

Internal Revenue Service

Department of the Treasury
Washington, DC 20224

Number: **201539025**
Release Date: 9/25/2015

Third Party Communication: None
Date of Communication: Not Applicable

Index Number: 6041.00-00, 6050W.00-00,
3406.00-00

Person To Contact: _____, ID No. _____

Telephone Number: _____

Refer Reply To:
CC:PA:02
PLR-146802-14

Date:
June 25, 2015

LEGEND

Taxpayer:

Customers:

Dear _____ :

This is in response to your ruling request submitted by your authorized representative concerning the federal income tax reporting requirements for Taxpayer under sections 6050W and 6041 of the Internal Revenue Code (Code) and the regulations thereunder. Specifically, Taxpayer requested a ruling that it is not a third party settlement organization operating a third party payment network and therefore does not have an information reporting obligation under section 6050W. Taxpayer also requested a ruling that it is not subject to information reporting under section 6041 or backup withholding under section 3406.

FACTS

Taxpayer is an _____ company providing _____ to its Customers through a number of _____

as well as through third party _____. Taxpayer also provides _____ to _____ Customers through distribution agreements with _____

Through these various channels, Customers can

from third-party providers.

Taxpayer's Agreements With Customers

Through agreements with Customers and Providers, Taxpayer with Providers on behalf of Customers. Taxpayer enters into agreements with Customers, in which it agrees to with Providers. As part of these arrangements, Taxpayer agrees to make payment to Providers of . Taxpayer also provides ancillary services, such as

. Taxpayer determines the amount charged to Customers for Providers' ; Providers have no control over, or knowledge of, this amount.

Payments made by Customers to Taxpayer for to be provided by Providers are made by credit card or debit card. Taxpayer acknowledges that these transactions between Taxpayer and Customer are payment card transactions subject to information reporting under section 6050W. Taxpayer receives Forms 1099-K for these transactions from various merchant acquiring entities or electronic payment facilitators. These transactions are not at issue in this ruling.

Taxpayer's Agreements With Providers

Taxpayer also enters into agreements with Providers, through which Taxpayer of Providers'. Customers are not a party to the agreements between Taxpayer and Providers. Under these agreements, Providers agree to provide by Taxpayer's Customers and agree to made by Customers through Taxpayer. Similarly, under the agreements Taxpayer agrees to Providers',

monthly or twice monthly payments to Providers for

and third party affiliated – Payment process

With respect to orders received through and affiliated third-party , Taxpayer collects payment from Customers at the time the are . Once a Provider has provided , Taxpayer pays the Provider the rate for its . Taxpayer pays Providers on a monthly or twice monthly basis, typically by automated clearinghouse network or other electronic funds transfer.

Third party merchants – Payment process

With respect to orders received through third party merchants, Taxpayer collects payment from the third party merchant after the Provider provided the

to the Customer. Once the Provider has provided _____, Taxpayer pays the Provider the _____ for its _____. Taxpayer pays Providers on a monthly or twice monthly basis, typically by automated clearinghouse network or other electronic funds transfer.

LAW AND ANALYSIS

Section 6050W

Section 6050W of the Code, as enacted by the Housing Assistance Tax Act of 2008, requires payment settlement entities to file an information return for each calendar year with respect to payments made in settlement of reportable payment transactions. Section 6050W covers two types of transactions: (1) payment card transactions and (2) third party network transactions. A payment settlement entity in the payment card context is a merchant acquiring entity; in the third party network context, it is a third party settlement organization (TPSO). I.R.C. § 6050W(b)(1).

The Code and regulations define a merchant acquiring entity as the bank or other organization with the contractual obligation to make payments to participating payees in payment card transactions. A payment card transaction is any transaction in which a payment card is accepted as payment. I.R.C. §§ 6050W(b)(2)-(3), 6050W(c)(3); Treas. Reg. § 1.6050W-1(b)(1)-(2).

The Code and regulations define a TPSO as the central organization that has the contractual obligation to make payments to the participating payees of third party network transactions. I.R.C. § 6050W(b)(3); Treas. Reg. § 1.6050W-1(c)(2). A third party network transaction is any transaction that is settled through a third party payment network. I.R.C. § 6050W(c)(3). A central organization is a TPSO with a reporting obligation if it provides a third party payment network that allows purchasers to transfer funds to providers of goods and services. Treas. Reg. § 1.6050W-1(c)(2). A third party payment network is any agreement or arrangement that (i) involves the establishment of accounts with a central organization by a substantial number of providers of goods or services who are unrelated to the central organization and who have agreed to settle transactions for the provision of goods or services with purchasers according to the terms of agreements; (ii) provides standards and mechanisms for settling the transactions; and (iii) guarantees payments to the providers of goods and services in settlement of transactions with purchasers. I.R.C. § 6050W(d)(3); Treas. Reg. § 1.6050W-1(c)(3).

Example 17, *Healthcare network*, of the regulations under section 6050W provides an illustration of circumstances in which there is a third party but no third party network. Treas. Reg. § 1.6050W-1(e), *Example 17*. The health care network is operated by a health carrier that (i) collects premiums from covered members, pursuant to contractual agreements between the covered member and the health carrier, to allow the covered members access to the health care network, and (ii) pays health care providers, pursuant to a separate contractual agreement between the health care provider and the health carrier, to compensate the health care providers for services rendered to covered members. The example concludes that the health carrier is not a TPSO operating a third party payment network that enables purchasers to transfer funds to providers of goods and services.

Section 6050W Analysis

Taxpayer is not a TPSO because it does not enable purchasers, Taxpayer's Customers, to transfer funds through the use of a payment network to providers of

the Providers. Instead, the Taxpayer engages in two separate agreements: (1) an agreement with Customers to _____ on behalf of its Customers and (2) an agreement with Providers to _____ for _____ for its Customers and pay amounts invoiced by Providers through an automated clearinghouse network or other electronic funds transfer.

For Taxpayer's agreements with its Providers, the primary business model of the Taxpayer is to _____ for Providers' _____, then offer those _____ for sale to Customers through its _____ and other distribution channels. The rates that Taxpayer charges Customers for Provider's _____ are determined by Taxpayer, not by Providers. These rates are determined on a Provider-by-Provider basis and do not consist of the amount paid to the Provider plus a fixed or percentage fee. The service that Taxpayer provides is not focused on the settlement of a transaction between Customer and Provider. Rather, it is focused on _____. When Taxpayer sells _____ to a Customer, it is only obligated to pay the Provider of the _____ the _____ and established in its separate contract with Provider. The _____ is not known to the Customer nor is the Customer a party to the Taxpayer-Provider contract. The Customer and the Provider do not have a direct relationship.¹ Thus, Taxpayer's primary function is not the facilitation of the settlement

¹ The agreements between Taxpayer and Customers and Taxpayer and Providers are not perfectly analogous to the agreements described in Example 17, *Healthcare network*, of the regulations under section 6050W, but they are similar to them in some respects. Specifically, the payments between Customers and Taxpayer and Taxpayer and Providers are not directly linked. In that manner, Taxpayer's situation resembles that of the health carrier, who collects certain amounts from covered members

of a transaction between the buyer and the seller of . In conclusion, Taxpayer is not a TPSO and thus does not have a reporting obligation under section 6050W.

Section 6041

Section 6041(a) of the Code provides that all persons engaged in a trade or business and making payment in the course of such trade or business to another person, of rent, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, or other fixed or determinable gains, profits, and income of \$600 or more in any taxable year, shall render a true and accurate return setting forth the amount of such gains, profits, and income, and the name and address of the recipient.

Treas. Reg. § 1.6041-1(a) states that, except as provided in Treas. Reg. § 1.6041-3, every person engaged in a trade or business shall make an information return for each calendar year with respect to payments made by him during the calendar year in the course of his trade or business to another person of fixed or determinable salaries, wages, commissions, fees, and other forms of compensation for services rendered aggregating \$600 or more.

Treas. Reg. § 1.6041-3(c) provides that returns of information are not required with respect to payments of bills for merchandise, telegrams, telephone, freight, storage, and similar charges. The word “merchandise” is commonly defined and understood to include goods and commodities. See, e.g., *Wilkinson-Beane v. Commissioner*, 420 F. 2d 352 (1st Cir. 1970) (stating that for purposes of section 471, the term “merchandise” generally referred to “‘goods purchased in condition for sale,’ ‘goods awaiting sale,’ ‘articles of commerce held for sale’... The common denominator, however, seems to be that the items in question are merchandise if held for sale.”); *Black’s Law Dictionary* (9th ed. 2009) (defining “merchandise” as “a movable object involved in trade or traffic; that which is passed from one person to another by purchase and sale”).

Section 3406(a) of the Code provides that, in the case of any reportable payment and where certain circumstances exist, the payor shall deduct and withhold from such payment a tax equal to the product of the fourth lowest rate of tax applicable under section 1(c) and such payment.

Section 3406(b)(1) states that the term “reportable payment” means any reportable interest or dividend payment, and any other reportable payment. Section 3406(b)(3) defines other reportable payments as any payment of a kind, and to a payee, required to be shown on a return required under section 6041, among others.

Section 6041 Analysis

pursuant to contractual agreements and pays other amounts to health care providers under separate contractual agreements.

Taxpayer is subject to reporting under section 6041. Taxpayer is engaged in a trade or business during the course of which it makes payments to Providers which fall within the broad language of section 6041(a). The payments made by Taxpayer to Providers clearly fall within at least one of the categories of payments included in section 6041, including “rent, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, or other fixed or determinable gains, profits, and income.” Moreover, these payments do not fit within any of the exceptions provided in Treas. Reg. § 1.6041-3. Specifically, we conclude that the payments are not made for merchandise or similar charges and thus do not fall within the exception contained in Treas. Reg. § 1.6041-3(c). The payments to Providers are made for the provision of _____ provided to Customers. At no time does Taxpayer hold such _____ in order to sell them to Customers; the _____ are provided directly to Customers after Customers have _____ Taxpayer. Unlike “merchandise” in the traditional sense, Taxpayer does not hold title to or possess the _____ ultimately provided to Customers by Providers.

Moreover, a 2004 revenue procedure that classifies businesses by Merchant Category Codes according to whether they predominantly furnish services or predominantly provide goods provides further support for the position that Taxpayer is predominately providing services and not goods or merchandise. Rev. Proc. 2004-43, 2004-2 C.B. 124 (obsoleted by T.D. 9699, removing regulations relating to information reporting and backup withholding for the Qualified Payment Card Agent Program). Under the revenue procedure, the following types of businesses, among others, are considered to predominately provide services and thus are subject to reporting under section 6041:

_____ Taxpayer’s
Providers fit within both of these business types, further supporting our conclusion that Taxpayer is making payments for services, not for goods or merchandise. Rev. Proc. 2004-43 was obsoleted following the enactment of section 6050W and the payment card reporting regime, but it still provides guidance in determining whether a particular business is a type that should be classified as one predominately furnishing services.

Taxpayer argues that the payments to Providers fall within the exception found in Treas. Reg. § 1.6041-3(c), which exempts from reporting under section 6041 payments for “merchandise, telegrams, telephone, freight, storage, and similar charges.” In making this argument, Taxpayer contends that the payments can be classified as for “merchandise” or “similar charges.” As discussed above, we do not view payments to Providers for _____ as merchandise; rather, these are payments for services. Furthermore, we are not persuaded by the argument that the payments are for a “similar charge.” The reporting exception contained in Treas. Reg. § 1.6041-3(c) encompasses costs relating to maintaining, transporting, and storing items held for sale, including specific enumerated charges—merchandise, telegrams, telephone, freight, and storage—and additional “similar charges” that are not listed. The payments to Providers are neither payments for merchandise nor payments related to maintaining, storing, or

transporting merchandise. Rather, these payments are payments for the core service that Taxpayer provides to Customers—offering for sale. Thus, these payments do not fit within the reporting exception in Treas. Reg. § 1.6041-3(c).

Taxpayer further argues that even if the payments to Providers are for services, Taxpayer is not required to report them under section 6041 because the payments are for services that are being resold to Customers, not for services directly provided to Taxpayer. The fact that Taxpayer will ultimately resell these does not change the nature of the payment to Providers. The payment is made for services, regardless of who ultimately receives the . Taxpayers did not provide any controlling authority to establish that the resale of such services would be treated differently for purposes of section 6041. Thus, our conclusion regarding the applicability of section 6041 is not changed by the fact that Taxpayer is reselling the purchased from Providers.

Because we conclude that Taxpayer is making payments described in section 6041(a) and does not qualify for any exception to reporting under section 6041, Taxpayer is subject to reporting under section 6041 with respect to payments to Providers to the extent that such amounts paid to a particular Provider are equal to or exceed \$600 during the taxable year. Moreover, to the extent that payments are subject to reporting under section 6041 they are subject to the backup withholding rules pursuant to section 3406.

CONCLUSION

Based exclusively on the information provided and the representations made, we have determined that Taxpayer does not have a reporting obligation under section 6050W as a TPSO. We have concluded that Taxpayer does have a reporting obligation under section 6041 and is subject to the backup withholding rules under section 3406.

In light of your request for a closing agreement, we will, accordingly, approve a closing agreement with Taxpayer with respect to those issues affecting its obligations related to information reporting on the basis set forth above. The necessary closing agreement for Taxpayer has been prepared in triplicate and is enclosed. In pursuance of our practice with respect to such agreements, the agreement contains a stipulation to the effect that any change or modification of applicable statutes enacted subsequent to the date of this agreement and made applicable to the taxable period involved will render the agreement ineffective to the extent that it is dependent upon such statutes.

This letter ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Internal Revenue Code provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely,

Drita Tonuzi
Associate Chief Counsel
(Procedure & Administration)