



Reporting Your Foreign Company to the IRS or Face Penalties

U.S. expats living abroad can have the choice of being self-employed and establishing their own company in their adopted country. However, the company is now a “foreign corporation” or a “[Controlled Foreign Corporation](#)” (CFC). Let’s discuss the requirements of what is required for U.S. expats with a CFC as far as U.S. tax reporting obligations.

What is a CFC?

A CFC is basically a company, or corporation, set up outside the U.S. and owned or controlled by a U.S. Person by over 50%. In many countries, there can be the equivalent of a limited liability corporation (LLC) but these entities are treated differently by the IRS than if it was a U.S. LLC. For example, in Belgium and the Netherlands, it is called a “SPRL”, or in France, “SARL”. In these countries, one must file a separate tax return with the taxing authorities unlike in the U.S., where it is treated as a pass-through on the individual tax return. Because of the U.S. practice, many U.S. expats are confused and do not treat their foreign company as a CFC. The CFC has additional tax reporting requirements to the IRS than an LLC holds.

What are the requirements for reporting to the IRS?

There are two basic requirements of reporting your CFC to the IRS as an entity. One is the [Form 5471](#) (Information Return of U.S. Persons with Respect to Certain Foreign Corporations). The additional requirement, established by the [Tax Cuts and Job Act](#) (TCJA) of 2017, is the “transition tax”, or “repatriation tax”, or better known to the IRS as Section 965. This tax is basically on the earnings held in the CFC and not reported to the U.S, or your “tax home”, as income. However, this article will explain the [Form 5471](#) on its requirements and penalties.

Who is required to file?

Any U.S. expat owning 90% of a CFC, or having a 10% interest as a shareholder, are required to file Form 5471. The failure to file the form could be very costly to the individual. Depending on your type of ownership, or control, of the CFC would indicate which additional schedules are required from the [Form 5471](#). This form has several schedules that are required depending on the filer’s relationship with the CFC.

There are different categories on the Form 5471 to describe who needs to file and which schedules. These would include:

1. Owning more than 10% of the foreign corporation
2. Controlling the foreign corporation for more than 30 days
3. A controlled foreign corporation is when U.S. persons own more than 50% of the corporation and each shareholder owns at least 10%, which means you are only a 10% owner, but the corporation is owned by a group of U.S. persons.
4. You did not need to have received any income from the corporation but fulfill one of the other categories
5. It does not matter whether you live abroad or in the U.S.
6. Foreign accounts owned the by the corporation and you have signature authority of the accounts would trigger for you to file the [FBAR](#) (Report of Foreign Bank and Financial Account) for each account. In addition, you may also be required to file a [Form 8938](#)



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(Statement of Specified Foreign Financial Assets) regarding the specific accounts depending on the totals and your filing status.

What is the Form 5471?

Form 5471 is filed as an information form for U.S. persons with a relationship to CFC along with their Form 1040 and subsequent schedules. The form is used to describe ownership and business operations of a foreign corporation with the U.S. person. The Form 5471 reports the operations of the foreign business, for example its balance sheet and income statement. An important thought to keep in mind is that it does not mean that the individual may be required to pay any additional tax on the income. Taxation will depend on whether the corporation is a CFC and if the income is subpart F income, and whether any distributions, salary, or income were made to the U.S. person owner. However, the TCJA changed some of that by taxing on the earnings retained in the company, which a CFC owner would be liable.

Failure to file and penalties

The failure to file the Form 5471 with the IRS can be very costly and possibly criminal. The maximum penalty could be \$50,000 for the failure to file each year. If the IRS sends a letter to request the filing, the initial penalty could be \$10,000. However, failure to act will increase the penalty to up to the \$50,000 maximum. If the IRS sends such a letter, it is highly recommended to seek legal counsel to handle the situation and file an IRS Penalty Abatement to fight them on the penalty.

Criminal penalties can also be applied to the U.S. person for failure to file this form. Even if the U.S. person instructs someone else to file the form and does not, the U.S. person is responsible and will face the penalties.

It is essential to keep in mind that penalties can be imposed for undisclosed foreign financial asset understatements as well as non-disclosure. However, if a U.S. person can demonstrate that the failure to comply was not willful and they are taking a reasonable step toward compliance, the IRS may reduce or eliminate the penalties.

What to do?

The IRS has the [Streamlined Filing Compliance Procedures](#) which allows taxpayers to amend their tax returns for the past three years and request an amnesty on penalties. However, if the IRS does send a letter, the renewed [Offshore Voluntary Disclosure Program](#) can be utilized to assist in reducing or eliminating the penalties with the assistance of a legal counsel.

Additional questions or assistance can be directed to [Mir Taxes](#) at info@mirtaxes.com. More details on Form 5471 can be found on the [IRS website](#).

See glossary and associated links below.



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Glossary & Links

- Controlled Foreign Corporation (CFC) - <https://www.investopedia.com/terms/c/cfc.asp>
- Form 5471 Information Return of U.S. Persons with Respect to Certain Foreign Corporations - <https://www.irs.gov/forms-pubs/about-form-5471>
- Tax Cuts and Job Act (TCJA) of 2017 - <https://www.irs.gov/tax-reform>
- Form 5471 - <https://www.irs.gov/pub/irs-pdf/i5471.pdf>
- FBAR Report of Foreign Bank and Financial Account - <https://bsaefiling.fincen.treas.gov/NoRegFBARFiler.html>
- Form 8938 - Statement of Specified Foreign Financial Assets - <https://www.irs.gov/forms-pubs/about-form-8938>
- Streamlined Filing Compliance Procedures - <https://www.irs.gov/individuals/international-taxpayers/streamlined-filing-compliance-procedures>
- Offshore Voluntary Disclosure Program - <https://www.irs.gov/compliance/criminal-investigation/how-to-make-an-offshore-voluntary-disclosure>
- Mir Taxes – www.mirtaxes.com Email at info@mirtaxes.com
- IRS website - <http://www.irs.gov/>

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