

FOREIGN-RELATED IRS INFORMATION RETURNS AND REQUIREMENTS

I. Introduction

The Internal Revenue Service (IRS) requires U.S. taxpayers to file information returns in connection with certain foreign entities they may have an interest in and certain foreign transactions they may have engaged in. *There are substantial monetary penalties for failure to file these returns in a timely fashion.* The most common information returns include the following: *(click on form number to go to that page)*

1. [Form 5471](#) - Information Return of U.S. Persons With Respect To Certain Foreign Corporations;
2. [Form 8865](#) - Return of U.S. Persons With Respect to Certain Foreign Partnerships;
3. [Form 5472](#) - Information Return of a 25% Foreign-Owned U.S. Corporation or a Foreign Corporation Engaged in a U.S. Trade or Business;
4. [Form 3520](#) - Annual Return To Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts;
5. [Form 3520-A](#): Annual Information Return of Foreign Trust With a U.S. Owner;
6. [Form 926](#) - Return by a U.S. Transferor of Property to a Foreign Corporation;
7. [Form 8854](#) - Initial and Annual Expatriation Information Statement; and
8. [Form 8898](#) - Statement for Individuals Who Begin or End Bona Fide Residence in a U.S. Possession.

This memorandum summarizes the information returns listed above. This is only a brief summary. The underlying rules are complex and technical. You should not only review the forms and instructions (which can be found through the links provided below) but you should also consult with your tax advisor.

II. Analysis

A. Form 5471 - Information Return of U.S. Persons¹ With Respect To Certain Foreign Corporations

1. *Who Must File?*

Form 5471 must be filed by certain U.S. persons who are shareholders, officers or directors of foreign corporations (or equivalent foreign entities). More specifically, the list of persons required to file Form 5471 includes the following:

- a. A U.S. person who is an officer or director of a foreign corporation in which any U.S. person owns or acquires ten percent (10%) or more of the stock of said corporation;
- b. A U.S. person who acquires stock in a foreign corporation which results in such person's owning ten percent (10%) or more of the stock of said corporation;
- c. A person who becomes a U.S. person while owning ten percent (10%) or more of the stock of a foreign corporation;
- d. A U.S. person who disposes of stock in a foreign corporation that reduces his interest to less than ten percent (10%) of the stock of said corporation; and
- e. A U.S. person who had control (who owned more than fifty percent (50%) of the stock or voting power) of a foreign corporation for an uninterrupted period of at least thirty (30) days during the tax year.

Note: in determining stock ownership, "constructive ownership" rules apply so that stock owned by parties related to a person may be treated as owned by that person.

In certain cases where more than one person must file this form for the same foreign corporation, it may be permissible for only one person to file the form.

2. *When to File*

Form 5471 is due with the income tax return of the shareholder in question. For most individuals, the form would therefore be due by April 15.

3. *Penalties for Failure to File*

The IRS may impose a \$10,000 penalty per foreign corporation for each year that a taxpayer fails to submit Form 5471. Moreover, if the information is not filed within 90 days after the IRS mails a notice of the failure to such a person, an additional \$10,000 penalty (per foreign corporation) is charged for each 30 day period, or fraction thereof, during which the

¹ "U.S. Persons" include U.S. citizens, residents, corporations, partnerships, trusts or estates.

failure continues after the initial 90 day period has expired. The additional penalty is limited to a maximum of \$50,000 for each failure to file.

4. *For More Information*

The IRS website has further information regarding Form 5471 at <http://www.irs.gov/businesses/corporations/article/0,,id=188039,00.html>

B. Form 8865 - Return of U.S. Persons With Respect to Certain Foreign Partnerships

1. *Who Must File*

The persons who most commonly are required to file Form 8865 include the following:

- a. Foreign partnerships that are controlled by U.S. partners;²
- b. Any U.S. person who is a partner in a foreign partnership (or an entity that has elected to be taxed as a partnership); and
- c. Controlled foreign corporations with more than one owner that elect to be treated as partnerships for tax purposes.

In certain cases where more than one person is required to file this form for the same foreign partnership, it may be permissible for only one person to file the form.

2. *When to File*

Form 8865 is due with the income tax return of the U.S. person in question. For most individuals, the form would therefore be due by April 15 or the due date resulting from an extension.

3. *Penalties for Failure to File*

A \$10,000 penalty is imposed for each tax year of each foreign partnership for failure to furnish the required information within the time prescribed. If the information is not filed within 90 days after the IRS has mailed a notice of the failure to the U.S. person, an additional \$10,000 penalty (per foreign partnership) is charged for each 30 day period, or fraction thereof, during which the failure continues after the 90 day period has expired. The additional penalty is limited to a maximum of \$50,000 for each failure.

4. *For More Information*

The IRS website has further information regarding Form 8865 at <http://www.irs.gov/instructions/i8865/ar01.html#d0e22>

² “Control” means that five or fewer U.S. persons who each own a ten percent (10%) or greater interest in the partnership also own (in the aggregate) more than fifty percent (50%) of the total partnership interests.

C. Form 5472 - Information Return of a 25% Foreign-Owned U.S. Corporation or Foreign Corporation Engaged in a U.S. Trade or Business

1. *Who Must File*

U.S. corporations in which foreign shareholders own 25% or more of the stock must file Form 5472 in any year in which the U.S. corporation has a reportable transaction³ with a foreign shareholder. Separate forms need to be filed for each such foreign shareholder.

2. *When to File*

Form 5472 is due with the U.S. corporation's income tax return.

3. *Penalties for Failure to File*

A penalty of \$10,000 will be assessed on any reporting corporation that fails to file Form 5472 when due and in the manner prescribed.

4. *For More Information*

Please see Form 5472 and related instructions at <http://www.irs.gov/pub/irs-pdf/f5472.pdf>.

D. Form 3520 - Annual Return To Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts

1. *Who Must File*

Grantors or beneficiaries of foreign trusts are required to file Form 3520 each time such a trust has a "reportable event." Reportable events include the following:

- a. The formation of a foreign trust;
- b. The transfer of cash or other assets by a settlor or grantor to a foreign trust;
- c. The receipt of any distributions by U.S. beneficiaries from a foreign trust;
- d. The receipt by a U.S. person of more than \$100,000 from a nonresident alien individual or a foreign estate (including foreign persons related to that nonresident alien individual or foreign estate) that is treated as a gift or bequest by the U.S. recipient;
- e. The receipt by a U.S. person of a gift from a foreign partnership or corporation of more than \$13,561; and

³ A reportable transaction is generally any exchange of money or property between the U.S. corporation and a foreign shareholder (except for the payment of dividends). For a more specific definition of a "reportable transaction," please see the instructions to Form 5472, a link to which is provided in Section C(4) herein.

- f. The loaning of money by a U.S. person to a foreign trust.

The U.S. grantor of a foreign trust also must annually file Form 3520.

2. *When to File*

Form 3520 is due with the income tax return of the U.S. person in question. For most individuals, the form would therefore be due on or before April 15 or the extended tax return due date.

3. *Penalties for Failure to File*

Failure to file Form 3520 can result in substantial penalties, including:

- a. 35% of the gross value of any property transferred or any distributions received from a foreign trust; and
- b. 5% of the amount of certain foreign gifts for each month for which the failure to report continues.

Additional penalties may be imposed if noncompliance continues after the IRS mails a notice of failure to comply with required reporting. No penalties will be imposed if the taxpayer can demonstrate that the failure to comply was due to reasonable cause and not willful neglect.

4. *For More Information*

Please see the instructions for Form 3520 at <http://www.irs.gov/pub/irs-pdf/i3520.pdf>

E. Form 3520-A: Annual Information Return of Foreign Trust With a U.S. Owner

1. *Who Must File*

A foreign trust with a U.S. owner must file Form 3520-A in order for the U.S. owner to satisfy certain annual information reporting requirements. However, each U.S. person treated as an owner of any foreign trust is responsible for ensuring that the foreign trust files Form 3520-A and furnishes the required annual statements to its U.S. owners and U.S. beneficiaries.

2. *When to File*

Form 3520-A must be filed by the 15th day of the third month after the end of the trust's tax year.

3. *Penalties for Failure to File*

The U.S. owner is subject to a penalty equal to 5% of the gross value of the portion of the trust's assets treated as owned by the U.S. person at the close of that year if the foreign trust: (a) fails to file a timely Form 3520-A or (b) does not furnish all of the required information or includes incorrect information. Additional penalties may be imposed if noncompliance continues after the IRS mails a notice of failure to comply with the required reporting. No

penalties will be imposed if the taxpayer can demonstrate that the failure to comply was due to reasonable cause and not willful neglect.

4. *For More Information*

Please see the instructions for Form 3520-A at <http://www.irs.gov/pub/irs-pdf/i3520a.pdf>

F. Form 926 - Return by a U.S. Transferor of Property to a Foreign Corporation

1. *Who Must File*

Generally, a U.S. citizen or resident, a domestic corporation, or an estate or trust (other than a foreign estate or trust) must file Form 926 to report a transfer of property (even if such property is not appreciated property) to a foreign corporation. Property includes cash if the total amount transferred exceeds \$100,000 and the transfer owns, directly or constructively, at least 10% of the foreign corporation's stock.

2. *When to File*

Form 926 is due with the income tax return of the transferor in the year of the transfer. For most individuals, the form would therefore be due by April 15 or the extended due date.

3. *Penalties for Failure to File*

The penalty for failure to file equals 10% of the fair market value of the property at the time of the transfer. The penalty shall not apply if the failure to comply is due to reasonable cause and not to willful neglect. The penalty is limited to \$100,000 unless the failure to comply was due to intentional disregard.

4. *For More Information*

Please see the instructions to Form 926 at <http://www.unclefed.com/IRS-Forms/2001/i926.pdf>

G. Form 8854 - Initial and Annual Expatriation Information Statement

1. *Who Must File?*

Taxpayers who are individuals must file Form 8854 to do either of the following:

a. Establish that the taxpayer has expatriated or terminated his long-term resident (LTR) status for tax purposes; or

b. Comply with certain annual information reporting requirements of Section 6039G of the Internal Revenue Code, if the taxpayer is subject to tax under Section 877 of the Internal Revenue Code.⁴

2. *When to File*

a. Initial Information Statement. If the taxpayer is filing Form 8854 because he ceased to be a U.S. citizen (expatriated) or terminated his U.S. residency during the tax year, there is no due date for filing this form. However, until the taxpayer files this form with the Internal Revenue Service and notifies either the Department of State or the Department of Homeland Security of his expatriation or termination of residency, he will continue to be treated, for tax purposes, as if he were still a U.S. citizen or resident. The date of the taxpayer's tax expatriation (the date the taxpayer is no longer subject to U.S. taxation on a worldwide basis) is the date on which the taxpayer has satisfied both requirements.

b. Annual Information Statement. If the taxpayer is a nonresident alien filing Form 8854 to comply with the annual information reporting requirements of section 6039G, this form should be attached to a timely filed Form 1040NR, U.S. Nonresident Alien Income Tax Return. If the taxpayer is not required to file Form 1040NR, he should submit this form by the due date for filing Form 1040NR.

3. *Penalties for Failure to File*

If the taxpayer is subject to section 877 and required to file Form 8854 for any tax year, and he fails to file or does not include all information required by the form or the form includes incorrect information, the taxpayer will owe a penalty of \$10,000 for that year, unless it is shown that such failure is due to reasonable cause and not willful neglect.

4. *For More Information*

Please see the instructions to Form 8854 at <http://www.irs.gov/pub/irs-pdf/i8854.pdf>

H. Form 8898 - Statement for Individuals Who Begin or End Bona Fide Residence in a U.S. Possession

1. *Who Must File?*

A taxpayer must file Form 8898 for the tax year in which he meets both of the following conditions:

⁴ Taxpayers are subject to taxation under Section 877 if they are former U.S. citizens or former LTRs, and any one of the following applies: (1) The taxpayer's average annual net income tax liability for the five years ending before the date of expatriation or termination of residency is more than (a) \$127,000 if expatriated in 2005, (b) \$131,000 if expatriated in 2006, or (c) \$136,000 if expatriated in 2007. This amount is subject to cost-of-living adjustments. The IRS will announce the amounts applicable to future years in annual revenue procedures that will be published in Internal Revenue Bulletins. (2) The taxpayer's net worth is \$2 million or more on the date of expatriation or termination of residency. (3) The taxpayer fails to certify on Form 8854 that he has complied with all U.S. federal tax obligations for the 5 years preceding expatriation or termination of residency.

a. The taxpayer's worldwide gross income in that tax year is more than \$75,000⁵, and

b. The taxpayer meets one of the following: (i) he takes a position for U.S. tax purposes that he became a bona fide resident of a U.S. possession⁶ after a tax year for which he filed a U.S. income tax return as a citizen or resident of the United States but not as a bona fide resident of the possession; (ii) he is a citizen or resident of the United States who takes the position for U.S. tax purposes that he ceased to be a bona fide resident of a U.S. possession after a tax year for which he filed an income tax return (with the IRS, the possession tax authorities, or both) as a bona fide resident of the possession; or (iii) he takes the position for U.S. tax purposes that he became a bona fide resident of Puerto Rico or American Samoa after a tax year for which he was required to file an income tax return as a bona fide resident of the U.S. Virgin Islands, Guam, or the CNMI.

2. *When to File*

Form 8898 must be filed by the due date (including extensions) for filing Form 1040 or Form 1040NR.

3. *Penalties for Failure to File*

If a taxpayer is required to file Form 8898 for any tax year, and he fails to file it or does not include all the information required by the form or the form includes incorrect information, the taxpayer may owe a penalty of \$1,000, unless it is shown that such failure is due to reasonable cause and not willful neglect.

4. *For More Information*

Please see the instructions for Form 8898 at <http://www.irs.gov/pub/irs-pdf/i8898.pdf>

To ensure compliance with requirements imposed by the IRS, we inform you that any U.S. tax advice contained in this communication (including any attachments) is not intended or written to be used, and cannot be used, for the purpose of (i) avoiding tax related penalties under the Internal Revenue Code, or (ii) promoting, marketing or recommending to another party any tax-related matters addressed herein.

For more information regarding this topic, please contact [Gary Kaplan](#) at 310.553.3610.

⁵ When figuring whether a taxpayer has worldwide gross income of more than \$75,000, do not include any of the taxpayer's spouse's income. If both the taxpayer and his spouse are required to file Form 8898, each should file a separate Form 8898.

⁶ For this purpose, the following are considered U.S. possessions: American Samoa, Guam, the Commonwealth of the Northern Mariana Islands (CNMI), the Commonwealth of Puerto Rico, and the U.S. Virgin Islands.