List of Organizations Contributions to Which Are Deductible Under Section 170 of the Code

Announcement 96-39

The name of an organization that no longer qualifies as an organization described in section 170(c)(2) of the Internal Revenue Code of 1986 is listed below.

Generally, the Service will not disallow deductions for contributions made to a listed organization on or before the date of announcement in the Internal Revenue Bulletin that an organization no longer qualifies. However, the Service is not precluded from disallowing a deduction for any contributions made after an organization ceases to qualify under section 170(c)(2) if the organization has not

timely filed a suit for declaratory judgment under section 7428 and if the contributor (1) had knowledge of the revocation of the ruling or determination letter, (2) was aware that such revocation was imminent, or (3) was in part responsible for or was aware of the activities or omissions of the organization that brought about this revocation.

If on the other hand a suit for declaratory judgment has been timely filed, contributions from individuals and organizations described in section 170(c)(2) that are otherwise allowable will continue to be deductible. Protection under section 7428(c) would begin on **(DATE)** 1996, and would end on the date the court first determines that the organization is not described in section 170(c)(2) as more particularly

set forth in section 7428(c)(1). For individual contributors, the maximum deduction protected is \$1,000, with a husband and wife treated as one contributor. This benefit is not extended to any individual who was responsible, in whole or in part, for the acts or omissions of the organization that were the basis for revocation.

Families for Children
Golden Valley, MN

**Correction of Errors in TD 8653,
1996-12 I.R.B. 4**

Announcement 96-40

TD 8653 was published in the

Federal Register on January 8, 1996 (61 Fed. Reg. 517), and corrected on March 21, 1996 (61 Fed. Reg. 11547). When reprinted in I.R.B. 1996-12 on March 18, 1996, the document contained the following typographical errors unrelated to the March 21, 1996, correction: Section 1.1221-2(g)(6)(v) of the Income Tax Regulations, as reprinted, contains references to ‘May 8, 1996’. The correct date, which appears in the *Federal Register*, is ‘May 7, 1996’. These corrections (and the correction reflected in the *Federal Register* on March 21, 1996) will appear in TD 8653 when it is republished in Cumulative Bulletin 1996-1.

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior

ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1986 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings.

If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified* and *superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C.—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.

E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contribution Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.

PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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RR	Revenue Ruling
RP	Revenue Procedure
TD	Treasury Decision
CD	Court Decision
PL	Public Law
EO	Executive Order
DO	Delegation Order
TDO	Treasury Department Order
TC	Tax Convention
SPR	Statement of Procedural Rules
PTE	Prohibited Transaction Exemption

EMPLOYMENT TAXES

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26 CFR 31.3402(r)–1 added; 31.3402(r)–IT, removed; withholding on distributions of Indian gaming profits to tribal members (TD 8634) 3, 17

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26 CFR 31.3406–0 revised; 31.3406(a)–1—31.3406(i)–1, 31.6051–4, 31.6413(a)–3, added; 35a.9999.OT, 35a.3406–2, removed; 301.6109–1, amended; backup withholding statement mailing requirements, and due diligence (TD 8637) 4, 29

26 CFR 31.6051–1(d), 31.6071(a)–1(a)(3), amended; 31.6051–2(c), 31.6081(a)–1(a)(3), 301.6011–2(c)(4)(i), revised; time for furnishing wage statements on termination of employer's operations (TD 8636) 4, 64; correction (Notice 21) 14, 30

26 CFR 31.6302–IT(h)(1)(ii)(A)(2), added; 31.6302–IT(h)(2), –(3), –(7), –(8), revised; federal tax deposits by electronic funds transfer (TD 8661) 17, 7

26 CFR 33 and 38, removed; parts declared obsolete (TD 8655) 12, 9

26 CFR 301.6109–1, amended grantor trust reporting requirements (TD 8633) 4, 20

26 CFR 301.7507–1, 301.7507–0, amended; treatment of acquisition of certain financial institutions (TD 8641) 6, 4

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26 CFR 301.6103(n)–1, amended; disclosure of returns and return information to procure property or services for tax administration purposes (DL–1–95) 6, 28

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26 CFR 20.2035–1; 26 CFR 23 and 24, 25.2517–1, removed; regulations declared obsolete (TD 8655) 12, 9

26 CFR 301.6109–1, amended; grantor trust reporting requirements (TD 8633) 4, 20

26 CFR 301.6011–2(c)(4)(i), revised; time for furnishing wage statements on termination of employer's operations (TD 8636) 4, 64

26 CFR 301.7507–1, 301.7507–0, amended; treatment of acquisition of certain financial institutions (TD 8641) 6, 4

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26 CFR 20.7520–3, amended; actuarial tables exceptions (TD 8630) 3, 19

26 CFR Part 26, revised; 301.9100–7T, amended; generation-skipping transfer tax (TD 8644) 7, 16

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26 CFR 25.2517–1, removed; regulations declared obsolete (TD 8655) 12, 9

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26 CFR 25.2522(c)-3, 25.7520-3 amended; actuarial tables exceptions (TD 8630) 3, 19; correction (Notice 22) 14, 30

26 CFR 25.2702-3, amended; grantor trust reporting requirements (TD 8633) 4, 20

26 CFR 25.2702-5, 25.2702-7, amended; sale of residence from qualified personal residence trust (PS-4-96) 18, 5

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26 CFR 48.4081-8; 48.4082-1, revised; 41.4101-1, amended; gasoline and diesel fuel dye injection systems (PS-6-95) 16, 27

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26 CFR 301.6103(n)-1, amended; disclosure of returns and return information to procure property or services for tax administration purposes (DL-1-95) 6, 28

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26 CFR 48.4081-4, 48.4082-1, -2T, 48.4101-3T, -4T, 48.6427-8T, -9T, removed; 48.4082-1, -2, 48.4101-1, -2, 48.6427-8, -9, added; 48.4041-0T, removed; 48.4041-1, -2, -2T, removed; 48.4041-21, amended; 48.4041-15—48.4041-21, transferred; 48.4042-1, amended; 48.4064-1(e)(2), amended; 48.4081-1, -2, -3, revised; 48.4081-4, -5, -7, amended; 48.4081-6, -8, revised; 48.4081-10T, -11T, -12T, removed; 48.4082-1, revised; 48.4082-2T, -3T, -4T, 48.4083, removed; 48.4082-2, -3, -4, 48.4083-1, added; 48.4101-2T, -3, -3T, -4T, removed; 48.4102-1, amended; 48.4221, removed; 48.4221-1, -2, -5, amended; 48.4221-8, -9, -10, -12, removed; 48.4221-11, redesignated; 48.4222(a)-1, (b)-1, revised; 48.4222(d)-1, amended; 40.6011(a)-1(b), amended; 40.6011(a)-3T, removed; Part 42,

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26 CFR 301.9100-7T, amended; generation-skipping transfer tax (TD 8644) 7, 16

26 CFR 53.4941(d)-2, amended; self-dealing for private foundations (TD 8639) 5, 12

26 CFR 301.6011-2(c)(4)(i), revised; time for furnishing wage statements on termination of employer's operations (TD 8636) 4, 64

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26 CFR 1.125–3, added; effect of Family and Medical Leave Act of 1993 on the operation of cafeteria plans (EE–20–95) 5, 15

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26 CFR 1.863–0, added; 1.863–1, –2, –3, revised; 1.863–4, amended; 1.863–5, removed; source of income from sales of inventory and natural resources produced in one jurisdiction and sold in another (INTL–3–95) 6, 29

26 CFR 1.882–5, 1.884–1, amended; effectively connected income and branch profits tax (INTL–54–95) 14, 39

26 CFR 1.1254–0, 1.1254–4, amended; treatment of gain from disposition of interest in certain natural resource recapture property by S corporations (PS–7–89) 8, 24

26 CFR 1.6081–4(a), revised: 1.6081–4(d), added; automatic extension of time for filing individual tax returns (IA–41–93) 11, 29

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26 CFR 31.3121(v)(2)–1, –2, added; FICA taxation amounts under employee benefit plans (EE–142–87) 12, 13

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26 CFR 301.6103(n)–1, amended; disclosure of returns and return information to procure property or services for tax administration purposes (DL–1–95) 6, 28

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26 CFR 1.411(d)–6T, added; notice of significant reduction in the rate of future benefit accrual (TD 8631) 3, 7

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26 CFR 1.597–1—1.597–7, added; 301.7507–1, 301.7507–9, amended; treatment of acquisition of certain financial institutions (TD 8641) 6, 4

26 CFR 1.671–4, revised; 1.6012–3, 301.6109–1, amended; grantor trust reporting requirements (TD 8633) 4, 20

26 CFR 1.704–4, 1.737–1 through 1.737–5, added; recognition of gain or loss by contributing partner on distribution of contributed property or other property (TD 8642) 7, 4

26 CFR 1.861–8, amended; 1.861–17, added; allocation and apportionment of research and experimental expenditures (TD 8646) 8, 10

26 CFR 1.861–9T, amended; 1.822–0, added; 1.882–5, revised; interest expense deduction of foreign corporations (TD 8658) 14, 13

26 CFR 1.864–4, 1.871–12, 1.884–0(b), amended; 1.884–1(d)(4), 1.884–2T(a)(5), 1.884–4(b)(1) and (2), revised; 1.884–1(i)(4), 1.884–2T(a)(6), 1.884–4(e)(1) and (2), added; effectively connected income and branch profits tax (TD 8657) 14, 4

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