

LB&I International Practice Service Process Unit – Audit

IPS Level	Number	Title	UIL Code	Number
Shelf	N/A	Individual Outbound	–	–
Volume	11	Foreign Corporations	Level 1 UIL	9433
Part	11.1	Individuals with Investments in a CFC	Level 2 UIL	9433.01
Chapter	11.1.2	CFC Information Reporting Issues	Level 3 UIL	9433.01-02
Sub-Chapter	11.1.2.1	Form 5471 - Information Return Filing Requirements	–	–

Unit Name	Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty
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Document Control Number (DCN)	FEN/9433.01_06(2013)(c)
Date of Last Update	10/7/15

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Process Overview

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Process Description

When a US Person (USP), as defined later, is required to file a Form 5471, *Information Return of U.S. Persons With Respect to Certain Foreign Corporations*, it is filed by attaching it to an income tax return, a partnership return, or an exempt organization return. For example, Forms 1040, 1120, 1041, 1065 or 990. The period for which the information is provided is the annual accounting period of the foreign entity that falls within a USP's tax year. [See Internal Revenue Code (IRC) § 6038(a)(1)]

Penalties under IRC § 6038 may apply when a Form 5471 is filed late, substantially incomplete, or not filed at all. For any of these three types of failures, an Initial Penalty of \$10,000 per Form 5471 per year may be assessed. [IRC § 6038(b)(1)] In addition, a Continuation Penalty of \$10,000 per Form 5471 per year may be assessed for every 30-day period (or fraction thereof) beginning 90 days after USP was notified that a failure exists. [IRC § 6038(b)(2)] The maximum Continuation Penalty per Form 5471 per year is \$50,000. [IRC § 6038(b)(2)] These penalties may apply per Form 5471 required on an annual basis. Finally, a reduction in foreign tax credits may be applicable; see index of other related processes at the end of this unit. [IRC § 6038(c)]

Congress enacted IRC § 6038 to curb tax abuses occurring because the IRS was unable to obtain information necessary to evaluate a domestic corporation's interests in, and transactions with, its foreign subsidiaries. [106 Cong. Rec. 11416, 86th Cong. 2d Sess. (1960)] "When properly developed and applied, penalties assist the Service in promoting sound tax administration by increasing the economic costs of noncompliance." [Chief Counsel Notice (CCN) CC-2004-036 (09/22/04)]

Example Circumstances Under Which Process Applies

This process applies when the taxpayer is determined to be a US Shareholder of a Controlled Foreign Corporation (CFC), as defined later, and:

- Filed a delinquent Form 5471
- Failed to file a Form 5471
- Filed a substantially incomplete Form 5471
- Penalties may be applicable per Form 5471 required per year

Determination of Process Applicability

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

The instructions for Form 5471 categorize USPs into different filing categories based on their relationship to the foreign corporation. Which category the USP is in determines what information the USP is required to provide. The statute of limitations on assessing and collecting these penalties differs from that for the return to which the Form 5471 was required to be attached.

Criteria	Resources	6103 Protected Resources
<p>The statute of limitations for assessing and collecting IRC § 6038 penalties ends three years after a substantially complete Form 5471 was filed.</p>	<ul style="list-style-type: none"> ▪ Memo from David W. Horton, Director LB&I-IIC, related Statute of Limitation 	
<p>Currently, there are four active categories of filers:</p> <ul style="list-style-type: none"> ▪ Category One, relating to certain shareholders of foreign personal holding companies, was repealed in 2004. ▪ Categories Two is filed by a United States (U.S.) citizen or resident who is an officer or director of a foreign corporation in which a USP has acquired certain ownership thresholds. ▪ Category Three is filed by the USP who has acquired or disposed of the certain ownership thresholds. ▪ Category Four and Five is covered by this unit and will be further analyzed on subsequent slides. 	<ul style="list-style-type: none"> ▪ Practice Unit, “Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty,” in process as of 4/15 	

Determination of Process Applicability (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

The instructions for Form 5471 categorize USP's into different filing categories based on their relationship to the foreign corporation. Which category the USP is in determines what information the USP is required to provide. The statute of limitations on assessing and collecting these penalties differs from that for the return to which the Form 5471 was required to be attached.

Criteria	Resources	6103 Protected Resources
<p>Category 4 Filer – Controlling Interest of CFC</p> <p>A Category Four filer is a USP who owns a controlling interest of a foreign corporation for an uninterrupted period of at least 30 days during the annual accounting period of the foreign corporation.</p> <p>A USP is a:</p> <ul style="list-style-type: none"> ▪ citizen or resident of the U.S., ▪ domestic corporation, ▪ domestic partnership, or ▪ estate or trust that is not a foreign estate or trust. <p>A USP that owns more than 50% of the combined voting power or value of all classes of stock of a foreign corporation has a controlling interest in that foreign corporation.</p>	<ul style="list-style-type: none"> ▪ IRC 6038(a)(1) Requirement. In general ▪ Treas. Reg. 1.6038-2(a) Requirement of return ▪ Treas. Reg. 1.6038-2(a) USP ▪ IRC 7701(a)(30) USP ▪ IRC 7701(a)(31) Foreign estate or trust ▪ Treas. Reg. 1.6038-2(d)(2) & (3) Special rule ▪ IRC 6038(d)(2) Control of corporation ▪ Treas. Reg. 1.6038-2(b) Control 	

Determination of Process Applicability (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

The instructions for Form 5471 categorize USP's into different filing categories based on their relationship to the foreign corporation. Which category the USP is in determines what information the USP is required to provide. The statute of limitations on assessing and collecting these penalties differs from that for the return to which the Form 5471 was required to be attached.

Criteria	Resources	6103 Protected Resources
<p>When a USP owns a controlling interest in a foreign corporation which owns a controlling interest in another foreign corporation, the USP is treated as indirectly owning a controlling interest in such other foreign corporation.</p> <p>When determining controlling interest, the constructive ownership rules of IRC §318(a) apply with some exceptions.</p>	<ul style="list-style-type: none"> ▪ IRC 6038(e)(2) Control of corporation ▪ IRC 318(a) constructive ownership 	

Determination of Process Applicability (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

The instructions for Form 5471 categorize USP's into different filing categories based on their relationship to the foreign corporation. Which category the USP is in determines what information the USP is required to provide. The statute of limitations on assessing and collecting these penalties differs from that for the return to which the Form 5471 was required to be attached.

Criteria	Resources	6103 Protected Resources
<p>Category 5 Filer – US Shareholder of a CFC</p> <p>A Category Five filer is a U.S. Shareholder who owned stock in a CFC for an uninterrupted period of 30 days or more during the corporation's tax year and owned such stock on the last day of that year.</p> <p>A U.S. Shareholder is a USP who owns 10% or more of the combined voting power of all classes of voting stock of a foreign corporation.</p> <p>USP is defined similar to that for Category Four with exceptions as provided by IRC §957(c).</p>	<ul style="list-style-type: none"> ▪ IRC 6038(a)(1) Requirement. In general. ▪ Practice Unit, "Determination of U.S. Shareholder and CFC Status," FEN/9433.01_03(2013) ▪ IRC 6038(a)(4) Requirement. Information required from certain shareholders in certain cases. ▪ IRC 6038(a)(4) Information required from certain shareholders in certain cases ▪ IRC 951(b) U.S. shareholder defined 	

Determination of Process Applicability (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

The instructions for Form 5471 categorize USP's into different filing categories based on their relationship to the foreign corporation. Which category the USP is in determines what information the USP is required to provide. The statute of limitations on assessing and collecting these penalties differs from that for the return to which the Form 5471 was required to be attached.

Criteria	Resources	6103 Protected Resources
<p>A CFC is a foreign corporation in which, on any day of its annual accounting period, US Shareholders own more than 50% of (a) the total voting power of all classes of stock or (b) the total value of stock.</p> <p>When determining ownership, direct, indirect and constructive ownership rules apply.</p>	<ul style="list-style-type: none"> ▪ IRC 957(c) USP ▪ IRC 957(a) General rule ▪ IRC 958(a) Direct and indirect ownership ▪ IRC 958(b) Constructive ownership 	

Determination of Process Applicability (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

The instructions for Form 5471 categorize USP's into different filing categories based on their relationship to the foreign corporation. Which category the USP is in determines what information the USP is required to provide. The statute of limitations on assessing and collecting these penalties differs from that for the return to which the Form 5471 was required to be attached.

Criteria	Resources	6103 Protected Resources
<p>Filing Exception – Multiple Filers of Same Information</p> <p>When multiple persons are required to file the same Form 5471, it may be jointly filed by attaching it to only one person's return. In that case, the other persons must attach a statement to their respective returns which:</p> <ul style="list-style-type: none"> ▪ states that the filing has or will be satisfied, ▪ provides the name, address and identifying number of the return to which the Form 5471 was or will be attached, and ▪ Identifies the IRS Service Center where the return was or will be filed. <p>If the return and Form 5471 were or will be filed electronically, e-file should be indicated on the joint filer statements.</p>	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.6038-2(j)(1) Two or more persons required to submit the same information ▪ Treas. Reg. 1.6038-2(j)(3) Statement required 	

Determination of Process Applicability (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

The instructions for Form 5471 categorize USP's into different filing categories based on their relationship to the foreign corporation. Which category the USP is in determines what information the USP is required to provide. The statute of limitations on assessing and collecting these penalties differs from that for the return to which the Form 5471 was required to be attached.

Criteria	Resources	6103 Protected Resources
<p>Item D on a jointly filed Form 5471 must list the name, address and identifying number of each person on whose behalf the Form 5471 was filed. Also, each person's status as officer, director and/or other must be noted. See form 5471 instructions.</p> <p>Starting in 2012, Schedule I, <i>Summary of Shareholder's Income From Foreign Corporation</i>, is required to be filed for each shareholder listed in Item D referenced above. The revised Schedule I has an added row to input shareholder identifying information.</p>		

Determination of Process Applicability (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

The instructions for Form 5471 categorize USP's into different filing categories based on their relationship to the foreign corporation. Which category the USP is in determines what information the USP is required to provide. The statute of limitations on assessing and collecting these penalties differs from that for the return to which the Form 5471 was required to be attached.

Criteria	Resources	6103 Protected Resources
<p>Filing Exception – Constructive Ownership</p> <p>A person that does not directly own an interest in a foreign corporation, but is attributed an interest in that foreign corporation from a USP that files the Form 5471, is excepted from the filing requirements.</p> <p>A person that does not directly or indirectly own an interest in a foreign corporation, but is attributed an interest in that foreign corporation from a nonresident alien by the constructive ownership rules of IRC 318(a), is excepted from the filing requirements.</p>	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.6038-2(j)(2)(i) Persons excepted from furnishing information ▪ Treas. Reg. 1.6038-2(i) Other persons excepted from Filing ▪ Treas. Reg. 1.6038-2(c) Attribution rules 	

Summary of Process Steps

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty	
Step 1	Verify Fact of Filing
Step 2	Penalty Case File Controls
Step 3	Penalty Determination
Step 4	Penalty Application/Closing Procedures

Step 1

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 1: Verify Fact of Filing

It has been determined the taxpayer had a requirement to file a Form 5471. Before commencing a penalty case file, first verify whether the taxpayer filed a timely and accurate information return Form 5471. The related income tax return may have been late filed with the Form 5471(s) attached or the related income tax return may have been filed timely but without a substantially complete Form 5471(s).

Considerations	Resources	6103 Protected Resources
<ul style="list-style-type: none"> ▪ Form 5471 is due when USP’s income tax return is due, including extensions ▪ Form 5471 is filed WITH the USP’s income tax return. ▪ As discussed in detail previously there are two exceptions to filing: <ul style="list-style-type: none"> ▪ Multiple Filers of Same Information ▪ Constructive Ownership ▪ No more dual filing requirement which required a copy of the Form 5471 be submitted to the Philadelphia campus in addition to being attached to the USP’s income tax return. ▪ There is no separate Master File Transaction (MFT) in Integrated Data Retrieval System (IDRS) for Form 5471 filings. ▪ Penalties may be asserted when the related income tax return is filed late or when substantially complete Form 5471(s) are not timely filed with the related income tax return, or when Form 5471(s) are not substantially complete. ▪ As you identify Form 5471s that were required, but not filed, for the exam year(s), consider reviewing whether those forms were required, but not filed, in earlier tax years. The statute of limitations for assessing and collecting penalties under IRC §6038 expires three years after a substantially complete Form 5471 is filed 	<ul style="list-style-type: none"> ▪ IRC 6038 ▪ Memo from David W. Horton, Director LB&I-IIC regarding Statute of Limitation for Foreign Information Return Penalties. ▪ Determination of Process Applicability Section (previous slides) 	

Step 1 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 1: Verify Fact of Filing

It has been determined the taxpayer had a requirement to file a Form 5471. Before commencing a penalty case file, first verify whether the taxpayer filed a timely and accurate information return Form 5471. The related income tax return may have been late filed with the Form 5471(s) attached or the related income tax return may have been filed timely but without a substantially complete Form 5471(s).

Considerations	Resources	6103 Protected Resources
<p>The related income tax returns are not required to be under examination for prior periods in order to assess penalties under IRC § 6038.</p>		
<p>Determining if the Return was filed late</p> <ul style="list-style-type: none"> ▪ If the last day for filing a return was a Saturday, a Sunday, or a legal holiday in the District of Columbia, filing timely is when the return is mailed on the next succeeding day which is not a Saturday, Sunday, or a legal holiday. ▪ If a return is postmarked prior to the due date and received after the due date, the due date is treated as the filing date. 	<ul style="list-style-type: none"> ▪ IRC 7503 - Time for performance of acts where last day falls on Saturday, Sunday of legal holiday, ▪ Rev. Rul. 81-269, 1981-2 C.B. 243 ▪ IRC 7502 Timely mailing is treated as timely filing and paying. 	
<p>For Form 1120s filed late after December 31, 2008, the Service automatically assesses an Initial Penalty of \$10,000 for each Form 5471 attached. It is assessed even when a request for reasonable cause was submitted with the Form 1120.</p>	<ul style="list-style-type: none"> ▪ IRM 21.8.2.19.2 Form 5471 Penalties Systemically Assessed from Late Filed Form 1120 	

Step 1 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 1: Verify Fact of Filing

It has been determined the taxpayer had a requirement to file a Form 5471. Before commencing a penalty case file, first verify whether the taxpayer filed a timely and accurate information return Form 5471. The related income tax return may have been late filed with the Form 5471(s) attached or the related income tax return may have been filed timely but without a substantially complete Form 5471(s).

Considerations	Resources	6103 Protected Resources
<p>The following items are helpful in determining whether all Form 5471s that were required to be filed were indeed filed or not filed:</p> <ul style="list-style-type: none"> ▪ Form 5471s; ▪ Tax returns (e.g., Forms 1120, 1040 etc.), plus those of the two preceding tax years; ▪ Forms 8832, Entity Classification Election; ▪ Tax organization chart, plus those of the two preceding tax years; ▪ Legal entity chart, plus those of the two preceding tax years; ▪ Certified English translations of certificates of corporate dissolution, officially stamped by the appropriate foreign government agency; and ▪ Joint filer's statements. <p>The above tools can be used to analyze, compare, and resolve questions to identify missing Form 5471s. All or some of the tools can be used depending on the number of foreign corporations owned by the USP. If necessary, a more experienced agent can provide guidance on how to use these tools</p>	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.6038-2(j)(3) Statement required 	

Step 1 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 1: Verify Fact of Filing

It has been determined the taxpayer had a requirement to file a Form 5471. Before commencing a penalty case file, first verify whether the taxpayer filed a timely and accurate information return Form 5471. The related income tax return may have been late filed with the Form 5471(s) attached or the related income tax return may have been filed timely but without a substantially complete Form 5471(s).

Considerations	Resources	6103 Protected Resources
If you determine the USP was required but did not file Form 5471(s) or failed to file substantially complete Form 5471(s), prepare a notice letter to notify the USP of the failure. The term substantially complete (substantial compliance) is discussed on the following slides. See Step 2 – Notice Letter.		

Step 1 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 1: Verify Fact of Filing

It has been determined the taxpayer had a requirement to file a Form 5471. Before commencing a penalty case file, first verify whether the taxpayer filed a timely and accurate information return Form 5471. The related income tax return may have been late filed with the Form 5471(s) attached or the related income tax return may have been filed timely but without a substantially complete Form 5471(s).

Considerations	Resources	6103 Protected Resources
<p>Review Form 5471s on their face for completeness</p> <p>IRC § 6038(a) requires certain information reported about foreign corporations and authorizes the Treasury to prescribe similar or related information that is necessary to carry out the provisions of the Code. Treasury Regulations under IRC §6038 describe such similar or related information and indicates that Form 5471 (including its instructions) will prescribe the manner in which all required information is reportable for each foreign corporation.</p> <p>The information required on Form 5471 must be furnished even though the information required may not affect the amount of any tax due under the IRC.</p> <p>Review USP's Form 5471s for the following errors on page one. If a Form 5471 is found that contains these errors, IRC § 6038 is not "substantially complied" with:</p> <ul style="list-style-type: none"> ▪ Item B: Category of the filer was omitted or incorrect, thus the Form 5471 schedules required to be completed can not be determined. 	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.6038-2(f) and (g) ▪ Treas. Reg. 1.6038-2(k)(4) Other penalties 	

Step 1 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 1: Verify Fact of Filing

It has been determined the taxpayer had a requirement to file a Form 5471. Before commencing a penalty case file, first verify whether the taxpayer filed a timely and accurate information return Form 5471. The related income tax return may have been late filed with the Form 5471(s) attached or the related income tax return may have been filed timely but without a substantially complete Form 5471(s).

Considerations	Resources	6103 Protected Resources
<p>Review Form 5471s on their face for completeness</p> <p>Item C: Percentage owned of voting stock of the foreign corporation was omitted (when no Item B category was indicated) or incorrect (when compared to the Item B category indicated), thus the Form 5471 schedules required to be completed can not be determined.</p> <p>Item 1a: Name or address of foreign corporation was omitted, thus other information provided on Form 5471 can not be associated with a specific foreign corporation.</p> <p>Items 1b(1) and 1b(2): Reference ID number was omitted when the EIN was not provided thus other information provided on Form 5471 can not be associated with a specific foreign corporation. (Note: The Reference ID number is only required for foreign corporation tax years beginning in 2012 and later.)</p>		

Step 1 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 1: Verify Fact of Filing

It has been determined the taxpayer had a requirement to file a Form 5471. Before commencing a penalty case file, first verify whether the taxpayer filed a timely and accurate information return Form 5471. The related income tax return may have been late filed with the Form 5471(s) attached or the related income tax return may have been filed timely but without a substantially complete Form 5471(s).

Considerations	Resources	6103 Protected Resources
<p>Review Form 5471s on their face for completeness</p> <p>Review USP's Form 5471(s) for the most common reasons for noncompliance with IRC § 6038:</p> <ul style="list-style-type: none"> ▪ stating that required information will be furnished upon request or audit, ▪ providing computer generated Form 5471(s) that were not IRS approved and did not conform to requirements, ▪ failing to provide financial statements for controlled foreign corporations, and ▪ providing consolidated financial statements of two or more foreign corporations. <p>According to a 1997 Field Service Advice (FSA), these common reasons relate to errors which were apparent from the face of a Form 5471.</p>	<ul style="list-style-type: none"> ▪ New Release IR-90-586 ▪ 2002 Non Docketed Service Advice Review (NSAR) 20167, 2002 WL 32167873 ▪ FSA 1997 WL 33381431, 1997 FSA Lexis 34 	

Step 1 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 1: Verify Fact of Filing

It has been determined the taxpayer had a requirement to file a Form 5471. Before commencing a penalty case file, first verify whether the taxpayer filed a timely and accurate information return Form 5471. The related income tax return may have been late filed with the Form 5471(s) attached or the related income tax return may have been filed timely but without a substantially complete Form 5471(s).

Considerations	Resources	6103 Protected Resources
<p>Review Form 5471s beyond their face for completeness</p> <ul style="list-style-type: none"> ▪ A 1997 FSA addresses whether USP “substantially complied” with IRC §6038 when significant understatements of related party purchases and/or sales were reported and significant inconsistencies were reported for earnings and profits. The FSA states that Congress did not intend that providing more of the required information than not (an aggregate approach) met substantial compliance. It was more important to determine substantial compliance on a significant item by significant item basis. ▪ CCA 200429007 provided a facts and circumstances analysis for “substantially incomplete” in contrast to a strict interpretation of the regulations that any over-reported or underreported transaction amount meant the form was “substantially incomplete”. The CCA provided seven factors to use in such analysis. Note - This CCA was issued in regard to Form 5472 but the analysis should also apply to Form 5471. 	<ul style="list-style-type: none"> ▪ FSA 1997 WL 33381431, 1997 FSA Lexis 34 ▪ CCA 200429007 	

Step 1 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 1: Verify Fact of Filing

It has been determined the taxpayer had a requirement to file a Form 5471. Before commencing a penalty case file, first verify whether the taxpayer filed a timely and accurate information return Form 5471. The related income tax return may have been late filed with the Form 5471(s) attached or the related income tax return may have been filed timely but without a substantially complete Form 5471(s).

Considerations	Resources	6103 Protected Resources
<ul style="list-style-type: none">Another CCA and its Summary advised that significant pieces of required information included (a) balance sheet and income statement amounts not in accord with U.S. Generally Accepted Accounting Principles (GAAP) and (b) income statement and income tax amounts that were not in both functional and U.S. currencies. Thus, the Form 5471 was not “substantially complete.”	<ul style="list-style-type: none">CCA 200645023	

Step 1 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 1: Verify Fact of Filing

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Considerations	Resources	6103 Protected Resources
<p>Review Form 5471s beyond their face for completeness</p> <p>The examiner should use the analyses in the previously listed guidance to determine whether an error was significant and whether the Service's ability to gather information necessary to conduct an effective examination was impacted. Both the 1997 FSA and CCA 200645023 focused on the significance of the required information. Depending on the complexity and magnitude of the error and the explanations provided by USP, an analysis using the seven factors in CCA 200429007 might be useful in determining whether the USP substantially complied with IRC §6038.</p>	<ul style="list-style-type: none"> ▪ CCA 200645023 ▪ CCA 200429007 	

Step 1 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 1: Verify Fact of Filing

It has been determined the taxpayer had a requirement to file a Form 5471. Before commencing a penalty case file, first verify whether the taxpayer filed a timely and accurate information return Form 5471. The related income tax return may have been late filed with the Form 5471(s) attached or the related income tax return may have been filed timely but without a substantially complete Form 5471(s).

Considerations	Resources	6103 Protected Resources
<p>Review Form 5471s beyond their face for completeness</p> <p>Generally, errors beyond the face of Form 5471(s) are noticed after you have researched information and/or obtained documentation while working issues identified on the exam risk analysis.</p> <p>The following guidance issued by the service provides analyses for determining whether the Form 5471 provided substantially complies with IRC §6038. Common to this guidance is the significance of the error (a) in amount and (b) in its impact on the Service's ability to obtain the information necessary to conduct effective exams.</p>		

Step 1 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 1: Verify Fact of Filing

It has been determined the taxpayer had a requirement to file a Form 5471. Before commencing a penalty case file, first verify whether the taxpayer filed a timely and accurate information return Form 5471. The related income tax return may have been late filed with the Form 5471(s) attached or the related income tax return may have been filed timely but without a substantially complete Form 5471(s).

Considerations	Resources	6103 Protected Resources
<p>Review Form 5471s beyond their face for completeness</p> <p># [REDACTED]</p> <p>[REDACTED].#</p> <p># [REDACTED]</p> <p>[REDACTED]#</p> <p> CAUTION: Form 5471s are required to be filed for dormant corporations. See Rev. Proc. 92-70</p>	<p>Rev. Proc. 92-70</p>	

Step 2

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 2: Penalty Case File Controls

You have determined that the taxpayer has failed to file a timely and accurate information return, the next step is to establish a penalty case file and prepare and issue the notice letter

Considerations	Resources	6103 Protected Resources
<p>Establish a penalty case file</p> <ul style="list-style-type: none"> ▪ Establish controls and prepare a penalty case file. This file must include the information that supports the requirements to file and establishes the Form 5471s have not been filed or not filed substantially complete. ▪ Submit Form 5345-D for managerial approval to establish controls: <ul style="list-style-type: none"> – Check box for “Control Penalty Investigation.” – MFT = PR, Activity Code = 586, Source Code = 99 – For Initial Penalty – MFT = PQ, Activity Code = 586, Source Code = 99, - For Continuation Penalty – ASED will default to 01/31/YY+4. Upon receipt of delinquent information returns, update ASED to three years from receipt date. – Reason for Request is “To control penalty investigations for Form 5471 returns not filed” ▪ Examiners charge time to the penalty case file. ▪ Issue the Notice Letter as discussed on the following slides. 	<ul style="list-style-type: none"> ▪ IRM 20.1.9.2 – Assessment Procedures for Penalties Not Subject to Deficiency Procedures ▪ Exhibit 20.1.9.1 – Quick Reference Guide to International Penalties ▪ IRM 20.1.9.2 (10) ▪ IRM 20.1.9.2(11) ▪ IRM 20.1.9.2(12) 	

Step 2 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 2: Penalty Case File Controls

You have determined that the taxpayer has failed to file a timely and accurate information return, the next step is to establish a penalty case file and prepare and issue the notice letter

Considerations	Resources	6103 Protected Resources
<p>Notice Letter Issuance</p> <p>As soon as you are aware of a USP that did not substantially comply with IRC § 6038, prepare a Notice (Pattern) Letter for Failure to File Form 5471. Additional notice letters can be prepared later as needed.</p> <p>The notice letter notifies USP that it failed to file a Form 5471 (i.e., filed late or not filed at all), or that the form filed was substantially incomplete. It explains that an Initial Penalty will be imposed. Also, that a Continuation Penalty applies for each 30-day period (or fraction thereof) beginning 90 days after the date of the letter until a substantially complete Form 5471 is provided.</p> <p>The notice letter is addressed to the person required to file Form 5471. The notice letter should indicate the name of the Examiner as the person to contact and to refer in the reply. Also, the examiner's phone number should be included.</p> <p>Include in the body of the notice letter the complete legal names of each foreign corporation for which a failure occurred. If necessary, a list of these legal names can be attached as page two.</p> <p>In the body of the notice letter, include the tax year(s) of the person required to file Form 5471s. If failures occurred in only one tax year for some foreign corporations and in additional tax years for others, then prepare more than one notice letter so that the relevant tax years are identified.</p>	<ul style="list-style-type: none"> ▪ IRM Exhibit 20.1.9-6 Pattern Letter for Failure to File Form 5471 	

Step 2 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 2: Penalty Case File Controls

You have determined that the taxpayer has failed to file a timely and accurate information return, the next step is to establish a penalty case file and prepare and issue the notice letter

Considerations	Resources	6103 Protected Resources
<p>Notice Letter Issuance</p> <ul style="list-style-type: none"> ▪ Notice letters must be signed by an examination group manager in SB/SE or a revenue agent in LB&I. ▪ Mail the notice letter to the person required to file as soon as possible for two reasons: 1) To obtain the information early to effectively conduct the exam; and 2) To start the 90-day notice period required by IRC § 6038(c)(1). Typically, USPs will provide corrected Form 5471(s) as soon as possible after receipt of the notice letter to avoid accumulating Continuation Penalties. ▪ Per the regulations, the notice letter must be mailed to the person required to file, not its representative. If not properly mailed, the USP might assert that the notice was ineffective at Appeals or in court. Consider using registered or certified mail “return receipt requested” to provide evidence that the notice letter was received. ▪ Keep a copy of all notice letters issued, and the certified or registered return receipts, in the case file. ▪ After the notice letter is mailed, do not discuss the notice with the representative until you review the Form 2848, <i>Power of Attorney and Declaration of Representative</i>. Verify the representative has authorization to represent the USP on the IRC § 6038 penalties. If not, consider suggesting that USP issue a separate Form 2848. 	<ul style="list-style-type: none"> ▪ IRM 20.1.9.2 (13) ▪ Treas. Reg. 1.6038-2(k)(1)(ii) 	

Step 2 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 2: Penalty Case File Controls

You have determined that the taxpayer has failed to file a timely and accurate information return, the next step is to establish a penalty case file and prepare and issue the notice letter

Considerations	Resources	6103 Protected Resources
<ul style="list-style-type: none"> ▪ Although you cannot discuss the civil penalties under IRC § 6038 with an unauthorized representative, you may obtain information to proceed with the penalty development. The representative may have details about the Form 5471s that are helpful regarding their compliance with IRC §6038 and enable you to effectively conduct the exam. ▪ Consider referring USP or its authorized representative to Treas. Reg. § 1.6038-2(k)(4), which sets forth the requirements for a valid reasonable cause statement. <p> CAUTION: There are no provisions under IRC § 6038 for an extension of the 90 day period to comply with a notice letter.</p>	<ul style="list-style-type: none"> ▪ <u>Treas. Reg. 1.6038-2(k)</u>– Reasonable cause provision 	

Step 2 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 2: Penalty Case File Controls

You have determined that the taxpayer has failed to file a timely and accurate information return, the next step is to establish a penalty case file and prepare and issue the notice letter

Considerations	Resources	6103 Protected Resources
<p>Review Form 5471s submitted in response to the notice letter</p> <ul style="list-style-type: none">▪ Date stamp Form 5471s as they are received in response to the notice letter. If such Form 5471 is substantially correct, the stamped date will determine whether -the Continuation Penalties apply and the amount of the penalty.▪ Review the Form 5471s to determine whether they substantially comply with IRC §6038. If not, then the Continuation Penalty periods are still in effect.▪ If you receive a Form 5471 you determine does not substantially comply with IRC § 6038, consider sending a subsequent letter to the USP advising of the failure. The letter will provide support in Appeals and in court that USP had knowledge that the subsequently submitted Form 5471s were substantially incomplete.		

Step 2 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 2: Penalty Case File Controls

You have determined that the taxpayer has failed to file a timely and accurate information return, the next step is to establish a penalty case file and prepare and issue the notice letter

Considerations	Resources	6103 Protected Resources
<p>Review Form 5471s submitted in response to the notice letter</p> <p>Consider using language, similar to the following, in the follow up letter for Form 5471s that were substantially incomplete:</p> <p>“This is to notify you that the attached Form 5471 for [name of foreign corporation] was not substantially complete. If you fail to file a substantially complete Form 5471 within 90 days after the date the notice letter was issued ([date]), an additional \$10,000 penalty will be imposed for each 30-day period (or fraction thereof) until a substantially complete Form 5471 is filed, but in an amount not to exceed \$50,000.”</p> <p>Retain a copy of the subsequent letter in the case file.</p> <p>Note: For Form 5471s that were not originally provided and not provided in response to the notice letter, there is no need to further advise the person responsible for filing that a substantially complete Form 5471 was not filed.</p>		

Step 3

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 3: Penalty Determination

The penalty case file has been established, the Notice Letter has been mailed to the UPS, and Form 5471s may or may not have now been filed substantially correct. Now you must determine what penalties, if any, apply, how they are computed, and whether the taxpayer can argue reasonable cause for failure to file.

Considerations	Resources	6103 Protected Resources
<p>Penalty Structure</p> <p>If Form 5471s are not filed on or before the due date (including extensions) of the USP's income tax return or if the applicable form does not include all the information required or includes incorrect information, the Initial and Continuation Penalties may apply as follows:</p> <p>The penalty per IRC § 6038(b) for failure to furnish all the required information timely on a Form 5471 is:</p> <ul style="list-style-type: none"> ▪ \$10,000 per Form 5471 that the U.S. shareholder fails to file ▪ If the information is not filed within 90 days after notice of the failure to the U.S. shareholder, additional penalties of \$10,000 apply per failure to file for each 30-day period, or fraction thereof, during which the failure continues. The maximum additional penalty for each Form 5471 is \$50,000. ▪ The maximum total penalty for each Failure To File Form 5471 is \$60,000 (\$10,000 Initial Penalty and the \$50,000 Continuation Penalty). <p>There is also a penalty under IRC § 6038(c) which results in the reduction of foreign tax credits, but this is beyond the scope of this IPS unit.</p>	<ul style="list-style-type: none"> ▪ IRC 6038(a) ▪ IRM 20.1.9.3.4 ▪ IRC 6038(b) ▪ IRC 6038(c) 	

Step 3 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 3: Penalty Determination

The penalty case file has been established, the Notice Letter has been mailed to the UPS, and Form 5471s may or may not have now been filed substantially correct. Now you must determine what penalties, if any, apply, how they are computed, and whether the taxpayer can argue reasonable cause for failure to file.

Considerations	Resources	6103 Protected Resources
<p>Reasonable Cause Exception</p> <ul style="list-style-type: none"> ▪ No penalty shall be imposed under IRC § 6038(b) on any failure which is shown to be due to reasonable cause and not due to willful neglect. ▪ Regarding the facts alleged to support reasonable cause, determine whether USP's supporting documents (and events) related to those facts were dated (or occurred) after the latest date that reasonable cause was relevant. Reasonable cause could not exist earlier than the due date for filing Form 5471 or the date of the Form 5471 notice letter. ▪ As previously discussed, there are two different penalties: the Initial Penalty and the Continuation Penalty. While both penalties are described within IRC §6038(b), only the Initial Penalty can be considered for the reasonable cause exception 	<ul style="list-style-type: none"> ▪ IRC 6038(c)(4)(B) ▪ IRC 6038(c)(4)(B) Special rules ▪ Treas. Reg. 1.6038-2(k)(3)(i) ▪ IRM 20.1.9.3.5 	

Step 3 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 3: Penalty Determination

The penalty case file has been established, the Notice Letter has been mailed to the UPS, and Form 5471s may or may not have now been filed substantially correct. Now you must determine what penalties, if any, apply, how they are computed, and whether the taxpayer can argue reasonable cause for failure to file.

Considerations	Resources	6103 Protected Resources
<ul style="list-style-type: none"> ▪ Determine whether USP’s statement of reasonable cause (for the failure to file a Form 5471, filing it late or filing it substantially incomplete) meets the regulation requirements. That statement must: <ul style="list-style-type: none"> – be in writing – provide all of the facts alleged as reasonable cause, and – contain a declaration that the statement was made under penalties of perjury. <p>If the reasonable cause statement did not include the declaration, advise USP that the statement does not satisfy the requirements of the regulations.</p>	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.6038-2(k)(3)(ii) Reasonable cause 	

Step 3 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 3: Penalty Determination

The penalty case file has been established, the Notice Letter has been mailed to the UPS, and Form 5471s may or may not have now been filed substantially correct. Now you must determine what penalties, if any, apply, how they are computed, and whether the taxpayer can argue reasonable cause for failure to file.

Considerations	Resources	6103 Protected Resources
<p>Reasonable Cause Exception</p> <p>Determine whether USP is in full compliance with IRC § 6038 reporting and record keeping requirements for all tax years open under the statutes. Request USP to file, furnish, report or maintain the information required under IRC § 6038 before considering any reasonable cause requests.</p>	<ul style="list-style-type: none">▪ IRM Exhibit 20.1.9-5 Reasonable Cause Relief	

Step 3 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 3: Penalty Determination

The penalty case file has been established, the Notice Letter has been mailed to the UPS, and Form 5471s may or may not have now been filed substantially correct. Now you must determine what penalties, if any, apply, how they are computed, and whether the taxpayer can argue reasonable cause for failure to file.

Considerations	Resources	6103 Protected Resources
<p>Review the definition and factors of reasonable cause</p> <p>Neither IRC § 6038, nor the regulations thereunder, defines “reasonable cause” for the failure to timely file a substantially complete Form 5471. The Committee Reports on the Omnibus Budget Reconciliation Act of 1989 stated that “reasonable cause exists if significant mitigating factors are present, such as the fact that a person has an established history of complying with the information reporting requirements.”</p> <p>The Code provides “reasonable cause” as a defense to several penalties. For example:</p> <ul style="list-style-type: none"> ▪ IRC § 6651(a) - Failure to file tax return, ▪ IRC § 6652 - Failure to file certain information returns, and ▪ IRC § 6679 - Failure to file returns including foreign corporations. <p>However, those statutes do not define “reasonable cause” either.</p> <ul style="list-style-type: none"> ▪ IRC § 6651(a) provides the penalty may be avoided if USP demonstrated that the failure was attributed to reasonable cause and not due to willful neglect. 	<ul style="list-style-type: none"> ▪ IRC 6651(a) ▪ IRC 6652 ▪ IRC 6679 	

Step 3 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 3: Penalty Determination

The penalty case file has been established, the Notice Letter has been mailed to the UPS, and Form 5471s may or may not have now been filed substantially correct. Now you must determine what penalties, if any, apply, how they are computed, and whether the taxpayer can argue reasonable cause for failure to file.

Considerations	Resources	6103 Protected Resources
<p>Review the definition and factors of reasonable cause</p> <ul style="list-style-type: none"> ▪ In <i>US v. Boyle</i>, the Supreme Court noted that Treas. Reg. § 301.6651(c)(1) (1984) required USP to demonstrate that it exercised ordinary business care and prudence but nevertheless was unable to file the return within the prescribed time. “Thus, the Service's correlation of ‘reasonable cause’ with ‘ordinary business care and prudence’ is consistent with Congress' intent, and over 40 years of case law as well.” ▪ In FSA 1997 WL 33381431, relying on <i>US v Nordbrock</i> and <i>Firestone v. Howerton</i>, it was noted that in the absence of a definition, courts generally agree that similar terms appearing in different sections of a statute should be interpreted the same way. The FSA stated that there was no reason to define reasonable cause under Code IRC § 6038 differently than exercising ordinary business care and prudence but nevertheless unable to file a substantially complete Form 5471. 	<ul style="list-style-type: none"> ▪ <i>U. S. v. Boyle</i>, 469 U.S. 241(1985) ▪ <i>U.S. v. Nordbrock</i>, 38 F. 3d 440 (9th Cir. 1994) ▪ <i>Firestone v. Howerton</i>, 671 F. 2d 317 (9th Cir. 1982). ▪ FSA 1997 WL 33381431. 	

Step 3 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 3: Penalty Determination

The penalty case file has been established, the Notice Letter has been mailed to the UPS, and Form 5471s may or may not have now been filed substantially correct. Now you must determine what penalties, if any, apply, how they are computed, and whether the taxpayer can argue reasonable cause for failure to file.

Considerations	Resources	6103 Protected Resources
<ul style="list-style-type: none"> ▪ In <i>Congdon v. US</i>, the court gave a good explanation of what is needed for reasonable cause analysis regarding Form 5471. The court referred to the IRM and the Code and stated that, “the elements that must be present to constitute reasonable cause are a question of law, but whether those elements are present in a given situation is a question of fact. To demonstrate reasonable cause, the plaintiff must show that he exercised ordinary business care and prudence.” 	<ul style="list-style-type: none"> ▪ <i>Congdon v. United States</i>, No. 4:09CV289, 2011 WL 3880524 (E.D. Tex. Aug. 11, 2011) 	

Step 3 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 3: Penalty Determination

The penalty case file has been established, the Notice Letter has been mailed to the UPS, and Form 5471s may or may not have now been filed substantially correct. Now you must determine what penalties, if any, apply, how they are computed, and whether the taxpayer can argue reasonable cause for failure to file.

Considerations	Resources	6103 Protected Resources
<p>Review the definition and factors of reasonable cause</p> <ul style="list-style-type: none"> ▪ The IRM provides factors to consider to determine whether USP exercised ordinary business care and prudence. Examples of what might be reasonable cause include: <ul style="list-style-type: none"> – Erroneous advice or reliance, – Unable to obtain records, and – Death, serious illness, or unavoidable absence. ▪ Ignorance of the law, by itself, is not reasonable cause. However, in conjunction with other factors, it might be. Such other factors to consider include: USP’s education, if USP was penalized before, if USP could not reasonably be expected to know of recent changes in the tax law or forms, and the level of complexity of a tax or compliance issue. 	<ul style="list-style-type: none"> ▪ IRM 20.1.1.3.2.2.5 ▪ CCN 2004-036 ▪ IRM 20.1.1.3.2.2.3 ▪ IRM 20.1.1.3.2.2.1 ▪ IRM 20.1.1.3.2.2.6 	

Step 3 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 3: Penalty Determination

The penalty case file has been established, the Notice Letter has been mailed to the UPS, and Form 5471s may or may not have now been filed substantially correct. Now you must determine what penalties, if any, apply, how they are computed, and whether the taxpayer can argue reasonable cause for failure to file.

Considerations	Resources	6103 Protected Resources
<ul style="list-style-type: none"> ▪ The fact that a foreign jurisdiction would impose a civil or criminal penalty on the taxpayer (or any other person) for disclosing the required information and/or refusal on the part of a foreign trustee to provide information for any other reason does not constitute reasonable cause. ▪ Generally, the most important factor in determining whether USP has reasonable cause and acted in good faith was the extent of USP's effort to report the proper tax liability. <p> CONSULTATION: Contact Counsel for assistance in evaluating whether USP had reasonable cause.</p>	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.6664-4(b)(1) 	

Step 4

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 4: Penalty Application/Closing Procedures

The Notice Letter has been issued and you understand the penalty determination factors, the final steps in this process are penalty application or non-application, and case closing procedures.

Considerations	Resources	6103 Protected Resources
<p>Application of Penalties – Initial Penalty</p> <ul style="list-style-type: none"> ▪ Now that you understand the penalty structure and reasonable cause considerations as discussed in step 3, let us discuss how these penalties are applied. Examiners must first take steps to secure documentation to support the USP is required to file the returns. Keep this documentation in the penalty file. Second, when the examiner secures a delinquent Form 5471, the examiner must determine whether it provides all required information and is accurate. If inaccurate or incomplete, the examiner must inform the taxpayer that the return is not considered filed until it is complete and accurate. ▪ Once it is determined penalties are applicable, the penalties imposed by IRC §6038 are asserted on Form 8278 <i>Assessment and Abatement of Miscellaneous Civil Penalties</i>. The Initial Penalty is asserted by examiners on Form 8278 using Penalty Reference Number (PRN) 623. 	<ul style="list-style-type: none"> ▪ IRM 20.1.9.3.3 ▪ Exhibit 20.1.9-3 	

Step 4 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 4: Penalty Application/Closing Procedures

The Notice Letter has been issued and you understand the penalty determination factors, the final steps in this process are penalty application or non-application, and case closing procedures.

Considerations	Resources	6103 Protected Resources
<ul style="list-style-type: none"> ▪ If the Continuation Penalty applies, the Continuation Penalties are asserted on Form 8278 using PRN 619. <p>These penalties <u>should not</u> be entered on Form 870, <i>Waiver of Restrictions on Assessment and Collection of Deficiency in Tax & Acceptance of Overassessment</i>, Form 4549, <i>Income Tax Examination Changes</i>, Form 4549-A <i>Income Tax Discrepancy Adjustments</i>, or any other examination report</p>	<ul style="list-style-type: none"> ▪ IRM 20.1.9.3.4 	

Step 4 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 4: Penalty Application/Closing Procedures

The Notice Letter has been issued and you understand the penalty determination factors, the final steps in this process are penalty application or non-application, and case closing procedures.

Considerations	Resources	6103 Protected Resources
<p>Application of Penalties – Continuation Penalty</p> <p>The maximum Continuation Penalty for IRC § 6038(b) is \$50,000 per required Form 5471. This is in addition to the Initial Penalty, making the total possible penalty \$60,000 per required form.</p>	<ul style="list-style-type: none">▪ IRM 20.1.9.3.4	

Step 4 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 4: Penalty Application/Closing Procedures

The Notice Letter has been issued and you understand the penalty determination factors, the final steps in this process are penalty application or non-application, and case closing procedures.

Considerations	Resources	6103 Protected Resources
<p>Form 8278 – Assessment and Abatement of Miscellaneous Civil Penalties</p> <ul style="list-style-type: none"> ▪ The assessment document for international penalties is Form 8278. Failure to file under IRC § 6038 has a penalty section on the form which covers both the Initial and the Continuation Penalties. ▪ If a Continuation Penalty is proposed in conjunction with an Initial Penalty, a separate Form 8278 is required for each type of penalty. Enclose a computation of the penalty and the applicable code section for each computation. ▪ Prepare a separate Form 8278 for each tax period. Calculate the total penalty due per year. ▪ The examiner will enter the dollar amount of the penalty on Form 8278 and attach Form 886-A, <i>Explanation of Items</i>. ▪ The taxpayer's signature is <u>not</u> required with respect to these penalties. ▪ Manager's signature is <u>required</u> in block 11a to meet the provision of IRC § 6751. 	<ul style="list-style-type: none"> ▪ IRM 20.1.9.2.1 	

Step 4 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 4: Penalty Application/Closing Procedures

The Notice Letter has been issued and you understand the penalty determination factors, the final steps in this process are penalty application or non-application, and case closing procedures.

Considerations	Resources	6103 Protected Resources
<p>Payments</p> <ul style="list-style-type: none"> ▪ Use Form 3244, <i>Payment Posting Voucher</i>, to list the payment amount, with Transaction Code (TC) 640 if the payment is received prior to assessment or with TC 670 if the payment is received after the assessment. Include the appropriate Designated Payment Code per IRM 21.3.4.7.1.3 ▪ The payment will be posted to MFT 55 for Individuals and MFT 13 for Entities 	<ul style="list-style-type: none"> ▪ IRM 20.1.9.2(21) Payments ▪ IRM 21.3.4.7.1.3 	

Step 4 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 4: Penalty Application/Closing Procedures

The Notice Letter has been issued and you understand the penalty determination factors, the final steps in this process are penalty application or non-application, and case closing procedures.

Considerations	Resources	6103 Protected Resources
<p>No filing requirement or accepting the filing without penalties</p> <ul style="list-style-type: none"> ▪ The examiner should complete Form 8278. <ul style="list-style-type: none"> – On Form 8278, enter “1” as the number of violations on the applicable penalty line and enter “0.1” as the amount assessed. – In the “Remarks” box enter “Blocking Series 52; Reason Code 62; Hold Code 0; Penalty Reason Code 0XX” (Refer to Document 6209, sections 8 Penalty Abatement/Suppression PRC chart for penalty reason codes). – Also note: Reasonable cause was considered and allowed”, or “No requirement to file”. A penalty reason code (PRC) is required to indicate why a penalty is being abated (penalty relief is granted or suppressed). 	<ul style="list-style-type: none"> ▪ IRM Exhibit 20.1.1-2 – Penalty Reason Code Chart 	

Step 4 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 4: Penalty Application/Closing Procedures

The Notice Letter has been issued and you understand the penalty determination factors, the final steps in this process are penalty application or non-application, and case closing procedures.

Considerations	Resources	6103 Protected Resources
<p>Prepare Form 886-A – <i>Explanation of Items</i></p> <p>Prepare Form 886-A - for failure to file Form 5471. Form 886-A should contain sections for:</p> <ul style="list-style-type: none"> - Facts - include all pertinent information to establish that the USP had a Form 8865 filing requirement and the USP failed to timely file or filed an inaccurate and incomplete form. -Law – Provide all relevant law, including IRC Sections, IRC Regulations and court cases. -Taxpayer's Position - including any reasonable cause request -Service's Position - including a detailed determination on reasonable cause <p>It is important to include all relevant information on Form 886-A. Form 886-A will be sent to the Campus for the penalty to be assessment or and will be forwarded sent to Appeals if USP chooses to appeal the penalty.</p> <p>A copy of Form 886-A should be provided to USP.</p>		

Step 4 (cont'd)

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Step 4: Penalty Application/Closing Procedures

The Notice Letter has been issued and you understand the penalty determination factors, the final steps in this process are penalty application or non-application, and case closing procedures.

Considerations	Resources	6103 Protected Resources
<p>Miscellaneous Case Closing Considerations</p> <ul style="list-style-type: none">▪ The case file should contain all working papers, correspondences and activity record in addition to the Form 8278 and Form 886-A.▪ The case file will be closed with a Form 3198.▪ The ERCS PR record may have to remain open if it represents other penalties besides those associated with a Form 5471. If so, ensure the earliest expiring penalty statute is reflected in ERCS.		

Other Considerations / Impact to Audit

Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty

Considerations	Resources	6103 Protected Resources
<p>Specific Powers of Attorney (POA) or Authorization to Disclose Tax Information:</p> <p>A Form 2848 <i>Power of Attorney and Declaration of Representative</i> (POA) is required prior to discussing penalty issues with a person other than the person subject to the assessment or required to file the Form 5471(s). The POA for the income tax return examination is not valid for the penalty issue under IRC § 6038. A separate Form 2048 can be secured for the IRC §6038 penalty considerations.</p> <p>Form 2848 Item #3 “Description of Matter” should include words similar to “Miscellaneous Penalty Under IRC § 6038.”</p>		

Training and Additional Resources

Chapter 11.1.2 CFC Information Reporting Issues

Type of Resource	Description(s) and/or Instructions for Accessing	References
Online treatise	<p>IRC § 6038 discussions of reporting requirements for USP with interest in foreign corporations.</p> <p>The treatise is included in LB&I's Westlaw subscription in the International resources section. Expand the section to show all resources to find Bittker & Lokken: <u>Federal Taxation of Income, Estates and Gifts</u>. Click on:</p> <ul style="list-style-type: none"> ▪ Table of Contents, ▪ Part 9 (Foreign Income and Foreign Taxpayers), and ▪ Chapter 65 (International Tax Enforcement). <p>Then, scroll to ¶ 65.5.4 Reporting Requirements for US Persons with Interests in Foreign Corporations and Partnerships.</p>	Fed. Tax'n Inc, Est and Gift
Other training materials	<p>The document provides guidance on when to open and how to close a penalty case. Also, it addresses where penalty work papers are placed in case files.</p> <p>The document is located in the Reference Materials section of the Information Gathering IPN SharePoint website.</p>	Penalty Case File Procedures

Glossary of Terms and Acronyms

Acronym	Definition
CCA	Chief Counsel Advice
CCN	Chief Counsel Notice
CFC	Controlled Foreign Corporation
Code	Internal Revenue Code
FSA	Field Service Advice
GAAP	Generally Accepted Accounting Procedures
IDRS	Integrated Data Retrieval System
IRC	Internal Revenue Code
LB&I	Large Business & International
MFT	Master File Transaction
NSAR	Non Docketed Service Advice Review
POA	Power of Attorney
PRN	Penalty Reference Number
SEC	Securities Exchange Commission
TC	Transaction Code
USP	United States Person

Index of Related Issues (cont'd)

Issue	Associated UIL(s)	References
Overview of Subpart F Income for U.S. Individual Shareholders	9433.01-01	FEN/9433.01_09(2013)
General Subpart F Computational Issues	9433.01-01	To be developed
Determination of U.S. Shareholder and CFC Status	9433.01-01	FEN/9433.01_03(2013)
Failure to File the Form 5471 – Category 2 & 3 Filers – Monetary Penalty	9433.01-02	In process as of 4/15
Failure to File the Form 926 – Monetary Penalty	9433.01	In process as of 4/15
Determination of PFIC Status	9433.02	In revision as of 4/15
Check-The-Box Rules for Foreign Entities	TBD	To be developed
Section 956 – Investments in US Property	9433.01-01	To be developed
Dispositions of a CFC - IRC1248	9433.01-01	To be developed
Distributions from a CFC	9433.01-01	To be developed
IRC 962 Election - Election by individuals to be subject to tax at corporate rates	9433.01-01	To be developed
Foreign Personal Holding Company Income	9433.01-01	In process as of 4/15
Foreign Base Company Sales Income	9433.01-01	To be developed
Foreign Base Company Services Income	9433.01-01	To be developed

Index of Related Issues

Issue	Associated UIL(s)	References
Information Gathering's Considering a reduction to the foreign tax credits of a US shareholder that did not file Form 5471 for a foreign corporation (IPS Unit in production)	9560.03	To be developed
Information Gathering's Considering penalties when a US shareholder did not file Form 5471 for a controlled foreign corporation	9560.01	In process as of 4/15