

# Estate Planning Considerations for Dual Residents: *Selected Reporting Requirements*

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Published on [www.lorman.com](http://www.lorman.com) - November 2020

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## **A. Selected Reporting Requirements**

### **1. Form 8840, Closer Connection Exception Statement for Aliens.**

This form is generally required to be filed by an NRA claiming a closer connection exception to U.S. residency. An NRA must provide general information to establish closer connections to his or her foreign tax home.

Timing and Penalties. Form 8840 is due with and at the same time as an NRA's income tax return. Failure to file this form results in ineligibility to claim the exception.

### **2. Form 3520, Annual Return to Report Transactions with Foreign Trusts and Receipt of Certain Foreign Gifts**

**(i) Reportable Events.** A U.S. person is required to file Form 3520 if such person:

- (1)** created or funded a foreign trust;
- (2)** is treated as the owner of a foreign trust;
- (3)** received a distribution from a foreign trust;
- (4)** made loans to a foreign trust;
- (5)** received gifts or bequests from an NRA greater than \$100,000;
- (6)** received gifts from a foreign corporation greater than \$16,649 (for 2020).

**(ii) Timing and Penalties.** Form 3520 is due at the same time as a U.S. person's income tax return. The following penalties are imposed for failure to comply with the Form 3520's filing requirements:

- (1) Transactions with Foreign Trusts (I.R.C. § 6677).** If Form 3520 is not timely filed or contains incomplete or incorrect information, the initial penalty is equal to

the greater of **\$10,000** or the following (as applicable):

- (a) 35%** of the gross value of any property transferred to a foreign trust;
- (b) 35%** of the gross value of the distribution received from a foreign trust;
- (c) 5%** of the gross value of the portion of the foreign trust's assets treated as owned by a U.S. person.<sup>1</sup>

Additional penalties may be imposed if the noncompliance continues for more than 90 days after the IRS mails a notice of failure to comply with the required reporting.

- (2) Receipt of Foreign Gifts or Bequests (I.R.C. § 6039F).** For failure to timely report foreign gifts/bequests from an NRA or a foreign corporation, a penalty of 5% of the amount of such foreign gifts/bequests applies for each month the failure continues, up to a maximum of 25%.

- (iii) Reasonable Cause Exception.** The above-described penalties will not be imposed if the U.S. person demonstrates that the failure is due to reasonable cause and not due to willful neglect.<sup>2</sup>

**3. Form 3520-A, Annual Information Return of Foreign Trust with a U.S. Owner.** This form generally requires the disclosure of the following:

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<sup>1</sup> I.R.C. § 6677(a).

<sup>2</sup> I.R.C. §§ 6677(d) and 6039F(c)(2).

(i) information about the foreign trust (including its income statement); (ii) information about any U.S. owner and the foreign trust's U.S. beneficiaries; and (iii) any distribution to its U.S. owners and U.S. beneficiaries. The form is required to be filed by the trustee of the foreign trust. However, each U.S. owner must ensure that the foreign trust complies with the filing requirement and furnishes annual statements to its U.S. beneficiaries.

Timing and Penalties. Form 3520-A is due by the 15th day of the third month following the foreign trust's taxable year. The trustee of the foreign trust must also furnish a foreign grantor trust income statement and foreign grantor trust beneficiary statement to each of its U.S. owners and U.S. beneficiaries by that date. Failure to file Form 3520-A may result in imposition of a penalty equal to the greater of \$10,000 or 5% of the gross value of the trust owned by the U.S. person. The penalty can be doubled if the U.S. owner also fails to file IRS Form 3520.

**4. Form 8621, Information Return by a Shareholder of a Passive Foreign Investment Company or Qualified Electing Fund.**

**(i) Reportable Events.** A U.S. person who is a direct or indirect owner of a PFIC is required to file Form 8621 if such person:

- (1)** Receives a direct or indirect distribution from a PFIC;
- (2)** Recognizes gain on disposition of PFIC stock;
- (3)** Reports information with respect to a QEF election or mark-to-market election;

- (4) Makes any of the elections listed in Part II of the Form (e.g., election to treat the PFIC as a QEF, election to extend time for payment of tax, deemed sale election, etc.); or
  - (5) Is required to file an annual report under I.R.C. § 1298(f).
- (ii) Timing and Penalties. Form 8621 is due with and at the same time as a U.S. person's income tax return. There are no stated penalties for failure to file the form, but the statute of limitations can be tolled on the entire return. Furthermore, a U.S. individual shareholder who fails to disclose a PFIC investment on either Form 8621 or Form 8938 when required can be subject to a \$10,000 penalty under IRC § 6038D(d).

**5. Form 5471, Information Return of U.S. Persons with respect to Certain Foreign Corporations.**

- (i) Reportable Events. A U.S. person is required to file Form 5471 for each foreign corporation in any of the following cases:
- (1) If a U.S. person is a U.S. shareholder of an I.R.C. § 965 specified foreign corporation at any time during any tax year of the foreign corporation;
  - (2) If a U.S. Person is an officer or a director of a foreign corporation and has acquired 10% or more (by value or by vote) of the foreign corporation;
  - (3) If a U.S. person (i) acquires 10% of ownership in a foreign corporation; (ii) acquires shares, that when added to the shares owned, equal or exceed 10% or

more of ownership in a foreign corporation; or (iii) disposes of shares in a foreign corporation that reduce ownership to less than 10%.

(4) If a U.S. person is a U.S. shareholder who had control (more than 50% of ownership by value or by vote) of a foreign corporation during the annual accounting period of the foreign corporation; and

(5) If a U.S. person owns 10% or more of shares of all classes of stock of a CFC.

(ii) Timing and Penalties. Form 5471 is due with and at the same time as a U.S. person's income tax return. A \$10,000 penalty is imposed for failure to timely file the form.

6. **Form 8938, Statement of Specified Foreign Financial Assets.** This form is required to be filed by any U.S. person owning a "specified foreign financial asset". The reporting threshold depends on whether the individual resides in the U.S. or files a joint income tax return with his or her spouse. "Specified foreign financial assets" generally include non-U.S. stock and securities, mutual funds, bank accounts and financial instruments and contracts. Interestingly, non-U.S. real estate is excluded (but not related leases).

Timing and Penalties. Form 8938 is due with and at the same time as a U.S. person's income tax return. A penalty of \$10,000 is imposed for failure to file in a timely, complete manner. If the IRS issues a notice of failure and the U.S. person fails to cure the noncompliance within 90 days, an



additional penalty is charged every 30 days thereafter up to a maximum of \$50,000.

7. **FinCen Form 114, Report of Foreign Bank and Financial Accounts ("FBAR")**. This report is required to be filed annually by a U.S. person with a financial interest in or signature authority over foreign financial accounts (e.g., bank accounts, brokerage accounts and cash value life insurance) if the aggregate value of such foreign financial accounts exceeds \$10,000. For purposes of this report, a financial interest means the owner of record or holder of title, and signature authority is the authority to directly control disposition. Spouses can file one FBAR for joint accounts, but only if the FBAR is timely filed.

Timing and Penalties. The FBAR is due electronically by April 15<sup>th</sup>, but an automatic 6-month extension is granted to those U.S. persons who miss the due date. Failure to file the FBAR may result in the following two types of civil penalties:

- (i) \$10,000 penalty for non-willful violations; and
- (ii) The greater of \$100,000 or 50% of all account balances for willful violations.

Under certain circumstances, criminal penalties of up to \$500,000 and imprisonment for up to 10 years can be imposed for willful violations.



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