

## Part III – Administrative, Procedural and Miscellaneous

### Treatment of United States Persons that Own Stock of Passive Foreign Investment Companies Through Certain Organizations and Accounts that Are Tax Exempt

Notice 2014-28

#### SECTION 1. PURPOSE

This notice announces that the Department of the Treasury (Treasury Department) and the Internal Revenue Service (IRS) will amend the regulations under section 1291 of the Internal Revenue Code (Code) to provide guidance concerning the treatment of United States persons (U.S. persons) that own stock of a passive foreign investment company within the meaning of section 1297(a) (PFIC) through: an organization or an account that is exempt from tax under section 501(a) because it is described in section 501(c), 501(d), or 401(a); a state college or university described in section 511(a)(2)(B); a plan described in section 403(b) or 457(b); an individual retirement plan or annuity as defined in section 7701(a)(37); or a qualified tuition program described in section 529 or 530.

#### SECTION 2. BACKGROUND

##### *.01 Sections 1291 and 1298*

Section 1291 imposes a special tax and interest charge on a U.S. person that is a shareholder of a PFIC and receives an excess distribution (within the meaning of section 1291(b)) from the PFIC or recognizes gain derived from a disposition of the

PFIC that is treated as an excess distribution (within the meaning of section 1291(a)(2)). Section 1298(a) sets forth attribution rules that treat a U.S. person as the owner of PFIC stock that is owned by another person. The section 1298(a) attribution rules will not apply to treat stock owned (or treated as owned) by a U.S. person as owned by any other person, except to the extent provided in regulations. Section 1298(a)(1)(B). Section 1298(f) provides that a U.S. person that is a shareholder of a PFIC must file an annual report containing the information required by the Secretary. Section 1298(g) provides that the Secretary shall provide such regulations as may be necessary or appropriate to carry out the purposes of sections 1291 through 1298.

#### *.02 Regulations under Sections 1291 and 1298*

On December 31, 2013, the Treasury Department and the IRS published temporary and proposed regulations under sections 1291 and 1298 (2014-3 I.R.B. 394) that defined the terms shareholder and indirect shareholder for purposes of section 1291. See §1.1291-1T(b)(7) and (8). These definitions are cross-referenced in the definition of shareholder and indirect shareholder in the section 1298(f) information reporting regulations, as well as in other PFIC regulations. See §§1.1291-9T(j), 1.1298-1T(a). Under §1.1291-1T(b)(7), the term shareholder means any U.S. person that owns stock of a PFIC directly or indirectly. Section 1.1291-1T(b)(8) defines the term indirect shareholder as a U.S. person that indirectly owns stock of a PFIC, and provides rules for attributing ownership of PFIC stock through domestic and foreign corporations, partnerships, S corporations, estates, and trusts. For example, §1.1291-1T(b)(8)(iii)(C) provides that, in general, each beneficiary of a foreign or domestic nongrantor trust that directly or indirectly owns stock of a PFIC is considered to own a proportionate amount

of the PFIC stock and, thus, each beneficiary that is a U.S. person is an indirect shareholder of the PFIC.

### *.03 Tax Exempt Organizations*

In general, §1.1291-1(e) provides that section 1291 applies to a PFIC shareholder that is an organization exempt from tax under chapter 1 of the Code only if a dividend from the PFIC owned by the organization would be taxable to the organization under subchapter F of Subtitle A of the Code (sections 501 through 530) (subchapter F). Section 1.1298-1T(c)(1) provides that a PFIC shareholder that is an organization exempt from tax under section 501(a) because it is described in section 501(c), 501(d), or 401(a), a state college or university described in section 511(a)(2)(B), a plan described in section 403(b) or 457(b), an individual retirement plan or annuity as defined in section 7701(a)(37), or a qualified tuition program described in section 529 or 530 (each a tax exempt organization or account) is required to file an annual report under section 1298(f) with respect to a PFIC only if income derived with respect to the PFIC would be taxable to the organization or account under subchapter F.

Neither the Code nor the section 1291 regulations provide specific guidance on the application of section 1291 to a U.S. person that owns stock of a PFIC through a tax exempt organization or account, other than an employees' trust described in section 401(a) that is exempt from tax under section 501(a) (section 401(a) trust). The attribution rules that generally apply to treat a U.S. beneficiary of a nongrantor trust as owning PFIC stock owned by the trust do not apply to a U.S. person that owns an interest in a section 401(a) trust. §1.1291-1T(b)(8)(iii)(C). Thus, a U.S. person that is a

beneficiary of a section 401(a) trust is not treated as an indirect shareholder with respect to any PFIC stock held by the trust for purposes of section 1291.

Although §1.1291-1(e) provides that organizations exempt from tax under chapter 1 of the Code generally are not subject to section 1291 with respect to their direct or indirect ownership of PFIC stock, a U.S. person that is a beneficiary of or has an interest in a tax exempt organization or account may be treated as a direct or indirect shareholder of the PFIC stock owned by the organization or account under §1.1291-1T(b)(7) and (8), and thus may be subject to taxation under section 1291.

### SECTION 3. TREATMENT OF U.S. PERSONS THAT OWN STOCK OF A PFIC THROUGH CERTAIN ORGANIZATIONS AND ACCOUNTS THAT ARE TAX EXEMPT

The Treasury Department and the IRS believe that the application of the PFIC rules to a U.S. person treated as owning stock of a PFIC through a tax exempt organization or account described in §1.1298-1T(c)(1) would be inconsistent with the tax policies underlying the PFIC rules and the tax provisions applicable to tax exempt organizations and accounts. For example, applying the PFIC rules to a U.S. person that is treated as a shareholder of a PFIC through the U.S. person's ownership of an individual retirement account (IRA) described in section 408(a) that owns stock of a PFIC would be inconsistent with the principle of deferred taxation provided by IRAs. Accordingly, the Treasury Department and the IRS will amend the definition of shareholder in the section 1291 regulations to provide that a U.S. person that owns stock of a PFIC through a tax exempt organization or account (as described in §1.1298-1T(c)(1)) is not treated as a shareholder of the PFIC. This amendment will affect all regulations that cross-reference the §1.1291-1T(b)(7) and (8) definitions of shareholder and indirect shareholder, including §1.1298-1T(a).

#### SECTION 4. EFFECTIVE DATE

The regulations incorporating the guidance described in this notice will be effective for taxable years of U.S. persons that own stock of a PFIC through a tax exempt organization or account ending on or after December 31, 2013.

#### SECTION 5. DRAFTING INFORMATION

The principal author of this notice is Susan E. Massey of the Office of Associate Chief Counsel (International). For further information regarding this notice contact Susan Massey at (202) 317-6934 (not a toll-free call).