

## **Form 5471 Filing Requirement Examples**

by

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Below are 2 sets of situations explaining the Form 5471 filing requirements. The first set covers various ownership situations of a US person's ownership of a foreign corporation. The second set involves the reporting requirements of a nonresident alien who becomes a US person.

### **I. US Person's Ownership of a Foreign Corporation**

Below are 12 situations of a US person's ownership of a foreign corporation where, unless otherwise specified, the US person is not an officer or director of the foreign corporation nor do any other US persons own stock in the foreign corporation.

In the cases where the US person is described by more than one filing category, the information requested in the Form 5471 instructions for both categories must be provided but not duplicated where the same information is requested by each category.

**1.** A US person acquires 5% of the foreign corporation during year 1. He has not owned any shares in the foreign corporation previously.

There is no Form 5471 filing requirement.

**2.** In year 2 he acquires an additional 6% ownership raising his ownership to 11%.

He must file as a Category 3 filer for year 2 because he meets the at-least-10% ownership requirement.

**3.** In year 3 his stock ownership does not change and remains at 11%.

He is not required to file Form 5471 for year 3 because there has been no change in his ownership even though he still meets the at-least-10% ownership requirement.

**4.** In year 4 his stock ownership does not change and remains at 11% but he becomes an officer or director of the foreign corporation on July 1, year 4.

He must file as a Category 2 filer for year 4 because he meets the filing requirement as an officer or director owning at least 10% of the foreign corporation because he *acquired* at least 10% in a prior year.

**5.** In year 5 he acquires an additional 22% ownership raising his ownership to 33% and ceases to be an officer or director of the corporation on June 30, year 5.

He must file as a Category 2 filer because he was an officer or director for part of year 5 and as a Category 3 filer for year 5 because he acquired an additional 10% stock interest.

**6.** In year 6 he acquires an additional 3% ownership raising his ownership to 36%.

He must file as a Category 3 filer for year 6 because the first provision in the Category 3 instructions says, "A U.S. person who acquires stock in a foreign corporation which, when added to any stock owned on the date of acquisition, meets the at least 10% stock ownership requirement with respect to the foreign corporation." In other words, even though his stock ownership only increases by 3%, he is a Category 3 filer because he has acquired stock and he meets the at least 10% ownership requirement.

7. On June 30, year 7 he divests himself of 9% reducing his ownership to 27%.

He is not required to file Form 5471 for year 7. If, instead, he were to divest himself of 12% reducing his ownership to 24%, he would still not be required to file Form 5471 for year 7 even though the divestiture was 10% or more, because his ownership after the divestiture is at least 10%.

8. On June 30, year 8 he divests himself of 18% reducing his ownership to 9%.

He must file as a Category 3 filer for year 8 because he has disposed of sufficient stock to reduce his interest below the at-least-10% ownership requirement. The filing is only to report the transaction and not to report income.

9. In year 9, his ownership remains at 9% but he becomes an officer or director of the foreign corporation.

He is not required to file Form 5471 for year 9.

10. In year 10, his ownership remains at 9% and he is an officer or director of the foreign corporation and an unrelated US person acquires 15% ownership of the foreign corporation.

He must file as a Category 2 filer for year 10, and the unrelated US person must file as a Category 3 filer.

***Each of the next 5 types of acquisitions is independent of the other, and each follows directly on situation 10.***

11a. In year 11 his ownership remains at 9% and the unrelated US person acquires an additional 27% ownership raising his ownership to 42%. The foreign corporation is not Controlled Foreign Corporation (CFC), though, because only 42% is owned by US persons owning at least 10% each. The 9% ownership share is not counted in the CFC computation (a US shareholder is defined as a US person owning at least 10%).

He must file as a Category 2 filer for year 10, and the unrelated US person must file as a Category 3 filer.

11b. In year 11 he acquires an additional 42% ownership raising his ownership to 51%.

He must file as a Category 4 filer because he owns more than 50%. He also files as a Category 5 filer for year 11 because the corporation has become a CFC; 66% of the ownership is by US shareholders (a US shareholder is defined as a US person owning at least 10%).

11c. In year 11 he acquires an additional 41% ownership raising his ownership to 50%. Either his wife or son (each a US person) acquires a 22% ownership.

He does not file as a Category 4 filer because he does not own more than 50% directly. The constructive ownership rules do not apply to Category 4 (nor to Categories 2 or 3).

Instead, he files as a Category 5 filer for year 11 because the corporation has become a CFC due to the fact that he directly and constructively owns 87% under the constructive ownership rules (see Treas. Reg. sections 1.6038-2(b)(c) and IRC section 318(a)), *i.e.*, 87% of the ownership is by US shareholders (a US shareholder is defined as a US person owning at least 10%).

Note that constructive ownership under section 318(a)(1)(A) includes spouse, children, and parents, but not great-grandchildren, grandparents or siblings.

**11d.** In year 11 his father (a US citizen) acquires a 42% ownership.

Because his father is a US person, per section 958(b) he constructively owns his father's 42% thus raising his ownership to 51% under the attribution rules of section 318. He must file as a Category 5 filer for year 11 because the corporation has become a CFC; 66% of the ownership is by US persons who are US shareholders (a US shareholder is defined as a US person owning at least 10%).

But he does not file as a Category 4 filer because the constructive ownership rules do not apply to Category 4 (nor to Categories 2 or 3) and he does not personally have more than 50% ownership.

**11e.** In year 11 his father (a nonresident alien) acquires a 42% ownership.

Because nonresident aliens are not US persons per section 957(a)(2) which references section 958(b)\*, the constructive ownership rules do not apply to his father's ownership. Therefore he does not constructively own his father's 42% and the corporation has not become a CFC. He does not file as a Category 5 filer for year 11. Only 15% of the ownership is by US shareholders (a US shareholder is defined as a US person owning at least 10%).

*\*Section 958(b) references section 318(a)(1)(A) to exclude constructive ownership of interests owned by nonresident alien members of a family as listed under section 318(a)(1)(A) (spouse, children, parents, and grandparents). Those interests are not treated as constructively owned by a US-person family member. (Please note that this is not the case for ownership by a nonresident alien family member of an interest in a foreign partnership if the US person directly or indirectly owns an interest in the foreign partnership. In that case, the constructive ownership rules of section 267(c)(2) and (4) apply per Treas. Reg. section 1.6038-3(b)(4), and the nonresident alien family member's interest is constructively owned by the US person.)*

But he must file as a Category 4 filer because, under the Section 6038 filing requirements, Treas. Reg. section 301.6038-2(c)(3) references the attribution rules of section 318(a) but does not exclude family members defined in section 318(a)(1)(A) who are NRAs (spouses, children, parents, or grandparents).

Interestingly the Form 5471 instructions exempt him (the US person) from the filing requirements under Category 4 or 5 if he does not own a direct or indirect interest in the foreign corporation, and is required to file Form 5471 solely because of constructive ownership from a nonresident alien. As discussed above, this is not what the Treasury Regulations say. In this case, to be completely safe given the established legal precedent that the IRS is not bound by its tax form instructions, he should file as a Category 4 filer.

**11f.** In year 11 he acquires an additional 42% ownership raising his ownership to 51%. In that same year, the foreign corporation (hereinafter referred to as FC-A) acquires 100% of the shares of FC-B.

He must file as a Category 4 filer because he owns more than 50% of FC-A. He also files as a Category 5 filer for year 11 because FC-A has become a CFC; 66% of the ownership is by US shareholders (a US shareholder is defined as a US person owning at least 10%).

He also must file a separate Form 5471 for year 11 as both a Category 4 and a Category 5 filer for FC-B because, per section 958(a)(2), he is treated as owing 51% of the shares of FC-B.

***The following type of acquisition is independent of the types under 11, and it follows directly on situation 9.***

**12.** In year 11 his brother (a US citizen) acquires a 42% ownership.

Even though his brother is a US person per section 958(b), the constructive ownership rules do not apply to the sibling's ownership. Therefore he does not constructively own his brother's 42%.

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The corporation has not become a CFC because his 9% ownership does not count as a US owner under section 958(b) because ownership shares that are less than 10% are not counted (a US shareholder is defined as a US person owning at least 10%). He does not file as a Category 5 filer for year 11.

Nor does he file as a Category 4 filer because he does not personally have more than 50% ownership.

But he must file as a Category 3 filer because he increased his ownership to 10% or more by constructively owning his brother's shares. The constructive ownership provisions applying to acquisitions and divestitures of ownership fall under section 6046(c) rather than section 958(b). Under section 6046(c), constructive ownership includes one's spouse, children, siblings, ancestors and lineal descendants only if they are US citizens or residents (section 6046(a)).

## **II. Ownership of a Foreign Corporation by a Nonresident Alien Who Becomes a US Person**

1. A nonresident alien's ownership (directly, indirectly and constructively) of a foreign corporation at the time he becomes a US person is in the 10% to 50% range. This includes a foreign person who elects to be a US person under section 6013(g) or (h).

He must file as a Category 3 filer because he became a US person while meeting the 10% stock ownership requirement with respect to the foreign corporation.

2. A nonresident alien's ownership (directly, indirectly and constructively) of a foreign corporation at the time he becomes a US person (including by section 6013(g) or (h) election) is more than 50%.

He must file as a Category 4 filer because he owns more than 50% of the foreign corporation. He also files as a Category 5 filer because the foreign corporation is a controlled foreign corp (CFC).

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