

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-92682; File No. SR-NSCC-2021-009)

August 17, 2021

Self-Regulatory Organizations; National Securities Clearing Corporation; Order Approving a Proposed Rule Change to Modify the Rules & Procedures of National Securities Clearing Corporation in Connection with the Implementation of Section 1446(f) of the Internal Revenue Code of 1986

On July 14, 2021, National Securities Clearing Corporation (“NSCC”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² proposed rule change SR-NSCC-2021-009 to modify NSCC’s Rules & Procedures (“Rules”)³ in connection with the implementation of Section 1446(f) of the Internal Revenue Code of 1986.⁴ The proposed rule change was published for comment in the Federal Register on July 23, 2021,⁵ and the Commission received no comment letters regarding the changes proposed in the proposed rule change. For the reasons discussed below, the Commission is approving the proposed rule change.

I. DESCRIPTION OF THE PROPOSED RULE CHANGE

A. Background

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ Capitalized terms not defined herein are defined in the Rules, available at http://www.dtcc.com/~media/Files/Downloads/legal/rules/nsc_rules.pdf.

⁴ 26 U.S.C. § 1446(f).

⁵ Securities Exchange Act Release No. 92437 (July 19, 2021), 86 Fed. Reg. 39092 (July 23, 2021) (“Notice of Filing”).

Section 1446(f) generally imposes a ten percent withholding tax on the payment of gross proceeds arising from the sale or other disposition by a non-U.S. person of an interest in a publicly traded partnership (“Section 1446(f) Withholding”) that is engaged in a U.S. trade or business.⁶ A tax withholding obligation is imposed on the buyer of the partnership interest, who is required to remit the withheld tax amount to the U.S. Internal Revenue Service (“IRS”), unless or to the extent an applicable exception applies. The buyer obligated to withhold the ten percent tax is liable for any amount that it underwithheld, plus associated interest and penalties. Further, partnerships that are publicly traded on exchanges (“PTPs”) in respect of transfers that occur on or after January 1, 2022 will be subject to Section 1446(f) Withholding. The U.S. Treasury Department (“Treasury Department”) and the IRS implemented a tax withholding requirement pursuant to Treasury Regulation Section 1.1446(f)-4(a).⁷

Section 1.1446(f)-4(b) provides certain exceptions to 1.1446(f)-4(a). Under one of the exceptions, U.S. clearing organizations, which, under its definition, would include NSCC, are discharged from fulfilling Section 1446(f) Withholding at this time. The Treasury Department and the IRS provided this exception because they understood that there are no nonqualified intermediary Members that participate directly in the net settlement system at a U.S. clearing organization at the present time.⁸

⁶ 26 U.S.C. § 1446(f)(1); Withholding of Tax and Information Reporting With Respect to Interests in Partnerships Engaged in a U.S. Trade or Business, 85 Fed. Reg. 76910 (Nov. 30, 2020) (“Final Regulations”).

⁷ Id.; 26 C.F.R. § 1.1446(f)-4(a).

⁸ Final Regulations, supra note 6, at 76922.

NSCC represents that, all of NSCC’s non-U.S. Members are currently of the types of entities permitted to perform the Section 1446(f) Withholding themselves either because (i) they are the types of entities allowed to perform U.S. tax withholdings pursuant to applicable Treasury Regulations, or (ii) they have entered into the requisite agreements with the IRS that allow them to perform U.S. tax withholdings (commonly known as the Qualified Intermediary Agreements).⁹ NSCC further represents that nearly all such Members have historically accepted the responsibility to perform all U.S. tax withholdings in respect of their NSCC accounts, and it is NSCC’s understanding that they would continue do the same for Section 1446(f) Withholding.¹⁰

B. Proposed Rule Changes

NSCC proposes to amend its Rules to ensure that all NSCC’s FFI Members¹¹ that are Members would accept the responsibility to perform the Section 1446(f) Withholding.¹²

First, NSCC proposes to add new definitions: Section 1446(f), Section 1446(f) Withholding, Section 1446(f) Withholding Agent, Section 1446(f) Withholding Compliance Date, and Tax Certification.¹³ Second, NSCC proposes to revise the FATCA

⁹ Notice of Filing, supra note 5, at 39093.

¹⁰ Id.

¹¹ The term “FFI Member” means any Member or Limited Member that is treated as a non-U.S. entity for U.S. federal income tax purposes. See Rules, supra note 3.

¹² NSCC states that, based on the types of services that NSCC provides to Limited Members, notwithstanding any exception, NSCC would not need to perform Section 1446(f) Withholding with respect to Limited Members’ activities at NSCC. Notice of Filing, supra note 5, at 39093.

¹³ Notice of Filing, supra note 5, at 39093.

compliance rule to add that, generally, each FFI Member that is a Member must agree not to conduct any transaction or activity through NSCC if such FFI Member is not a Section 1446(f) Withholding Agent.¹⁴ Third, NSCC proposes to require FFI Members to be Section 1446(f) Withholding Agents and to notify NSCC when they have reason to know that they are not, or will not be, Section 1446(f) Withholding Agents.¹⁵ Fourth, NSCC proposes to require a Member who is a non-U.S. entity and is not a Section 1446(f) Withholding Agent to not transact through NSCC, and a Member who is a non-U.S. entity to provide Tax Certification to certify that it is FATCA Compliant or a Section 1446(f) Withholding Agent.¹⁶ Fifth, NSCC proposes to make certain other technical changes to its Rules.¹⁷

II. DISCUSSION AND COMMISSION FINDINGS

Section 19(b)(2)(C) of the Act¹⁸ directs the Commission to approve a proposed rule change of a self-regulatory organization if it finds that such proposed rule change is consistent with the requirements of the Act and rules and regulations thereunder applicable to such organization. After carefully considering the proposed rule change, the Commission finds that the proposed rule change is consistent with the requirements

¹⁴ The term “Section 1446(f) Withholding Agent” would mean an FFI Member that is a Member and has certified to NSCC that Section 1446(f) Withholding would not apply to any Gross Credit Balance of such FFI Member by providing to NSCC a Tax Certification (as defined below and in the proposed rule text). Id.

¹⁵ Id.

¹⁶ Notice of Filing, supra note 5, at 39094.

¹⁷ Notice of Filing, supra note 5, at 39093-94.

¹⁸ 15 U.S.C. 78s(b)(2)(C).

of the Act. In particular, the Commission finds that the proposed rule change is consistent with Section 17A(b)(3)(F) of the Act.¹⁹

A. Consistency with Section 17A(b)(3)(F)

Section 17A(b)(3)(F) of the Act requires, in part, that the rules of a clearing agency, such as NSCC, be designed to promote the prompt and accurate clearance and settlement of securities transactions.²⁰

As described above, Section 1446(f) provides NSCC an exception from the obligation to perform Section 1446(f) Withholding at this time. However, if a direct clearing member of a U.S. clearing organization is not a type of entity permitted to perform Section 1446(f) Withholding, the Treasury Department and the IRS will issue proposed guidance that would remove the current exception to require Section 1446(f) Withholding by U.S. clearing organizations, such as NSCC, on that direct clearing member.²¹ If the Treasury Department and the IRS were to revise Section 1446(f) and revoke NSCC's exception, NSCC would be required to clear and settle each transfer of PTP interest on a gross basis in order to perform Section 1446(f) Withholding on such transfer. Given that NSCC currently clears and settles all transactions on a netted basis, NSCC represents that any obligation imposed on NSCC to clear and settle transfers of PTP interest on a gross basis may be disruptive to the efficiency and liquidity of the trading of PTP interests in the capital markets.²²

¹⁹ 15 U.S.C. 78q-1(b)(3)(F).

²⁰ Id.

²¹ Final Regulations, supra note 6, at 76922.

²² Notice of Filing, supra note 5, at 39094.

NSCC is proposing that, unless waived by NSCC, beginning on the Section 1446(f) Withholding Compliance Date, each FFI Member that is a Member would be required to agree not to conduct any transaction or activity through NSCC if such FFI Member is not a Section 1446(f) Withholding Agent. In addition, each FFI Member that is a Member would be required to provide periodic certifications to NSCC regarding its Section 1446(f) Withholding Agent status. Taken together, these membership requirements would help to ensure that all NSCC FFI Members that are Members would accept their responsibility to perform the Section 1446(f) Withholding and to be a Section 1446(f) Withholding Agent.

By ensuring that all NSCC FFI Members that are Members would accept their responsibility to perform the Section 1446(f) Withholding, the Commission believes the current exception for NSCC with respect to Section 1446(f) would continue to operate as intended. Therefore, NSCC would be able to continue to clear and settle all transactions (including transfers of PTP interest) on a netted basis and avoid any potential disruption to the efficiency and liquidity of the trading of PTP interests in the capital market. By avoiding any potential disruption to the efficiency and liquidity of the trading of PTP interest in the capital market, the Commission believes that the proposal would help to promote the prompt and accurate clearance and settlement of transactions, consistent with Section 17A(b)(3)(F) of the Act.²³

The Commission believes the proposal to make technical changes to the Rules is also consistent with Section 17A(b)(3)(F) of the Act. The proposed technical changes to

²³ 15 U.S.C. 78q-1(b)(3)(F).

the Rules would help ensure that the Rules remain accurate and clear to Members. Having accurate and clear Rules would help Members to better understand their rights and obligations regarding NSCC's clearance and settlement services. The Commission believes that when Members better understand their rights and obligations regarding NSCC's clearance and settlement services, they can act in accordance with the Rules. The Commission believes that better enabling Members to comply with the Rules would promote prompt and accurate clearance and settlement of transactions, consistent with Section 17A(b)(3)(F) of the Act.²⁴

III. CONCLUSION

On the basis of the foregoing, the Commission finds that the proposed rule change is consistent with the requirements of the Act and in particular with the requirements of Section 17A of the Act²⁵ and the rules and regulations promulgated thereunder.

²⁴ Id.

²⁵ 15 U.S.C. 78q-1.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act²⁶ that proposed rule change SR-NSCC-2021-009, be, and hereby is, APPROVED.²⁷

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.²⁸

Jill M. Peterson
Assistant Secretary

²⁶ 15 U.S.C. 78s(b)(2).

²⁷ In approving the proposed rule change, the Commission considered the proposals' impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

²⁸ 17 CFR 200.30-3(a)(12).