June 17, 2003

Mr. Glenn Kirkland  
Internal Revenue Service, Room 6411  
1111 Constitution Avenue, N.W.  
Washington, D.C. 20224  
  
RE: Comments on Form 3520-A and Form 3520  
  
Dear Mr. Kirkland:  
  
[4] The American Institute of Certified Public Accountants (AICPA) is writing in response to the Service's April 18, 2003, request for comments on Form 3520-A, "Annual Information Return of Foreign Trust with a U.S. Owner." Although not specifically requested, we have also commented on Form 3520, "Annual Return To Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts" because it is closely linked to Form 3520-A. The AICPA is the national, professional organization of certified public accountants comprised of more than 350,000 members. Our members advise clients on federal, state, and international tax matters, and prepare income and other tax returns for millions of Americans. They provide services to individuals, not-for-profit organizations, small and medium-sized businesses, as well as America's largest businesses.

[5] In our attached comments, we urge the IRS to: (1) exempt Canadian Registered Retirement Savings Plans (RRSPs) and Registered Education Savings Plans (RESPs) from the Form 3520-A filing requirements, and exempt their U.S. owners from the Form 3520 filing requirements for reporting transfers to RRSPs and RESPs; (2) develop a Form 3520 worksheet tailored to foreign trust distributions as a substitute for using Form 4970; (3) change the due date for Form 3520-A to April 15, with extensions; and (4) adopt a uniform method for filing prior years' Forms 3520 and 3520-A to facilitate compliance.

[6] Thank you for the opportunity to comment on these forms. Please feel free to contact me at (202) 414-1705, or Robert.zarzar@us.pwcglobal.com; Rick Gimbert, Chair of the Form 3520 Task Force, at (404) 220-1849, or rgimbert@deloitte.com; or Eileen Sherr, AICPA Technical Manager, at (202) 434-9256, or esherr@aicpa.org, to discuss any of our comments further. Thank you for taking the time to consider this matter.

Sincerely,  
  
/s/  
  
Robert A. Zarzar  
Chair, Tax Executive Committee

cc:  
Willard W. Yates, IRS Office of the Associate Chief Counsel  
(International)  
Amanda A. Ehrlich, IRS Office of Associate Chief Counsel  
(International)  
Barbara Angus, U.S. Department of Treasury International Tax Counsel

AICPA COMMENTS ON FORM 3520-A AND FORM 3520

A. Canadian RRSPs and RESPs Should Not Be Subject to Filing Forms 3520-A and 3520

1. Canadian Registered Retirement Savings Plans

[7] Currently, any Canadian Registered Retirement Savings Plan (RRSP) with a U.S. owner, which is treated as a foreign trust, must file a Form 3520-A. However, no Form 3520-A is required if the U.S. beneficiary files an election under Rev. Proc. 2002-23, 2002-15 I.R.B. (March 26, 2002), to defer U.S. income tax until the income is distributed.

[8] Any U.S. citizen or resident who makes a transfer to an RRSP must also file Form 3520 to report the transfer. However, no Form 3520 is required if, at the time of transfer, the RRSP qualifies for exemption under the U.S.-Canada income tax treaty, and this reliance is disclosed on the U.S. person's income tax return. (See Notice 97-34, 1997-1 C.B. 422.).

[9] In Notice 2003-25, 2003-18 I.R.B. (May 2, 2003), Treasury and the IRS acknowledge that many U.S. persons with interests in RRSPs -- as well as RRSP custodians -- are unfamiliar with the requirements for filing Forms 3520 and 3520-A. Therefore, the Notice delays the imposition of these filing requirements on RRSPs until the 2002 tax year, with an automatic due date extension for 2002 filings to August 15, 2003. The Notice also affirms that RRSPs have no filing obligation for any year in which the plan beneficiary elects under Rev. Proc. 2002-23.

[10] It is unclear whether an RRSP meets the reg. section 301.7701-4 definition of a "trust," as an arrangement in which trustees take title to property to protect or conserve it for beneficiaries. If an RRSP does not rise to the level of a "trust," it may merely be a custodial, nominee, or agency relationship -- similar to an IRA -- and Forms 3520 and 3520-A would not be required, regardless of whether the elections described above are made.

[11] Notice 97-34 indicates that the section 6048(a) reporting requirements exist to ensure that U.S. transferors comply with section 679. Under the section 679 grantor trust rules, all foreign trust income is reportable by the grantor. Currently, all income earned in an RRSP with a U.S. owner or beneficiary is either currently taxed in the U.S. or deferred until distribution. The only way to defer U.S. income tax is by making an election that requires disclosure to be valid.

[12] Therefore, Form 3520 is not necessary to ensure that U.S. RRSP transferors comply with section 679. U.S. transferors must either currently report income or comply with the election procedures discussed above.

[13] Likewise, Canadian RRSP custodians should not be required to file Form 3520-A. Currently, because RRSPs are not required to file Form 3520-A if their U.S. beneficiaries file the election described in Rev. Proc. 2002-23, many are exempt from the filing requirement. However, the RRSP custodians have difficulty ascertaining with any degree of certainty whether an election was or was not filed by the U.S. beneficiary.

2. Canadian Registered Education Savings Plans

[14] Canadian Registered Education Savings Plans are similar to U.S. Section 529 educational savings accounts arrangements in which a donor (subscriber) enters into a trust agreement with a provider and agrees to make contributions to fund a beneficiary's post-secondary education costs. RESPs will often constitute "foreign trusts" for U.S. tax purposes, and in most cases, RESPs with a U.S. subscriber will be treated as grantor trusts.

[15] Most U.S.-resident Canadians and U.S. citizens and residents with RESPs are not aware that (1) RESPs are treated differently from RRSPs when it comes to informational reporting; and (2) RESPs often are "foreign trusts," requiring special information returns. This is undoubtedly leading to missed filing deadlines.

[16] RESP income is taxed to U.S. subscriber citizens and residents currently and must be reported and disclosed on their Form 1040, U.S. Individual Income Tax Return. Transfers to an RESP are also reportable as gifts on Form 709, U.S. Gift (and Generation-Skipping Transfer) Tax Return. U.S. subscribers of RESPs cannot avoid the information reporting requirements by taking advantage of a treaty exemption, as they can with RRSPs.

[17] Like the parallel retirement savings vehicle, RESPs are generally maintained by Canadian financial institutions and have many subscribers, each of whom may change their U.S. income tax status from year to year. It would be impossible for the financial institution maintaining the RESP to track the movement of all subscribers on an annual basis to determine whether a given RESP account has a U.S.-resident owner.

[18] Transfers to and ownership of RESPs should be exempt from the Forms 3520 and 3520-A filing requirements. U.S. owners are already required to disclose RESP income and transfers on their U.S. income and gift tax returns; therefore, requiring additional disclosures on Forms 3520 and 3520-A is duplicative. Disclosure on Forms 1040 and 709 should be sufficient disclosure for RESPs.

[19] Serious consideration should be given to treating RESPs and RRSPs alike and affording treaty protection to both. This can be accomplished by a Treasury interpretation that both plans fall under either Article XVIII, para. 7, or Article XXI, para. 1, of the U.S.- Canada treaty. Under this interpretation, RESP subscribers could elect income recognition deferral using the same procedures as RRSPs.

[20] By essentially treating RESPs as equivalent to U.S. Section 529 plans, parents could save for their children's college education no matter on which side of the border they happen to be residing. The amounts involved are relatively modest; and this tactic makes good policy sense. Canadian RESPs have existed for over 10 years, and the United Kingdom is considering a similar savings plan. To date, neither country has attempted to tax U.S. Section 529 plans for U.S. citizens who temporarily reside in their countries. Giving this consideration to two of our largest trading partners and closest allies would encourage continued preferential treatment of Section 529 plans held by U.S. citizens living in Canada and in the U.K.

B. Using Form 4970 to Compute Tax on Accumulation Distributions for Form 3520

[21] Form 3520, Part III, Line 49, requires that Form 4970 be used to compute the tax on total accumulation distributions. However, Form 4970 is not geared to distributions from a foreign trust. The Form 4970 instructions direct beneficiaries of foreign trusts to Form 3520 to compute their tax. Form 3520 indicates that Form 4970 should only be used as a worksheet.

[22] Completing Form 4970 for distributions from a foreign trust is difficult. For example, Form 4970 does not use the terminology of foreign trusts nor does it account for the "gross up" of distributions for foreign taxes paid or credited under sections 666-667. it also references Form 1041, Schedule J, which is not generally filed by foreign trusts.

[23] Instead of the Form 4970, a new worksheet specifically tailored to the foreign trust rules should be developed as part of Form 3520 for distributions from foreign trusts. This would save preparation time and minimize confusion and errors.

[24] We believe that the treaty relief afforded RRSPs also exempts RRSP distributions from the accumulation tax on Form 4970. The instructions to the Form should make this clear.

C. Due Date for Form 3520-A

[25] The Form 3520-A instructions and Notice 97-24, 1997-1 C.B. 409, indicate that Form 3520-A is due by the 15th day of the third month following the close of the trust's tax year (March 15 for calendar year trusts). However, under reg. section 404.6048-1, which pre-dates the current version of section 6048, Form 3520-A was due on the 15th day of the fourth month (April 15) following the close of the tax year covered by the return.

[26] Although the current March 15 requirement ensures that the U.S. owner or beneficiary has time to review and include the foreign trust's Form 3520-A information on their Form 3520, it can cause unnecessary confusion. In many cases, the deadline is inadvertently missed. Often, the same preparer is charged with completing both Form 3520-A and Form 3520; therefore, sufficient information is available to the U.S. owner or beneficiary to complete Form 3520 correctly and timely by its April 15 due date.

[27] In a case where Forms 3520-A and 3520 are being filed for the first time, many taxpayers assume that all their U.S. tax returns are due on April 15, and that extensions are available to file returns after that date. Currently, if the taxpayer engages an income tax return preparer, but does not provide the preparer any information about the existence of a foreign trust until after March 15, Form 3520-A cannot be timely filed, and there is no extension available. An April 15 due date for the Form 3520-A, which could be extended in the same manner as Form 3520 (by requesting an extension for the individual's income tax return), would alleviate this problem.

[28] Alternatively, a relief provision targeted to first-year late filings would alleviate many Form 3520-A due date concerns. For example, if a first-year Form 3520-A is filed by April 15 or the extended due date of the related Form 1040, it should be treated as timely filed. For subsequent years, Forms 3520-A would need to be filed by March 15.

[29] We would strongly urge that an April 15 due date be adopted in all cases of Form 3520 and 3520-A to avoid confusion and simplify administration.

D. Uniform Method for Filing Prior Year Forms 3520 and/or 3520- A

[30] In our experience, most non-U.S. persons establish foreign trusts or are named as beneficiaries of foreign trusts many years before deciding to seek U.S. residency. Many of these owners and beneficiaries become U.S. residents for short periods of time (such as for temporary work assignments), and are often unaware that they must file an information return for the foreign trust in addition to filing a U.S. income tax return. Also, U.S. citizens living abroad either do not seek U.S. tax advice or receive incorrect or incomplete advice when they establish foreign trusts. Although these taxpayers include the foreign trust's income on their individual income tax returns, they may not file Forms 3520 or 3520-A.

[31] Establishing a uniform method for voluntary filing of all prior years' information returns as one package would encourage these taxpayers to come into compliance with the foreign trust reporting rules and avoid unnecessary paperwork and correspondence and minimize penalties. Guidance on what, if any, penalties may be waived for this kind of voluntary compliance would also be helpful. A well-publicized amnesty period might achieve the same results, highlighting the rules and encouraging more taxpayers to comply. Specific guidance would also be welcome as to how many prior years' Form 3520-A must be filed if a taxpayer is in arrears for several years and is coming forward voluntarily, especially if no distributions have been made (in the case of a foreign nongrantor trust), or in cases where the trust is a foreign grantor trust with a U.S. owner and U.S. tax has been paid on all trust income during the U.S. person's residency period. Also, guidance as to where and to whose attention such prior years' forms must be sent would be helpful. These changes would encourage taxpayers who are not currently in compliance to come into compliance with the foreign trust reporting rules.

E. Conclusions

[32] Exempt Canadian RRSPs and RESPs from the Form 3520-A filing requirements, and exempt their U.S. owners from the Form 3520 filing requirements for reporting transfers to RRSPs and RESPs.

Develop a Form 3520 worksheet tailored to foreign trust distributions as a substitute for using Form 4970 to make Form 3520 calculations.

Change the due date of Form 3520-A to April 15, and allow extensions, particularly for the first filing year. An extension of the Form 1040 should extend the due date for Form 3520-A.

Establish a uniform method for filing prior years' Forms 3520 and 3520-A to facilitate compliance.

American Chamber of Commerce in Canada  
  
Proposal For Simplified Reporting Regime For Canadian RRSPs and  
RRIFs in Accordance With Notice 2003-25

[33] Notice 2003-25 outlines the current reporting requirements and filing deadlines for U.S. beneficiaries of Canadian Eligible Plans1. Treasury and the IRS have indicated that they are interested in simplifying the current reporting procedures and possibly coordinating them with the election available under Rev. Proc. 2002-23.

[34] As more fully explained in Appendix 1, Notice 2003-25 requires a US beneficiary of an eligible plan to file form 3520 upon receiving a distribution from the eligible plan. Transfers to an eligible plan and income accrued in that plan do not have to be reported on form 3520 or form 3520-A, they can be reported as described in Appendix 1.

Concerns with the Current Reporting Requirements

[35] The preparation of form 3520 will place a substantial reporting burden on the beneficiary of an RRSP or RRIF ("the plan") from which a distribution is made. In order to avoid harsh tax treatment of the distribution, the beneficiary must obtain a Foreign Grantor Trust Beneficiary Statement from the trustee of the plan. This also places a reporting burden on the custodian of the plan, the Canadian financial institution. The custodian may not have the means to assist with providing this statement.

[36] The foreign trust must also produce records and testimony when requested or summoned by the IRS. This is another onerous responsibility placed on the custodian. Failure to produce the records may cause the IRS to redetermine the tax consequences of the beneficiary's distributions from the trust. Alternatively, the trust can appoint a US agent. A Canadian custodian may have legal difficulties complying with an IRS request for information and/or appointing a US agent.

[37] Failure to timely file form 3520 as a result of the lack of information or co-operation from the custodian may result in significant monetary penalties for the U.S. beneficiary.

Proposed Alternative to the Current Reporting Requirements for Distributions from a RRSP or RRIF

[38] In order to simplify the compliance burden on the beneficiary and the custodian/trustee, while meeting the needs of the IRS and Treasury, we propose that the following information be accepted in lieu of filing form 3520.

[39] 1. In addition to the current information requirement for electing under Rev. Proc. 2002-23, the beneficiary would be required to attach to their timely filed return (including extensions) a statement that includes the following information:

The amount of the distribution; and

The nature/type of the distribution.

2. Attachment of additional official documents to the timely filed return.

Standard Year-end Statement from the custodian. This statement is provided to beneficiaries in the normal course of the custodian's business. This statement would provide the following information:

The plan balance at the end of the year. Since the prior year's return would include a statement with the end of year balance, this would effectively provide a beginning balance for the current year.

The type as well as the amount of marketable securities held in the plan at the end of the year.

Tax reporting slips issued by the custodian for all plan distributions. (See attached Schedule A for the types of distributions and the corresponding Canadian reporting requirement).

T4RSP (see attached copy)

T4RIF (see attached copy)

NR4 (see attached copy)

Conclusion

[40] The proposed alternative provides the information that would otherwise be reported on form 3520, such as the date, type and amount (FMV) of the distribution as well as information on the trust and its beneficiary.

[41] The alternate information provided is controlled by the Canadian government and therefore should be a reliable substitute for form 3520.

[42] The proposed alternative simplifies the reporting procedure for both the U.S. beneficiary as well as the custodian. The custodian already produces the alternate information to be provided each year, therefore the reporting requirement is not changed in any way.

[43] The proposed alternative should provide the IRS and Treasury with substantially the same tax information required on Form 3520, while simplifying the compliance burden on the beneficiary and custodian. Therefore, the alternative should meet the IRS and Treasury guidelines for a simplified reporting regime for RRSPs and RRIFs while coordinating the reporting with the election described in Rev. Proc. 2002-23.

FOOTNOTE TO FULL TEXT

1An eligible plan as referred to in Notice 2003-25 is defined in section 3 of Revenue Procedure 2002-23 as a Canadian registered retirement savings plan ("RRSP"), a Canadian registered retirement income fund ("RRIF"), a registered pension plan, or a deferred profit sharing plan.

END OF FOOTNOTE TO FULL TEXT

Appendix 1: Background Summary

Form 3520-A: Annual Information Return of Foreign Trust With a U.S. Owner

Each U.S. owner of a foreign trust (i.e. RRSP or RRIF) is responsible for ensuring that the foreign trust files this annual return. Form 3520-A sets forth a full and complete accounting of all trust activities, trust operations and other relevant information. Form 3520-A is due by the 15th day of the third month after the end of the trust's tax year (or March 15th for a Canadian RRSP).

The U.S. owner is also required to ensure that the trust provides required annual statements to all of its U.S. owners (Foreign Grantor Trust Owner Statement) and U.S. beneficiaries (Foreign Grantor Trust Beneficiary Statement).

The penalty for failure to file form 3520-A is equal to 5% of the gross value of the trust's assets that are owned by the U.S. person.

Exception: Per Notice 2003-25, an eligible plan (including Canadian RRSP's, Registered Retirement Income Fund's, Registered Pension Plan's and Deferred Profit Sharing Plan's) is relieved of any obligation to file form 3520-A for any year in which the beneficiary has elected under Rev. Proc. 2002-23 to defer the taxation of income accrued in but not distributed by the plan. Paragraph four of Rev. Proc. 2002-23 states that the election is valid if the beneficiary attaches to their timely filed return a statement that includes the following information:

A statement that the taxpayer is claiming the benefit of Article XVIII(7) of the Convention under this revenue procedure;

The name if [sic] the trustee of the plan and the plan account number, if any; and

The balance in the plan at the beginning of the current year.

A copy of this statement is attached to each timely filed income tax return for each year subsequent to the current year, until the tax year in which a final distribution is made from the plan.

Form 3520: Annual Return to Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts

A U.S. person that receives a distribution from a foreign trust is required to file form 3520. Form 3520 provides information about the owner(s) of the trust and the trust itself. The form also provides information regarding the distributions from the trust during the year as well as calculating the amount of ordinary income to be included on the beneficiary's income tax return. Form 3520 is due on the date that the federal income tax return is due.

A US person who receives a distribution from a foreign trust must complete "schedule A" of Part III of form 3520, unless the US person receives a beneficiary statement from the foreign trust. Schedule A computes the entire distribution as either current year ordinary income or as accumulation distribution, which results in harsh US taxation.

The penalty for failure to report a distribution on form 3520 is 35% of the gross amount of the distribution.

Notice 97-34 provides that no reporting is required for transfers if the trust qualifies at the time of the transfer for treaty benefits under the U.S.-Canada income tax treaty. Reliance on the treaty in any tax year must be disclosed on Form 8833, Treaty- Based Return Position Disclosure under section 6114 or 7701(b).

        Schedule A: Distributions from an RRSP or RRIF

\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_  
Description of Distribution                       Information  
                                                  Slip and box  
                                                  number  
\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_  
Withdrawal from an RRSP                           T4RSP - Box 22  
  
Beneficiaries can withdraw amounts from  
their RRSP before it starts to pay a  
retirement income.  
  
Beneficiaries can withdraw unused                 T4RSP - Box 20  
contributions made to an RRSP based  
on an approved Form T3012A, Tax  
Deduction Waiver on the Refund of Unused  
RRSP Contributions Made in XXXX  
  
Annuity payments from an RRSP  
  
When an RRSP matures, beneficiaries can  
draw an annuity from that RRSP.                   T4RSP - Box 16  
  
In addition to receiving a retirement             No slip issued -  
income out of the RRSP, beneficiaries             transfer would  
can also choose to transfer the property          appear on annual  
to a RRIF or buy an eligible annuity.             RRSP statement.  
  
Commutation payments from an RRSP  
  
A commutation payment is a fixed or               T4RSP - Box 22  
single lump-sum payment from an RRSP  
annuity that is equal to the current  
value of all or part of the future  
annuity payments from the plan.  
  
Minimum amount from a RRIF  
  
Starting in the year after the year a             T4RIF - Box 16  
RRIF is established, beneficiaries have  
to be paid a yearly minimum amount.  
  
Excess amount from a RRIF  
  
In any year, beneficiaries can be paid            T4RIF - Box 24  
more than the minimum amount for that             (included in Box 16)  
year. Amounts paid from a RRIF in a year  
that is more than the  minimum amount  
for that year are called excess amounts.  
Under certain circumstances,  
beneficiaries can directly transfer the  
excess amount from a RRIF to an RRSP.  
  
Amounts deemed received on deregistration  
of an RRSP or a RRIF  
  
If in the year, the RRSP or RRIF was              T4RSP - Box 26  
changed and it no longer satisfies the            Or  
rules under which it was registered, it           T4RIF - Box 20  
is no longer an RRSP or a RRIF. It is  
now an amended plan or fund. In such a  
case, the beneficiary is considered to  
have received an amount that equals the  
fair market value of all the property  
the plan or fund held at the time it  
ceased being an RRSP or RRIF.  
  
Other income and deductions from an RRSP  
or a RRIF  
  
This applies if in the tax year an RRSP           T4RSP - Box 28  
or RRIF trust acquired or disposed of a           Or  
non-qualified investment, trust property          T4RIF - Box 22  
was used as security for a loan, trust  
property was sold for an amount less  
than its fair market value, or the trust  
acquired property for an amount more  
than its fair market value.  
  
Deceased Beneficiary  
  
Transfer to the surviving spouse or               T4RSP - Box 18  
common-law partner (named as beneficiary          Or  
in the RRSP contract)                             T4RIF - Box 16  
If, before the end of the year following  
the year of death of a beneficiary, all  
of the property the RRSP/RRIF held is  
paid to the deceased beneficiary's spouse  
or common-law partner, that payment can be  
transferred to an RRSP or RRIF tax-free.  
  
For All Other Situations  
  
The FMV of the property held in the               T4RSP - Box 34  
RRSP/RREF is distributed to the                   Or  
deceased's estate.                                T4RIF - Box 18  
  
Lifelong Learning Plan  
  
Beneficiaries can withdrawal up to                T4RSP - Box 25  
$20,000 tax-free from an RRSP if the  
participant meets the requirements of  
the lifelong learning plan. This  
distribution must be paid back over a  
prescribed number of years.  
  
Home Buyers' Plan  
  
Beneficiaries can withdrawal up to                T4RSP - Box 27  
$20,000 tax-free from an RRSP if the  
participant meets the requirements of  
the home buyers' plan. This distribution  
must be paid back over a prescribed  
number of years.  
  
Breakdown of a marriage  
  
Distributions from an RRSP or RRIF for            T4RSP - Box 35  
the purpose of dividing marital assets            Or  
are transferred tax-free to the                   T4RIF - Box 35  
receiving spouse or common law partner.  
  
Transfers between Registered Plans  
  
Beneficiaries can make tax free                   No slip issued -  
transfers between registered plans.               transfer would  
                                                  appear on annual  
                                                  RRSP statement.  
  
Statement of Amounts Paid or Credited to          NR4 - Box 16  
Nonresidents of Canada

Statements T4RIF, T4RSP, NR4  
  
[Forms omitted]  
  
AIM Statement  
  
[Form omitted]  
  
\* \* \* \* \*

June 5, 2003

The Honorable Pamela F. Olson  
Acting Assistant Secretary (Tax Policy)  
Department of the Treasury  
1500 Pennsylvania Avenue, NW  
Room 3120  
Washington, DC 20220  
  
The Honorable B. John Williams  
Chief Counsel  
Internal Revenue Service  
1111 Constitution Avenue, NW  
Room 3026  
Washington, DC 20224  
  
Re: Suggestions for the 2003-2004 IRS/Treasury Priority Guidance Plan

Dear Ms. Olson and Mr. Williams:

The AICPA is pleased to offer our suggestions regarding the 2003-2004 IRS/Treasury Priority Guidance Plan, which were prepared by the AICPA Tax Division's committees, technical resource panels, and task forces, and approved by our Tax Executive Committee.

The attached suggestions are presented by name of the AICPA working group that developed them, and are not prioritized within each heading. For your convenience, we have listed the contact information-for both the chair and the AICPA staff liaison for each working group. Please feel free to contact any of these individuals with your specific questions or concerns.

In addition to our specific, listed suggestions, the AICPA again encourages Treasury and the IRS to continue to pursue tax simplification. We recognize -- and very much appreciate -- recent steps you have taken, such as (1) harmonizing transfer pricing documentation (Notice 2002-77); (2) clarifying changes to the personal residence sale regulations; and (3) promoting the objective of clarity and transparency in the regulations under sections 6011, 6111, and 6112.

Although you must balance competing interests and concerns when drafting guidance, we urge you to consider the following as part of the process:

Use the simplest approach to accomplish a policy goal;

Provide safe-harbor alternatives;

Offer clear and consistent definitions;

Use horizontal drafting (a rule placed in one Code section should apply in all other Code sections) to the greatest extent possible;

Build on existing business and industry-standard record- keeping practices;

Provide a balance between simple general rules and more complex detailed rules; and

Match a rule's complexity to the sophistication of the targeted taxpayers.

The recent passage of the Jobs and Growth Tax Relief Reconciliation Act of 2003 and your immediate need for feedback for next year's plan, have not yet allowed our committees and TRPs to formally identify the guidance needs arising out of the Act. However, our Individual Taxation Technical Resource Panel has identified one area of particular need and we have listed that information under their heading.

Finally, please let us know if there are other types of information which we can offer to facilitate the business plan process. We would be happy to accommodate your needs.

Please feel free to contact me at (202) 414-1705, or robert.zarzar@pwc.com; or Edward S. Karl, AICPA Director at (202) 434-9228, or ekarl@aicpa.org, if we can assist you in any way.

Sincerely,  
  
/s/  
  
Robert A. Zarzar  
Chair  
Tax Executive Committee  
AICPA  
Washington, DC

Enclosure

AICPA Tax Division  
Comments on the 2003 - 2004 IRS/Treasury Priority Guidance Plan  
June 5, 2003

Consolidated Tax Issues Task Force (Kevin A. Duvall, Chair, (713) 750-8366, kevin.duvall@ey.com; or George L. White, AICPA Technical Manager, (202) 434-9268, gwhite@aicpa.org)

1. Guidance is needed on the application of the active business test in section 355(b) to consolidated groups.

2. Guidance is needed on the application of sections 382(l)(5) and (6) to consolidated groups.

Corporations and Shareholders Taxation Technical Resource Panel (Mark A. Schneider, Chair, (301) 634-4983, gmschneider@bdo.com; or George L. White, AICPA Staff Liaison, (202) 434-9268, gwhite@aicpa.org)

1. Guidance is needed regarding the application of section 382, including the amount of depreciation or amortization subject to limitation under section 382(h)(2)(B).

2. Guidance is needed regarding the scope of and exceptions to section 382(l)(1), including the application of such rules to merger transactions and multiple ownership changes.

3. Guidance is needed regarding the "business expansion" issue under section 355(b), particularly with respect to stock or asset acquisitions.

4. Guidance is needed to implement section 382(h)(9) outside of consolidation.

Employee Benefits Taxation Technical Resource Panel (Carol E. Zurcher, Chair, (407) 599-5900, czurcher@tbzwcpa.com; or Lisa A. Winton, AICPA Staff Liaison, (202) 434-9234, lwinton@aicpa.org)

1. Guidance is needed on the use of electronic technology for delivery of safe harbor 401(k) plan notices; qualified joint and survivor annuity/qualified pre-retirement survivor annuity (QJSA/QPSA) notices and waivers; spousal consents under section 417; and ERISA 204(h) notices.

2. Guidance is needed on various matters under section 414(m), including: what constitutes management functions for 414(m)(5) purposes; what are the results when a member of an affiliated service group is also part of a separate controlled group; and how the shareholder/partner requirement of 414(m)(2) applies in the context of a tax-exempt service organization.

3. Guidance is needed on 401(k)/(m) testing for mergers and acquisitions occurring during a plan year; application of the "same desk" rule to non-corporate plan sponsors; and clarification of the successor employer and severance of employment concepts.

Individual Taxation Technical Resource Panel (Patricia Thompson, Chair, (401) 831-0200, patt@pgco.com; or James S. Clark, AICPA Technical Manager, (202) 434-9229, jclark@aicpa.org)

1. Guidance is needed on what constitutes "substantial administrative or management functions" for the purpose of allowing the home office deduction.

2. Guidance is needed regarding related travel deductions under section 162, particularly with respect to the Soliman case, the Walker case, Rev. Rul. 90-23, Rev. Rul. 94-24, and Notice 93-12.

3. Finalize guidance under section 121 regarding unforeseen circumstances related to the sale of residence when health issues or employment changes are involved.

4. Guidance is needed on the interrelationship of sections 121 and 469 when a rental property that is converted into a personal residence is disposed of without recognizing gain.

5. Guidance is needed under section 1(h), as amended by section 302 of the Jobs and Growth Tax Relief Reconciliation Act of 2003, particularly with regard to holding periods and qualified foreign corporations.

6. Regulations are needed under section 163(h) to follow through on Notice 88-74. In particular, debt used to acquire an interest in a residence incident to divorce should be treated as acquisition debt for interest expense purposes.

7. Regulations are needed regarding interests on interspousal notes issued incident to a divorce, especially in light of a number of Tax Court cases. (See Seymour v. Commissioner, 109 T.C. No. 14 (1997); Gibbs v. Commissioner, T.C. Memo 1997-196; and Armacost v. Commissioner, T.C. Memo 1998- 150.)

8. Guidance is needed on using deferred vacation home losses to offset gains on the sale of the vacation property under section 280A. Section 280A limits the current deductibility of expenses associated with vacation home rentals; excess deductions may be carried over to succeeding years. Guidance must resolve the question of whether gain from the sale of the vacation property is considered gross rental income that would allow the excess deductions to be taken in the year of the sale.

9. Foreign tax credit amounts of less than $300 and $600 for regular tax purposes may be claimed without filing Form 1116. This treatment should also be extended to apply for AMT purposes.

10. Proposed section 529 regulations would permit corporations, partnerships, trusts, and other entities to contribute to Tuition Saving Plans or purchase tuition credits on behalf of a designated beneficiary. In addition, the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) clarified that non-individuals could contribute to a Coverdell Education Savings Plan. Guidance is needed on the income tax treatment for a donor entity, a beneficiary, or a donor entity's employee related to the beneficiary. This guidance should determine whether the contributions would be treated as a gift by the non- individual entity as it would be if given by an individual. If there is an income issue, guidance must also address: (a) whether the income should be recognized at contribution or distribution; and (b) whether the income should be treated as wages subject to social security and Medicare taxes.

11. Guidance is needed on the interaction of the regular and alternative minimum taxes on the disposition of "incentive stock option" stock which results in losses for AMT purposes and capital gain for regular tax purposes. (A basis adjustment on disposition would be a more appropriate result than an AMT capital loss carryforward.)

International Taxation Technical Resource Panel (Andrew M. Mattson, Chair, (408) 369-2566, andy@mohlernixon.com; or Eileen R. Sherr, AICPA Technical Manager, (202) 434-9256, esherr@aicpa.org)

1. Guidance is needed in the following areas related to Subpart F/Deferral:

Regulations to implement section 304(b)(6) (regarding the avoidance of multiple inclusions) and address whether previously taxed income is a corporate-level or shareholder-level attribute in (a) the section 959 successor-in-interest regulations and (b) the reserved portions of the proposed section 367(b) regulations.

Update the existing PFIC regulations (in particular, the section 1295 regulations) to take into account the enactment of section 1297(e), which eliminates the overlap of the PFIC and Subpart F regimes under certain circumstances.

More complete and definitive guidance under the PFIC provisions, in particular with respect to determining a corporation's PFIC status.

Finalize the proposed section 898 regulations on conforming year-ends of certain foreign corporations to the year-ends of their U.S. shareholders.

Regulations under section 954(h), providing guidance on the subpart F exception for active financial services income.

2. Guidance is needed in the following areas related to inbound transactions:

Regulations under section 1446, relating to withholding on effectively connected income of a partnership.

Finalize the proposed section 163(j) "earnings stripping" regulations (in particular, clarifying the definition of "guaranty") and provide a definition of "interest equivalents" (reserved in the proposed regulations).

Issue guidance on the application of section 864(c)(6) and (7) and on the treatment of effectively connected income (or losses allocable to effectively connected income) as an attribute under section 381.

3. Guidance is needed in the following areas related to outbound transactions:

Clarify the scope of the anti-abuse rule under the final section 367(e) regulations with examples of when it may apply and of when it would not apply.

Finalize the section 367(a) and 367(d) temporary regulations.

Issue new proposed section 987 regulations, relating to foreign currency translation gains and losses with respect to branch transactions (taking into account public comments with respect to Notice 2000-20). [Note: the AICPA will be submitting comments on this.]

Issue proposed and temporary section 367(a)(5) regulations and reconsider Example 4 in reg. section 1.367(b)-4(b).

Issue guidance under section 1248(f)(2) dealing with certain distributions of stock of foreign corporations to domestic corporations.

4. Guidance is needed regarding foreign tax credits, in particular:

Amend the regulations under section 853 to eliminate separate company reporting of the foreign tax credit for mutual funds and conform the regulations to Code changes made more than 20 years ago. In addition, modify Form 1116, Foreign Tax Credit (Individual, Estate, or Trust) to indicate that distributions from regulated investment companies are exempt from per-country reporting. (We believe this is non-controversial and should be easy to implement. See February 26, 2003, AICPA letter to IRS International Director, Carol Dunahoo, with proposed marked-up regulatory language, at <https://www.cpa2biz.com/ResourceCenters/Tax/> International/FTC\_rptg\_mutual\_funds.htm)

Guidance is needed under section 904(d) to provide "look- through" treatment for royalties from related foreign persons that are not controlled foreign corporations.

The section 904(f) regulations relating to overall foreign losses should be revised to replace the outdated 1987 regulations and Notice 89-3.

5. Guidance is needed in the following other areas:

Issue guidance under section 6011 clarifying that filing a Form 8873 relating to the Extraterritorial Income Exclusion constitutes adequate disclosure for reportable transactions for tax shelter disclosure regulations purposes. (Rev. Proc. 2003-25 could be amended to include this as a transaction with a significant book-tax difference that would not be subject to tax shelter reporting requirements.)

Revise the section 1503 regulations to clarify how dual consolidated losses of separate units should be calculated, In particular, provide guidance with respect to the meaning of the term "attributable."

Clarify and relax the double reporting rules under the section 1461 regulations and the treaty-based reporting requirements under section 6114.

Provide guidance on the treatment of triggered gain recognition agreements (GRA) under section 367 when there is gain under the GRA but no gain at the time of the trigger.

Provide guidance on the treatment of global service contracts as foreign base company services income.

Clarify the rules that apply to the basis of property brought into U.S. tax jurisdiction.

Issue guidance retaining and expanding the "cost" safe harbor rule for transfer pricing of inter-company services. (See reg. section 1.482-2(b)(7).)

Issue guidance under section 6048 clarifying various exemptions from the Form 3520 and Form 3520A reporting for situations where the treaty statement (outlined in Rev. Proc. 2002-23) takes the place of Form 8833 for reporting purposes. [Note: the AICPA will be submitting comments on this.]

IRS Practice and Procedures Committee (James A. Dougherty, Chair (202) 879-4937, jdougherty@deloitte.com; or Benson S. Goldstein, AICPA Technical Manager, (202) 434-9279, bgoldstein@aicpa.org)

1. On February 28, 2003, Treasury released final regulations designed to address "abusive tax avoidance transactions" and disclosure, registration, and list-keeping under sections 6011, 6111, and 6112. Treasury should continue to update the guidance involving these regulations, including the six categories of reportable transactions described in the regulations.

2. Guidance is needed to resolve the uncertainty remaining about the specifics of interest-netting computations and ensure that all taxpayers are treated consistently. In particular, guidance should define "same taxpayer" and address the discrepancies that result between applying section 6621(d) versus section 6402.

3. The current estimated tax rules under sections 6654 and 6655 are antiquated, vague, and leave many issues unanswered. Appropriate administrative action should be taken to make the estimated tax rules more consistent with current business and financial practice, and legislation should be enacted where needed.

4. The Form 1040 Checkbox Initiative, introduced in 2000, enables taxpayers to authorize their paid return preparers to work with the IRS to resolve any processing-related problems with respect to their returns. Granting this limited authority to third parties to discuss factual return issues without obtaining a more formal power of attorney has reduced the time, frustration, and costs incurred by taxpayers, the IRS, and tax practitioners in resolving minor problems. However, under current administrative guidelines, the third party's authority to act on a taxpayer's behalf is only effective through the filing deadline (i.e., April 15) of the particular return involved. Administrative action should be taken to (a) extend the duration of this grant of authority to a date significantly past April 15; and (b) expand the types of forms for which this grant of authority is available.

5. Guidance is needed on the information reporting requirements for payments made following an employee's death. There are inconsistencies between the Form 1099 instructions and Rev. Rul. 86-109, the current authority on reporting death benefits and compensation paid after death. Guidance is also needed on reporting other post-death payments, such as those from nonqualified deferred compensation and stock option exercise.

6. The IRS is considering implementation of a program to pre- certify eligibility for the earned income tax credit (EIC). Should this program be implemented, the IRS should provide timely guidance regarding the scope and administration of the program.

7. The IRS has released proposed regulations regarding the payment of a "user fee" by taxpayers who file an Offer in Compromise. If the IRS issues final regulations authorizing a user fee, further guidance will be necessary about exempting low-income and certain other taxpayers.

Partnership Taxation Technical Resource Panel (Elizabeth Ann Case, Chair, (202) 414-1628, elizabeth.case@us.pwcglobal.com; or Marc A. Hyman, AICPA Technical Manager, (202) 434-9231, mhyman@aicpa.org)

1. Guidance is needed to address the revaluation of partnership assets where the assets were either contributed to the partnership or previously revalued by the partnership. This guidance should include (a) how the multiple layers under section 704(c) are maintained; (b) the impact on minimum gain calculations under section 704(b); and (c) the impact on nonrecourse debt allocations under section 752.

2. Proposed (and final) regulations are needed for compensatory and non-compensatory partnership options and convertible instruments. Proposed guidance should consider whether an additional book-up event is allowed under reg. section 1.704- 1(b)(2)(iv)(f), thereby allowing a revaluation of partnership capital upon admission of a service partner and avoiding a capital shift. Without amending the revaluation provision, a service partner may fall outside safe harbor provisions of Rev. Proc. 201-43. Therefore, we suggest expanding the current regulation to permit a revaluation of partnership assets upon admission of a service partner.

3. Clarification is needed under section 42 regarding what items (other than impact fees) are included in the eligible low income housing credit basis, such as tap fees, offsite costs, construction loan fees and bond costs.

4.Regulations are needed to implement TRA of 1997 (P.L. 105-34) section 1246(a) and (b) that amended section 706(c)(2)(A). The regulations should address allocation of partnership income or loss between (a) a transferor and transferee of a gifted partnership interest and (b) a decedent and the decedent's estate or other beneficiary for the year of death, and under section 753 with regard to the determination of income in respect of a decedent for the year of death.

5. Final regulations are needed under reg. section 301.7701- 3(d) regarding the special rules for the relevance of foreign eligible entities.

6. Guidance is needed on the application of sections 704(c)(1)(B) and 737 in the context of Rev. Rul. 99-6 transactions.

S Corporation Taxation Technical Resource Panel (Kenneth N. Orbach, Chair, (561) 297-2779, orbach@fau.edu; or Marc A. Hyman, AICPA Technical Manager, (202) 434-9231, mhyman@aicpa.org)

1. Guidance is needed under section 409(p) regarding the definition of synthetic equity as related to S corporations. This project could be combined with the planned employee retirement benefits project to issue guidance on prohibited allocations of securities in S corporations. (See item 37, page 5 of the Third Quarterly, Update of the 2002-2003 Priority Guidance Plan.)

2. Clarification is needed on what rules apply when an S corporation makes a QSub election for an insolvent subsidiary.

3 . Clarification is needed about who should sign the final return of a corporation that is the target of a section 338(h)(10) acquisition by an S corporation.

4. Clarification is needed on whether an S corporation can simultaneously make some pro rata distributions according to current stock ownership and other distributions that meet the varying interest rule of reg. section 1.1361-1(l)(2)(iv) without creating a second class of stock.

5. Guidance is needed about when, if ever, holders of bank director's shares are treated as shareholders of the S corporation for purposes of section 1361, and if so, when those shares constitute a second class of stock.

Tax Accounting Technical Resource Panel (Robert A. Kilinskis, Chair, (312) 242-9855, rkilinskis@deloitte.com; or George L. White, AICPA Technical Manager, (202) 434-9268, gwhite@aicpa.org)

1. Finalize guidance under sections 162 and 263 regarding deduction and capitalization of expenditures.

2. Finalize guidance under section 451 regarding the treatment of advance payments.

3. Guidance is needed under the dollar-value last-in, first-out (LIFO) inventory method for taxpayers that define LIFO items based on components of cost.

4. Guidance is needed on whether a change to the Inventory Price Index Computation method of reg. section 1.472-8(e)(3) includes an item definition change.

5. Provide guidance that allows a cost-of-goods-sold offset anytime advanced payments are included in income before goods under an agreement are delivered.

6. Reconsider Rev. Ruls. 71-234 and 77-480 to allow use of the rolling average cost of inventory to the extent it approximates actual cost.

7. Reconsider Rev. Rul. 70-564 to allow the carryover of LIFO layers following section 351 and 721 transactions provided the new entity chooses to use a LIFO method.

8. Provide guidance on the terms and conditions for method changes made pursuant to section 381, including whether LIFO changes should be made on a cut-off basis.

9. Provide guidance that section 481(a) and audit protection apply for changes to or from the percentage-of-completion method under section 460.

10. Provide procedural guidance for taxpayers that changed revenue recognition for financial reporting purposes under SAB 101 and continued historical book/tax conformity, i.e., tax revenue followed book revenue before and after the SAB 101 change.

Tax Exempt Organizations Resource Panel (Jody Blazek, Chair (713) 523-5739, jody@bvcpa.com; or Lisa A. Winton, AICPA Staff Liaison, (202) 434-9234, lwinton@aicpa.org)

1. Guidance is needed under section 512 to determine how the rules on UBIT, lobbying expenditures and political intervention apply to Internet activities of tax-exempt organizations.

2. Additional guidance is needed under section 337 regarding the formation of joint ventures between exempt and non-exempt organizations, including the impact on exempt status and unrelated business income in order to transfer assets between them.

3. Guidance is needed under section 512 for a simplified and uniform method of cost allocation for large organizations to use for UBIT activities.

4. Guidance is needed to establish voluntary compliance program methods that allow exempt organizations to correct improper positions taken with regard to IRS forms and procedures.

5. Guidance is needed under section 501(m) on what constitutes commercial-type insurance with respect to HMOs serving a special-needs population.

Trust, Estate and Gift Tax Technical Resource Panel (Evelyn M. Capassakis, Chair (646) 394-2363, evelyn.capassakis@us.pwc.com, or Eileen R. Sherr, AICPA Technical Manager, (202) 434-9256, esherr@aicpa.org)

1. Guidance is needed on the disclosure rules on listed transactions as applied to estates and trusts under sections 6011, 6111 and 6112 for tax shelters and reportable transactions.

2. Guidance and revenue procedures are needed regarding the Patriot Charitable Trust created under the Homeland Security Act of 2002.

3. Guidance is needed on implementing the generation skipping transfer (GST) tax under the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA).

4. Guidance is needed on the application of the two-percent floor on certain miscellaneous itemized deductions of an estate or trust under section 67(a) where there are a series of tiered trusts, and each trust distributes excess deductions on termination (i.e., subtrust funding) to another trust, thereby potentially subjecting the same dollars to multiple reductions for the two-percent floor.

5. Guidance is needed on calculating taxes paid for gift tax purposes. Based on EGTRRA, it appears that (a) gift tax calculations use the applicable exclusion amount and the applicable credit amount; and (b) gift tax actually paid on prior transfers disappears from the calculation until the taxpayer dies and receives a credit on the estate tax return for the tax paid on previous transfers.

6. Guidance is needed on how the GST applies to grandfathered domestic trusts that become foreign trusts. This issue may be analogous to a GST-grandfathered trust which migrates from one state to another; thus, similar rules and safe harbors should be considered.

7. Guidance is needed under section 642(c) on whether income in respect of a decedent (IRD) that is reported and used in calculating the estate's charitable deduction on the estate tax return should be treated as "gross income" and allowed as a charitable deduction on the estate's fiduciary income tax return when the IRD is paid to a charitable organization pursuant to the governing instrument.

8. Under section 644, update Rev. Procs. 90-30, 90-31, 90-32, and 90-33 (which provide sample safe harbor language/forms for charitable remainder trusts) to take into account the significant changes in the law over the past decade.

9. Finalize regulations under section 643 regarding state law definition of income for trust purposes.

10. Guidance is needed under section 664 regarding capital gains for charitable remainder trusts.

11. Finalize regulations under section 671 regarding reporting requirements for widely held fixed investment trusts.

12. Guidance is needed under sections 671 and 2036 regarding tax reimbursement provisions in grantor trusts.

13. Finalize regulations under sections 2055 and 2522 based on the Boeshore decision.

14. Guidance is needed under section 2519 regarding net gifts.

15. Guidance is needed under section 2642 regarding issues relating to the generation skipping transfer tax (GSTT) exemption.