



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224
October 20, 2000

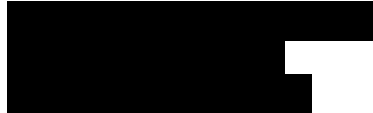
OFFICE OF
CHIEF COUNSEL

Number: **INFO 2000-0420**

Release Date: 12/29/2000

UIL No.: 6042.00-00

CC:PA:APJP:1:NRose
COR-118157-00



Dear Mr. [REDACTED]:

This is in response to your letter of September 6, 2000, which is a follow-up to your letter of March 20, 2000, regarding the reporting of dividends from mutual funds. You requested that the Internal Revenue Service instruct your bank to change the way it reports its clients' money market mutual fund dividends on Form 1099-DIV. Your letters indicate that the bank reports ordinary dividends on the Form 1099-DIV in an amount greater than that shown on the clients' year-end statement from the mutual fund. The difference between the two figures is shown as a "service fee" (or investment expense) on the Form 1099-DIV. You noted that other mutual funds report dividends net of investment expenses.

As discussed below, the reporting of dividends under the information reporting rules depends on whether the fund is a nonpublicly offered mutual fund. Since we do not have the relevant information about this fund, we will set forth the applicable rules so that you can determine whether it is publicly or nonpublicly offered.

Section 6042 of the Internal Revenue Code (the Code) provides that payors of dividends of \$10 or more per year, must file a return according to the regulations, and provide a statement showing such payments to the payee of the dividends. Distributions from mutual funds are considered dividends for purposes of section 6042.

With respect to mutual funds, the determination of whether the amount of ordinary dividends can be net of the fund's expenses depends on whether the fund is publicly offered or nonpublicly offered. Section 67 of the Code and the regulations thereunder provides, in general, that pass-through entities, such as regulated investment companies (commonly known as mutual funds), may not provide indirect deductions by netting certain expenses against dividends. However, only nonpublicly offered mutual funds are subject to this rule, as the Code provides an exception for publicly offered mutual funds. Shareholders of nonpublicly offered mutual funds may only be able to

COR-118157-00

deduct their share of the fund's expenses if they itemize deductions, and only as miscellaneous deductions on their Schedule A, Form 1040.

To reflect this rule, the Instructions for Form 1099-DIV state that the filer should enter ordinary dividends in box 1, and the stockholder's pro rata share of certain deductible expenses from nonpublicly offered mutual funds in Box 5, Investment Expenses. The amount from Box 5 must be included in the amount in Box 1. Thus, the form instructs nonpublicly offered funds to report dividends in exactly the manner that your bank reported.

The Form 1099-DIV itself contains similar instructions. The form's Instructions for the Recipient direct the recipient to include the amount from Box 1, on the Ordinary Dividend line of Form 1040. The amount shown in Box 5 is the recipient's share of the fund's expenses, and may be deductible by the recipient on Schedule A, Form 1040, as a miscellaneous deduction. For your convenience, we have attached these instructions.

Therefore, your bank's reporting of your mutual fund dividends on Form 1099-DIV in this manner was correct, so long as it is a nonpublicly offered fund. "Nonpublicly offered regulated investment company" is defined as a fund which is not (1) continuously offered pursuant to a public offering; (2) regularly traded on an established securities market; or (3) held by at least 500 persons at all times during the taxable year. If any of those three conditions are met, the fund is publicly offered and would not report its dividends in this manner. See section 67(c)(2)(B)(i) of the Code and section 1.67-2T(g)(3) of the regulations.

We hope this is helpful. If you need further assistance, please call Nancy Rose (ID #50-06240) at (202) 622-4910.

Sincerely,

John J. McGreevy
Acting Senior Technician Reviewer
Branch 1
Administrative Provisions and Judicial
Practice

Attachments