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ADVISORY

# 1099-OLD vs. 1099-INT

## Interest Income Reporting for Convertible Notes

# THE CORE PROBLEM

Many startups issue convertible promissory notes and struggle with which tax form to use to report interest income — Form 1099-OLD or Form 1099-INT. A maze of tax considerations underpins the proper reporting.



# ORIGINAL ISSUE DISCOUNT (OID) vs. INTEREST INCOME

## What's the Difference?



### OID

- OID is applicable when a debt instrument, such as a convertible note, is issued at a discount from its stated redemption price at maturity. OID accrues annually using the constant yield (economic accrual) method, irrespective of whether there is a payment to the investor during the year. The holder of the instrument includes in income the OID amount during the year. IRC § 1272(a)(1), Treas. Reg. § 1.1272-1, IRC § 1273(a).
- OID is computed as the excess of a debt instrument's stated redemption price at maturity over its issue price. Definitionally, the term "stated redemption price at maturity" does not include any qualified stated interest (QSI) payments. These are payments that are unconditionally payable in cash or in property (other than in debt instruments of the issuer) at least annually at a single fixed rate or qualified variable rate. Note, a debt instrument that only pays a stated interest amount upon maturity or conversion does not get treated as QSI because the payments are not made at least annually and is, thus, treated as OID (assuming that the debt instrument's redemption price at maturity or conversion is over its issue price). IRC § 1273(a)(2); Treas. Reg. § 1.1273-1(b)-(c).

### Interest Income

- Used when interest is actually paid or credited to the investor's account during the tax year as it relates to a convertible note. This includes "qualified stated interest payments" (which as mentioned are amounts excluded from OID treatment). Treas. Reg. § 1.61-7(c), Treas. Reg. § 1.446-2, Treas. Reg. § 1.1273-1(c).
- In contrast to OID, the relevant calculation here is simpler, focusing on the exact amount of stated interest paid or credited during the year.

*Note: Contingent payments beyond the conversion feature on convertible debt may fall under the contingent payment debt instrument (CPDI) rules of Treas.*

*Reg. § 1.1275-4, which are beyond the scope of this briefing.*

# 1099-OID VS. 1099-INT

## What's the Difference?

Understanding the distinction between Form 1099-OID (Original Issue Discount) and Form 1099-INT (Interest Income) is crucial for both issuers and investors, especially in the context of convertible notes.

### Form 1099-OID (Original Issue Discount)

- The issuer is responsible for calculating and reporting the OID for each year the debt instrument is outstanding, based on complex IRS regulations that include various exceptions discussed below, on Form 1099-OID.

### Form 1099-INT (Interest Income)

- The issuer is also responsible for calculating and reporting the interest income for each year and in this case, reports such amount on Form 1099-INT.

The key distinction lies in the timing and nature of the income: **1099-OID is about the accrual of discount over the life of a debt** instrument, reported annually regardless of payment, whereas **1099-INT is about the payment of stated interest**, reported when received or credited. Incorrect classification can lead to compliance issues for both the issuer and the investor.

# TWO KEY EXCEPTIONS TO OID REPORTING

Most convertible notes are analyzed under the standard 1099-OID rules, but two situations create important exceptions: short-term notes, and notes where the computed OID is de minimis. Each can change how interest is reported and when tax is recognized. Interest on notes meeting the **Short-term Exception** do not get reported on 1099-OID and instead [1099-INT](#) when paid subject to certain reporting thresholds. Interest under the **De Minimis OID Rule** is not reported, given that the amount is treated as zero.

## Notes Under One Year (Short-Term Exception)\*

The IRS generally exempts obligations with a fixed maturity of **1 year or less** from OID rules. See IRC § 1272(a)(2)(C).

## De Minimis OID Rule\*\*

If the computed OID is **less than ¼ of 1% of the stated redemption price at maturity** multiplied by the number **of full years from the date of issue to maturity**, then the OID amount is treated as zero. See IRC § 1273(a)(3); Treas. Reg. § 1.1273-1(d).

*\* Note, certain holders of debt that meet the criteria of the Short-Term Exception may still be subject to a current income inclusion. These holders include, for example, a taxpayer using the accrual method of accounting. See IRC § 1281.*

*\*\* Weighted average maturity applies for multi-payment notes (Treas. Reg. § 1.1273-1(d)(3) & (e)(3)).*

# PRACTICAL COMPLIANCE NOTES FROM IRS INSTRUCTIONS ON FORMS 1099-INT AND 1099-OID

Reporting Thresholds	Exempt Recipients — i.e., No Filing Required	Combined Reporting Option	Short-Term OID Goes on 1099-INT, Not 1099-OID
<p>File at <b>\$10</b> or more of interest on corporate debt, including convertible notes.</p> <p>A separate <b>\$600</b> threshold covers certain trade-or-business interest (damages, death benefits, tax-refund interest) — this threshold is not typically relevant to convertible notes.</p>	<p>Neither form is required for payments to corporations, IRAs, HSAs, Archer MSAs, tax-exempt organizations, U.S. agencies, brokers, registered securities dealers, among others.</p>	<p>For most taxable obligations (not specified private activity bonds), the issuer may report both QSI and OID on a single Form 1099-OID: <b>QSI in Box 2</b>, and <b>OID typically in Box 1</b> (the OID accrued for the year).</p>	<p>The IRS instructions direct filers to report OID on obligations with a term of 1 year or less on Form 1099-INT, Box 1, rather than Form 1099-OID (i.e., interest relating to the Short-Term Exception). This applies even though the income is economically OID.</p>

**Source:** Internal Revenue Service (IRS) Instructions for Forms 1099-INT and 1099-OID (Rev. January 2024). See [IRS.gov/Form1099INT](https://www.irs.gov/Form1099INT) and [IRS.gov/Form1099OID](https://www.irs.gov/Form1099OID) for the most current version.

# DEMAND NOTES WITH NO STATED MATURITY

## The Rule

A convertible note payable on demand has **no fixed maturity date**, which would be problematic in computing a yield under the constant-yield method. However, Treas. Reg. § 1.1272-1(d) fixes the yield at the **stated interest rate**, so OID accrues annually at that rate for as long as the note remains outstanding. See Treas. Reg. § 1.1272-1(d).

## Illustration: Reg. § 1.1272-1(j), Example 10

**Facts:** V buys W's note at original issue for \$100,000. The debt instrument calls for an accrual of 9% interest which compounds annually. The debt instrument is redeemable at any time at V's option for \$100,000 plus accrued interest. V uses annual accrual periods to accrue OID on the debt instrument.

**Result:** Under Treas. Reg. § 1.1272-1(d), the yield is 9% compounded annually. If the note is not redeemed in the tax year, **\$9,000 of OID is allocable to that year.**

**Bottom Line:** *A demand convertible note is not "open-ended" for tax — Treas. Reg. § 1.1272-1(d) fixes yield at the stated rate, so interest accrues (and must be reported) each year it remains outstanding.*



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