

Dated: December 13, 2018.

Leslie Kux,

Associate Commissioner for Policy.

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DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[REG-132881-17]

RIN 1545-BO30

Regulations Reducing Burden Under FATCA and Chapter 3

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations eliminating withholding on payments of gross proceeds, deferring withholding on foreign passthru payments, eliminating withholding on certain insurance premiums, and clarifying the definition of investment entity. This notice of proposed rulemaking also includes guidance concerning certain due diligence requirements of withholding agents and guidance on refunds and credits of amounts withheld.

DATES: Written or electronic comments and requests for a public hearing must be received by February 19, 2019.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG-132881-17), Internal Revenue Service, Room 5203, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions may also be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to CC:PA:LPD:PR (REG-132881-17), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue NW, Washington, DC 20224; or sent electronically via the Federal eRulemaking Portal at <http://www.regulations.gov> (IRS REG-132881-17).

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, John Sweeney, Nancy Lee, or Subin Seth, (202) 317-6942; concerning submissions of comments and/or requests for a public hearing, Regina Johnson, (202) 317-6901 (not toll free numbers).

SUPPLEMENTARY INFORMATION:

Background

This document contains amendments to the Income Tax Regulations (26 CFR part 1) under chapter 4 (sections 1471

through 1474) commonly known as the Foreign Account Tax Compliance Act (FATCA). This document also contains amendments to the Income Tax Regulations (26 CFR part 1) under sections 1441 and 1461.

On January 28, 2013, the Department of the Treasury (Treasury Department) and the IRS published final regulations under chapter 4 in the **Federal Register** (TD 9610, 78 FR 5873), and on September 10, 2013, corrections to the final regulations were published in the **Federal Register** (78 FR 55202). The regulations in TD 9610 and the corrections thereto are collectively referred to in this preamble as the 2013 final chapter 4 regulations. On March 6, 2014, the Treasury Department and the IRS published temporary regulations under chapter 4 (TD 9657, 79 FR 12812) that clarify and modify certain provisions of the 2013 final chapter 4 regulations, and corrections to the temporary regulations were published in the **Federal Register** on July 1, 2014, and November 18, 2014 (79 FR 37175 and 78 FR 68619, respectively). The regulations in TD 9657 and the corrections thereto are referred to in this preamble as the 2014 temporary chapter 4 regulations. A notice of proposed rulemaking cross-referencing the 2014 temporary chapter 4 regulations was published in the **Federal Register** on March 6, 2014 (79 FR 12868).

On March 6, 2014, the Treasury Department and the IRS published temporary regulations under chapters 3 and 61 in the **Federal Register** (TD 9658, 79 FR 12726) to coordinate with the regulations under chapter 4, and corrections to those temporary regulations were published in the **Federal Register** (79 FR 37181) on July 1, 2014. Collectively, the regulations in TD 9657 and the corrections thereto are referred to in this preamble as the 2014 temporary coordination regulations. A notice of proposed rulemaking cross-referencing the 2014 temporary coordination regulations was published in the **Federal Register** on March 6, 2014 (79 FR 12880).

On January 6, 2017, the Treasury Department and the IRS published final and temporary regulations under chapter 4 in the **Federal Register** (TD 9809, 82 FR 2124), and corrections to those final regulations were published on June 30, 2017 in the **Federal Register** (82 FR 27928). Collectively, the regulations in TD 9809 and the corrections thereto are referred to in this preamble as the 2017 chapter 4 regulations. A notice of proposed rulemaking cross-referencing the temporary regulations in TD 9809 and proposing regulations under chapter 4

relating to verification requirements for certain entities was published in the **Federal Register** on January 6, 2017 (82 FR 1629). Also on January 6, 2017, the Treasury Department and the IRS published final and temporary regulations under chapters 3 and 61 in the **Federal Register** (TD 9808, 82 FR 2046), and corrections to those final regulations were published on June 30, 2017 in the **Federal Register** (82 FR 29719). Collectively, the regulations in TD 9808 and the corrections thereto are referred to in this preamble as the 2017 coordination regulations. A notice of proposed rulemaking cross-referencing the temporary regulations in TD 9808 was published in the **Federal Register** on January 6, 2017 (82 FR 1645).

Pursuant to Executive Order 13777, Presidential Executive Order on Enforcing the Regulatory Reform Agenda (82 FR 9339), the Treasury Department is responsible for conducting a broad review of existing regulations. In a Request for Information published on June 14, 2017 (82 FR 27217), the Treasury Department invited public comment concerning regulations that should be modified or eliminated in order to reduce unnecessary burdens. In addition, in Notice 2017-28 (2017-19 I.R.B. 1235), the Treasury Department and the IRS invited public comment on recommendations for the 2017-2018 Priority Guidance Plan for tax guidance, including recommendations relating to Executive Order 13777. In response to the invitations for comments in the Request for Information and Notice 2017-28, the Treasury Department and the IRS received comments suggesting modifications to the regulations under chapters 3 and 4. See also Executive Order 13789, Identifying and Reducing Tax Regulatory Burdens, issued on April 21, 2017 (82 FR 19317) and the second report issued in response (82 FR 48013) (stating that the Treasury Department continues to analyze all recently issued significant regulations and is considering possible reforms of recent regulations, which include regulations under chapter 4).

Based on public input, and taking into account the burden-reducing policies described in Executive Orders 13777 and 13789, these regulations propose certain amendments to the regulations under chapters 3 and 4, including certain refund related issues for which comments were received. The Explanation of Provisions section of this preamble describes these proposed amendments and addresses public comments received in response to the Request for Information and Notice 2017-28, other than comments that would require a statutory change or

were addressed in prior Treasury decisions. The Explanation of Provisions section of this preamble also discusses comments to the 2017 chapter 4 regulations and 2017 coordination regulations to the extent the comments relate to amendments that are included in these proposed regulations. The Treasury Department and the IRS continue to study other public comments.

Explanation of Provisions

I. Elimination of Withholding on Payments of Gross Proceeds From the Sale or Other Disposition of Any Property of a Type Which Can Produce Interest or Dividends From Sources Within the United States

Under sections 1471(a) and 1472, withholdable payments made to certain foreign financial institutions (FFIs) and certain non-financial foreign entities (NFFE) are subject to withholding under chapter 4. Section 1473(1) states that, except as otherwise provided by the Secretary, the term “withholdable payment” means: (i) Any payment of interest (including any original issue discount), dividends, rents, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, and other fixed or determinable annual or periodical gains, profits, and income, if such payment is from sources within the United States; and (ii) any gross proceeds from the sale or other disposition of any property of a type which can produce interest or dividends from sources within the United States.

Since the enactment of chapter 4, the Treasury Department and the IRS have received comments from withholding agents on the burden of implementing a requirement to withhold on gross proceeds. The comments have noted in particular the lead time required to implement such a requirement and the potential complexity of a sufficient regulatory framework. The comments assert that withholding on gross proceeds would require significant efforts by withholding agents, including executing brokers that do not obtain tax documentation. The comments assert that adding this withholding requirement is of limited incremental benefit in supporting the objectives of chapter 4 with respect to foreign entities investing in U.S. securities. In response to these comments, the Treasury Department and the IRS have repeatedly issued guidance deferring the date when withholding on gross proceeds would begin. The 2017 chapter 4 regulations provide that such withholding will begin on January 1, 2019.

Many U.S. and foreign financial institutions, foreign governments, the Treasury Department, the IRS, and other stakeholders have devoted substantial resources to implementing FATCA withholding on withholdable payments. At the same time, 87 jurisdictions have an IGA in force or in effect and 26 jurisdictions are treated as having an IGA in effect because they have an IGA signed or agreed in substance, which allows for international cooperation to facilitate FATCA implementation. The Treasury Department and the IRS have determined that the current withholding requirements under chapter 4 on U.S. investments already serve as a significant incentive for FFIs investing in U.S. securities to avoid status as nonparticipating FFIs, and that withholding on gross proceeds is no longer necessary in light of the current compliance with FATCA. For these reasons, under the authority provided under section 1473(1) these proposed regulations would eliminate withholding on gross proceeds by removing gross proceeds from the definition of the term “withholdable payment” in § 1.1473-1(a)(1) and by removing certain other provisions in the chapter 4 regulations that relate to withholding on gross proceeds. As a result of these proposed changes to the chapter 4 regulations, only payments of U.S. source FDAP that are withholdable payments under § 1.1473-1(a) and that are not otherwise excepted from withholding under § 1.1471-2(a) or (b) would be subject to withholding under sections 1471(a) and 1472.

II. Deferral of Withholding on Foreign Passthrough Payments

An FFI that has an agreement described in section 1471(b) in effect with the IRS is required to withhold on any passthrough payments made to its recalcitrant account holders and to FFIs that are not compliant with chapter 4 (nonparticipating FFIs). Section 1471(d)(7) defines a “passthrough payment” as any withholdable payment or other payment to the extent attributable to a withholdable payment.

In Notice 2010-60 (2010-37 I.R.B. 329), the Treasury Department and the IRS requested comments on methods a participating FFI could use to determine whether payments it makes are attributable to withholdable payments. In Notice 2011-34 (2011-19 I.R.B. 765), the Treasury Department and the IRS set forth a proposed framework for participating FFIs to withhold on such payments based on a methodology for determining a “passthrough payment percentage” to be applied to certain payments made by FFIs. After the

publication of Notice 2011-34, stakeholders noted the burdens and complexities in implementing a system for withholding on these payments along the lines of that described in the notice. In light of those comments, the framework outlined in Notice 2011-34 was not incorporated into the 2013 final chapter 4 regulations. In addition, the Treasury Department and the IRS have repeatedly issued guidance deferring the date when withholding on these payments would begin (referred to in guidance as “foreign passthrough payments”). The 2017 chapter 4 regulations provide that such withholding will not begin until the later of January 1, 2019, or the date of publication in the **Federal Register** of final regulations defining the term “foreign passthrough payment.”

The Treasury Department and the IRS have received comments noting that withholding on foreign passthrough payments may not be needed given the number of IGAs in effect. One comment also recommended that if the Treasury Department and the IRS determine, based on an evaluation of the data received from FFIs on payments to nonparticipating FFIs in 2015 and 2016, that withholding on foreign passthrough payments is necessary, the Treasury Department and the IRS should develop a more targeted solution.

Both in recognition of the time necessary to implement a system for withholding on foreign passthrough payments and in recognition of the successful engagement of Treasury and partner jurisdictions to conclude intergovernmental agreements to implement FATCA, these proposed regulations further extend the time for withholding on foreign passthrough payments. Accordingly, under proposed regulation § 1.1471-4(b)(4), a participating FFI will not be required to withhold tax on a foreign passthrough payment made to a recalcitrant account holder or nonparticipating FFI before the date that is two years after the date of publication in the **Federal Register** of final regulations defining the term “foreign passthrough payment.” The proposed regulations also make conforming changes to other provisions in the chapter 4 regulations that relate to foreign passthrough payment withholding.

Notwithstanding these proposed amendments, the Treasury Department and the IRS remain concerned about the long-term omission of withholding on foreign passthrough payments. The Treasury Department and the IRS acknowledge the progress made in implementing FATCA. Nevertheless, concerns remain regarding account

holders of participating FFIs that remain recalcitrant account holders or nonparticipating FFIs and regarding payments made to nonparticipating FFIs. Withholding on foreign passthrough payments serves important purposes. First, it provides one way for an FFI that has entered into an FFI agreement to continue to remain in compliance with its agreement, even if some of its account holders have failed to provide the FFI with the information necessary for the FFI to properly determine whether the accounts are U.S. accounts and perform the required reporting, or, in the case of account holders that are FFIs, have failed to enter into an FFI agreement. Second, withholding on foreign passthrough payments prevents nonparticipating FFIs from avoiding FATCA by investing in the United States through a participating FFI “blocker.” For example, a participating FFI that is an investment entity could receive U.S. source FDAP income free of withholding under chapter 4 and then effectively pay the amount over to a nonparticipating FFI as a corporate distribution. Despite being attributable to the U.S. source payment, the payment made to the nonparticipating FFI may be treated as foreign source income and therefore not a withholdable payment subject to chapter 4 withholding.

Accordingly, the Treasury Department and the IRS continue to consider the feasibility of a system for implementing withholding on foreign passthrough payments. The Treasury Department and the IRS request additional comments from stakeholders on alternative approaches that would serve the same compliance objectives as would foreign passthrough payment withholding and that could be more efficiently implemented by FFIs.

III. Elimination of Withholding on Non-Cash Value Insurance Premiums Under Chapter 4

Under § 1.1473–1(a)(1), a withholdable payment generally includes any payment of U.S. source FDAP income, subject to certain exclusions, such as for “excluded nonfinancial payments.” Excluded nonfinancial payments do not include premiums for insurance contracts. The 2013 final chapter 4 regulations included, however, a transitional rule that deferred withholding on payments with respect to offshore obligations until January 1, 2017, which was extended in the 2014 chapter 4 regulations to include premiums paid by persons acting as insurance brokers with respect to offshore obligations. Additionally, in response to comments noting the burden of providing to withholding

agents withholding certificates and withholding statements for payments of insurance premiums, the chapter 4 regulations provide a rule generally allowing a withholding agent to treat as a U.S. payee a U.S. broker receiving a payment of an insurance premium in its capacity as an intermediary or an agent of a foreign insurer. The IRS also generally permits non-U.S. insurance brokers that are NFFEs to become qualified intermediaries in order to alleviate burden on the foreign brokers and U.S. withholding agents.

Notwithstanding these allowances, the Treasury Department and the IRS continued to receive comments requesting elimination of withholding under chapter 4 on premiums for insurance contracts that do not have cash value (non-cash value insurance premiums). The comments cited the burden on insurance brokers of documenting insurance carriers, intermediaries, and syndicates of insurers for chapter 4 purposes, noting examples to demonstrate the volume and complexity of placements with insurers of the insurance policies typically arranged by the brokers for their clients. The comments argued that withholding on non-cash value insurance premiums is not necessary to further the purposes of chapter 4.

At the same time, certain foreign entities that conducted a relatively small amount of insurance business had taken the position that they were not passive foreign investment companies (PFICs) under section 1297(a). Section 1297(a) generally defines a PFIC as a foreign corporation if 75 percent or more of the corporation’s gross income for the taxable year is passive income or 50 percent or more of its assets produce, or are held for the production of, passive income. Section 1297(b)(2)(B), prior to a recent change in law (described below), provided an exception from the U.S. owner reporting and anti-deferral rules applicable to PFICs for corporations “predominantly engaged” in an insurance business. Withholding under chapter 4 on non-cash value insurance premiums strengthened the IRS’s enforcement efforts, with respect to the use of the exception in section 1297(b)(2)(B) by U.S. owners of foreign corporations for tax avoidance and evasion, by facilitating reporting of the U.S. owners to avoid withholding on premiums received by the entity.

The preamble to the 2017 chapter 4 regulations noted that future changes to the PFIC rules may create an opportunity to revise the treatment of foreign insurance companies under chapter 4. 82 FR 2140. On December 22,

2017, the Tax Cuts and Jobs Act, Public Law 115–97 (2017) amended section 1297(b)(2)(B) to provide a more limited exception to PFIC status by replacing the exception for corporations predominantly engaged in an insurance business with a more stringent test based generally on a comparison of the corporation’s insurance liabilities and its total assets. This amendment is expected to mitigate the need for reporting on the U.S. owners of these companies under chapter 4 because the Treasury Department and the IRS anticipate that these entities will either amend their business models on account of the change in law or will otherwise comply with the PFIC reporting requirements.

In light of the aforementioned change in law and in furtherance of the burden-reducing policies in Executive Orders 13777 and 13789, these proposed regulations provide that premiums for insurance contracts that do not have cash value (as defined in § 1.1471–5(b)(3)(vii)(B)) are excluded nonfinancial payments and, therefore, not withholdable payments.

IV. Clarification of Definition of Investment Entity

Under § 1.1471–5(e)(4)(i)(B), an entity is an investment entity (and therefore a financial institution) if the entity’s gross income is primarily attributable to investing, reinvesting, or trading in financial assets and the entity is “managed by” another entity that is a depository institution, custodial institution, insurance company, or an investment entity described in § 1.1471–5(e)(4)(i)(A). Section 1.1471–5(e)(4)(v), *Example 2*, illustrates this rule with an example in which a fund is an investment entity because another financial institution (an investment advisor) provides investment advice to the fund and has discretionary management of the assets held by a fund and the fund meets the gross income test. In *Example 6* of § 1.1471–5(e)(4)(v), a trust is an investment entity because the trustee (an FFI) manages and administers the assets of the trust in accordance with the terms of the trust instrument and the trust meets the gross income test. Section 1.1471–5(e)(4)(v), *Example 8*, provides an example in which an entity is an investment entity because an introducing broker (that is, a broker using another broker to clear and settle its trades) has discretionary authority to manage the entity’s assets and provides services as an investment advisor and manager to the entity and the entity meets the gross income test.

The Treasury Department and the IRS received a comment requesting that

“discretionary authority” be more narrowly construed for purposes of treating an entity as an investment entity described in § 1.1471–5(e)(4)(i)(B). The comment suggested that an entity should not be treated as an investment entity solely because the entity invests in a mutual fund or similar vehicle because the investments made by the mutual fund are not tailored to the entity that invests in it. The comment requested the same result for a variety of other types of investment products and solutions with varying degrees of investor involvement and standardization, including an investment in a “discretionary mandate.” According to the comment, a “discretionary mandate” is an investment product or solution offered by a financial institution to certain clients where the financial institution manages and invests the client’s funds directly (rather than the client investing in a separate entity) in accordance with the client’s investment goals. The comment noted that some discretionary mandate clients claim to be passive NFFEs rather than FFIs.

As described in the examples, the “managed by” category of investment entities generally covers entities that receive specific professional management advice from an advisor that is tailored to the investment needs of the entity. A financial institution does not have discretionary authority over an entity merely because it sells the entity shares in a widely-held fund that employs a predetermined investment strategy. These proposed regulations clarify that an entity is not “managed by” another entity for purposes of § 1.1471–5(e)(4)(i)(B) solely because the first-mentioned entity invests all or a portion of its assets in such other entity, and such other entity is a mutual fund, an exchange traded fund, or a collective investment entity that is widely held and is subject to investor-protection regulation. In contrast, an investor in a discretionary mandate described above is “managed by” the financial institution under § 1.1471–5(e)(4)(i)(B).

The clarification in these proposed regulations is similar to the guidance published by the OECD interpreting the definition of a “managed by” investment entity under the Common Reporting Standard.

V. Modifications to Due Diligence Requirements of Withholding Agents Under Chapters 3 and 4

A. Treaty Statements Provided With Documentary Evidence for Chapter 3

Under chapter 3, a withholding agent must generally obtain either a

withholding certificate or documentary evidence and a treaty statement in order to apply a reduced rate of withholding based on a payee’s claim for benefits under a tax treaty. The 2017 coordination regulations added a requirement that when a treaty statement is provided with documentary evidence by an entity beneficial owner to claim treaty benefits, the statement must identify the specific limitation on benefits (LOB) provision relied upon in the treaty. In addition, the 2017 coordination regulations added a three-year validity period applicable to treaty statements provided with documentary evidence and a transition period that expires January 1, 2019, for withholding agents to obtain new treaty statements that comply with the new LOB requirement for accounts that were documented with documentary evidence before January 6, 2017 (preexisting accounts). The QI agreement in Revenue Procedure 2017–15, 2017–3 I.R.B. 437 (2017 QI agreement) cross-references the 2017 coordination regulations for the three-year validity period for treaty statements provided with documentary evidence and provides a two-year transition rule for accounts documented before January 1, 2017. Similar provisions are included in the WP and WT agreements in Revenue Procedure 2017–21, 2017–6 I.R.B. 791 (2017 WP and WT agreements).

Comments have noted the burden of complying with the new treaty statement requirements, including difficulties in obtaining new treaty statements for preexisting accounts within the transitional period given the large number of account holders impacted by this requirement. The comments requested an additional one-year period for withholding agents to obtain new treaty statements for preexisting accounts, and the removal of the three-year validity period for a treaty statement that meets the LOB requirement. A comment also noted that a three-year validity period for a treaty statement is not needed for certain categories of entities whose treaty status is unlikely to change, such as publicly traded corporations and government entities.

In response to these comments, these proposed regulations include several changes to the rules on treaty statements provided with documentary evidence. First, these proposed regulations extend the time for withholding agents to obtain treaty statements with the specific LOB provision identified for preexisting accounts until January 1, 2020 (rather than January 1, 2019). Second, these proposed regulations add

exceptions to the three-year validity period for treaty statements provided by tax exempt organizations (other than tax-exempt pension trusts or pension funds), governments, and publicly traded corporations, entities whose qualification under an applicable treaty is unlikely to change. See proposed § 1.1441–1(e)(4)(ii)(A)(2). In addition, these proposed regulations correct an inadvertent omission of the actual knowledge standard for a withholding agent’s reliance on the beneficial owner’s identification of an LOB provision on a treaty statement provided with documentary evidence, the same as the standard that applies to a withholding certificate used to make a treaty claim. See proposed § 1.1441–6(c)(5)(i). The proposed amendments described in this section V.A. will also be incorporated into the 2017 QI agreement and 2017 WP and WT agreements, and a QI, WP, or WT may rely upon these proposed modifications until such time.

B. Permanent Residence Address Subject to Hold Mail Instruction for Chapters 3 and 4

In response to comments received on the 2014 temporary coordination regulations and the 2014 QI agreement regarding the definition of a “permanent residence address,” the 2017 coordination regulations (and the 2017 chapter 4 regulations by cross-reference) allow an address to be treated as a permanent residence address despite being subject to a hold mail instruction when a person provides documentary evidence establishing residence in the country in which the person claims to be a resident for tax purposes. Comments noted that the allowance to obtain documentary evidence establishing residence in a particular country is unnecessarily strict when the person is not claiming treaty benefits, and that it is unclear what documentary evidence may be used to establish residence for purposes of this allowance.

These proposed regulations provide that the documentary evidence required in order to treat an address that is provided subject to a hold mail instruction as a permanent residence address is documentary evidence that supports the person’s claim of foreign status or, for a person claiming treaty benefits, documentary evidence that supports the person’s residence in the country where the person claims treaty benefits. Regardless of whether the person claims treaty benefits, the documentary evidence on which a withholding agent may rely is the documentary evidence described in

§ 1.1471–3(c)(5)(i), without regard to the requirement that the documentation contain a permanent residence address.

A comment also requested the removal of any limitation on reliance on a permanent residence address subject to a hold mail instruction because many account holders prefer to receive electronic correspondence rather than paper mail. In response to this comment, proposed § 1.1471–1(b)(62) adds a definition of a hold mail instruction to clarify that a hold mail instruction does not include a request to receive all correspondence (including account statements) electronically.

These proposed regulations apply for purposes of chapters 3 and 4. A QI, WP, or WT may rely upon these proposed modifications until they are incorporated into the 2017 QI agreement and 2017 WP and WT agreements.

VI. Revisions Related to Credits and Refunds of Overwithheld Tax

A. Withholding and Reporting in a Subsequent Year

Under § 1.1441–5(b)(2)(i)(A), a U.S. partnership is required to withhold on an amount subject to chapter 3 withholding (as defined in § 1.1441–2(a)) that is includible in the gross income of a partner that is a foreign person. A U.S. partnership satisfies this requirement by withholding on distributions to the foreign partner that include an amount subject to chapter 3 withholding. To the extent a foreign partner's distributive share of income subject to chapter 3 withholding is not actually distributed to the partner, the U.S. partnership must withhold on the partner's distributive share of the income on the earlier of the date that the statement required under section 6031(b) (Schedule K–1, Partner's Share of Income, Deductions, Credits, etc.) is mailed or otherwise provided to the partner or the due date for furnishing the statement. Under section 6031(b), a partnership that files its return for a calendar year (calendar-year partnership) must generally furnish to each partner a Schedule K–1 on or before March 15 following the close of the taxable year, a due date that may be extended up to six months. See §§ 1.6031(b)–1T(b) and 1.6081–2T(a). Similar requirements apply to a foreign partnership that has entered into an agreement with the IRS to act as a WP. See the 2017 WP agreement. A foreign partnership other than a WP generally satisfies its withholding requirement in the same manner for amounts received from a withholding agent that failed to withhold to the extent required. See § 1.1441–5(c)(2) and (c)(3)(v). For

purposes of chapter 4, similar withholding rules apply to a partnership that receives a withholdable payment allocable to a foreign partner. See § 1.1473–1(a)(5)(ii) and (vi).

Under § 1.1461–1(c)(1) and (2), a partnership is required to report on Form 1042–S, Foreign Person's U.S. Source Income Subject to Withholding, any amount subject to withholding that is allocable to a foreign partner for a calendar year. The partnership must file Form 1042–S (and furnish a copy to the partner) by March 15 of the calendar year following the year in which it receives the amount subject to withholding. The due date for filing a Form 1042–S may be automatically extended by 30 days (and an additional 30 days at the discretion of the IRS). See § 1.6081–8T(a). Amounts that are reportable on Forms 1042–S are also required to be reported on a withholding agent's income tax return, Form 1042, Annual Withholding Tax Return for U.S. Source Income of Foreign Persons. The due date for Form 1042 is March 15, which may be automatically extended for six months. See § 1.6081–10. Similar reporting rules apply to a partnership that receives a withholdable payment and withholds under chapter 4. See § 1.1474–1(c) and (d)(1).

Because the extended due date for filing a Form 1042–S generally occurs before the extended due date for furnishing a Schedule K–1 to a foreign partner, a partnership may be required to report an amount subject to withholding on a Form 1042–S before it performs all of the withholding required on such amount under § 1.1441–5(b)(2)(i)(A) or § 1.1473–1(a)(5)(ii) and (vi). To address this case, the Instructions for Form 1042 require a domestic partnership to report any withholding that occurs with respect to an amount that a partnership received but did not distribute to a partner in a calendar year (preceding year) on the partnership's Form 1042 for the following calendar year (subsequent year) (referred to as the "lag method" of reporting). In this case, the partnership would deposit the amount in the subsequent year and designate the deposit as made for that year for reporting on Form 1042. To correspond to the timing of the reporting on Form 1042, the partnership must also report this withholding on Forms 1042–S filed and issued for the subsequent year. For example, a calendar year domestic partnership that receives U.S. source dividends in 2017 (but does not make a distribution to its foreign partners), must withhold on the foreign partners' share of the dividend income by the

time the partnership issues Schedules K–1 to the foreign partners, which could be as late as September 15, 2018. The lag method of reporting requires the partnership to report the withholding on the Forms 1042–S and 1042 for the 2018 year (which are issued and filed in 2019). The WP agreement includes a similar requirement to that described in this paragraph when a WP withholds after the due date for Form 1042–S (including extensions). The Instructions for Form 1042 provide a similar reporting rule for a domestic trust that withholds in a subsequent year on income of the trust that it is required to distribute but has not actually distributed to a foreign beneficiary. See § 1.1441–5(b)(2)(ii) and (iii). The WT agreement includes a similar requirement for a WT.

Apart from the cases described in the preceding paragraph, in certain other cases, a withholding agent is permitted to withhold an amount in a subsequent year that relates to the preceding year. For example, a withholding agent adjusting underwithholding under § 1.1461–2(b) or § 1.1474–2(b) may withhold the additional amount by the due date (without extensions) of Form 1042. In these cases, the Instructions for Form 1042 provide that, in contrast to the reporting required by partnerships and certain trusts described in the preceding paragraph, a withholding agent withholding in a subsequent year must designate the deposit and report the tax for the preceding year.

Comments have noted issues that arise under the lag method when a partner files an income tax return to report the partnership income allocated to the partner and to claim credit under section 33 (or a refund) based on the partnership's withholding. When a partnership applies the lag method, it issues a Form 1042–S for the subsequent year (and the related withholding) that generally reflects the income received by the partnership in the preceding year. However, the income is reported to the partner on Schedule K–1 for the preceding year, thus resulting in a mismatch between the income allocated to the partner and the withholding on that income. Because a partner must attach to its income tax return a Form 1042–S that it receives from a partnership to claim a credit or refund of overwithholding under § 301.6402–3(e), the partner cannot support the claim with the Form 1042–S until after the year in which the partner is required to report the income shown on the Schedule K–1.

These proposed regulations generally require a withholding agent (including a partnership or trust) that withholds in a

subsequent year to designate the deposit as attributable to the preceding year and report the amount on Forms 1042 and 1042-S for the preceding year. This proposed rule incorporates the existing rule for withholding agents (other than partnerships and trusts) from the form instructions, and extends the rule to partnerships and trusts. An exception to this requirement for a partnership that is not a calendar-year partnership (a fiscal-year partnership) provides that such partnership may designate a deposit as made for the subsequent year and report the amount on Forms 1042 and 1042-S for the subsequent year. This exception allows a fiscal-year partnership flexibility to determine the year for reporting that will result in the best matching of the income and the related withholding.

These proposed regulations also provide a revised due date for a partnership to file and furnish Form 1042-S when it withholds the tax after March 15 of the subsequent year that it designates as deposited for the preceding year. Under this new rule, the due date for a partnership to file and furnish a Form 1042-S in such a case will be September 15 of the subsequent year. This revised due date corresponds to the due date for a partnership to file Form 1042 with an extension and the due date for a calendar-year partnership to furnish a Schedule K-1 to a partner with an extension so that the partnership has sufficient time to determine the amount of withholding due and to coordinate with the extended due date for furnishing the Schedule K-1.

Based on the revisions included in these proposed regulations, the IRS intends to amend the Instructions for the 2019 Form 1042 to remove the requirement that a partnership or trust apply the lag method and to incorporate these proposed regulations. The IRS also intends to amend the Instructions to the 2019 Form 1042-S to require that in a case when a partnership is filing Form 1042-S after March 15 for a partner's distributive share of an amount received by the partnership in the preceding year, the partnership must file and issue a separate Form 1042-S for such amount for the preceding year (in addition to any Forms 1042-S filed and issued to the partner for amounts that are withheld when distributed to the partner before March 15 and reported for the preceding year).

The Treasury Department and the IRS intend to amend the WP and WT agreements to the extent necessary to incorporate the proposed regulations, and until such time a WP or WT may rely on these proposed modifications for

purposes of its filing and deposit requirements.

B. Adjustments to Overwithholding Under the Reimbursement and Set-Off Procedures

Under § 1.1461-2(a), a withholding agent that has overwithheld and deposited the tax may adjust the overwithheld amount under either the reimbursement procedure or the set-off procedure. Under the reimbursement procedure, a withholding agent may repay the beneficial owner or payee the amount of tax overwithheld and then reimburse itself by reducing, by the amount of such repayment, any deposit of withholding tax otherwise required to be made before the end of the calendar year following the year of overwithholding. The withholding agent must make any repayment to the beneficial owner or payee before the earlier of the due date for filing Form 1042-S (without extensions) for the calendar year of overwithholding or the date on which the Form 1042-S is actually filed with the IRS, and must state on a timely filed Form 1042 (without extensions) for the calendar year of overwithholding that the filing constitutes a claim for credit in accordance with § 1.6414-1.

Under the set-off procedure, a withholding agent may apply the overwithheld amount against any amount which would otherwise be subject to withholding that is paid to the beneficial owner or payee before the earlier of the due date for filing Form 1042-S (without extensions) for the calendar year of overwithholding or the date that the Form 1042-S is actually filed with the IRS. Similar rules for adjusting overwithholding apply for purposes of chapter 4. See § 1.1474-2(a)(3) and (4).

If a withholding agent cannot apply the reimbursement or set-off procedure, a beneficial owner or payee must file a claim for credit or refund with the IRS in order to recover the overwithheld tax. Informal comments have requested to expand the cases in which a withholding agent may apply the reimbursement and set-off procedures in order to limit the need for a beneficial owner or payee to claim a credit or refund. These proposed regulations respond to these comments by modifying the reimbursement procedure to allow a withholding agent to use the extended due date for filing Forms 1042 and 1042-S to make a repayment and claim a credit. These proposed regulations also include revisions to conform the requirements for the set-off procedures to those that apply to the reimbursement procedures. In addition,

these proposed regulations remove the requirement that a withholding agent include with its Form 1042 a statement that the filing constitutes a claim for credit when it applies reimbursement in the year following the year of the overwithholding. This statement is no longer necessary because Form 1042 was revised in 2016 to provide separate fields for adjustments to overwithholding and underwithholding.

These proposed regulations also provide that a withholding agent may not apply the reimbursement and set-off procedures after the date on which Form 1042-S has been furnished to the beneficial owner or payee (in addition to, under the current regulations, after the date a Form 1042-S has been filed). Because of the liberalizing amendments described in the preceding paragraph, this change is needed to ensure that a Form 1042-S furnished to a beneficial owner or payee reflects any repayments made pursuant to these adjustment procedures and is consistent with the associated Form 1042-S that is filed with the IRS. A QI, WP, or WT may rely upon the proposed modifications described in this section VI.B until they are incorporated into the 2017 QI agreement and 2017 WP and WT agreements.

C. Reporting of Withholding by Nonqualified Intermediaries

A withholding agent that makes a payment subject to chapter 3 withholding to a nonqualified intermediary (as defined in § 1.1441-1(c)(14)) can reliably associate the payment with documentation when it obtains a valid intermediary withholding certificate (that is, Form W-8IMY, Certificate of Foreign Intermediary, Foreign Flow-Through Entity, or Certain U.S. Branches for United States Tax Withholding) from the nonqualified intermediary and a withholding statement that allocates the payment among the payees and includes the documentation for each payee as described in § 1.1441-1(b)(2)(vii)(B) and (e)(3)(iii). For purposes of chapter 4, a withholding agent making a withholdable payment to a nonqualified intermediary that is a participating FFI or a registered deemed-compliant FFI may rely on a withholding statement that includes an allocation of the payment to a chapter 4 withholding rate pool of payees, and must obtain payee-specific documentation for payees that are not includible in a chapter 4 withholding rate pool to permit any reduced rate of withholding. See § 1.1471-3(c)(3)(iii)(B).

To the extent that a withholding agent cannot reliably associate a withholdable

payment made to a nonqualified intermediary with valid documentation under § 1.1471-3(c), the withholding agent must presume that the payment is made to a nonparticipating FFI and withhold 30 percent of the payment. See § 1.1471-3(f)(5). In such a case, the withholding agent is required to report the payment as a chapter 4 reportable amount made to an unknown recipient on a Form 1042-S that reports the nonqualified intermediary as an intermediary and the amount withheld as chapter 4 withholding. See the Instructions for Form 1042-S. If the amount withheld upon under chapter 4 is an amount subject to withholding under chapter 3, the withholding agent is relieved from its obligation to also withhold under chapter 3 on the payment. § 1.1441-3(a)(2). To the extent that a nonqualified intermediary is required to report the same payments to its account holders on Forms 1042 and 1042-S under the chapter 3 or 4 regulations, the nonqualified intermediary need not withhold when chapter 3 or 4 withholding has already been applied by its withholding agent, and it substantiates the withholding by attaching to its Form 1042 a copy of the Form 1042-S furnished by the withholding agent.

Comments have noted that some U.S. withholding agents charge fees for the administrative burden associated with reviewing underlying documentation that is included with a withholding statement provided by a nonqualified intermediary. In other cases, nonqualified intermediaries may not be able to obtain such documentation from account holders. For these reasons, some nonqualified intermediaries provide withholding agents with valid Forms W-8IMY to establish their chapter 4 statuses but do not provide any underlying payee documentation or withholding rate pool information to substantiate the allocations to payees shown on a withholding statement. Comments have stated that the requirement for withholding agents to report the withholding applied to withholdable payments as chapter 4 withholding in these cases (because the payees are presumed to be nonparticipating FFIs) has made it difficult for account holders to claim foreign tax credits from foreign jurisdictions that do not view the chapter 4 withholding tax as a creditable income tax. These comments recommended various proposals to allow a nonqualified intermediary to report the withholding as chapter 3 withholding applied to its account holders.

In response to the comments described in the preceding paragraph, these proposed regulations modify the rules for reporting by a nonqualified intermediary under §§ 1.1461-1(c)(4)(iv) and 1.1474-1(d)(2)(ii) to address a case in which a nonqualified intermediary receives a payment for which a withholding agent has withheld at the 30-percent rate under chapter 4 and reported the payment on Form 1042-S as made to an unknown recipient. In such a case, these proposed regulations permit a nonqualified intermediary that is a participating FFI or registered deemed-compliant FFI to report the withholding applied to the nonqualified intermediary on a Form 1042-S as chapter 3 withholding to the extent that the nonqualified intermediary determines that the payment is not an amount for which withholding is required under chapter 4 based on the payee's chapter 4 status. Under the existing reporting requirements, the nonqualified intermediary would be required to file a Form 1042 and would need to be furnished a copy of the Form 1042-S filed by the withholding agent to substantiate the credit against its withholding tax liability for the withholding applied by its withholding agent. Under the modified requirement, the nonqualified intermediary would be permitted to substantiate the credit even though the Form 1042-S furnished to it reports chapter 4 withholding and the corresponding Forms 1042-S that the nonqualified intermediary issues reports chapter 3 withholding. This change should assist account holders using Form 1042-S to claim foreign tax credits in their jurisdictions of residence in these cases. The Treasury Department and the IRS are of the view that this determination should be limited to a nonqualified intermediary that is a participating FFI or registered deemed-compliant FFI given the role of these FFIs in documenting their account holders for chapter 4 purposes and their compliance requirements under the chapter 4 regulations or an applicable IGA jurisdiction.

Reliance on Proposed Regulations

Under section 7805(b)(1)(C), taxpayers may rely on the proposed regulations until final regulations are issued, except as otherwise provided in this paragraph. With respect to the elimination of withholding on non-cash value insurance premiums under proposed § 1.1473-1(a)(3)(iii), the clarification of the definition of a "managed by" investment entity under proposed § 1.1471-5(e)(4)(i)(B), and the revised allowance for a permanent residence address subject to a hold mail

instruction under proposed §§ 1.1441-1(c)(38) and 1.1471-1(b)(99), taxpayers may apply the modifications in these proposed regulations for all open tax years until final regulations are issued. For the revisions included in these proposed regulations that relate to credits and refunds of withheld tax, taxpayers may not rely on these proposed regulations until Form 1042 and Form 1042-S are updated for the 2019 calendar year.

Special Analyses

The Administrator of the Office of Information and Regulatory Affairs (OIRA), Office of Management and Budget (OMB), has waived review of this proposed rule in accordance with section 6(a)(3)(A) of Executive Order 12866. OIRA will subsequently make a significance determination of the final rule, pursuant to section 3(f) of Executive Order 12866 and the April 11, 2018, Memorandum of Agreement between the Treasury Department and the OMB.

The Treasury Department and the IRS expect the proposed regulation, when final, to be an Executive Order 13771 deregulatory action and request comment on this designation.

Paperwork Reduction Act

The collection of information contained in these proposed regulations is in a number of provisions, including §§ 1.1441-1, 1.1461-1, 1.1461-2, 1.1474-1, and 1.1474-2. The IRS intends that the information collection requirements of these regulations will be implemented through the use of Forms 1042 and 1042-S. As a result, for purposes of the Paperwork Reduction Act (44 U.S.C. 3507), the reporting burden associated with the collection of information in these regulations will be reflected in the information burden and OMB control number of the appropriate IRS form.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid control number.

The proposed regulations will not increase the number of taxpayers required to file a return. Current filers may have to modify slightly how they report, but the burden of reporting should not increase.

As described in section VI.A of the Explanations of Provisions, the proposed regulations allow a partnership that withholds in a subsequent year to designate the deposit as attributable to the preceding year and report the withholding on Forms 1042 and 1042-S for the preceding year

(rather than the subsequent year). In addition, the proposed regulations allow a partnership that withholds after March 15 of the subsequent year to file Form 1042-S on or before September 15 of such year. The IRS intends to modify Form 1042-S to add a check box to the form so that a partnership filer can indicate that it qualifies for the September 15 due date for filing the form. A partnership that relies on the September 15 due date may need to file an additional Form 1042-S if it is filing to report a partner's distributive share of an amount received by the partnership in the preceding year and it has already filed a Form 1042-S for such partner for the same year. Information on the number of partnerships that withhold in a year subsequent to the year in which the amount was received is not available. However, as an upper bound, table 1 shows the estimated number of partnerships that file Form 1042.

As explained in section IV.B of the Explanation of Provisions, the proposed regulations provide additional time for withholding agents to apply the reimbursement or set-off procedure to adjust overwithholding. The proposed revision may increase the amounts reported by filers of Forms 1042 and 1042-S, but should not affect the number of filers. It is unknown how many withholding agents will use the reimbursement and set-off procedures as a result of the modifications to those procedures in the proposed regulations. However, as an upper bound, table 1 shows the estimated number of withholding agents that report non-zero amounts as adjustments to overwithholding.

Finally, as described in section IV.C of the Explanation of Provisions, the proposed regulations permit certain nonqualified intermediaries to report on certain payments on Form 1042-S using the code for chapter 3 withholding rather than the code for chapter 4 withholding in certain cases in which chapter 4 withholding is applied on payments made to the nonqualified intermediaries. This modification in the proposed regulations should not affect the number of filers or increase any burdens, but rather change how nonqualified intermediaries report to certain recipients. It is not possible to estimate the number of nonqualified intermediaries that may change the code from chapter 4 to chapter 3, so as an upper bound, table 1 shows the estimated number of withholding agents that are nonqualified intermediaries that file Form 1042-S.

TABLE 1—RELATED TAX FORM COUNTS

| | Number of respondents (estimated) |
|---|-----------------------------------|
| Total number of Form 1042 filers | 45,000–50,000 |
| Partnership filers of Form 1042 | 2,000–3,000 |
| Form 1042 filers reporting adjustments to overwithholding | 4,000–5,000 |
| Nonqualified intermediaries filers of Form 1042-S | 500 |

Tax Form 1042 data are from administrative tax files while the Form 1042-S information is from a 2016 data file on foreign tax withholding.

Books and records relating to a collection of information must be retained as long as their contents may be material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential, as required by 26 U.S.C. 6103.

Regulatory Flexibility Act

It is hereby certified that the collection of information requirements in this notice of proposed rulemaking will not have a significant economic impact on a substantial number of small business entities within the meaning of section 601(6) of the Regulatory Flexibility Act (5 U.S.C. chapter 6). This notice of proposed rulemaking reduces the information required to be reported under chapters 3 and 4 as required by TDs 9610, 9657, 9658, 9808, and 9809, information collections that were certified by the Treasury Department and the IRS as not resulting in a significant economic impact on a substantial number of small business entities. The burden-reducing information collections of this notice of proposed rulemaking provide benefits for small business entities consistent with the Regulatory Flexibility Act's objective that information collections achieve statutory objectives while minimizing any significant impact on small business entities. Therefore, a Regulatory Flexibility Analysis is not required.

Pursuant to section 7805(f), this regulation has been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small businesses.

Statement of Availability of IRS Documents

IRS Revenue Procedures, Revenue Rulings, Notices, and other guidance cited in this preamble are published in

the Internal Revenue Bulletin (or Cumulative Bulletin) and are available from the Superintendent of Documents, U.S. Government Publishing Office, Washington, DC 20402, or by visiting the IRS website at www.irs.gov.

Comments and Requests for Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any comments that are submitted timely to the IRS as prescribed in this preamble under the "Addresses" heading. The Treasury Department and the IRS request comments on all aspects of the proposed rules but specifically on foreign passthru payment withholding and the definition of investment entity, as discussed in section II of the Explanation of Provisions. All comments will be available for public inspection and copying. A public hearing will be scheduled if requested in writing by any person that timely submits written comments. If a public hearing is scheduled, notice of the date, time, and place for the public hearing will be published in the **Federal Register**.

Drafting Information

The principal authors of these proposed regulations are John Sweeney, Nancy Lee, and Subin Seth, Office of Associate Chief Counsel (International). However, other personnel from the IRS and the Treasury Department participated in their development.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

Proposed Amendments to the Regulations

Accordingly, 26 CFR part 1 is proposed to be amended as follows:

PART 1—INCOME TAXES

■ **Paragraph 1.** The authority citation for part 1 is amended by revising the entries for §§ 1.1471-1, 1.1471-2, 1.1471-3, 1.1471-4, and 1.1474-4 to read in part as follows:

Authority: 26 U.S.C. 7805 * * *

* * * * *
Section 1.1471-1 also issued under 26 U.S.C. 1471 and 26 U.S.C. 1473.

Section 1.1471-2 also issued under 26 U.S.C. 1471 and 26 U.S.C. 1473.

Section 1.1471-3 also issued under 26 U.S.C. 1471 and 26 U.S.C. 1473.

Section 1.1471-4 also issued under 26 U.S.C. 1471 and 26 U.S.C. 1474.

* * * * *

Section 1.1474–1 also issued under 26 U.S.C. 1473 and 26 U.S.C. 1474.

■ **Par. 2.** Section 1.1441–1 is amended by revising paragraphs (c)(38) and (e)(4)(ii)(A)(2) to read as follows:

§ 1.1441–1 Requirement for the deduction and withholding of tax on payments to foreign persons.

(c) * * *
(38) *Permanent residence address*—(i) *In general.* The term *permanent residence address* is the address in the country of which the person claims to be a resident for purposes of that country's income tax. In the case of a withholding certificate furnished in order to claim a reduced rate of withholding under an income tax treaty, whether a person is a resident of a treaty country must be determined in the manner prescribed under the applicable treaty. See § 1.1441–6(b). The address of a financial institution with which the person maintains an account, a post office box, or an address used solely for mailing purposes is not a permanent residence address unless such address is the only address used by the person and appears as the person's registered address in the person's organizational documents. Further, an address that is provided subject to a hold mail instruction (as defined in § 1.1471–1(b)(62)) is not a permanent residence address unless the person provides the documentary evidence described in paragraph (c)(38)(ii) of this section. If, after a withholding certificate is provided, a person's permanent residence address is subsequently subject to a hold mail instruction, the addition of the hold mail instruction is a change in circumstances requiring the person to provide the documentary evidence described in paragraph (c)(38)(ii) of this section in order for a withholding agent to use the address as a permanent residence address. If the person is an individual who does not have a tax residence in any country, the permanent residence address is the place at which the person normally resides. If the person is an entity and does not have a tax residence in any country, then the permanent residence address of the entity is the place at which the person maintains its principal office.

(ii) *Hold mail instruction.* An address that is subject to a hold mail instruction (as defined in § 1.1471–1(b)(62)) can be used by a withholding agent as a permanent residence address if the person has provided the withholding agent with documentary evidence described in § 1.1471–3(c)(5)(i) (without

regard to the requirement in § 1.1471–3(c)(5)(i) that the documentary evidence contain a permanent residence address). The documentary evidence described in § 1.1471–3(c)(5)(i) must support the person's claim of foreign status or, in the case of a person that is claiming treaty benefits, must support residence in the country where the person is claiming a reduced rate of withholding under an income tax treaty.

(e) * * *
(4) * * *
(ii) * * *
(A) * * *
(2) *Documentary evidence for treaty claims and treaty statements.*

Documentary evidence described in § 1.1441–6(c)(3) or (4) shall remain valid until the last day of the third calendar year following the year in which the documentary evidence is provided to the withholding agent, except as provided in paragraph (e)(4)(ii)(A)(2). A treaty statement provided by an entity that identifies a limitation on benefits provision for a publicly traded corporation shall not expire at the time provided in the preceding sentence if a withholding agent determines, based on publicly available information at each time for which the treaty statement would otherwise be renewed, that the entity is publicly traded. A withholding agent described in the preceding sentence must retain a record of the information relied upon (to confirm that the entity is publicly traded) for as long as it may be relevant to the determination of the withholding agent's tax liability under section 1461 and § 1.1461–1.

Notwithstanding the second sentence of this paragraph (e)(4)(ii)(A)(2), a treaty statement provided by an entity that identifies a limitation on benefits provision for a government or tax-exempt organization (other than a tax-exempt pension trust or pension fund) shall remain valid indefinitely. Notwithstanding the validity periods (or exceptions thereto) prescribed in this paragraph (e)(4)(ii)(A)(2), a treaty statement will cease to be valid if a change in circumstances makes the information on the statement unreliable or incorrect. For accounts opened and treaty statements obtained prior to January 6, 2017 (including those from

publicly traded corporations, governments, and tax-exempt organizations), the treaty statement will expire January 1, 2020.

■ **Par. 3.** Section 1.1441–6 is amended by adding a sentence at the end of paragraph (c)(5)(i) to read as follows:

§ 1.1441–6 Claim of reduced withholding under an income tax treaty.

(c) * * *
(5) * * *
(i) * * * A withholding agent may rely on the taxpayer's claim on a treaty statement regarding its reliance on a specific limitation on benefits provision absent actual knowledge that such claim is unreliable or incorrect.

■ **Par. 4.** Section 1.1461–1 is amended by:

- 1. Adding two sentences after the first sentence in paragraph (a)(1).
- 2. Redesignating paragraph (c)(1)(i) as paragraph (c)(1)(i)(A) and adding paragraphs (c)(1)(i) introductory text and (c)(1)(i)(B).
- 3. Adding a sentence at the end of paragraph (c)(4)(iv).

The additions read as follows:

§ 1.1461–1 Payment and returns of tax withheld.

(a) * * * (1) * * * In a case in which a withholding agent is permitted to withhold on an amount subject to reporting (as defined in paragraph (c)(2) of this section) in a calendar year (subsequent year) following the calendar year (preceding year) in which the withholding agent paid such amount (or, for a partnership or trust withholding with respect to a foreign partner, beneficiary, or owner, the year the partnership or trust received such amount), the withholding agent shall designate the deposit of the withholding as made for the preceding year and report the tax liability on Form 1042 for the preceding year. In the case of a partnership that withholds as described in the preceding sentence and does not file its federal income tax return on a calendar-year basis, however, such partnership may instead designate the deposit as made for the subsequent year and report the tax liability on Form 1042 for the subsequent year. * * *

(c) * * *
(1) * * *

(i) *Withholding agent information reporting.* This paragraph (c)(1)(i) describes the general requirements for a withholding agent to file an information return on Form 1042–S and describes a special rule for a withholding agent that

withholds in a subsequent year as described in paragraph (a)(1) of this section.

* * * * *

(B) *Special reporting by withholding agents that withhold in a subsequent year.* Notwithstanding the first sentence of paragraph (c)(1)(i)(A) of this section, if a withholding agent designates the deposit of such withholding as made for the preceding calendar year as described in paragraph (a)(1) of this section, the withholding agent is required to report the amount on Form 1042-S for the preceding year. With respect to a withholding agent described in the previous sentence that is a partnership and that withholds after March 15 of the subsequent year, such partnership may file and furnish the Form 1042-S on or before September 15 of that year. In the case of a partnership that designates the deposit of such withholding as made for the subsequent year as permitted in paragraph (a)(1) of this section, however, the partnership shall report the amount on Form 1042-S for the subsequent year.

* * * * *

(4) * * *

(iv) * * * If a nonqualified intermediary that is a participating FFI or a registered deemed-compliant FFI receives a payment that has been withheld upon at a 30-percent rate under chapter 4 by another withholding agent and that is reported as made to an unknown recipient on Form 1042-S provided to the nonqualified intermediary, the nonqualified intermediary may report the payment (or portion of the payment) on Form 1042-S as made to a recipient that has been withheld upon under chapter 3 when the payment is not an amount for which withholding is required under chapter 4 based on the payee's chapter 4 status and the nonqualified intermediary reports the correct withholding rate for the recipient.

* * * * *

■ **Par. 5.** Section 1.1461-2 is amended by:

- 1. Revising the second sentence of paragraph (a)(2)(i) introductory text.
- 2. Revising paragraphs (a)(2)(i)(A) and (B).
- 3. Adding paragraph (a)(2)(i)(C).
- 4. Revising paragraph (a)(3).

The revisions and addition read as follows:

§ 1.1461-2 Adjustments for overwithholding or underwithholding of tax.

(a) * * *

(2) * * *

(i) * * * In such a case, the withholding agent may reimburse itself

by reducing, by the amount of tax actually repaid to the beneficial owner or payee, the amount of any deposit of withholding tax otherwise required to be made by the withholding agent under § 1.6302-2(a)(1)(iii) for any subsequent payment period occurring before the end of the calendar year following the calendar year of overwithholding. * * *

(A) The repayment to the beneficial owner or payee occurs before the earliest of the due date (including extensions) for filing the Form 1042-S for the calendar year of overwithholding, the date the Form 1042-S is actually filed with the IRS, or the date the Form 1042-S is furnished to the beneficial owner or payee;

(B) The withholding agent states on a timely filed (including extensions) Form 1042-S for the calendar year of overwithholding the amount of tax withheld and the amount of any actual repayment; and

(C) The withholding agent states on a timely filed (including extensions) Form 1042 for the calendar year of overwithholding the amount of adjustments made to overwithholding under paragraph (a)(1) of this section and the amount of any credit claimed under § 1.6414-1.

* * * * *

(3) *Set-off.* Under the set-off procedure, the withholding agent may repay the beneficial owner or payee by applying the amount overwithheld against any amount of tax which otherwise would be required under chapter 3 or 4 of the Internal Revenue Code or the regulations under part 1 of this chapter to be withheld from income paid by the withholding agent to such person. Any such set-off that occurs for a payment period in the calendar year following the calendar year of overwithholding shall be allowed only if—

(i) The repayment to the beneficial owner or payee occurs before the earliest of the due date (including extensions) for filing the Form 1042-S for the calendar year of overwithholding, the date the Form 1042-S is actually filed with the IRS, or the date the Form 1042-S is furnished to the beneficial owner or payee;

(ii) The withholding agent states on a timely filed (including extensions) Form 1042-S for the calendar year of overwithholding the amount of tax withheld and the amount of any repayment made through set-off; and

(iii) The withholding agent states on a timely filed (including extensions) Form 1042 for the calendar year of overwithholding the amount of

under paragraph (a)(1) of this section and the amount of any credit claimed under § 1.6414-1.

* * * * *

■ **Par. 6.** Section 1.1471-1 is amended by:

- 1. Removing paragraph (b)(60) and redesignating paragraphs (b)(61) and (b)(62) as new paragraphs (b)(60) and (b)(61).
- 2. Adding new paragraph (b)(62).
- 3. Revising paragraph (b)(99).

The addition and revision read as follows:

§ 1.1471-1 Scope of chapter 4 and definitions.

* * * * *

(b) * * * (62) *Hold mail instruction.* The term *hold mail instruction* means a current instruction by a person to keep the person's mail until such instruction is amended. An instruction to send all correspondence electronically is not a hold mail instruction.

* * * * *

(99) *Permanent residence address.* The term *permanent residence address* has the meaning set forth in § 1.1441-1(c)(38).

* * * * *

■ **Par. 7.** Section 1.1471-2 is amended by:

- 1. Removing the language “or constitutes gross proceeds from the disposition of such an obligation” from the first sentence of paragraph (a)(1).
- 2. Removing and reserving paragraph (a)(2)(iii)(B).
- 3. Removing paragraph (a)(2)(vi).
- 4. Removing the language “, or any gross proceeds from the disposition of such an obligation” from the first and second sentences of paragraph (b)(1).
- 5. Removing the language “and the gross proceeds allocated to a partner from the disposition of such obligation as determined under § 1.1473-1(a)(5)(vii)” from paragraph (b)(3)(i).
- 6. Removing the language “and further includes a beneficiary's share of the gross proceeds from a disposition of such obligation as determined under § 1.1473-1(a)(5)(vii)” from paragraph (b)(3)(ii).
- 7. Removing the language “and the gross proceeds from the disposition of such obligation to the extent such owner is treated as owning the portion of the trust that consists of the obligation” from paragraph (b)(3)(iii).

The revision reads as follows:

§ 1.1471-2 Requirement to deduct and withhold tax on withholdable payments to certain FFIs.

(a) * * *

(2) * * *

(iii) * * *
 (B) [Reserved]
 * * * * *

§ 1.1471-3 [Amended]

- **Par. 8.** Section 1.1471-3 is amended by:
 - 1. Removing the language that reads “and that is excluded from the definition of a withholdable payment under § 1.1473-1(a)(4)” from paragraph (a)(3)(ii)(A)(4).
 - 2. Removing paragraph (c)(8)(iv) and redesignating paragraph (c)(8)(v) as new paragraph (c)(8)(iv).
- **Par. 9.** Section 1.1471-4 is amended by:
 - 1. Removing the language “or the gross proceeds from the disposition of such an obligation” from the seventh sentence of paragraph (b)(1).
 - 2. Revising paragraph (b)(4).
 The revision reads as follows:

§ 1.1471-4 FFI agreement.

* * * * *
 (b) * * *
 (4) *Foreign passthru payments.* A participating FFI is not required to deduct and withhold tax on a foreign passthru payment made by such participating FFI to an account held by a recalcitrant account holder or to a nonparticipating FFI before the date that is two years after the date of publication in the **Federal Register** of final regulations defining the term *foreign passthru payment*.
 * * * * *

- **Par. 10.** Section 1.1471-5 is amended by adding a sentence at the end of paragraph (e)(4)(i)(B) to read as follows:

§ 1.1471-5 Definitions applicable to section 1471.

* * * * *
 (e) * * *
 (4) * * *
 (i) * * *
 (B) * * * Notwithstanding the preceding sentence, an entity is not managed by another entity for purposes of this paragraph (e)(4)(i)(B) solely because the first-mentioned entity invests all or a portion of its assets in such other entity, if such other entity is a mutual fund, exchange traded fund, or a collective investment entity that is widely-held and is subject to investor protection regulation.
 * * * * *

- **Par. 11.** Section 1.1473-1 is amended by:
 - 1. Revising paragraph (a)(1).
 - 2. Removing the fourth sentence of paragraph (a)(2)(vii)(A).
 - 3. Removing and reserving paragraph (a)(3).
 - 4. Revising paragraph (a)(4)(iii).

- 5. Removing paragraph (a)(4)(iv) and redesignating paragraphs (a)(4)(v) through (viii) as new paragraphs (a)(4)(iv) through (vii).
- 6. Removing paragraph (a)(5)(vii).
 The revisions read as follows:

§ 1.1473-1 Section 1473 definitions.

(a) * * * (1) *In general.* Except as otherwise provided in this paragraph (a) and § 1.1471-2(b) (regarding grandfathered obligations), the term *withholdable payment* means any payment of U.S. source FDAP income (as defined in paragraph (a)(2) of this section).

* * * * *
 (3) [Reserved]
 (4) * * *

(iii) *Excluded nonfinancial payments.* Payments for the following: services (including wages and other forms of employee compensation (such as stock options)), the use of property, office and equipment leases, software licenses, transportation, freight, gambling winnings, awards, prizes, scholarships, interest on outstanding accounts payable arising from the acquisition of goods or services, and premiums for insurance contracts that do not have cash value (as defined in § 1.1471-5(b)(3)(vii)(B)). Notwithstanding the preceding sentence, excluded nonfinancial payments do not include the following: Payments in connection with a lending transaction (including loans of securities), a forward, futures, option, or notional principal contract, or a similar financial instrument; premiums for cash value insurance contracts or annuity contracts; amounts paid under cash value insurance or annuity contracts; dividends; interest (including substitute interest described in § 1.861-2(a)(7)) other than interest described in the preceding sentence; investment advisory fees; custodial fees; and bank or brokerage fees.
 * * * * *

- **Par. 12.** Section 1.1474-1 is amended by:
 - 1. Adding two sentences after the first sentence in paragraph (b)(1).
 - 2. Revising paragraph (b)(2).
 - 3. Redesignating paragraph (d)(1)(i) as paragraph (d)(1)(i)(A) and adding paragraphs (d)(1)(i) introductory text and (d)(1)(i)(B).
 - 4. Adding a sentence after the first sentence in paragraph (d)(2)(ii).
 The revisions and additions read as follows:

§ 1.1474-1 Liability for withheld tax and withholding agent reporting.

* * * * *
 (b) * * *
 (1) * * * In a case in which a withholding agent is permitted to

withhold on a chapter 4 reportable amount (as defined in paragraph (d)(2) of this section) in a calendar year (subsequent year) following the calendar year (preceding year) in which the withholding agent paid such amount (or, for a partnership or trust withholding with respect to a foreign partner, beneficiary, or owner, the year the partnership or trust received such amount), the withholding agent shall designate the deposit of the withholding as made for the preceding year and shall report the tax liability on Form 1042 for the preceding year. In the case of a partnership that withholds as described in the preceding sentence and does not file its federal income tax return on a calendar-year basis, however, such partnership may instead designate the deposit as made for the subsequent year and report the tax liability on Form 1042 for the subsequent year.* * *
 (2) *Special rule for foreign passthru payments that include an undetermined amount of income subject to tax.*
 [Reserved]

* * * * *
 (d) * * *
 (1) * * *
 (i) *Withholding agent information reporting.* This paragraph (d)(1)(i) describes the general requirements for a withholding agent to file an information return on Form 1042-S and describes a special rule for a withholding agent that withholds in a subsequent year as described in paragraph (b)(1) of this section.
 * * * * *

(B) *Special reporting by withholding agents that withhold in a subsequent year.* Notwithstanding the first sentence of paragraph (d)(1)(i)(A) of this section, if a withholding agent designates the deposit of such withholding as made for the preceding calendar year as described in paragraph (b)(1) of this section, the withholding agent is required to report the amount on Form 1042-S for the preceding year. With respect to a withholding agent described in the previous sentence that is a partnership and that withholds after March 15 of the subsequent year, such partnership may file and furnish the Form 1042-S on or before September 15 of that year. In the case of a partnership that designates the deposit of such withholding as made for the subsequent year as permitted in paragraph (b)(1) of this section, however, the partnership shall report the chapter 4 reportable amount on Form 1042-S for the subsequent year.
 * * * * *
 (2) * * *
 (ii) * * * A chapter 4 reportable amount also does not include an

amount received by a nonqualified intermediary that is a participating FFI or a registered deemed-compliant FFI if the nonqualified intermediary reports such amount as having been withheld upon under chapter 3 to the extent permitted under § 1.1461-1(c)(4)(iv).

* * *

* * * * *

■ **Par. 13.** Section 1.1474-2 is amended by revising the second sentence of paragraph (a)(3)(i) introductory text, paragraphs (a)(3)(i)(A) through (C), and paragraph (a)(4) to read as follows:

§ 1.1474-2 Adjustments for overwithholding or underwithholding of tax.

(a) * * *

(3) * * *

(i) * * * In such a case, the withholding agent may reimburse itself by reducing, by the amount of tax actually repaid to the beneficial owner or payee, the amount of any deposit of withholding tax otherwise required to be made by the withholding agent under § 1.6302-2(a)(1)(iii) for any subsequent payment period occurring before the end of the calendar year following the calendar year of overwithholding.

(A) The repayment to the beneficial owner or payee occurs before the earliest of the due date (including extensions) for filing the Form 1042-S for the calendar year of overwithholding, the date the Form 1042-S is actually filed with the IRS, or the date the Form 1042-S is furnished to the beneficial owner or payee;

(B) The withholding agent states on a timely filed (including extensions) Form 1042-S for the calendar year of overwithholding the amount of tax withheld and the amount of any actual repayment; and

(C) The withholding agent states on a timely filed (including extensions) Form 1042 for the calendar year of overwithholding the amount of adjustments made to overwithholding under paragraph (a)(1) of this section and the amount of any credit claimed under § 1.6414-1.

* * * * *

(4) *Set-off.* Under the set-off procedure, the withholding agent may repay the beneficial owner or payee by applying the amount overwithheld against any amount of tax which otherwise would be required under chapter 3 or 4 of the Internal Revenue Code or the regulations under part 1 of this chapter to be withheld from income paid by the withholding agent to such person. Any such set-off that occurs for a payment period in the calendar year following the calendar year of overwithholding shall be allowed only if—

(i) The repayment to the beneficial owner or payee occurs before the earliest of the due date (including extensions) for filing the Form 1042-S for the calendar year of overwithholding, the date the Form 1042-S is actually filed with the IRS, or the date the Form 1042-S is furnished to the beneficial owner or payee;

(ii) The withholding agent states on a timely filed (including extensions) Form 1042-S for the calendar year of overwithholding the amount of tax withheld and the amount of any repayment made through set-off; and

(iii) The withholding agent states on a timely filed (including extensions) Form 1042 for the calendar year of overwithholding the amount of adjustments made to overwithholding under paragraph (a)(1) of this section and the amount of any credit claimed under § 1.6414-1.

* * * * *

Kirsten Wielobob,
Deputy Commissioner for Services and Enforcement.

[FR Doc. 2018-27290 Filed 12-13-18; 4:15 pm]

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DEPARTMENT OF DEFENSE

Office of the Secretary

32 CFR Part 220

[Docket ID: DOD-2016-HA-0107]

RIN 0720-AB68

Collection From Third Party Payers of Reasonable Charges for Healthcare Services

AGENCY: Office of the Assistant Secretary of Defense (Health Affairs), DoD.

ACTION: Proposed rule.

SUMMARY: This rule exercises the Department of Defense’s (DoD’s) authority to update current regulations to compute reasonable charges for inpatient and ambulatory (outpatient) institutional resources and also for pharmaceuticals, durable medical equipment (DME), supplies, immunizations, injections or other medications administered or furnished by DoD military treatment facilities (MTFs) under their three existing healthcare cost recovery programs—Third Party Collections, Medical Services Account, and Medical Affirmative Claims. Specifically, the rule updates the reasonable charges methodologies for inpatient and ambulatory institutional billing to allow

for the use of Itemized Resource Utilization (IRU) based rates—developed from the cost to provide inpatient and ambulatory institutional healthcare resources—in addition to current bundled prospective reimbursement approaches of diagnostic related group (DRG), ambulatory payment classification (APC), ambulatory surgery center (ASC) and ambulatory procedure visit (APV) based rates. It also revises the reasonable charges methodology for pharmaceuticals, DME, supplies, immunizations, injections or medication administered to allow for their calculation using either Civilian Health and Medical Program of the Uniformed Services (CHAMPUS) prevailing rates or IRU based rates—developed from the cost to provide these healthcare items and resources— regardless of whether CHAMPUS prevailing rates are available. The additional IRU methodology implements an itemized rate and reasonable charges structure that improves collections and operation of DoD’s healthcare cost recovery programs by ensuring MTFs receive appropriate reimbursement for institutional healthcare resources as well as for pharmaceuticals, DME, supplies, immunizations, injections or medication provided or administered and is more consistent with civilian health insurance industry practice. The proposed rule also replaces “hospital” with “institutional” throughout most of the regulation to align it with civilian health insurance industry terminology and better promote identification and separate billing of institutional and professional services.

DATES: Comments must be received by February 19, 2019.

ADDRESSES: You may submit comments, identified by docket number and/or Regulatory Information Number (RIN) and title, by any of the following methods:

- *Federal Rulemaking Portal:* <http://www.regulations.gov>. Follow the instructions for submitting comments.
- *Mail:* Department of Defense, Office of the Deputy Chief Management Officer, Directorate for Oversight and Compliance, 4800 Mark Center Drive, Mailbox #24, Alexandria, VA 22350-1700.

Instructions: All submissions received must include the agency name and docket number or RIN for this **Federal Register** document. The general policy for comments and other submissions from members of the public is to make these submissions available for public viewing on the internet at <http://www.regulations.gov> as they are