

**MEMO# 1112**

April 18, 1989

# **AMENDMENTS TO BACKUP WITHHOLDING REGULATIONS**

- 1 - April 18, 1989 TO: TAX MEMBERS NO. 14-89 UNIT INVESTMENT TRUST MEMBERS NO. 22-89 CLOSED-END FUND MEMBERS NO. 18-89 OPERATIONS MEMBERS NO. 15-89 TRANSFER AGENT SHAREHOLDER ADVISORY COMMITTEE NO. 9-89 RE: AMENDMENTS TO BACKUP WITHHOLDING REGULATIONS

The attached temporary regulations amend temporary regulations issued in November 1987 which (1) provided rules for imposing backup withholding following receipt of a "B Notice" from the IRS that payees had provided incorrect taxpayer identification numbers (TINs) and (2) clarified the due diligence standard and its exceptions. (See Institute Memorandum to Tax Members No. 46-87, Unit Investment Trust Members No. 31-87, Closed-End Fund Members No. 5-87, Operations Members No. 29-87 and Transfer Agent Shareholder Advisory Committee No. 24-87, dated December 8, 1987). The attached regulations also incorporate certain changes to the temporary regulations that were previously announced by the IRS in IRS Notices 88-77 and 88-89 (See Institute Memoranda to Tax Members No. 37-88, Unit Investment Trust Members No. 44-88, Closed-End Fund Members No. 35-88, Operations Members No. 21-88 and Transfer Agent Shareholder Advisory Committee No. 16-88, dated July 7, 1988, and to Tax Members No. 45-88, Unit Investment Trust Members No. 50-88, Closed-End Fund Members No. 42-88, Operations Members No. 25-88 and Transfer Agent Shareholder Advisory Committee No. 20-88, dated August 5, 1988). While the attached regulations provide some limited relief from the backup withholding and due diligence rules, they do not adequately address comments made by the Institute regarding the most difficult problems created by these regulations. (See Institute Memoranda to Tax Committee No. 7-88, Operations Committee No. 13-88, Closed-End Fund Committee No. 14-88 and Transfer Agent Shareholder Advisory Committee No. 8-88, dated April 21, 1988, and to Tax Committee No. 10-88, Unit Investment Trust Committee No. 14-88, Operations Committee No. 14-88 and Transfer Agent Shareholder Advisory Committee No. 11-88, dated - 2 - May 13, 1988). For example, no relief has been provided either to permit funds to open accounts without TINs (unless a certified TIN is received before year-end) or for situations where an account is opened through a broker and subsequent accounts are opened without the broker's assistance.

1. Backup Withholding The amended regulations revise the notice that payors send to payees to inform the payees that documents in addition to the Form W-9 may need to be sent to be payor to change a TIN or name (or both) on an account. Substitute notices drafted to satisfy the requirements of the original regulations will continue to be acceptable. The amended regulations also relax, to some extent, the original regulations' requirement that payors send B Notices to payees within 5 business days after being notified of an incorrect TIN. The Explanation of Provisions issued with the regulations indicates that the IRS will send notices to payors approximately 2 or 3

weeks before the date on the notice. The amended regulations clarify that the date on the notice from the IRS will be considered the effective date of that notice. If a payor receives the notice following the date on the notice, the effective date will be the actual date of receipt. Thus, the IRS anticipates that payors will have more than, and in any event at least, 5 business days to send B Notices to payees. If a payee has several accounts bearing incorrect TINs with a single payor, the amended regulations remove the requirement that separate notices be sent for each account and permit the payor to send a single notice. The amended regulations also provide that, for purposes of determining whether a payor has been notified twice within three calendar years that a payee's TIN is incorrect, only a notice from the IRS (or a broker) that contains the same payee information as that on the payee's account is considered a "first" notice.

2. Due Diligence The old regulations provided that if a payor of a pre-1984 account who had not satisfied all of the required mailings wanted to receive administrative relief from the incorrect TIN penalty for 1988 or subsequent calendar years, a separate mailing must have been sent by June 30, 1988 to all payees of pre-1984 accounts without certified TINs. The amended regulations provide that relief may be granted to those payors who failed to mail by June 30, 1988 to all payees, so long as the failure to mail was limited to a de minimis number of accounts (i.e., the lesser of 5,000 accounts or one percent of the total number of accounts).

3 - To receive relief in future years, the payor must make a separate mailing to all such accounts in the following year and nonseparate mailings in all following years until a certified TIN is received. The instructions for filing the request for administrative relief are also clarified by the new regulations. The amended regulations also clarify that the IRS, in its administrative discretion, will not enforce the penalty on post- 1983 accounts opened without a certified TIN for a calendar year if the certified TIN is received after the account is opened and before December 31 of such year. Finally, the new regulations provide that if backup withholding is imposed because of notified payee underreporting on a payee whose income is so low as not to be subject to tax, withheld accounts can be refunded to the payee even though, as a general rule, refunds are permissible only if the withholding is the result of an error of the payor. We will keep you informed of developments.

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