



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

OFFICE OF
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The Honorable Todd Russell Platts
Member, U.S. House of Representatives
2209 East Market Street
York, Pennsylvania 17402

Dear Congressman Platts:

This letter responds to your inquiry dated June 16, 2009, on behalf of your constituent, . asks about the proper year for reporting interest income on an 18-month certificate of deposit (CD).

states that opened the CD at a bank in January 2008. The CD matures in July 2009, at which time is entitled to receive the interest accrued during the 18-month term. Early in 2009, the bank issued a Form 1099-INT reporting interest income that accrued on the CD during 2008.

contends that is not subject to tax on the interest in 2008 because did not make any withdrawals during 2008. further contends that is not taxed in 2008 under the "constructive receipt" rules in section 1.451-2 of the Income Tax Regulations (the Regulations) because the terms of the CD impose an early withdrawal penalty equal to six months' interest, and that penalty is a "substantial limitation or restriction" (within the meaning of those regulations) on ability to control the interest in 2008.

Whether an early withdrawal penalty is a substantial limitation or restriction on a taxpayer's ability to control receipt of interest does not determine the tax treatment if the term of the CD exceeds one year. Although a substantial early withdrawal penalty can result in no constructive receipt under section 1.451-2 of the Regulations, the original issue discount (OID) rules in section 1272 of the Internal Revenue Code (the Code) may require taxpayers to include interest as it accrues on CDs that have a stated maturity date of more than one year. See section 1272(a)(2)(C) of the Code and section 1.1275-1(d) of the Regulations.

A CD generally has OID if the amount deposited with the bank when the CD is issued is less than the amount payable at maturity (including certain stated interest payable on the CD). Any stated interest on a CD not paid or constructively received at least annually over the term of the CD is OID (see section 1273 of the Code and section 1.1273-1 of the Regulations). If the stated term of the CD is more than one year, and the stated interest is not actually or constructively received at least annually over the 18-month term of the CD, then the CD has OID in an amount equal to the stated interest payable at maturity on the CD. Therefore, even though there is no actual or constructive receipt of stated interest on the CD during 2008, your constituent must include in his 2008 income the OID (stated interest) that accrues on the CD during 2008 under the OID rules.

The issuer of a CD that has OID should provide to the taxpayer a Form 1099-OID, or similar statement, if the total OID for the calendar year is \$10 or more. This statement will show the amount of OID and the stated interest the taxpayer must include in income. If a taxpayer receives an incorrect Form 1099, he or she should contact the issuer to obtain a correct form, which should be marked "Corrected."

I hope this information is helpful. If you have any questions, please call
or at .

Sincerely,

George J. Blaine
Associate Chief Counsel
(Income Tax and Accounting)