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## RULES and REGULATIONS

## DEPARTMENT OF THE TREASURY

## Internal Revenue Service

## 26 CFR Part 5f

[T.D. 7852]

## Temporary Income Tax Regulations Under the Tax Equity and Fiscal Responsibility Act of 1982; Registration Requirements With Respect to Debt Obligations

Monday, November 15, 1982

**\*51361** AGENCY: Internal Revenue Service, Treasury.

**ACTION:** Temporary regulations.

**SUMMARY:** This document provides temporary regulations with respect to the requirement that debt obligations be issued in registered form. Changes to the applicable tax law were made by section 310 of the Tax Equity and Fiscal Responsibility Act of 1982. The regulations affect issuers and holders of obligations, and provide them with the guidance needed to comply with the law. In addition, these temporary regulations serve as the text of the proposed regulations cross-referenced in the notice of proposed rulemaking in the Proposed Rules section of this issue of the Federal Register.

**DATE:** Generally, the regulations apply to obligations issued after December 31, 1982.

**FOR FURTHER INFORMATION CONTACT:** Diane L. Kroupa of the Legislation and Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T (202) 566-3590).

**SUPPLEMENTARY INFORMATION:****Background**

This document contains temporary regulations relating to the requirement that certain debt obligations be issued in registered form under [sections 103](#) and [163 of the Internal Revenue Code](#) of 1954, as amended by the Tax Equity and Fiscal Responsibility Act of 1982 (Pub. L. 97-248, 96 Stat. 595). The temporary regulations provided by this document will remain in effect until superseded by final regulations on this subject.

**Rules**

The temporary regulations provide generally that any obligation issued after December 31, 1982, must be issued in registered form. If an obligation issued after December 31, 1982, is not issued in registered form, the issuer will be denied a deduction for interest paid or accrued on such obligation. Further, interest on an obligation is-

sued after such date that otherwise would be exempt from tax will not be tax exempt unless the obligation is issued in registered form. The regulations provide examples of certain obligations that are not required to be registered.

The temporary regulations provide that an obligation is issued in registered form if the transfer of the obligation can only be effected by the surrender of the old instrument to the issuer and either reissuance of the old instrument or issuance of a new instrument to the new holder. An obligation is also considered issued in registered form if the right to the principal of, and any stated interest on, the obligation can be transferred only through a book entry system. A book entry is a record of the ownership of an obligation.

On September 15, 1982, the Service issued a news release soliciting comments on provisions of the Tax Equity and Fiscal Responsibility Act of 1982 relating to the requirement of registration of debt obligations. The Service has received numerous comments, all of which have been carefully considered in the preparation of these regulations. In addition, persons are encouraged to make written comments by mail and oral comments at the public hearing. Notice of the time and place of the hearing appears in the notice of hearing section of this issue of the Federal Register.

#### Non-Applicability of [Executive Order 12291](#)

The Commissioner has determined that this temporary regulation is not a major rule subject to review under [Executive Order 12291](#) or the Treasury and OMB implementation of the Order dated April 28, 1982.

#### Regulatory Flexibility Act

No general notice of proposed rulemaking is required by [5 U.S.C. 553 \(b\)](#) for temporary regulations. Accordingly, the Regulatory Flexibility Act does not apply and no Regulatory Flexibility Analysis is required for these rules.

#### Drafting Information

The principal author of these proposed regulations is Diane L. Kroupa of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

#### List of Subjects in 26 CFR Part 5f

Income taxes, Deductions, Exemptions, Tax Equity and Fiscal Responsibility Act of 1982.

#### Adoption of amendments to the regulations

PART 5f—[AMENDED]26 CFR § 5f.103

26 CFR § 5f.163

26 CFR § 5f.168

Accordingly, Part 5f, Temporary Income Tax Regulations under the Tax Equity and Fiscal Responsibility Act of 1982, is amended by adding new §§ 5f.103-1 and 5f.163-1 immediately before § 5f.168 (f)(8)-1, to read as fol-

lows:

26 CFR § 5f.103

§ 5f.103-1 Obligations issued after December 31, 1982, required to be in registered form.

(a) Registration; general rule. Interest on a registration-required obligation (as \*51362 defined in paragraph (b) of this section) shall not be exempt from tax notwithstanding [section 103 \(a\)](#) or any other provision of law, exclusive of any treaty obligation of the United States, unless the obligation is issued in registered form (as defined in paragraph (c) of this section).

(b) Registration-required obligation. For purposes of this section, the term “registration-required obligation” means any obligation except any one of the following:

(b)(1) An obligation not of a type offered to the public. The determination as to whether an obligation is not of a type offered to the public shall be based on whether similar obligations are in fact publicly offered or traded.

(b)(2) An obligation that has a maturity at the date of issue of not more than 1 year.

(b)(3) An obligation issued before January 1, 1983. An obligation first issued before January 1, 1983, shall not be considered to have been issued on or after that date merely as a result of the existence of a right on the part of the holder of such obligation to convert the obligation from registered form into bearer form, or as a result of the exercise of such a right.

(b)(4) An obligation described in § 5f.163-1 (c) (relating to certain obligations issued to foreign persons).

(c) Registered form— (1) General rule. An obligation is in registered form if—

(c)(i) The obligation is registered as to both principal and any stated interest and transfer of the obligation may be effected only by the surrender of the old instrument and either the reissuance by the issuer of the old instrument to the new holder or the issuance by the issuer of a new instrument to the new holder, or

(c)(ii) The right to the principal of, and stated interest on, the obligation may be transferred only through a book entry system (as described in paragraph (c) (2) of this section).

(c)(ii)(2) Special rule for registration of a book entry obligation. An obligation shall be considered transferable through a book entry system if the ownership of an interest in the obligation is required to be reflected in a book entry, whether or not physical securities are issued. A book entry is a record of ownership that identifies the owner of an interest in the obligation.

(d) Effective date. The provisions of this section shall apply to obligations issued after December 31, 1982, unless issued on an exercise of a warrant for the conversion of a convertible obligation if such warrant or obligation was offered or sold outside the United States without registration under the Securities Act of 1933 and was issued before August 10, 1982.

(e) Obligations first issued after December 31, 1982, where the right exists for the holder to convert such obligation from registered form into bearer form. [Reserved]

(f) Examples. The application of this section may be illustrated by the following examples:

*Example (1).* Municipality X publicly offers its general debt obligations to United States persons. The obligations have a maturity at issue exceeding 1 year. The obligations are registration-required obligations under § 5f.103-1(b). When individual A buys an obligation, X issues an obligation in A's name evidencing A's ownership of the principal and interest under the obligation. A can transfer the obligation only by surrendering the obligation to X and by X issuing a new instrument to the new holder. The obligation is issued in registered form.

*Example (2).* Municipality Y issues a single obligation on January 4, 1983, in bearer form, to Bank M provided that (i) Bank M will not at any time transfer any interest in the obligation to any person unless the transfer is recorded on Municipality Y's records (except by means of a transfer permitted in (ii) of this example), and (ii) interests in the obligation that are sold by Bank M (and any persons who acquire interests from M) will be reflected in book entries. C, an individual, buys an interest in Y's obligation from Bank M. Bank M records such transfer by reflecting C's ownership on Bank M's books. Bank M receives the interest or principal payments with respect to C's interest in the obligation as agent for C. Any transfer of C's interest must be reflected in a book entry system. Since C's interest can only be transferred through a book entry system, the obligation is considered issued in registered form. Interest received by C is excludable from gross income under [section 103 \(a\)](#).

*Example (3).* Municipality Z wishes to sell its debt obligations having a maturity in excess of 1 year. The obligations are sold to Banks N, O, and P, all of which are located in Municipality Z. By their terms the obligations are freely transferable, although each of the banks has stated that it acquired the obligations for purposes of investment and not for resale. Obligations similar to the obligations sold by Municipality Z are traded in the market for municipal securities. The obligations issued by Municipality Z are of a type offered to the public and are therefore registration-required under § 5f.103-1 (b).

(g) Cross-references. See section 103A(j)(1) for the registration requirement of certain mortgage subsidy bonds issued after December 31, 1981, and § 6a.103A-1(a)(5) for the definition of registered form for such obligations issued after December 31, 1981, and on or before December 31, 1982. See also [section 103\(h\)](#) (requiring registration of certain energy bonds issued on or after October 18, 1979).

#### 26 CFR § 5f.163

§ 5f.163-1 Denial of interest deduction on certain obligations issued after December 31, 1982, unless issued in registered form.

(a) Denial of deduction generally. Interest paid or accrued on a registration-required obligation (as defined in paragraph (b) of this section) shall not be allowed as a deduction under [section 163](#) or any other provision of law unless such obligation is issued in registered form (as defined in § 5f.103-1(c)).

(b) Registration-required obligation. For purposes of this section, the term “registration-required obligation” means any obligation except any one of the following:

(b)(1) An obligation issued by a natural person.

(b)(2) An obligation not of a type offered to the public. The determination as to whether an obligation is not of a type offered to the public shall be based on whether similar obligations are in fact publicly offered or traded.

(b)(3) An obligation that has a maturity at the date of issue of not more than 1 year.

(b)(4) An obligation issued before January 1, 1983. An obligation first issued before January 1, 1983, shall not

be considered to have been issued on or after such date merely as a result of the existence of a right on the part of the holder of such obligation to convert such obligation from registered form into bearer form, or as a result of the exercise of such a right.

(b)(5) An obligation described in subparagraph (1) of paragraph (c) (relating to certain obligations issued to foreign persons).

(c) Obligations issued to foreign persons—(c)(1) General rule. An obligation is described in this subparagraph if—

(c)(1)(i) There are arrangements reasonably designed to ensure that such obligation will be sold (or resold in connection with its original issuance) only to a person who is not a United States person, and

(c)(1)(ii) In the case of an obligation which is not in registered form—

(c)(1)(ii)(A) Interest on such obligation is payable only outside the United States and its possessions, and

(c)(1)(ii)(B) On the face of such obligation there is a statement that any United States person who holds such obligation will be subject to limitations under the United States income tax laws, including the limitations provided in sections 165(j) and 1232(d).

(c)(2) Rules for application of this paragraph —(c)(2)(i) Obligations which satisfy paragraph (c)(1)(i) of this section; conversion into bearer or registered form. An obligation, whether **\*51363** originally issued in registered or bearer form, which satisfies the requirements of paragraph (c) (1)(i) of this section will not constitute a registration-required obligation, regardless of whether it is converted from bearer into registered form or from registered into bearer form, if at all times during which such obligation is in bearer form it also satisfies the requirements of paragraph (c)(1)(ii) (A) and (B) of this section. Failure of such an obligation to satisfy the requirements of paragraph (c)(1)(ii) (A) and (B) of this section during such time that the obligation is in registered form will not cause the obligation to be a registration-required obligation.

(c)(2)(ii) Obligations in registered form which do not satisfy paragraph (c)(1)(i) of this section; conditions under which such obligations may be converted into bearer form. [Reserved]

(c)(2)(iii) Arrangements reasonably designed to ensure sale to non-United States persons. An obligation for which there are arrangements reasonably designed to ensure that it will be sold (or resold in connection with its original issuance) only to a person who is not a United States person shall include an obligation offered for sale outside the United States which, in connection with its issuance, need not be registered under the Securities Act of 1933 because such obligation is intended for distribution to persons who are not United States persons. For this purpose, an obligation sold to United States persons within or without the United States on the basis of the exemption of section 4(2) of the Securities Act of 1933 shall not be considered to be intended for distribution to persons who are not United States persons. An obligation which is offered for sale outside the United States will not be considered to be required to be registered under the Securities Act of 1933 if the issuer, in reliance on the advice of independent counsel received prior to the issuance thereof, determines in good faith that the obligation need not be registered under the Securities Act of 1933 for the reason that it is intended for distribution to persons who are not United States persons.

(c)(2)(iv) Interest payable outside of the United States. Interest will be considered to be payable only outside the

United States or its possessions if payment of such interest only can be made upon presentation of a coupon, or upon the making of any other demand for payment, outside the United States and its possessions to the issuer or a paying agent. The fact that payment is made by a draft on a United States bank, by a wire transfer from a United States account, or by a direct transfer of funds into an account maintained by the payee in the United States does not affect this result. However, interest is considered to be paid within the United States or its possessions if a coupon is presented, or a demand for payment is otherwise made, to the issuer or a paying agent (whether a United States or foreign person) in the United States or its possessions even if the funds paid are credited to an account maintained by the payee outside the United States or its possessions.

(c)(2)(v) Determination on obligation-by-obligation basis. A determination of whether an obligation satisfies each of the requirements of paragraphs (c)(1) (i) and (ii) (A) and (b) of this section shall be made on an obligation-by-obligation basis.

(d) Effective date. The provisions of this section shall apply to obligations issued after December 31, 1982, unless issued on an exercise of a warrant for the conversion of a convertible obligation if such warrant or obligation was offered or sold outside the United States without registration under the Securities Act of 1933 and was issued before August 10, 1982.

(e) Obligations first issued after December 31, 1982, where the right exists for the holder to convert such obligation from registered form into bearer form. [Reserved]

(f) Examples. The application of this section may be illustrated by the following examples:

*Example (1).* All of the shares of Corporation X are owned by two individuals, A and B. X desires to sell all of its assets to Corporation Y, all of the shares of which are owned by individual C. Following the sale, Corporation X will be completely liquidated. As partial consideration for the Corporation X assets, Corporation Y delivers a promissory note to X, secured by a security interest and mortgage on the acquired assets. The note given by Y to X is not of a type offered to the public.

*Example (2).* Corporation Z has a credit agreement with Bank M pursuant to which Corporation Z may borrow amounts not exceeding \$10X upon delivery of Z's note to Bank M. The note Z delivers to M is not of a type offered to the public.

*Example (3).* Individuals D and E operate a retail business through partnership DE. D wishes to loan partnership DE \$5X. DE's note evidencing the loan from D is not of a type offered to the public.

*Example (4).* Individual F owns one-third of the shares of Corporation W. F makes a cash advance to W. W's note evidencing F's cash advance is not of a type offered to the public.

*Example (5).* Closely-held Corporation R places its convertible debentures with 30 individuals who are United States persons. The offering is not required to be registered under the Securities Act of 1933. Similar debentures are publicly offered and traded. The obligations are not considered of a type not offered to the public.

*Example (6).* In 1980, Corporation V issued its bonds due in 1986 through an offering registered with the Securities and Exchange Commission. Although the bonds were initially issued in registered form, the terms of the bonds permit a holder, at his option, to convert a bond into bearer form at any time prior to maturity. Similarly, a person who holds a bond in bearer form may, at any time, have the bond converted into registered form.

(f)(i) Assume G bought one of Corporation V's bonds upon the original issuance in 1980. In 1983, G requests that V convert the bond into bearer form. Except for the change from registered to bearer form, the terms of the bond are unchanged. The bond held by G is not considered issued after December 31, 1982, under § 5f.163-1(b)(4).

(f)(ii) Assume H buys one of Corporation V's bonds in the secondary market in 1983. The bond H receives is in registered form, but H requests that V convert the obligation into bearer form. There is no other change in the terms of the instrument. The bond held by H is not considered issued after December 31, 1982, under § 5f.163-1(b)(4).

(f)(iii) Assume the same facts as in (ii) except that in 1984 I purchases H's V Corporation bond, which is in bearer form. I requests V to convert the bond into registered form. There is no other change in the terms of the instrument. In 1985, I requests V to convert the bond back into bearer form. Again, there is no other change in the terms of the instrument. The bond purchased by I is not considered issued after December 31, 1982, under § 5f.163-1(b)(4).

*Example (7).* Corporation U wishes to make a public offering of its debentures to United States persons. U issues a master note to Bank N. The terms of the note require that any person who acquires an interest in the note must have such interest reflected in a book entry. Bank N offers for sale interests in the Corporation U note. Ownership interests in the note are reflected on the books of Bank N. Corporation U's debenture is considered issued in registered form.

*Example (8).* Issuer S wishes to make a public offering of its debt obligations to United States persons. The obligations will have a maturity in excess of one year. On November 1, 1982, the closing on the debt offering occurs. At the closing, the net cash proceeds of the offering are delivered to S, and S delivers a master note to the underwriter of the offering. On January 2, 1983, S delivers the debt obligations to the purchasers in definitive form and the master note is cancelled. The obligations are not registration-required because they are considered issued before January 1, 1983.

*Example (9).* In July 1983, Corporation T sells an issue of debt obligations maturing in 1985 to the public in the United States. Three of the obligations of the issue are issued to J in bearer form. The balance of the obligations of the issue are issued in registered form. The terms of the registered and bearer obligations are identical. The obligations issued to J are of a type offered to the public and are registration-required obligations. Since the \*51364 three obligations are issued in bearer form, T is subject to the tax imposed under section 4701 with respect to the three bearer obligations. In addition, interest paid or accrued on the three bearer obligations is not deductible by T. Moreover, since the issuance of the three bearer obligations is subject to tax under section 4701, J is not prohibited from deducting losses on the obligations under section 165 (j) or from treating gain on the obligations as capital gain under section 1232 (d). The balance of the obligations in the issue do not give rise to liability for the tax under section 4701, and the deductibility of interest on such obligations is not affected by [section 163 \(f\)](#).

*Example (10).* Broker K acquires a bond issued in 1980 by the United States Treasury through the Bureau of Public Debt. Broker K sells interests in the bond to the public after December 31, 1982. A purchaser may acquire an interest in any interest payment falling due under the bond or an interest in the principal of the bond. The bond is held by Custodian L for the benefit of the persons acquiring these interests. On receipt of interest and principal payments under the bond, Custodian L transfers the amount received to the person whose owner-

ship interest corresponds to the bond component giving rise to the payment. Under section 1232B, each bond component is treated as an obligation issued with original issue discount equal to the excess of the stated redemption price at maturity over the purchase price of the bond component. The interests sold by K are obligations of a type offered to the public. Further, the interests are, in accordance with section 1232B, considered issued after December 31, 1982. Accordingly, the interests are registration-required obligations under § 5f.163-1 (b).

There is a need for immediate guidance with respect to the provisions contained in this Treasury decision. For this reason, it is found impracticable to issue it with notice and public procedure under [subsection \(b\) of section 553 of title 5 of the United States Code](#) or subject to the effective date limitation of subsection (d) of that section.

([Sec. 103 \(j\)](#), [163 \(f\)](#), and [7805 of the Internal Revenue Code](#) of 1954 (96 Stat. 596, [26 U.S.C. 103 \(j\)](#); 96 Stat. 596, [26 U.S.C. 163 \(f\)](#); 68A Stat. 917, [26 U.S.C. 7805](#)), and in section 310 of the Tax Equity and Fiscal Responsibility Act of 1982 (96 Stat. 595).

Roscoe L. Egger, Jr.,

Commissioner of Internal Revenue.

Approved: November 6, 1982.

John E. Chapoton,

Assistant Secretary of the Treasury.

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