

Analysis of the Merchant Card Information Reporting Requirement Contained In the American Housing Rescue and Foreclosure Prevention Act of 2008 (HR3221)

The American Housing Rescue and Foreclosure Prevention Act of 2008 passed the U.S. House of Representatives on July 24, 2008 and the U.S. Senate on July 26, 2008. The legislation is expected to be signed into law before July 31, 2008.

The legislation includes a section which mandates that, beginning in 2011, the acquiring industry must annually report the total amount of credit and debit card transactions of individual merchants to the Internal Revenue Service (IRS) and to the merchants. The same requirement applies to third-party network transactions, such as those via PayPal or Google Checkout, which do not involve payment cards. In certain cases, the reporting entity will have to impose backup withholding on settlements with merchants, in addition to the reporting requirement.

Who is subject to the reporting requirement?

HR3221 refers to those subject to reporting as participating payees, which are defined as merchants or those who accept payments from a third-party settlement organization. In effect, this is any person or organization that accepts credit or debit cards or third-party network transactions. The requirement applies only to those persons or organizations that have more than 200 reportable transactions and more than \$20,000 in reportable transactions in a given year.

Who must report?

The burden of collecting the necessary information and delivering annual reports to the IRS and merchants is on the payment settlement entity.

In most cases involving credit or debit cards, this entity will be the bank or other organization which has the contractual obligation to make payment in settlement of a payment card transaction (i.e., the “merchant acquiring entity”).

In the case of third party network transactions, the entity responsible for reporting is the “central” organization which has the contractual obligation to make payment to payees of the network (i.e., the “third party settlement organization”);.

If reportable transactions contain more than one payee, and the transaction is ultimately settled through an intermediary, the intermediary party is considered the payee of the initial payment settlement entity and is also then considered the payment settlement entity with regard to the final settlement of the transaction with the participating payee (the merchant). In other words, if Company A settles with Company B and Company B then splits that among Companies C and D,

then Company A is the entity responsible for reporting the settlement with Company B, reporting that information to both the IRS and Company B. Company B then becomes the reporting entity for the second part of the transaction, reporting its settlements with Companies C and D to both the IRS and the companies.

Finally, in a case where an electronic payment facilitator or any other third party makes payment on behalf of a settlement entity, the facilitator/third party is responsible for reporting.

What is a reportable transaction?

Reportable transactions include any payment card transaction (credit/debit cards) regardless of whether the card is physically present, and any third party network transaction (ACH, PayPal, Google Checkout, etc.). Each transaction reporting the gross amount paid to a merchant will also have to be tagged with the name, address, and taxpayer ID number (TIN) of the merchant.

When will the reporting requirement take effect?

The requirement goes into effect December 31, 2010, which means that reports will have to be filed for tax years 2011 and beyond.

What happens next?

Many important details are not spelled out specifically in the legislation. The Treasury Department, which includes the IRS, must now draft a set of regulations that will spell out such things as:

- When and how the reporting must take place;
- How to avoid “double counting” certain transactions;
- How the law/regulations will be enforced and by whom; and
- What penalties will apply in cases of noncompliance.

These regulations will take months to develop and will be subject to a public comment process before they take effect.