

APPENDIX TABLE OF CONTENTS

OPINIONS AND ORDERS

Opinion of the United States Court of Appeals for the Second Circuit (July 28, 2021)	1a
Judgment of the United States Court of Appeals for the Second Circuit (July 28, 2021).....	15a
Final Judgment of the United States District Court for the Eastern District of New York (December 20, 2019)	17a
Stipulation (December 20, 2019)	19a
Memorandum Decision and Order of the United States District Court for the Eastern District of New York (Decided November 17, 2019, Filed November 18 2019).....	23a

STATUTES

Relevant Statutory Provisions	41a
-------------------------------------	-----

APPENDIX TABLE OF CONTENTS (Cont.)

OTHER DOCUMENTS

IRS E-Notice 2003-25 (January 2003)	58a
IRM 1.11.5.1.2.....	61a
IRM 3.21.19.10.....	62a
IRM 3.21.19.11.....	65a
IRM 3.21.19.12.....	69a
Chief Counsel Memorandum (November 9, 2011)	73a
1997 Form 3520 and Instructions (Transcription of Tax Form).....	86a
2007 Form 3520 and Instructions (Transcription of Tax Form).....	99a

**OPINION OF THE UNITED STATES COURT
OF APPEALS FOR THE SECOND CIRCUIT
(JULY 28, 2021)**

6 F.4th 432

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

EMILY S. WILSON,
as Executrix of the Estate of Joseph A. Wilson,
THE ESTATE OF JOSEPH A. WILSON,

Plaintiffs-Appellees,

v.

UNITED STATES OF AMERICA,

Defendant-Appellant.

Docket No. 20-603

Before: LIVINGSTON, Chief Judge,
WESLEY, CARNEY, Circuit Judges.

WESLEY, Circuit Judge:

Joseph Wilson was the sole owner and beneficiary of an overseas trust. Section 6048 of the Internal Revenue Code (“IRC”) requires U.S. owners of a foreign trust to ensure that the trust files an annual return, *see* 26 U.S.C. § 6048(b), and U.S. beneficiaries of a foreign trust to file a return reporting the distributions they received, *see id.* § 6048(c). Section 6677 of

the IRC imposes different penalties for the late filing of two types of returns: a 35% penalty for beneficiaries who fail to timely report their distributions, *see id.* § 6677(a); and a 5% penalty for owners who fail to ensure that their trust timely files an annual return, *see id.* § 6677(b). Wilson filed both returns for tax year 2007 late. The Internal Revenue Service (“IRS”) assessed a 35% penalty against Wilson for failing to timely disclose the distribution he received from his trust. Wilson paid and then filed for a refund, arguing he should have been charged only a 5% penalty that applies to trust owners. He died before his claim was resolved.

Emily S. Wilson, executrix of Wilson’s estate, and Wilson’s estate (“Plaintiffs”) brought this action contending the government should have imposed only a 5% penalty because Wilson was responsible for reporting all the required information, including the distributions he received, as the trust owner. The United States District Court for the Eastern District of New York (Cogan, J.) agreed, finding that under the IRC, Wilson should have been penalized only as the trust owner. We vacate the court’s judgment and hold that when an individual is both the sole owner and beneficiary of a foreign trust and fails to timely report distributions she received from the trust, the government has the authority under the IRC to impose a 35% penalty.

BACKGROUND

Wilson established a foreign trust in 2003 with a value of approximately \$9 million.¹ In 2007, Wilson

¹ As Plaintiffs alleged in their complaint, Wilson’s intention

liquidated the trust and distributed all its assets, approximately \$9.2 million,² to himself.

Section 6048 of the IRC imposes disclosure requirements related to foreign trusts. Subsection (c) instructs “any United States person [who] receives . . . during any taxable year . . . any distribution from a foreign trust” to “make a return with respect to such trust for such year” that includes, *inter alia*, “the aggregate amount of the distributions so received from such trust.” 26 U.S.C. § 6048(c). In other words, § 6048(c) requires beneficiaries of a foreign trust—such as Wilson—to disclose distributions they received from the trust in an annual filing. Subsection (b) orders U.S. owners “of any portion of a foreign trust” to “ensure that . . . such trust makes a return for such [taxable] year which sets forth a full and complete accounting of all trust activities and operations for the year” and “other information as the Secretary [of the Treasury] may prescribe.” *Id.* § 6048(b).

To satisfy these two separate reporting requirements, Wilson and the trust needed to file Forms 3520-A and 3520. Form 3520-A, the “Annual Information Return of Foreign Trust With a U.S. Owner,” provides that “[a] foreign trust with a U.S. owner must file Form 3520-A in order for the U.S. owner to satisfy its annual information reporting requirements under [§] 6048(b).” J.A. 128. It contains a section to report distributions from the trust. Form 3520, the “Annual Return To

was to hide his assets from his then-wife because he believed she was preparing to divorce him; she did. Wilson’s motivation for establishing the trust is irrelevant to the resolution of this appeal.

² The trust earned interest at up to 5% per year.

Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts,” directs owners of “any part of the assets of a foreign trust” to provide the information in Part II and beneficiaries of a foreign trust to disclose distributions they received in Part III. *Id.* at 109. If the owner of a foreign trust received a distribution and completes Part II of Form 3520, and the trust has filed Form 3520-A, the instructions for Form 3520 state “do not separately disclose distributions again in Part III.” *Id.* at 114.

Wilson failed to file Form 3520 and failed to ensure that his trust file Form 3520-A by their respective deadlines for tax year 2007.³ As a result, he did not timely disclose the \$9.2 million distribution he received or report other information about his trust. The IRS assessed a late penalty of \$3,221,183, 35% of the \$9.2 million distribution. This penalty derives from § 6677(a) of the IRC, which provides “if any notice or return required to be filed by [§] 6048” is not filed on time or is incomplete, “the person required to file such notice or return shall pay a penalty equal to . . . 35 percent of the gross reportable amount.” 26 U.S.C. § 6677(a).

Wilson initially paid the penalty, but less than two months later submitted a claim to the IRS seeking a full refund. He argued that because he was both the sole beneficiary and the sole owner of the trust, only a 5% penalty applies for his failure to timely report

³ Wilson also failed to file information returns for tax years 2005 and 2006. The IRS assessed penalties for these years, but “[a]ll penalties, with the exception of the penalties for . . . 2007 . . . were settled in IRS appeals. The settled penalties were promptly paid in full, together with statutory interest.” J.A. 8.

the distribution to himself. The 5% penalty stems from § 6677(b) of the IRC, which states “[i]n the case of a return required under [§] 6048(b),” the reporting requirement for trust owners, a 5% penalty will substitute the 35% penalty. *Id.* § 6677(b)(2).

While Wilson’s claim for a refund was pending, he passed away. Plaintiffs brought this action against the government to recover the money for Wilson’s estate, pursuing Wilson’s 5% penalty argument and alleging in the alternative that there was “reasonable cause” that excused Wilson’s untimely filing.⁴ The government moved to dismiss only the 5% penalty claim, arguing that Plaintiffs did not exhaust their refund claim in the administrative process, which the district court denied.⁵ Plaintiffs moved for partial summary judgment on their 5% penalty argument, which the district court granted, concluding that “[t]he IRS can . . . assess only the 5% penalty unde . . . § 6677—not both or either the 5% and/or 35% penalty—for Wilson’s untimely filing of his 2007 Form 3520.” *Wilson v. United States*, No. 19-CV-5037 (BMC), 2019 WL 6118013, at *8 (E.D.N.Y. Nov. 18, 2019). The government appeals, arguing that the district court erred in its construction of the IRC.

⁴ Section 6677 contains a “reasonable cause” exception, providing that “[n]o penalty shall be imposed . . . on any failure which is shown to be due to reasonable cause and not due to willful neglect.” 26 U.S.C. § 6677(d).

⁵ “The [g]overnment does not appeal the [d]istrict [c]ourt’s denial of [its] partial motion to dismiss.” Appellant’s Br. at 15 n.8.

DISCUSSION

“We review a grant of summary judgment *de novo*; specifically, where the disposition presents only a legal issue of statutory interpretation, as here, we review *de novo* whether the district court correctly interpreted the statute.” *Power Auth. v. M/V Ellen S. Bouchard*, 968 F.3d 165, 170 (2d Cir. 2020) (internal quotation marks and citation omitted). In interpreting any statute, we start with the plain meaning of the text, and absent any ambiguity, we end there too. *See, e.g., United States v. Venturella*, 391 F.3d 120, 125 (2d Cir. 2004).

I. The Plain Meaning of Sections 6048 and 6677 of the IRC

The plain language of the IRC’s disclosure and penalty provisions, §§ 6048 and 6677, unambiguously demonstrates that when an owner of a foreign trust fails to timely disclose a distribution she received as a beneficiary of that trust, she violates § 6048(c) and thereby triggers the 35% penalty under § 6677(a). Section 6048(c) states in relevant part:

If any United States person receives (directly or indirectly) during any taxable year of such person any distribution from a foreign trust, such person shall make a return with respect to such trust for such year which includes . . . (B) the aggregate amount of the distributions so received from such trust during such taxable year.

26 U.S.C. § 6048(c)(1). Normally understood, “any United States person,” *id.*, includes everyone, U.S. owners and beneficiaries of foreign trusts alike. The

statute makes no exception for a beneficiary who is also the owner of a foreign trust. Wilson was therefore required under § 6048(c) to timely report the distribution he received from his trust.⁶

Under § 6677(a), “if any notice or return required to be filed by [§] 6048 . . . is not filed on . . . time . . . the person required to file such notice or return shall pay a penalty equal to . . . 35 percent of the gross reportable amount.” *Id.* § 6677(a). “[I]n the case of a failure relating to [§] 6048(c),” the “gross reportable amount” is “the gross amount of the distributions.” *Id.* § 6677(c). Because Wilson failed to timely report under § 6048(c), the IRS assessed—in accordance with § 6677(a) and (c)—a penalty of 35% of Wilson’s \$9.2 million distribution.

Nothing in other parts of §§ 6048 and 6677 diminishes or eliminates the applicability of the 35% penalty to Wilson as a beneficiary of the trust. However, the district court relied on § 6677(b) to conclude that the 35% penalty cannot apply. *See Wilson*, 2019 WL 6118013, at *6. Section 6677(b) “substitut[es] ‘5 percent’ for ‘35 percent’ [of the gross reportable amount]” as the applicable penalty for the failure to timely file “a return required under [§] 6048(b),” which is the reporting requirement for owners of foreign trusts. 26 U.S.C. § 6677(b). According to the court, because Wilson violated § 6048(b) by failing to timely file as an owner, § 6677(b)’s “mandate[] that the 5% replace

⁶ The timely filing requirement is found in § 6048(d), which directs that “[a]ny notice or return required under [§ 6048] shall be made at such time and in such manner as the Secretary [of the Treasury] shall prescribe.” 26 U.S.C. § 6048(d)(3).

the 35%” applies. *Wilson*, 2019 WL 6118013, at *6 (emphasis omitted).

The problem with the district court’s analysis is that § 6677(b) leaves untouched the 35% penalty that applies to all other reporting requirements under § 6048, including to a return disclosing distributions required by § 6048(c). The district court and Plaintiffs do not identify any text in the statute that elides the requirement to disclose distributions received as a beneficiary under § 6048(c) when the beneficiary is also the owner of a foreign trust. Nor is there any textual support for the court and Plaintiffs’ view that when the owner and beneficiary are one, a failure to timely report the distribution received violates *only* § 6048(b) and *not* § 6048(c). Even if the information the owner must report under § 6048(b) covers the trust’s distributions, nothing in the statute indicates that as a result, § 6048(b) displaces or merges with the separate requirement to report distributions under § 6048(c). *See id.* at *6–7. Because *Wilson*’s failure to timely report the distribution he received violates § 6048(c) even if that same failure also violates his reporting requirements as an owner under § 6048(b), the 5% penalty under § 6677(b) does not supplant the 35% penalty.

The district court and Plaintiffs’ remaining textual arguments fail to defeat this conclusion. The district court criticized the government’s justification of the 35% penalty as presenting “an irreconcilable textual conflict,” asserting that because § 6677(a) instructs the penalty should not “exceed the gross reportable amount,” “a taxpayer should not be liable for any two penalties if their combined assessment would add up to more than the gross reportable amount for any

one violation.” *Id.* at *7 (quoting 26 U.S.C. § 6677(a)). “Because the gross reportable amount for an owner’s untimely filing . . . is ‘the gross value of the portion of the trust’s assets at the close of the year,’ Wilson’s \$0 in trust assets at the end of 2007 yields a \$0 gross reportable amount”—the government’s pursuit of “\$3,221,183 above \$0 [therefore] violates the statute.” *Id.*

The court’s reasoning misses the fact that “gross reportable amount” has more than one meaning under § 6677(c).⁷ The definition of “gross reportable amount” varies depending on the subsection of § 6048 an individual violated. For example, “in the case of a failure relating to [§] 6048(b)(1)” (the owner’s filing requirement), the gross reportable amount is “the gross value of the portion of the trust’s assets at the close of the year.” 26 U.S.C. § 6677(c)(2) (emphasis added). By contrast, “*in the case of a failure relating to* [§] 6048(c)” (the beneficiary’s filing requirement), the gross reportable amount is “the gross amount of the distributions.” *Id.* § 6677(c)(3) (emphasis added). As a result, the prohibition against applying a penalty that “exceed[s] the gross reportable amount,” *id.* § 6677(a), refers not to a single, common amount but instead is based on the specific violation. A 35% penalty of the “gross amount of the distributions,” here \$3.2 million, does not exceed the “gross reportable amount” of the \$9.2 million Wilson received as the beneficiary.

⁷ The district court acknowledged “gross reportable amount” has more than one meaning in its discussion of the government’s administrative exhaustion argument, *see Wilson*, 2019 WL 6118013, at *3 n.1, yet did not raise this during its subsequent analysis.

Equally unavailing is Plaintiffs' contention that the government may only assess one penalty because § 6677(a) states that a "person required to file . . . [a] return [under § 6048] shall pay *a* penalty equal to . . . 35 percent." *See id.* § 6677(a) (emphasis added); Appellees' Br. at 31. "[A] penalty" does not mean the government may impose only a single penalty even if the taxpayer violates multiple filing requirements under § 6048. This is made clear by the fact that the same sentence upon which Plaintiffs rely states, in full, that "the person . . . shall pay a penalty equal to . . . 35 percent of the gross reportable amount," 26 U.S.C. § 6677(a) (emphasis added), and as discussed above "gross reportable amount" has different meanings, permitting more than one penalty depending on the nature of the untimely filing. The structure and text of § 6677 reflect that if an individual fails to timely file "any . . . return required to be filed by [§] 6048," *id.* (emphasis added), she is subject to a 35% penalty based on each return she fails to file as required under § 6048.⁸ Construed in its statutory context, "a penalty" cannot carry the weight with which Plaintiffs burden it.

The plain language of §§ 6048 and 6677 requires that when an individual fails to timely report the distributions she received from a foreign trust, the 35% penalty applies; her concurrent status as owner of the trust does not alter this rule. Because the

⁸ Except, of course, she is subject to a 5% penalty under § 6677(b) if she fails to file the return required by owners of foreign trusts pursuant to § 6048(b). The modification of the penalty for that specific violation of § 6048 does not imply, however, that only one penalty applies even if the individual violates multiple reporting requirements under § 6048.

statute's meaning is clear based from its text, we need not consider any extrinsic sources. *See New York v. Nat'l Highway Traffic Safety Admin.*, 974 F.3d 87, 95 (2d Cir. 2020).

II. The Applicability of Forms 3520 and 3520-A

The district court and Plaintiffs devote their energies to the two types of forms Wilson and the trust needed to file: Forms 3520 and 3520-A. As noted earlier, Form 3520-A is the annual return that the trust must file for the owner to comply with her reporting requirements under § 6048(b), whereas Form 3520 has separate sections to be completed by trust owners and beneficiaries. Plaintiffs reiterate the district court's view that "a person in Wilson's situation—*i.e.* a sole grantor/owner and sole beneficiary of a foreign trust—would have only been required to file a single Form 3520." *Wilson*, 2019 WL 6118013, at *6. The court relied on the instructions under Part III of Form 3520:

If you received an amount from a portion of a foreign trust of which you are treated as the owner and you have correctly reported any information required on Part II [to be completed by the trust owner] and the trust has filed a Form 3520-A with the IRS, do not separately disclose distributions again in Part III.

Id. at *7 (citation omitted). According to the court, because a trust owner who received a distribution and reported it in the trust's Form 3520-A "is not required to otherwise report the distribution on Form 3520," "Form 3520 disregards the beneficiary status of the trust owner in favor of his owner status,

at least for the limited purpose of tracking distributions to the owner.” *Id.*

The district court’s analysis is wrong for two reasons. First, even if Wilson needed to file “a single Form 3520,” *id.* at *6, § 6048 is concerned with the actual disclosure requirements, not the form on which the required disclosures are made. Filing a Form 3520 without providing all of the required information, such as the distributions, still violates § 6048. Second, the court overlooks the fact that regardless of whether the person files Form 3520, Form 3520-A, or both, she must disclose any distributions she received from a foreign trust even if she is the sole owner and sole beneficiary. The option to disclose the distributions that an owner received from the trust in Form 3520-A does not “favor” the owner status. Indeed, as the government articulated, “[t]he instructions simply provide that, if the foreign trust at issue filed a Form 3520-A that properly reported all distributions as part of the trust’s annual reporting (which did not occur here), the trust owner can simply direct the IRS to the [Form] 3520-A already filed (by checking the appropriate box on Part II of Form 3520 and attaching his ownership statement) and need not report that information again on Part III of the Form 3520.” Appellant’s Br. at 47–48.

Relatedly, Plaintiffs argue that Form 3520-A (the annual return for the trust), which includes separate subsections to report distributions to owners and beneficiaries, and the instructions for the form “evidence that the [IRS] did not view a distribution to the trust owner to be reported as a distribution to a trust beneficiary.” Appellees’ Br. at 22. Plaintiffs see this as “further evidence that the [IRS] did not view a

distribution made to a trust owner as falling within the reporting requirements [of §] 6048(c) for beneficiaries.” *Id.* Form 3520-A and its instructions carry no such implications. The separate reporting for owners and beneficiaries does not erase the owner’s concurrent beneficiary status for the purpose of § 6048(c). Moreover, even if we were to find that the forms generate some ambiguity, “[t]he only role [extratextual] materials can properly play is to help ‘clear up . . . not create’ ambiguity about a statute’s original meaning.” *McGirt v. Oklahoma*, 140 S. Ct. 2452, 2469 (2020) (citation omitted).⁹

Lastly, Plaintiffs emphasize that we should rule in their favor because when there is doubt about the applicability of a tax penalty, it should be “construed most strongly against the government, and in favor of the citizen.” *Gould v. Gould*, 245 U.S. 151, 153 (1917). Given the absence of any doubt, we have no occasion to give Wilson the benefit Plaintiffs urge.

⁹ Plaintiffs’ contention that the IRS’s “published guidance”—its instructions for the forms and statements in the Internal Revenue Manual—warrant *Chevron* or *Skidmore* deference is inapposite. See *Chevron, U.S.A., Inc. v. Nat. Res. Def. Council, Inc.*, 467 U.S. 837 (1984); *Skidmore v. Swift & Co.*, 323 U.S. 134 (1944); Appellees’ Br. at 23–24. First, it is unclear that the IRS’s “publicly stated positions,” Appellees’ Br. at 23, constitute “rules carrying the force of law” as required for *Chevron* deference. *United States v. Mead Corp.*, 533 U.S. 218, 227 (2001). Second, the deference doctrines apply only if the statute is ambiguous, which we do not find. See *Chevron*, 467 U.S. at 842–43. Third, regardless, deference to the IRS’s statements for the point that owners are required to file Form 3520 does not change the fact that, by statute, owners who are also beneficiaries must disclose distributions they receive.

CONCLUSION

We VACATE the judgment of the district court and REMAND for further proceedings consistent with this opinion. It is further ORDERED that Appellees' motions for leave to file a supplemental appendix that includes documents outside the record on appeal and for leave to file a sur-reply brief are DENIED as moot.

**JUDGMENT OF THE UNITED STATES COURT
OF APPEALS FOR THE SECOND CIRCUIT
(JULY 28, 2021)**

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

EMILY S. WILSON,
as Executrix of the Estate of Joseph A. Wilson,
THE ESTATE OF JOSEPH A. WILSON,

Plaintiffs-Appellees,

v.

UNITED STATES OF AMERICA,

Defendant-Appellant.

Docket No. 20-603

Before: Debra Ann LIVINGSTON, Chief Judge,
Richard C. WESLEY, Susan L. CARNEY,
Circuit Judges.

The appeal in the above captioned case from a judgment of the United States District Court for the Eastern District of New York was argued on the district court's record and the parties' briefs. Upon consideration thereof,

IT IS HEREBY ORDERED, ADJUDGED and DECREED that the judgment of the district court is VACATED and the cause is REMANDED to the

App.16a

district court for further proceedings consistent with this Court's opinion.

For the Court:

/s/ Catherine O'Hagan Wolfe
Clerk of Court

**FINAL JUDGMENT OF THE
UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF NEW YORK
(DECEMBER 20, 2019)**

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

EMILY S. WILSON, as Executrix of the
Estate of Joseph a. Wilson and
THE ESTATE OF JOSEPH A. WILSON,
Plaintiffs,

v.

UNITED STATES OF AMERICA,
Defendant.

Case No. 2:19-cv-05037-BMC

Before: U.S. District Judge Brian M. COGAN

FINAL JUDGMENT

Following this Court's Memorandum Decision and Order dated November 17, 2019, the parties have entered into a Stipulation dated December 20, 2019. Accordingly, the Court hereby enters Final Judgment, pursuant to Federal Rule of Civil Procedure 54, in favor of the Plaintiffs. The Plaintiffs are entitled to judgment for an overpayment to the Internal Revenue Service ("IRS") in the amount of \$3,221,183.00 that Joseph A. Wilson paid for the

penalty that the IRS assessed against him, plus assessed interest of \$268,651.52 paid by Mr. Wilson, for a total overpayment of \$3,489,834.52. Mr. Wilson made the overpayment on June 26, 2017. The Plaintiffs are further entitled to statutory interest on the overpayment running from June 26, 2017, at the rate provided by 26 U.S.C. §§ 6611 and 6621.

As the prevailing parties for purposes of Federal Rule of Civil Procedure 54(d)(1) only, the Plaintiffs shall be awarded their costs in this action.

/s/ Brian M. Cogan
U.S. District Judge

December 20, 2019

**STIPULATION
(DECEMBER 20, 2019)**

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

EMILY S. WILSON, as Executrix of the
Estate of Joseph a. Wilson and
THE ESTATE OF JOSEPH A. WILSON,
Plaintiffs,

v.

UNITED STATES OF AMERICA,
Defendant.

Case No. 2:19-cv-05037-BMC

STIPULATION

The Plaintiffs, Emily S. Wilson, as Executrix of the Estate of Joseph A. Wilson, and the Estate of Joseph A. Wilson, and the defendant, United States of America, by their respective undersigned counsel, hereby stipulate and agree as follows:

1. Mr. Wilson was the sole owner and sole beneficiary of the Perfect Partner Trust (“the Trust”) in 2007. The Trust was properly treated as a foreign grantor trust under the Internal Revenue Code (26 U.S.C).
2. Under the Court’s Memorandum Decision and Order dated November 17, 2019, the maximum and

sole penalty that the IRS could have lawfully imposed against Mr. Wilson under 26 U.S.C. § 6677 for his failure to comply with 26 U.S.C. § 6048 with regard to the Trust for the 2007 tax year was 5 percent of the “gross reportable amount,” defined in § 6677(c)(2) as “the gross value of the portion of the trust’s assets at the close of the year treated as owned by the United States person.”

3. For purposes of applying § 6677(c)(2) in this case, the relevant trust is the Trust, the relevant year is 2007, and the relevant United States person is Mr. Wilson. The parties agree that “the gross value of the portion of the trust’s assets at the close of the year treated as owned by the United States person” was \$0.00 because Mr. Wilson fully liquidated the Trust’s accounts during the 2007 year by making one or more distributions to himself as beneficiary.

4. The Memorandum Decision and Order thus compels the result that the maximum and sole penalty that the IRS could have lawfully imposed against Mr. Wilson under § 6677 as the owner and beneficiary of the Trust for his failure to comply with § 6048 for 2007 is 5 percent of \$0.00, or \$0.00 total. Plaintiffs are thus entitled to judgment for an overpayment to the Internal Revenue Service (“the IRS”) in the amount of the \$3,221,183.00 that Mr. Wilson paid for the penalty that the IRS assessed against him, plus assessed interest of \$268,651.52 that Mr. Wilson paid, for a total overpayment of \$3,489,834.52. Mr. Wilson made the overpayment on June 26, 2017. Plaintiffs are entitled to statutory interest on the overpayment of \$3,489,834.52 running from June 26, 2017 at the rate provided by 26 U.S.C. §§ 6611 and 6621.

5. Because of the foregoing, the Court need not determine whether Mr. Wilson's failure to comply with § 6048 for the 2007 tax year with regard to the Trust was "due to reasonable cause and not due to willful neglect" under § 6677(d). In the event of a reversal on any appeal and a remand to this Court, plaintiffs may pursue this alternate ground for relief, and the defendant may raise any defenses.

6. A proposed final judgment that is consistent with the foregoing is attached. Notwithstanding the United States' agreement to the preceding paragraphs of this stipulation and to the form of the attached final judgment in favor of the Plaintiffs, nothing herein shall be construed as a waiver of the United States' right to appeal from the Memorandum Decision and Order, or from the Final Judgment entered herein.

AGREED:

**Emily S. Wilson, as Executrix of the Estate
United States of America, of Joseph A. Wilson,
and the Estate of Joseph A. Wilson,**

Plaintiffs

/s/ Robert M. Adler (consent)

ROBERT M. ADLER

Nossaman LLP

1401 New York Avenue, N.W.

8th Floor

Washington, DC 20005

Telephone: (202) 887-1428

Fax: (202) 466-3215

Email: radler@nossaman.com

/s/ Gary S. Redish (consent)

GARY S. REDISH

MICHAEL COHEN

Winne Banta Basralian & Kahn, P.C.

Court Plaza South – East Wing

21 Main Street, Suite 101

Hackensack, NJ 07601

Telephone: (201) 487-4800

Fax: (201) 487-8529

Email: gredish@winnebanta.com

mcohen@winnebanta.com

United States of America,

Defendant

/s/ Edward J. Murphy

EDWARD J. MURPHY

THELMA A. LIZAMA

U.S. Department of Justice, Tax Division

P.O. Box 55

Washington, DC 20044

Telephone: (202) 307-6064 (Murphy)

(202) 616-3339 (Lizama)

Fax: (202) 514-5238

Email: Edward.J.Murphy@usdoj.gov

Thelma.A.Lizama@usdoj.gov

**MEMORANDUM DECISION AND ORDER OF
THE UNITED STATES DISTRICT COURT FOR
THE EASTERN DISTRICT OF NEW YORK
(DECIDED NOVEMBER 17, 2019,
FILED NOVEMBER 18 2019)**

UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF NEW YORK

EMILY S. WILSON,
as Executrix of the Estate of Joseph A. Wilson
and THE ESTATE OF JOSEPH A. WILSON,

Plaintiffs,

v.

THE UNITED STATES OF AMERICA,

Defendant.

Case No. 2:19-cv-05037 (BMC)

Before: Brian M. COGAN, U.S. District Judge.

COGAN, District Judge.

Following a six-month period after filing an Amended Claim for Refund with the IRS, plaintiffs bring the present action for the return of \$3,221,183. the Government moves for partial dismissal and plaintiffs cross-move for partial summary judgment and judgment on the pleadings. For the reasons discussed below, the Government's partial motion to dismiss is denied. Furthermore, plaintiffs' motion for partial

summary judgment is granted and plaintiffs' motion for judgment on the pleadings is denied as premature.

BACKGROUND

As alleged in the complaint, Joseph Wilson established an overseas trust in 2003. Wilson named himself the grantor of the trust and was its sole owner and beneficiary. The singular purpose of the trust was to “place assets beyond the reach of his then-wife, who he had reason to believe was preparing to file a divorce action against him.” (She did.) Wilson funded the trust with approximately \$9 million in U.S. Treasury bills, accruing annual interest of 5% or less. All principal had previously been taxed in the United States.

From 2003-2007, Wilson filed “various income tax and information returns” with the IRS, reporting the trust’s assets and the interest it accrued. In 2007, upon conclusion of the divorce proceedings, Wilson terminated the trust and transferred the assets—at that point \$9,203,381—back to his bank accounts in the United States.

Despite general compliance with IRS requirements, Wilson was late in filing his Form 3520 for calendar year 2007. Form 3520 is an annual report disclosing distributions from a foreign trust, with different requirements for trust grantors/owners and for trust beneficiaries. After Wilson filed his 2007 Form 3520, the IRS assessed a late penalty of \$3,221,183, representing 35% of the distributions from the trust during the 2007 calendar year. Because Wilson had transferred 100% of his trust’s funds back to his own domestic accounts during 2007, the penalty also amounted to 35% of his total trust assets.

Wilson had apparently suspected from the beginning that the IRS over-assessed his penalty, as he paid the full \$3,221,183 (plus \$268,651.52 statutory interest) directly to the IRS Appeals office in Fort Lauderdale. Less than two months later, Wilson submitted a Claim for Refund to the IRS, seeking the entire \$3,221,183 plus interest. After waiting the statutorily-required period of six months without word from the IRS, Wilson filed a complaint in the United States Court of Federal Claims. In the complaint, Wilson alleged, *inter alia*, that the IRS erroneously assessed a 35% tax under I.R.C. (hereinafter “26 U.S.C.”) § 6048(c), which applies to trust beneficiaries, when it should have assessed a 5% tax under 26 U.S.C. § 6048(b), which applies to a trust grantor/owner.

The Court of Federal Claims dismissed the complaint, without prejudice, finding that Wilson’s Claim for Refund “had been improperly executed” and so was not “duly filed.” The court therefore held that it lacked subject matter jurisdiction to hear the case. The court further stated that Wilson “has time to re-file his claim for refund, wait the necessary six months to allow the Commissioner to act on it, then file a new complaint if his claim is rejected.”

Even before the Court of Federal Claims issued its decision, Wilson had filed an Amended Claim for Refund “in an effort to cure any possible deficiencies asserted by the Defendant” in its motion to dismiss. Wilson submitted an explanatory statement with his Amended Claim for Refund, again maintaining that

[t]he IRS’ determination was based on its erroneous position that the Trust distributions were made to the taxpayer, as the Trust beneficiary; and therefore, the 35% penalty

provision of Code § 6677 and § 6048(c) applied. However, although the taxpayer was the named beneficiary of the Trust, he was also the sole owner/grantor of the Trust. Pursuant to Code § 6048(b), the taxpayer submits that only a 5% penalty is applicable when the owner/grantor fails to timely report a foreign grantor trust distribution made to himself as a beneficiary.

Another six months had gone by with neither hide nor hair of an IRS notification regarding Wilson's Amended Claim for Refund, and Mr. Wilson passed away while waiting.

Plaintiffs filed the present complaint in this Court and allege that Wilson's estate is entitled to a refund on two grounds:

1. That "reasonable cause" existed for Wilson's untimely filing of Form 3520; and
2. That "[i]n assessing a 35% penalty, the IRS' position is based on its erroneous position that, pursuant to I.R.C. § 6058(c), the Taxpayer, as the beneficiary of the Trust, was subject to a 35% penalty on the amount of the trust distributions not timely reported in Form 3520. In so asserting, the IRS ignores I.R.C. § 6048(b) which applies to the Taxpayer herein who was the grantor/owner of the Trust. In these circumstances, any responsibility for the failure to timely report, in Form 3520, the 2007 distributions from the Trust fell on the grantor/owner under I.R.C. § 6048 (b)—not I.R.C. § 6048(c). Under I.R.C. § 6048 (c), only a 5% penalty may be imposed."

The Government moved to dismiss the second ground. The Court held oral argument on the motion to dismiss, during which plaintiffs cross-moved for partial summary judgment and judgment on the pleadings.

DISCUSSION

I. Government's Partial Motion to Dismiss

The Government moves to dismiss plaintiffs' second ground for a refund—that the IRS wrongfully assessed a 35% penalty under 26 U.S.C. § 6048(c) rather than a 5% penalty under 26 U.S.C. § 6048(b). The Government argues that the Court lacks subject matter jurisdiction to consider this ground because plaintiffs did not exhaust it below.

“[A] prerequisite to a lawsuit seeking a tax refund is a refund claim filed with the IRS that sets forth in detail the ground for the refund and facts sufficient to apprise the IRS of the basis for the refund.” *303 West 42nd St. Enterprises, Inc. v. I.R.S.*, 181 F.3d 272, 277-78 (2d Cir. 1999). Specifically, the taxpayer needs to “set forth facts sufficient to enable the Commissioner of Internal Revenue to make an intelligent administrative review of the claim.” *Scovill Mfg. Co. v. Fitzpatrick*, 215 F.2d 567, 569 (2d Cir. 1954). “The reason for this is both to prevent surprise and to give adequate notice to the Commissioner of the nature of the claim, and its underlying facts, so that a thorough administrative investigation and determination can be made.” *Burlington Northern, Inc. v. United States*, 231 Ct. Cl. 222, 226 (1982). This purpose is met so long as the grounds are “at least impliedly contained in the application for refund.” *See Carione v. United States*, 291 F. Supp. 2d 141, 146 (E.D.N.Y. 2003).

The Government says that plaintiffs did not sufficiently “apprise the Commissioner of the exact basis” for the refund because they “failed to “appl[y] the formula for computing the penalty amount in § 6677.” But the Court has difficulty fathoming how the Commissioner could validly claim that he lacked notice of plaintiffs’ second ground for refund. *See 303 West 42nd St. Enterprises, Inc.*, 181 F.3d at 277-78. Throughout the entirety of the proceedings, Wilson and the plaintiffs have maintained (1) that the IRS wrongfully assessed 35% of the gross reportable amount under 26 U.S.C. 6048(c) and 6677(a), and (2) that the IRS should have assessed only 5% of the gross reportable amount under 26 U.S.C. 6048(b) and 6677(b), because Wilson was the grantor/owner of the trust.

Moreover, plaintiffs certainly “set forth facts sufficient to enable . . . an intelligent administrative review of [this] claim.” *See Scovill Mfg. Co.*, 215 F.2d at 569. At all stages, Wilson and the plaintiffs provided support to demonstrate that Wilson was the grantor/owner and sole beneficiary of the trust; that Wilson had transferred the entirety of the trust’s assets to his own accounts in the United States; the exact amount of money that was in the trust and thereafter distributed during 2007; and the dates of all relevant trust activity. This is to say nothing of the various IRS filings and disclosures specifically related to the trust that Wilson had filed since 2003 and submitted along with his claims and complaints. The Court finds the foregoing more than sufficient to preserve the ground for litigation.

The Government insists at last ditch, however, that over the course of the case plaintiffs have revised

their articulation of this ground to the point where at least a part of it now lies beyond the pale of administrative exhaustion. Plaintiffs originally argued that the appropriate penalty for untimely filing Form 3520 is 5% of that year's "trust distributions." Plaintiffs now argue that the penalty is 5% of the "trust assets."¹ The Government contends that this new formulation veers far enough from the administrative claim to now preclude it as a ground for refund in the present lawsuit. That is incorrect.

This nitpicked distinction falls short of the type of variance that would preclude plaintiffs' argument in this Court. *See, e.g., Scovill Mfg. Co.*, 215 F.2d at 569-70 (holding that a claim was not barred where the characterization of the tax obligation shifted, but the ultimate theory for refund remained the same). Section 6677(a) of Title 26 provides that "the person required to file such notice or return shall pay . . . [a certain percentage] of the gross reportable amount" (emphasis added). At all times it was abundantly clear—and certainly "at least impliedly" expressed—that Wilson sought a refund as a grantor/owner for exactly 5% of the gross reportable amount. *See Carione*, 291 F. Supp. 2d at 146.

Moreover, plaintiffs "set forth facts sufficient to enable the Commissioner" to determine what that gross reportable amount should be—in this case, the

¹ This change in plaintiffs' argument likely stems from confusion around the fact that the 5% penalty is assessed against the "gross reportable amount," *see* 26 U.S.C. § 6677(a)(2), the definition of which changes depending upon whether the filing party is a beneficiary (distribution) or the grantor/owner (assets), *compare* 26 U.S.C. § 6677(c)(2) *with* (c)(3).

“gross value of the portion of the trust’s assets at the close of the year.” 26 U.S.C. § 6677(c)(2). At all points, the Commissioner was aware that Wilson had (allegedly) dissolved the trust and transferred all its assets back to the United States prior to the end of 2007, leaving the gross reportable amount at \$0. There is thus no serious question that the Commissioner was able to carry out “a thorough administrative investigation and determination” of plaintiffs’ claim in this case. *See Burlington Northern, Inc.*, 231 Ct. Cl. at 226. He had all the relevant facts and legal theories at his disposal. That Wilson applied the wrong sub-definition for “gross reportable amount” should not preclude the claim when he also identified the proper legal theory for refund and set forth facts sufficient to show that he deserved the refund under the correct sub-definition.

Wilson has always maintained that he should have been assessed 5% under 26 U.S.C. §§ 6048(b) and 6677(b), and the Commissioner cannot fairly claim that this argument was an unfair surprise. Moreover, plaintiffs’ mistaken reading of the statute was both so obvious and so devoid of any real prejudice to the Commissioner’s “investigation” that there is no credible argument to the contrary.

The cases that the Government sites in opposition are not persuasive. Although *United States v. Janis*, 428 U.S. 433, 440 (1976), held that “[i]n a refund suit the taxpayer bears the burden of proving the amount he is entitled to recover,” this standard is relevant to proof at trial, not to administrative exhaustion.

In *Bartley v. United States*, 123 F.3d 466 (7th Cir. 1997), the Court held that the taxpayer had not exhausted her administrative remedies because she

had failed to file the appropriate form, and instead mailed an unsworn letter that “simply sought a refund of an uncertain amount for all three of the tax years in question.” *Id.* at 468. The present case exhibits none of these flaws—Wilson filed the proper Form with the IRS and explained in great detail why he believed the IRS mistakenly assessed 35%, instead of 5%, of the gross reportable amount for calendar year 2007.

In *Snead v. Elmore*, 59 F.2d 312, 314 (5th Cir. 1932), the Court *did* hold that a claim for refund “must have indicated . . . the amount claimed,” but the refund sought in that case required a determination of the “book value of the assets” and whether “the original cost of the stock exceeded the true value of the corporate net assets.” These values would have been inaccessible to the Commissioner absent an exact dollar amount claimed. Here, on the other hand, there are only four numbers that define the entirety of the claim in all its possible iterations—5%, 35%, \$0, and \$9,203,381.

Nor, in any event, does *Snead* present the proper standard in this Circuit, where the administrative claim need only “set forth facts sufficient to enable the Commissioner of Internal Revenue to make an intelligent administrative review of the claim.” *See Scovill Mfg. Co.*, 215 F.2d at 569. Furthermore, the court in *Snead* held that the purpose of the exhaustion requirement is to “enable the claimed errors to be corrected by the Commissioner and suits to be minimized.” *Snead*, 59 F.2d at 314. In our case, that very goal was surely accomplished by presenting the Commissioner with the theory that a 35% assessment was incorrect and the 5% assessment was correct, as

well as the documents to prove that was the case and to what a 5% assessment should amount.

Finally, in *Nucorp, Inc. v. United States*, 23 Cl. Ct. 234 (1991), the court held that

[t]he claims merely state that a refund is requested for windfall profit tax overpaid in 1984, due to the net income limitation and withholding error. The claims fail to identify the facts on which they are based. The claims fail to identify the oil producing properties at issue, nor do they provide any of the figures necessary to perform net income limitation calculations. The claims fail to identify the amounts of withholding error. Finally, the claims fail to state the exact amount of taxes allegedly overpaid, or the exact amount of the refunds requested.

All, or even some, of the claim's deficiencies in *Nucorp* understandably stymied the Commissioner's meaningful review. However, in our case, plaintiffs do identify sufficient facts on which the claim for refund is based; do provide the figures necessary to perform a refund calculation (again, there are only four possible figures relevant to the claim); and do alert the Commissioner to the erroneous assessment percentage as well as to the proposed correct percentage.

The Government's motion to dismiss is therefore denied.

II. Plaintiffs' Cross-Motion for Partial Summary Judgment

Plaintiffs' cross-motion for partial summary judgment asks the Court to decide that: (1) the Court has

jurisdiction over the grounds raised in plaintiffs' complaint; (2) Wilson, as the sole grantor/owner and sole beneficiary of a foreign trust, is subject only to a 5% penalty for untimely filing IRS Form 3520 under 26 U.S.C. §§ 6048 and 6677; and (3) the 5% penalty should be assessed against the trust's account balance at the close of 2007.

Under Federal Rule of Civil Procedure 56, a court may grant summary judgment when "the movant shows that there is no genuine dispute as to any material fact and the movant is entitled to judgment as a matter of law." "Where the record taken as a whole could not lead a rational trier of fact to find for the nonmoving party, there is no genuine issue for trial." *Matsushita Elect. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 587 (1986) (internal quotation marks omitted). However, "only admissible evidence need be considered by the trial court in ruling on a motion for summary judgment." *Raskin v. Wyatt Co.*, 125 F.3d 55, 66 (2d Cir. 1997).

A dispute as to a material fact is "genuine" . . . if the evidence is such that a reasonable jury could return a verdict for the nonmoving party." *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248 (1986). The opposing party must put forward some "concrete evidence from which a reasonable juror could return a verdict in his favor" to withstand a motion for summary judgment. *Id.* at 256. "Credibility determinations, the weighing of the evidence, and the drawing of legitimate inferences from the facts are jury functions, not those of a judge, whether he is ruling on a motion for summary judgment or for a directed verdict." *Id.* When deciding a motion for summary judgment, "[t]he evidence of the non-movant is to be

believed, and all justifiable inferences are to be drawn in his favor.” *Id.* (internal quotation mark omitted).

The Court’s subject matter jurisdiction has been addressed was addressed above regarding plaintiffs’ second ground for refund. *See* Part I *supra*. Both grounds that plaintiffs raise in their complaint are properly before the court.

Plaintiffs ask the Court to “determine that a 5% penalty, pursuant to [26 U.S.C. §] 6048(b), is applicable due to [Wilson’s] late filing of the Form 3520 for calendar year 2007.” The Government does not disagree that the owner of a foreign trust who untimely files Form 3520 is subject to a 5% assessment under 26 U.S.C. §§ 6048(b), but rather contends that the “35% penalty and the 5% penalty are separate penalties that can be applied independently of one another” against Wilson for untimely filing Form 3520.

It is undisputed that Wilson was the sole owner of the foreign trust as well as its sole beneficiary. It is further undisputed that Wilson untimely filed his Form 3520 for calendar year 2007 and that during 2007 Wilson transferred \$9,203,381 of the trust’s assets to his own bank accounts in the United States. These being the only material facts relevant to the present question, it is ripe for summary judgment. *See* Fed. R. Civ. P. 56.

“In a statutory construction case, the beginning point must be the language of the statute.” *Estate of Cowart v. Nicklos Drilling Co.*, 505 U.S. 469, 475 (1992). Even more to the point, “when the text of a statute is clear, that is the end of the matter.” Antonin Scalia, *A Matter of Interpretation* 16 (Amy Gutmann ed., 1997). This goes for tax statutes as well. *See, e.g.*,

C.I.R. v. Lundy, 516 U.S. 235, 249-51 (1996) (deferring to the plain language of 26 U.S.C. § 6512 and the adjacent sections in interpreting the application of a look-back period for a tax refund).

Section 6048(b) of Title 26 applies to a “United States Owner of [a] Foreign Trust.” It requires the foreign trust owner to “submit such information as the Secretary may prescribe with respect to such trust for such year.” In contrast, 26 U.S.C. § 6048(c) applies to “United States Beneficiaries of Foreign Trusts,” who are required to file tax returns with respect to “any distribution from a foreign trust” during any taxable year.

Penalties for violating the provisions of 26 U.S.C. § 6048 are codified under 26 U.S.C. § 6677. Subsection (a) of that statute prescribes the penalty for untimely filing “any notice or return required to be filed by section 6048.” In relevant part, 26 U.S.C. § 6677(a)(1) states:

[T]he person required to file such notice or return shall pay . . . 35 percent of the gross reportable amount. . . . At such time as the gross reportable amount with respect to any failure can be determined by the Secretary, any subsequent penalty imposed under this subsection with respect to such failure shall be reduced as necessary to assure that the aggregate amount of such penalties do not exceed the gross reportable amount (and to the extent that such aggregate amount already exceeds the gross reportable amount the Secretary shall refund such excess to the taxpayer).

That provision is modified by 26 U.S.C. § 6677(b)(2), which provides that “subsection (a) shall be applied by substituting ‘5 percent’ for ‘35 percent’” for returns required to be filed by the owner of a foreign trust.

Because Wilson was the owner of the foreign trust, there is no doubt both that § 6048(b) applied to him and that his violation of § 6048(b) would result in a 5% penalty under § 6677(b). But Wilson was also a beneficiary—indeed, the only beneficiary—of the foreign trust. The Government therefore argues that he could be independently penalized as a beneficiary for untimely filing Form 3520 under § 6048(c). The Court disagrees.

At the outset, it is imperative to understand that a person in Wilson’s situation—*i.e.* a sole grantor/owner and sole beneficiary of a foreign trust—would have only been required to file a single Form 3520 for fiscal year 2007. So the question then becomes, whether 26 U.S.C. § 6677 permits a single person untimely filing a single IRS form to be penalized as two different people—as an owner *and* as a beneficiary.

A plain language reading of 26 U.S.C. § 6677 counsels that a trust owner cannot be penalized as a beneficiary for violating a provision of 26 U.S.C. § 6048(b). There is a clear instruction under 26 U.S.C. § 6677(b)(2) to “substitute” 5% for 35%, not to choose between the two or to simply apply a 5% assessment without reference to an otherwise applicable penalty. Therefore, the statute mandates that the 5% *replace* the 35% whenever there is a “case of a return required under section 6048(b).”

When a foreign trust owner is required to file Form 3520, it falls under 26 U.S.C. § 6048(b)’s purview of

“such information as the Secretary may prescribe with respect to” an owner of a foreign trust. Undeniably, then, a violation of that section should be treated under 26 U.S.C. § 6677(b)(2)’s substitution clause, which replaces “35 percent” with “5 percent.” But even if this were not inescapably evident, “in case of doubt [in the interpretation of statutes levying taxes,] they are construed most strongly against the Government, and in favor of the citizen.” *Gould v. Gould*, 245 U.S. 151, 153 (1917).

Moreover, the Government’s argument, if accepted, would result in an irreconcilable textual conflict. Section 6677(a)(1) of Title 26 states that once the Secretary determines the gross reportable amount “with respect to any failure,” the Secretary must ensure that the taxpayer’s penalties under § 6677 “do not exceed the gross reportable amount.” Although this language is primarily concerned with subsequent late fees, the underlying directive appears to limit all penalties for a violation to no more than the “gross reportable amount.” Therefore, it follows that a taxpayer should not be liable for any two penalties if their combined assessment would add up to more than the gross reportable amount for any one violation.

But that would be the case if the Government got its way. Because the gross reportable amount for an owner’s untimely filing Form 3520 under § 6677(c)(2) is “the gross value of the portion of the trust’s assets at the close of the year,” Wilson’s \$0 in trust assets at the end of 2007 yields a \$0 gross reportable amount. Any additional penalty resulting from the same “fail-

ure” would violate the statute. The Government seeks \$3,221,183 above \$0, which violates the statute.²

Beyond the statutory text, certain aspects of Form 3520 itself imply that a foreign trust owner who receives distributions from his own trust should be treated as an owner—and not as a beneficiary—for failures related to the Form’s filing. For example, Part III of the instructions for the 2007 Form 3520 states:

If you received an amount from a portion of a foreign trust of which you are treated as the owner and you have correctly reported any information required on Part II and the trust has filed a Form 3520-A with the IRS, do not separately disclose distributions again in Part III.

Part II of Form 3520 is only to be filled out by the “U.S. Owner of a Foreign Trust” and Form 3520-A is the “Annual Information Return of Foreign Trust With a U.S. Owner.” Thus, if a trust owner has received a distribution from his trust and thereafter reported the distribution in his 3250-A filing, he is not required to otherwise report the distribution on Form 3520.

² This conclusion would appear to result from any joint owner/beneficiary’s transfer to himself of more than roughly 75% of his foreign trust’s assets in a given year. In such cases, the assessment for a beneficiary of 35% of his distributions would always exceed the “gross value . . . of the trust’s assets” remaining at the close of the year. The same is true for an owner/beneficiary’s transfer to himself of less than 4% of his trust’s assets during a given year. In that case, the assessment for a trust owner of 5% of the remaining trust assets would always exceed the “gross amount of the distributions.” *See* 26 U.S.C. § 6677(c)(1).

From this, it would appear that Form 3520 disregards the beneficiary status of the trust owner in favor of his owner status, at least for the limited purpose of tracking distributions to the owner.

The IRS can therefore assess only the 5% penalty under 26 U.S.C. § 6677—not both or either the 5% and/or 35% penalty—for Wilson’s untimely filing of his 2007 Form 3520.

Plaintiffs next ask the Court for summary judgment as to whether “the 5% penalty should properly be based on the amount of the [trust’s] account balances, if any, at the close of 2007, pursuant to [26 U.S.C. §] 6677(c)(2).” It should. Because Wilson is treated as the owner of the foreign trust for the purpose of his Form 3520 filing, he is liable for penalty under 26 U.S.C. § 6677(b) for a violation of 26 U.S.C. § 6048 (b)(1). Under 26 U.S.C. § 6677(b), the proper assessment is “5% of the gross reportable amount.” The gross reportable amount for “a failure relating to section 6048(b)(1)” is “the gross value of the portion of the trust’s assets at the close of the year treated as owned by the United States person.”

III. Plaintiffs’ Cross-Motion for Judgment on the Pleadings

Plaintiffs also cross-move for judgment on the pleadings. However, the Government has not yet answered plaintiffs’ complaint. Because a party may only move for judgment on the pleadings “after the pleadings are closed,” that motion was premature. *See* Fed. R. Civ. P. 12(c). Therefore, the motion for judgment on the pleadings is denied without prejudice except to the extent that this decision disposes of arguments that plaintiff intended to make.

CONCLUSION

The Government's motion to dismiss is denied. Plaintiffs' [17] motion for partial summary judgment is granted and plaintiffs' motion for judgment on the pleadings is denied.

SO ORDERED.

/s/ Brian M. Cogan
U.S. District Judge

Dated: Brooklyn, New York
November 17, 2019

RELEVANT STATUTORY PROVISIONS

26 U.S.C. § 6048 [In effect in 2007]

Information with Respect to Certain Foreign Trusts

- (a) Notice of certain events.
 - (1) General rule. On or before the 90th day (or such later day as the Secretary may prescribe) after any reportable event, the responsible party shall provide written notice of such event to the Secretary in accordance with paragraph (2).
 - (2) Contents of notice. The notice required by paragraph (1) shall contain such information as the Secretary may prescribe, including—
 - (A) the amount of money or other property (if any) transferred to the trust in connection with the reportable event, and
 - (B) the identity of the trust and of each trustee and beneficiary (or class of beneficiaries) of the trust.
 - (3) Reportable event. For purposes of this subsection—
 - (A) In general. The term “reportable event” means—
 - (i) the creation of any foreign trust by a United States person,
 - (ii) the transfer of any money or property (directly or indirectly) to a foreign trust by a United States person, including a transfer by reason of death, and

App.42a

(iii) the death of a citizen or resident of the United States if—

(I) the decedent was treated as the owner of any portion of a foreign trust under the rules of subpart E of part I of subchapter J of chapter 1, or

(II) any portion of a foreign trust was included in the gross estate of the decedent.

(B) Exceptions.

(i) Fair market value sales. Subparagraph (A)(ii) shall not apply to any transfer of property to a trust in exchange for consideration of at least the fair market value of the transferred property. For purposes of the preceding sentence, consideration other than cash shall be taken into account at its fair market value and the rules of section 679(a)(3) shall apply.

(ii) Deferred compensation and charitable trusts. Subparagraph (A) shall not apply with respect to a trust which is—

(I) described in section 402(b), 404(a)(4), or 404A, or

(II) determined by the Secretary to be described in section 501(c)(3).

(4) Responsible party. For purposes of this subsection, the term “responsible party” means—

(A) the grantor in the case of the creation of an inter vivos trust,

- (B) the transferor in the case of a reportable event described in paragraph (3)(A)(ii) other than a transfer by reason of death, and
 - (C) the executor of the decedent's estate in any other case.
- (b) United States owner of foreign trust.
- (1) In general. If, at any time during any taxable year of a United States person, such person is treated as the owner of any portion of a foreign trust under the rules of subpart E of part I of subchapter J of chapter 1, such person shall be responsible to ensure that—
 - (A) such trust makes a return for such year which sets forth a full and complete accounting of all trust activities and operations for the year, the name of the United States agent for such trust, and such other information as the Secretary may prescribe, and
 - (B) such trust furnishes such information as the Secretary may prescribe to each United States person (i) who is treated as the owner of any portion of such trust or (ii) who receives (directly or indirectly) any distribution from the trust.
 - (2) Trusts not having United States agent.
 - (A) In general. If the rules of this paragraph apply to any foreign trust, the determination of amounts required to be taken into account with respect to such trust by a United States person under the rules of subpart E of part I of subchapter J of chapter 1 shall be determined by the Secretary.

- (B) United States agent required. The rules of this paragraph shall apply to any foreign trust to which paragraph (1) applies unless such trust agrees (in such manner, subject to such conditions, and at such time as the Secretary shall prescribe) to authorize a United States person to act as such trust's limited agent solely for purposes of applying sections 7602, 7603, and 7604 with respect to—
- (i) any request by the Secretary to examine records or produce testimony related to the proper treatment of amounts required to be taken into account under the rules referred to in subparagraph (A), or
 - (ii) any summons by the Secretary for such records or testimony. The appearance of persons or production of records by reason of a United States person being such an agent shall not subject such persons or records to legal process for any purpose other than determining the correct treatment under this title of the amounts required to be taken into account under the rules referred to in subparagraph (A). A foreign trust which appoints an agent described in this subparagraph shall not be considered to have an office or a permanent establishment in the United States, or to be engaged in a trade or business in the United States, solely because of the activities of such agent pursuant to this subsection.

- (C) Other rules to apply. Rules similar to the rules of paragraphs (2) and (4) of section 6038A(e) shall apply for purposes of this paragraph.
- (c) Reporting by United States beneficiaries of foreign trusts.
- (1) In general. If any United States person receives (directly or indirectly) during any taxable year of such person any distribution from a foreign trust, such person shall make a return with respect to such trust for such year which includes—
 - (A) the name of such trust,
 - (B) the aggregate amount of the distributions so received from such trust during such taxable year, and
 - (C) such other information as the Secretary may prescribe.
 - (2) Inclusion in income if records not provided.
 - (A) In general. If adequate records are not provided to the Secretary to determine the proper treatment of any distribution from a foreign trust, such distribution shall be treated as an accumulation distribution includible in the gross income of the distributee under chapter 1. To the extent provided in regulations, the preceding sentence shall not apply if the foreign trust elects to be subject to rules similar to the rules of subsection (b)(2)(B).
 - (B) Application of accumulation distribution rules. For purposes of applying section 668 in a case to which subparagraph (A) applies,

the applicable number of years for purposes of section 668(a) shall be 1/2 of the number of years the trust has been in existence.

(d) Special rules.

(1) Determination of whether united states person makes transfer or receives distribution. For purposes of this section, in determining whether a United States person makes a transfer to, or receives a distribution from, a foreign trust, the fact that a portion of such trust is treated as owned by another person under the rules of subpart E of part I of subchapter J of chapter 1 shall be disregarded.

(2) Domestic trusts with foreign activities. To the extent provided in regulations, a trust which is a United States person shall be treated as a foreign trust for purposes of this section and section 6677 if such trust has substantial activities, or holds substantial property, outside the United States.

(3) Time and manner of filing information. Any notice or return required under this section shall be made at such time and in such manner as the Secretary shall prescribe.

(4) Modification of return requirements. The Secretary is authorized to suspend or modify any requirement of this section if the Secretary determines that the United States has no significant tax interest in obtaining the required information.

(5) United states person's return must be consistent with trust return or Secretary notified of

inconsistency. Rules similar to the rules of section 6034A(c) shall apply to items reported by a trust under subsection (b)(1)(B) and to United States persons referred to in such subsection.

**26 U.S.C. § 6048 [Effective March 18, 2010]
Information with Respect to
Certain Foreign Trusts**

(a) Notice of certain events

(1) General rule On or before the 90th day (or such later day as the Secretary may prescribe) after any reportable event, the responsible party shall provide written notice of such event to the Secretary in accordance with paragraph (2).

(2) Contents of notice The notice required by paragraph (1) shall contain such information as the Secretary may prescribe, including—

- (A) the amount of money or other property (if any) transferred to the trust in connection with the reportable event, and
- (B) the identity of the trust and of each trustee and beneficiary (or class of beneficiaries) of the trust.

(3) Reportable event. For purposes of this subsection—

- (A) In general The term “reportable event” means—
 - (i) the creation of any foreign trust by a United States person,
 - (ii) the transfer of any money or property (directly or indirectly) to a foreign trust

by a United States person, including a transfer by reason of death, and

(iii) the death of a citizen or resident of the United States if—

(I) the decedent was treated as the owner of any portion of a foreign trust under the rules of subpart E of part I of subchapter J of chapter 1, or

(II) any portion of a foreign trust was included in the gross estate of the decedent.

(B) Exceptions.

(i) Fair market value sales Subparagraph (A)(ii) shall not apply to any transfer of property to a trust in exchange for consideration of at least the fair market value of the transferred property. For purposes of the preceding sentence, consideration other than cash shall be taken into account at its fair market value and the rules of section 679(a)(3) shall apply.

(ii) Deferred compensation and charitable trusts Subparagraph (A) shall not apply with respect to a trust which is—

(I) described in section 402(b), 404(a)(4), or 404A, or

(II) determined by the Secretary to be described in section 501(c)(3).

(4) Responsible party. For purposes of this subsection, the term “responsible party” means—

App.49a

- (A) the grantor in the case of the creation of an inter vivos trust,
 - (B) the transferor in the case of a reportable event described in paragraph (3)(A)(ii) other than a transfer by reason of death, and
 - (C) the executor of the decedent's estate in any other case.
- (b) United States owner of foreign trust
- (1) In general. If, at any time during any taxable year of a United States person, such person is treated as the owner of any portion of a foreign trust under the rules of subpart E of part I of subchapter J of chapter 1, such person shall submit such information as the Secretary may prescribe with respect to such trust for such year and shall be responsible to ensure that—
 - (A) such trust makes a return for such year which sets forth a full and complete accounting of all trust activities and operations for the year, the name of the United States agent for such trust, and such other information as the Secretary may prescribe, and
 - (B) such trust furnishes such information as the Secretary may prescribe to each United States person (i) who is treated as the owner of any portion of such trust or (ii) who receives (directly or indirectly) any distribution from the trust.
 - (2) Trusts not having United States agent
 - (A) In general. If the rules of this paragraph apply to any foreign trust, the determination

App.50a

of amounts required to be taken into account with respect to such trust by a United States person under the rules of subpart E of part I of subchapter J of chapter 1 shall be determined by the Secretary.

- (B) United States agent required. The rules of this paragraph shall apply to any foreign trust to which paragraph (1) applies unless such trust agrees (in such manner, subject to such conditions, and at such time as the Secretary shall prescribe) to authorize a United States person to act as such trust's limited agent solely for purposes of applying sections 7602, 7603, and 7604 with respect to—
- (i) any request by the Secretary to examine records or produce testimony related to the proper treatment of amounts required to be taken into account under the rules referred to in subparagraph (A), or
 - (ii) any summons by the Secretary for such records or testimony.

The appearance of persons or production of records by reason of a United States person being such an agent shall not subject such persons or records to legal process for any purpose other than determining the correct treatment under this title of the amounts required to be taken into account under the rules referred to in subparagraph (A). A foreign trust which appoints an agent described in this

App.51a

subparagraph shall not be considered to have an office or a permanent establishment in the United States, or to be engaged in a trade or business in the United States, solely because of the activities of such agent pursuant to this subsection.

- (C) Other rules to apply Rules similar to the rules of paragraphs (2) and (4) of section 6038A(e) shall apply for purposes of this paragraph.
- (c) Reporting by United States beneficiaries of foreign trusts.
 - (1) In general. If any United States person receives (directly or indirectly) during any taxable year of such person any distribution from a foreign trust, such person shall make a return with respect to such trust for such year which includes—
 - (A) the name of such trust,
 - (B) the aggregate amount of the distributions so received from such trust during such taxable year, and
 - (C) such other information as the Secretary may prescribe.
 - (2) Inclusion in income if records not provided
 - (A) In general. If adequate records are not provided to the Secretary to determine the proper treatment of any distribution from a foreign trust, such distribution shall be treated as an accumulation distribution includible in the gross income of the distributee under chapter 1. To the extent provided in regula-

tions, the preceding sentence shall not apply if the foreign trust elects to be subject to rules similar to the rules of subsection (b) (2)(B).

(B) Application of accumulation distribution rules. For purposes of applying section 668 in a case to which subparagraph (A) applies, the applicable number of years for purposes of section 668(a) shall be 1/2 of the number of years the trust has been in existence.

(d) Special rules

(1) Determination of whether United States person makes transfer or receives distribution. For purposes of this section, in determining whether a United States person makes a transfer to, or receives a distribution from, a foreign trust, the fact that a portion of such trust is treated as owned by another person under the rules of subpart E of part I of subchapter J of chapter 1 shall be disregarded.

(2) Domestic trusts with foreign activities. To the extent provided in regulations, a trust which is a United States person shall be treated as a foreign trust for purposes of this section and section 6677 if such trust has substantial activities, or holds substantial property, outside the United States.

(3) Time and manner of filing information Any notice or return required under this section shall be made at such time and in such manner as the Secretary shall prescribe.

(4) Modification of return requirements The Secretary is authorized to suspend or modify

any requirement of this section if the Secretary determines that the United States has no significant tax interest in obtaining the required information.

(5) United States person's return must be consistent with trust return or Secretary notified of inconsistency Rules similar to the rules of section 6034A(c) shall apply to items reported by a trust under subsection (b)(1)(B) and to United States persons referred to in such subsection.

26 U.S.C. § 6677 [In effect in 2007]

Failure to File Information with Respect to Certain Foreign Trusts

(a) Civil penalty. In addition to any criminal penalty provided by law, if any notice or return required to be filed by section 6048—

- (1) is not filed on or before the time provided in such section, or
- (2) does not include all the information required pursuant to such section or includes incorrect information,

the person required to file such notice or return shall pay a penalty equal to 35 percent of the gross reportable amount. If any failure described in the preceding sentence continues for more than 90 days after the day on which the Secretary mails notice of such failure to the person required to pay such penalty, such person shall pay a penalty (in addition to the amount determined under the preceding sentence) of \$ 10,000 for each 30-day period (or fraction

thereof) during which such failure continues after the expiration of such 90-day period. In no event shall the penalty under this subsection with respect to any failure exceed the gross reportable amount.

(b) Special rules for returns under section 6048(b). In the case of a return required under section 6048(b)—

- (1) the United States person referred to in such section shall be liable for the penalty imposed by subsection (a), and
- (2) subsection (a) shall be applied by substituting “5 percent” for “35 percent”.

(c) Gross reportable amount. For purposes of subsection (a), the term “gross reportable amount” means—

- (1) the gross value of the property involved in the event (determined as of the date of the event) in the case of a failure relating to section 6048(a),
- (2) the gross value of the portion of the trust’s assets at the close of the year treated as owned by the United States person in the case of a failure relating to section 6048(b)(1), and
- (3) the gross amount of the distributions in the case of a failure relating to section 6048(c).

(d) Reasonable cause exception. No penalty shall be imposed by this section on any failure which is shown to be due to reasonable cause and not due to willful neglect. 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 is not reasonable cause.

(e) Deficiency procedures not to apply. Subchapter B of chapter 63 (relating to deficiency procedures for income, estate, gift, and certain excise taxes) shall not apply in respect of the assessment or collection of any penalty imposed by subsection (a).

**26 U.S.C. § 6677 [Effective March 18, 2010]
Failure to File Information with Respect to
Certain Foreign Trusts**

(a) Civil penalty. In addition to any criminal penalty provided by law, if any notice or return required to be filed by section 6048—

- (1) is not filed on or before the time provided in such section, or
- (2) does not include all the information required pursuant to such section or includes incorrect information, the person required to file such notice or return shall pay a penalty equal to the greater of \$10,000 or 35 percent of the gross reportable amount. If any failure described in the preceding sentence continues for more than 90 days after the day on which the Secretary mails notice of such failure to the person required to pay such penalty, such person shall pay a penalty (in addition to the amount determined under the preceding sentence) of \$10,000 for each 30-day period (or fraction thereof) during which such failure continues after the

App.56a

expiration of such 90-day period. At such time as the gross reportable amount with respect to any failure can be determined by the Secretary, any subsequent penalty imposed under this subsection with respect to such failure shall be reduced as necessary to assure that the aggregate amount of such penalties do not exceed the gross reportable amount (and to the extent that such aggregate amount already exceeds the gross reportable amount the Secretary shall refund such excess to the taxpayer).

(b) Special rules for returns under section 6048(b). In the case of a return required under section 6048(b)—

- (1) the United States person referred to in such section shall be liable for the penalty imposed by subsection (a), and
- (2) subsection (a) shall be applied by substituting “5 percent” for “35 percent”.

(c) Gross reportable amount. For purposes of subsection (a), the term “gross reportable amount” means—

- (1) the gross value of the property involved in the event (determined as of the date of the event) in the case of a failure relating to section 6048(a),
- (2) the gross value of the portion of the trust’s assets at the close of the year treated as owned by the United States person in the case of a failure relating to section 6048(b)(1), and

(3) the gross amount of the distributions in the case of a failure relating to section 6048(c).

(d) Reasonable cause exception. No penalty shall be imposed by this section on any failure which is shown to be due to reasonable cause and not due to willful neglect. 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 is not reasonable cause.

(e) Deficiency procedures not to apply. Subchapter B of chapter 63 (relating to deficiency procedures for income, estate, gift, and certain excise taxes) shall not apply in respect of the assessment or collection of any penalty imposed by subsection (a).

**IRS E-NOTICE 2003-25
(JANUARY 2003)**

US INTERNAL REVENUE SERVICE
January 2003
Notice 2003-252003-1 C.B. 8552003-18 I.R.B. 855

Notice 2003-25

Subject Matter

Canadian Retirement Plan Trust Reporting

Core Terms

extension of time, reporting, plans, reporting requirements, income tax return, tax year, simplified, election, eligible, annual, notice

Text

Internal Revenue Code section 6048 requires information reporting with respect to certain foreign trusts. Persons subject to these information reporting rules must file Form 3520 (Annual Return to Report Transactions with Foreign Trusts and Receipt of Certain Foreign Gifts) or Form 3520-A (Annual Information Return of Foreign Trust with a U.S. Owner), as applicable.

Form 3520 is generally filed on an annual basis on or before the due date for the U.S. owner's or U.S. beneficiary's income tax return. A person may obtain an extension of time to file Form 3520 by obtaining an extension of time to file the applicable income tax return. Form 3520-A is generally due by the fifteenth day of the third month after the end of the trust's tax year. A person may seek an extension of time to file

App.59a

Form 3520-A by filing Form 2758 (Application for Extension of Time to File Certain Excise, Income, Information, and Other Returns). Specific penalties under Internal Revenue Code section 6677 apply if a Form 3520 or Form 3520-A is not timely filed or if the required information is incomplete or incorrect.

Treasury and the Internal Revenue Service have become aware that many taxpayers with interests in Canadian registered retirement savings plans (RRSPs), as well as the custodians of such plans, are unfamiliar with the requirements for filing Forms 3520 and 3520-A. Under the circumstances, the IRS has determined that it will enforce neither filing requirements, nor penalties under section 6677, for Forms 3520 and 3520-A with respect to such plans for tax years before 2002, and will grant additional time to file these forms for 2002. Any person who is required to file a 2002 Form 3520 or Form 3520-A with respect to an RRSP or other eligible plan within the meaning of section 3 of Revenue Procedure 2002-23, 2002-1 C.B. 744, is granted an automatic extension of time to file until August 15, 2003. If a person obtains an extension of time to file a Form 3520 or Form 3520-A for a date later than August 15, 2003, then such later extension date applies. Penalties for failure to file will not apply to a person who files by the relevant extension date.

In addition, if the beneficiary of an eligible plan has made an election in accordance with section 4 of Rev. Proc. 2002-23 and the beneficiary complies with the annual reporting requirements of Rev. Proc. 2002-23, the plan is relieved of any obligation to file Form 3520-A for any year for which such requirements are met.

Treasury and the IRS are interested in establishing for future taxable years a simplified reporting regime for RRSPs and persons with interests in RRSPs. In addition to streamlining the reporting requirements, Treasury and the IRS are considering coordinating them with the election described in Rev. Proc. 2002-23. Treasury and the IRS also will consider whether there are other pension plans similar to RRSPs for which similar simplified reporting is appropriate.

The principal author of this notice is Amanda A. Ehrlich of the Office of Associate Chief Counsel (International). For further information regarding this notice, contact Amanda A. Ehrlich or Willard W. Yates at (202) 622-3880 (not a toll-free call).

IRM 1.11.5.1.2

Part 1. Organization, Finance, and Management

Chapter 11. Internal Management Documents System

Section 5. Publishing the Internal Revenue Manual (IRM)

1.11.5.1.2 (08-01-2017)

Authority

(1) By law, federal agencies are expected to document, publish and maintain records of policies, authorities, procedures and organizational operations. The IRM is the source for the IRS. See IRM 1.11.1.3 for IMD authorities and legal obligations.

(2) United States Code Title 44 states that the U.S. Government Publishing Office is to perform all printing, binding, and blank-book work for the Federal Government. In addition, USC 44 grants the Congressional Joint Committee on Printing (JCP) the authority to regulate printing, duplicating, and distribution of products by Federal Government agencies, including the IRS. See IRM 1.171.1 .1 for the authorities for publishing government products.

(3) The Freedom of Information Act (FOIA), at 5 USC 552(a)(2)(c), requires each agency to maintain and make available for public inspection and copying a current index providing identifying information for the public. The redacted IRM and the Document 10988, IRM Index, posted on the Internal Revenue Service Web Site, <https://www.irs.gov/>, fulfill this requirement.

Source: https://www.irs.gov/irm/part1/irm_01-011-005

IRM 3.21.19.10

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE

Part 3-Submission Processing

**Chapter 3.21-International Returns
and Documents Analysis
3.21.19-Foreign Trust System**

**3.21.19.10-& diams; Correspondence & diams;
(01-01-2013)**

(1) Issue correspondence to resolve any conditions causing the return to be unworkable or unprocessable.

Exception: Do not correspond on returns prepared by Collections, Section 6020(b) or by Examination, “Substitute for Return (SFR)”.

(2) Form 3520 only: Always prepare correspondence action sheet 3653C and edit CCC “U” on a blank Form 3520 return where the taxpayer states they have no activity to report.

Note: Beginning with 1997, Form 3520 and its instructions required U.S. Owners of a foreign trust to complete Part II of Form 3520 even if they did not have any transactions with the trust that were reportable on Parts I or III. However, this requirement was not explicitly stated in the Code. Recent legislation, effective for tax years beginning after March 18, 2010, now codifies this requirement that a U.S. owner of a foreign trust must file a Form 3520 every year.

App.63a

Reminder: Inform the U.S. Owner that they must complete the 2nd checkbox on page 1 of Form 3520, and Part II of the form.

(3) Examine the return so that all of the conditions can be included in the same correspondence.

If . . . and . . . Then . . .

Correspondence is Requires a response,

1. Complete an approved needed Correspondence Action Sheet indicating the letter number (86C, 854C, etc.), Master File Tax (MFT), and the appropriate paragraphs.

Note: Within these paragraphs, there may be Fill-ins that the tax examiner will be required to enter, such as, tax period, form number, DLN, etc.

2. Attach the Correspondence Action Sheet to the front of the return below the Entity area.
3. Edit Action Code '215' on Form 3520-A, or CCC 'U' on Form 3520.
4. Continue editing the return.
5. Leave the return in the batch.

Correspondence is Does not require a

1. Complete an approved needed response, Correspondence Action Sheet indicating the letter number (86C, 854C, etc.), Master File Tax (MFT), and the appropriate paragraphs.

App.64a

Note: Within these paragraphs, there may be Fill-ins that the tax examiner will be required to enter, such as, tax period, form number, DLN, etc.

2. Photocopy and attach the Correspondence Action Sheet below the Entity area on the front of the return. Be sure the name and address shows clearly above the approved Correspondence Action Sheet.
3. Forward the copy to the Correspondence area.
4. Edit an Action Trail (*e.g.*, 3104C SENT) in the lower left corner going vertically up the side of the return.
5. Finish editing the return and leave in batch.

Note: There may be additional letters that are exclusive to the Tax Examiner's campus. These letters are for specific forms or conditions where it was deemed necessary for processing. The Tax Examiner should go to his or her Lead or Manager for copies of these letters to facilitate processing.

IRM 3.21.19.11

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE

Part 3 - Submission Processing

**Chapter 3.21-International Returns
and Documents Analysis**

3.21.19-Foreign Trust System

3.21.19.11-& diams; Correspondence & diams;

**3.21.19.11-& diams; Correspondence & diams;
(01-01-2015)**

(1) Note: Initiate taxpayer correspondence for the primary taxpayer information only (Section 1a):

- We will be forcing posting for anything else
- Any exceptions must be approved by the designated LB & I representative

(2) There are two types of correspondence that Code and Edit may encounter:

- (1) Correspondence received from taxpayers, and
- (2) Issuing correspondence to taxpayers.

(3) Issue correspondence to resolve any conditions causing the return to be unworkable or unprocessable.

Note: Initiate taxpayer correspondence for primary taxpayer (line 1b) information only (section 1a).

Note: We will be forcing processing for anything else.

App.66a

Note: Any exceptions must be approved by the designated LB & I representative. Use 3635C letter with the following open paragraph ≡ ≡ > ≡ ≡.

Note: Do not correspond on returns prepared by Collections, Section 6020(b) or by Examination, “Substitute for Return (SFR)”.

(4) Form 3520 only: Always prepare correspondence action sheet 3653C and edit CCC “U” on a blank Form 3520 return where the taxpayer states they have no activity to report.

Note: Beginning with 1997, Form 3520 and its instructions required U.S. Owners of a foreign trust to complete Part II of Form 3520 even if they did not have any transactions with the trust that were reportable on Parts I or III. However, this requirement was not explicitly stated in the Code. Recent legislation, effective for tax years beginning after March 18, 2010, now codifies this requirement that a U.S. owner of a foreign trust must file a Form 3520 every year.

Reminder: Inform the U.S. Owner that they must complete the 2nd checkbox on page 1 of Form 3520, and Part II of the form.

(5) Examine the return so that all of the conditions can be included in the same correspondence.

If . . .	and . . .
<u>Correspondence</u> is needed	Requires a response,
Then . . .	
1. Complete <u>an approved Correspondence Action Sheet</u> indicating the letter number (86C, 854C, etc.), Master File Tax (MFT), and the appro-	

App.67a

<p>appropriate paragraphs.</p>	
<p>2. Attach <u>the Correspondence Action Sheet</u> to the front of the return below the Entity area.</p>	
<p>3. Edit Action Code '215' on Form 3520-A, or CCC 'U' on Form 3520.</p>	
<p>4. Continue editing the return.</p>	
<p>5. Leave the return in the batch.</p>	
<p>Note: Within these paragraphs, there may be Fill-ins that the tax examiner will be required to enter, such as, tax period, form number, DLN, etc.</p>	
<p>If . . .</p>	<p>And . . .</p>
<p><u>Correspondence</u> is needed</p>	<p><u>Does not</u> require a response,</p>
<p>Then . . .</p>	
<p>1. Complete an approved Correspondence Action Sheet indicating the letter number (86C, 854C, etc.), Master File Tax (MFT), and the appropriate paragraphs.</p>	
<p>2. Photocopy and attach <u>the Correspondence Action Sheet</u> below the <u>Entity</u> area on the front of the return. Be sure the name and address shows clearly above the approved Correspondence Action Sheet.</p>	
<p>3. Forward the copy to the Correspondence area.</p>	
<p>4. Edit an Action Trail (e.g., 3104C SENT) in the lower left corner going vertically up the side of the return.</p>	
<p>5. Finish editing the return and leave in batch.</p>	

App.68a

Note: Within these paragraphs, there may be Fill-ins that the tax examiner will be required to enter, such as, tax period, form number, DLN, etc.

Note: There may be additional letters that are exclusive to the Tax Examiner's campus. These letters are for specific forms or conditions where it was deemed necessary for processing. The Tax Examiner should go to his or her Lead or Manager for copies of these letters to facilitate processing.

IRM 3.21.19.12

Department of the Treasury
Internal Revenue Service

Part 3-Submission Processing

**Chapter 3.21-International Returns
and Documents Analysis
3.21.19-Foreign Trust System**

**3.21.19.12-& diams; Correspondence & diams;
(11-10-2015)**

(1) Initiate correspondence with the primary U.S. taxpayer only:

- Do not correspond with the Canadian Bankers Association.
- Any exceptions must be approved by the designated LB & I representative.

(2) There are two types of correspondence that Code and Edit may encounter:

- Correspondence received from taxpayers, and
- Correspondence issued to taxpayers.

(3) Issue correspondence to resolve any conditions causing the return to be unworkable or unprocessable.

Note: Do not correspond on returns prepared by Collections, Section 6020(b) or by Examination, “Substitute for Return (SFR)”.

App.70a

(4) Form 3520 only: Always prepare correspondence action sheet 3653C and edit CCC “U” on a blank Form 3520 return where the taxpayer states they have no activity to report. Inform the U.S. Owner that they must complete the 2nd checkbox on page 1 of Form 3520, and Part II of the form.

Note: Beginning with 1997, Form 3520 and its instructions required U.S. Owners of a foreign trust to complete Part II of Form 3520 even if they did not have any transactions with the trust that were reportable on Parts I or III. However, this requirement was not explicitly stated in the Code. Recent legislation, effective for tax years beginning after March 18, 2010, now codifies this requirement that a U.S. owner of a foreign trust must file a Form 3520 every year.

(5) Examine the return so that all of the conditions can be included in the same correspondence

If . . .	And . . .
Correspondence is needed	Requires a response,
Then . . .	
1. Complete an approved Correspondence Action Sheet indicating the letter number (86C, 854C, etc.), Master File Tax (MFT), and the appropriate paragraphs.	
2. Attach the Correspondence Action Sheet to the front of the return below the Entity area.	
3. Edit Action Code “215” on Form 3520-A, or CCC “U” on Form 3520.	

App.71a

4. Continue editing the return.	
5. Leave the return in the batch.	
Note: Within these paragraphs, there may be Fill-ins that the tax examiner will be required to enter, such as, tax period, form number, DLN, etc.	
If . . .	And . . .
Correspondence is needed	Does not require a response,
Then . . .	
1. Complete an approved Correspondence Action Sheet indicating the letter number (86C, 854C, etc.), Master File Tax (MFT), and the appropriate paragraphs.	
2. Photocopy and attach the Correspondence Action Sheet below the Entity area on the front of the return. Be sure the name and address shows clearly above the approved Correspondence Action Sheet.	
3. Forward the copy to the Correspondence area.	
4. Edit an Action Trail (e.g., 3104C SENT) in the lower left corner going vertically up the side of the return.	
5. Finish editing the return and leave in batch.	
Note: Within these paragraphs, there may be Fill-ins that the tax examiner will be required to enter, such as, tax period, form number, DLN, etc.	

Note: There may be additional letters that are exclusive to the Tax Examiner's campus. These letters are for specific forms or conditions where it was deemed necessary for processing. The Tax Examiner should

App.72a

go to his or her Lead or Manager for copies of these letters to facilitate processing.

**CHIEF COUNSEL MEMORANDUM
(NOVEMBER 9, 2011)**

OFFICE OF CHIEF COUNSEL
INTERNAL REVENUE SERVICE

MEMORANDUM

Number: 201150029

Release Date: 12/16/2011

CC: PA:02:GTArmstrong
POSTS-129684-11

UILC: 6048.00-00, 6677.00-00

date: November 09, 2011

to: Daisy D. Batman
Appeals Officer, International Specialist

from: Ashton P. Trice
Chief, Branch 2
(Procedure & Administration) CC:PA:02

Subject: Divisibility of the penalty under section 6677

This Chief Counsel Advice responds to your request for assistance. This advice may not be used or cited as precedent.

Issue

Whether the penalty imposed by section 6677 for failure to file information with respect to foreign trusts is a “divisible tax” such that a taxpayer would need to pay only a portion of the penalty to meet the full payment rule established by *Flora v. United States*, 362 U.S. 145 (1960).

Conclusions

A penalty assessment pursuant to section 6677 is not a “divisible tax” within the meaning of *Flora v. United States*, 362 U.S. 145 (1960). A taxpayer must pay the full amount of the penalty to challenge the entire penalty assessment under section 6677 for a particular year. Notwithstanding that requirement, a taxpayer may pay that portion of the penalty assessment that relates to a separate filing requirement if the taxpayer wants to contest only that portion of the penalty. The taxpayer could not, however, challenge the merits of the remaining portions of the assessment absent prior payment of the remaining portions.

Background

Under section 6048, the Service generally requires annual information reporting by U.S. persons with respect to contributions to, ownership of, and distributions from a foreign trust. Section 6677 generally imposes penalties on persons who fail to comply with section 6048.

You asked whether an assessment of a penalty under section 6677 for a failure to comply with section 6048 is a “divisible tax.” Normally, a taxpayer must pay the full amount of the tax at issue to provide a refund court jurisdiction over the taxpayer’s liability (the “full payment rule”). A divisible tax is one for which the taxpayer need only pay a “divisible” portion prior to bringing a suit for refund.

Law and Analysis

1. Section 6048

Section 6048 contains three distinct and separate reporting obligations. First, under section 6048(a), a responsible party must inform the Service of each occasion upon which a U.S. person creates a foreign trust, transfers money or property to a foreign trust, or when a citizen or resident of the United States dies if the decedent owned a portion of a foreign trust. Second, under section 6048(b), a U.S. person treated as owning a foreign trust under the grantor trust rules (sections 671 through 679) must report information with respect to that trust and also must ensure that the trust itself reports information to the Service and to each U.S. person treated as owning, or receiving a distribution from, the trust. Lastly, under section 6048(c), any U.S. person who receives a distribution from a foreign trust during the taxable year must report information about that distribution to the Service.

Any U.S. person or responsible party who is required to report information under section 6048(a) or (c) or who is required to report information under section 6048(b) because he is treated as the owner of a foreign trust under the grantor trust rules, must file a Form 3520 (Annual Return To Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts) by the due date (including extensions) for his U.S. tax return. Under section 6048(b), the U.S. owner of a foreign trust is required to file a Form 3520 for each taxable year even if there is no transaction with the foreign trust during the year. A separate Form 3520 is required with respect to each

foreign trust for which the person is required to report information.

Any foreign trust with a U.S. owner is required to file a Form 3520-A (Annual Information Return of Foreign Trust with a U.S. Owner) by the 15th day of the 3rd month after the end of the trust's tax year. The foreign trust also is required to give copies of the Foreign Grantor Trust Owner Statement (page 3 of Form 3520-A) and Foreign Grantor Trust Beneficiary Statement (page 4 of Form 3520-A) to the U.S. owners and U.S. beneficiaries by the same date. Form 3520 instructs a U.S. owner of a foreign trust who has not received a Foreign Grantor Trust Owner Statement from the foreign trust to complete a substitute Form 3520-A to the best of his ability and attach it to his Form 3520.

2. Section 6677

The amount of the section 6677 penalty for a failure to file a correct and complete Form 3520 will depend upon which subsection of section 6048 is violated. Where a U.S. person or responsible party fails to report a transaction with a foreign trust under subsection (a) or (c), the person will owe an initial penalty equal to the greater of \$10,000 or 35 percent of the "gross reportable amount."¹ "Gross reportable amount" for these purposes means the gross value of the property involved in the event reportable under section 6048(a), or the gross amount of the distributions in the case of a failure relating to section 6048(c). I.R.C. § 6677(c)(1), (3). For example, if a U.S. person files a

¹ Prior to 2010, the initial penalty was 35% of the gross reportable amount.

Form 3520, but fails to report a transaction with the foreign trust valued at \$30,000, the U.S. person will owe a penalty (absent showing of reasonable cause) equal to \$10,500 (35% of \$30,000).

If a U.S. person fails to file a Form 3520 when required by section 6048(b)² or a foreign trust that is treated as owned by a U.S. person fails to file Form 3520-A and that U.S. person does not file a substitute Form 3520-A, the U.S. person will owe an initial penalty under section 6677(b) equal to the greater of \$10,000 or 5 percent of the “gross reportable amount.”³ Here, “gross reportable amount” means the value of the foreign trust’s assets at the close of the year treated as owned by the U.S. person. I.R.C. § 6677(c)(2). For example, if a foreign trust with a U.S. owner and assets of \$250,000 fails to file a complete and correct Form 3520-A and the U.S. owner fails to file a substitute Form 3520-A, the U.S. owner will owe an initial penalty (absent showing of reasonable cause) equal to \$12,500 (5% of \$250,000).

In all cases, an additional \$10,000 penalty is imposed for each 30-day period during which the failure to file an information return continues (beginning 90 days after notification of the failure). The total amount of the penalties cannot exceed the gross reportable amount.

² A U.S. person treated as the owner of a foreign trust who fails to file Form 3520 when required under section 6048(b) will be subject to a penalty for such failure only with respect to tax years beginning after March 18, 2010.

³ Prior to 2010, the initial penalty was 5% of the gross reportable amount for failure to file Form 3520-A.

Section 6677(d) provides that no penalty will be imposed by section 6677 on any failure that is shown to be due to reasonable cause and not due to willful neglect. 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 does not constitute reasonable cause.

3. Divisibility

Prior to bringing a suit for refund in a federal district court or the Court of Federal Claims, a taxpayer must pay the full amount of tax that will be at issue before the court. *See Flora v. United States*, 362 U.S. 145 (1960) (Flora II); *Boynton v. United States*, 566 F.2d 50 (9th Cir. 1977). In *Flora*, the Supreme Court considered a suit for refund in which the taxpayer only paid a small portion of the tax at issue. Analyzing the structure of 28 U.S.C. § 1346(a)(1) (the statute granting jurisdiction over tax refund suits), its legislative history, and related jurisdictional statutes, the Court found “full payment of an assessed tax . . . a condition precedent to the right to sue the collector for a refund.” *Flora v. United States*, 357 U.S. 63, 68 (1958) (Flora I), *aff’d on reh’g*, 362 U.S. 145 (1962) (Flora II). Accordingly, the Court concluded the taxpayer’s suit for refund could not proceed because the court lacked jurisdiction under 28 U.S.C. § 1346 absent full payment of the tax. The Court did recognize, however, that in some instances full payment may not be necessary, for example, in the case of excise taxes which “may be divisible into a tax on each transaction or event.” *Flora*, 362 U.S. at 171 n. 37, 38 (1960).

From that recognition was born the “divisible tax” exception to the full payment rule. Where a tax is considered a “divisible tax,” the taxpayer need only pay a portion of the tax before instituting suit (assuming other jurisdictional prerequisites are met). “A divisible tax . . . is one that represents the aggregate of taxes due on multiple transactions (e.g., sale of items subject to excise taxes).” *Rocovich v. United States*, 933 F.2d 991, 995 (Fed. Cir. 1991) (citing *Flora II*). It is a tax the assessment of which reflects the cumulation of several separable assessments based on separate transactions. *See Fidelity Bank, N.A. v. United States*, 616 F.2d 1181, 1182 n.1 (10th Cir. 1980). Certain courts have found that the “divisible tax” exception only applies in two types of situations: “(1) a suit challenging unpaid excise taxes; or (2) a suit challenging a 100% penalty pursuant to [section] 6672 for failure to withhold and pay over employment taxes.” *Ardalan v. United States*, 748 F.2d 1411, 1414 (10th Cir. 1984); *see also Bell Capital Mgmt. v. United States*, 207 U.S. Dist. LEXIS 82085, *11-12 (N.D. Ga. 2007); *Thorton v. United States*, 1992 U.S. Dist. LEXIS 6819 (S.D. Fla. 1992). Other courts, however, have recognized the exception can apply in additional situations. *See, e.g., Hankin v. United States*, 891 F.2d 480, 481 (3rd Cir. 1989) (acknowledging penalties imposed under sections 6700 and 6701 are “divisible into separate portions or transactions”); *Nordbrock v. United States*, 173 F. Supp.2d 959 (D. Ariz. 2000), *aff’d* 248 F.3d 1172 (9th Cir. 2001) (finding penalty on tax return preparers pursuant to section 6695 divisible).⁴

⁴ One section of the Code explicitly defines a “divisible tax” as any tax imposed by subtitle C (employment taxes) and the penalty imposed by section 6672 with respect to such taxes. I.R.C. § 6331

Payment of the divisible part of a tax or penalty that constitutes a “divisible tax” satisfies the full payment rule established by *Flora*. Accordingly, where a taxpayer pays the divisible portion of a “divisible tax” prior to bringing a suit for refund, the court in which the suit is brought will have jurisdiction over the entire amount of, and the liability for, the “divisible tax” at issue. *See, e.g., Nielson v. United States*, 976 F.2d 951 (5th Cir. 1992).

In *Nielson*, the Fifth Circuit considered the scope of a district court’s jurisdiction where a taxpayer, pursuant to section 6703, pays only 15 percent of the penalty at issue prior to bringing suit. Section 6703 authorizes partial payment of penalties imposed under sections 6700, 6701, and 6702 (without explicitly calling those penalties “divisible taxes”). Although the taxpayer contended the court’s jurisdiction was limited to determining liability for the 15 percent paid, the district court found the taxpayer liable for the entire amount of the penalty (*i.e.*, the 15 percent paid plus the 85 percent unpaid). The Fifth Circuit agreed with the district court’s finding. Analogizing section 6703 to section 6694 (which also provides for

(i)(2). This definition only applies, however, in a situation in which the Service levies with respect to an unpaid divisible tax during the pendency of a court proceeding challenging that tax. Moreover, this definition lacks any reference to excise taxes. *See Nakano v. United States*, 2009 U.S. Dist. LEXIS 130862 (D. Ariz. 2009) (noting and holding that an excise tax is not a divisible tax within the meaning of section 6331(i)(2)). Because it fails to encompass excise taxes, which the Supreme Court has specifically identified as being subject to the “divisible tax” exception, and because of the limiting language of section 6331(i)(2), this definition cannot control for purposes of determining whether a tax is “divisible” in the context of the *Flora* rule.

15 percent partial payment) and relying on the legislative history of both sections, the Fifth Circuit found that where a taxpayer makes partial payment of the penalty under those sections, he is suing for a determination of his liability for the entire penalty, not just the amount paid.

While neither section 6703 or 6694 explicitly refers to these penalties as “divisible taxes,” they do create an exception for these penalties from the full payment rule akin to the “divisible tax” exception. Because of that similarity, we conclude that the reasoning in *Nielson* guides our analysis here. In addition, the conclusion in *Nielson* (that the court had jurisdiction over the entire penalty assessment) finds support in cases adjudicating liability under section 6672, a penalty traditionally labeled a “divisible tax.” See *Steele v. United States*, 280 F.2d 89 (8th Cir. 1960) (allowing corporate officers to pay as to one employee, institute a suit for refund, and have the court “sett[l]e the question of the right of the government to have made the penalty assessment against them”). Therefore, a determination that the penalty under section 6677 constitutes a “divisible tax” would enable a person liable for that penalty to partially pay, satisfy the full payment rule, and trigger a refund court’s jurisdiction over the entire penalty amount. Based on the precedent above and for the reasons below, however, we conclude that the penalty under section 6677 does not constitute a “divisible tax,” and therefore a court could not exercise jurisdiction over any amount of the penalty not paid.

As stated above, section 6048 imposes three distinct and separate reporting obligations on the following parties: (1) U.S. persons that create, or

transact with, a foreign trust (or in the case of a decedent who is a U.S. resident or citizen treated as owning a foreign trust, the responsible party); (2) U.S. persons that are treated as owning a foreign trust (as well as the trust itself); and (3) U.S. persons that receive a distribution from a foreign trust. Section 6677 imposes a penalty for each failure to meet the requirements of section 6048. Accordingly, where there are multiple, unreported transactions during the taxable year, the U.S. person will owe a penalty for each unreported transaction. Similarly, where a U.S. person is treated as the owner of multiple foreign trusts for which no Forms 3520-A have been filed, the U.S. person will owe a penalty with respect to each foreign trust. The amount of each penalty will depend on the gross amount of the unreported transaction or the amount of the assets in the unreported trust. A penalty assessment under section 6677, therefore, can reflect an aggregate of penalties imposed for multiple failures to meet any of the reporting obligations imposed by section 6048. Because that single assessment can in actuality be a cumulation of separable penalties specific to each failure, the penalty assessment would appear to be a “divisible tax.”

In *Christian Laymen in Partnership, Ltd. v. United States*, 1989 WL 168769 (W.D. Okla. 1989), the refund claimant (a partnership) contested an assessment of the penalty under section 6698 for failure to file a partnership return. Section 6698 imposes a penalty for each month, not to exceed five months, that the partnership fails to file its return. Even though the partnership failed to file for over five months, it only paid a portion equal to one month’s worth of the penalty, contending the “divisible

tax” exception applied. At the urging of the government, the court disagreed and found that the penalty under section 6698 was not divisible, noting: “[t]here is only one failure to file. The penalty is increased for the continuing failure to file, but is not increased as a result of separate acts or transactions.” *Id.* at *2. The court concluded that because the penalty is for a single act (the failure to file the return) and not based on separate acts, the partnership needed to pay the full penalty amount before successfully bringing suit. A section 6677 penalty shares characteristics with the section 6698 penalty when the assessment is based on additional penalties for failure to file the required information return after notice from the Service. In each case, there is only one failure to file. The penalty assessment under section 6677, however, may also be tied to multiple acts, *i.e.*, the failure to file a separate, complete and correct Form 3520 for each separate trust or the failure to report each separate transaction. Accordingly, unlike the penalty under section 6698, the penalty may increase based on the number of violations of section 6048’s requirements, again lending credence to the argument that a penalty assessment under section 6677 is a “divisible tax” with respect to each unreported transaction or trust.

The conclusion that payment of a portion of the penalty could afford jurisdiction over the entire assessment covering multiple penalties is difficult to reconcile, however, with the reasonable cause defense to the penalty. Section 6677(d) states that no penalty shall be imposed on any failure which is shown to be due to reasonable cause and not due to willful neglect. An assessment under section 6677 may actually be a

cumulation of failures to file multiple Forms 3520 or report multiple transactions because of the multiple obligations imposed by section 6048, each with its own unique “gross reportable amount.” Because a taxpayer can show reasonable cause for “any failure” under section 6677, a taxpayer could have different reasonable cause defenses for different failures that make up the penalty. It follows that were the section 6677 penalty a “divisible tax,” it could create a potential situation in which the taxpayer pays one portion of the penalty and because, assuming it were a “divisible tax,” the court would have jurisdiction over the entire penalty assessment, the taxpayer could present different reasonable cause defenses to different portions of the penalty, including portions that are not paid prior to suit. That result does not square with the purpose behind the “divisible tax” exception to the full payment rule.

In addition, unlike other assessable penalties under sections 6700, 6701, 6702 and 6694, the penalty under section 6677 does not have a statutory provision authorizing partial payment prior to a refund suit. I.R.C. §§ 6703, 6694(c). While this factor is not dispositive, it does stand the penalty here in stark contrast with other assessable penalties. *See Rocovich v. United States*, 933 F.2d 991 (Fed. Cir. 1991) (noting the lack of statutory authority for deeming the estate tax a “divisible tax”).

Therefore, because of the multiple reporting obligations under section 6048 that could apply and the possibility of multiple reasonable cause defenses to those reporting obligations, we conclude that the penalty under section 6677 is not a “divisible tax” for the purposes of the full payment rule. We reach this

conclusion even in light of the fact that the penalty assessment, in certain circumstances, can constitute an aggregate of separable assessments for failures related to separate transactions or trusts. Notwithstanding that conclusion, we also conclude that if a taxpayer chooses only to contest a portion of the penalty relating to one or more particular failures to report, but not all failures, the taxpayer may pay that portion and sue for refund. If the taxpayer desires to challenge the entire penalty assessment, however, the taxpayer must pay the entire tax under dispute prior to bringing a refund suit.

Case Development, Hazards and Other Considerations

This writing may contain privileged information. Any unauthorized disclosure of this writing may undermine our ability to protect the privileged information. If disclosure is determined to be necessary, please contact this office for our views.

Please call (202) 622-4940 if you have any further questions.

**1997 FORM 3520
AND INSTRUCTIONS
(TRANSCRIPTION OF TAX FORM)**

Form **3520**
Department of the Treasury
Internal Revenue Service

**Annual Return To Report Transactions With
Foreign Trusts and Receipt of Certain Foreign Gifts**

OMB No. 1545-0159

1997

File in duplicate. Instructions are separate.

**All information must be in English.
Show all amounts in U.S. dollars. File a
separate Form 3520 for each foreign trust.**

For calendar year 1997, or tax year beginning,
19, ending, 19

Check appropriate box(es): See Instructions.

Initial return Final return Amended return

Check box that applies to U.S. person filing return:

Individual Partnership Corporation
 Trust Executor

Check all applicable boxes:

- (a)** You are a U.S. transferor who, directly or indirectly, transferred money or other property during the current tax year, to a foreign trust or **(b)** you held an outstanding obligation of a related foreign trust (or a person related to the trust) issued during the current tax year, that you treated as a “qualified obligation” (defined on page 3 of the instructions) during the current tax year. See the instructions for Part I.

App.87a

- You are a U.S. owner of all or any portion of a foreign trust at any time during the tax year. See the instructions for Part II.
- (a)** You are a U.S. person who, during the current tax year, received a distribution from a foreign trust or **(b)** a related foreign trust held an outstanding obligation issued by you (or a person related to you) during the current tax year that you treated as a “qualified obligation” (defined on page 3 of the instructions) during the current tax year. See the instructions for Part III.
- You are a U.S. person who, during the current tax year, received certain gifts or bequests from a foreign person. See the instructions for Part IV.

Service Center where U.S. person filing this return files its income tax return ►

- 1a** Name of U.S. person(s) filing return
- b** Identification number
- c** Number, street, and room or suite no. (If a P.O. box, see instructions.)
- d** Spouse’s identification number (see instr.)
- e** City or town
- f** State or province
- g** ZIP or postal code
- h** Country

- 2a** Name of foreign trust (if applicable)
- b** Identification number (if any)

App.88a

- c** Number, street, and room or suite no.
- d** City or town
- e** State or province
- f** ZIP or postal code
- g** Country

3 Did the foreign trust appoint a U.S. agent (defined on page 3 of the instructions) who can provide the IRS with all relevant trust information?

- Yes No

If "Yes," complete lines 3a through 3g.

- 3a** Name of U.S. agent
- b** Identification number (if any)
- c** Number, street, and room or suite no.
- d** City or town
- e** State or province
- f** ZIP or postal code
- g** Country

- 4a** Name of U.S. decedent (see instr.)
- b** Address
- c** TIN of decedent
- d** Date of death
- e** EIN of estate

Part I Transfers by U.S. Persons to a Foreign Trust
During the Current Tax Year (See instructions.)

- | |
|---|
| <p>5a Name of trust creator (if different from line 1a)</p> <p>b Address</p> <p>c Identification number (if any)</p> |
|---|

- | |
|---|
| <p>6a Country code of country where trust was created</p> <p>b Country code of country whose law governs the trust</p> <p>c Date trust was created</p> |
|---|

- | |
|---|
| <p>7a Will any other person be treated as the owner of the transferred assets after the transfer?</p> <p><input type="checkbox"/> Yes <input type="checkbox"/> No</p> |
|---|

- | |
|---|
| <p>b Name of other foreign trust owners, if any
(a)</p> |
|---|

<p>Address (b)</p>

<p>Country of residence (c)</p>
--

<p>Identification number, if any (d)</p>

<p>Relevant code section (e)</p>

App.90a

Under penalties of perjury, I declare that I have examined this return, including any accompanying reports, schedules, or statements, and to the best of my knowledge and belief, it is true, correct, and complete.

Signature

Title

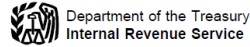
Date

Preparer's Signature

Preparer's identification number

Date

1997



Instructions for Form 3520

Annual Return To Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts

Section references are to the Internal Revenue Code unless otherwise noted.

GENERAL INSTRUCTIONS

Changes to Note

As a result of changes made by the Taxpayer Relief Act of 1997:

- The excise tax under section 1491 was repealed with respect to transfers after August 4, 1997.
- With respect to transfers by a U.S. person to a foreign nongrantor trust after August 4, 1997, the transfer is treated as a sale or exchange and the transferor must recognize as gain the excess of the fair market value (FMV) of the transferred property over its adjusted basis. Although the gain is not reported on Form 3520, it is to be reported on the appropriate form or schedule on your income tax return. Also complete Part I of Form 3520. See section 684 of the Code.
- FMV transfers by a U.S. person to a foreign nongrantor trust (other than transfers that are treated as FMV transfers by reason of the receipt of a qualified obligation which are reported on Schedule E, Form 3520) after August 4, 1997, are no longer reportable on Form 3520.

App.92a

- The U.S. beneficiary and U.S. owner's tax return must be consistent with the Form 3520-A, Annual Information Return of Foreign Trust With a U.S. Owner, filed by the foreign trust unless you report the inconsistency to the IRS. If you are treating items on your tax return differently from the way the foreign trust treated them on its return, file Form 8082, Notice of Inconsistent Treatment or Amended Return. Get Form 8082 for more details.

Purpose of Form

U.S. persons file Form 3520 to report:

- Certain transactions with foreign trusts, and
- Receipt of certain large gifts or bequests from certain foreign persons.

A separate Form 3520 must be filed for transactions with each foreign trust.

WHO MUST FILE

File Form 3520 if:

1. You are the responsible party for reporting a reportable event that occurred during the current tax year, or you held an outstanding obligation of a related foreign trust (or a person related to the trust) that you treated as a qualified obligation during the current tax year. Responsible party, reportable event, and qualified obligation are defined on page 3.

Complete the first part of page 1 and the relevant portions of Part I. See the instructions for Part I.

App.93a

2. You are a U.S. person who, during the current tax year, is treated as the owner of any part of the assets of a foreign trust under the grantor trust rules.

Complete the first part of page 1 and Part II. See the instructions for Part II.

3. You are a U.S. person who, during the current tax year, received a distribution from a foreign trust, or a related foreign trust held an outstanding obligation issued by you (or a person related to you) that you treated as a qualified obligation (defined on page 3) during the current tax year.

Complete the first part of page 1 and Part III. See the instructions for Part III.

4. You are a U.S. person who, during the current tax year, received either:

- a. More than \$100,000 from a nonresident alien individual or a foreign estate (including foreign persons related to that nonresident alien individual or foreign estate) that you treated as gifts or bequests, or
- b. More than \$10,276 from foreign corporations or foreign partnerships (including foreign persons related to such foreign corporations or foreign partnerships) that you treated as gifts.

Complete the first part of page 1 and Part IV. See the instructions for Part IV.

Note: You may also be required to file Form TD F 90-22.1, Report of Foreign Bank and Financial Accounts.

Exceptions to filing Form 3520

Form 3520 does not have to be filed to report the following transactions:

- Transfers to foreign trusts described in sections 402(b), 404(a)(4), or 404A.
- FMV transfers by a U.S. person to a foreign nongrantor trust (other than transfers that are treated as FMV transfers by reason of the receipt of a qualified obligation) made after August 4, 1997.
- Transfers to foreign trusts that have a current determination letter from the IRS recognizing their status as exempt from income taxation under section 501(c)(3).
- Transfers to, distributions from, and ownership of Canadian Registered Retirement Savings Plans if the trust would qualify for treaty benefits under the Convention Between the United States of America and Canada with Respect to Taxes on Income and on Capital. However, if for any taxable year you rely on the tax treaty with Canada to avoid information reporting, you are required to disclose this position pursuant to section 6114. *See* Pub. 901, U.S. Tax Treaties.
- Distributions from foreign trusts that are taxable as compensation for services rendered (within the meaning of section 672(f)(2)(B) and its regulations), so long as the recipient reports the distribution as compensation income on its applicable Federal income tax return.

- Distributions from foreign trusts to domestic trusts that have a current determination letter from the IRS recognizing their status as exempt from income taxation under section 501(c)(3).

[. . .]

Definitions

[. . .]

A qualified obligation, for purposes of this form, is any obligation if:

1. The obligation is reduced to writing by an express written agreement,
2. The term of the obligation does not exceed 5 years (including options to renew and roll-overs) and it is repaid within the 5-year term,
3. All payments on the obligation are denominated in U.S. dollars,
4. The yield to maturity of the obligation is not less than 100% of the applicable Federal rate under section 1274(d) for the day on which the obligation is issued and not greater than 130% of the applicable Federal rate,
5. The U.S. person agrees to extend the period for assessment of any income or transfer tax attributable to the transfer and any consequential income tax changes for each year that the obligation is outstanding, to a date not earlier than 3 years after the maturity date of the obligation, unless the maturity date of the obligation does not extend beyond the end of the U.S. person's taxable year

and is paid within such period (this is done on Part I, Schedule A, and Part III, as applicable), and

6. The U.S. person reports the status of the note, including principal and interest payments, on Part I, Schedule A, and Part III, as applicable, for every year that the loan is outstanding.

[. . .]

A related person generally includes any person who is related to you for purposes of sections 267 and 707(b). This includes, but is not limited to:

- A member of your family—your brothers and sisters, half-brothers and half-sisters, spouse ancestors (parents, grandparents, etc.), lineal descendants (children, grandchildren, etc.), and the spouses of any of these persons.
- A corporation in which you, directly or indirectly, own more than 50% in value of the outstanding stock. See section 643(i)(2)(B). In addition, see the regulations pursuant to sections 267 and 707(b) for further guidance on related parties.

A related foreign trust. A person is related to a foreign trust if such person, without regard to the transfer at issue, is a grantor of the trust, a beneficiary of the trust, or is related to any grantor or beneficiary of the trust. See definition of a related person above.

A reportable event includes:

App.97a

1. The creation of a foreign trust by a U.S. person.
2. The transfer of any money or property, directly or indirectly, to a foreign trust by a U.S. person, including a transfer by reason of death if:
 - a. The transfer was a gratuitous transfer (defined on page 2),
 - b. With respect to a transfer prior to August 5, 1997, you received at least FMV for the property transferred and did not immediately recognize all of the gain (if any) on the property transferred, or
 - c. With respect to a FMV transfer prior to August 5, 1997, the transfer was to a related foreign trust.
3. The death of a citizen or resident of the United States if:
 - a. The decedent was treated as the owner of any portion of a foreign trust under the grantor trust rules, or
 - b. Any portion of a foreign trust was included in the gross estate of the decedent.
4. A trust that was not a foreign trust becomes a foreign trust.

Responsible party means:

- The transferor in the case of a reportable event (defined above).
- The executor of the decedent's estate in any other case.

Who Must Sign

If the return is filed by an individual or a fiduciary, it must be signed by that individual or fiduciary. If it is filed by a partnership, it must be signed by a general partner or limited liability company member. If it is filed by a corporation, it must be signed by the president, vice president, treasurer, assistant treasurer, chief accounting officer, or other corporate officer (such as a tax officer) who is authorized to sign. The paid preparer must complete the required preparer information and:

- Sign the return, by hand, in the space provided for the preparer's signature (signature stamps are not acceptable).
- Give a copy of the return to the filer.

**2007 FORM 3520
AND INSTRUCTIONS
(TRANSCRIPTION OF TAX FORM)**

Form 3520 <small>Department of the Treasury Internal Revenue Service</small>	Annual Return To Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts <small>▶ See separate instructions.</small>	<small>OMB No. 1545-0159</small> 2007
--	---	---

**Note: All information must be in English.
Show all amounts in U.S. dollars. File a
separate Form 3520 for each foreign trust.**

For calendar year 2007, or tax year beginning, 2007, ending , 20
Check appropriate box(es): <input type="checkbox"/> Initial return <input type="checkbox"/> Final return <input type="checkbox"/> Amended return
Check box that applies to person filing return: <input type="checkbox"/> Individual <input type="checkbox"/> Partnership <input type="checkbox"/> Corporation <input type="checkbox"/> Trust <input type="checkbox"/> Executor

Check all applicable boxes:

- (a) You are a U.S. transferor who, directly or indirectly, transferred money or other property during the current tax year to a foreign trust,
- (b) You held an outstanding obligation of a related foreign trust (or a person related to the trust) issued during the current tax year, that you reported as a “qualified obligation” (defined in the instructions) during the current tax year,
- (c) You are the executor of the estate of a U.S. decedent and (1) the decedent made a transfer to a foreign trust by reason of death, (2) the decedent was treated as the owner of any portion of a foreign trust immediately prior to

App.100a

death, or (3) the decedent's estate included any portion of the assets of a foreign trust. See the instructions for Part I.

- You are a U.S. owner of all or any portion of a foreign trust at any time during the tax year. See the instructions for Part II.
- (a)** You are a U.S. person who, during the current tax year, received a distribution from a foreign trust or **(b)** You are a U.S. person and you are also a grantor or beneficiary of a foreign trust that has made a loan of cash or marketable securities directly or indirectly to you during the current tax year that you reported as a "qualified obligation" (defined in the instructions) during the current tax year. See the instructions for Part III.
- You are a U.S. person who, during the current tax year, received certain gifts or bequests from a foreign person. See the instructions for Part IV.

Service Center where U.S. person's income tax return is filed ►

- 1a** Name of U.S. person(s) filing return
- b** Identification number
- c** Number, street, and room or suite no. (If a P.O. box, see instructions.)
- d** Spouse's identification number (see instr.)
- e** City or town
- f** State or province
- g** ZIP or postal code

App.101a

<p>h Country</p>
<p>2a Name of foreign trust (if applicable)</p> <p>b Employer identification number if any)</p> <p>c Number, street, and room or suite no. (if a P.O. box, see instructions)</p> <p>d City or town</p> <p>e State or province</p> <p>f ZIP or postal code</p> <p>g Country</p>
<p>3 Did the foreign trust appoint a U.S. agent (defined in the instructions) who can provide the IRS with all relevant trust information?</p> <p><input type="checkbox"/> Yes <input type="checkbox"/> No</p> <p>If “Yes,” complete lines 3a through 3g.</p>
<p>3a Name of U.S. agent</p> <p>b Identification number (if any)</p> <p>c Number, street, and room or suite no. (if a P.O. box, see instructions)</p> <p>d City or town</p> <p>e State or province</p> <p>f ZIP or postal code</p> <p>g Country</p>
<p>4a Name of U.S. decedent (see instr.)</p> <p>b Address</p> <p>c TIN of decedent</p>

App.102a

d Date of death

e EIN of estate

f Check applicable box:

- U.S. decedent made transfer to a foreign trust by reason of death.
- U.S. decedent treated as owner of foreign trust immediately prior to death.
- Assets of foreign trust were included in estate of U.S. decedent.

Under penalties of perjury, I declare that I have examined this return, including any accompanying reports, schedules, or statements, and to the best of my knowledge and belief, it is true, correct, and complete.

Signature

Title

Date

Preparer's Signature

Preparer's identification number

Date

2007



Instructions for Form 3520

**Annual Return To Report Transactions With Foreign Trusts
and Receipt of Certain Foreign Gifts**

GENERAL INSTRUCTIONS

Purpose of Form

U.S. persons (and executors of estates of U.S. decedents) file Form 3520 to report:

- Certain transactions with foreign trusts and
- Receipt of certain large gifts or bequests from certain foreign persons.

A separate Form 3520 must be filed for transactions with each foreign trust.

Who Must File

File Form 3520 if:

1. You are the responsible party for reporting a reportable event that occurred during the current tax year, or you held an outstanding obligation of a related foreign trust (or a person related to the trust) that you treated as a qualified obligation during the current tax year. Responsible party, reportable event, and qualified obligation are defined on pages 3 and 4.

Complete the identifying information on page 1 of the form and the relevant portions of Part I. See the instructions for Part I.

2. You are a U.S. person who, during the current tax year, is treated as the owner of any part of the assets of a foreign trust under the grantor trust rules.

App.104a

Complete the identifying information on page 1 of the form and Part II. See the instructions for Part II.

3. You are a U.S. person who received (directly or indirectly) a distribution from a foreign trust during the current tax year **or** a related foreign trust held an outstanding obligation issued by you (or a person related to you) that you treated as a qualified obligation (defined on page 3) during the current tax year.

Complete the identifying information on page 1 of the form and Part III. See the instructions for Part III.

4. You are a U.S. person who, during the current tax year, received either:

- a. More than \$100,000 from a nonresident alien individual or a foreign estate (including foreign persons related to that nonresident alien individual or foreign estate) that you treated as gifts or bequests; or
- b. More than \$13,258 from foreign corporations or foreign partnerships (including foreign persons related to such foreign corporations or foreign partnerships) that you treated as gifts.

Complete the identifying information on page 1 of the form and Part IV. See the instructions for Part IV.

Note: You may also be required to file Form TD F 90-22.1, Report of Foreign Bank and Financial Accounts.

Exceptions To Filing

Form 3520 does not have to be filed to report the following transactions.

- Transfers to foreign trusts described in sections 402(b), 404(a)(4), or 404A.
- Most fair market value (FMV) transfers by a U.S. person to a foreign trust. However, some FMV transfers must nevertheless be reported on Form 3520 (e.g., transfers in exchange for obligations that are treated as qualified obligations, transfers of appreciated property to a foreign trust for which the U.S. transferor does not immediately recognize all of the gain on the property transferred, transfers involving a U.S. transferor that is related to the foreign trust). See Section III of Notice 97-34, 1997-25 I.R.B. 22.
- Transfers to foreign trusts that have a current determination letter from the IRS recognizing their status as exempt from income taxation under section 501 (c)(3).
- Transfers to, ownership of, and distributions from a Canadian registered retirement savings plan (RRSP) or a

Canadian registered retirement income fund (ARIF), where the U.S. citizen or resident alien holding an interest in such RRSP or RRIF is eligible to file Form 8891, U.S. Information Return for Beneficiaries of Certain Canadian Registered Retirement Plans, with respect to the RRSP or RRIF.

- Distributions from foreign trusts that are taxable as compensation for services rendered

App.106a

(within the meaning of section 672(f)(2)(B) and its regulations), so long as the recipient reports the distribution as compensation income on its applicable federal income tax return.

- Distributions from foreign trusts to domestic trusts that have a current determination letter from the IRS recognizing their status as exempt from income taxation under section 501 (c)(3).
- Domestic trusts that become foreign trusts to the extent the trust is treated as owned by a foreign person, after application of section 672(f).

Who Must File

File Form 3520 if:

1. You are the responsible party for reporting a reportable event that occurred during the current tax year, or you held an outstanding obligation of a related foreign trust (or a person related to the trust) that you treated as a qualified obligation during the current tax year. Responsible party, reportable event, and qualified obligation are defined on pages 3 and 4.

Complete the identifying information on page 1 of the form and the relevant portions of Part I. See the instructions for Part I.

2. You are a U.S. person who, during the current tax year, is treated as the owner of any part of the assets of a foreign trust under the grantor trust rules.

App.107a

Complete the identifying information on page 1 of the form and Part II. See the instructions for Part II.

3. You are a U.S. person who received (directly or indirectly) a distribution from a foreign trust during the current tax year or a related foreign trust held an outstanding obligation issued by you (or a person related to you) that you treated as a qualified obligation (defined on page 3) during the current tax year.

Complete the identifying information on page 1 of the form and Part III. See the instructions for Part III.

4. You are a U.S. person who, during the current tax year, received either:

- a. More than \$100,000 from a nonresident alien individual or a foreign estate (including foreign persons related to that nonresident alien individual or foreign estate) that you treated as gifts or bequests; or
- b. More than \$13,258 from foreign corporations or foreign partnerships (including foreign persons related to such foreign corporations or foreign partnerships) that you treated as gifts.

Complete the identifying information on page 1 of the form and Part IV. See the instructions for Part IV.

Note. You may also be required to file Form TD F 90-22.1, Report of Foreign Bank and Financial Accounts.

Definitions

[. . .]

Qualified Obligation

A qualified obligation, for purposes of this form, is any obligation only if:

1. The obligation is reduced to writing by an express written agreement;
2. The term of the obligation does not exceed 5 years (including options to renew and rollovers) and it is repaid within the 5-year term;
3. All payments on the obligation are denominated in U.S. dollars;
4. The yield to maturity of the obligation is not less than 100% of the applicable federal rate under section 1274(d) for the day on which the obligation is issued and not greater than 130% of the applicable federal rate;
5. The U.S. person agrees to extend the period for assessment of any income or transfer tax attributable to the transfer and any consequential income tax changes for each year that the obligation is outstanding, to a date not earlier than 3 years after the maturity date of the obligation, unless the maturity date of the obligation does not extend beyond the end of the U.S. person's tax year and is paid within such period (this is done on Part I, Schedule A, and Part 111, as applicable); and
6. The U.S. person reports the status of the obligation, including principal and interest payments, on Part I, Schedule C, and Part III, as applicable, for each year that the obligation is outstanding.

[. . .]

Related Person

A related person generally includes any person who is related to you for purposes of section 267 and 707(b). This includes, but is not limited to:

- A member of your family—your brothers and sisters, half-brothers and half-sisters, spouse, ancestors (parents, grandparents, etc.), lineal descendants (children, grandchildren, etc.), and the spouses of any of these persons.
- A corporation in which you, directly or indirectly, own more than 50% in value of the outstanding stock.

See section 643(i)(2)(B) and the regulations under sections 267 and 707(b).

Person related to a foreign trust.

A person is related to a foreign trust if such person, without regard to the transfer at issue, is a grantor of the trust, a beneficiary of the trust, or is related to any grantor or beneficiary of the trust. See the definition of related person on page 3.

Reportable Event

A reportable event includes:

1. The creation of a foreign trust by a U.S. person.
2. The transfer of any money or property, directly or indirectly, to a foreign trust by a U.S. person, including a transfer by reason of death. This includes transfers that are deemed to have occurred under sections 679(a)(4) and (5).

3. The death of a citizen or resident of the United States if:

- The decedent was treated as the owner of any portion of a foreign trust under the grantor trust rules or
- Any portion of a foreign trust was included in the gross estate of the decedent.

Responsible Party

Responsible party means:

- The grantor in the case of the creation of an inter vivos trust,
- The transferor, in the case of a reportable event (defined above) other than a transfer by reason of death, or
- The executor of the decedent's estate in any other case (whether or not the executor is a U.S. person).