American Institute of CPAs
1455 Pennsylvania Avenue, NW
Washington, DC 20004-1081

August 5, 2013

Mr. Daniel I. Werfel
Principal Deputy Commissioner
Internal Revenue Service
1111 Constitution Avenue, NW
Washington, DC 20224

The Honorable William J. Wilkins
Chief Counsel
Internal Revenue Service
1111 Constitution Avenue, NW
Washington, DC 20224

Ms. Lisa Zarlenga
Tax Legislative Counsel
Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, DC 20220

Mr. Curtis G. Wilson
Associate Chief Counsel for
Passthroughs and Special Industries
Internal Revenue Service
1111 Constitution Avenue, NW
Washington, DC 20224

Re: Comments on REG-130507-11 relating to guidance under section 1411, as added by the Health Care and Education Reconciliation Act of 2010, regarding net investment income tax as relevant to international entities (controlled foreign corporations (CFCs) and passive foreign investment corporations (PFICs)) (12/5/2012)

Dear Messrs. Werfel, Wilkins, and Wilson, and Ms. Zarlenga:

The American Institute of Certified Public Accountants (AICPA) submits the comments below in response to the above mentioned proposed regulations published on December 5, 2012, regarding guidance on the new section 1411 net investment income (NII) tax as relevant to international entities. Section 1411 imposes a tax on unearned income on investments of certain individuals, estates, and trusts, whose income is above the statutory threshold amounts.

The AICPA is the world's largest member association representing the accounting profession, with nearly 386,000 members in 128 countries and a 125-year heritage of serving the public interest. Our members advise clients on federal, state and international tax matters and prepare income and other tax returns for millions of Americans. Our members provide services to individuals, not-for-profit organizations, small and medium-sized businesses, as well as America's largest businesses.

The AICPA has the following recommendations for the final section 1411 regulations with respect to international tax entities:

1. We agree with, and support, the American Bar Association (ABA) Section of Taxation comments, Part X, concerning Prop. Reg. § 1.1411-10 regarding

controlled foreign corporations and passive foreign investment companies, dated April 5, 2013 ("ABA's recommendations"), that recommend assessing the section 1411 tax [at the same time as Chapter 1, Normal Taxes and Surtaxes[1],] or imposing a look-through regime to determine section 1411 implications as if the U.S. shareholder or qualified electing fund (QEF) shareholder earned the income directly.

2. Should the Department of Treasury ("Treasury") and the Internal Revenue Service (IRS) deem it necessary to provide an option for taxation at the time of repatriation, rather than at the time income is earned for purposes of Chapter 1, we recommend that the final guidance reverse the default and elective methods under Prop. Reg. § 1.1411-10. Under the proposed regulations as currently drafted, section 1411 tax is imposed on amounts included in gross income under sections 951(a) and 1293(a) ("Subpart F" and QEF) when income is repatriated, rather than when the income is taxed for Chapter 1. There is elective treatment under the proposed regulations to impose section 1411 tax when the income is taxed for Chapter 1. The default ordering under the proposed regulations creates significant taxpayer recordkeeping burdens, basis differences between Chapter 1 and section 1411, and adds an enormous amount of complexity for the average taxpayer. Instead, we recommend that the default rule impose section 1411 tax at the same time the income is taxed for Chapter 1, with elective treatment to impose section 1411 tax on repatriation.

   The proposed regulations as currently drafted create a significant administrative burden for both taxpayers and the IRS. Under the default rule contained in the proposed regulations, taxpayers will need to determine when income is taxed under section 1411, which adds to the already significant burdens imposed under the Subpart F and PFIC regimes. Furthermore, the default rules under the proposed regulations as currently drafted create basis differences that will require tracking when a CFC or QEF investment is disposed. IRS personnel will need to be trained under the proposed default regime. It is likely that the default regime in the proposed regulations will result in a significant compliance error rate, increase pressure on the IRS exam function, and result in a greater number of audit cases referred to either appeals, National Taxpayer Advocate, or both.

   In addition to burdensome tracking needs, special consideration is needed for income taxed pursuant section 956, a component of Subpart F, which is tantamount to the payment of a dividend. The timing of income recognition under

[1] Chapter 1, Normal Taxes and Surtaxes, encompasses Sections 1 through 1400U-3 of the Internal Revenue Code and provides the framework for determining taxable income and the amount of income tax owed.

section 956 frequently approximates actual cash flow, or in the case of a guarantee or pledge, creates a deemed repatriation of foreign earnings. Prop. Reg. § 1.1411-10(c)(2) does not take into account that section 956 already aligns the timing of taxation with the repatriation of earnings. Should Treasury choose not to conform the timing of taxation under section 1411 to the timing of taxation under section 956, the proposed regulations under section 1411 could have the impact of deferring taxation under section 1411 to years subsequent to an actual repatriation of earnings.

Should final guidance not adopt the ABA's recommendations, we bring to your attention a potential omission in the proposed regulations. The proposed regulations generally impose section 1411 tax at the time of cash flow. The final regulations should also consider income inclusions under section 1296, the mark-to-market regime for passive foreign investment companies. Mark-to-market reporting recognizes income for Chapter 1 on an annual basis rather than at the time of repatriation. [Under the proposed guidance, it appears that income resulting from section 1296 is subject to Chapter 1 and section 1411 at the same time. While we agree that this is a simplifying convention, it is a departure from the general approach of the proposed regulations and imposes section 1411 tax annually based on market value fluctuations and not at the time of an actual dividend.]

3. Should the final guidance not adopt the ABA's recommendations, we recommend that the first direct or indirect U.S. owner of the controlled foreign corporation or QEF make all elections. Under Prop. Reg. § 1.1411-10(d)(2) and (3), section 1411 elections are made by the partners and shareholders when the CFC or QEF is held by a domestic partnership or an S corporation. This requirement vastly increases the complexity of the compliance for partnerships, S corporations, their respective owners and for the IRS exam personnel. The proposed regulation puts domestic partnerships and S corporations in a situation where they will be required to provide information to their partners and shareholders under both the default and the elective regimes, significantly increasing the compliance burden for the partnership or S corporation. On exam, IRS personnel will need to investigate at the partner or shareholder level, rather than streamlining exam efforts at the entity level. We recommend that any elections under the proposed regulations be made by the direct owner or the first U.S. investor or the first U.S. shareholder with indirect ownership if the CFC or QEF investment is held through a chain of foreign entities. If the regulations are revised as we suggest, generally, the taxpayer with primary responsibility for filing Form 5471, Information Return of U.S. Persons With Respect To Certain Foreign Corporations, or the PFIC shareholder eligible to make a section 1295 election to treat a PFIC as a QEF will

be responsible for making the elections under section 1411. By requiring elections to be made by the direct U.S. owner, or first U.S. owner in a chain of indirect ownership, the taxpayer making the section 1411 elections is the taxpayer who is in the best position to have knowledge related to the operations of the investment and track the consequences of any elections made.

4. If the final regulations do not reflect the "look through" approach outlined in the ABA's recommendations, we recommend that the final regulations align the treatment of Subpart F and PFIC income for purposes of Chapter 1 and section 1411. The IRS and courts have held that Subpart F and PFIC inclusions are "other income" and not dividend income. Prop. Reg. § 1.1411-10, treating Subpart F and PFIC income as dividends, is inconsistent with Notice 2004-70, 2004-2 CB 724, and Rodriquez, 137 TC 14, 12/7/2011. For further discussion on the IRS authority to treat the early inclusions as dividends for purposes of section 1411, see the New York State Bar Association Tax Section comments on section 1411, Section IV, dated May 22, 2013.

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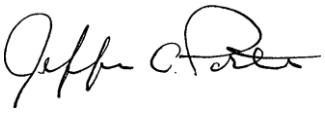
We welcome the opportunity to discuss these comments or to answer any questions that you may have.

I can be reached at (304) 522-2553, or jporter@portercpa.com; or you may contact Christine Ballard, Chair, AICPA International Tax Technical Resource Panel, at (408) 369-3738 or christine.ballard@mossadams.com; or Kristin Esposito, AICPA Technical Manager, at (202) 434-9241, or kesposito@aicpa.org.

Sincerely,



Jeffrey A. Porter, CPA
Chair, Tax Executive Committee

cc: Ms. Melissa Liquerman, Chief Branch 2, Office of the Associate Chief Counsel for Passthroughs and Special Industries, Internal Revenue Service
Ms. Donna M. Young, Deputy Associate Chief Counsel (Passthroughs and Special Industries), Internal Revenue Service

Mr. David Kirk, Attorney, Office of the Associate Chief Counsel for Passthroughs and Special Industries, Internal Revenue Service
Ms. Adrienne Mikolasheck, IRS Office of Chief Counsel for Passthroughs and Special Industries, Internal Revenue Service