DEFENDING AMERICA'S SMALL AND FAMILY-OWNED BUSINESSES

VIA ELECTRONIC MAIL (International@finance.senate.gov)

April 14, 2015

The Honorable Rob Portman
Co-Chairman
International Tax Reform Working Group
Senate Committee on Finance
219 Dirksen Senate Office Building
Washington, D.C. 20510-6200

The Honorable Charles Schumer
Co-Chairman
International Tax Reform Working Group
Senate Committee on Finance
219 Dirksen Senate Office Building
Washington, D.C. 20510-6200

Dear Chairmen Portman and Schumer:

The S Corporation Association greatly appreciates the opportunity to comment to the Senate Committee on Finance International Tax Reform Working Group. The S Corporation Association is the only organization in Washington, D.C. exclusively devoted to promoting and protecting the interests of America's 4.5 million Subchapter S corporations. The S Corporation Association was founded in 1996.

The S Corporation Association's comments provided below are focused on ensuring that Subchapter S corporations and their shareholders are treated equitably under any reform of the U.S. international tax rules. The S Corporation Association is particularly concerned with this issue given that a number of prior international tax reform proposals and discussion drafts do not provide such equitable treatment.

For example, both the Tax Reform Act of 2014 (H.R. 1), and the 2013 Senate Finance Committee International Tax Reform Discussion Draft would, to varying degrees, inappropriately (and we believe unintentionally) subject shareholders of Subchapter S corporations to double taxation in certain circumstances.

In order to ensure equitable treatment, we respectfully request that the following principles be utilized in connection with any international tax reform proposal considered by your working group:

1. Shareholders of Subchapter S corporations should not be subject to any applicable transition and/or anti-abuse rules related to the replacement of the current U.S. worldwide system of taxation with a territorial (or participation exemption) system if such shareholders are not eligible for any applicable tax relief provisions (such as a dividends received deduction ("DRD")) provided by such a system; and

2. Because of the unique foreign tax credit rules applicable to shareholders of Subchapter S corporations (i.e., that such shareholders are eligible for the Section 901 direct foreign tax credit but not eligible for the Section 902 indirect foreign tax credit), Subchapter S corporations should continue to be able to structure their international operations in branch form regardless of any changes to the entity classification rules.

With respect to implementation of a territorial system, a number of existing tax reform proposals have provided for a DRD with respect to active foreign earnings that is limited to certain Subchapter C corporation shareholders of controlled foreign corporations.

To the extent similar proposals are considered by your working group, it is respectfully submitted that because shareholders of Subchapter S corporations are not eligible for the DRD, any transition and/or anti-abuse rules related to the DRD not apply to such shareholders. In particular, any "deemed" repatriation or base erosion rules should not apply to shareholders of Subchapter S corporations.

Similarly, any limitations to the Subpart F or foreign tax credit rules should also not apply to such shareholders. Application of any of these transition and/or anti-abuse rules to shareholders of Subchapter S corporations would unfairly impose the costs of a new territorial system on taxpayers who would not benefit from that system. Further, application of any of these rules could subject the income of shareholders of Subchapter S corporations to double taxation without the benefit of a DRD to mitigate such double taxation.

Finally, a number of existing tax reform proposals also propose changes to the entity classification rules. In this regard, it is particularly important that Subchapter S corporations be allowed to continue to conduct their international operations through foreign branches in order to avoid double taxation, in light of the fact that their individual shareholders are eligible for the Section 901 direct foreign tax credit, but not the Section 902 indirect foreign tax credit. Under such a structure, the worldwide income of a Subchapter S corporation is subject to U.S. tax on a current basis in the hands of the shareholders with appropriate measures to avoid double taxation (i.e., the Section 901 direct foreign tax credit).

The S Corporation Association appreciates the opportunity to comment to your working group and would be pleased to work with you to ensure that shareholders of Subchapter S corporations are treated equitably. If you have any further questions or need additional information, please feel free to contact me at your convenience.

Respectfully submitted,

Brian Reardon
President
The S Corporation Association