

Internal Revenue Service

Department of the Treasury
Washington, DC 20224

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Legend

Taxpayer:

Customer:

Platform 1:

Platform 2:

Payer:

Dear _____ :

This is in response to the May 3, 2018 ruling request submitted on your behalf by your authorized representative concerning your federal income tax reporting obligations under section 6050W of the Internal Revenue Code (Code) and the regulations thereunder. Specifically, you have requested a ruling that:

1. Taxpayer is a third party settlement organization (TPSO) with respect to payments settled using Taxpayer's Platform 1 and Platform 2; and
2. If Taxpayer qualifies as a TPSO, then for purposes of determining whether the de minimis rules in section 6050W(e) are satisfied, a "transaction" is defined as the number of payments processed on behalf of a Payer, regardless of the number of times the Customer receives a payment through Taxpayer's Platform.

FACTS

Taxpayer is a provider of software and services designed for (organizations), as well as (institutions). Taxpayer's services

Taxpayer provides services in the following areas:

. In addition, Customers can combine Taxpayer's software services with other services, including payment processing.

Taxpayer's payment processing services (PPS) are divided into two categories.

via credit card, debit card, or automated clearing house (ACH) transactions. Taxpayer's PPS provides institution Customers with payment processing services that are used by .

provides Customers with the ability to accept credit card, debit card and ACH transactions over the Internet for payments. This PPS is governed by the Addendum. In order to use this PPS, a Customer must complete several steps prior to accepting online payments. First, it must create an account by providing certain information about the Customer and creating a user name and password. The Customer must then select a payment gateway¹ and payment processor² so that it may create a separate merchant account. For this PPS, Customers have the option of either purchasing (Platform 1) for its payment gateway or using an approved third-party payment gateway.³

¹ A payment gateway facilitates a payment transaction by transferring information between a payment portal (such as a website, mobile application, etc.) and the front-end processor or acquiring bank.

² A payment processor is generally responsible for forwarding the transaction information to the respective card association for verification and authorization. Once the payment processor receives confirmation that the credit card details have been verified, it will relay the information back to the merchant via the payment gateway. If verification is denied by the card association, then the payment processor will relay the information to the merchant who will then decline the transaction.

³ If a Customer chooses not to use Platform 1, then it must enter into separate contractual arrangements with a third-party payment gateway and payment processor. However, the Customer must first submit an application to Taxpayer to ensure that its processor's platform is compatible with Taxpayer's software. So long as the third-party platform is compatible, the fund disbursements, reconciliations, and chargebacks are managed by the third-party processor, not Platform 1. This ruling does not opine on the federal income tax reporting obligations of these third-party payment processors.

Platform 1 provides organization Customers with the ability to safely and securely receive and manage payments from their Payers. It allows Customers to access an online portal where they can view their transactions, perform reconciliations, and create reports. Platform 1 also provides screening to detect online payment fraud and uses encryption software to store a Payer's payment information. In order to provide this software and these services, Taxpayer has entered into agreements with a payment processor,⁴ and a merchant acquiring entity (MAE). Customers must also enter into separate Agreements with these entities. Taxpayer is a merchant payment processor that processes payments that its Customers receive from individuals.⁵

The payment flow process can be illustrated as follows: Payers enter their payment information into an online form in Taxpayer's PPS software. If the Customer selected to have payments processed by Platform 1, then the payments are deposited into a trust account at the MAE and disbursed to the Customer (less any refunds, chargebacks or processing fees) on a fixed schedule.

has a platform called ⁶ that allows participating Customers to accept payments as well as provide and customer support (Platform 2). In order to participate, Customers must comply with the terms outlined in the "Platform 2 and the "Platform 2 Agreement." The Customer selects the applicable payment plan, payment methods, and related disclosures and pays an annual to Taxpayer based on the number of Payers. Taxpayer provides the PPS software that allows the Customer to track by Payer. It also allows Payers to view and pay balances through an online account.

Platform 2 allows institution Customers to accept payments online via check, credit card, debit card and ACH transactions. Taxpayer contracts with a payment gateway and payment processor on behalf of the Customers.⁷ In order to provide these services, Taxpayer enters into agreements with the credit card networks, other processors and banks. In addition, these third parties require Customers to enter into Agreements with Taxpayer's contracted payment processors.

⁴ Taxpayer indicated that it recently entered into an agreement with a new third-party payment processor. Our understanding is that this new agreement will not materially change the payment flow process; therefore, this new agreement does not affect our analysis.

⁵ Taxpayer is not a depository institution and does not offer banking services or "money service business" as those terms are defined by the United States Department of Treasury.

⁶ Our understanding is that Taxpayer recently acquired , but that Taxpayer is responsible for reporting any payment card transaction that is settled through . So for the purposes of this ruling, we will refer to as the same entity as Taxpayer.

⁷ The Customers do not need to select or enter into separate contractual arrangements with the payment gateways and payment processors as they do in Program 1.

In order to initiate payments, a Payer enters their payment information into an online form using the Taxpayer's PPS software. If the Payer chooses to pay with a credit card, then the Payer's payment information and payment amount is sent to the payment gateway for approval and then sent to the credit card processor and combined into one or more batches for deposit. The payments are then deposited into Taxpayer's bank account and distributed to the Customer (less Taxpayer's fees) in accordance with the payment schedule selected by the Customer.

LAW & ANALYSIS

Section 6050W

Section 6050W of the Code, as enacted by the Housing Tax 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. The annual information return must set forth (1) the name, address, and taxpayer identification number (TIN) of the participating payee to whom payments were made and (2) the gross amount of the reportable payment transactions with respect to that payee. I.R.C. § 6050W(a). The regulations define gross amount to mean the total dollar amount of the aggregate reportable payment transactions for each participating payee, without regard to any adjustments for credits, cash equivalents, discount amounts, fees, refunded amounts, or any other amounts. Treas. Reg. § 1.6050W-1(a)(6). Taxpayers required to make returns under section 6050W do so by filing Forms 1099-K, Payment Card and Third Party Network Transactions.

Section 6050W covers two types of reportable payment transactions: (1) payment card transactions and (2) third party network transactions. I.R.C. § 6050W(c). 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)(2); 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 and services with purchasers according to the terms of agreements; (ii) provides standards and mechanisms for settling transactions; and (iii) guarantees payments to the providers of goods and services in settlement of transactions with the purchasers. I.R.C. § 6050W(d)(3); Treas. Reg. § 1.6050W-1(c)(3). Neither the Code nor the regulations defines what constitutes a “substantial number” of providers for the purposes of defining a third party payment network. However, in its technical explanation of the Housing Assistance Tax Act of 2008, the Joint Committee on Taxation interpreted the term “substantial number” to mean, for example, more than 50 providers of goods and services. Joint Committee on Taxation, Technical Explanation of Division C of H.R. 3221, The “Housing Assistance Tax Act of 2008” as Scheduled for Consideration by the House of Representatives on July 23, 2008 (JCX-63-08) at 61, July 23, 2008.

A participating payee, in the case of a third party network transaction, is any person who accepts payment from a third party settlement organization in the settlement of such transaction. I.R.C. § 6050W(d)(1)(A)(ii).

A TPSO is not required to report third party network transactions for a participating payee unless the amount to be reported exceeds \$20,000 and the aggregate number of transactions with that participating payee exceeds 200. I.R.C. § 6050W(e).

Analysis

Taxpayer is a TPSO⁸ with respect to transactions settled through both Platform 1 and Platform 2 because it is a central organization that has the contractual obligation to make payments to the participating payees of a third party network transaction and provides a third party payment network that allows recipients of goods and services to transfer funds to providers of goods and services.⁹

Taxpayer has established a third party payment network because it has an arrangement: (1) through which a substantial number of providers of goods and services who are unrelated to Taxpayer have established accounts with Taxpayer and have agreed to settle transactions for the provision of goods and services; (2) which provides standards and mechanisms for settling transactions, as provided in the contractual agreement between Taxpayer and Customers; and (3) which guarantees

⁸ The analysis in this section applies for payments processed through both Platform 1 and Platform 2.

⁹ Although the term “goods and services” is not defined in section 6050W or the regulations under that section, such term includes services offered by Customers to Payers through Taxpayer’s Platforms. This ruling does not opine as to whether all of the payments settled through Taxpayer’s Platforms are payments for goods and services.

that persons providing goods and services pursuant to this arrangement will be paid for providing these goods and services, as provided in the contractual agreement between Taxpayer and Customers.

Here, the providers of goods and services are the Customers who make their goods and services, including _____, and _____ services, available to Payers. Over _____ of these Customers, who are unrelated to Taxpayer, have established accounts with Taxpayer to settle transactions for the provision of their goods and services. The standards and mechanisms for settling transactions between Customers and Payers for the provision of these goods and services are provided in the contractual agreement between Taxpayer and Customers, along with a guarantee that Customers will be paid for their provision of goods and services after Taxpayer receives payment from Payers. Therefore, Taxpayer has established a third party payment network and is a TPSO with respect to transactions settled through both Platform 1 and Platform 2.

A third party network transaction occurs any time a transaction is settled through a third party payment network. Each time one of Taxpayer's Platforms successfully process a payment from a Payer is a single transaction. The frequency with which Taxpayer remits payment to a Customer is not determinative of what constitutes a transaction for the purposes of section 6050W.

As a TPSO, Taxpayer is required to report third party network transactions for a participating payee – here, a Customer – when the amount to be reported exceeds \$20,000 and the aggregate number of transactions with that Customer exceeds 200. Taxpayer must report the gross amount of all reportable payment transactions with respect to that Customer on a Form 1099-K.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

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

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

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,

Adrienne Griffin
Chief, Branch 2
(Procedure and Administration)

cc: