

## LB&I Process Unit Knowledge Base – International

Library Level	Number	Title
<b>Shelf</b>		Individual Outbound
<b>Book</b>	11	Foreign Entities: Foreign Corporations (Individual Outbound)
<b>Chapter</b>	11.1	Individuals with Investments in a CFC
<b>Section</b>	11.1.2	CFC Information Reporting Issues
<b>Subsection</b>	11.1.2.1	Form 5471- Information Return Filing Requirements

<b>Unit Name</b>	Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty	
<b>Primary UIL Code</b>	9433.01-02	CFC Information Reporting Issues

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# Process Overview

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

When a U.S. person (USP) is required to file a Form 5471 (an information return) under IRC 6046(a), it is filed by attaching it to an individual income tax return, a partnership return, a corporation return, an estate return or a trust return. It shall be filed on the due date including extensions for that return.

In general, for purposes of Category 2 and Category 3, a USP is (1) a citizen or resident of the U.S., (2) a domestic partnership, (3) a domestic corporation or (4) an estate or trust that is not a foreign estate or trust defined in IRC 7701(a)(31). See Treas. Reg. 1.6046-1(f)(3).

Under IRC 6679(a), any person required to file an information return under IRC 6046(a) who fails to file the return at the time provided in such section, or who files a return which does not show the information required pursuant to such section, shall pay a penalty of \$10,000, unless it is shown that the failure is due to reasonable cause. In addition, a continuation penalty of \$10,000 per Form 5471 may be assessed for every 30-day period (or fraction thereof) beginning 90 days after the USP was notified that a failure exists. The maximum continuation penalty per Form 5471 is \$50,000. These penalties may apply to each required Form 5471 on an annual basis. Criminal penalties may also apply for failure to file the information required by IRC 6046.


For example, this process applies when a U.S. citizen or resident is an officer or director of a foreign corporation in which a USP has acquired stock - meeting the 10 percent stock ownership requirement, or when a USP acquires stock in a foreign corporation - meeting the 10 percent stock ownership requirement, and the officer /director or USP:

- Filed a delinquent Form 5471
- Failed to file a Form 5471
- Filed an incomplete Form 5471

# Process Applicability

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

The instructions for Form 5471 separates 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 is different than the statute of limitations for the return to which the Form 5471 is required to be attached.

Criteria	Resources
<ul style="list-style-type: none"> <li>▪ Generally, IRC 6679 penalties with respect to IRC 6046 information returns should be assessed within three years after a complete Form 5471 is filed.</li> </ul> <p> <b>CONSULTATION:</b> Please coordinate with local Counsel in any cases where the Service cannot assess penalties within the three year period.</p>	<ul style="list-style-type: none"> <li>▪ Practice Unit, “Failure to File the Form 5471 – Category 4 &amp; 5 Filers – Monetary Penalty,” DCN: FEN/P/11_01_02_01-01 (formerly FEN/9433.01_06(2013)c)</li> <li>▪ IRC 6679</li> <li>▪ IRC 6046</li> </ul>
<p><u>Category of Filers:</u></p> <ul style="list-style-type: none"> <li>▪ The instructions to Form 5471 set forth the categories of filers:               <ul style="list-style-type: none"> <li>– Category 2 Filer- a U.S. citizen or resident who is an officer or director of a foreign corporation in which a USP has acquired stock meeting certain ownership thresholds or with respect to which a USP is treated as a U.S. shareholder under IRC 953(c),</li> <li>– Category 3 Filer- a USP who has acquired or disposed of stock meeting certain ownership thresholds, a USP who is treated as a U.S. shareholder under IRC 953(c), or a person who becomes a USP while meeting the ownership threshold,</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>▪ IRC 953(c)</li> </ul>

# Process Applicability (cont'd)

Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty	
Criteria	Resources
<p><u>Category of Filers (cont'd):</u></p> <ul style="list-style-type: none"> <li>– Category 4 Filer- a USP who has control of a foreign corporation, where control is ownership of more than 50 percent of the combined voting power or value and</li> <li>– Category 5 Filer- a U.S. shareholder or a USP who is treated as a U.S. shareholder under IRC 953(c), who owns 10 percent or more of the combined voting stock of a controlled foreign corporation (CFC) on the last day of the corporation's tax year.</li> </ul>	
<ul style="list-style-type: none"> <li>▪ IRC 6046 is the underlying authority for Category 2 and 3 filers, and IRC 6038 is the underlying authority for Category 4 and 5 filers.</li> </ul>	<ul style="list-style-type: none"> <li>▪ IRC 6046</li> <li>▪ IRC 6038</li> </ul>
<ul style="list-style-type: none"> <li>▪ Previously, there was a Category 1 filing requirement for certain U.S. officers, directors and shareholders of foreign personal holding companies. The Category 1 filing became obsolete when the foreign personal holding company regime was repealed in 2004.</li> </ul>	

# Process Applicability (cont'd)

Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty	
Criteria	Resources
<p><u>Category 2 Filer:</u></p> <ul style="list-style-type: none"> <li>▪ A Category 2 filer is a U.S. citizen or resident who is an officer or director of a foreign corporation in which a USP:               <ul style="list-style-type: none"> <li>– Has acquired (in one or more transactions) stock which meets the 10 percent stock ownership requirement (described below) with respect to the foreign corporation,</li> <li>– Has acquired (in one or more transactions) an additional 10 percent or more (in value or voting power) of the outstanding stock of the foreign corporation or</li> <li>– Is a U.S. shareholder under IRC 953(c).</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>▪ IRC 6046</li> <li>▪ Treas. Reg. 1.6046-1(a)</li> <li>▪ IRC 953(c)</li> </ul>
<ul style="list-style-type: none"> <li>▪ A USP has acquired stock in a foreign corporation when that person has an unqualified right to receive the stock, even though the stock is not actually issued.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6046-1(f)(1)</li> </ul>
<p><u>Stock Ownership Requirement:</u></p> <ul style="list-style-type: none"> <li>▪ For purposes of Category 2 and Category 3, the stock ownership threshold (when applicable) is met if a USP owns:               <ul style="list-style-type: none"> <li>– 10 percent or more of the total value of the foreign corporation's stock or</li> <li>– 10 percent or more of the total combined voting power of all classes of stock with voting rights.</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>▪ IRC 6042(a)(2)</li> <li>▪ Treas. Reg. 1.6046-1(a) and (c)</li> </ul>

# Process Applicability (cont'd)

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

Criteria	Resources
<p><u>Category 3 Filer:</u></p> <ul style="list-style-type: none"><li>▪ A Category 3 filer is:<ul style="list-style-type: none"><li>– A USP who acquires stock in a foreign corporation which, when added to any stock owned on the date of acquisition, meets the 10 percent stock ownership requirement with respect to the foreign corporation,</li><li>– A USP who acquires stock which, without regard to stock already owned on the date of acquisition, meets the 10 percent stock ownership requirement with respect to the foreign corporation,</li><li>– A person who is treated as a U.S. shareholder under IRC 953(c) with respect to the foreign corporation,</li><li>– A person who becomes a USP while meeting the 10 percent stock ownership requirement with respect to the foreign corporation or</li><li>– A USP who disposes of sufficient stock in the foreign corporation to reduce his or her interest to less than the 10 percent stock ownership requirement.</li></ul></li></ul>	<ul style="list-style-type: none"><li>▪ IRC 6046</li><li>▪ IRC 953(c)</li><li>▪ Treas. Reg. 1.6046-1(c)</li></ul>



# Process Applicability (cont'd)

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

Criteria	Resources
<p><u>Filing Exception – Multiple Filers of Same Information:</u></p> <ul style="list-style-type: none"> <li>▪ When multiple persons are required to file Form 5471 and applicable schedules with respect to the same CFC, it may be jointly filed by attaching it to only one person's return. However, for Category 3 filers, the required information may only be filed by another person having an equal or greater interest (measured in terms of value or voting power of the stock of the foreign corporation).</li> </ul>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6046-1(e)(1)</li> <li>▪ Treas. Reg. 1.6046-1T(e)(5)</li> <li>▪ Form 5471 Instructions</li> </ul>
<ul style="list-style-type: none"> <li>▪ 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.</li> </ul>	
<ul style="list-style-type: none"> <li>▪ The other persons must attach a statement to their respective returns which:               <ul style="list-style-type: none"> <li>– States that the filing has or will be satisfied,</li> <li>– Provides the name, address and identifying number of the return to which the Form 5471 was or will be attached and</li> <li>– Identifies the IRS Service Center where the return was or will be filed.</li> </ul> </li> </ul>	
<ul style="list-style-type: none"> <li>▪ If the return and Form 5471 were or will be filed electronically, e-file should be indicated on the joint filer statements.</li> </ul>	

# Process Applicability (cont'd)

Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty	
Criteria	Resources
<p><u>Filing Exception – Constructive Ownership:</u></p> <ul style="list-style-type: none"> <li>▪ A USP described in Category 3 does not have to file Form 5471 if all of the following conditions are met:               <ul style="list-style-type: none"> <li>– The USP does not own a direct interest in the foreign corporation,</li> <li>– The USP is required to furnish the information requested solely because of constructive ownership (as determined under Treas. Reg. 1.6046-1(i)) from another USP and</li> <li>– The USP through which the constructive shareholder owns an interest in the foreign corporation files Form 5471 to report all of the required information.</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6046-1(e)(4)(iii)</li> <li>▪ Treas. Reg. 1.6046-1(i)</li> </ul>
<ul style="list-style-type: none"> <li>▪ No statement is required to be attached to tax returns for persons claiming the constructive ownership exception. An officer or director that would otherwise be required to file Form 5471 as a Category 2 filer does not need to file Form 5471 with respect to a Category 3 filer meeting the constructive ownership exception for Category 3 described above.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6046-1(e)(4)(iv)</li> </ul>
<p><u>Filing Exception – 95 Percent Exception (Category 2 Only):</u></p> <ul style="list-style-type: none"> <li>▪ A Category 2 filer does not have to file Form 5471 if immediately after a reportable stock acquisition, three or fewer USPs own 95 percent or more in value of the outstanding stock of the foreign corporation and the USP making the acquisition files a return for the acquisition as a Category 3 filer.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6046-1(e)(4)(ii)</li> </ul>

# Summary of Process Steps

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

### Process Steps

After determining the taxpayer has a filing requirement as outlined in the Determination of Process Applicability section, first verify whether the taxpayer filed a timely and accurate Form 5471. The next step is to establish a penalty case file and prepare and issue the notice letter. Then, determine what penalties may apply and how they are computed, as well as whether the taxpayer can argue reasonable cause for failure to file. The final steps in this process are penalty application or non-application, and case closing procedures.

#### [Step 1](#)

Verify Fact of Filing

#### [Step 2](#)

Penalty Case File Controls

#### [Step 3](#)

Penalty Determination

#### [Step 4](#)

Penalty Application/Closing Procedures

# Step 1: Verify Fact of Filing

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

### Step 1

It was determined the taxpayer has a filing requirement as outlined in the Determination of Process Applicability section. Before commencing a penalty case file, first verify whether the taxpayer filed a timely and accurate Form 5471. The related income tax return (or other return) may have been late filed with the Form(s) 5471 attached or the related income tax return (or other return) may have been filed timely but without a substantially complete Form(s) 5471.

#### Considerations

- Form 5471 is due when the USP's income tax return is due, including extensions, and is filed WITH the USP's income tax return (or other return).
- As discussed in detail previously, there are exceptions to filing:
  - Multiple filers of same information
  - Constructive ownership
  - 95 percent exception (Category 2 only)
- There is no longer a 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.

#### Resources

- IRC 6046

# Step 1: Verify Fact of Filing (cont'd)

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

### [Step 1](#)

Considerations	Resources
<ul style="list-style-type: none"><li>▪ There is no separate Master File Transaction (MFT) in Integrated Data Retrieval System (IDRS) for Form 5471 filings.</li><li>▪ Penalties may be asserted when the related income tax return is filed late or when a complete Form(s) 5471 is not timely filed with the related income tax return, unless the failure is due to reasonable cause.</li></ul>	
<ul style="list-style-type: none"><li>▪ While identifying Forms 5471 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. Generally, IRC 6679 penalties with respect to IRC 6046 information returns should be assessed within three years after a complete Form 5471 is filed.</li></ul>	<ul style="list-style-type: none"><li>▪ IRC 6679</li><li>▪ IRC 6046</li></ul>
<ul style="list-style-type: none"><li>▪ Also, the related income tax returns for the prior years are not required to be under exam to assess penalties under IRC 6679.</li></ul>	<ul style="list-style-type: none"><li>▪ IRC 6679</li></ul>

# Step 1: Verify Fact of Filing (cont'd)

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

### [Step 1](#)

Considerations	Resources
<p><u>Determining if the Return was Filed Late:</u></p> <ul style="list-style-type: none"> <li>▪ If the last day for filing a return was a Saturday, a Sunday, or a legal holiday in the District of Columbia, filing timely occurred if the return was mailed on or before the next succeeding day which was not a Saturday, Sunday, or a legal holiday.</li> <li>▪ If a return was postmarked prior to the due date and received after the due date, the date of the postmark is treated as the filing date.</li> </ul>	<ul style="list-style-type: none"> <li>▪ IRC 7503</li> <li>▪ Treas. Reg. 1.7503-1</li> <li>▪ Rev. Rul. 81-269 – Limitation Period</li> <li>▪ 1981-2 C.B. 243</li> <li>▪ IRC 7502</li> <li>▪ Treas. Reg. 1.7502-1</li> </ul>
<ul style="list-style-type: none"> <li>▪ For Forms 1120 filed late after December 31, 2008, the Service automatically assesses an initial penalty of \$10,000 for each Form 5471 attached.</li> </ul>	<ul style="list-style-type: none"> <li>▪ IRM 21.8.2.21.2- <i>Form 5471 Penalties Systemically Assessed from Late-Filed Form 1120 Series or Form 1065</i></li> </ul>

# Step 1: Verify Fact of Filing (cont'd)

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

### Step 1

Considerations	Resources
<ul style="list-style-type: none"> <li>▪ The following items are helpful in determining whether all Forms 5471 that were required to be filed were filed or not filed:               <ul style="list-style-type: none"> <li>– Forms 5471,</li> <li>– Returns (such as Forms 1120), plus those of the two preceding tax years,</li> <li>– Forms 8832 - <i>Entity Classification Election</i>,</li> <li>– Tax organization chart, plus those of the two preceding tax years,</li> <li>– Legal entity chart, plus those of the two preceding tax years,</li> <li>– Certified English translations of certificates of corporate dissolution, officially stamped by the appropriate foreign government agency and</li> <li>– Joint filer's statements.</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>▪ Form 8832</li> <li>▪ Treas. Reg. 1.6046-1T(e)(5)</li> </ul>
<div style="background-color: black; width: 100%; height: 100%; position: relative;"> <span style="color: red; font-weight: bold; position: absolute; top: 5px; left: 5px;">#</span> <span style="color: red; font-weight: bold; position: absolute; bottom: 5px; right: 5px;">#</span> </div>	

# Step 1: Verify Fact of Filing (cont'd)

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

### [Step 1](#)

Considerations	Resources
<ul style="list-style-type: none"><li>▪ If the USP was a Category 2 or Category 3 filer and required to file Form(s) 5471 but did not file Form(s) 5471, prepare a notice letter to notify the USP of the failure.</li></ul>	<ul style="list-style-type: none"><li>▪ Step 2 – Notice Letter</li></ul>
<ul style="list-style-type: none"><li>▪ IRC 6046(b) provides that the returns required by IRC 6046(a) shall be in the form and set forth the information as the Secretary requires to carry out the provisions of the income tax laws. The regulations describe information required under IRC 6046(a) and provide that the information is furnished on Form 5471.</li></ul>	<ul style="list-style-type: none"><li>▪ Treas. Reg. 1.6046-1(a)(2)(ii)</li><li>▪ Treas. Reg. 1.6046-1(c)(4)</li><li>▪ IRC 6046(a)</li></ul>



# Step 1: Verify Fact of Filing (cont'd)

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

### [Step 1](#)

Considerations	Resources
<p><u>Review Form(s) 5471 on their Face for Completeness:</u></p> <ul style="list-style-type: none"> <li>▪ Item B: Category of the filer was omitted or incorrect, thus the Form 5471 schedules required to be completed could not be determined.</li> </ul>	
<ul style="list-style-type: none"> <li>▪ Item C: Percentage of the foreign corporation voting stock owned 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 could not be determined.</li> <li>▪ Note: A Category 2 USP filer will not complete Item C.</li> </ul>	
<ul style="list-style-type: none"> <li>▪ Item 1a: Name or address of foreign corporation was omitted, thus other information provided on Form 5471 could not be associated with a specific foreign corporation.</li> </ul>	
<ul style="list-style-type: none"> <li>▪ Items 1b(1) and 1b(2): Reference identification number was omitted when the Employer Identification Number (EIN) was not provided, thus other information provided on Form 5471 could not be associated with a specific foreign corporation.</li> <li>▪ Note: The reference identification number is only required for foreign corporation tax years beginning in 2012 and later.</li> </ul>	

# Step 1: Verify Fact of Filing (cont'd)

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

### [Step 1](#)

Considerations	Resources
<p><u>Review Form(s) 5471 on their Face for Completeness (cont'd):</u></p> <ul style="list-style-type: none"><li>▪ Item 1c: Country of incorporation was omitted, thus the information reported on Form 5471 could not be correctly evaluated in conjunction with other information known during early phases of the exam. The same concern arises for the following omitted or incomplete items:<ul style="list-style-type: none"><li>– 1d: Date of incorporation</li><li>– 1e: Principal place of business</li><li>– 1f: Principal business activity code number</li><li>– 1g: Principal business activity</li><li>– 1h: Functional currency</li></ul></li></ul>	
<ul style="list-style-type: none"><li>▪ Item 2d: Name and address of person with custody of foreign corporation's books and records was omitted, when both Items 2a and 2c were omitted, thus efficient and effective planning was impacted during early phases of the exam.</li></ul>	

# Step 1: Verify Fact of Filing (cont'd)

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

### [Step 1](#)

Considerations	Resources
<p><u>Review Form(s) 5471 on their Face for Completeness (cont'd):</u></p> <ul style="list-style-type: none"> <li>▪ Review the USP's Form(s) 5471 for any schedule required (based on the filing category indicated on Item B) but not prepared. Note: Annual Form 5471 instructions include a chart titled <i>Filing Requirements for Categories of Filers</i> that indicates the schedules required by category of filer.</li> </ul>	
<ul style="list-style-type: none"> <li>▪ # [REDACTED] #</li> </ul>	
<ul style="list-style-type: none"> <li>▪ Review the USP's Form(s) 5471 for the most common reasons for noncompliance:               <ul style="list-style-type: none"> <li>– Stating that required information will be furnished upon request or audit,</li> <li>– Providing computer generated Form(s) 5471 that were not IRS approved and did not conform to requirements,</li> <li>– Failing to provide financial statements for foreign corporations and</li> <li>– Providing consolidated financial statements of two or more foreign corporations.</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>▪ News Release IR-90-58 (03/29/90), 1990 WL 707926</li> </ul>

# Step 1: Verify Fact of Filing (cont'd)

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

### [Step 1](#)

Considerations	Resources
<p>Review Form(s) 5471 on their Face for Completeness (cont'd):</p> <ul style="list-style-type: none"><li>▪ # [REDACTED]</li><li>▪ [REDACTED] #</li></ul>	
<ul style="list-style-type: none"><li>▪ The doctrine of substantial compliance may apply when considering whether a Category 2 or Category 3 filer timely filed complete Form(s) 5471.</li></ul>	

# Step 2: Penalty Case File Controls

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

### Step 2

It was 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
<p><u>Establish a Penalty Case File:</u></p> <ul style="list-style-type: none"> <li>▪ Establish controls and prepare a penalty case file. This file must include the information that supports the requirements to file and establishes that the Forms 5471 have not been filed or that the information provided was not complete.</li> </ul>	<ul style="list-style-type: none"> <li>▪ IRM 20.1.9.2 – <i>Assessment Procedures for Penalties Not Subject to Deficiency Procedures</i></li> <li>▪ IRM Exhibit 20.1.9-1 – <i>Quick Reference Guide to International Penalties</i></li> </ul>
<ul style="list-style-type: none"> <li>▪ Submit Form 5345-D for managerial approval to establish controls:               <ul style="list-style-type: none"> <li>– Check box for “Control Penalty Investigation.”</li> <li>– MFT = PQ, Activity Code = 586, Source Code = 99 - For Initial &amp; Continuation Penalty.</li> <li>– ASED is three years from the date the Form 5471 was filed. If the information return has not been filed prior to submitting the Form 5345-D then use the EE alpha statute. Update the ASED on ERCS as necessary.</li> <li>– Reason for Request is “To control penalty investigations for Form 5471 returns not filed.”</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>▪ IRM 20.1.9.2.1 - <i>Penalty Case Controls</i></li> <li>▪ Form 5345-D</li> </ul>
<ul style="list-style-type: none"> <li>▪ Examiners should charge time to the penalty case file.</li> <li>▪ Issue the notice letter as discussed on the following slides.</li> </ul>	<ul style="list-style-type: none"> <li>▪ IRM 20.1.9.2 (11) - <i>Request the Returns</i></li> <li>▪ IRM 20.1.9.2 (12) - <i>Notice Letter Provisions</i></li> </ul>

## Step 2: Penalty Case File Controls (cont'd)

### Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

#### [Step 2](#)

Considerations	Resources
<p><u>Notice Letter Issuance:</u></p> <ul style="list-style-type: none"><li>▪ As soon as becoming aware of a person that did not comply with IRC 6046, prepare a Notice (Pattern) Letter for Failure to File Form 5471 – Schedule O. Additional notice letters can be prepared later as needed.</li></ul>	<ul style="list-style-type: none"><li>▪ IRC 6046</li></ul>
<ul style="list-style-type: none"><li>▪ The notice letter informs the USP that it failed to file a Form 5471 (late or not filed), or that the form filed was incomplete. It explains that an initial penalty will be imposed and that a continuation penalty applies for each 30-day period (or fraction thereof) beginning 90 days after the date of the letter until a complete Form 5471 is provided.</li></ul>	
<ul style="list-style-type: none"><li>▪ The notice letter is addressed to the person required to file Form(s) 5471. The notice letter should include the name and phone number of the examiner. Also, the notice letter should state that the person should contact the examiner in response to the letter, and reference the examiner in any reply to the letter.</li></ul>	

# Step 2: Penalty Case File Controls (cont'd)

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

### [Step 2](#)

Considerations	Resources
<p><u>Notice Letter Issuance (cont'd):</u></p> <ul style="list-style-type: none"> <li>▪ 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.</li> </ul>	
<ul style="list-style-type: none"> <li>▪ In the body of the notice letter, include the tax year(s) of the person required to file Form(s) 5471. 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 the relevant tax years are properly identified.</li> </ul>	
<ul style="list-style-type: none"> <li>▪ Notice letters must be signed by an examination group manager in SB/SE or a revenue agent in LB&amp;I.</li> </ul>	<ul style="list-style-type: none"> <li>▪ IRM 20.1.9.2 (13) - <i>Notice Letters</i></li> </ul>
<ul style="list-style-type: none"> <li>▪ 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 6679. Typically, USPs will provide corrected Forms 5471 as soon as possible after receipt of the notice letter to avoid accumulating continuation penalties.</li> </ul>	<ul style="list-style-type: none"> <li>▪ IRC 6679(a)</li> </ul>

# Step 2: Penalty Case File Controls (cont'd)

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

### [Step 2](#)

Considerations	Resources
<p><u>Notice Letter Issuance (cont'd):</u></p> <ul style="list-style-type: none"> <li>The notice letter must be mailed to the person required to file, not its representative. # [REDACTED]</li> </ul>	
<ul style="list-style-type: none"> <li>Keep a copy of all notice letters issued, and the certified or registered return receipts, in the case file.</li> </ul>	
<ul style="list-style-type: none"> <li>After the notice letter is mailed, do not discuss the notice letter with a representative who is not authorized for such discussions. Review Form(s) 2848 - <i>Power of Attorney and Declaration of Representative</i> received to ensure that the representative has such authorization.</li> <li>For a valid authorization, Form 2848 Item #3 “Description of Matter” should include words similar to “Miscellaneous Penalty Under IRC 6679.” If there is not a valid authorization, consider suggesting that the USP issue a separate Form 2848.</li> </ul>	<ul style="list-style-type: none"> <li>Form 2848 - <i>Power of Attorney and Declaration of Representative</i></li> </ul>



# Step 2: Penalty Case File Controls (cont'd)

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

### [Step 2](#)

Considerations	Resources
<p><u>Notice Letter Issuance (cont'd):</u></p> <ul style="list-style-type: none"> <li>▪ # [REDACTED] #</li> </ul>	
<ul style="list-style-type: none"> <li>▪ Consider referring the USP or its authorized representative to Treas. Reg. 301.6679-1 which sets forth the requirements for a valid reasonable cause statement.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 301.6679-1(a)(3)</li> </ul>
<ul style="list-style-type: none"> <li>▪ There is no provision under IRC 6679 for an extension of the 90-day period to comply with a notice letter. When it is reasonable to allow an extension (such as for extreme hardship, natural disaster or other highly unusual situations), document such extensions and the new due date in the case file.</li> </ul>	<ul style="list-style-type: none"> <li>▪ IRC 6679</li> </ul>

# Step 2: Penalty Case File Controls (cont'd)

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

### [Step 2](#)

Considerations	Resources
<p><u>Review Form(s) 5471 Submitted in Response to the Notice Letter:</u></p> <ul style="list-style-type: none"> <li>▪ Date stamp Form(s) 5471 as they are received in response to the notice letter. If a submitted Form 5471 is correct, that date will determine whether, and the extent to which, continuation penalties apply.</li> </ul>	
<ul style="list-style-type: none"> <li>▪ Review submitted Form(s) 5471 to determine whether they comply with IRC 6046. If not, then the continuation penalty periods are still in effect.</li> </ul>	<ul style="list-style-type: none"> <li>▪ IRC 6046</li> </ul>
<ul style="list-style-type: none"> <li>▪ # [REDACTED] #</li> </ul>	<ul style="list-style-type: none"> <li>▪ Step 1</li> </ul>

# Step 2: Penalty Case File Controls (cont'd)

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

### [Step 2](#)

Considerations	Resources
<p>Review Form(s) 5471 Submitted in Response to the Notice Letter (cont'd):</p> <ul style="list-style-type: none"><li>▪ # [REDACTED]</li><li>[REDACTED]</li><li>[REDACTED]</li><li>[REDACTED]</li><li>[REDACTED] #</li></ul>	
<ul style="list-style-type: none"><li>▪ For Form(s) 5471 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 complete Form 5471 was not filed.</li></ul>	

# Step 3: Penalty Determination

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

### Step 3

The penalty case file has been established, the notice letter has been mailed to the taxpayer, and Form(s) 5471 may or may not have now been filed correctly. Next, determine what penalties may apply and how they are computed, as well as whether the taxpayer can argue reasonable cause for failure to file.

Considerations	Resources
<p><u>Penalty Structure:</u></p> <ul style="list-style-type: none"> <li>If Form(s) 5471 are not filed on or before the due date (including extensions) of the individual's income tax return or if the applicable form does not include all the information required or includes incorrect information, then initial and continuation penalties may be applicable as follows:</li> </ul>	<ul style="list-style-type: none"> <li>Treas. Reg. 1.6046-1(j) and (k)</li> </ul>
<ul style="list-style-type: none"> <li>The penalty per IRC 6679 for failure to furnish all the required information under IRC 6046 on a timely Form 5471 is \$10,000 per Form 5471 that the U.S. shareholder fails to file.</li> </ul>	<ul style="list-style-type: none"> <li>IRM 20.1.9.15 - <i>IRC 6679—Return of U.S. Persons With Respect to Certain Foreign Corporations and Partnerships</i></li> <li>IRC 6679</li> </ul>
<ul style="list-style-type: none"> <li>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.</li> </ul>	
<ul style="list-style-type: none"> <li>The maximum total penalty for each failure to file Form 5471 is \$60,000 (\$10,000 initial penalty and the \$50,000 continuation penalty).</li> </ul>	

# Step 3: Penalty Determination (cont'd)

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

### [Step 3](#)

Considerations	Resources
<p><u>Reasonable Cause Exception:</u></p> <ul style="list-style-type: none"> <li>▪ No penalty shall be imposed under IRC 6679(a)(1) on any failure which is shown to be due to reasonable cause.</li> </ul>	<ul style="list-style-type: none"> <li>▪ IRC 6679(a)(1)</li> </ul>
<ul style="list-style-type: none"> <li>▪ Regarding the facts alleged to support reasonable cause, determine whether the USP's supporting documents (and events) that related to those facts were dated (or occurred) after the latest date that reasonable cause was relevant.</li> </ul>	
<ul style="list-style-type: none"> <li>▪ As previously discussed, there are two separate penalties: the initial penalty and the continuation penalty. While both penalties are described within IRC 6679, only the initial penalty can be considered for the reasonable cause exception.</li> </ul>	<ul style="list-style-type: none"> <li>▪ IRM 20.1.9.15.5 - <i>Reasonable Cause</i></li> </ul>
<ul style="list-style-type: none"> <li>▪ Determine whether the USP's statement of reasonable cause (for the failure to file a Form 5471, filing it late or filing it incomplete) meets the regulation requirements. That statement must:               <ul style="list-style-type: none"> <li>- Be in writing,</li> <li>- Provide all of the facts alleged as reasonable cause and</li> <li>- Contain a declaration that the statement was made under penalties of perjury.</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 301.6679-1(a)(3)</li> </ul>
<ul style="list-style-type: none"> <li>▪ If the reasonable cause statement does not include the declaration, advise the USP that the statement does not satisfy the requirements of the regulations.</li> </ul>	

# Step 3: Penalty Determination (cont'd)

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

### [Step 3](#)

Considerations	Resources
<p><u>Reasonable Cause Exception (cont'd):</u></p> <ul style="list-style-type: none"> <li>▪ Determine whether the USP is in full compliance with IRC 6046 reporting and record keeping requirements for all tax years open under the statutes. Request the USP file, furnish, report or maintain the information required under IRC 6046 before considering any reasonable cause requests.</li> </ul>	<ul style="list-style-type: none"> <li>▪ IRM Exhibit 20.1.9-5 - <i>Reasonable Cause Relief</i></li> <li>▪ IRC 6046</li> </ul>
<p><u>Review the Definition and Factors of Reasonable Cause:</u></p> <ul style="list-style-type: none"> <li>▪ If the USP exercises ordinary business care and prudence and is nevertheless unable to provide any item of information required under IRC 6046 and the regulations, such failure is considered due to reasonable cause.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 301.6679-1(a)(3)</li> </ul>
<ul style="list-style-type: none"> <li>▪ The IRM provides factors to consider to determine whether the USP exercised ordinary business care and prudence. Examples of what might be reasonable cause include:               <ul style="list-style-type: none"> <li>- Erroneous advice or reliance,</li> <li>- Unable to obtain records and</li> <li>- Death, serious illness, or unavoidable absence.</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>▪ IRM 20.1.1.3.2.2.5 - <i>Erroneous Advice or Reliance</i></li> <li>▪ CC-2004-036</li> <li>▪ IRM 20.1.1.3.2.2.3 - <i>Unable to Obtain Records</i></li> <li>▪ IRM 20.1.1.3.2.2.1 - <i>Death, Serious Illness or Unavoidable Absence</i></li> </ul>

# Step 3: Penalty Determination (cont'd)

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

### [Step 3](#)

Considerations	Resources
<p><u>Review the Definition and Factors of Reasonable Cause (cont'd):</u></p> <ul style="list-style-type: none"><li>▪ 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: the USP's education, if the USP was penalized before, if the 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.</li></ul>	<ul style="list-style-type: none"><li>▪ <i>IRM 20.1.1.3.2.2.6 - Ignorance of the Law</i></li></ul>
<ul style="list-style-type: none"><li>▪ 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 generally constitute reasonable cause.</li></ul>	

# Step 4: Penalty Application/Closing Procedures

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

### Step 4

Now that the notice letter has been issued and the penalty determination factors are defined, the final steps in this process are penalty application or non-application, and case closing procedures.

Considerations	Resources
<p><u>Application of Penalties – Initial Penalty:</u></p> <ul style="list-style-type: none"> <li>Examiners must first take steps to secure appropriate documentation to support the requirements to file the returns and keep them in the penalty file. Next, 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.</li> </ul>	
<ul style="list-style-type: none"> <li>The initial penalty is asserted by examiners on Form 8278 using penalty reference number (PRN) 613. This penalty can be asserted when an examiner determines the USP has not timely filed the required information or has not filed complete and accurate information.</li> </ul>	<ul style="list-style-type: none"> <li>IRM 20.1.9.15.3 - <i>Penalty Assertion</i></li> <li>IRM 20.1.9.15.4 - <i>Penalty Computation</i></li> <li>Form 8278</li> </ul>



# Step 4: Penalty Application/Closing Procedures (cont'd)

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

### [Step 4](#)

Considerations	Resources
<p><u>Application of Penalties – Initial Penalty (cont'd):</u></p> <ul style="list-style-type: none"> <li>As mentioned earlier, if any failure continues more than 90 days after the day on which the notice of such failure was mailed to the taxpayer (90-day period), additional penalties will apply. The continuation penalty is \$10,000 for each 30-day period (or fraction thereof) during which such failure continues after the expiration of the 90-day period. These additional penalties are also asserted on Form 8278 using PRN 704.</li> </ul>	
<ul style="list-style-type: none"> <li>The maximum continuation penalty for IRC 6679 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.</li> </ul>	<ul style="list-style-type: none"> <li>IRM 20.1.9.15.4 - <i>Penalty Computation</i></li> <li>IRC 6679</li> </ul>

# Step 4: Penalty Application/Closing Procedures (cont'd)

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

### [Step 4](#)

Considerations	Resources
<p><u>Form 8278 – Assessment and Abatement of Miscellaneous Civil Penalties:</u></p> <ul style="list-style-type: none"> <li>Form 8278 is the assessment document for international penalties. Failure to file under IRC 6046 has a penalty section on the form which covers both the initial and the continuation penalties.</li> </ul>	<ul style="list-style-type: none"> <li>Form 8278</li> <li>IRC 6046</li> <li>20.1.9.2.2 - <i>Penalty Assessment– Form 8278, Assessment and Abatement of Miscellaneous Civil Penalties</i></li> </ul>
<ul style="list-style-type: none"> <li>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.</li> </ul>	
<ul style="list-style-type: none"> <li>The examiner will enter the dollar amount of the penalty on Form 8278 and attach Form 886-A - <i>Explanation of Items</i>.</li> </ul>	<ul style="list-style-type: none"> <li>Form 886-A</li> </ul>
<ul style="list-style-type: none"> <li>The taxpayer's signature is not required with respect to these penalties. The Manager's signature is required in block 11a to meet the provision of IRC 6751.</li> </ul>	<ul style="list-style-type: none"> <li>IRC 6751</li> </ul>

# Step 4: Penalty Application/Closing Procedures (cont'd)

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

### [Step 4](#)

Considerations	Resources
<p><u>Payments:</u></p> <ul style="list-style-type: none"> <li>▪ 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.</li> </ul>	<ul style="list-style-type: none"> <li>▪ IRM 20.1.9.2(21) - <i>Payment</i></li> <li>▪ Form 3244</li> <li>▪ IRM 21.3.4.7.1.3 - <i>Designated Payment Code (DPC)</i></li> </ul>
<ul style="list-style-type: none"> <li>▪ The payment will be posted to MFT 55 for individuals and MFT 13 for entities.</li> </ul>	
<p><u>No Filing Requirement or Accepting the Filing Without Penalties:</u></p> <ul style="list-style-type: none"> <li>▪ The examiner should complete Form 8278.               <ul style="list-style-type: none"> <li>– On Form 8278, enter “1” as the number of violations on the applicable penalty line and enter “0.1” as the amount assessed.</li> <li>– In the “Remarks” box enter “Blocking Series 52; Reason Code 62; Hold Code 0; Penalty Reason Code 0XX” (Refer to Document 6209, <i>Penalty Abatement/Suppression PRC</i> chart for penalty reason codes).</li> <li>– 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).</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>▪ IRM Exhibit 20.1.1-2 - <i>Penalty Reason Code Chart</i></li> <li>▪ Form 8278</li> </ul>

# Step 4: Penalty Application/Closing Procedures (cont'd)

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

### [Step 4](#)

Considerations	Resources
<u>Miscellaneous Case Closing Considerations:</u> <ul style="list-style-type: none"><li>▪ The case file should contain all working papers, correspondence, and an activity record in addition to the Form 8278 and Form 886-A.</li></ul>	<ul style="list-style-type: none"><li>▪ Form 8278</li><li>▪ Form 886-A</li></ul>
<ul style="list-style-type: none"><li>▪ The case file will be closed with a Form 3198.</li></ul>	<ul style="list-style-type: none"><li>▪ Form 3198</li></ul>
<ul style="list-style-type: none"><li>▪ The ERCS (Examination Returns Control System) PQ 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.</li></ul>	<ul style="list-style-type: none"><li>▪ Form 5471</li></ul>

# Other Considerations / Impact to Audit

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

Considerations	Resources
<p><u>Specific Power of Attorney (POA) or Authorization to Disclose Tax Information:</u></p> <ul style="list-style-type: none"><li>▪ A Form 2848 is required prior to discussing penalty issues with a person other than the person subject to the assessment or required to file the returns. A POA for the income tax return does NOT cover the penalty issue.</li></ul>	<ul style="list-style-type: none"><li>▪ Form 2848 Item #3 “Description of Matter” should include words similar to “Miscellaneous Penalty Under IRC 6679.”</li></ul>

# Index of Referenced Resources

<b>Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty</b>
IRC 953(c)
IRC 6038
IRC 6042(a)(2)
IRC 6046
IRC 6679
IRC 6751
IRC 7502
IRC 7503
Treas. Reg. 1.6046-1
Treas. Reg. 1.6046-1T(e)
Treas. Reg. 1.7502-1
Treas. Reg. 1.7503-1
Treas. Reg. 301.6679-1(a)(3)
Rev. Rul. 81-269 – Limitation Period
1981-2 C.B. 243
CC-2004-036

# Index of Referenced Resources (cont'd)

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

IR 90-58

IRM 20.1.1.3.2.2.1 - *Death, Serious Illness or Unavoidable Absence*

IRM 20.1.1.3.2.2.3 - *Unable to Obtain Records*

IRM 20.1.1.3.2.2.5 - *Erroneous Advice or Reliance*

IRM 20.1.1.3.2.2.6 - *Ignorance of the Law*

IRM 20.1.9.15 - *IRC 6679—Return of U.S. Persons With Respect to Certain Foreign Corporations and Partnerships*

IRM 20.1.9.15.3 - *Penalty Assertion*

IRM 20.1.9.15.4 - *Penalty Computation*

IRM 20.1.9.15.5 - *Reasonable Cause*

IRM 20.1.9.2 - *Assessment Procedures for Penalties Not Subject to Deficiency Procedures*

IRM 20.1.9.2.1 - *Penalty Case Controls*

IRM 20.1.9.2.2 - *Penalty Assessment—Form 8278, Assessment and Abatement of Miscellaneous Civil Penalties*

IRM 21.3.4.7.1.3 - *Designated Payment Code (DPC)*

IRM 21.8.2.21.2 - *Form 5471 Penalties Systemically Assessed from Late-Filed Form 1120 Series or Form 1065*

IRM Exhibit 20.1.1-2 - *Penalty Reason Code Chart*

IRM Exhibit 20.1.9-1 - *Quick Reference Guide to International Penalties*

# Index of Referenced Resources (cont'd)

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

IRM Exhibit 20.1.9-5 - *Reasonable Cause Relief*

Form 886-A

Form 2848

Form 3198

Form 3244

Form 5345-D

Form 5471

Form 5471 Instructions

Form 6751

Form 8278

Form 8832



# Training and Additional Resources

## Failure to File the Form 5471 – Category 2 and 3 Filers – Monetary Penalty

Type of Resource	Description
Reference Materials – Treaties	<ul style="list-style-type: none"><li>▪ <i>Bittker &amp; Lokken Fed. Tax'n Inc</i>, Est and Gift Para 65.8.2.</li></ul> <p>Click on:</p> <ul style="list-style-type: none"><li>▪ Table of Contents</li><li>▪ Part 9 (Foreign Income and Foreign Taxpayers)</li><li>▪ Chapter 65 (Introduction and Classification of Individuals and Entities)</li><li>▪ Paragraph 65.8 (Information Reporting with Respect to Foreign Business Entities)</li><li>▪ Paragraph 65.8.2 (U.S. Persons with Interests in Foreign Corporations)</li></ul>

# Glossary of Terms and Acronyms

Term/Acronym	Definition
CFC	Controlled Foreign Corporation
EIN	Employer Identification Number
ERCS	Examination Returns Control System
IDRS	Integrated Data Retrieval System
IR	Information Release
IRC	Internal Revenue Code
LB&I	Large Business & International
MFT	Master File Transaction
POA	Power of Attorney
PRC	Penalty Reason Code
PRN	Penalty Reference Number
TC	Transaction Code
USP	United States Person

# Index of Related Practice Units

Associated UILs	Related Practice Unit	DCN
9433.01-01	Determination of U.S. Shareholder and CFC Status	FEN/T/11_01_01_01-01 (formerly FEN/9433.01_03(2013)b)
9433.01-01	Overview of Subpart F Income for U.S. Individual Shareholders	FEN/T/11_01_01_02-01 (formerly FEN/9433.01_09(2013)b)
9433.01-02	Failure to File the Form 926 – Return by a U.S. Transferor of Property to a Foreign Corporation – Monetary Penalty	FEN/P/11_01_02_02-01 (formerly FEN/9433.01_12(2016))
9433.01-02	Failure to File the Form 5471 – Category 4 & 5 Filers – Monetary Penalty	FEN/P/11_01_02_01-01 (formerly FEN/9433.01_06(2013)c)