

To Report or Not to Report, That Is the Question

by *Anthony Delfiner and Hal Margolit*

Tax filing season for 2019 returns is finally here! It's time to make good on your New Year's resolution to file your tax returns earlier this year. We recommend getting a head start in gathering the tax information necessary to prepare your personal and business tax filings. Figuring out which forms you have to file is part of this process.

An area of tax compliance that is fraught with filing pitfalls is foreign informational reporting. In our experience, businesses and individuals may be unaware of their responsibilities to file foreign informational tax returns. Some may be informed of the rules, but due to cultural differences believe that an account or investment is not considered foreign. Foreign informational filing requirements must be considered to make sure nothing slips through the cracks. Ignoring or forgetting to address these filings can be very costly. For example, the penalty for failure to file an FBAR (Report of Foreign Bank and Financial Accounts) report can be as much as \$10,000 for a non-willful violation; willful violations can cost even more.

The following is a list of IRS foreign informational reporting forms that you may need to consider as part of your tax filing requirements this year and what could potentially trigger an obligation to file FinCen Form 114 (Report of Foreign Bank and Financial Accounts). If you are a United States person and either own or have control of a bank/financial account in another country, you need to consider filing this form. This filing generally comes into play if the aggregate of your accounts exceeds \$10,000 at any time during the calendar year.

- **Form 8938** (Statement of Specified Foreign Financial Assets) – U.S. taxpayers need to file this form to report specified foreign financial assets (such as financial accounts maintained by a foreign institution, interests in foreign social security, foreign corporate stock, an interest in a foreign entity or a financial instru-

ment issued by a non-US person). There are varying requirements as to who must file and the thresholds that require filing. For example, if you are married filing jointly and living in the US, you may need to file this form if the value of your foreign financial assets exceeds \$100,000 on the last day of the tax year or \$150,000 at any time during the year.

- **Forms 5471 and 5472** (Information Return of US Persons with Respect to Certain Foreign Corporations and Return of Foreign-Owned US Corporation) – If you or your company own or are an officer of a foreign corporation, or your corporation is owned by a foreign shareholder, you may need to file one of these forms. The filings are long and complex, requiring a variety of disclosures. There also may be potential US tax implications due to the inclusion of foreign source income.

- **Form 8621** (Return by US Shareholder of a Passive Foreign Investment Company) – Did you ever wonder what needed to be done with the thousands of pages of additional information you received with your partnership Schedule K-1? Some of these disclosures may relate to income distributions from a Passive Foreign Investment Company, otherwise known as a PFIC. If your partnership has invested in such a foreign entity, you may be required to file this form with your tax filings and even calculate additional tax and interest based upon information disclosed on this form. Foreign mutual funds are also considered PFICs. Failure to file the form can result in missing tax advantageous elections for PFICs, which can be costly. Also, your return will not be considered complete and it would not be subject to the statute of limitations. This means your tax return can be subject to IRS audit at any time, regardless of when you filed it.

- **Form 926** (Return by US Transfer of Property to a Foreign Corporation) – This is another foreign return you may be required to prepare based on supplemental information provided on your Schedule K-1. If you or an investment owned by you makes a transfer of property

(this includes cash) to a foreign corporation, you may be required to file this form. Transfers qualify if the transferor owns, directly or indirectly, at least 10% of the voting power of the foreign corporation, or if the total amount transferred to the foreign corporation during a 12-month period is more than \$100,000. If not filed, penalties can be as much as 10% of the fair market value of the property transferred (to a maximum amount of \$100,000).

- **Forms 3520 and 3520-A** (Annual Return to Report Transactions with Foreign Trusts and Annual Informational Return of Foreign Trust with a US Owner) – A 3520 filing is required if a US person forms a foreign trust, transfers assets to a foreign trust, receives distributions from a foreign trust, or receives a gift or bequest from a foreign person in excess of \$100,000 or \$16,076 from a foreign partnership or corporation. Trustees of foreign grantor trusts with US grantors are required to file form 3520-A, which reports the income and balance sheet of the trust. Failure to file these forms can be expensive; 3520 penalties can be as much as 35% of the gross value of any distributions received, or 5% per month of the amount of certain foreign gifts, up to 25%. The 3520-A is no better--penalties can amount to 5% of the value of the trust's assets attributed to the US grantor.

The above list is not meant to be a complete list of foreign informational reporting forms you need to be cognizant of. These informational filings can be confusing and are often complex. We deal with these filings and issues on a consistent basis for our clients, helping them understand their reporting obligations and cut through their complexities.

If you currently have or have had foreign filing compliance issues, please contact Anthony Delfiner at 267-768-3817 or Hal Margolit at 267-768-3826 for assistance.

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