

# The Estate Planner

---

*By Lewis J. Saret\**

## The 3.8-Percent Medicare Contribution Proposed Regulations—Part I

### Introduction

---

On November 30, 2012, the Treasury released proposed regulations that provide guidance with respect to Code Sec. 1411. Code Sec. 1411, the subject of a previous column,<sup>1</sup> refers to the 3.8-Percent Net Investment Income Tax ("3.8-percent tax") that takes effect this year. This column, which is the first of two parts, continues that discussion by focusing on the proposed regulations.

Code Sec. 1411, which is listed under the new subchapter 2A, places a 3.8-percent tax on net investment income for individuals, trusts and estates. Code Sec. 1411 raises several issues. The IRS, through the proposed regulations, aims to provide further guidance in areas of uncertainty, to offer an extensive explanation of terms and applicability to individuals, trusts and estates, and to clarify the treatment of the tax under several special circumstances. Since the tax placed by Code Sec. 1411 has a significant impact on individuals, trusts and estates, a firm understanding of the proposed regulations associated with Code Sec. 1411 is critical.

### The Proposed Regulations

---

The proposed regulations are divided into 11 sections: Reg. §1.1469-11, and Reg. §1.1411-1 through Reg. §1.1411-10. The regulations indicate that most provisions are to go into effect for tax years beginning after December 31, 2013.<sup>2</sup> In addition, the preamble to the proposed regulations states that Treasury and the IRS intend to finalize the proposed regulations in 2013. However, the preamble also states that



CCH

a Wolters Kluwer Business



**Lewis J. Saret** is the founder of the Law Office of Lewis J. Saret, in Washington, D.C. He concentrates his practice in the area of federal taxation, with particular emphasis on estate and business succession planning, and may be reached at [lewis.saret@gmail.com](mailto:lewis.saret@gmail.com).

taxpayers may rely on the proposed regulations for Code Sec. 1411 compliance purposes until the effective date of the final regulations. To the extent the proposed regulations provide taxpayers with the ability to make an election, taxpayers may make the election, including regroupings described in Reg. §1.469-11(b)(3)(iv), provided that the election is made in the manner described in the applicable provision of the proposed regulations. Any election made in reliance on these proposed regulations will be in effect for the year of the election, and will remain in effect for subsequent tax years. However, if final regulations provide for the same or a similar election, taxpayers who opt not to make an election in reliance on these proposed regulations will not be precluded from making that election pursuant to the final regulations.<sup>3</sup>

Generally, the proposed regulations offer guidance on the following areas:

- Code Sec. 1411's relationship to chapter 1 (Proposed Reg. §1.1411-1)
- Application to individuals (Proposed Reg. §1.1411-2)
- Application to trusts and estates (Proposed Reg. §1.1411-3)
- Net investment income (Proposed Reg. §1.1411-4)
- Net investment income derived from trades or businesses that are passive activities or trading in financial instruments or commodities (Proposed Reg. §1.1411-5)
- Investment in working capital (Proposed Reg. §1.1411-6)
- Dispositions of interest in partnerships and S corps (Proposed Reg. §1.1411-7)
- Distributions from qualified plans (Proposed Reg. §1.1411-8)
- Self-employment income (Proposed Reg. §1.1411-9)
- Controlled foreign corporations (CFCs) and passive foreign investment corporations (PFICs) (Proposed Reg. §1.1411-10)
- Certain rules that provide a regrouping "fresh start" under Code Sec. 469 for certain taxpayers (Proposed Reg. §1.469-11)

**Note.** Although Proposed Reg. §1.469-11 is not technically a proposed regulation under Code Sec. 1411, it was released as part of the Code Sec. 1411 Proposed Regulations because of its relevance to the calculation of the 3.8-percent tax. Proposed Reg. §1.469-11 allows taxpayers

to regroup their activities for tax purposes once any time during the current tax year or thereafter.<sup>4</sup>

## Relationship to Chapter 1

Code Sec. 1411 imposes a new tax on investment income, under new chapter 2A of the Code. However, other than certain specific cross-references in Code Sec. 1411, Code Sec. 1411 does not provide definitions of its key terms. In addition, the legislative history of Code Sec. 1411 does not indicate that Congress intended terms used in Code Sec. 1411 to have the same meaning as those used for other federal income taxes. Therefore, under the proposed regulations, unless otherwise specified, Code Sec. 1411 will follow the same rules and principles as chapter 1 when determining the tax. This holds significant implications. The following are a few examples of how this affects the calculation of the 3.8-Percent Net Investment Income tax under Code Sec. 1411:

- Gains that are not included for chapter 1 purposes, such as gains from involuntary conversions or the sale of a principal residence, are also not included under Code Sec. 1411.<sup>5</sup>
- References to disallowance provisions of chapter 1 that apply when determining adjusted gross income under chapter 1, such as at-risk limitations or partner loss limitations, also apply for purposes of Code Sec. 1411.<sup>6</sup>
- Deductions that are carried over to another tax year due to provisions from certain other Code sections which are included in the calculation of adjusted gross income under chapter 1 are also allowed to be included in the calculation of net investment income for Code Sec. 1411, regardless of the deduction's original tax year.<sup>7</sup>

Although, as discussed above, Code Sec. 1411 generally follows closely the rules laid out in chapter 1, in order to preserve the purpose of the statute, the proposed regulations deviate from certain provisions of chapter 1. To illustrate, the following are two differences between Code Sec. 1411 and chapter 1:

1. Substitute interest and dividends, although not categorized as "interest" and "dividends" under chapter 1, are still included as such in the calculation of net investment income for Code Sec. 1411.<sup>8</sup>
2. Certain types of distributions from some items of income that are excluded from gross income for chapter 1 purposes may still be included in the determination of net investment income for

Code Sec. 1411. An example is distributions described Code Sec. 959(d) or Code Sec. 1293(c), which relate to controlled foreign corporations and passive foreign investment corporations and which are included in net investment income.<sup>9</sup>

**Caution.** The Preamble to the proposed regulations states that the IRS will closely scrutinize transactions that manipulate a taxpayer's net investment income to reduce or eliminate the amount of the 3.8-percent tax. Specifically, the Preamble states that "[i]n appropriate circumstances, the IRS will challenge such transactions based on applicable statutes and judicial doctrines. Thus, for example, if an investment arrangement that in form gives rise to income that does not constitute net investment income is in substance properly treated for Federal tax purposes as the holding of securities by one party as agent for another, the arrangement will be taxed in accordance with its substance."<sup>10</sup>

## Application to Individuals

Proposed Reg. §1.1411-2 specifically addresses the application of Code Sec. 1411 to individuals. Code Sec. 1411 states that for individuals, a 3.8-percent tax will apply each tax year on the lesser of either:

- an individual's net investment income (NII); or
- the excess of an individual's modified adjusted gross income (MAGI), over a threshold amount.

The three threshold amounts, which are fixed, are defined in Code Sec. 1411 as the following:

1. \$250,000 for married taxpayers filing jointly
2. \$125,000 for married taxpayers filing separately
3. \$200,000 for all other cases

In addition, Proposed Reg. §1.1411-2 defines the term "modified adjusted gross income," which is unique to the calculation of the 3.8-percent tax for individuals, as an individual's adjusted gross income according to Code Sec. 62, increased by any income excluded from gross income according to Code Sec. 911(a)(1) net of all associating deductions according to Code Sec. 911(d)(6).<sup>11</sup> The term "net investment income" is discussed below.

Since the statute also does not define the term "individual" beyond the exclusion of nonresident aliens, the proposed regulations suggest that a workable definition for "individual" would be any natural person who is a citizen or resident of the United States.<sup>12</sup> In addition, Proposed Reg. §1.1411-2 also

clarifies the treatment of tax calculations for the following situations:

- Married couples where one spouse is a nonresident alien
- *Bona fide* residents of U.S. territories
- Individuals with short accounting periods

## Joint Returns When a Nonresident Alien Is Married to a U.S. Citizen or Resident

Although Code Sec. 1411 explains the application of the 3.8-percent tax for U.S. citizens, residents and nonresident aliens, it does not provide any guidance for married couples where one spouse is a nonresident alien and the other is a U.S. citizen or resident. The proposed regulations provide that absent an election, spouses are to determine their NII and MAGI separately, and the tax would apply for the U.S. citizen or resident only. The nonresident alien spouse is exempt from the tax. In addition, the U.S. citizen or resident will be treated as married filing separately and so will be subject to the \$125,000 threshold for MAGI.<sup>13</sup>

Proposed Reg. §1.1411-2 also gives spouses who file a joint federal income tax return pursuant to a Code Sec. 6013(g) election the option to make an election to be treated as making a Code Sec. 6013(g) election for purposes of the 3.8-percent tax. The effect of such an election would be to include the combined income of the U.S. citizen/resident spouse and the nonresident alien spouse in the Code Sec. 1411(a)(1) calculation and the combined MAGI will be subject to the threshold of \$250,000.<sup>14</sup> The procedural details regarding making such an election are set forth in Proposed Reg. §1.1411-2(a)(2)(B)(2).

**Example 1.** In 2013, Jim and Della, earned \$80,000 and \$130,000 in net income, respectively. Jim and Della also each earned an additional \$20,000 in net investment income. Jim and Della are married, and Della is a U.S. citizen, but Jim is a nonresident alien. Since Jim is a nonresident alien, his income is exempted from the 3.8-Percent Net Investment Income tax. Della, who is a U.S. citizen, is still subject to the tax, but is subject to a \$125,000 threshold on her MAGI since she is married filing separately. Thus, for 2013, Della's NII is \$20,000 and her MAGI is \$130,000 + \$20,000 = \$150,000, which is \$25,000 above the threshold. Therefore, Della's

3.8-Percent Net Investment Income tax for 2013 would be  $\$20,000 \times 3.8\% = \$760$ , and Jim's for 2013 would be zero.

**Example 2.** Same facts as Example 1, except Jim and Della choose to make a Code Sec. 6013(g) election and consider their income jointly. Thus, their combined NII would be \$40,000 and their combined MAGI would be  $\$80,000 + \$130,000 + \$40,000 = \$250,000$ . Since they are married filing jointly, their MAGI is subject to a \$250,000 threshold, which reduces their MAGI after threshold to zero. Thus, for 2013, Della and Jim's 3.8-Percent Net Investment Income tax would be zero.

## Bona Fide Residents of U.S. Territories

Proposed Reg. §1.1411-2 provides guidance on the application of the 3.8-percent tax to residents of U.S. territories,<sup>15</sup> which are American Samoa, Guam, the Northern Mariana Islands, Puerto Rico and the U.S. Virgin Islands.<sup>16</sup> Application of Code Sec. 1411 for *bona fide* residents of a U.S. territory depends on whether the U.S. territory has a mirror code system of taxation with respect to the United States.<sup>17</sup> The tax imposed by Code Sec. 1411(a) generally does not apply to *bona fide* residents of mirror code jurisdictions because they will not have an income tax liability to the United States if they fully comply with the tax laws of the relevant territory. The following three territories hold this characteristic: Guam, the Northern Mariana Islands and the U.S. Virgin Islands.<sup>18</sup> The tax imposed under Code Sec. 1411(a) is applicable to *bona fide* residents of non-mirror code jurisdictions if they have U.S. reportable income that gives rise to both net investment income and modified adjusted gross income exceeding the threshold amount in Code Sec. 1411—namely Puerto Rico and American Samoa. Therefore, only individuals who are not nonresident aliens with respect to the United States and reside in Puerto Rico or American Samoa are subject to Code Sec. 1411.

## Individuals with a Short Tax Year

A short tax year is a tax year that is less than 12 months. If an individual has a short tax year, it raises the question of whether his or her MAGI threshold amount would be reduced to reflect the shortened year. The proposed regulations clarify this issue by providing that the threshold amount is generally not prorated in the case of a short tax year of an indi-

vidual. However, they also provide a special rule for an individual who has a short tax year resulting from a change of annual accounting period. Under Code Sec. 443(b)(1), a taxpayer that undergoes a change in annual accounting period under Code Sec. 442 and has a short period must annualize its taxable income. The taxpayer's federal income tax is the tax computed on the annualized taxable income by multiplying the taxable income for the short period by 12 and dividing the result by the number of months in the short period. Proposed Reg. §1.1411-2(d)(2)(ii) provides that an individual taxpayer that has a short period resulting from a change of annual accounting period must reduce the applicable threshold amount to an amount that bears the same ratio to the full threshold amount provided under Code Sec. 1411(b) as the number of months in the short period bears to 12.<sup>19</sup>

**Example 3.** Jack, a single man, has a tax year from January 1 to December 31. On July 1, Jack passes away. Thus, Jack's short tax year would begin on January 1 and end on July 1. To determine Jack's 3.8-Percent Net Investment Income tax, the entire threshold amount of \$200,000 would be used for his short tax year.

## Application to Estates and Trusts

Code Sec. 1411 applies a similar 3.8-percent tax to estates and trusts. Like the tax applied to individuals, a 3.8-percent tax for a particular tax year is applied to the lesser of two components:

1. The estate's or trust's undistributed net investment income (UNII)
2. The excess of the estate's or trust's adjusted gross income (AGI) over a threshold<sup>20</sup>

Code Sec. 1411 provides that the threshold for trusts and estates is the dollar amount that begins the highest tax bracket for that particular tax year. This amount is adjusted each year and will be approximately \$11,650 for 2013.

In addition, Proposed Reg. §1.1411-3, which specifically addresses the application of Code Sec. 1411 to estates and trusts, also provides guidance for estates or trusts with a short tax year. As for individuals, the MAGI threshold is not reduced for an estate's or trust's shortened tax year, unless the cause of the short tax year is a change in annual accounting period.<sup>21</sup> If that is the case, the new threshold is calculated with the following formula:



New Threshold = Original Threshold x (Number of months in tax year/12).<sup>22</sup>

The proposed regulations also clarify which trusts and estates are taxable under Code Sec. 1411 and which are exempted. For the determination of applicability under Code Sec. 1411, Proposed Reg. §1.1411-3 provides that the 3.8-Percent Net Investment Income tax applies to all estates and trusts that are subject to the provisions Code subtitle A, chapter 1, subchapter J, part I.<sup>23</sup>

The Preamble to the proposed regulations notes that, because Congress did not provide a rule specifying the particular trusts subject to Code Sec. 1411, the proposed regulations take the position that Code Sec. 1411 applies to ordinary trusts described in Reg. §301.7701-4(a). The general rule set forth in Proposed Reg. §1.1411-3(a)(1)(i) implements this approach. This rule excludes from the application of Code Sec. 1411 business trusts described in Reg. §301.7701-4(b), which are treated as business entities under Reg. §301.7701-2 and as eligible entities for purposes of entity classification in Reg. §301.7701-3. Accordingly, such trusts are not subject to Code Sec. 1411 at the entity level.

In addition, the general rule excludes certain state law trusts that are subject to specific taxation regimes in chapter 1 other than part I of subchapter J. This exclusion is consistent with the exception in the entity classification regulations for entities where a specific provision of the Code provides for special treatment of that organization. See Reg. §301.7701-1(b). Examples of these trusts include common trust funds taxed under Code Sec. 584 and expressly not subject to taxation under chapter 1 (per Code Sec. 584(b)) and designated settlement funds taxed under Code Sec. 468B in lieu of any other taxation under subtitle A (per Code Sec. 468B(b)(4)).

However, Code Sec. 1411 does apply to trusts subject to the provisions of part I of subchapter J, even though such trusts may have special computational rules within those provisions.<sup>24</sup>

**Note.** Although the IRS believes trusts described under part I of subchapter J of the Code should be subject to these provisions, the IRS invites comment if taxpayers believe that calculating this tax for a specific trust would be difficult enough that it would place an undue burden on the taxpayers and should therefore be excluded. Therefore, since the IRS is open to excluding certain types of trusts under part 1 of subchapter J, planners

and taxpayers should pay particular attention to raise any administrative issues with specific trusts that they foresee.

## Application to Specific Trusts

The proposed regulations exempt certain trusts from the application of Code Sec. 1411, including the following types of trusts<sup>25</sup>:

- Trusts whose interests are devoted to purposes listed in Code Sec. 170(c)(2)(B)
- Charitable remainder trusts, with certain exceptions
- Trusts that are exempt from taxation under subtitle A (such as Code Sec. 220(e)(1) or Code Sec. 529(a))
- Tax-exempt trusts under Code Sec. 501
- Grantor trusts
- Certain foreign trusts

Although most of the trusts listed above are always exempted, certain trusts are exempted only under particular circumstances. The proposed regulations provide additional guidance on the specific treatment and calculations for the tax for these trusts. The proposed regulations also provide specific guidance with respect to the following types of trusts:

- Grantor trusts
- Electing small business trusts (ESBTs)
- Charitable remainder trusts

## Grantor Trusts

Grantor trusts are treated as trusts that are deemed owned or partly owned by a grantor or another person for income tax purposes and are exempted from the 3.8-percent tax by Proposed Reg. §1.1411-3(b)(5).<sup>26</sup> On the other hand, however, any income and deductions attributable to the grantor trust are treated as part the owner's taxable income, not the trust's for purposes of the 3.8-percent tax. This means a grantor trust is not subject to the tax under Code Sec. 1411. However, any income from a grantor trust that is included as taxable income for the owner, is considered as investment income, and so will also increase the owner's net investment income.<sup>27</sup>

**Example 4.** In 2013, the Valjean Trust Fund, a grantor trust created and treated (for income tax purposes) as owned by Jean Valjean, had income of \$40,000. Jean Valjean who is unmarried, earned \$170,000 in salary for 2013 and did not have any additional investment income. For the calculation of tax applicable to the Valjean Trust

Fund, since Valjean Trust Fund is a grantor trust, the trust is not subject to the Code Sec. 1411 3.8-percent tax. However, for the calculation of Jean Valjean's 3.8-percent tax, Jean would include the \$40,000 of income attributable to the Valjean Trust Fund because it is a grantor trust along with his own net investment income. Thus, his NII for 2013 is \$40,000 and his MAGI is \$210,000. Since his MAGI above the threshold of \$200,000 is less than his NII, under Code Sec. 1411, he is subject to a 3.8-percent tax of  $\$10,000 \times 3.8\% = \$380$ .

## Electing Small Business Trusts (ESBTs)

Proposed Reg. §1.1411-3(c)(1) provides special computational rules for ESBTs.

For purposes of federal income taxation under chapter 1, Code Sec. 641(c)(1) provides that (1) the portion of any ESBT which consists of stock in one or more S corporations shall be treated as a separate trust, and (2) the amount of the tax imposed by chapter 1 on such separate trust shall be determined with certain modifications detailed in Code Sec. 641(c)(2).

Reg. §1.641(c)-1(a) provides that an ESBT is treated as two separate trusts for purposes of chapter 1.

Generally, the proposed regulations preserve the chapter 1 treatment of the ESBT as two separate trusts for computational purposes but consolidates the ESBT into a single trust for determining the adjusted gross income threshold in Code Sec. 1411(a)(2)(B)(ii). This rule applies a single section 1(e) threshold so as to not inequitably benefit ESBTs over other taxable trusts.<sup>28</sup>

Specifically, the proposed regulations set forth the following computational steps:

1. To determine the ESBT's undistributed net investment income, separately calculate the undistributed net investment income for the S portion and the non-S portion in the manner set forth in Proposed Reg. §1.1411-3(e). Add these two amounts together to determine the ESBT's undistributed net investment income.<sup>29</sup>
2. To determine the ESBT's adjusted gross income as defined in Reg. §1.1411-3(a)(1)(ii)(B)(1), increase or decrease the non-S portion's adjusted gross income by the net income/loss of the S portion. The S portion's net income/loss also includes all deductions, carryovers or loss limitations applicable to the S portion as a single item of ordinary income/loss.<sup>30</sup>

3. The 3.8-percent tax is applied to the lesser of the ESBT's UNII or its AGI above the threshold.

**Example 5.**<sup>31</sup> In Year 1, the non-S portion of the Bag End Trust, an ESBT, has dividend income of \$15,000, interest income of \$10,000 and capital gain of \$5,000. The Bag End Trust's S portion has net rental income of \$21,000 and a capital loss of \$7,000. The Trustee's annual fee of \$1,000 is allocated 60 percent to the non-S portion and 40 percent to the S portion. The Bag End Trust makes a distribution from income to a single beneficiary of \$9,000.

### Step one.

(A) The Bag End Trust must compute the undistributed net investment income for the S portion and non-S portion. The undistributed net investment income for the S portion is \$20,600 and is determined as shown in Chart 1.

**Chart 1.**

Net Rental Income	\$21,000
Trustee Annual Fee	(\$400)
Total S portion undistributed net investment income	\$20,600

(B) No portion of the capital loss is allowed because, pursuant to Reg. §1.1411-4(d)(2), net gain cannot be less than zero and excess capital losses are not properly allocable deductions under Reg. §1.1411-4(f). In addition, pursuant to Reg. §1.641(c)-1(i), no portion of the \$9,000 distribution is allocable to the S portion. The undistributed net investment income for the non-S portion is \$20,400 and is determined as shown in Chart 2.

**Chart 2.**

Dividend Income	\$15,000
Interest Income	\$10,000
Capital Gain	\$5,000
Trustee Annual Fee	(\$600)
Distributable net income distribution	(\$9,000)
Total non-S portion undistributed net investment income	\$20,400

(C) The Bag End Trust will combine the undistributed net investment income of the S portion

and non-S portion from (A) and (B) to arrive at the Bag End Trust's combined undistributed net investment income (see Chart 3, below).

**Chart 3.**

S portion's undistributed net investment income	\$20,600
Non-S portion's undistributed net investment income	\$20,400
Combined undistributed net investment income	\$41,000

**Step two.**

(A) The ESBT will calculate its adjusted gross income. The ESBT's adjusted gross income is the non-S portion's adjusted gross income increased or decreased by the net income or net loss of the S portion.

(B) The adjusted gross income for the ESBT is \$38,000 and is determined as shown in Chart 4.

**Chart 4.**

Dividend Income	\$15,000
Interest Income	\$10,000
Capital Gain	\$5,000
Trustee Annual Fee	(\$600)
Distributable net income distribution	(\$9,000)
S Portion Income (see (ii)(C))	\$17,600
Adjusted gross income	\$38,000

**Step three.** The Bag End Trust will pay tax on the lesser of: the combined undistributed net investment income (\$41,000 calculated in (i)(C)); or the excess of adjusted gross income (\$38,000 calculated in (ii)(B)) over the dollar amount at which the highest tax bracket applicable to a trust begins for the tax year.

## Charitable Remainder Trusts

Although the proposed regulations state that charitable remainder trusts are generally not subject to the 3.8-percent tax under Code Sec. 1411, it is important to note that the IRS provides special rules for the treatment of annuities and unitrust distributions to beneficiaries. Since annuities and unitrust

distributions increase net investment income for beneficiaries, the proposed regulations provide the following new rules to maintain the character and distribution ordering rules of Reg. §1.664-1(d) for purposes of Code Sec. 1411. Specifically, net investment income of the beneficiaries that is attributable to the beneficiary's annuity and unitrust distribution is equal to be the lesser of either:

- total amount distributed that year; or
- current and accumulated net investment income of the charitable remainder trust.<sup>32</sup>

For this purpose, the accumulated net investment income of a charitable remainder trust is the total amount of net investment income received by the charitable remainder trust for all tax years that begin after December 31, 2012, decreased by the sum of all distributed net investment income attributable to all prior tax years of the trust that began after December 31, 2012.

In addition, Proposed Reg. §1.1411-3 also provides guidance on charitable remainder trusts with multiple beneficiaries. Under these circumstances, net investment income will be attributed to beneficiaries based on their respective shares of the total annuity or unitrust distribution. This means that if a charitable remainder trust has two beneficiaries, one who received 75 percent of total unitrust distributions and one who received 25 percent, the beneficiary who received 75 percent of distributions would increase his net investment income by what amounts to 75 percent of total distributions.

## Application to Specific Estates

The proposed regulation highlights two types of estates that require special treatment. The two types are bankruptcy estates and foreign estates.

## Bankruptcy Estates

In order to remain consistent with Code Sec. 1398, which provides the rules for the income taxation of certain bankruptcy estates where the debtor is an individual, Proposed Reg. §1.1411-3 indicates that for the calculation of the 3.8-percent tax for chapter 7 or chapter 11 bankruptcy estates, the bankruptcy estate is to be treated as a married taxpayer filing a separate return.<sup>33</sup> This means regardless of the marital status of the debtor, the MAGI threshold amount used for the bankruptcy estate is \$125,000.

## Foreign Trusts and Estates

In the preamble, the IRS expresses uncertainty as to whether Code Sec. 1411 and related regulations should be applied to the U.S. beneficiaries of foreign trusts and foreign estates. Specifically, the IRS requests comment on whether investment income

earned by foreign trusts and estates and distributions made by foreign trusts and estates to U.S. beneficiaries should subject to the 3.8-percent tax.<sup>34</sup> Therefore, taxpayers who are beneficiaries to foreign trusts or estates should pay particular attention to the development of this section and are encouraged to provide comments and suggestions regarding this section.

### ENDNOTES

\* The author gratefully acknowledges the assistance of Jenny Ong in the preparation of this column.

<sup>1</sup> Lewis J. Saret, *The Estate Planner, The 3.8% Medicare Contribution Tax*, TAXES, Jan. 2013, at 19.

<sup>2</sup> Proposed Reg. §§1.1411-1(a), -2(e), -3(g), -4(i), -5(d), -6(c), -7(f), -8(c), -9(i).

<sup>3</sup> Preamble, at 84.

<sup>4</sup> Proposed Reg. §1.149-11.

<sup>5</sup> Preamble, at 8.

<sup>6</sup> Preamble, at 8.

<sup>7</sup> Preamble, at 9.

<sup>8</sup> Preamble, at 9.

<sup>9</sup> Preamble, at 9. Additional information regarding CFCs and PFICs can be found at

Proposed Reg. §1.1411-10.

<sup>10</sup> Preamble, at 10.

<sup>11</sup> Proposed Reg. §1.1411-2(c).

<sup>12</sup> Proposed Reg. §1.1411-2(a)(1).

<sup>13</sup> Proposed Reg. §1.1411-2(a)(2)(i)(A).

<sup>14</sup> Proposed Reg. §1.1411-2(a)(2)(i)(B).

<sup>15</sup> Preamble, at 12.

<sup>16</sup> Proposed Reg. §1.1411-2(a)(2)(iv)(C)(2).

<sup>17</sup> Proposed Reg. §1.1411-2(a)(2)(iv)(A).

<sup>18</sup> Preamble, at 13.

<sup>19</sup> Proposed Reg. §1.1411-2(d)(2)(ii).

<sup>20</sup> Code Sec. 1411(a)(2)(B).

<sup>21</sup> Proposed Reg. §1.1411-3(a)(2).

<sup>22</sup> Proposed Reg. §1.1411-3(a)(2)(ii).

<sup>23</sup> Proposed Reg. §1.1411-3(a)(1)(i).

<sup>24</sup> Such trusts include pooled income funds

described in Code Sec. 642(c)(5), cemetery perpetual care funds described in Code Sec. 642(i), qualified funeral trusts described in Code Sec. 685 and certain Alaska Native settlement trusts described in Code Sec. 646.

<sup>25</sup> Proposed Reg. §1.1411-3(b).

<sup>26</sup> Preamble, at 18.

<sup>27</sup> Preamble, at 18.

<sup>28</sup> Preamble, at 19.

<sup>29</sup> Proposed Reg. §1.1411-3(c)(1)(ii)(A).

<sup>30</sup> Proposed Reg. §1.1411-3(c)(1)(ii)(B).

<sup>31</sup> Proposed Reg. §1.1411-3(f), Example 3.

<sup>32</sup> Proposed Reg. §1.1411-3(c)(2)(i).

<sup>33</sup> Proposed Reg. §1.1411-3(d)(1).

<sup>34</sup> Preamble, at 22.

This article is reprinted with the publisher's permission from the TAXES—THE TAX MAGAZINE, a monthly journal published by CCH, a Wolters Kluwer business. Copying or distribution without the publisher's permission is prohibited. To subscribe to the TAXES—THE TAX MAGAZINE or other CCH Journals please call 800-449-8114 or visit [www.CCHGroup.com](http://www.CCHGroup.com). All views expressed in the articles and columns are those of the author and not necessarily those of CCH.

a Wolters Kluwer business