Flume and Form 5471 Penalties for Unreported Foreign Corporations: A Glimpse at Unique Aspects of an International Tax Dispute

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Hale E. Sheppard examines issues that are relevant not only to Flume but also to all taxpayers with interests in foreign accounts, foreign entities, and/or other foreign assets.

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I. Introduction

Fighting the IRS on just one front is difficult, but battling the tax authorities in multiple procedures at the same time can be downright challenging, not to mention expensive, time-consuming, and frustrating. Unfortunately for taxpayers with international aspects, defending themselves against the IRS often requires participation in several administrative or judicial actions, even though the proposed taxes and penalties all arise from the same set of facts. A perfect example of this phenomenon is *Flume*, a recent Tax Court case focusing on whether the taxpayers had a duty to file Forms 5471 (*Information Return of U.S. Persons with Respect to Certain Foreign Corporations*) to report certain foreign entities and whether the IRS was entitled to pursue levy actions to secure payment of the relevant penalties.[1] This article examines a long list of interesting tax, legal, and procedural issues that are relevant not only to *Flume* but also to all taxpayers with interests in foreign accounts, foreign entities, and/or other foreign assets.

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II. Overview of Form 5471 Duties and Penalties

In order to appreciate the significance of *Flume*, one must first have some understanding of the Form 5471 filing requirement. Four categories of U.S. persons

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who are officers, directors, and/or shareholders of certain foreign corporations ordinarily must file a Form 5471 with the IRS[2]:

A Category 2 filer is a U.S. individual (*i.e.*, U.S. citizen or U.S. resident) who is either an officer or director of a foreign corporation in which a U.S. person has acquired during the relevant year (i) stock in the foreign corporation that meets the "10 percent ownership test" or (ii) an additional 10 percent or more of the stock of the foreign corporation. For these purposes, the "10 percent ownership test" is met if the U.S. person owns 10 percent or more of the foreign corporation by vote or value.

- A Category 3 filer includes several types of persons, including any U.S. person who acquires stock in a foreign corporation, and when such stock is added to any stock that the U.S. person already owns, he meets the "10 percent ownership test" described above.
- A Category 4 filer is a U.S. person who had "control" of a controlled foreign corporation ("CFC") for an uninterrupted period of 30 days during the relevant year, which means that such U.S. person held more than 50 percent of the stock of a CFC by vote or value. For these purposes, a "CFC" is a foreign corporation that has "U.S. shareholders" who/that own (directly, indirectly, or constructively) more than 50 percent of the total voting power or stock value of the foreign corporation on any day of the relevant year.
- A Category 5 filer is a " U.S. shareholder" who/that owns stock in a foreign corporation that is a CFC for at least 30 uninterrupted days during the relevant year and who/that held the stock on the last day of the relevant year. In this context, the term " U.S. shareholder" means any U.S. person who/that owns (directly, indirectly, or constructively) 10 percent or more of the foreign corporation, by vote or value.

Form 5471 is filed as an attachment to the U.S. person's federal income tax return, which, in the case of individuals, is Form 1040 (*U.S. Individual Income Tax Return*).[3] If a person fails to file a Form 5471, files a late Form 5471, or files a timely but "substantially incomplete" Form 5471, then the IRS may assert a penalty of $10,000 per violation, per year.[4] This standard penalty increases at a rate of $10,000 per month, to a maximum of $50,000, if the problem persists after notification by the IRS.[5]

The IRS will not impose penalties if there was "reasonable cause" for a missing Form 5471 or late Form 5471. Additionally, the IRS will refrain from assessing penalties if the U.S. person filed a timely Form 5471 with certain omissions or inaccuracies, provided that it was "substantially complete."[6]

III. Newest Form 5471 Penalty Case

This brings us to the most recent case involving Form 5471 penalties, *Flume*, which was decided by the Tax Court in January 2017. The facts of the case, as well as the positions of the parties, have been cobbled together to the best of the author's ability using multiple sources.[7]

Mr. Flume ("Husband") and Mrs. Flume ("Wife") are U.S. citizens who moved to Mexico in 1993. Before heading south, Husband worked as an urban planner and real estate developer in the United States. Husband was engaged in the same type of activities in Mexico, operating a real estate company that developed land, sold lots, and built high-end homes.

In 1995, Husband and another U.S. individual, Norwick Adams, formed a corporation in Mexico called Franchise Food Service de Mexico S.A. de C.V. ("Franchise Food"). They started as equals, each owning 50 percent, *i.e.*, 25,000 of the 50,000 total shares. Husband was also the President. Franchise Food was created in order to operate Mexican locations of Whataburger and Fanny Ice Cream. These two establishments were sold in 1998, but Franchise Food remained in existence. Husband claimed that he sold 20,500 of his shares in February 2002 to the wife of Mr. Adams, who was a Mexican citizen and resident. The sale had the effect of reducing Husband's ownership in Franchise Foods to 4,500 shares, which was nine percent. Although not discussed in *Flume*, Husband presumably engaged in this stock sale in an attempt to alleviate the duty to file Forms 5471 for Franchise Food after 2002; he likely took the position that he was not a Category 5 filer because he was not a "U.S. shareholder."

In addition to Franchise Food, Husband and Wife formed at least two other foreign corporations, one of which was Wilshire Holdings, Inc. ("Wilshire Belize"). This entity was formed in 2001, in Belize, with just two bearer shares. Certificate 1, worth 25,000 shares, was assigned to Husband. Certificate 2, also worth 25,000 shares, pertained to Wife. Husband denied this ownership throughout the tax dispute, alleging that on the same day that Wilshire Belize was formed in 2001, "amended" articles of association took effect, which changed the original ownership structure to the following: (i) Certificate 3 showed that Victor M. Mendez Tornell, a Mexican citizen and resident, and, coincidentally, the spouse of the architect who worked for Husband in his Mexican real estate business, owned 36,500 shares, or 73 percent; (ii) Certificate 4 showed that Husband owned 4,500 shares, or nine percent; (iii) Certificate 5 showed that Wife owned 4,500 shares, or nine percent; and (iv) Certificate 6 showed that the daughter of Husband and Wife owned 4,500 shares, or nine percent. Husband

offered no proof of this new ownership structure other than the "amended" articles of association, which he ultimately admitted to the Tax Court had been "backdated."

In 2005, Wilshire Belize opened an account at UBS in Switzerland. A number of documents and communications related to such account undermined the position by Husband that he was just a minor owner of Wilshire Belize. For instance, Husband and Wife opened the Swiss account using the original articles of association (showing Husband and Wife as 50/50 owners) and not the "amended" articles of association described above; Husband and Wife were listed as the "beneficial owners" of the account; Husband signed account-related documents in his capacity as "First Director" of Wilshire Belize; Husband and Wife controlled the investment activity in the account; and Husband and Wife signed the wire-transfer orders in 2008 and 2009, as "directors" of Wilshire Belize, to empty the Swiss account and remit all funds to a U.S. account. With respect to this last action, the IRS asked the Tax Court to infer that the motive of Husband and Wife in domesticating the Swiss funds in 2008 and 2009 was to avoid being caught as a result of the IRS's criminal investigation of UBS: "In March and July 2008, [Husband] extensively discussed with a UBS representative the Internal Revenue Service's investigation of UBS [and] during a discussion with a UBS representative on July 3, 2008, [Husband] was preoccupied with and worried about the Internal Revenue Service's investigation of UBS."

Husband and Wife filed timely Forms 1040 for 2001 through 2009, but they did not attach any Forms 5471 for Franchise Food or Wilshire Belize.

The IRS started an audit in 2012, presumably as a result of data that the IRS received directly from UBS in connection with its criminal investigation of UBS.[8] The revenue agent sought information from Husband and Wife during the audit using various tools, including information document requests ("IDRs") and at least one formal document request ("FDR"). Husband and Wife only partially responded to these demands by the revenue agent. Therefore, in August 2012, the revenue agent sent pre-assessment notices about potential Form 5471 penalties. Then, in October 2012, the revenue agent sent a letter warning Husband and Wife that additional penalties of $10,000 per month would be imposed until they filed the required Forms 5471. In January 2013, Husband sent to the revenue agent Forms 5471 for 2001 and 2002 with respect to Franchise Food, but he filed no Forms 5471 for Wilshire Belize. In February and March 2013, the revenue agent assessed a total of $110,000 in Form 5471 penalties, as follows: (i) $20,000 for 2001, for penalties related to Franchise Food and Wilshire Belize; (ii) $20,000 for 2002, for penalties related to Franchise Food and Wilshire Belize; and (iii) $10,000 for each of 2003, 2004, 2005, 2006, 2007, 2008, and 2009 for penalties related only to Wilshire Belize.

Husband did not voluntarily pay the Form 5471 penalties, so the IRS eventually sent him the pre-levy notice in December 2013, indicating that the IRS intended to start seizing assets in order to satisfy the penalties and notifying Husband of his right to request a collection due process ("CDP") hearing. Husband filed a timely request for a CDP hearing, claiming, among other things, that (i) the Forms 5471 for 2001 and 2002 for Franchise Foods, filed with the revenue agent approximately a decade late and only in response to a letter from the revenue agent warning of imminent penalties, sufficed to satisfy the filing duty; and (ii) Husband was not required to file Forms 5471 for Wilshire Belize for 2001 through 2009 because he had only a nine-percent ownership interest, and thus was not a "U.S. shareholder," or Category 5 filer.

Fighting the IRS on just one front is difficult, but battling the tax authorities in multiple procedures at the same time can be downright challenging, not to mention expensive, time-consuming, and frustrating.

The IRS settlement officer conducting the CDP hearing rejected the first argument on grounds that the Forms 5471 for Franchise Food were filed years after the fact and, in all events, were "inaccurate and incomplete" because they were filed under the wrong Category and had "$0" or "unknown" written in several boxes. The settlement officer rejected the second argument too, pointing out that the revenue agent had obtained "compelling third-party documentation" from UBS showing that Husband and Wife were owners, officers, and directors of Wilshire Belize from 2001 through 2009. Husband did not provide the settlement officer with a narrative explaining why "reasonable cause" existed for the violations and did not present a collection alternative, such as an offer-in-compromise or installment agreement. Accordingly, the settlement officer issued his notice of determination concluding that the IRS was free to proceed with the proposed levy of assets.

Husband was not willing to go down without a fight; he filed a timely petition with the Tax Court challenging the conclusions reached by the settlement officer

in the notice of determination. This petition was brief, completed using the fill-in form available on the Tax Court website. Husband summarized his entire case for the Tax Court in the following manner: "Taxpayer has complied with Form 5471 reporting requirements as required by law and has filed the appropriate tax forms" and "Taxpayer has documents and IRS filings indicating proper filing of tax forms in accordance with ownership of tax reporting entities."

In their pre-trial memo to the Tax Court, the IRS attorneys essentially took the same main positions as those adopted earlier by the settlement officer in connection with the CDP hearing. First, the IRS attorneys argued that penalties related to Franchise Food for 2001 and 2002 were appropriate because the Forms 5471 were filed approximately a decade after the deadline, they were filed under the wrong Category, such that the appropriate schedules on Forms 5471 had not been filled in, and they were "incomplete and inconsistent with the information" that Husband previously supplied to the revenue agent during the audit. Second, the IRS attorneys maintained that, despite Husband's claim that he only owned nine percent of Wilshire Belize from 2001 through 2009, the documents show that he personally owned 50 percent and constructively owned another 50 percent through his wife. This renders Wilshire Belize a CFC and requires the filing of a Form 5471. Third, the IRS attorneys reminded the Tax Court that the revenue agent issued an FDR in December 2012 with which Husband had failed to substantially comply. Thus, the IRS attorneys warned that they would ask the Tax Court to ban the attempted introduction by Husband of any foreign-based documentation covered by the FDR that was not provided to the revenue agent in a timely manner in response to the FDR.

In his post-trial memo to the Tax Court, Husband presented the same arguments that he had previously (and unsuccessfully) raised with settlement officer during the CDP hearing. They consisted of the fact that (i) the Forms 5471 for 2001 and 2002 for Franchise Food, filed with the revenue agent during the audit in 2013, sufficed to satisfy the filing duty; and (ii) Husband was not required to file Forms 5471 for Wilshire Belize for 2001 through 2009 because he had only a nine-percent ownership interest.

Along with these longstanding arguments, Husband introduced two new ones in his post-trial memo. First, he contended that the Forms 5471 for 2001 and 2002 were "substantially complete" because Franchise Food was "dormant" and thus had a less-stringent filing requirement under Rev. Proc. 92-70. As Husband explained, "[t]he first page of Form 5471 was completed correctly and substantially complies with the requirements of Form 5471." Second, Husband argued that he reasonably relied on his return preparer in Mexico.

The IRS attorneys, in their own post-trial memo, quickly attacked the Husband's new positions. They pointed out that Franchise Food was not dormant after the stock sale in February 2002, as it continued to be involved in a joint real estate venture for many years thereafter. Moreover, from a technical perspective, the IRS attorneys underscored that the "dormant" rules only apply if a CFC is dormant during the entire year at issue, and Franchise Food was active until at least February 2002.

In terms of the reasonable-reliance defense, the IRS attorneys explained that this is inapplicable because Husband could not demonstrate that his return preparer in Mexico was qualified to complete Forms 1040 and give related advice; he admitted that he never had a call or meeting with the preparer, and he conceded that he never provided the preparer information about Franchise Food or Wilshire Belize. The IRS attorneys summarized their resistance to the reasonable-reliance defense as follows: "Given [Husband's] testimony that he does not know his return preparer's professional qualifications and failed to provide necessary and accurate information, he cannot have relied on his preparer's advice, if any such advice were, in fact, given."

The Tax Court reduced this case to its essence in making its ruling. With respect to Franchise Food, the Tax Court concluded that (i) Husband was a Category 5 filer in 2001 and a Category 3 filer in 2002, thus obligated to file a Form 5471 for each year; and (ii) the argument that the Forms 5471 filed in 2013, years after the deadline and as a part of the audit, should be given "retroactive effect" lacks merit. Regarding Wilshire Belize, the Tax Court noted that Husband was a Category 4 and Category 5 filer for 2001 through 2009, and Husband "merely provided self-serving testimony and a backdated document to support his claim that he maintained only a 9% ownership interest during the tax years in issue." Finally, the Tax Court rejected the notion that Husband should be relieved of Form 5471 penalties under a reasonable-reliance theory because Husband was unable to demonstrate that his return preparer in Mexico had sufficient qualifications and expertise, and Husband never gave the preparer information about Franchise Food and Wilshire Belize during the relevant years.

IV. Interesting Aspects of Case

Like most Tax Court cases, *Flume* raises some interesting issues, many of which can only be found if one were to

review all the pleadings and have existing knowledge of the unique aspects of an international tax dispute. The issues are discussed below.

A. Assessable Penalties—Five Ways to Fight the IRS

Flume is interesting, in that it demonstrates how taxpayers might find themselves fighting Form 5471 penalties (and a long list of other international information returns penalties) on several different fronts, simultaneously or consecutively.

Form 5471 sanctions are "assessable" penalties. This means that, unlike other penalties that are related to tax returns (as opposed to information returns), taxpayers effectively get no opportunity to challenge Form 5471 penalties *before* they are "assessed," that is, placed in the IRS's records as a debt/liability of the taxpayer. These penalties are not addressed in an examination report, and the IRS will not include them in a notice of deficiency, such that taxpayers cannot quarrel over Forms 5471 penalties with the Tax Court, at the same time they challenge tax increases and related penalties.[9]

Because Form 5471 penalties are immediately "assessable" and not subject to the normal deficiency procedures, because the IRS's computers have been automatically assessing penalties for late Forms 5471 since 2009, and because the IRS often fails to place a freeze/hold on collection actions during the period that taxpayers are exercising their right to post-assessment, pre-payment review, taxpayers often find themselves challenging Form 5471 penalties in one or more of the following manners[10]:

- First, upon receipt of the initial penalty-assessment and collection notice, many taxpayers file a penalty-abatement request.
- Second, if the IRS rejects this penalty-abatement request, which is frequently the case, then taxpayers administratively appeal by filing a protest letter. Taxpayers ordinarily are instructed to direct their Protest Letter to the "Service Center Appeals Coordinator."
- Third, while waiting for an audience with the Appeals Office in response to the protest letter, the IRS often continues to take a variety of collection actions to recoup the Form 5471 penalties, including, but not limited to, filing a Notice of Federal Tax Lien, and/or issuing "Final Notice and Notice of Intent to Levy." When this occurs, taxpayers are obligated to file a request for a CDP hearing within a 30-day period, taking the position that the liens or proposed levies are improper because if the IRS were to grant penalty abatement, then the liability would disappear and collection actions by the IRS would become moot.
- Fourth, in situations where the settlement officer conducting the CDP hearing disagrees with the taxpayer, he will issue a notice of determination concluding that the IRS is authorized to continue with the lien or proposed levy. In response to the notice of determination, taxpayers, like those in *Flume*, can file a petition with the Tax Court, arguing that the settlement officer abused his or her discretion.
- Fifth, certain taxpayers choose to avoid the preceding procedures, opting instead to pay the Form 5471 penalties under duress, file an administrative claim for refund, and, if the IRS fails to respond to the claim within six months or issues a Notice of Disallowance, then taxpayers can initiate a refund lawsuit in federal court. Refund actions are also initiated by taxpayers when the IRS uses its power of "administrative offset" under Code Sec. 6402 to take a tax overpayment/refund from a later year and automatically apply it to satisfy Form 5471 penalties from an earlier year.

It is unclear from the record how many of the five methodologies the Husband utilized in *Flume*, and the situation was different from most, in that the Form 5471 penalties were assessed by a revenue agent during a field audit. Nevertheless, the case grants us the opportunity to review the multiple (and sometimes overlapping) manners in which taxpayers facing automatic Form 5471 penalties resist the IRS.

B. Evidence Exclusion Resulting from FDRs

Flume is interesting because it showcases one of the IRS's unique weapons in the context of audits involving international issues, the FDR. The revenue agent in *Flume* apparently issued various IDRs to Husband, seeking information and documentation about foreign accounts and foreign entities. Dissatisfied with the amount or type of data provided in response to the IDRs, the revenue agent decided to issue an FDR at some point.

Code Sec. 982(a) generally provides that if a taxpayer fails to "substantially comply" with an FDR issued by the IRS during an audit regarding the proper tax treatment of any item, then, if the IRS later files a motion with the court tasked with determining the proper tax treatment, such court shall prohibit the taxpayer from introducing at trial any "foreign-based documentation" covered by the FDR.[11] Stated another way, if the taxpayer does not relinquish certain "foreign-based documentation" during the audit in response to an FDR, then the taxpayer essentially forfeits the ability to ever present such documentation to help his or her case. There are exceptions

to this general rule, of course. Code Sec. 982(b)(1) states that the prohibition against a taxpayer presenting at trial certain "foreign-based documentation" does not apply in situations where the taxpayer can demonstrate that the failure to provide the documentation in response to the FDR was due to "reasonable cause."[12]

The world becomes more globalized each day, and the complexity of international tax rules, procedures, and disputes increases accordingly.

The main events commonly leading to a dispute over an FDR are as follows. The IRS initiates an audit. The revenue agent then issues IDRs to the taxpayer requesting certain information and/or documentation, some of which may pertain to international issues. The taxpayer has several practical and strategic reasons for "cooperating" during an audit, which requires responding to IDRs. First, if a taxpayer provides the IRS with all potentially relevant data during an audit, including items requested in IDRs, there is a chance that the taxpayer might convince the revenue agent that the tax returns under audit are accurate, and the IRS should issue a "no change" letter to conclude the matter.

Second, Code Sec. 7491(a) and Tax Court Rule 142(a)(2) generally provide that if a taxpayer introduces "credible evidence" with respect to any factual issue relevant to determining the liability of the taxpayer, then the IRS will have the burden of proof in any court proceeding. Code Sec. 7491(a)(2) states that this burden-shifting rule only applies if the taxpayer has complied with all substantiation requirements, has maintained all necessary records, and has "cooperated" with reasonable requests from the IRS for witnesses, information, documents, meetings, and interviews.

Third, a taxpayer responds to IDRs in order to potentially shift the burden of proof to the IRS in situations where the IRS is relying on so-called "naked Forms 1099" to assess additional income taxes against a taxpayer. Code Sec. 6201 provides that if a taxpayer raises a reasonable dispute with respect to an information return filed with the IRS by a third-party, and the taxpayer has "fully cooperated" with the IRS during the audit, then the burden of proof shifts to the IRS. In the context of Code Sec. 6201, "cooperation" means allowing the IRS access to, and inspection of all witnesses, information, and documents within the taxpayer's control.

Finally, a taxpayer responds to IDRs for purposes of positioning itself for fee reimbursement if the taxpayer manages to defeat the IRS. Code Sec. 7430 generally indicates that a taxpayer that is the "prevailing party" in a tax dispute may recoup reasonable costs from the IRS. The taxpayer will not be considered the "prevailing party," if the tax/legal position taken by the IRS was "substantially justified," and a significant factor in making this determination is whether the taxpayer presented "all relevant information" under the taxpayer's control, as well as "all relevant legal arguments" supporting the taxpayer's position. In other words, whether a taxpayer can recover fees pursuant to Code Sec. 7430 depends, in part, on the taxpayer "cooperating" during the tax dispute process.

Despite these four reasons for adequately responding to IDRs, some taxpayers still do not do so. The revenue agent has several options if this occurs. These include, but are certainly not limited to, (i) generating an unfavorable examination report for the taxpayer based on the limited data available, thereby obligating the taxpayer to challenge issues either with the Appeals Office or the Tax Court; (ii) issuing an administrative summons, and possibly seeking assistance from IRS attorneys to enforce the summons in court if the taxpayer neglects to fully comply; and/or (iii) sending the taxpayer an FDR, if the situation involves "foreign-based documentation."

Assuming that the revenue agent selects the third option (*i.e.*, resorting to an FDR), various actions could ensue. For instance, the taxpayer could simply ignore the FDR, in which case the revenue agent could conclude the audit based on the data at hand and then issue an examination report or Notice of Deficiency, as appropriate. If the taxpayer were to later challenge the proposed taxes and penalties in Tax Court or another appropriate court, the IRS could file a motion under the general rule in Code Sec. 982(a) to prohibit the taxpayer from introducing as evidence at trial, any "foreign-based documentation" that the taxpayer did not deliver in a timely manner to the revenue agent in response to the FDR. The taxpayer, of course, could raise defenses to this proposed exclusion of evidence by the IRS. The most common defenses would be that the taxpayer "substantially complied" with the FDR, and, even if this were not the case, there was "reasonable cause" for the taxpayer's non-compliance.[13]

In *Flume*, the revenue agent issued an FDR, to which Husband only partially responded. Accordingly, in its pretrial memo to the Tax Court, the IRS stated the following:

> The Revenue Agent issued a Formal Document Request (FDR) to petitioner on December 5, 2012.

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Petitioner failed to substantially comply with the FDR. Should petitioner attempt to introduce into evidence any foreign-based documentation covered by the FDR, [the] respondent will request that the Court prohibit the introduction of such evidence pursuant to the provisions of I.R.C. § 982(a).

C. Form 8938 Penalties

Flume is noteworthy in that it reminds us that, had the years at issue not been limited to 2001 through 2009, Husband likely would have been subjected to Form 8938 penalties, too.

Code Sec. 6038D, which mandates the filing of Form 8938, was enacted as part of the Foreign Account Tax Compliance Act ("FATCA").[14] The general rule in Code Sec. 6038D(a) can be divided into the following parts:

- Any specified person ("SP"),
- Who/that holds an interest,
- During any portion of a tax year,
- In a specified foreign financial asset ("SFFA"),
- Must attach to his/her/its timely tax return,
- A complete and accurate Form 8938,
- If the aggregate value of all SFFAs, and
- Exceeds the applicable filing threshold.

Holding an interest in an asset means different things in different contexts. When it comes to Form 8938, an SP generally holds an interest in an SFFA if any income, gains, losses, deductions, credits, gross proceeds, or distributions attributable to the holding or disposition of the SFFA are (or should be) reported, included, or otherwise reflected on the SP's annual tax return.[15] The regulations clarify that an SP has an interest in the SFFA *even if* no income, gains, losses, deductions, credits, gross proceeds, or distributions are attributable to the holding or disposition of the SFFA for the year in question.[16] The regulations also indicate that an SP must file a Form 8938, despite the fact that none of the SFFAs that must be reported affect the U.S. tax liability of the SP for the year.[17]

For purposes of Code Sec. 6038D, the term SFFA includes two major categories: (i) foreign financial accounts[18] and (ii) other foreign financial assets, which are held for investment purposes.[19] The second category includes stocks or securities issued by a non-U.S.-person, financial instruments or contracts held for investment purposes whose issuer or counterparty is a non-U.S.-person, and any interest in a foreign entity.[20] The regulations enlarge and clarify the categories, identifying the following items as SFFAs: (i) stock issued by a foreign corporation; (ii) a capital interest or profits interest in a foreign partnership; (iii) a note, bond, debenture, or other form of debt issued by a foreign person; (iv) an interest in a foreign trust; (v) an interest swap, currency swap, basis swap, interest rate cap, interest rate floor, commodity swap, equity swap, equity index swap, credit default swap, or similar agreement with a foreign counterparty; and (vi) any option or other derivative instrument with respect to any of the items listed as examples or with respect to any currency or commodity that is entered into with a foreign counterparty or issuer.[21]

If an SP fails to file the Form 8938 in a timely manner, then the SP "shall" pay a penalty of $10,000.[22] The penalty increases to a maximum of $50,000 if the SP does not rectify the problem quickly after contact from the IRS.[23] An SP who unintentionally fails to file a timely, accurate Form 8938 can avoid penalties under Code Sec. 6038D if the SP can demonstrate that the violation was due to reasonable cause and not due to willful neglect.[24]

Flume only addresses international violations from 2001 through 2009, and the Form 8938 filing requirement did not take effect until 2011. However, had the case involved later years, one can assume that the IRS would also have asserted penalties of $10,000 per year for the failure by Husband to report on Form 8938 all of his SFFAs, such as his interest in Franchise Food, Wilshire Belize, and the UBS account.

D. FBAR Penalties

Congress enacted the Bank Secrecy Act in 1970.[25] One purpose of this legislation was to require the filing of certain reports, like the FBAR, where doing so would be helpful to the U.S. government in carrying out criminal, tax, and regulatory investigations.[26] Among the important provisions of the Bank Secrecy Act is 31 USC §5314. This statute, in conjunction with the underlying regulations and FBAR Instructions, requires the filing of an annual FBAR in cases where (i) a U.S. person, including U.S. citizens, U.S. residents, and domestic entities, (ii) had a direct financial interest in, an indirect financial interest in, signature authority over, or some other type of authority over, (iii) one or more financial accounts, (iv) located in a foreign country, (v) and the aggregate value of such account or accounts exceeded $10,000, (vi) at some point during the calendar year at issue.[27]

Concerned with widespread non-compliance with the FBAR filing requirement, the U.S. government has taken certain actions in recent years. For instance, the Treasury Department transferred authority to enforce the FBAR provisions from the Financial Crimes Enforcement

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Network ("FinCEN") to the IRS.[28] The IRS is now empowered to investigate potential FBAR violations, issue summonses, assess civil penalties, issue administrative rulings, and take "any other action reasonably necessary" to enforce the FBAR rules.[29]

Congress, for its part, enacted new FBAR penalty provisions in October 2004 as part of the American Jobs Creation Act ("Jobs Act").[30] Under the law in existence before the Jobs Act, the government could only assert civil penalties against taxpayers where it could demonstrate that they "willfully" violated the FBAR rules.[31] Even if the government managed to satisfy this evidentiary standard, it was only authorized to assert civil FBAR penalties ranging from $25,000 to $100,000, depending on the highest balance of the unreported foreign accounts.[32]

Thanks to the Jobs Act passed in 2004, the IRS may now impose a civil penalty on any person who fails to file an FBAR when required, period.[33] In the case of non-willful violations, the maximum penalty is $10,000,[34] but the IRS cannot assert this penalty if the violation was due to "reasonable cause."[35] The Jobs Act calls for higher maximum penalties where willfulness exists. Specifically, in situations where a taxpayer deliberately failed to file an FBAR, the IRS may assert a penalty equal to $100,000 or 50 percent of the balance in the account at the time of the violation, whichever amount is larger.[36] Given the large balances in some unreported accounts, FBAR penalties under the Jobs Act can be enormous.

Flume is a Tax Court case, and the Tax Court made it clear several years ago, in a famous case called *Williams*, that it lacked jurisdiction to hear FBAR penalty cases, at both the pre-assessment stage and post-assessment collection stage.[37] The rationale for this limited power of the Tax Court originates in the fact that FBAR penalties are assessed under Title 31 of the U.S. Code, while the Code and its "tax" issues are located in Title 26 of the U.S. Code. Code Sec. 7422, which describes the authority of the Tax Court, states that the Tax Court and its divisions "shall have such jurisdiction as is conferred on them by this title [26] … "

Although FBAR issues were not addressed in *Flume* because it was a Tax Court case, one might assume that the IRS assessed, or could have assessed, FBAR penalties with respect to the UBS account. This is logical given that (i) the Tax Court held that the Husband had a reportable interest in the unreported UBS account because he owned more than 50 percent of Wilshire Belize, in whose name the account was held; (ii) the assessment period for FBAR penalties is six years from the date of the violation, and FBAR violations have historically occurred on June 30 of the calendar year after the year in question (*e.g.*, an FBAR violation for 2009 took place on June 30, 2010); (iii) the UBS account was not emptied until 2009; (iv) the IRS began its audit in 2012, at which time it likely could have assessed FBAR penalties for 2005 through 2009; and (v) the IRS concluded its audit and assessed multiple Form 5471 penalties (with full awareness of the UBS account) the next year, in 2013.

E. Do Not Forget About the Taxes

This article is focused on the Tax Court case addressing only Form 5471 penalties. It is important to understand, though, that it does not reflect *all* the problems that Husband and Wife had with the IRS. As one would expect in a situation involving expatriates, operating a business in Mexico, forming various foreign entities, and holding at least one foreign account, income tax issues also arose. These matters were addressed in separate litigation with the Tax Court, centered on alleged deficiencies in 2006, 2007, 2008, and 2009.[38] Among other things, the IRS claimed that Husband and Wife, as sole owners of Wilshire Belize, had unreported Subpart F income stemming from the investment income earned by the UBS account held in the name of Wilshire Belize.[39] Perhaps most interesting was the penalty charge by the IRS. In the Notice of Deficiency, the IRS took the position that (i) Husband and Wife understated the actual income that they received from their foreign entities; (ii) failed to report investment income earned by the UBS account; (iii) utilized Wilshire Belize, formed in a "tax haven country," to operate a business and make investments "in order to avoid paying U.S. income taxes on their worldwide income"; (iv) "intentionally sought to disguise their true ownership" of Wilshire Belize and Franchise Food by creating documents indicating that foreign individuals were the majority owners; (v) "purposely" opened the UBS account in the name of Wilshire Belize when they were the true owners with sole signature authority; and (vi) instructed UBS not to invest in U.S. securities in an effort to avoid detection. Despite this long list of allegations, the IRS merely asserted the lowest penalty, *i.e.*, the negligence penalty under Code Sec. 6662.[40]

F. First-Time Abatement Policy As Applied to Form 5471

The IRS has a general first-time-penalty-abatement policy, and taxpayers facing large Form 5471 penalties often cite

this policy in seeking relief.[41] This policy states that the IRS will grant abatement, with respect to virtually all delinquency penalties (including late-filing penalties under Code Sec. 6651, late-payment penalties under Code Sec. 6651, and federal tax deposit penalties under Code Sec. 6656) in situations where a taxpayer has not been required to file a certain return before, or the taxpayer has no prior penalties of this type.[42] If the taxpayer meets these criteria, then the IRS generally issues a letter to the taxpayer confirming that abatement is being granted solely on the basis of the first-time-penalty-abatement policy, not because the taxpayer has demonstrated that it had reasonable cause for the violation.[43]

`*Flume* is interesting in that, although there was no evidence presented that Husband had ever been penalized for not filing Forms 5471 before 2001, Husband did not raise the first-time-abatement policy in his defense. Consequently, neither the IRS nor the Tax Court had the opportunity to show how broadly or narrowly they would interpret this policy.

G. The "Decision Tree" for Form 5471 Penalties

In determining the appropriateness of penalties, the IRS and the courts often turn to general notions of "reasonable cause." Here are some common justifications accepted by the IRS. First, a taxpayer may establish reasonable cause by showing that it exercised ordinary business care and prudence but nevertheless was unable to comply with the law.[45] Second, a taxpayer's misunderstanding of fact or law may constitute reasonable cause. The regulations provide that "[c]ircumstances that may indicate reasonable cause and good faith include an honest misunderstanding of fact or law that is reasonable in light of all of the facts and circumstances, including the experience, knowledge, and education of the taxpayer."[46] Third, a taxpayer's ignorance of the law may give rise to reasonable cause. The IRS's Penalty Handbook acknowledges that reasonable cause "may be established if the taxpayer shows ignorance of the law in conjunction with other facts and circumstances," such as the level of complexity of a tax or compliance issue.[47] Fourth, a taxpayer's reasonable reliance on an independent, informed, qualified tax professional often reaches the level of reasonable cause.[48]

Form 5471 penalties generally are *not* resolved by applying the standards described above, but rather by utilizing an obscure "Decision Tree" designed by the IRS specifically for Form 5471 penalties. This "Decision Tree," found in the Internal Revenue Manual, features standards that are much more stringent than those located elsewhere.[49] The following guidance from the "Decision Tree" demonstrates that attaining abatement of Form 5471 penalties can be significantly more challenging than one might expect:

- If the taxpayer claims that it was unaware of the Form 5471 filing requirement, the "Decision Tree" instructs the IRS to deny abatement because "ordinary business care and prudence requires taxpayers to determine their tax obligations when establishing a business in a foreign country."
- The "Decision Tree" mandates that penalty abatement be denied where the taxpayer seeks clemency because of financial problems.
- The "Decision Tree" further indicates that the IRS will show no mercy in situations where a taxpayer states that Form 5471 was late because the transactions, tax laws, or business structure was complicated.
- If the taxpayer claims that multiple layers of ownership prevent the taxpayer from obtaining all the data necessary to file a timely Form 5471, the "Decision Tree" instructs the IRS not to abate penalties.
- Rejection of the penalty abatement request will also occur, according to the "Decision Tree," when the taxpayer cites challenges in obtaining the necessary foreign data as the excuse for late Forms 5471.
- The "Decision Tree" demands imposition of penalties if the reason for late Forms 5471 is that the person with sole authority to file Forms 5471 was absent for a reason other than death or serious illness. Moreover, even if death or serious illness of the sole responsible person is claimed, the IRS will only accept this justification if (i) the corporation can provide tangible proof, such as an insurance claim, police report, letters or bills from hospitals, or newspaper clippings describing the event; (ii) the absence was not foreseeable; (iii) the absence occurred before and in close proximity to the filing deadline; and (iv) the taxpayer filed the Forms 5471 within two weeks of when the absence ended.
- The IRS will not waive Form 5471 penalties under the "Decision Tree" if the taxpayer personally neglected to submit a filing-extension request. Likewise, the "Decision Tree" denies abatement where the taxpayer hired a third-party (such as an accounting firm) to prepare returns and believed, erroneously, that such third-party submitted a filing-extension request on behalf of the taxpayer.
- Abatement requests will also be rejected under the "Decision Tree" if the taxpayer relies on the ignorance-of-the-law defense and the taxpayer was either a U.S. resident or resided outside the United States but failed to hire and get advice from a U.S. tax professional.

- For purposes of seeking penalty abatement, the "Decision Tree" clarifies that reliance on an accountant or attorney might be appropriate in certain situations, but reliance by a taxpayer on the following types of people is not reasonable: Bookkeeper, financial advisor, business associate, information in a tax plan or promotion, and person assisting in establishing the corporation.
- Finally, the "Decision Tree" indicates that it might abate penalties based on the reasonable-reliance-on-a-qualified-tax-professional defense if, and only if, the taxpayer relied on an accountant or attorney; the taxpayer provided such tax professional all relevant information; the taxpayer supplied the information before the deadline for filing Form 5471; the tax professional advised the taxpayer that it was not required to file Form 5471; the taxpayer has tangible evidence to prove the preceding facts, and, in the opinion of the IRS, the taxpayer's reliance was reasonable. The "Decision Tree" goes on to state that the taxpayer's reliance will be considered unreasonable (and thus Form 5471 penalties will not be abated) if the taxpayer did not take reasonable steps to independently investigate or the taxpayer did not get a second opinion. This aspect of the "Decision Tree" is particularly remarkable because it is contrary to the legal precedent established by the U.S. Supreme Court years ago on this exact point. In a famous tax case from 1985, *Boyle*, the highest court in the land explained that requiring taxpayers to challenge their advisors or seek a second opinion "would nullify the very purpose of seeking the advice of a presumed expert in the first place."[50]

Flume is interesting, in that none of the documents mention anybody applying the Form 5471 penalty "Decision Tree": Not the revenue agent during the audit, not the settlement officer during the CDP hearing, not the IRS attorneys in their filings with the Tax Court, and not the Tax Court in its opinion.

H. Continuation Penalty

Flume is interesting because the determination by the Tax Court does not reflect the true magnitude of the sanctions. As explained above, if a taxpayer fails to file a Form 5471, files a late Form 5471, or files a timely but "substantially incomplete" Form 5471, then the IRS may assert a penalty of $10,000 per violation, per year.[51] Moreover, if the IRS sends the taxpayer a notice about missing Forms 5471 and the taxpayer refuses to file them within the appointed time, then the penalty jumps by $10,000 per month, until reaching a maximum of $50,000.[52] The penalties about which the parties were fighting in *Flume* totaled $110,000; this represents the amount assessed by the IRS at the time that it issued the "Final Notice and Notice to Your Right to a Hearing," which triggered the CDP Hearing, the notice of determination, and the litigation in Tax Court. However, the pre-trial memo filed by the IRS attorneys indicates that $40,000 in additional penalties exist as a result of Husband's failure to file Forms 5471 after the revenue agent demanded that he do so.

I. Form 5471 Violations and Assessment Periods

The standard penalty of $10,000 per year, per violation can hurt a taxpayer. The most significant consequence of not filing Forms 5471 has nothing to do with money, though. It concerns time, specifically the amount of time that the IRS has to audit the relevant issues. A relatively obscure procedural provision, Code Sec. 6501(c)(8)(A), contains a powerful tool for the IRS. It generally states that where a taxpayer fails to file a timely Form 5471 (and/or a long list of other international information returns), the assessment period remains open "with respect to any tax return, event, or period" to which the Form 5471 relates until three years after the taxpayer ultimately files Form 5471.[53] Thus, if the taxpayer never files a Form 5471, then the general three-year assessment period never begins to run against the IRS. This prevents taxpayers with Form 5471 violations from "waiting out" the IRS.

Code Sec. 6501(c)(8) was not specifically addressed in *Flume*, but logic dictates that it was raised by the IRS. This is because the IRS audit did not begin until 2012, and Form 5471 penalties were not assessed until 2013, yet the IRS managed to reach all the way back to 2001.

J. Substantially Complete Defense—Doomed from the Outset

As explained above, Husband in *Flume* introduced two new arguments after going to Tax Court, in his post-trial memo, one of which was that the Forms 5471 for 2001 and 2002 for Franchise Food, filed with the IRS years after the deadline, should avoid penalties because they were "substantially complete." This position is interesting, in that it entirely overlooks the IRS's recent guidance about "substantial completeness" and Forms 5471.

The Large Business and International ("LB&I") division of the IRS trains its personnel in various ways, one of which is issuing them so-called International Practice

Units ("IPUs"). The IPUs began in 2012 and were first released to the public two years later, in 2014. IPUs do not constitute legal precedent, but many revenue agents give them considerable weight in conducting audits, determining whether penalties apply, *etc*.[54]

In October 2015, the LB & I division released an IPU focused on penalties for Form 5471 violations by certain categories of U.S. persons.[55] It contains a fair amount of information about the rare circumstances under which the IRS will consider a Form 5471 to be "substantially complete." Based on the items cited in the IPU, revenue agents might determine that Forms 5471 are "substantially incomplete" and should be penalized in the following situations: where the taxpayer (i) omits identification data on Form 5471 (such as the filing category, amount of voting stock owned, full name and location of foreign corporation, *etc.*); (ii) states that certain information will be provided only upon request by the IRS; (iii) uses unapproved, computer-generated Forms 5471, (iv) lacks proper financial statements for the foreign corporation; (v) fails to report figures in U.S. dollars and/or using U.S. GAAP, when required; (vi) cites as an excuse the high administrative cost of complying with Form 5471 requirements; (vii) has demonstrated Form 5471 compliance in past years; (viii) overstates and/or understates certain amounts, even if this results in little to no overall change; (ix) reports unnecessary information, presumably on the theory that superfluous data distract the IRS from the real issues; (x) shows a "mismatch" on Forms 5471 for successive years; (xi) leaves blank one or more required Schedules on Form 5471; or (xii) has either one large error or omission, or several smaller errors or omissions.[56]

K. Potential Loss of Passport from Form 5471 Penalties

Congress enacted a law in December 2015 authorizing the IRS, with help from the State Department, to deprive certain individuals with tax debts of a U.S. passport. This new passport-denial-and-revocation power, found in Code Sec. 7345, was part of the Fixing America's Surface Transportation ("FAST") Act. To date, the IRS has not yet issued regulations, a Revenue Procedure, a Notice, or anything else clarifying and/or expanding on the language in Code Sec. 7345. However, the IRS's website was recently updated to indicate that the IRS will begin enforcing the new law "in early 2017."[57]

The general rule under Code Sec. 7345(a) is that, if the IRS determines that an individual taxpayer has a seriously delinquent tax debt ("SDTD"), then it will send a "certification" to the Secretary of the Treasury, who, in turn, will send the "certification" to the Secretary of State, who will then deny, revoke, or limit the U.S. passport of the individual, as appropriate.

Code Sec. 7345(b)(1) defines the term SDTD to mean (i) a federal tax liability, (ii) which has been assessed, (iii) which remains unpaid, (iv) which is more than $50,000, and (v) with respect to which either the IRS has filed an NFTL and the administrative rights under Code Sec. 6320, including the right to request a CDP hearing, have been exhausted or lapsed, or the IRS has levied.[58]

Taxpayers, therefore, should be aware of the lessons gleaned from Flume and contact tax practitioners specializing in international issues when the seemingly inevitable scrutiny by the IRS begins.

For its part, Code Sec. 7345(b)(2) provides several exceptions to the general definition, explaining that the following types of tax debts are *not* considered SDTDs: (i) a debt that the taxpayer is paying in a timely manner pursuant to an installment agreement under Code Sec. 6159; (ii) a debt that the taxpayer is paying in a timely manner pursuant to an offer-in-compromise under Code Sec. 7122; (iii) a debt with respect to which the IRS has suspended collection activity because the taxpayer filed a proper request for a CDP hearing, and such hearing is still pending; (iv) an individual has elected innocent spouse relief under Code Sec. 6015(b) or Code Sec. 6015(c); and (v) an individual has requested innocent spouse relief under Code Sec. 6015(f).

Code Sec. 7345(c) addresses reversal of the SDTD certification, which some refer to as "decertification." Code Sec. 7345(c)(1) explains that the IRS must notify the Secretary of the Treasury, who will then notify the Secretary of State, in three circumstances: (i) if any certification is later found to be erroneous; (ii) if the individual "fully satisfies" the debt that triggered the certification; or (iii) the debt is no longer an SDTD as a result of Code Sec. 7345(b)(2), as described in the preceding paragraph. In other words, notice of "decertification" must occur when the original certification was unwarranted; the individual completely pays off the SDTD; the individual enters into an Installment Agreement; the individual

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resolves matters through an Offer-in-Compromise, or the individual has properly sought innocent spouse relief from the liability.[59]

Code Sec. 7345(b)(1) indicates that an SDTD is a federal tax liability that exceeds $50,000, but it does not clarify the components of the calculation. To find this answer, one must look to the legislative history. The congressional conference report states that an SDTD generally includes any "outstanding debt for federal taxes in excess of $50,000, *including interest and any penalties*," for which a post-lien notice or a pre-levy notice has been filed.[60] Likewise, the so-called Bluebook issued by the U.S. Joint Committee on Taxation states that an SDTD entails taxes and "interest and any penalties."[61]

Code Sec. 7345(b)(1) explains that an SDTD is a "federal tax liability" greater than $50,000, and the legislative history indicates that this term covers not only the federal income taxes related to Forms 1040 of an individual taxpayer but also corresponding penalties and interest. What remains murky is whether "assessable penalties" will be considered part of an SDTD.

The term "assessable penalties" refers to those items found in Code Sec. 6671 through Code Sec. 6725. For its part, Code Sec. 6671(a) expressly states that "assessable penalties" shall be paid by the taxpayer upon notice and demand by the IRS and "shall be assessed and collected in the same manner as taxes." It goes on to clarify that any reference in the Code to the term "tax" shall include "assessable penalties."[62]

Let us see how this might play out, understanding that Code Sec. 7345 speaks to "federal tax liabilities" and Code Sec. 6671 explicitly states that "assessable penalties" are considered "taxes." Because the Form 5471 penalty is $10,000 per violation, because such penalties are rooted in Code Sec. 6679 (*i.e.*, within the list of "assessable penalties"), and because it is not uncommon for individuals to be required to file multiple Forms 5471 per year, a noncompliant individual could find himself facing Form 5471 penalties in excess of $50,000 very quickly. Case in point, the penalties assessed against Husband in *Flume* reached $110,000, and that was before taking into account the $40,000 in continuation penalties. It is still unclear whether unpaid "assessable penalties," alone, could trigger an SDTD certification and thus deprive an individual of a passport under Code Sec. 7345. If this is the case, the importance of Form 5471 sanctions and a long list of other "assessable penalties" will increase dramatically, and the ferocity with which taxpayers will fight them likely will skyrocket, too.

L. Conclusion

Flume provides an opportunity to highlight many issues unique to international tax disputes, including, but definitively not limited to, (i) the variety of procedures for challenging an "assessable" penalty; (ii) the significance of the IRS issuing an FDR (as opposed to a standard IDR) during an audit; (iii) the potential need to file multiple international information returns, including Forms 5471 for foreign corporations, Forms 8938 for foreign financial assets, and FBARs for foreign financial accounts; (iv) the narrow application of the First-Time-Abatement policy in certain situations; (v) the use by the IRS of a stringent "Decision Tree" in determining whether penalty abatement is warranted; (vi) the unlimited extension of the assessment-period when taxpayers fail to file certain international information returns; and (vii) the loss of U.S. passports for taxpayers with SDTDs. The world becomes more globalized each day, and the complexity of international tax rules, procedures, and disputes increases accordingly. Taxpayers, therefore, should be aware of the lessons gleaned from *Flume* and contact tax practitioners specializing in international issues when the inevitable scrutiny by the IRS begins.

ENDNOTES

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1 *E.S. Flume*, 113 TCM 1097, Dec. 60,822(M), TC Memo. 2017-21.

2 Code Sec. 6038; Reg. §1.6038-2; Code Sec. 6046; Reg. §1.6046-1; Code Sec. 6679; Reg. §301.6679-1; Instructions to Form 5471.

3 Code Sec. 6038(a)(2); Reg. §1.6038-2(i).

4 Code Sec. 6038(b)(1); Reg. §1.6038-2(k)(1)(i); Code Sec. 6046(f); Reg. §1.6046-1(k).

5 Code Sec. 6038(b)(2); Reg. §1.6038-2(k)(1)(ii); Code Sec. 6046(f); Reg. §1.6046-1(k).

6 Reg. §1.6038-2(k)(3)(i) and (ii).

7 The author obtained and reviewed the following documents in describing *Flume*: Petition filed July 7, 2014 (enclosing notice of determination dated June 3, 2014); Answer by IRS filed August 27, 2014; First Stipulation of Facts filed September 30, 2015; First Supplemental Stipulation of Facts filed September 30, 2015; Pre-Trial Memorandum by Taxpayer filed September 11, 2015; Pre-Trial Memorandum by IRS filed September 30, 2015; Opening Brief by IRS filed January 15, 2016; Answering Brief by Taxpayer filed March 9, 2016; Reply Brief by IRS filed April 8, 2016; and *Flume*, 113 TCM 1097, Dec. 60,822(M), TC Memo. 2017-21.

8 Exhibit 47-J to the First Stipulation of Facts consists of a certification from legal counsel for UBS regarding records concerning the account held by Wilshire Belize. The certification is dated January 18, 2010, which was years before the audit commenced.

9 The IRS's internal guidance confirms this, stating that "[d]eficiency procedures under Subchapter B of Chapter 63 (relating to deficiency procedures for income, estate, gift, and certain excise taxes) do *not* apply to penalties

discussed in this section." IRM pt. 20.1.9.2 (Apr. 22, 2011); IRM Exhibit 20.1.9-4.

10 For details about collection freezes and the right to post-assessment, pre-payment review, *see* IRM pt. 21.8.2.20.2 (Oct. 1, 2013).

11 Code Sec. 982(a). The taxpayer's response to the FDR must also be timely, which means within 90 days of the date on which the IRS mailed the FDR. *Id*.

12 Code Sec. 982(b)(1).

13 Code Sec. 982(a) contains the "substantial compliance" defense and Code Sec. 982(b)(1) contains the "reasonable cause" defense.

14 Foreign Account Tax Compliance Act ("FATCA"), P.L. 111-147, Hiring Incentives to Restore Employment Act, Code Sec. 511, March 18, 2010.

15 Reg. §1.6038D-2(b)(1).

16 Reg. §1.6038D-2(b)(1).

17 Reg. §1.6038D-2(a)(8).

18 Code Sec. 6038D(b)(1); Reg. §1.6038D-3(a)(1).

19 Code Sec. 6038D(b)(2); Reg. §1.6038D-3(b)(1).

20 Code Sec. 6038D(b)(2); Reg. §1.6038D-3(b)(1).

21 Reg. §1.6038D-3(d).

22 Code Sec. 6038D(d)(1); Reg. §1.6038D-8(a).

23 Code Sec. 6038D(d)(2); Reg. §1.6038D-8(c).

24 Code Sec. 6038D(g); Reg. §1.6038D-8(e)(1).

25 Bank Secrecy Act in 1970 (P.L. 91-508), Title I and Title II (Oct. 26, 1970).

26 *Id*., at §202.

27 31 USC §5314; 31 CFR §1010.350(a).

28 68 FR 26489 (May 16, 2003).

29 31 CFR §103.56(g), 68 FR 26489 (May 16, 2003).

30 American Jobs Creation Act ("Jobs Act"), P.L. 108-357 (Oct. 22, 2004).

31 31 USC §5321(a)(5)(A) (as in effect before Oct. 22, 2004).

32 31 USC §5321(a)(5)(B)(ii) (as in effect before Oct. 22, 2004).

33 31 USC §5321(a)(5)(A).

34 31 USC §5321(a)(5)(B)(i).

35 31 USC §5321(a)(5)(B)(ii).

36 31 USC §5321(a)(5)(C)(i).

37 *J.B. Williams*, 131 TC 54, Dec. 57,547 (2008).

38 *See Flume*, Tax Court Docket No. 31162-14 (covering 2006, 2007, and 2008) and *Flume*, Tax Court Docket No. 9126-14 (covering 2009).

39 *Flume*, Tax Court Docket No. 31162-14, Petition (with copy of notice of deficiency attached) filed December 31, 2014.

40 *Flume*, Tax Court Docket No. 31162-14, Petition (with copy of notice of deficiency attached) filed December 31, 2014. Unless otherwise stated, uses of the terms "Section" and "Sections" in this article refer to the Internal Revenue Code of 1986, as amended.

41 IRM pt. 20.1.1.3.6.1(7) (Aug. 5, 2014).

42 IRM pt. 20.1.1.3.6.1(7) (Aug. 5, 2014).

43 IRM pt. 20.1.1.3.6.1(7) (Aug. 5, 2014).

44 IRM pt. 20.1.1.3.6.1(8) and (9) (Aug. 5, 2014).

45 IRM pt 20.1.1.3.1.2 (Aug. 20, 1998).

46 Reg. §1.6664-4(b)(1).

47 IRM pt. 20.1.1.3.1.2.1 (Aug. 20, 1998).

48 Reg. §1.6664-4(c)(1).

49 IRM Exhibit 21.8.2-1—Failure to File or Late-Filed Form 5471—Decision Tree.

50 *R.W. Boyle*, SCt, 85-1 USTC ¶13,602, 469 US 241, 251, 105 SCt 687.

51 Code Sec. 6038(b)(1); Reg. §1.6038-2(k)(1)(i); Code Sec. 6046(f); Reg. §1.6046-1(k).

52 Code Sec. 6038(b)(2); Reg. §1.6038-2(k)(1)(ii); Code Sec. 6046(f); Reg. §1.6046-1(k).

53 Code Sec. 6501(c)(8)(B) contains a limitation stating that the assessment period will remain open only with respect to "the item or items" related to the late Form 5472 if the taxpayer can demonstrate that the delinquency was due to reasonable cause and not due to willful neglect.

54 Jasper L. Cummings, Jr,. *LB&I International Practice Units*, TAX NOTES 1077 (Nov. 23, 2015); Kristen A. Parrilla & Jamie Arora, *IRS Plans to Release International Training Materials,* TAX NOTES 1317 (Mar. 24, 2014).

55 "Failure to File the Form 5471—Category 4 and 5 Filers—Monetary Penalty." International Practice Unit (updated as of Oct. 7, 2015).

56 "Failure to File the Form 5471—Category 4 and 5 Filers—Monetary Penalty." International Practice Unit (updated as of Oct. 7, 2015).

57 *See www.irs.gov/businesses/small-businesses-self-employed/revocation-or-denial-of-passport-in-case-of-certain-unpaid-taxes*, as of February 19, 2017. The website states the following: "The IRS has not yet started certifying tax debt to the State Department [but] certifications to the State Department will begin in early 2017."

58 Code Sec. 7345(f) indicates that the $50,000 threshold will be adjusted annually for inflation and rounded to the nearest multiple of $1,000.

59 Legislative history states that, "[i]n the case of a claim for innocent spouse relief, the decertification is only with respect to the spouse claiming relief, not both." *See* U.S. House of Representatives, 114th Cong., 1st Sess., Conference Report 114-357, Dec. 1, 2015, at 532.

60 U.S. House of Representatives, 114th Cong., 1st Sess., Conference Report 114-357, Dec. 1, 2015, at 531.

61 U.S. Joint Committee on Taxation. General Explanation of Tax Legislation Enacted in 2015. JCS-1-16 (Mar. 2016), at 92.

62 Code Sec. 6671(a); Reg. §301.6671-1(a).

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