new york state society of
NYSSCPA
certified public accountants

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May 3, 2012

M. Grace Fleeman Senior Technical Reviewer, Branch 1
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c/o Joseph S. Henderson

Sent electronically, via e-mail: joseph.s.henderson@irscounsel.treas.gov
And via facsimile to both, by request: 202-622-4408

Re: Comments on RRSP–Late Elections

The New York State Society of Certified Public Accountants, representing more than 28,000 CPAs in public practice, industry, government and education, submits the following comments to you regarding RRSP late elections. The NYSSCPA thanks the Internal Revenue Service for accepting its comments.

The NYSSCPA's International Taxation Committee deliberated the topic of RRSP late elections, and drafted the attached comments. If you would like additional discussion with us, please contact Melissa Gillespie, Chair of the International Taxation Committee, at (212) 880-2620, or Ernest J. Markezin, NYSSCPA staff, at (212) 719-8303.

Sincerely,
N Y S S C P A
Richard E. Piluso
President

Attachment

NEW YORK STATE SOCIETY OF

CERTIFIED PUBLIC ACCOUNTANTS

COMMENTS ON RRSP–LATE ELECTIONS

May 3, 2012

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New York State Society of Certified Public Accountants

Comments on RRSP–Late Elections

The New York State Society of Certified Public Accountants respectfully submits these comments, and has identified the reporting of foreign retirement plans, and, in particular, Canadian registered retirement savings plans and Canadian registered retirement funds (together referred to as "RRSPs"), held by Unites States (U.S.) persons, as a significant issue that deserves additional attention from Treasury and the Internal Revenue Service ("IRS").

We understand that you might have the matter under consideration, and believe that U.S. treatment of RRSPs is a matter to which we can lend some clarity.

We have prepared this letter to share our views in relation to these matters.

RRSP–Late Elections

Pursuant to Paragraph 7 of Article XVIII, Pensions and Annuities of the U.S.-Canada Tax Treaty (the "Treaty"), a U.S. person is permitted to make an election to defer the recognition of any income derived by an RRSP in which he or she has a beneficial interest provided that an appropriate election is made. Specifically, Paragraph 7 of Article XVIII, Pensions and Annuities of the Treaty states:

> A natural person who is a citizen or resident of a Contracting State and a beneficiary of a trust, company, organization or other arrangement that is a resident of the other Contracting State, generally exempt from income taxation in that other State and operated exclusively to provide pension or employee benefits may elect to defer taxation in the first-mentioned State, subject to rules established by the competent authority of that State, with respect to any income accrued in the plan but not distributed by the plan, until such time as and to the extent that a distribution is made from the plan or any plan substituted therefor.

This paragraph specifically grants the competent authority, *i.e.*, Secretary of the Treasury or his delegate, the authority to establish rules for the making of a valid election. To facilitate the making of the election, the IRS has issued Form 8891, *U.S. Information Return for Beneficiaries of Certain Canadian Registered Retirement Plans.* In addition to making such an election, Form 8891 can be used to report contributions to Canadian RRSPs, the undistributed earnings of RRSPs, and the distributions from RRSPs.

Generally, Form 8891 would be required to be completed by any U.S. person in the year he or she acquires an interest in an RRSP and by any Canadian person with an interest in an RRSP for the first year that he or she becomes a U.S. person. If a taxpayer fails to make an election in the tax return for the first year that the election would be relevant to the taxpayer, there is a significant cost and burden associated with having the election made effective from the time it first became relevant.

Specifically, it is necessary for a taxpayer to apply for a private letter ruling, which would involve engaging tax professionals to draft the ruling request and significant fees payable to the IRS. This financial burden is often significant relative to the income of an RRSP.

While we acknowledge that ignorance is no excuse, there is a general lack of familiarity with Form 8891 by both taxpayers and tax advisers alike. Many taxpayers do not disclose such financial interests to their tax return preparer; nor do tax return preparers request such information from a taxpayer because each is unaware of the need to report the interest in an RRSP to the IRS. The taxpayers are genuinely surprised to discover that their retirement savings, which they cannot access and which are meant to be invested and growing tax-free in Canada, could be subject to U.S. tax and U.S. tax reporting.

In the vast majority of cases, the failure to make a legitimate election is the result of an oversight or misunderstanding by taxpayers or tax return preparers. Given that the treaty is meant to shelter the income derived by an RRSP from U.S. tax, an omission to make such an election on a timely basis should not be viewed as an attempt to avoid tax.

Since 2009, the IRS has engaged in three offshore voluntary disclosure programs relating to foreign bank accounts and various other foreign reporting requirements: one program is currently in process. The purpose of each program is to encourage taxpayers to bring their foreign information reporting obligations into full compliance. Over the past few years, the IRS has come to realize there are certain assets, for example, foreign bank accounts, foreign pension funds, and foreign retirement accounts, that require additional guidance from the IRS as to how to report and what is reportable.

The failure to report these accounts, in many situations, is not due to the intent to evade tax but due to the fact that it is an area which is very complicated and many taxpayers and tax practitioners, were, and still are, unaware of the reporting rules relating to such foreign investments. In this environment, it seems inconsistent to force taxpayers to require a private letter ruling for which they are seeking to make an election after the due date for filing the relevant income tax return.

We respectfully recommend the following:

1. Rather than having a requirement that the taxpayer make a positive election, the IRS should treat all relevant taxpayers as having made an election under Paragraph 7 of Article XVIII, Pensions and Annuities of the U.S.-Canada Tax Treaty unless the taxpayer opts out. This would not relieve the taxpayer of the information filing obligations under Form 8891, and an appropriate penalty for failure to file.
2. If the recommendation in No. 1 is not acceptable, we would ask that the IRS introduce a more streamlined method for addressing late elections. Specifically, a mechanism similar to that introduced for the late filing of IRS Form 8832 (Rev. January 2012), *Entity Classification Election*, would be a balanced approach. In such a circumstance, a taxpayer would be required to provide a reason for his or her failure to file on a timely basis and confirm that nothing else was filed that is inconsistent with the election being made.
   However, a taxpayer would not be required to pursue a private letter ruling and incur the associated costs.

Non-Canadian Retirement Plans

Additionally, we ask that Treasury consider giving greater guidance in relation to the treatment of foreign retirement plans, and consider mechanisms for addressing potential inequities associated with such plans.

As has been seen with the IRS' appropriate focus on offshore reporting in recent years, markets are experiencing greater globalization. As a result, there are significant numbers of immigrants who have worked in their home country before coming to the U.S. and significant numbers of U.S. persons working abroad. While living and working abroad, these people often would have been required to participate in a local retirement savings plan. Such plans typically prevent taxpayers from accessing the amounts invested until they reach retirement age. The foreign jurisdiction, seeking to encourage self-sufficiency in retirement, often provides no or low taxes on the income of the retirement savings plan in the same way the U.S. provides tax concessions to Employer-Sponsored Retirement Plan 401(k) plans and Individual Retirement Accounts (IRAs). Despite the fact that the U.S. would support this objective, it appears that U.S. tax law could potentially tax the income derived in the foreign retirement plan on a current basis or, if deferred, subject it to interest and other charges.

While this matter is addressed specifically in the Treaty to allow deferral for RRSPs, U.S. persons with investments in retirement plans in jurisdictions not covered by any U.S. tax treaty or retirement plans in locations with treaties that do not address the tax treatment of retirement plans, are often left in a difficult situation. To the extent that the retirement savings plan is a trust, they may be required to recognize the income currently (as in the case of a grantor trust) or, to the extent that the retirement savings plan is a corporation, it could be a controlled foreign corporation resulting in current income inclusion or a passive foreign investment company resulting in either current income recognition or a harsh interest charge at the time of distribution of the income.

Such treatments are inconsistent with the shared objective of the U.S. and foreign government, *i.e.*, financial security in retirement for the U.S. person.

Treasury should consider mechanisms to address this inequitable result. Such mechanisms may include:

- Introducing provisions to future tax treaties and protocols that would mirror the election allowed in the Treaty; and
- Legislation to provide for the deferral of tax on compulsory employer contributions to foreign retirement plans and income in legitimate foreign retirement savings plans that were compulsorily established by a U.S. person while they were living or working outside the U.S.

With some simple safeguards, it should be possible to avoid any such concessions from being used for broad based U.S. tax avoidance purposes. We also request additional guidance to be issued regarding the reporting of the various foreign pension and retirement plans as there is much uncertainty as how to report both the income earned in these plans, as well as the value of these plans (particularly on the new IRS Form 8938, *Statement of Specified Foreign Financial Assets*) on the annual tax returns. Again, failure to report is due to a lack of understanding the U.S. rules; not an intent to evade U.S. taxation.