

**MEMO# 10229**

August 25, 1998

## **SEPTEMBER 16, 1998 MEETING -- PROPOSED TAX REPORTING REQUIREMENTS FOR WIDELY HELD FIXED INVESTMENT TRUSTS**

1 Prop. Treas. Reg. sec. 1.671-4(j). Issuance of this guidance has been on the IRS business plan for the past three years. See, e.g., Institute Memorandum to Tax Committee No. 9-96, Accounting/Treasurers Committee No. 11-96, Unit Investment Trust Committee No. 8-96 and Transfer Agent Advisory Committee No. 12-96, dated March 6, 1996. [10229] August 25, 1998 TO: TAX COMMITTEE No. 28-98 UNIT INVESTMENT TRUST COMMITTEE No. 25-98 ACCOUNTING/TREASURERS COMMITTEE No. 37-98 TRANSFER AGENT ADVISORY COMMITTEE No. 51-98 RE: SEPTEMBER 16, 1998 MEETING -- PROPOSED TAX REPORTING REQUIREMENTS FOR WIDELY HELD FIXED INVESTMENT TRUSTS

The Internal Revenue Service has released the attached proposed regulations<sup>1</sup> that are intended to clarify the tax reporting obligations imposed upon trustees, custodians and brokers with respect to interests in "widely held fixed investment trusts." In general, these regulations would apply to those unit investment trusts ("UITs") that are treated for federal tax purposes as grantor trusts, rather than as regulated investment companies ("RICs"). As proposed, the regulations would be effective for calendar years beginning after the date on which they are finalized. IRS has scheduled a public hearing on the proposed regulations for November 5, 1998 and provided a November 12, 1998 deadline for written comments. Requests to testify at the hearing, accompanied by an outline of the oral presentation, must be submitted to IRS by October 15, 1998. September 16, 1998 Meeting A meeting of members will be held on Wednesday, September 16 at 10:00 a.m. to discuss these proposed regulations and develop comments to be submitted by the Institute (at the hearing and in writing). The meeting will be held in the Institute's 11th Floor Conference Room. Lunch will be served following the meeting. ACTION REQUESTED If you and/or a colleague plan to attend the September 16 meeting, please complete the attached meeting response form and fax it to the Institute's Alice Bennett at 202-326-5841. Alice also may be reached by telephone at 202-218-3560. Summary Description of the Proposed Regulations

2 For example, amounts treated as income to a unitholder during 2002 would be reported to IRS by February 28, 2003 and to the unitholder by March 15, 2003 so that the information could be reflected properly on the unitholder's tax return for 2002 that would be due on April 15, 2003. 3 For example, a broker holding units in street name, rather than the trustee for the trust in which the street position is held, would be responsible for providing tax information to the beneficial owners of the units. 4 The list of exempt recipients includes, among others, corporations, individual retirement plans, securities

dealers, entities registered under the Investment Company Act of 1940, financial institutions, middlemen, brokers and widely held fixed investment trusts. The remainder of this memorandum summarizes the proposed regulations. All questions regarding these regulations and/or specific positions being developed by the Institute and its members with respect to them may be directed to the Institute's Deanna Flores at 202-371-5436 or to the undersigned at 202-326-5832. Definitions A widely held fixed investment trust is defined by the proposed regulations as an investment trust in which any interest is held by a "middleman." The term middleman is defined to include custodians, nominees (including joint owners who are not husband and wife) and brokers holding positions for customers in street name. Reporting Obligations (In General) The proposed regulations provide fairly detailed rules (discussed below) pursuant to which unitholders would receive tax information on "written statements" no later than March 15 of the year following the year for which the income is reportable; this information also would be reported to IRS on Forms 1099 no later than February 28 (two weeks before it must be provided to unitholders).<sup>2</sup> The obligation to report this information generally would rest with the trustee or middleman with the most direct contact with the beneficial owner.<sup>3</sup> The proposed regulations also provide rules designed to ensure that this information would be available to all relevant parties, e.g., middlemen. Specific Information to be Provided The proposed regulations would impose specific obligations (1) on trustees and middlemen for providing tax information to unitholders and IRS; (2) on trustees for furnishing information to middlemen, exempt recipients,<sup>4</sup> and non-calendar-year taxpayers; and (3) on middlemen for furnishing information to exempt recipients and non-calendar-year taxpayers. All amounts would be calculated using the cash method of accounting and reported on a gross, rather than net, basis. Reporting to Unitholders Tax information that generally must be provided to each unitholder under the proposed regulations would include, among other things: (1) all items of income, deduction and credit of the trust attributable to the unitholder; (2) in the case of any calendar year during which the trust sold or otherwise disposed of an asset: 5 Items of income, deduction and credit of the trust, for example, would need to be expressed, under the proposed regulations, both in total dollar amount for the trust and as a dollar amount per unit outstanding on the last day of the period requested. - 3 - (a) the unitholder's proportionate interest in the gross proceeds relating to the trust asset; (b) the date of sale or disposition; (c) the percentage of that trust asset that was sold or disposed of; and (d) a schedule showing the portion (expressed in percentage terms) of the total fair market value of all assets held by the trust that the asset represented, as of the last day of the quarter, for each quarter that the asset was held by the trust; (3) each individual unitholder's share of any "affected" expenses that the individual may deduct, if at all, only as miscellaneous itemized deductions under section 67(b); (4) in the case of trusts holding pools of debt instruments (e.g., mortgage pools) the yield on which may be affected by reason of prepayments -- defined under section 1272(a)(6)(C)(iii) -- any information necessary to compute: (a) the accrual of market discount, in the case of a REMIC regular interest or a collateralized debt obligation not issued with original issue discount ("OID"); and (b) the accrual of OID and market discount, in the case of a REMIC regular interest or a collateralized debt obligation issued with OID; and (5) any other information necessary for a unitholder to properly report the income, deductions and credit attributable to the unitholder under the grantor trust rules of section 671. Reporting to Middlemen, Exempt Recipients and Non-Calendar-Year Taxpayers The proposed regulations also provide procedures pursuant to which (a) "requesting persons" (e.g., middlemen and brokers, other exempt recipients and non-calendar-year taxpayers holding units directly and not through middlemen) would receive necessary tax information from trustees and (b) exempt recipients and non-calendar-year taxpayers would receive this information from middlemen. All such information would be required to be made available on a calendar-

quarter and on a calendar-year basis, as of the last day of the calendar quarter or year. Requests for this information could be made in writing or by telephone. Under the regulations, trustees would be required to cause to be printed in a publication generally read by and available to requesting persons the name, address and telephone number of a representative or official of the trust who would provide the information (including that identified above) that must be reported to unitholders,<sup>5</sup> and the number of units outstanding on the last business - 4 - day of the period(s) requested. Trustees would be required to provide the requested information on or before the later of (a) the 30th day after the close of the period for which the information was requested or (b) the day that is two weeks after the receipt of the request. The information could be furnished by telephone, by written statement, by causing it to be printed in a publication generally read by and available to requesting persons (so long as the trustee notified the requesting person in writing or by telephone of the publication, including the date of publication and, if possible, the page number in which the information will appear), or by any other method agreed to by the parties. Middlemen receiving requests from exempt recipients and non-calendar-year taxpayers for tax information would be required to provide it on or before the later of (a) the 45th day after the close of the period for which the information was requested or (b) the day that is four weeks after the receipt of the request. IRS Requests for Comments IRS specifically has requested comments on numerous issues, including: (1) specific instances of industry practice that differ significantly from the framework of the proposed regulations and suggestions for tailoring the regulations to account for these differences; (2) whether the proposed rules for communicating cost basis calculation information to unitholders would be effective, or whether a different approach consistent with the taxation of grantor trusts would be more effective; (3) whether, for trusts with "fungible" assets, an approach other than the proposed asset- by-asset approach for reporting sales and determining basis would be administratively feasible or, alternatively, whether an aggregate approach would be more appropriate and, if so, the manner in which such an approach would be applied; (4) whether the information reporting rules applicable to widely held fixed investment trusts holding section 1272(a)(6) debt instruments or pools of debt instruments (where principal is subject to acceleration) also should be applied to trusts holding instruments or pools not subject to this section; (5) whether trusts should be required to provide tax reporting information to accommodate unitholders not on the cash method of accounting; and (6) whether it would be administratively feasible in the context of a widely held fixed investment trust to require, as the proposed regulations would, that unitholders be provided with information regarding any item that, if taken into account separately by any unitholder, could result in an income tax liability for the unitholder different from that which would result if the unitholder did not take the item into account separately (and, if not, whether a different approach consistent with the taxation of grantor trusts would be more appropriate). - 5 - \* \* \* Keith D. Lawson Senior Counsel Attachments