

[TEXT OF THE FATCA COMMENT LETTER SUBMITTED BY  
THE AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS]

March 28, 2011

The Honorable Douglas H. Shulman  
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

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

Submitted electronically via [Notice.Comments@irs.counsel.treas.gov](mailto:Notice.Comments@irs.counsel.treas.gov) (NOT-112379-10)

RE: Request for Guidance on Foreign Trusts as Part of the HIRE Act

Dear Messrs. Shulman, Wilkins, and Wilson:

The American Institute of Certified Public Accountants (AICPA) requests that guidance be issued on the numerous foreign trust issues arising from the application of the foreign account tax compliance act (FATCA) provisions included in the Hiring Incentives to Restore Employment (HIRE) Act of 2010, P.L. 111-147, enacted March 18, 2010. In response to IRS Ann. 2010-22 (as modified by IRS Ann. 2010-34, IRB 685), our comments identify various issues and suggestions for guidance in implementing the HIRE Act with regard to foreign trusts.

The AICPA is the national professional organization of certified public accountants comprised of approximately 370,000 members. 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.

**EXECUTIVE SUMMARY**

Our comments address various issues related to foreign trusts under the HIRE Act. Specifically, we address issues pertaining to the following:

- Treating the Use of Foreign Trust Property as a Distribution
- Clarifications with Respect to Foreign Trusts that are Treated as Having a U.S. Beneficiary
- Disclosure of Information with Respect to Foreign Financial Assets

## **DISCUSSION AND ANALYSIS:**

### **1. Treating the Use of Foreign Trust Property as a Distribution**

Section 533 of the HIRE Act amended *Internal Revenue Code (Code) section 643(i)* to provide that if a trustee permits a U.S. person to use trust property without payment to the trust for the fair market value of the use of such property, such use will be treated as a distribution. Such deemed distributions will create an administrative burden on trustees and beneficiaries, who will have to track the usage of trust property by each individual and assign a fair value to such usage, in some cases for property that is not generally rented and, therefore, for which a rental value cannot be easily determined.

Under the rules of foreign trust taxation (i.e. Code *section 643*), such a distribution would be reportable by the U.S person, but would not necessarily be subject to U.S. taxation. The U.S person's taxation related to the deemed distribution would depend on whether the trust had earned income in the current year or accumulated income in prior years. n1

#### ***Guidance Requested***

We request that guidance be issued with respect to section 533 of the HIRE Act, as follows:

##### **A. Clarify Who is to Determine Fair Value**

Section 533 of the HIRE Act provides that if a trustee permits a U.S. person to use trust property without paying fair market value for the use of such property, such use will be treated as a distribution. Revised Code *section 643(i)* currently does not address whose responsibility it is to determine the fair value of property usage. We suggest that the IRS clarify whether the trustee or the U.S. person utilizing the property is responsible for determining the fair value of the property usage.

When an actual distribution is made by a foreign trust to a U.S. person, the U.S. person may either use information provided on a foreign trust beneficiary statement or may use a permitted “default” method<sup>n2</sup> to complete Form 3520 and compute the tax, if any, on the distribution. In either case, the U.S. person will have information regarding the amount he or she received from the foreign trust during the year. In the case of a deemed distribution based on the fair value of property usage, clarification is needed regarding who is responsible for determining the fair value of such usage. We suggest that the beneficiary should not be responsible for determining fair market value of the usage of trust property, and that such responsibility should rest with the trustee.

#### **B. Limiting Rule to Usage of Property for Which a Rental Market Exists**

In order to ease what will be a substantial administrative burden on trustees and beneficiaries, we suggest that future guidance related to *section 533* of the HIRE Act should identify specific categories of property for which a ready rental market exists, and that the deemed distribution rules only apply to the use of such property. Although it should be possible to obtain an appraisal of fair market rent for certain types of property, such as real property, without a large amount of effort, it may be more difficult to determine fair rental value for other types of property. Therefore, we recommend that the specific types of property to which these rules will apply be enumerated.

It would further ease the administrative burden if certain “safe harbor” provisions are included in future guidance. For example, we suggest that when furnished real property owned by a foreign trust is utilized by a U.S. person, the fair rental value should be determined for the furnished property as a whole if there is a rental market for furnished housing in the area (such as beach houses or ski houses), rather than requiring that fair rental value be broken down between the contents of a house and

the house itself.

### **C. Determining Fair Market Value**

If the suggestions in Subpart A and B, above, are not adopted, guidance is requested on the standards to be used to determine the fair market value of the use of foreign trust property by a U.S. person.

### **D. Limiting Rule to Usage of Property over a De Minimis Amount**

Similar to the HIRE Act *section 511* and new Code *section 6038D* authority for Treasury regulations n3 , we suggest Treasury has the regulatory and administrative authority to provide appropriate exceptions. We further suggest that Treasury should provide that a de minimis fair market value amount and/or a minimal number of days of usage be permitted without causing a deemed distribution from a foreign trust to a U.S. person.

### **E. Simultaneous Use of Trust Property by More Than One U.S. Person**

We request guidance as to how the uncompensated use of trust property should be reported when more than one U.S. person simultaneously uses the same property. For example, foreign trust (FT) owns a vacation home. FT has two discretionary beneficiaries who are U.S. persons (Father and Son). Father and Son take a two-week vacation together and stay in the vacation home. We request guidance on the reporting requirements and income tax effects for both Father and Son under these circumstances.

We suggest that Treasury clarify that the fair rental value of property usage can only be subject to informational reporting and income taxation (if any) as a result of a deemed distribution once; i.e., if the fair rental value of the vacation home in the above example is \$ 5,000, and the two U.S. beneficiaries use the property simultaneously, the total reportable amount with respect to such usage should not exceed \$ 5,000. The \$ 5,000 amount should either be reported by

one person or divided among all the U.S. persons using the property. We suggest that guidance be issued as to whether and under what circumstances one beneficiary may be allowed to file and thus relieve the other beneficiaries of the need to file, or whether in all cases each beneficiary must report a pro-rata share of the value of the deemed distribution (and on what basis the pro-rata shares are determined; such as the amount of days spent using the property, etc.)

#### **F. Guests of Beneficiary**

Guidance is requested as to the reporting requirements and income tax effects of a U.S. beneficiary who has access to trust property and allows another individual to use such property. For example, if Father, a U.S. person, is a discretionary beneficiary of Foreign Trust, and Father permits Son, also a U.S. person but not a discretionary beneficiary of the Trust, to use property owned by the Trust (either with or without Father simultaneously using the property), guidance is requested as to the reporting requirements and income tax effects of such usage to Father as well as to Son.

## **2. Clarifications With Respect to Foreign Trusts that are Treated as Having a U.S. Beneficiary**

*Sections 531 and 532 of the HIRE Act amended Code section 679(c), re-designated Code section 679(d) as subsection (e) and added a new subsection (d). These statutory changes expand the scope of foreign trusts treated as having a U.S. beneficiary to include situations where:*

- A U.S. beneficiary's interest in the trust is contingent on a future event;
- Any person has the discretion to make distributions from the trust (including by power of appointment), unless the terms of the trust specifically identify the class of persons to whom such distributions may be made and none of those persons are U.S. persons during the taxable year;
- Agreements or understandings regarding the accumulation or payment of income or corpus to a U.S. person exist

between the foreign trust and a U.S. person who directly or indirectly transferred property to the foreign trust; and

- The foreign trust received transfers from a U.S. person (directly or indirectly), unless such person demonstrates to the IRS that the trust does not have any U.S. beneficiaries.

### ***Guidance Requested***

We request that guidance be issued to clarify the application of *sections 531 and 532* of the HIRE Act, as follows:

#### **A. U.S. Person with Power of Appointment over a Foreign Trust**

If a foreign trust permits the extension of a limited power of appointment in favor of a U.S. person, and each person in whose favor the power may be exercised is not a U.S. person, the IRS should confirm that the trust will not be treated as having a U.S. beneficiary in that particular tax year.

We note that in the case of a foreign trust with a limited power of appointment, it would be possible for the status of the trust to change from year to year based on a change in U.S. tax residency or U.S. citizenship status of an individual in whose favor a limited power of appointment may be exercised, if such individual is treated as a beneficiary.

In the case of a limited power of appointment, guidance is requested regarding what level of inquiry and documentation will be required in order to determine the residency status of the class of persons in whose favor a power may be extended. Guidance is needed for situations in which a trust precludes U.S. persons from being beneficiaries but the trust provides for a general power of appointment or limited power of appointment that is not specifically limited to beneficiaries.

#### **B. Agreements between a U.S. Transferor and a Foreign Trust Treated as Terms of the Trust**

Guidance is requested regarding the type of agreements or understandings that will be included in this category. Specifically, if a U.S. transferor to a foreign trust requests that the trustee consider certain parameters before making distributions, but such request is not binding on the trustee, clarification is requested as to whether such a non-binding request would be included.

### **C. Demonstrating That a Foreign Trust Does Not have U.S. Beneficiaries**

Guidance is requested as to how a U.S. transferor to a foreign trust may demonstrate that the trust does not have U.S. beneficiaries. A beneficiary's U.S. tax residency status can change from year to year, and there is no current method or guidance available for a U.S. transferor to rely upon in order to determine the U.S. tax residency status of trust beneficiaries. We request that guidance be issued explaining what information and/or documentation a U.S. transferor must obtain in order to demonstrate whether a foreign trust has U.S. beneficiaries.

We suggest that guidance include a "safe harbor" provision which would enable a U.S. transferor to take the position that a foreign trust does not have any U.S. beneficiaries if the trust document provides that the trustees may not:

1. accumulate or pay trust corpus or income to or for the benefit, either directly or indirectly, of a U.S. person;
2. if the trust is terminated at any time during the tax year, no part of the trust income or corpus could be paid to or for the benefit of, either directly or indirectly, a U.S. person; and
3. the trust may not be amended to add U.S. persons as beneficiaries.

### **3. Disclosure of Information with Respect to Foreign Financial Assets**

New Code section 6038D, as created by section 511 of the HIRE Act, requires disclosure of specified foreign financial assets by U.S. persons if the aggregate value of all such assets exceeds \$ 50,000. The definition of foreign financial asset includes any interest in a foreign entity, as defined in new *section 1473* (as added by the Act). New Code section 1473(5), as created by section 501 of the HIRE Act, provides that a foreign entity means any entity that is not a U.S. person as defined in new Code *section 1473* (as added by the HIRE Act).

***Guidance Requested***

Guidance is requested as to whether a beneficiary of a foreign trust is required to report their interest in such trust as an interest in a foreign entity under new Code *section 1473(5)*. If so, guidance is requested as to how a beneficiary of a trust is to value their interest in such trust for purposes of determining whether the \$ 50,000 reporting threshold is met.

The AICPA submitted comments to the Service on November 19, 2010 and April 30, 2010, regarding suggested changes to the reporting requirements for the Report on Foreign Bank and Financial Accounts (FBAR). For consistency and policy reasons, we suggest similar guidance and recommendations for this \$ 50,000 income tax reporting requirement. To the greatest extent possible, there should be common definitions, filing requirements and other details on both the relevant guidance and regulations that are anticipated to be issued by the IRS, especially as it relates to the HIRE Act and foreign trusts, and the final regulations issued by FinCEN regarding FBAR.

We note that this letter focuses on the foreign trust issues associated with the HIRE Act. The HIRE Act also made many changes to the withholding area (i.e., the “FATCA” provisions), which the AICPA plans to address in a separate letter.

\* \* \* \* \*

We thank you for the opportunity to present our comments and welcome the opportunity to discuss these issues further with you or others at the IRS. Please feel free to contact F. Gordon Spoor, Chair of the AICPA Trust, Estate, and Gift Tax Technical Resource Panel, at [fgs@spoorcpa.com](mailto:fgs@spoorcpa.com) or (727) 343-7166; Karen Brodsky, Chair of the AICPA Foreign Trust Tax Task Force, at [kbrodsky@deloitte.com](mailto:kbrodsky@deloitte.com), or (212) 436-3025; or Eileen Sherr, AICPA Senior Technical Manager, at [esherr@aicpa.org](mailto:esherr@aicpa.org), or (202) 434-9256 to discuss the above comments or if you require any additional information.

Sincerely,

Patricia A. Thompson,  
CPA Chair,  
AICPA Tax Executive Committee  
Washington, DC

cc:

The Honorable Michael Mundaca,  
Assistant Secretary (Tax Policy),  
Treasury Department

Ms. Catherine Hughes,  
Attorney Advisor,  
Treasury Department

Mr. James F. Hogan,  
Chief, Branch 4, CC:PSI:4,  
Passthroughs and Special Industries - Branch 4,  
IRS

Ms. Kathryn T. Holman ,  
Office of Associate Chief Counsel (International)

Ms. M. Grace Fleeman,  
Senior Technical Reviewer,  
International - Branch 1,  
IRS

Mr. Willard Yates,  
Attorney-Advisor,  
International - Branch 1,  
IRS

Ms. Lara Banjanin,  
Attorney-Advisor, International - Branch 1,  
IRS

**FOOTNOTES:**

n1

We note that the Society of Trust and Estate Practitioners (STEP) submitted a letter dated December 30, 2010 to the IRS that assumes an income recognition event irrespective of whether the trust has income. However, the statute does not require such an income recognition event.

n2

The “default” method is used when a U.S. beneficiary does not receive enough information from the trustee of a foreign trust regarding a distribution to determine the character and taxation of the distribution under U.S. tax rules. The default method may also be used at the election of the beneficiary. The default method essentially uses an averaging technique to determine the portion of a distribution that is to be treated as attributable to current year income and prior year income, in order to compute tax and possibly an interest charge on the distribution.

n3

(h) REGULATIONS. ~ The Secretary shall prescribe such regulations or other guidance as may be necessary or appropriate to carry out the purposes of this section, including regulations or other guidance which provide appropriate exceptions from the application of this section. . . .”