

MEMO# 3458

February 6, 1992

CORPORATE INFORMATION REPORTING SURVEY

February 6, 1992 TO: TAX COMMITTEE NO. 4-92 ACCOUNTING/TREASURERS COMMITTEE NO. 7-92 OPERATIONS COMMITTEE NO. 4-92 TRANSFER AGENT ADVISORY COMMITTEE NO. 6-92 RE: CORPORATE INFORMATION REPORTING SURVEY

Introduction Serious

consideration is being given by Congress and the Internal Revenue Service ("IRS") to requiring payors to report certain tax information to corporate payees. One possible proposal would limit such reporting to corporate payees with assets of \$10 million or less. The Government Operations Committee of the U.S. House of Representatives intends to hold hearings regarding corporate information reporting this summer and has asked the IRS to prepare, by June 1992, a detailed cost/benefit analysis of a corporate document matching program. For the IRS to complete this analysis, they will need data on the costs that such a program would impose on the business community. These costs would include both costs associated with (1) sending IRS Forms 1099-DIV, 1099-INT and 1099-B to corporate shareholders and (2) receiving IRS Forms 1099-DIV, 1099-INT and 1099-B from entities in which corporations invest. Many have argued that the costs to the business community of such a program would substantially outweigh any benefit that might be derived, especially if the reporting requirement applied to all corporate payees. To help determine the costs that such a program might impose on the investment company industry, we have developed the attached survey, which we ask you to return by February 28, 1992. Background For several years, the House Government Operations Committee and the General Accounting Office ("GAO") have been urging the IRS to implement a program that requires reporting of tax information to corporate payees and then "matches" the information provided to corporations with the information included in their tax returns. The IRS has in the past resisted efforts to establish such a program because, in IRS' view, the amount of noncompliance among corporate payees is small compared to the costs and complexities associated with such a program. GAO believes, however, that the amount of noncompliance is much larger. Attached is a report prepared by the House Government Operations Committee, entitled "The Feasibility of Initiating a System for the Verification of Corporate Tax Returns Through an Information and Document Matching Program at IRS". In the report, the Committee recommends that IRS work with its Information Reporting Program Advisory Committee ("IRPAC"), of which I am a member, to develop a comprehensive cost-benefit analysis of a prototype corporate document matching program. The analysis is to include an estimate of the costs that such a reporting and matching program would impose on the payor community and the corporate recipients of these information returns. The House Committee further recommends that a pilot corporate matching program (limited initially to the reporting of interest, dividends and rents) be implemented, with IRS receiving information returns for the 1993 tax year and beginning to

"match" information returns with corporate tax returns in calendar year 1995. If the pilot effort is successful, it is recommended that IRS expand the program to collect capital gain and royalty income information returns. Finally, the Committee recommends that the IRS present to Congress the results of their comprehensive cost/benefit analysis and their plans for the pilot test no later than June 1992.

Possible Information Reporting System The IRS is presently studying a possible information reporting system that would have, among other things, the following features:

- (1) Forms 1099 for corporations would be different from current calendar year Forms 1099 for individuals in that, while reporting would still be done annually following the calendar year-end, the reports sent to corporate payees would include a month-by-month breakdown of payments made, separately stating US- source and foreign-source income. To facilitate this new reporting scheme, the current Form 1099 would be expanded to allow for up to twelve additional entries, one for each month in the calendar year. Up to thirteen entries (a total- amount entry and twelve monthly entries) could also be needed to show any foreign-source income paid by the fund. Monthly breakdowns of payments could be needed under this system to permit reconciliation of the information reported on calendar-year Forms - 2 - 1099 with the fiscal-year tax returns of many corporate payees. Forms 1099-B would remain essentially the same, with information reported on a transactional basis.
- (2) Payors would be required to identify on the information return the tax status of the entity (e.g., individual, partnership, corporation, etc.) to which they are providing the information.
- (3) Payments of reportable income (such as interest, dividends and capital gains) would be reported to shareholders on the cash method of accounting (even though many corporations report income on the accrual method).
- (4) Corporate income tax returns would separately state interest and dividends (at the least) based upon domestic or foreign source. This requirement would be needed to match domestic-source interest and dividend income (which would be reported by domestic payors to domestic payees) with the amount of such income included on the tax return.
- (5) A new form similar to Schedule B of Form 1040 would be needed so that corporations could list on their tax returns each of the payors of certain types of income, such as dividends and interest, that they receive.

Survey Request The attached survey is intended to assist the Institute and the IRS Advisory Committee in preparing an analysis of the burdens that a corporate reporting and document matching program would impose upon the business community in general and the investment company industry in particular. The first part of the survey relates to information returns that would be sent by funds to corporate shareholders. It is likely that most of the costs arising under this part would be incurred at the transfer agent level. The second part of the survey relates to information returns that would be received by the funds on their portfolio investments. It is likely that many of the costs associated with receipt of Forms 1099 would be incurred at the fund accounting level. Thus, it may be necessary to collect data from different persons within each fund complex to complete this survey. It is unclear whether any corporate reporting system would be limited to certain corporate payees, such as those with assets of less than \$10 million, or whether reporting would be required for all payees. For purposes of the attached survey, please assume that such a reporting system would apply to all corporations, regardless of asset size.

- 4 - To meet the short time frame set by the House Committee, we ask each fund complex to complete one copy of the survey and return it to me no later than Friday, February 28. If you have any questions regarding this survey, please call me at 202/955-3585. We will keep you informed of developments.

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should not be considered a substitute for, legal advice.