

Filing Categories For Form 5471: Understanding the Nuances of the Filing Categories

By Robert J. Misy, Jr.*



Tax professionals have always been intimidated by the various categories of filers of Form 5471. Previously, there were only four categories that were oddly numbered two through five. The latest version of Form 5471 provides for categories one through five with both a new Category 1 and an old Category 5 consisting of three subcategories.

This article will discuss the numerous filing categories starting with old categories two through four before evaluating the new subcategories for Category 5 filers and the new Category 1 filers. Determining the appropriate filing category(ies) is critical to determining the schedules to file. A typical Form 5471 filer will file pursuant to more than one category.

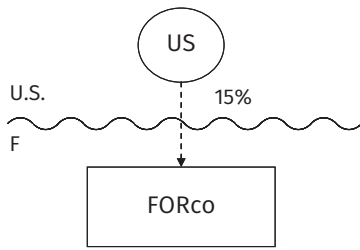
Categories 2 and 3 are referred to as transactional filings because the Internal Revenue Service (“IRS”) only requires their filing during the year of the underlying transaction. The schedules for these transactional filings require minimal financial information. However, the transactional filings include Schedule G, “Other Information,” for which an affirmative answer to any of the numerous queries will result in the IRS inquiring about an additional international return.

Certain U.S. officers and directors constitute Category 2 filers.¹ A U.S. officer or director is a Category 2 filer when a U.S. person (not necessarily the filer) acquires a 10% stock interest or an additional 10% stock interest in a foreign corporation.²

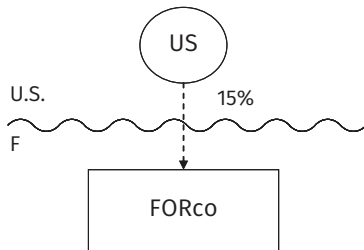
Example 1. Uncle Sam is a U.S. individual who acquires, during the taxable year, 15% of the outstanding stock of FORco, a foreign corporation. Among the officers of FORco is George Washington, the Chief Financial Officer, who is also the only U.S. person who is on FORco’s Board of Directors. Because George Washington is a U.S. person who is an officer, as well as a director, of FORco, George Washington is a Category 2 filer even though George Washington does not own any shares.

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EXAMPLE 1.



EXAMPLE 2.



A U.S. person has acquired stock in a foreign corporation when that U.S. person has an unqualified right to receive the stock, even though the stock is not actually issued.³ A U.S. person is either (a) a U.S. citizen or (b) a resident alien by virtue of either holding a green card or being physically present in the United States for 183 days over the past three years.⁴ A shareholder meets the 10% threshold by owning either (i) 10% or more of the total value of the foreign corporation's stock, or (ii) 10% or more of the total combined voting power of all classes of stock with voting rights.

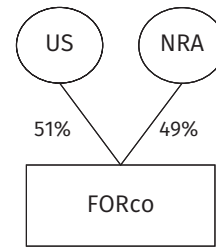
Category 3 filers include U.S. persons who either acquire 10% or more of the stock of a foreign corporation⁵ or acquire stock that, without regard to stock already owned on the date of the acquisition, meet the 10% stock ownership requirements with respect to the foreign corporation.⁶

Example 2. Uncle Sam is a U.S. individual who acquires, during the taxable year, 15% of the outstanding stock of FORco, a foreign corporation. Because Uncle Sam has acquired more than 10% of the stock in a foreign corporation, Uncle Sam is a Category 3 filer.

Category 3 filers also include:

- U.S. shareholders of captive foreign insurance companies⁷;
- Foreign 10% shareholders who become U.S. persons, such as a nonresident alien becoming a U.S. resident⁸; or

EXAMPLE 3.



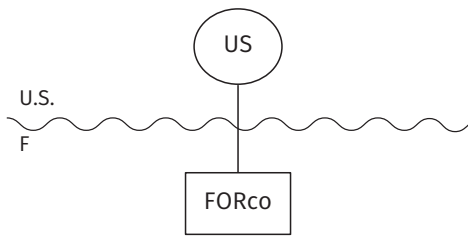
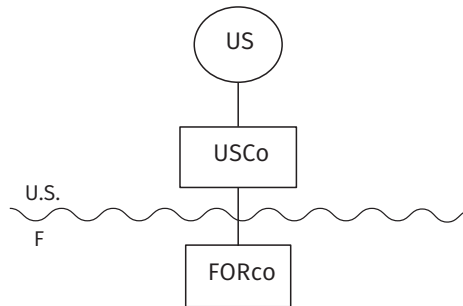
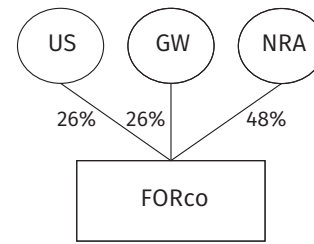
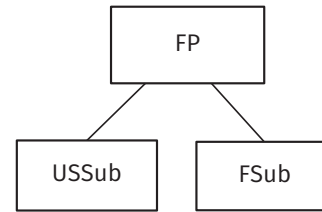
- U.S. persons who dispose of sufficient stock in the foreign corporation to reduce their ownership interest to less than 10%.⁹

Categories 4 and 5 are referred to as annual filings because the IRS requires their filing each year the underlying ownership occurs. In determining the ownership thresholds for the annual filings, the filer applies the constructive attribution rules of Code Sec. 318.¹⁰ However, there is no attribution from a foreign person to a U.S. person under the “to-entity” attribution rules.¹¹ Moreover, the “from-entity” attribution to a 50% shareholder is reduced to a 10% threshold.¹²

As with the transactional filings, the annual filings require Schedule G “Other Information,” for which an affirmative answer to any of the numerous queries will result in the IRS inquiring about an additional return. However, the schedules for these annual filings require significant financial information of the foreign corporation. In addition to an Income Statement (Schedule C) and a Balance Sheet (Schedule F), the schedules require computation of Foreign Income Taxes (Schedule E), Subpart F Income (Schedule I), Global Intangible Low-Taxed Income (Schedule I-1), Current Earnings and Profits (Schedule H), Accumulated Earnings and Profits (Schedule J), and Intercompany Transactions (Schedule M). The amount of financial information for the foreign corporation is similar to that of a U.S. corporate tax return on Form 1120.

A Category 4 filer is any U.S. person who controls a foreign corporation for at least 30 days during the taxable year. Control means the ownership of stock having over 50% of the voting power or value of all the stock of the foreign corporation.¹³

Example 3. Uncle Sam, a U.S. person, owns 51% of the stock of FORco, a foreign corporation, for the entire taxable year. Norman Ray Allen, a nonresident alien, owns the remaining 49%. Because Uncle Sam controls the foreign corporation for the entire taxable year, which is more than 30 days, Uncle Sam is a Category 4 filer.

EXAMPLE 4.**EXAMPLE 5.****EXAMPLE 6.****EXAMPLE 7.**

Category 5 reporting applies to a U.S. Shareholder of a Controlled Foreign Corporation (“CFC”) for 30 days or more during the year and who owns stock on the last day of the year.¹⁴ A foreign corporation is a CFC if, on any day during the foreign corporation’s taxable year, U.S. Shareholders own either more than 50% of the combined voting power of all classes of stock or more than 50% of the total value of the foreign corporation.¹⁵ The 50% test only considers U.S. Shareholders. Subpart F defines a U.S. Shareholder as any U.S. person *owning at least 10%* of the total combined voting power of all classes of voting stock of the foreign corporation.¹⁶ The IRS considers all forms of ownership, including direct, indirect (*i.e.*, beneficial ownership through intervening entities), and constructive (*i.e.*, attribution of ownership from one related party to another), in applying both the 10% shareholder and the 50% aggregate ownership tests.¹⁷ By application of the definition of a CFC, a Category 5 filer will also be a Category 4 filer.

A Category 5-a filing occurs when a U.S. Shareholder is related to FORco,¹⁸ under either direct or indirect ownership.¹⁹

Example 4. Uncle Sam owns 100% of FORco. By directly owning 100% of FORco, Uncle Sam is a Category 5-a filer and, of course, a Category 4 filer.

Example 5. Uncle Sam owns 100% of USCo, which owns 100% of FORco. By indirectly owning 100%

of FORco (through USCo), Uncle Sam is a Category 5-a filer.

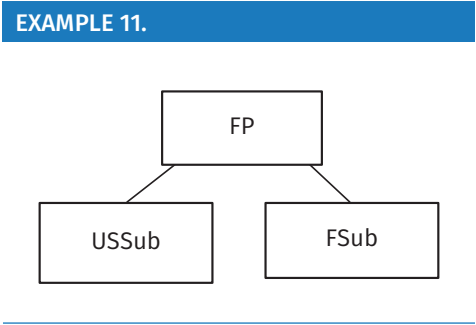
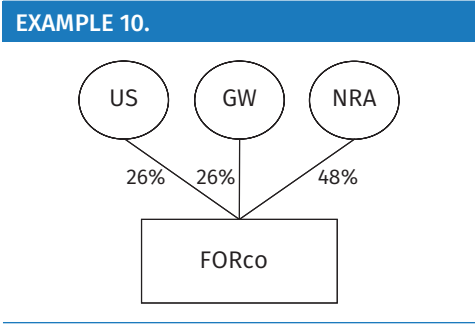
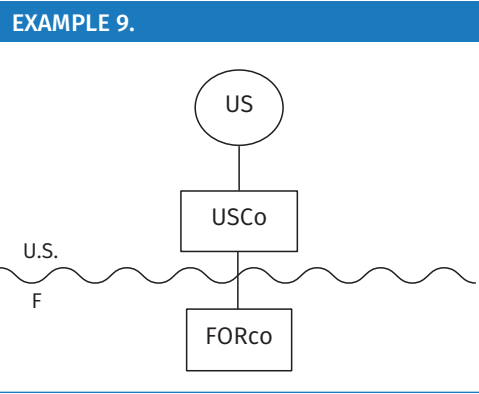
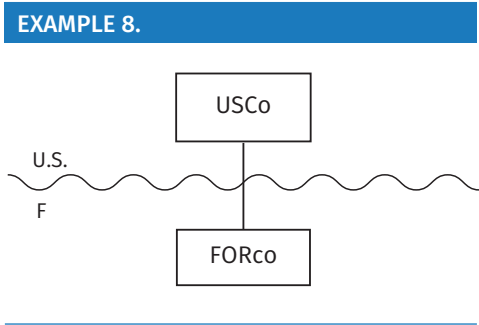
If the U.S. Shareholder does not directly or indirectly own more than 50%, the U.S. Shareholder is unrelated and is a Category 5-b filer, which has fewer reporting schedules.

Example 6. Uncle Sam and George Washington, both U.S. persons, each own 26% of FORco for the entire taxable year. The remaining 48% is owned by Norman Ray Allen, a nonresident alien. Because the two 10% shareholders, Uncle Sam and George Washington, combine to own more than 50% of the value of FORco during the entire taxable year, FORco is a CFC and Uncle Sam and George Washington are both U.S. Shareholders who are Category 5-b filers.

A U.S. Shareholder that is a related corporation *via* constructive ownership²⁰ is a Category 5-c filer.

Example 7. Foreign Parent owns 100% of both USSub and FSub. Under constructive attribution,²¹ USSub constructively owns the FSub shares owned by Foreign Parent. Accordingly, USSub owns all the FSub shares, rendering USSub a U.S. Shareholder of a CFC (FSub). USSub is a Category 5-c filer.

The new Category 1 filings leverage on the definition of a Specified Foreign Corporation (“SFC”) under the transition tax.²² An SFC is either (1) a CFC or (2) any



foreign corporation with a U.S. C corporation as a U.S. Shareholder. The transition tax required the U.S. Shareholder to include any accumulated earnings and profits of the foreign subsidiary as income in 2017.²³ Procedurally, a U.S. Shareholder could have availed itself of either an installment election or as an S corporation election to defer their tax due. An installment election permitted any recipients of a deemed repatriation under the transition tax to defer the tax over eight years of installment payments *via* an election.²⁴ A U.S. Shareholder of an S corporation could make an S corporation election to indefinitely defer the tax.²⁵ A variety of events could trigger a payment of tax after either election.

Similar to the subcategories under Category 5 filings, Category 1 also has three subcategories—1-a, 1-b, and 1-c.

Subcategory 1-a applies to a Category 1 filer where the SFC is a related party, considering both direct and indirect ownership,²⁶ that is a CFC. The subcategory 1-a schedules require the most financial information of the Category 1 filing subcategories.

Example 8. USCo, a U.S. C corporation, owns 100% of FORco. By directly owning 100% of FORco, USCo is a related CFC and, accordingly, an SFC. So USCo is a Category 1-a filer.

Example 9. Uncle Sam owns 100% of USCo, which owns 100% of FORco. By indirectly owning 100%

of FORco (through USCo), Uncle Sam is a Category 1-a filer.

Subcategory 1-b applies to an unrelated U.S. Shareholder of an SFC and, accordingly, requires fewer reporting schedules.

Example 10. Uncle Sam and George Washington, both U.S. persons, each own 26% of FORco for the entire taxable year. The remaining 48% is owned by Norman Ray Allen, a nonresident alien. Because the two 10% shareholders, Uncle Sam and George Washington, combine to own more than 50% of the value of FORco during the entire taxable year, FORco is a CFC (and, accordingly, an SFC) and Uncle Sam and George Washington are both unrelated U.S. shareholders who are Category 1-b filers.

Subcategory 1-c applies to a U.S. Shareholder of a foreign corporation that is related only *via* constructive ownership.

Example 11. Foreign parent owns 100% of both USSub and FSub. Under constructive attribution,²⁷ USSub constructively owns the FSub shares owned by foreign parent. Accordingly, USSub owns all the FSub shares, rendering USSub a U.S. Shareholder of a CFC (FSub), which is an SFC. USSub is a Category 1-c filer.

Because the policy of the transition tax was to clear the accounts for accumulated earnings and profits of foreign

corporations in anticipation of the dividends received deduction regime that began in 2018,²⁸ it seems odd that Category 1 filings would apply to an SFC that did not exist in 2017. Schedule J (*Accumulated Earnings and Profits*) and Schedule P (*Previously-Taxed Earnings and Profits*) that all Category 1 filers file appear to overlap with the types of filings the Category 5 filers must file.

In future revisions, the IRS should exclude post-2017 incorporated foreign corporations from the Form 5471 definition of an SFC.

Form 5471's new filing categories and subcategories have added more complexity to an already complex information reporting form. The IRS should strive to simplify Form 5471.

ENDNOTES

* Robert J. Misy previously worked for the IRS Chief Counsel (International) in Washington, DC and San Jose, CA before managing the international tax practice of a region of a Big Four firm. He is a graduate of the law schools at Vanderbilt University and Georgetown University and has authored books on international taxation and federal tax procedure. Robert is a member of the Board of Advisors for the INTERNATIONAL TAX JOURNAL.

¹ Code Sec. 6046(a)(1)(A).

² Instructions for Form 5471.

³ Reg. §1.6046-1(f)(1).

⁴ Code Sec. 7701(b). The 183-day test counts each day this year as a whole day, each day last year

as one-third of a day, and each day two years ago as one-sixth of a day.

⁵ Code Sec. 6046(a)(1)(B)(i).

⁶ Code Sec. 6046(a)(1)(B)(ii).

⁷ Code Secs. 953(c) and 6046(a)(1)(C).

⁸ Code Sec. 6046(a)(1)(D).

⁹ Reg. §1.6046-1(c)(1)(ii)(C). There is no statutory authority for this regulatory requirement.

¹⁰ Code Sec. 6038(e)(1).

¹¹ Code Sec. 6038(e)(1).

¹² Code Sec. 6038(e)(1).

¹³ Code Sec. 6038(e); Reg. §1.6038-2(b).

¹⁴ Code Sec. 6038(a)(4).

¹⁵ Code Sec. 957(a).

¹⁶ Code Sec. 951(b).

¹⁷ Code Sec. 958.

¹⁸ Code Sec. 954(d)(3).

¹⁹ Code Sec. 958(a).

²⁰ Code Sec. 954(b).

²¹ Code Sec. 318(a)(3)(C) and Reg. §1.958-2(d)(1)(iii).

²² Code Sec. 965.

²³ Code Sec. 965(a).

²⁴ *Id.*

²⁵ Code Sec. 965(i).

²⁶ Code Sec. 958(a).

²⁷ Code Sec. 318(a)(3)(C) and Reg. §1.958-1.

²⁸ Code Sec. 245A.



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