DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[REG–124850–08]

RIN 1545–BI04

Transactions With Foreign Trusts and Information Reporting on Transactions With Foreign Trusts and Large Foreign Gifts

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking and notice of public hearing.

SUMMARY: This document contains proposed regulations that provide guidance regarding information reporting of transactions with foreign trusts and receipt of large foreign gifts and regarding loans from, and uses of property of, foreign trusts. This document also contains proposed amendments to the regulations relating to foreign trusts having one or more United States beneficiaries. The proposed regulations affect United States persons who engage in transactions with, or are treated as the owners of, foreign trusts, and United States persons who receive large gifts or bequests from foreign persons. This document also provides notice of a public hearing on the proposed regulations.

DATES:

Comments: Electronic or written public comments must be received by July 8, 2024.

Public Hearing: A public hearing on these proposed regulations has been scheduled for August 21, 2024, at 10 a.m. ET. Requests to speak and outlines of topics to be discussed at the public hearing must be received by July 8, 2024. If no outlines are received by July 8, 2024, the public hearing will be cancelled. Requests to attend the public hearing must be received by 5:00 p.m. ET on August 19, 2024.

ADDRESSES: Commenters are strongly encouraged to submit public comments electronically. Submit electronic submissions via the Federal eRulemaking Portal at *www.regulations.gov* (indicate IRS and REG–124850–08) by following the online instructions for submitting comments. Requests for a public hearing must be submitted as prescribed in the ''Comments and Requests for a Public Hearing'' section. Once submitted to the Federal eRulemaking Portal, comments cannot be edited or withdrawn. The Department of the Treasury (Treasury Department) and the IRS will publish for public availability any comments submitted to the IRS's public docket.

Send paper submissions to: CC:PA:01:PR (REG–124850–08), Room 5203, Internal Revenue Service, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044.

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, Lara A. Banjanin at (202) 317–6933 or S. Eva Wolf at (202) 317–3893 (not toll-free numbers); concerning submissions of comments, the hearing, or to be placed on the building access list to attend the hearing, Vivian Hayes at (202) 317–6901 (not a toll-free number) or by email at *publichearings@irs.gov* (preferred).

SUPPLEMENTARY INFORMATION:

Background

I. In General

This document contains proposed amendments to 26 CFR part 1 under sections 643(i), 679, 6039F, 6048, and 6677 of the Internal Revenue Code (Code) (the *proposed regulations*). Section 6048, as significantly modified by the Small Business Job Protection Act of 1996 (*1996 Act*), Public Law 104–188 (110 Stat. 1755), and further amended by the Taxpayer Relief Act of 1997 (*1997 Act*), Public Law 105–34 (111 Stat. 788), and the Hiring Incentives to Restore Employment Act (*HIRE Act*), Public Law 111–147 (124 Stat. 71), generally requires U.S. persons to report transactions that involve foreign trusts. Section 6677, as significantly modified by the 1996 Act and further amended by the HIRE Act, imposes penalties on U.S. persons for failing to comply with section 6048. Section 6039F, which was added to the Code by the 1996 Act, and modified by the Tax Cuts and Jobs Act, Public Law 115–97 (131 Stat. 2054), requires U.S. persons to report the receipt of large gifts or bequests from foreign persons, and in the event of a failure to provide this information, section 6039F(c) imposes penalties and allows the IRS to recharacterize the purported gift or bequest as income. Section 643(i), which was added to the Code by the 1996 Act and amended by the HIRE Act, and section 679, as amended by the 1996 Act and the HIRE Act, provide additional rules intended to prevent taxpayers from avoiding U.S. income tax consequences through the use of foreign trusts.

On June 2, 1997, the Treasury Department and the IRS issued Notice 97–34, 1997–1 CB 422, which provides guidance on sections 643(i), 679, 6039F, 6048 and 6677 (the *foreign trust and gift provisions*) as enacted or modified by the 1996 Act. On August 7, 2000, the Treasury Department and the IRS published a notice of proposed rulemaking and a notice of public hearing (REG–209038–89) under section 679 in the **Federal Register** (65 FR 48185). On July 20, 2001, the Treasury Department and the IRS published final regulations under section 679. TD 8955 (66 FR 37866).

U.S. persons currently provide information required by the foreign trust and gift provisions on Form 3520, *Annual Return to Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts,* and Form 3520–A, *Annual Information Return of Foreign Trust With a U.S. Owner (Under section 6048(b)).* In 2015, section 2006(b)(9) and (10) of the Surface Transportation and Veterans Health Care Choice Improvement Act of 2015 (*Surface Transportation Act*), Public Law 114–41 (129 Stat. 443), modified the due dates for Forms 3520 and 3520–A for taxable years beginning after December 31, 2015. On March 16, 2020, the Treasury Department and the IRS issued Revenue Procedure 2020–17, 2020–12 IRB 539, which exempts from section 6048 information reporting requirements certain U.S. individuals' transactions with, and ownership of, certain tax-favored foreign trusts that are established and operated exclusively or almost exclusively to provide pension or retirement benefits, or to provide medical, disability, or educational benefits.

II. Purpose of Foreign Trust and Gift Provisions

During the mid- to late-1990s, abusive tax schemes, including offshore schemes involving foreign trusts, reemerged in the United States after last peaking in the 1980s. GAO, *Efforts to Identify and Combat Abusive Tax Schemes Have Increased, But Challenges Remain,* GAO–02–733 (Washington, DC: May 22, 2002). In these schemes, foreign trusts were used to transfer large amounts of assets offshore, where it was much more difficult for the IRS to identify whether U.S. persons owned an interest in such trusts, and whether such persons were reporting and paying the required taxes on their income from such trusts. Many of the foreign trusts were established in tax haven jurisdictions with bank secrecy laws. Before the 1996 Act amended sections 6048 and 6677, there was no requirement for U.S. persons to report distributions from foreign trusts, and the penalty for failing to report transfers to a foreign trust, or an annual foreign trust information return (on

Form 3520–A), was limited to five percent of the transfer or trust corpus, as applicable, not to exceed $1,000. Given that, it was difficult for the IRS to obtain information about income earned by U.S.-owned foreign trusts and distributions to U.S. beneficiaries of foreign trusts, and sections 6048 and 6677 were generally ineffective at ensuring that U.S. persons provided this information. The result was ''rampant tax avoidance.'' 141 Cong. Rec. S13859 (daily ed. Sept. 19, 1995) (remarks of Senator Moynihan).

The foreign trust and gift provisions in the 1996 Act were designed to accommodate changes in the use of foreign trusts and to limit avoidance and evasion of U.S. tax. The most significant changes were made to sections 6048 and 6677 to enhance the IRS's ability to obtain the information necessary to enforce the tax laws that apply to U.S. persons' transactions with, and ownership of, foreign trusts. Other changes included enactment of new section 643(i) and amendments to section 679, each of which is designed to prevent tax avoidance through the use of foreign trusts. In addition, the legislation included new section 6039F, which enables the IRS to obtain information about large foreign gifts or bequests received by U.S. persons.

III. Overview

A. Section 643(i)

Section 643(i), as originally enacted in 1996, generally provides that, if a foreign trust makes a loan of cash or marketable securities directly or indirectly to any grantor or beneficiary of the foreign trust who is a U.S. person (other than an entity that is exempt from tax under Chapter 1 of the Code), or to a U.S. person related (under sections 267 and 707(b)) to such a grantor or beneficiary, the amount of the loan is treated as a distribution by the trust to the grantor or beneficiary. Section 643(i) also authorizes the Secretary to issue regulations providing exceptions, under which a loan by a foreign trust would not be treated as a distribution to the grantor or beneficiary of the trust. The 1996 Act's legislative history explains that these regulations are expected to provide an exception under section 643(i) for loans with arm's-length terms, and in applying this exception, the regulations should consider whether there is a reasonable expectation that the grantor, beneficiary, or related person would repay the loan. H.R. Conf. Rep. No. 737, 104th Cong., 2d Sess., at 334 (1996).

Section V.A of Notice 97–34 provides that a loan of cash or marketable securities by a foreign trust to a U.S. grantor or U.S. beneficiary of the trust, or to a U.S. person who is related to a U.S. grantor or U.S. beneficiary of the trust, is treated as a distribution under section 643(i) unless the loan is made in consideration for a ''qualified obligation'' that satisfies certain specified requirements. Notice 97–34 states that what constitutes a qualified obligation will be provided in regulations. (Section III.C of Notice 97–34 provides similar qualified obligation rules for transfers to foreign trusts. See section III.B of this Background.)

In 2010, Congress expanded the scope of section 643(i) in response to concerns that U.S. persons were avoiding the application of section 643(i) by using trust property other than cash or marketable securities without compensating the foreign trust for the use of the property. Section 533 of the HIRE Act amended section 643(i) to provide that any uncompensated use of trust property by a U.S. grantor or U.S. beneficiary of the foreign trust, or any U.S. person related to such U.S. grantor or U.S. beneficiary, generally is treated as a distribution of the fair market value of the use of such property to the U.S. grantor or U.S. beneficiary. This rule does not apply if the foreign trust is paid fair market value for the use of the trust property within a reasonable timeframe.

Loans and use of trust property are reported on Part III of Form 3520. Taxpayers provide this information based on guidance in section V.A of Notice 97–34, as well as the instructions for Form 3520. This information allows the IRS to determine whether the loan or use of trust property should be treated as a distribution pursuant to section 643(i).

B. Section 679

1. 1976 Act

Section 679 was enacted by the Tax Reform Act of 1976 (*1976 Act*), Public Law 94–455 (90 Stat. 1520). Section 679 treats a U.S. person who directly or indirectly transfers property to a foreign trust as the owner of the portion of the foreign trust attributable to the transferred property to the extent that, under the terms of the trust, the income or corpus of the trust may be paid to or accumulated for the benefit of a U.S. person during the taxable year, including if the trust were to be terminated during the taxable year.

2. 1996 Act Amendments

Section 1903 of the 1996 Act made several important changes to section 679. For example, Congress was concerned that taxpayers were attempting to avoid the application of section 679(a)(1) by transferring property to a foreign trust in exchange for obligations from the foreign trust that might not be repaid and arguing that such obligations satisfied the fair market value exception in section 679(a)(2). H.R. Conf. Rep. No. 737, 104th Cong., 2d Sess., at 334–35 (1996). The fair market value exception provides that section 679(a)(1) does not apply to any transfer of property to a foreign trust in exchange for consideration of at least the fair market value of the transferred property. Accordingly, Congress added new section 679(a)(3), which generally provides that obligations issued by the foreign trust, by any grantor or beneficiary of the trust, or by any person related to any grantor or beneficiary, are not taken into account in applying the fair market value exception except as provided in regulations.

Section III.C of Notice 97–34 implemented the fair market value exception of section 679(a)(2)(B) and (a)(3) by providing that, if a U.S. person transfers money or other property to a related foreign trust in exchange for an obligation issued by the trust or by a person related to the trust, the obligation is taken into account for purposes of determining whether the U.S. person received fair market value from the foreign trust only if the obligation is a *qualified obligation* that satisfies certain specified requirements. (Section V.A of Notice 97–34 provides similar qualified obligation rules that apply with respect to loans from foreign trusts under section 643(i). See section III.A of this Background.) In 2001, the Treasury Department and the IRS issued final regulations under section 679 in TD 8955 (66 FR 37886) that included the section 679 qualified obligation rules described in Notice 97–34. See § 1.679–4(d).

A U.S. person's transfers to a foreign trust are reported on Part I of Form 3520, together with information about any qualified obligations received from the trust. Taxpayers provide this information based on the final regulations under section 679, as well as the instructions for Form 3520. This information allows the IRS to determine whether the U.S. person should be treated as an owner of the foreign trust under section 679.

3. HIRE Act Amendments

In 2010, the HIRE Act made five amendments to section 679, three of which are consistent with the final regulations under section 679, and two of which set forth new rules not reflected in the final regulations.

First, section 531(a) of the HIRE Act added new language to section 679(c)(1) to clarify that an amount is treated as accumulated for the benefit of a U.S. person even if the U.S. person's interest in the foreign trust is contingent on a future event. This statutory amendment is consistent with § 1.679–2(a)(2)(i), which states that the determination as to whether income or corpus may be paid to or accumulated for the benefit of a U.S. person is made without regard to whether the income or corpus actually is distributed to the U.S. person during the year, or whether the U.S. person's interest in the income or corpus of the trust is contingent on a future event.

Second, section 531(b) of the HIRE Act added a new paragraph (4) to section 679(c) to clarify that, if any person has the discretion to make a distribution from the foreign trust to or for the benefit of any person, the trust shall be treated as having a U.S. beneficiary unless the terms of the trust specifically identify the class of persons to whom such distributions may be made, and none of those persons are U.S. persons during the taxable year. This statutory amendment is consistent with § 1.679–2(a)(1), which provides that a foreign trust is treated as having a U.S. beneficiary unless no part of the trust's income or corpus may be paid or accumulated to or for the benefit of a U.S. person, and if the trust is terminated at any time during the taxable year, no part of the trust's income or corpus could be paid to or for the benefit of a U.S. person.

Third, section 531(c) of the HIRE Act added a new paragraph (5) to section 679(c) to clarify that, if any U.S. person who directly or indirectly transfers property to a foreign trust is directly or indirectly involved in any agreement or understanding that may result in the income or corpus of the trust being paid to or accumulated for the benefit of a U.S. person, then such an agreement or understanding shall be treated as constituting a term of the trust. This statutory amendment is consistent with § 1.679–2(a)(4)(i), which, assuming that a transferor of property to a trust is generally directly or indirectly involved with any agreements regarding the accumulation or disposition of the income and corpus of the trust, allows the IRS to treat a foreign trust as having a U.S. beneficiary by looking beyond the language of the trust instrument to all written and oral agreements and understandings related to the trust, memoranda or letters of wishes, all records that relate to the actual distribution of income and corpus, and all other documents relating to the trust, whether or not of any purported legal effect.

Fourth, section 532 of the HIRE Act added a new paragraph (d) to section 679, which provides a presumption that a foreign trust has a U.S. beneficiary in certain circumstances. If a U.S. person directly or indirectly transfers property to a foreign trust (other than certain compensatory and charitable trusts), the IRS may treat the trust as having a U.S. beneficiary for purposes of applying section 679 to the transfer unless the U.S. person submits such information to the IRS as the IRS may require and demonstrates to the satisfaction of the IRS that the trust satisfies the requirements of section 679(c)(1).

Finally, section 533(c) of the HIRE Act added a new paragraph (6) to section 679(c), which generally treats a loan of cash or marketable securities to, or the use of any other trust property by, any U.S. person, whether or not a beneficiary under the terms of the trust, as paid to or accumulated for the benefit of a U.S. person. Section 679(c)(6) does not apply to the extent that the U.S. person repays the loan at a market rate of interest or pays the fair market value of the use of the property within a reasonable period of time. The effect of section 679(c)(6) is that, if a foreign trust is not already treated as having a U.S. beneficiary, a loan by the trust of cash or marketable securities to a U.S. person or the uncompensated use of trust property by a U.S. person may cause the foreign trust to be treated as having a U.S. beneficiary, with the result that a U.S. person who transferred property to the trust may be treated as the owner of the trust under section 679(a).

Final regulations were issued under section 679 in 2001, and although instructions for Form 3520 and Form 3520–A have been updated to take into account the HIRE Act amendments to section 679, regulations implementing these amendments have not been issued.

C. Section 6039F

Section 1905 of the 1996 Act created new reporting requirements under section 6039F for U.S. persons (other than certain exempt organizations) that receive large gifts (including bequests) from foreign persons. The new information reporting provisions require U.S. persons to provide information concerning the receipt of large amounts that they treat as foreign gifts or bequests, giving the IRS an opportunity to review the characterization of these payments and determine whether they are properly treated as gifts.

Section 6039F(b) generally defines the term *foreign gift* as any amount received from a person other than a U.S. person that the recipient treats as a gift or bequest. However, a foreign gift does not include a qualified transfer (within the meaning of section 2503(e)(2)) or a distribution from a foreign trust. A distribution from a foreign trust must be reported as a distribution under section 6048(c) (discussed in section III.E of this Background) rather than as a gift under section 6039F.

Section 6039F(c) provides that, if a U.S. person fails, without reasonable cause, to report a foreign gift as required by section 6039F, then (i) the tax consequences of the receipt of the gift will be determined by the Secretary and (ii) the U.S. person will be subject to a penalty equal to 5 percent of the amount of the gift for each month the failure to report the foreign gift continues, with the total penalty not to exceed 25 percent of the value of the gift. Under sections 6039F(a) and (d), reporting is required if the value of the aggregate foreign gifts received by a U.S. person during any taxable year exceeds $10,000, as modified by cost-of-living adjustments. Under section VI.B.1 of Notice 97–34, however, a U.S. person is required to report gifts from a foreign individual or foreign estate only if the aggregate amount of gifts from that foreign individual or foreign estate exceeds $100,000 during the U.S. person's taxable year. Section VI.B.3 of Notice 97–34 provides guidance on when a U.S. person must aggregate foreign gifts received from foreign persons that the U.S. person knows or has reason to know are related to each other. Once the $100,000 threshold has been met, the U.S. person must identify each foreign gift in excess of $5,000 but is not required to identify the transferor.

A U.S. person who receives foreign gifts that exceed the threshold amounts must report the foreign gifts on Part IV of Form 3520. Taxpayers provide this information based on guidance in section VI of Notice 97–34, as well as the instructions for Form 3520.

D. Section 6048

Section 6048(a) through (c) contains three distinct reporting obligations with respect to a U.S. person's transactions with, and ownership of, foreign trusts.

1. Section 6048(a)

Section 6048(a) generally requires a responsible party to file information returns upon the occurrence of certain reportable events. A responsible party is the U.S. grantor of an inter vivos foreign trust, the U.S. transferor, or the executor of a U.S. decedent's estate. A reportable event is (a) the creation of any foreign trust by a U.S. person; (b) the direct or

indirect transfer of any money or property to a foreign trust by a U.S. person, including a transfer by reason of death; or (c) the death of a U.S. citizen or resident if the decedent was treated as the owner of any portion of a foreign trust or if any portion of a foreign trust was included in the gross estate of the decedent. Section 6048(a)(3)(B)(i) provides an exception for transfers for fair market value (the fair market value exception), and section 6048(a)(3)(B)(ii) provides an exception for transfers to certain deferred compensation and charitable trusts. (These exceptions correspond to the current substantive exemptions to the scope of section 679. See section 679(a)(1) and (2)(B).)

A reportable event is reported on Part I of Form 3520. Section III of Notice 97–34 and the instructions for Form 3520 provide information to taxpayers regarding this reporting. Section 6048(a) enables the IRS to obtain the information necessary to enforce sections 679 (discussed in section III.B of this Background) and 684 (added by section 1131(b) of the 1997 Act to provide for recognition of gain on certain transfers to foreign trusts).

2. Section 6048(b)

Section 6048(b)(1) generally requires a U.S. person who is treated as the owner of any portion of a foreign trust under the grantor trust rules (*U.S. owner*) to ensure that the trust (i) files an annual information return to provide a full accounting of all the trust activities for the trust's taxable year and (ii) furnishes an annual information statement to each U.S. owner and to any other U.S. person who receives (directly or indirectly) any distribution from the trust during the year (*U.S. beneficiary*). In addition, the U.S. owner must submit such information as the IRS may prescribe with respect to the foreign trust.

Section 6048(b)(2) provides that, unless a foreign trust with a U.S. owner appoints a U.S. agent, the Secretary may determine the amounts required to be taken into account with respect to such trust by the U.S. owner under the grantor trust rules. The U.S. agent will be required to act as the foreign trust's limited agent solely for purposes of applying sections 7602, 7603, and 7604 with respect to any request or summons by the Secretary in connection with the tax treatment of any items related to the trust. Certain rules (similar to the rules of section 6038A(e)(2) and (4)) relating to the enforcement of requests for certain records with respect to foreign-owned corporations will apply. Information about the U.S. agent must be reported on both the U.S. owner's Form 3520 and the foreign trust's Form 3520–A.

The foreign trust's annual information return is Form 3520–A, and any additional information required to be submitted by the U.S. owner is provided on Part II of Form 3520. The information statements that the foreign trust must furnish to each U.S. owner and to each U.S. beneficiary who receives a distribution are the Foreign Grantor Trust Owner Statement and the Foreign Grantor Trust Beneficiary Statement, as applicable. Taxpayers provide this information based on guidance in section IV of Notice 97–34, as well as the instructions for Form 3520 and Form 3520–A. If the foreign trust fails to file Form 3520–A, section 6677 imposes a penalty on the U.S. owner. In order to avoid penalties under section 6677, the U.S. owner must complete a substitute Form 3520–A for the foreign trust and attach it to the U.S. owner's Form 3520. See instructions for Part II of Form 3520.

3. Section 6048(c)

Section 6048(c)(1) provides that any U.S. person who directly or indirectly receives any distribution from a foreign trust is required to file an information return to report the name of the trust, the aggregate amount of the distributions received, and any other information that the Secretary may prescribe. Section 6048(c)(2) generally provides that, if adequate records are not provided to the Secretary to determine the proper treatment of a distribution from a foreign trust, the distribution is treated as an accumulation distribution. However, to the extent provided in regulations, this rule does not apply if the foreign trust authorizes a U.S. person to act as its limited agent under rules similar to the rules of section 6048(b)(2)(B) (discussed in section III.D.2 of this Background). Section 6048(d)(5) (discussed in section III.D.4 of this Background) provides that a U.S. person's treatment of a distribution from a foreign trust must be consistent with the trust's treatment of such item or the Secretary must be notified of the inconsistency.

Distributions from a foreign trust are reported on Part III of Form 3520. Taxpayers provide this information based on guidance in section V of Notice 97–34, as well as the instructions for Form 3520. Section 6048(c) enables the IRS to obtain the information it needs to enforce the rules relating to the taxation of accumulation distributions (sections 665 through 669), as well as sections 672(f), 643(h), and 643(i). Section 6048(c) requires any U.S. person, including a U.S. owner and U.S. beneficiary of a foreign trust, who receives a distribution from a foreign trust to report information about the distribution. See *Wilson* v. *United States,* 6 F.4th 432 (2d Cir. 2021), rev'g, No. 19–CV–5037 (BMC), 2019 WL 6118013 (E.D.N.Y. Nov. 18, 2019) (holding that when an individual is both the sole owner and beneficiary of a foreign trust and fails to timely report distributions received from the trust, the IRS may impose a penalty under section 6677 equal to 35 percent of the gross reportable amount).

4. Section 6048(d)

Section 6048(d)(1) provides that, for purposes of section 6048, in determining whether a U.S. person makes a transfer to, or receives a distribution from, a foreign trust, the fact that a portion of the trust is treated as owned by another person under the grantor trust rules is disregarded.

Section 6048(d)(2) provides that, to the extent provided in regulations, a domestic trust will be treated as a foreign trust for purposes of sections 6048 and 6677 if the trust has substantial activities, or holds substantial property, outside the United States. The legislative history includes the statement ''that in exercising its regulatory authority to treat a U.S. trust as a foreign trust for purposes of information reporting purposes, the Secretary of the Treasury will take into account the information that such a trust reported under the domestic trust reporting rules.'' H.R. Conf. Rep. 737, 104th Cong., 2d Sess. at 338 (1996). Section VIII.C of Notice 97–34 states that the Treasury Department and the IRS are studying the appropriate scope of section 6048(d)(2) and that, until further guidance is issued, a domestic trust is not treated as a foreign trust pursuant to section 6048(d)(2).

Section 6048(d)(3) provides that any notice or return required under section 6048 is to be made at such time and in such manner as the Secretary prescribes.

Section 6048(d)(4) authorizes the IRS to suspend or modify any requirement of section 6048 if the IRS determines that the United States has no significant tax interest in obtaining the required information. The Treasury Department and the IRS previously have issued guidance providing that information reporting under section 6048(c) is not required with respect to distributions from certain foreign compensatory trusts, provided that the U.S. person who receives the distribution reports the distribution as compensation income on an applicable Federal income tax return, and that information reporting under section 6048(a) through (c) is not required with respect to certain

Canadian retirement plans. See Section V of Notice 97–34; Rev. Proc. 2014–55, 2014–44 I.R.B. 753. In addition, on March 16, 2020, the Treasury Department and the IRS issued Revenue Procedure 2020–17, which exempts from section 6048 information reporting requirements certain U.S. individuals' transactions with, and ownership of, certain tax-favored foreign trusts that are established and operated exclusively or almost exclusively to provide pension or retirement benefits or to provide medical, disability, or educational benefits.

Section 6048(d)(5) (added by section 1027(b) of the 1997 Act) provides that a U.S. person who either is treated as an owner of any portion of a foreign trust or receives (directly or indirectly) any distribution from a foreign trust must treat any portion owned or any item distributed in a manner that is consistent with the trust's treatment of such ownership or item; otherwise, the U.S. person must notify the Secretary of the inconsistency. A similar rule in section 6034A(c) (added by section 1027(a) of the 1997 Act) generally provides that a beneficiary of an estate or trust is required to file a return in a manner that is consistent with the information received from the estate or trust, unless the beneficiary files with the return a notification of inconsistent treatment identifying the inconsistency. The Treasury Department and the IRS are of the view that the rules in sections 6034A(c) and 6048(d)(5) are to be interpreted as comparable to the consistency rules that already apply to S corporation shareholders and partners in partnerships. H.R. Conf. Rep. 220, 105th Cong., 1st Sess. at 551 (1997). Taxpayers may use Form 8082, *Notice of Inconsistent Treatment or Administrative Adjustment Request (AAR),* to report an inconsistency.

Although regulations were issued under section 6048, these regulations now are obsolete because they were issued under an earlier version of section 6048. These regulations were removed as a result of regulations issued pursuant to Executive Order 13789. See TD 9849 (84 FR 9231).

E. Section 6677

Under section 6677, as amended by section 1901(b) of the 1996 Act, a U.S. person who fails to file a required information return under section 6048(a) or (c) is subject to an initial penalty of 35 percent of the gross reportable amount (generally, the value of the property transferred or received). If an information return required under section 6048(b) is not filed, the U.S. person who is treated as the owner of the foreign trust is subject to an initial penalty of five percent of the gross reportable amount (the trust corpus at the end of the year). See also *Wilson* v. *United States,* 6 F.4th 432 (2d Cir. 2021) (holding that *gross reportable amount* has multiple meanings under section 6677(c) that differ depending on the part of section 6048 that is violated), rev'g, No. 19–CV–5037 (BMC), 2019 WL 6118013 (E.D.N.Y. 2019). In all cases, if the failure to file an information return continues for more than 90 days after the day on which the IRS mails notification of the failure, an additional $10,000 penalty is imposed for each 30-day period (or fraction thereof) during which the failure continues. The total amount of the penalties with respect to any failure cannot exceed the gross reportable amount with respect to that failure. If the gross reportable amount is partially reported, then the penalties are applied based on the amount that is unreported. Section VII of Notice 97–34.

Section 535 of the HIRE Act strengthened the penalty structure by further amending section 6677 to allow the IRS to impose penalties when it does not have enough information to determine the gross reportable amount. Section 6677, as amended, provides that the initial penalty is the greater of $10,000 or 35 percent (five percent in the case of a failure to comply with section 6048(b)) of the gross reportable amount. Thus, the IRS may impose an initial penalty of $10,000 on a U.S. person who fails to report information without having any information about the foreign trust's gross reportable amount. The amendment did not change the rules for the additional penalties of $10,000 for each 30-day period (or fraction thereof) during which the failure to report continues.

Section 6677, as amended, also provides that, if the IRS, after having assessed penalties, obtains sufficient information to determine the gross reportable amount, any subsequent penalty imposed will be reduced as necessary to ensure that the aggregate amount of the penalties does not exceed the gross reportable amount. To the extent that the amount already paid exceeds the gross reportable amount, the IRS will refund the excess to the U.S. person pursuant to section 6402.

Section 6677(d) provides that no penalty will be imposed on any failure that is shown to be due to reasonable cause and not due to willful neglect. It further provides that the fact that a foreign jurisdiction would impose a civil or criminal penalty on the U.S. person (or any other person) for disclosing the required information is not reasonable cause.

Section 6677(e) provides that subchapter B of chapter 63 (relating to deficiency procedures for income, estate, gift, and certain excise taxes) does not apply in respect of the assessment or collection of any penalty imposed under section 6677.

F. Section 643(a)(7)

Section 643(a)(7), which was added to the Code by section 1906(b) of the 1996 Act, provides that the Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of part I of subchapter J of chapter 1 of the Code (sections 641 through 685), including regulations to prevent avoidance of such purposes.

G. Information Return Due Dates

Section 2006(b) of the Surface Transportation Act provides that, in the case of returns for taxable years beginning after December 31, 2015, the Secretary, or the Secretary's designee, shall modify the appropriate regulations addressing certain due dates. Section 2006(b)(9) provides that the due date of Form 3520–A shall be the 15th day of the third month after the close of the trust's taxable year, and the maximum extension shall be a 6-month period beginning on such day. Section 2006(b)(10) states that the due date of Form 3520 for calendar year filers shall be April 15 with a maximum extension for a 6-month period ending on October 15.

Explanation of Provisions

I. Section 643(i)—Loans to and Uses of Foreign Trust Property by U.S. Persons

These proposed regulations provide rules relating to loans from foreign trusts to U.S. persons and uses of foreign trust property by U.S. persons. They generally incorporate the section 643(i) guidance that was provided in Notice 97–34 (discussed in section III.A of the Background), with certain modifications to provide procedural rules, such as how to determine a loan's yield to maturity and how to extend the period of assessment for any income tax associated with the loan, and anti-abuse rules, such as requiring payments and information reporting to be timely. In addition, the proposed regulations provide guidance implementing the HIRE Act amendments to section 643(i).

A. Application of Section 643(i) to Loans by or Uses of Property of a Foreign Trust

Proposed § 1.643(i)–1 provides rules for determining when a loan of cash or marketable securities from a foreign nongrantor trust, made to a U.S. person who is either a grantor or beneficiary of

the foreign trust or is related to a U.S. person who is a grantor or beneficiary of the foreign trust, will be treated as a distribution under subchapter J of chapter 1 of the Code (a *section 643(i) distribution*) to the U.S. grantor or beneficiary of the foreign trust. These rules also apply to determine whether a distribution is made when any such U.S. persons use the property of the foreign trust.

These rules apply solely for purposes of subparts B, C, and D (sections 651–652, 661–664, and 665–668) of part I of subchapter J of chapter 1 of the Code, and thus section 643(i) does not apply to a foreign trust to the extent that it is a grantor trust described in subpart E (sections 671 through 679) of part I of subchapter J. Although section 643(i) applies to loans of cash or marketable securities from a foreign trust to a U.S. grantor or a U.S. person related to a U.S. grantor, these provisions of section 643(i) predate the HIRE Act, which enacted section 679(c)(6). Under section 679, a U.S. person who transfers property to a foreign trust is treated as the owner of the portion of the trust attributable to the property transferred to the trust if there is a U.S. beneficiary of any portion of the trust, unless an exception applies. Section 679(c)(6) provides that any direct or indirect loan of cash or marketable securities to a U.S. person, or direct or indirect use of any other trust property by a U.S. person, whether or not the U.S. person is a beneficiary under the terms of the trust, will be treated as paid to or accumulated for the benefit of a U.S. person, unless an exception applies (see proposed § 1.679–2(a)(5)(iii)). That is, the U.S. person will be treated as a beneficiary of the foreign trust for purposes of section 679. In most circumstances, this causes the foreign trust to be a grantor trust under section 679, removing it from the purview of section 643(i). Section 643(i), therefore, will rarely apply to a U.S. grantor or a U.S. person related to a U.S. grantor. It might apply, however, if the U.S. grantor created but did not make a transfer to the foreign trust.

Proposed § 1.643(i)–1(b)(1) provides that, unless an exception applies, any loan of cash or marketable securities made from a foreign trust (whether from trust corpus or income) directly or indirectly to a U.S. grantor or beneficiary of the trust or to any U.S. person related to a U.S. grantor or beneficiary of the trust is treated as a section 643(i) distribution to such U.S. grantor or beneficiary as of the date on which the loan is made. For these purposes, a loan to a grantor trust or to a disregarded entity is treated as a loan to the owner of the grantor trust or of the disregarded entity. For example, a loan to a single member LLC treated as a disregarded entity is treated as a loan to the owner of the LLC.

Proposed § 1.643(i)–1(b)(2)(i) describes indirect loans for purposes of section 643(i) to include loans made through an intermediary, agent, or nominee. Proposed § 1.643(i)–1(b)(2)(i) also provides three examples of indirect loans: (1) a loan made by any person to a U.S. grantor or beneficiary of a foreign trust or any U.S. person related to a U.S. grantor or beneficiary if the foreign trust guarantees (within the meaning of § 1.679–3(e)(4)) the loan; (2) a loan made by any person related (within the meaning of proposed § 1.643(i)–1(d)(9)) to the foreign trust to a U.S. grantor or beneficiary of the foreign trust or to a U.S. person related to a U.S. grantor or beneficiary; and (3) a loan made by a foreign trust to a foreign person, other than to a nonresident alien individual who is a grantor or beneficiary of the trust, if the foreign person is related (within the meaning of proposed § 1.643(i)–1(d)(9)) to a U.S. grantor or beneficiary of the trust. See proposed § 1.643(i)–1(b)(2)(i)(A) through (C). However, the loans described in examples (2) and (3) above are excepted from section 643(i) treatment if the U.S. grantor or beneficiary of the foreign trust satisfies the information reporting requirements of proposed § 1.6048–4 with respect to the loan and attaches to a Federal income tax return an explanatory statement that demonstrates to the satisfaction of the IRS that the loan would have been made without regard to the U.S. grantor's or beneficiary's relationship to the foreign trust. See proposed § 1.643(i)–1(b)(2)(ii). There is no such exception for a loan made by any person that is guaranteed (within the meaning of § 1.679–3(e)(4)) by a foreign trust because a foreign trust is unlikely to guarantee such a loan absent its relationship with the U.S. grantor or beneficiary.

Proposed § 1.643(i)–1(b)(2)(iii) provides that loans from a foreign trust to a U.S. grantor or beneficiary or U.S. person related to a U.S. grantor or beneficiary through an intermediary are treated as made directly from the foreign trust to the U.S. grantor or beneficiary or U.S. person related to a U.S. grantor or beneficiary.

In order to discourage grantors and beneficiaries of a foreign trust from changing their U.S. residence in a particular year to avoid the application of section 643(i), proposed § 1.643(i)–1(b)(3) provides an anti-abuse rule. If a nonresident alien who is a grantor or beneficiary of a foreign trust receives a loan from the foreign trust and becomes a U.S. person within two years, that grantor or beneficiary will be subject to section 643(i) with respect to the outstanding amount of the loan as of the date the grantor or beneficiary acquires U.S. residence or citizenship if the loan was not a qualified obligation as of the date that it was made.

Proposed § 1.643(i)–1(c) provides that any direct or indirect use of other property of a foreign trust by a U.S. grantor or beneficiary or any U.S. person related to a U.S. grantor or beneficiary is treated as a section 643(i) distribution to the U.S. grantor or beneficiary in the taxable year in which the use occurs. Use of property of a foreign trust by a grantor trust or a disregarded entity is treated as use by the owner of the grantor trust or of the disregarded entity. For example, use of trust property by a single member LLC treated as a disregarded entity would be treated as use by the owner of the LLC.

Proposed § 1.643(i)–1(c)(2)(i) describes indirect use of trust property to include use by an agent or nominee. Indirect use of trust property also includes use by a foreign person, other than a nonresident alien individual who is a beneficiary of the foreign trust, if the foreign person is related to a U.S. grantor or beneficiary of the trust, unless the U.S. grantor or beneficiary reports the use of trust property on Part III of Form 3520, as required by proposed § 1.6048–4, and attaches to the U.S. grantor's or beneficiary's Federal income tax return an explanatory statement that demonstrates to the satisfaction of the IRS that the use of trust property would have been made without regard to the U.S. grantor's or beneficiary's relationship to the foreign trust. See proposed § 1.643(i)–1(c)(2).

B. Exceptions

Proposed § 1.643(i)–2(a) provides four exceptions to the general rule of proposed § 1.643(i)–1(b)(1):

First, the general rule will not apply to any loan of cash in exchange for a qualified obligation within the meaning of proposed § 1.643(i)–2(b)(2)(iii). The proposed regulations do not provide an exception from the general rule for loans of marketable securities as such a rule would be more difficult to apply, and it is less likely that a foreign trust would make a loan of marketable securities. The Treasury Department and the IRS request comments on whether qualified obligation rules are needed for loans of marketable securities.

Second, in the case of a use of trust property other than a loan of cash or marketable securities, the general rule will not apply to the extent that the

foreign trust receives the fair market value of such use within a reasonable period (described in proposed § 1.643(i)–2(a)(2)(ii) as 60 days or less) from the start of the use of the trust property. The fair market value of the use will be based on all the facts and circumstances, including the type of property used and the period of use.

Third, the general rule will not apply to any de minimis use of trust property (described in proposed § 1.643(i)–2(a)(3) as aggregate use by members of a group consisting of the U.S. grantors and beneficiaries and the U.S. persons related to them for a total of 14 days or less during the taxable year), other than a loan of cash or marketable securities, by a U.S. grantor or beneficiary or a U.S. person related to a U.S. grantor or beneficiary.

Fourth, the general rule will not apply to a loan of cash that is made by a foreign corporation to a U.S. beneficiary of the foreign trust to the extent the aggregate amount of all such loans to the beneficiary does not exceed undistributed earnings and profits of the foreign corporation attributable to amounts that are, or have been, included in the beneficiary's gross income under section 951, 951A, or 1293. This exception is intended to prevent double taxation that could result by reason of the application of section 643(i) to an amount that has already been included in the U.S. beneficiary's gross income as a subpart F income inclusion, a global intangible low-taxed income inclusion, an inclusion by reason of a controlled foreign corporation's investment of earnings in United States property, or a qualified electing fund inclusion. The Treasury Department and the IRS request comments on whether the scope of the exception is appropriate, and whether ordering rules to determine the sourcing of loan amounts, for example, rules based on the principles of section 959 or similar to the provisions of § 1.672(f)–4(c)(3), or other clarifications on the exception's application, are necessary.

C. Qualified Obligations

Proposed § 1.643(i)–2(b) provides rules for determining whether a loan of cash is made in exchange for a qualified obligation. Proposed § 1.643(i)–2(b)(2) defines the terms *obligor, obligation,* and *qualified obligation.* The definitions of obligation and qualified obligation are consistent with the amended definitions of obligation and qualified obligation in proposed § 1.679–1(c)(6) and § 1.679–4(d), respectively. The term *obligor* means a person who issues an obligation (within the meaning of proposed § 1.643(i)–2(b)(2)(i)) to a foreign trust in exchange for a loan of cash. The term *obligation* means any instrument or contractual arrangement that constitutes indebtedness under general principles of Federal income tax law (for example, a bond, note, debenture, certificate, bill receivable, account receivable, note receivable, open account, or other evidence of indebtedness), and an annuity contract that would not otherwise be classified as indebtedness under general principles of Federal income tax law. Under proposed § 1.643(i)–2(b)(2)(iii)(A), the term *qualified obligation* means an obligation that satisfies all of the following requirements:

First, the obligation must be in writing.

Second, the term of the obligation must not exceed five years.

Third, all payments on the obligation must be made in cash in U.S. dollars. The Treasury Department and the IRS stress this requirement to make all payments in cash in U.S. dollars, in light of abusive transactions in which taxpayers have used an inflated valuation of in-kind property to purportedly repay an obligation.

Fourth, the obligation must be issued at par and must provide for stated interest at a fixed rate or a qualified floating rate within the meaning of § 1.1275–5(b).

Fifth, the yield to maturity must be not less than 100 percent and not greater than 130 percent of the applicable Federal rate in effect under section 1274(d) on the day on which the obligation is issued. The yield to maturity and the applicable Federal rate must be based on the same compounding period. If an obligation is a variable rate debt instrument that provides for stated interest at a qualified floating rate, the rules in §§ 1.1274–2(f)(1) and 1.1275–5(e) apply to determine the obligation's yield to maturity.

Sixth, all stated interest on the obligation must be qualified stated interest within the meaning of § 1.1273–1(c).

In addition to these six initial requirements, for both the first year and each succeeding year in which the obligation remains outstanding, the three requirements of proposed § 1.643(i)–2(b)(2)(iii)(B) must be satisfied in order for the obligation to remain a qualified obligation. First, the U.S. grantor or beneficiary (as the person who would be subject to income tax if an obligation either is not a qualified obligation or ceases to be a qualified obligation) must extend the period for assessment on Part III of Form 3520 (under rules described in proposed § 1.643(i)–2(b)(2)(iii)(B)(*1*)) of any income tax attributable to the loan and any consequent income tax changes for each year that the obligation is outstanding to a date not earlier than three years after the maturity date of the obligation issued in consideration for the loan. Second, the U.S. grantor or beneficiary must report the status of the obligation, including any payments made, on Part III of Form 3520. Third, the obligor must make all payments of principal and interest on the obligation according to the terms of the obligation.

Proposed § 1.643(i)–2(b)(3) provides that, if the terms of the obligation are modified and the modification is treated as an exchange under § 1.1001–3, the new obligation that is deemed issued in the exchange under § 1.1001–3 must satisfy the requirements in proposed § 1.643(i)–2(b)(2)(iii) to be a qualified obligation using the original obligation's issue date. If the modification is not treated as an exchange under § 1.1001–3, then the obligation is retested as of the date of the modification to determine whether the obligation, as modified, continues to satisfy the requirements to be a qualified obligation.

Proposed § 1.643(i)–2(b)(4) provides that if, while the obligation is outstanding, the U.S. obligor directly or indirectly issues another obligation to the foreign trust in exchange for cash, the outstanding obligation is deemed to have the maturity date of the new obligation for purposes of determining whether the term of the outstanding obligation exceeds five years. The outstanding obligation must be retested as of the issue date of the new obligation to determine whether the outstanding obligation continues to be a qualified obligation. The new obligation also must be separately tested to see if it satisfies the requirements to be a qualified obligation.

Proposed § 1.643(i)–2(b)(5) provides that the IRS may treat two or more obligations issued by a U.S. obligor as a single obligation that is not a qualified obligation if they are structured with a principal purpose to avoid the application of section 643(i).

Proposed § 1.643(i)–2(b)(6) provides that, if a qualified obligation ceases to be a qualified obligation (for example, because a modification causes the term of the obligation to exceed five years), the U.S. grantor or beneficiary is treated as receiving a section 643(i) distribution from the foreign trust. In general, the amount of the section 643(i) distribution is the obligation's outstanding stated principal amount plus any accrued but

unpaid qualified stated interest (within the meaning of § 1.1273–1(c)) as of the date of the event that causes the obligation to no longer be a qualified obligation. If the IRS treats two or more obligations as a single obligation that is not a qualified obligation under proposed § 1.643(i)–2(b)(5), then the amount of the section 643(i) distribution will not exceed the sum of the outstanding stated principal amounts of the obligations plus any accrued but unpaid qualified stated interest as of the date determined by the IRS.

D. Trust Property Attributable to Nongrantor Trust Portion

Proposed § 1.643(i)–2(c) provides rules for determining the extent to which a loan or use of trust property from a partial nongrantor trust will be attributable to the nongrantor trust portion. Generally, a loan or use of trust property from a partial nongrantor trust must be apportioned in a manner that is reasonable based on all the facts and circumstances, including the terms of the governing instrument, local law, and the practice of the trustee, if it is reasonable and consistent. However, if a loan or use of trust property can be made from only one portion of the foreign trust because the type of property loaned or used is held only by that portion, then the loan or use of property is attributable to that portion.

E. Reporting

The Treasury Department and the IRS are of the view that it is appropriate to require reporting, pursuant to the authority granted to the Treasury Department and the IRS by section 643(a)(7), of all loans and uses of trust property that are potentially subject to section 643(i), in order to ensure that the IRS has the information necessary to enforce taxpayer compliance with these rules. Thus, proposed § 1.643(i)–2(d) provides that any loan of cash or marketable securities by a foreign trust to a U.S. person and any use by a U.S. person of property belonging to a foreign trust, without regard to whether such loan or use of property is treated as a section 643(i) distribution, also is a distribution within the meaning of proposed § 1.6048–4(b) and subject to the information reporting described under proposed § 1.6048–4(a). See proposed § 1.6048–4(b)(3)(ii) and (iii) and (b)(4)(ii) and (iii).

F. Amount Treated as Section 643(i) Distribution

Proposed § 1.643(i)–3(a) provides rules for determining the amount that is treated as a section 643(i) distribution if an exception does not apply. In the case of a loan of cash, the amount of the section 643(i) distribution is the issue price of the loan as of the date the loan is treated as a distribution from the foreign trust. In the case of a loan of marketable securities, the amount of the section 643(i) distribution is the fair market value of the securities as of the date the loan is treated as a distribution from the foreign trust. In the case of the use of trust property without fair market value compensation, the amount of the section 643(i) distribution is the fair market value of the use of the property less any payments made for the use of the property within a reasonable period of time.

G. Allocation of Section 643(i) Distribution Among Multiple U.S. Grantors and Beneficiaries

Proposed § 1.643(i)–3(b) provides a rule for allocating a section 643(i) distribution among multiple U.S. grantors and beneficiaries. If a U.S. person who is not a U.S. grantor or beneficiary of a foreign trust but who is related to more than one U.S. grantor or beneficiary of the foreign trust receives a loan of cash or marketable securities from the trust, or uses trust property, and the loan or use is treated as a section 643(i) distribution, then each U.S. grantor or beneficiary who is related to the U.S. person receiving the loan or using trust property is treated as receiving an equal share of the section 643(i) distribution.

H. Tax Consequences of a Section 643(i) Distribution

Proposed § 1.643(i)–3(c) provides rules to determine the tax consequences of a section 643(i) distribution to a foreign trust treated as making a section 643(i) distribution and to a U.S. grantor or beneficiary treated as receiving the distribution. Proposed § 1.643(i)–3(c)(2) provides that a foreign trust generally must treat the section 643(i) distribution as an amount properly paid, credited, or required to be distributed by the trust as described in section 661(a)(2) for which the trust may be allowed a distribution deduction in computing its taxable income. In addition, a section 643(i) distribution of marketable securities would cause a foreign trust to be deemed to have elected to have section 643(e)(3) apply to such distribution, which would cause the trust to recognize gain or loss as if the marketable securities had been sold at fair market value. Any capital gain recognized by the foreign trust would be included in the trust's distributable net income (*DNI*) pursuant to section 643(a)(6)(C). As a result of the deemed election, a U.S. grantor or beneficiary would be treated as including in gross income under section 662(a)(2) the fair market value of the marketable securities, and in computing its taxable income, the foreign trust would be allowed to deduct the fair market value of the marketable securities to the extent allowed under section 661(a)(2).

Proposed 1.643(i)–3(c)(2)(iii) provides that the foreign trust may issue a Foreign Nongrantor Trust Beneficiary Statement (described in proposed § 1.6048–4(c)(2)) to each U.S. grantor or beneficiary who receives any loan of cash or marketable securities or uses other trust property during the taxable year of the trust or is related to a U.S. person who receives any loan of cash or marketable securities or uses other trust property during the taxable year of the trust, whether or not such U.S. grantor or beneficiary would be required to take the amount into account as a section 643(i) distribution. A U.S. grantor or beneficiary who does not receive a Foreign Nongrantor Trust Beneficiary Statement with respect to a section 643(i) distribution is required to determine the tax consequences of the distribution under the default calculation method in proposed § 1.643(i)–3(c)(3)(ii).

Proposed § 1.643(i)–3(c)(3) provides that a U.S. grantor or beneficiary who is treated as receiving a section 643(i) distribution must determine the tax consequences of the distribution using either the actual calculation method or the default calculation method. Under the actual calculation method, set out under proposed § 1.643(i)–3(c)(3)(i), a U.S. grantor or beneficiary must treat a section 643(i) distribution as an amount properly paid, credited, or required to be distributed by the foreign trust as described in section 662(a)(2) (relating to inclusions in gross income by beneficiaries of trusts accumulating income or distributing corpus). The tax consequences of the section 643(i) distribution to a U.S. grantor or beneficiary are determined by using information provided in the Foreign Nongrantor Trust Beneficiary Statement and applying the rules of subparts C and D of part I of subchapter J of chapter 1 of the Code.

Under the default calculation method, as provided in proposed § 1.643(i)–3(c)(3)(ii), a U.S. grantor or beneficiary must determine the tax consequences of the section 643(i) distribution under the rules provided in proposed § 1.6048–4(d)(3). For an explanation of the default calculation method, see section IV.C of this Explanation of Provisions.

A U.S. grantor or beneficiary may not use the actual calculation method unless the U.S. grantor or beneficiary

has received a Foreign Nongrantor Trust Beneficiary Statement (described in proposed § 1.6048–4(c)(2)) from the foreign trust. A U.S. grantor or beneficiary who previously has used the default calculation method must consistently use the default calculation method to determine the tax consequences of all subsequent distributions from the same foreign trust (including distributions other than section 643(i) distributions), except in the year in which the foreign trust terminates. See proposed § 1.6048–4(b) for the definition of the term *distribution,* and see proposed § 1.6048–4(d)(3)(iii) for rules relating to the tax consequences to a U.S. grantor or beneficiary in the year in which a foreign trust terminates.

I. Subsequent Transactions

Proposed § 1.643(i)–3(d)(1) provides rules regarding the treatment of any subsequent transaction between a foreign trust and an obligor regarding the principal of any loan of cash or marketable securities (or use of trust property) that is treated as a section 643(i) distribution, including complete or partial repayment, satisfaction, cancellation, discharge, return of trust property, or otherwise, but not including payments of interest. Proposed § 1.643(i)–3(d)(2) provides that any subsequent transaction with respect to the principal of any loan of cash or marketable securities or return of trust property treated as a section 643(i) distribution has no tax consequences to a foreign trust. However, payment to a foreign trust other than the repayment of principal of any loan treated as a section 643(i) distribution, such as the payment of interest, is treated as income to the trust.

Proposed § 1.643(i)–3(d)(3) provides the consequences to an obligor of subsequent transactions between a foreign trust and the obligor related to a section 643(i) distribution. Generally, any subsequent transaction regarding the principal of any loan of cash or marketable securities or return of trust property treated as a section 643(i) distribution is treated as a transfer that is not a gratuitous transfer by a U.S. person for purposes of § 1.671–2(e)(2)(i) and chapter 1 of the Code. Thus, the repayment of principal would not cause an obligor to be treated as the owner of the foreign trust. However, if an obligor satisfies the principal of any loan of cash or marketable securities treated as a section 643(i) distribution through a transfer of property to the foreign trust, the obligor will recognize as gain or loss the difference between the fair market value of the property transferred and its adjusted basis in the hands of the obligor under the rules of section 1001 and the regulations issued under section 1001.

II. Section 679—Foreign Trusts Treated as Having a U.S. Beneficiary

The proposed regulations amend the definition of *U.S. person* in § 1.679–1(c)(2), the definition of *obligation* in § 1.679–1(c)(6), and the definition of *qualified obligation* in § 1.679–4(d). The amended definitions generally are consistent with the definitions of the same terms in proposed §§ 1.643(i)–1(d)(12) and 1.643(i)–2(b)(2), except that the definition of a *U.S. person* in proposed § 1.679–1(c)(2) does not exclude tax-exempt entities.

The proposed regulations also make two additions to § 1.679–2 that provide guidance on two statutory provisions added to section 679 by the HIRE Act. First, proposed § 1.679–2(a)(5) and proposed § 1.679–2(b)(3) provide guidance to determine when a loan from a foreign trust to a U.S. person or the use of foreign trust property by a U.S. person causes the foreign trust to be treated as having a U.S. beneficiary. Second, proposed § 1.679–2(d) implements section 679(d), which generally provides that, if a U.S. person directly or indirectly transfers property to a foreign trust, the trust is presumed to have a U.S. beneficiary in certain circumstances.

A. Definition of U.S. Person

Proposed § 1.679–1(c)(2) amends the current definition of *U.S. person* for purposes of §§ 1.679–1 through 1.679–6 to remove the explicit statement that a nonresident alien individual who elects under section 6013(g) to be treated as a resident of the United States is a U.S. person for purposes of section 679 without intending a substantive change from the existing regulation regarding the treatment of persons who make an election under section 6013(g). Additionally, a U.S. person for purposes of section 679 will include a nonresident alien individual who elects under section 6013(h) to be treated as a resident of the United States. An election under either section 6013(g) or (h) is effective for all purposes of chapter 1 of the Code, including section 679, and thus, no specific reference to either rule should be required.

Under the definition of *U.S. person* in the proposed regulations, however, a dual resident taxpayer (within the meaning of § 301.7701(b)–7(a)(1)) is not treated as a U.S. person with respect to any taxable year (or portion of a taxable year) for which such person computes U.S. tax liability as a nonresident alien pursuant to § 301.7701(b)–7. The Treasury Department and the IRS are of the view that it is not necessary to treat a dual resident taxpayer who has elected to compute such person's income tax liability as a nonresident alien as a U.S. person for purposes of §§ 1.679–1 through 1.679–6 in order to carry out the purposes of section 679. However, see § 1.679–5 for rules that may apply if a dual resident taxpayer who has been computing U.S. tax liability as a nonresident alien begins to compute tax liability as a U.S. resident.

B. Definition of Obligation

Proposed § 1.679–1(c)(6) amends the current definition of *obligation* for purposes of §§ 1.679–1 through 1.679–6 to conform to the definition of obligation in proposed § 1.643(i)–2(b)(2)(i).

C. Loans From Foreign Trusts and Uses of Trust Property

Proposed § 1.679–2(a)(5)(i) provides guidance under section 679(c)(6), which was added to the Code by the HIRE Act. As a general rule, any direct or indirect loan of cash or marketable securities (whether from trust income or corpus) by a foreign trust to, or the direct or indirect use of any other property of a foreign trust by, any U.S. person (whether or not a beneficiary under the terms of the trust) will be treated as causing trust income or corpus to be paid to or accumulated for the benefit of a U.S. person for purposes of § 1.679–2(a)(1). For these purposes, a loan to, or use of any other property of a foreign trust by, a grantor trust or a disregarded entity is treated as a loan to, or use of trust property by, the owner of the grantor trust or of the disregarded entity. (For example, a loan to a single member LLC treated as a disregarded entity would be treated as a loan to the owner of the LLC.) Consequently, a foreign trust that is not already treated as having a U.S. beneficiary under § 1.679–2 is treated as having a U.S. beneficiary for purposes of § 1.679–1, with the result that a U.S. grantor who has made a transfer to the foreign trust is treated as the owner of the trust (or a portion of the trust). See proposed § 1.6048–4 for rules relating to information reporting with respect to loans from foreign trusts and the use of property of a foreign trust.

Proposed § 1.679–2(a)(5)(ii) provides that an indirect loan from a foreign trust to a U.S. person includes a loan made by any person, whether U.S. or foreign, if the foreign trust provides a guarantee (within the meaning of § 1.679–3(e)(4)) for the loan. An indirect loan from a foreign trust to a U.S. person also

includes a loan made through an intermediary, such as an agent or nominee of the foreign trust or of the U.S. beneficiary, and a loan from a person related (within the meaning of proposed § 1.643(i)–1(d)(9)) to the foreign trust.

Proposed § 1.679–2(a)(5)(iii) provides three exceptions to the general rule of proposed § 1.679–2(a)(5)(i).

First, the general rule does not apply if the U.S. person who receives the loan of cash or marketable securities, or who uses trust property, is described in section 501(c)(3).

Second, the general rule does not apply to any loan of cash received by a U.S. person in exchange for a qualified obligation within the meaning of proposed § 1.643(i)–2(b)(2)(iii)(A), provided the obligor timely makes all payments within the meaning of proposed § 1.643(i)–2(b)(2)(iii)(B)(3).

Third, the general rule does not apply if the U.S. person who uses trust property (other than a loan of cash or marketable securities) pays the foreign trust the fair market value of the use of such property within a reasonable period from the date of the start of the use of the property. The fair market value is based on all the facts and circumstances, including the type of property used and the period of use. Proposed § 1.679–2(a)(5)(iv) provides two safe harbors in which this fair market value exception applies.

Proposed § 1.679–2(a)(5)(v) addresses the interaction of proposed § 1.679–2(a)(5) with section 643(i) and confirms that section 643(i) does not apply to the extent a foreign trust is treated as having acquired a U.S. beneficiary and is treated as owned by a U.S. person under section 679 (discussed in section I.A of this Explanation of Provisions).

Proposed § 1.679–2(b)(3) provides that a loan of cash or marketable securities or the use of trust property that does not qualify for the exceptions described in proposed § 1.679–2(a)(5)(iii) is treated as paid to or accumulated for the benefit of a U.S. person if the loan is made to, or the property is used by, a foreign entity described in § 1.679–2(b)(1), or if the loan is made through, or the property is used by, an intermediary or is made by any other means where a U.S. person may obtain an actual or constructive benefit, as described in § 1.679–2(b)(2).

D. Presumption That Foreign Trust Has U.S. Beneficiary

Proposed § 1.679–2(d)(1) provides guidance under section 679(d) regarding whether a foreign trust is deemed to have a U.S. beneficiary. As a general rule, if a U.S. person directly or indirectly transfers property to a foreign trust (other than a compensatory or charitable trust described in § 1.679–4(a)(2) or (3)), the IRS may treat the trust as having a U.S. beneficiary for purposes of applying § 1.679–1 unless the U.S. person, for the tax year in which the transfer is made, (i) satisfies the information reporting requirements of proposed § 1.6048–2 with respect to the transfer, and (ii) attaches an explanatory statement to the U.S. person's Federal income tax return demonstrating to the satisfaction of the IRS that the trust satisfies the requirements of § 1.679–2(a)(1) immediately after the transfer. Section 1.679–2(a)(1) provides that a foreign trust is treated as having a U.S. beneficiary unless, during the taxable year in which the U.S. person made the transfer, (i) no part of the income or corpus of the foreign trust may be paid to or accumulated for the benefit of, directly or indirectly, a U.S. person, and (ii) if the foreign trust is terminated at any time during the taxable year, no part of the income or corpus of the trust could be paid to or for the benefit of, directly or indirectly, a U.S. person.

Proposed § 1.679–2(d)(2) provides that the IRS may request additional information related to the foreign trust and its potential beneficiaries to determine whether the trust satisfies the requirements of § 1.679–2(a)(1). Unless the U.S. person provides such additional information within 60 days (90 days if the U.S. person is outside the United States) after the IRS's written notice and request, the trust will be presumed to have a U.S. beneficiary.

E. Definition of Qualified Obligation

Proposed § 1.679–4(d) amends the current definition of *qualified obligation* for purposes of § 1.679–4 to conform to the definition of qualified obligation in proposed § 1.643(i)–2(b)(2)(iii) and the additional rules in proposed §§ 1.643(i)–2(b)(3) through (6) (discussed in section I.C of this Explanation of Provisions).

III. Section 6039F—Information Reporting Rules for U.S. Recipients of Foreign Gifts

The proposed regulations provide information reporting rules for U.S. recipients of foreign gifts by generally incorporating the section 6039F guidance that was provided in Notice 97–34 (discussed in section III.C of the Background). They also provide additional guidance that is needed to implement all of section 6039F and to address certain abuses of which the IRS has become aware and relevant statutory developments since 1997, including the enactment of section 2801 dealing with gifts and bequests from certain expatriates.

A. In General

Proposed § 1.6039F–1(a)(1) provides that any U.S. person who treats an amount received from a foreign person as a foreign gift during a taxable year must report that amount on Part IV of Form 3520 by the fifteenth day of the fourth month after the close of the U.S. person's taxable year. Proposed § 1.6039F–1(a)(2) provides that, if the U.S. person qualifies for an automatic extension of time to file an income tax return under section 6081 and § 1.6081–5(a)(5) because the U.S. person resides outside of the United States and Puerto Rico, and the U.S. person's main place of business or post of duty is outside of the United States or Puerto Rico, Form 3520 must be filed by the fifteenth day of the sixth month after the close of the U.S. person's taxable year. In either case, if the U.S. person has been granted an extension of time to file an income tax return pursuant to section 6081, an extension of time for filing Form 3520 is automatically granted to the fifteenth day of the tenth month following the close of the U.S. person's taxable year. See proposed § 1.6039F–1(a)(1) and (2). Proposed § 1.6039F–1(a)(3) provides that, if the U.S. person dies, the executor of the U.S. person's estate must report the foreign gift on Part IV of Form 3520 by the fifteenth day of the fourth month following the close of the 12-month period which began with the first day of the U.S. person's final taxable year or, if the executor has been granted an extension of time to file the U.S. person's final income tax return pursuant to section 6081, by the fifteenth day of the tenth month following the close of the 12-month period which began with the first day of the U.S. person's final taxable year. No additional extension of time to file Form 3520 is allowed.

For purposes of proposed § 1.6039F–1, the term *U.S. person* means a United States person as defined under section 7701(a)(30). However, under proposed § 1.6039F–1(f), consistent with the approach in proposed §§ 1.643(i)–1(d)(12)(ii) and 1.679–1(c)(2)(ii), neither a dual resident taxpayer nor a dual status taxpayer is treated as a U.S. person for purposes of proposed § 1.6039F–1 for a taxable year or any portion of a taxable year that the taxpayer is treated as a nonresident alien for purposes of computing U.S. tax liability. See section III.F of this Explanation of Provisions.

B. Definition of ''Foreign Gift'' and Coordination With Section 6048(c)

For purposes of proposed § 1.6039F–1, the term *foreign gift* is defined to include any amount received from a person other than a U.S. person that the recipient treats as a gift, bequest, devise, or inheritance for Federal income tax purposes. The term, however, does not include any qualified transfer within the meaning of section 2503(e)(2) (relating to certain transfers for educational or medical expenses) or any transfer from a foreign trust that is treated as a distribution (within the meaning of proposed § 1.6048–4(b)) and reported on a return under proposed § 1.6048–4. Proposed § 1.6039F–1(b)(1) also provides that a U.S. person who receives a transfer from a foreign trust must treat the transfer as a distribution from the trust that is reportable under proposed § 1.6048–4, rather than reportable as a foreign gift under proposed § 1.6039F–1(a), even if the U.S. person treats the transfer as a gift for another purpose, such as computing the U.S. person's Federal income tax liability.

Proposed § 1.6039F–1(b)(2) includes an anti-avoidance rule that provides that the term *foreign gift* includes transfers from a person other than a U.S. person that the recipient does not treat as a gift, bequest, devise, or inheritance for Federal income tax purposes, such as a purported loan, if based on all the facts and circumstances the IRS determines that the transfer is in substance a gift. The IRS has become aware of U.S. persons who are seeking to circumvent the section 6039F information reporting rules by claiming that the amounts they receive from foreign persons are not foreign gifts because they do not treat them as gifts but that they are otherwise not taxable (claiming instead that the transfers are loans). These amounts, however, objectively have all the indicia of being a gift. Under the existing principles of Federal tax law, the IRS therefore will recharacterize these amounts as foreign gifts that should have been reported under section 6039F.

C. Exceptions

Proposed § 1.6039F–1(c) provides a number of exceptions to the general rule in proposed § 1.6039F–1(a). Proposed § 1.6039F–1(c)(1) provides that the general rule does not apply if the recipient of the foreign gift is described in section 501(c) and is exempt from tax under section 501(a). Proposed § 1.6039F–1(c)(2)(i) through (iii) provides exceptions from information reporting under proposed § 1.6039F–1(a) for amounts below the reporting thresholds.

Under proposed § 1.6039F–1(c)(2)(i)(A), a U.S. person is not required to report foreign gifts from foreign individuals or foreign estates if, during the U.S. person's taxable year, the aggregate amount of foreign gifts received, directly or indirectly, from any one individual or estate (the *transferor*) does not exceed $100,000, as modified by cost of living adjustments under proposed § 1.6039F–1(c)(2)(v). For purposes of determining whether the $100,000 reporting threshold is met, all foreign gifts (including covered gifts and bequests) from the transferor and from any foreign persons related to the transferor are aggregated. See proposed § 1.6039F–1(c)(2)(i)(B).

If the aggregate amount of foreign gifts from a transferor exceeds the $100,000 reporting threshold, the proposed regulations require the U.S. person to separately identify each foreign gift in excess of $5,000 received from the transferor and from each foreign person related to the transferor, and to provide identifying information about the transferor and related foreign persons, including foreign individuals or foreign estates (for example, name and address). Specific identifying information about the transferor is not currently required to be provided on Form 3520. The Treasury Department and the IRS are of the view that the additional identifying information would assist the IRS in its determination of whether these amounts are properly treated as foreign gifts, and the burden imposed on the U.S. person should be minimal because the U.S. person would need to know the transferor's identity in order to know whether the transferor is foreign and in order to apply the aggregation rule.

Under proposed § 1.6039F–1(c)(2)(ii), notwithstanding the reporting threshold described above, beginning on the date on which final regulations under section 2801 (tax on gifts and bequests from expatriates) apply, a U.S. person who receives foreign gifts that are covered gifts or bequests will be required to report the covered gifts or bequests under proposed § 1.6039F–1(a) if the aggregate amount of all covered gifts and bequests received by the U.S. person during the calendar year exceeds the exclusion amount under section 2801(c). See proposed § 1.6039F–1(h)(2). This exclusion amount is the dollar amount of the per-donee gift tax exclusion in effect under section 2503(b) for the calendar year ($18,000 for 2024).

Under proposed § 1.6039F–1(c)(2)(iii), a U.S. person is not required to report foreign gifts from a foreign corporation or partnership if, during the U.S. person's taxable year, the aggregate amount of transfers received from any particular corporation or partnership does not exceed $10,000, as modified by cost-of-living adjustments under proposed § 1.6039F–1(c)(2)(v). The proposed regulations provide rules for aggregating and reporting foreign gifts from persons related to the transferor.

Proposed § 1.6039F–1(c)(2)(iv) provides that, with respect to spouses who file joint income tax returns under section 6013, the reporting threshold amounts apply separately to each spouse.

D. Valuation Principles

Proposed § 1.6039F–1(d) provides that the amount of a foreign gift is the value of the property at the time of the transfer. The value of the property is the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or sell, and both having reasonable knowledge of relevant facts. The value is to be determined in accordance with the Federal gift tax valuation principles of section 2512 and sections 2701 through 2704 (chapter 14 of the Code) and the related regulations.

E. Penalty for Failure To File Information

Proposed § 1.6039F–1(e)(1) describes penalties for failure to furnish the information required by proposed § 1.6039F–1(a) by the due date (including extensions) of Form 3520. The tax consequences of the receipt of the foreign gift will be determined by the IRS based on all the facts and circumstances. A U.S. person who fails to furnish the required information is subject to a penalty equal to five percent of the amount of the foreign gift for each month (or portion thereof) for which the failure continues, but not to exceed 25 percent of the amount of the foreign gift.

For purposes of determining the tax consequences of the receipt of the foreign gift, the IRS may take into account the purported gift rules in § 1.672(f)–4 (which address the treatment of a purported gift, as defined in § 1.672(f)–4(d), from a partnership or foreign corporation). Unless an exception described in § 1.672(f)–4(b), (e) or (f) applies, § 1.672(f)–4 generally requires a U.S. person who receives a purported gift or bequest, directly or indirectly, from a partnership or foreign corporation to include the purported gift or bequest in gross income as ordinary income.

Proposed § 1.6039F–1(e)(2)(i) explains that no penalty is imposed if the U.S.

person shows that the failure to comply is due to reasonable cause and not due to willful neglect. The determination of whether a failure is due to reasonable cause and not due to willful neglect will be made under the principles set out in § 1.6664–4 and § 301.6651–1(c) and will be made on a case-by-case basis, taking into account all pertinent facts and circumstances.

F. Special Rules for Dual Resident and Dual Status Taxpayers

Proposed § 1.6039F–1(f)(1) provides a special rule for dual resident taxpayers (within the meaning of § 301.7701(b)–7(a)(1)). A dual resident taxpayer who, pursuant to a provision of an income tax treaty that provides for resolution of conflicting claims of residence by the United States and the treaty partner, claims to be treated as a resident of the treaty partner as provided in § 301.7701(b)–7 is taxed as a nonresident for U.S. tax purposes for the portion of the taxable year that the individual is treated as a nonresident. The Treasury Department and the IRS are of the view that, because the dual resident taxpayer's filing of relevant forms pursuant to § 301.7701(b)–7 provides adequate information for the IRS to identify residents in this category in order to ensure their tax compliance, reporting on Form 3520 by such a taxpayer is not essential to effective IRS tax enforcement efforts relating to this category of residents.

Similarly, proposed § 1.6039F–1(f)(2) provides a special rule for dual status taxpayers. As provided in § 1.6012–1(b)(2)(ii), a dual status taxpayer who, during the taxable year, abandons U.S. citizenship or U.S. residence or acquires U.S. citizenship or U.S. residence is not treated as a U.S. person for the part of the year that the taxpayer is treated as a nonresident alien for purposes of computing the taxpayer's income tax liability as reflected on the Form 1040NR or other similar schedule attached to such Form 1040NR.

These rules are relevant both for purposes of determining whether a dual resident taxpayer or dual status taxpayer who receives a foreign gift is a U.S. person required to report the foreign gift on Form 3520 and for purposes of determining whether a gift or bequest from a dual resident taxpayer or dual status taxpayer is a gift from a foreign person.

IV. Section 6048—Information With Respect to Certain Foreign Trusts

The proposed regulations provide information reporting rules with respect to a U.S. person's transfers to, creation of, ownership of, and receipt of distributions from foreign trusts. These proposed regulations generally implement the rules set forth in Notice 97–34, Revenue Procedure 2014–55, and Revenue Procedure 2020–17 (discussed in section III.D of the Background) but also provide additional exceptions to section 6048 reporting and include certain other modifications.

A. Section 6048(a)—Notice of Certain Events

The proposed regulations under section 6048(a) require a responsible party to provide notice of reportable events that occur during the taxable year on Part I of Form 3520. See proposed § 1.6048–2(a)(1).

Proposed § 1.6048–2(c) defines *responsible party* as the grantor in the case of the creation of an inter vivos foreign trust, the transferor in the case of a transfer of property to a foreign trust by a U.S. person other than a transfer by reason of death, or the executor of the estate of a deceased grantor or transferor in any other case, even if the executor is not a U.S. person.

Proposed § 1.6048–2(b) defines a *reportable event* as: (i) the creation of a foreign trust by a U.S. person, (ii) any direct, indirect, or constructive transfer, within the meaning of § 1.679–3 or § 1.684–2, of property (including cash) to a foreign trust by a U.S. person, including a transfer by reason of death, and (iii) 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 if any portion of a foreign trust was included in the gross estate of the decedent. A reportable event also includes a U.S. person's transfer of property to a domestic trust that becomes a foreign trust, as described in § 1.684–4 (outbound migrations of domestic trusts), and a U.S. person's transfer of property in exchange for any obligation of the foreign trust or of a related person, as described in § 1.679–4, without regard to whether the obligation is a qualified obligation. A reportable event does not include transfers to certain foreign charitable trusts, foreign compensatory trusts, and tax-favored foreign retirement and non-retirement savings trusts, as discussed in section IV.D.2.i of this Explanation of Provisions. See proposed § 1.6048–5.

Form 3520 generally must be filed by the fifteenth day of the fourth month after the close of the responsible party's taxable year, but no later than the fifteenth day of the tenth month if the responsible party receives an extension of time to file the responsible party's income tax return under section 6081. See proposed § 1.6048–2(a)(2)(i). However, if the responsible party who is a grantor or transferor qualifies for an automatic extension of time to file an income tax return under section 6081 and § 1.6081–5(a)(5) because the responsible party resides outside of the United States and Puerto Rico, and the responsible party's main place of business or post of duty is outside of the United States or Puerto Rico, Form 3520 must be filed by the fifteenth day of the sixth month after the close of the responsible party's taxable year. See proposed § 1.6048–2(a)(2)(ii). If the responsible party who is a grantor or transferor dies, the executor of the responsible party's estate must file Form 3520 by the fifteenth day of the fourth month after the close of the 12-month period which began on the first day of the responsible party's final taxable year. See proposed § 1.6048–2(a)(2)(iii).

B. Section 6048(b)—U.S. Owners of Foreign Trusts

The proposed regulations under section 6048(b) generally require any U.S. person who is treated as the owner (*U.S. owner*) of any portion of a foreign trust under the grantor trust rules to ensure that the foreign trust: (i) files Form 3520–A with the IRS by the fifteenth day of the third month after the end of the trust's taxable year (March 15 if the trust's taxable year is a calendar year) with a maximum extension of a 6-month period beginning on such day, (ii) furnishes a Foreign Grantor Trust Owner Statement (described in proposed § 1.6048–4(c)(1)(i)) to each U.S. owner of the foreign trust, and (iii) furnishes a Foreign Grantor Trust Beneficiary Statement (described in proposed § 1.6048–4(c)(1)(ii)) to each U.S. person to whom the trust made distributions during the trust's taxable year. The foreign trust must attach copies of each Foreign Grantor Trust Owner Statement and each Foreign Grantor Trust Beneficiary Statement to the Form 3520–A. See proposed § 1.6048–3(a)(1). If the foreign trust does not comply with all these requirements, the U.S. owner is required to: (i) complete and file Part II of Form 3520 by the U.S. owner's Form 3520 due date, and (ii) complete the foreign trust's Form 3520–A and related statements and file them with Part II of the U.S. owner's Form 3520. Further, the U.S. owner must furnish the Foreign Grantor Trust Beneficiary Statement to each U.S. beneficiary by the due date of the U.S. owner's Form 3520. See proposed § 1.6048–3(a)(2). If neither the foreign trust nor the U.S. owner complies with these requirements, the penalty for failure to comply is imposed on the U.S.

owner. See proposed § 1.6677–1(b). As discussed in section IV.D.2.i of this Explanation of Provisions, the proposed regulations under section 6048(b) do not apply to tax-favored foreign retirement and non-retirement savings trusts. See proposed § 1.6048–5.

The proposed regulations require a U.S. person who receives a Foreign Grantor Trust Owner Statement or Foreign Grantor Trust Beneficiary Statement from a foreign trust to treat any item reported by the trust consistently with the trust's treatment of such item unless the U.S. person notifies the IRS about any inconsistency on Form 8082. See proposed § 1.6048–3(b). If the U.S. person fails to notify the IRS about the inconsistency, or if the U.S. person receives information believed to be incorrect from the foreign trust, then, similar to the rules of section 6034A(c) (addressing reporting in respect of income tax returns), any adjustment relating to an unreported item is treated as a mathematical or clerical error under section 6213(b), with the result that the adjustment would not be subject to the usual restrictions on assessment and the U.S. grantor or U.S. beneficiary would have no right to file a Tax Court petition based on the adjustment.

Proposed § 1.6048–3(c) provides that, unless a foreign trust with a U.S. owner appoints a limited U.S. agent, the determination of amounts required to be taken into account with respect to the trust by the U.S. owner under the grantor trust rules will be determined by the IRS based on all the facts and circumstances. Proposed § 1.6048–3(d) provides rules relating to the appointment and duties of the limited U.S. agent. Proposed § 1.6048–3(d) also provides rules concerning the issuance of a summons to a U.S. person (either directly or as the limited agent of the foreign trust) or to the foreign trust to produce records or testimony to determine the amounts required to be taken into account under the grantor trust rules.

C. Section 6048(c)—Reporting by U.S. Persons Receiving Distributions From Foreign Trusts

1. In General

Unless an exception described in proposed § 1.6048–5 applies, proposed regulations under section 6048(c) generally require a U.S. person to complete and file Part III of Form 3520 for each taxable year in which the U.S. person receives (directly or indirectly) any distribution from a foreign trust (including a foreign trust that the U.S. person is treated as owning under the grantor trust rules). Part III of Form 3520 must be filed by the due date of the U.S. person's Form 3520 for that taxable year. See proposed § 1.6048–4(a). The Treasury Department and the IRS interpret section 6048(c) as requiring any U.S. person, including a U.S. owner, to report the receipt of foreign trust distributions. This interpretation is consistent with both the plain language of section 6048(c) and its purpose—to address Congress's concerns that U.S. taxpayers were avoiding their U.S. tax obligations through the use of foreign trusts that are less visible to the IRS—and empowers the IRS to obtain information that would allow it to enforce U.S. tax laws.

2. Distributions

Proposed § 1.6048–4(b)(1) provides that, as a general rule, the term *distribution* for purposes of proposed § 1.6048–4 means any transfer of property from a foreign trust received directly or indirectly by a U.S. person to the extent such property exceeds the fair market value of any property or services received by the foreign trust in exchange, without regard to whether any portion of the trust is treated as owned by the grantor or another person under the grantor trust rules, whether the recipient is designated as a beneficiary under the terms of the trust, or whether the distribution has any income tax consequences. A distribution includes any amount actually or constructively received and includes the receipt of a gift or bequest described in section 663(a). For purposes of proposed § 1.6048–4(b)(1), a transfer of property from a foreign trust to a grantor trust or to a disregarded entity is treated as a transfer to the U.S. owner of the grantor trust or of the disregarded entity.

Proposed § 1.6048–4(b)(2)(i) provides that the term *distribution* also includes any transfer of property from a foreign trust received by a U.S. person through an intermediary, nominee, or agent. In such a case, the intermediary, nominee, or agent generally is treated as an agent of the foreign trust, and the property is treated as distributed to the U.S. person in the year the property is transferred or made available to the U.S. person. However, proposed § 1.6048–4(b)(2)(ii) provides that, if the IRS determines that the intermediary, nominee, or agent is an agent of the U.S. person, then the property is treated as being transferred from the foreign trust to the U.S. person on the date of the transfer from the foreign trust to the intermediary, nominee, or agent. Regardless of the income tax consequences of such a transfer, pursuant to proposed § 1.6048–4(b)(2)(iii), the U.S. person receiving an indirect transfer of property from a foreign trust must report it on Part III of Form 3520.

Proposed § 1.6048–4(b)(3) provides that a *distribution* includes any transfer of property from an entity owned by a foreign trust to a U.S. person who is related (within the meaning of § 1.679–1(c)(5)) to the foreign trust. It also explains that the transfer is treated as a distribution from the entity to the foreign trust followed by a distribution from the foreign trust to the U.S. person, unless the U.S. person demonstrates to the satisfaction of the IRS that the distribution from the entity is attributable to the U.S. person's ownership interest in the entity. This rule is the converse of the rule of § 1.679–3(f)(1), which provides that a transfer by a U.S. person to an entity owned by a foreign trust is treated as a transfer to the foreign trust followed by a transfer from the foreign trust to the entity, unless the U.S. person demonstrates to the satisfaction of the IRS that the transfer to the entity is attributable to the U.S. person's ownership interest in the entity.

Proposed § 1.6048–4(b)(4) provides that a *distribution* includes the migration of a foreign trust to a domestic trust. In such a case, the income and corpus of the foreign trust is treated as distributed to the domestic trust on the date the foreign trust becomes a domestic trust. See § 301.7701–7 for the rules that apply to determine whether a trust is a foreign trust or domestic trust.

Proposed § 1.6048–4(b)(5)(i) provides that a *distribution* includes any loan of cash or marketable securities made from a foreign trust (whether from corpus or income) directly or indirectly to a U.S. person. It also clarifies that a loan to a grantor trust or to an entity disregarded as an entity separate from its owner will be treated as a loan to the owner of the grantor trust or of the disregarded entity. Loans from a foreign trust also include a loan made by any foreign or U.S. person if the foreign trust guarantees the loan, as well as a loan made to a U.S. person through any intermediary, nominee or agent.

Proposed § 1.6048–4(b)(5)(ii) further provides that a *distribution* includes any loan of cash or marketable securities made directly or indirectly to a U.S. grantor or beneficiary (as defined in proposed § 1.643(i)–1(d)(1)) of a foreign nongrantor trust or to a U.S. person related (as defined in proposed § 1.643(i)–1(d)(9)) to a U.S. grantor or beneficiary of such foreign nongrantor trust without regard to whether the foreign trust receives an obligation (within the meaning of proposed

§ 1.643(i)–2(b)(2)(i)) in exchange for the loan.

Proposed § 1.6048–4(b)(5)(iii) provides that a loan of cash or marketable securities from a foreign trust must be reported by the U.S. person who receives the loan without regard to whether the loan would have any U.S. income tax consequences to a U.S. grantor or beneficiary of the foreign trust. If the U.S. person who receives the loan is related to a U.S. grantor or beneficiary of a foreign nongrantor trust, then the U.S. grantor or beneficiary also must report the distribution.

Proposed § 1.6048–4(b)(6)(i) provides that a *distribution* includes the fair market value of the direct or indirect use of trust property by a U.S. person without regard to whether the use of trust property would be treated as having any U.S. income tax consequences to a U.S. grantor or beneficiary of the foreign trust. For these purposes, the use of trust property by a grantor trust or a disregarded entity is treated as used by the owner of the grantor trust or of the disregarded entity, respectively. Proposed § 1.6048–4(b)(6)(ii) further provides that a *distribution* includes the fair market value of the direct or indirect use of trust property by a U.S. grantor or beneficiary of a foreign nongrantor trust or by a U.S. person related to such U.S. grantor or beneficiary whether or not the foreign trust is paid the fair market value for such use. Proposed § 1.6048–4(b)(6)(iii) provides that the use of trust property must be reported on Part III of Form 3520 by the U.S. person that uses the trust property without regard to whether the use of trust property would have any U.S. income tax consequences to a U.S. grantor or beneficiary of the foreign trust. If the U.S. person who uses the trust property is related to a U.S. grantor or beneficiary of a foreign nongrantor trust, then the U.S. grantor or beneficiary also must report the distribution.

The Treasury Department and the IRS are of the view that because, under section 643(i), a distribution to a U.S. person related to a U.S. grantor or beneficiary affects the U.S. grantor's or beneficiary's income tax liability, it is appropriate to require reporting by both the U.S. person receiving a distribution from a foreign trust and the U.S. grantor or beneficiary of the foreign trust who is related to that U.S. person. Requiring both parties to report the distribution ensures that the IRS has the information it needs for tax compliance efforts.

Proposed § 1.6048–4(b)(7) confirms that the term *distribution* also includes any covered gift or bequest (within the meaning of section 2801(e)) that is received from a foreign trust.

3. Information Statements

Proposed § 1.6048–4(c) lists four types of information statements that may be provided by a foreign trust if a U.S. person receives a distribution (including a loan of cash or marketable securities or the use of other trust property) from the foreign trust—Foreign Grantor Trust Owner Statement, Foreign Grantor Trust Beneficiary Statement, Foreign Nongrantor Trust Beneficiary Statement, and Foreign-Owned Grantor Trust Beneficiary Statement. The instructions for Form 3520 will be modified after these regulations are finalized to include a list of items that must be included on a Foreign-Owned Grantor Trust Beneficiary Statement. The list will be similar to the lists of items that must be included on the Foreign Grantor Trust Beneficiary Statement and the Foreign Nongrantor Trust Beneficiary Statement. A U.S. person who receives one of these statements may use the statement to determine the tax consequences of the distribution.

4. Tax Consequences of Distributions

Proposed § 1.6048–4(d) describes the rules that a U.S. person (other than a U.S. owner of the distributing trust) must use to determine the tax consequences of a distribution from a foreign trust other than a distribution that is a loan of cash or marketable securities or the use of other trust property that is not treated as a section 643(i) distribution under proposed § 1.643(i)–1. Two methods to determine the tax consequences are provided: (i) the actual calculation method and (ii) the default calculation method. If the U.S. person who receives the distribution does not receive a copy of the relevant statement (see proposed § 1.6048–4(c)), the U.S. person must determine the tax consequences of the distribution under the default calculation method. A U.S. person who receives the relevant statement generally may compute the tax consequences of the distribution under either the actual calculation method or the default calculation method. However, a U.S. person may not use the actual calculation method if the U.S. person knows or has reason to know that the information in the relevant statement is incorrect. Additionally, if the U.S. person has previously used the default calculation method with respect to distributions from the foreign trust, the U.S. person must consistently use the default calculation method to determine the tax consequences of any subsequent distributions from the trust for all future years, except for the year in which the trust terminates.

Under the actual calculation method provided in proposed § 1.6048–4(d)(2), a U.S. person who receives a Foreign Grantor Trust Beneficiary Statement or a Foreign-Owned Grantor Trust Beneficiary Statement from the foreign trust determines the income tax consequences of the distribution as a distribution being made from a grantor trust. Thus, if the distribution is a gift under section 102, the U.S. person does not include the distribution in gross income, but the distribution remains subject to the proposed § 1.6048–4 reporting requirements. A U.S. person who receives a Foreign Nongrantor Trust Beneficiary Statement determines the tax consequences of the distribution by applying the rules of subparts C and D of Part 1 of subchapter J of chapter 1 of the Code.

Under the default calculation method provided in proposed § 1.6048–4(d)(3)(i)(A), the U.S. person treats a portion of the distribution as a distribution of current income based on the average amount of the distributions that the U.S. person received from the foreign trust during the prior three taxable years, with only the excess amount of the distribution (that is, the amount that exceeds 125 percent of that average) treated as an accumulation distribution within the meaning of section 665(b) consisting of undistributed net income (*UNI*) of the foreign trust. In applying the default calculation method, in the absence of actual information provided on a statement described in proposed § 1.6048–4(c), the U.S. person must presume that the applicable number of years the foreign trust has been in existence is ten years and that no taxes described in section 665(d) have been imposed on the trust in any applicable previous year (even if a distribution has been made and tax under section 665(d) has previously been imposed). These rules are consistent with the default calculation method that is currently prescribed in the instructions for Part III of Form 3520. The U.S. person's use of the default calculation method does not affect any calculations made by the foreign trust for purposes of trust accounting. See proposed § 1.6048–4(d)(3)(ii).

5. Accumulation Distributions and U.S. Agents

Proposed § 1.6048–4(e) provides that, if a U.S. person fails to provide adequate records to the IRS for purposes of determining the income tax consequences of a distribution from a foreign trust (within the meaning of

proposed § 1.6048–4(b)) other than a loan or use of trust property that is not treated as a section 643(i) distribution under proposed § 1.643(i)–1, then the entire distribution is treated as an accumulation distribution includible in the U.S. person's income. However, if the trustee of the foreign trust authorizes a U.S. person to act as the trust's limited agent under the rules prescribed in proposed § 1.6048–3(e), then the IRS can summons and examine trust records through the U.S. agent and thus may determine the tax consequences of the distribution under the general rules provided in proposed § 1.6048–4(d)(1) rather than treating the entire distribution as an accumulation distribution.

6. Coordination With the Rule for Reporting Large Foreign Gifts

Proposed § 1.6048–4(f) addresses the interaction of proposed § 1.6048–4 and proposed § 1.6039F–1. If a U.S. person receives a distribution from a foreign trust, the U.S. person must report the distribution under proposed § 1.6048–4(a) and not under proposed § 1.6039F–1, regardless of whether the distribution is taxable to the U.S. person.

D. Exceptions

1. Exceptions To Reporting Transfers of Property to Foreign Trusts

Proposed § 1.6048–5(a) provides an exception from section 6048(a) reporting based on section 6048(a)(3)(B). The proposed regulations provide that, for purposes of proposed § 1.6048–2, a reportable event does not include any of the following: (1) a transfer of property to a foreign trust that is a transfer for fair market value within the meaning of § 1.679–4(b) (other than a transfer described in the following sentence); (2) any transfer of property to certain compensatory foreign trusts, as described in section 402(b), 404(a)(4), or 404A; and (3) any transfer of property to a foreign trust provided that the trust has received a determination letter from the IRS that has not been revoked that recognizes the trust as an organization described in section 501(c)(3) that is exempt from Federal income tax under section 501(a). However, a reportable event does include a transfer for fair market value if the transfer is made by a U.S. transferor that is a related person (as defined in § 1.679–1(c)(5)) with respect to the foreign trust in exchange for any obligation of the trust or of a related person, without regard to whether such obligation is a qualified obligation described in proposed § 1.679–4(d).

2. Additional Exceptions To Reporting Transactions With Foreign Trusts

Proposed § 1.6048–5(b) through (e) provides additional exceptions from section 6048 reporting based on the authority granted to the IRS by section 6048(d)(4) to suspend or modify the requirements of section 6048.

i. Tax-Favored Foreign Retirement Trusts, Non-Retirement Savings Trusts, and de Minimis Savings Trusts

Proposed § 1.6048–5(b) provides an exception from section 6048(a) through (c) and proposed §§ 1.6048–2 through 1.6048–4 for certain eligible U.S. individuals' transactions with, or ownership of, certain tax-favored foreign retirement trusts, non-retirement savings trusts, and de minimis savings trusts. These exceptions to section 6048 reporting generally follow the exceptions provided under Rev. Proc. 2020–17, but are modified to address comments received, including comments requesting that future guidance include an increase to the applicable contribution limitation thresholds, rules for tax-favored foreign retirement trusts that may allow limited contributions of unearned income, and relief with respect to certain trusts that do not fall within the listed categories but that have values below a certain threshold.

A *tax-favored foreign retirement trust* means a foreign trust that is established under the laws of a foreign jurisdiction to operate exclusively or almost exclusively to provide, or to earn income for the provision of, pension or retirement benefits and ancillary or incidental benefits, and that meets certain additional requirements, such as contribution limitations or value thresholds, conditions for withdrawal, and information reporting. See proposed § 1.6048–5(b)(2). A *tax-favored foreign non-retirement savings trust* means a foreign trust that is established under the laws of a foreign jurisdiction to operate exclusively or almost exclusively to provide, or to earn income for the provision of, medical, disability, or educational benefits, and that also meets certain additional requirements, such as contribution limitations, conditions for withdrawal, and information reporting. See proposed § 1.6048–5(b)(3). A *tax-favored foreign de minimis savings trust* means a foreign trust that is established under the laws of a foreign jurisdiction to operate as a savings vehicle, that is not treated as a tax-favored foreign retirement trust or a tax-favored foreign non-retirement savings trust, and that meets certain additional requirements, such as information reporting, and whose value is under a de minimis threshold. See proposed § 1.6048–5(b)(4).

The Treasury Department and the IRS are of the view that it would be appropriate to exempt U.S. individuals from the requirement to provide information about these foreign trusts for several reasons. First, these foreign trusts generally are subject to written restrictions, such as contribution limitations, conditions for withdrawal, and information reporting, under the laws of the country in which they are established that are broadly consistent with the eligibility requirements under the Code for U.S. trusts serving similar policy goals. Second, U.S. individuals with an interest in these trusts may be required under section 6038D to separately report information about their interests in accounts held by, or through, these trusts. Additionally, with respect to tax-favored foreign de minimis savings trusts and tax-favored foreign retirement trusts, the Treasury Department and the IRS are of the view that exempting U.S. individuals from the section 6048 requirements based on the value of the trust is appropriate and consistent with the reporting thresholds under section 6038D.

ii. Distributions From Certain Foreign Compensatory Trusts

The proposed regulations implement the exception from section 6048(c) reporting provided in section V of Notice 97–34 for distributions from certain foreign compensatory trusts described in § 1.672(f)–3(c)(1) (section 402(b) employee trusts and foreign rabbi trusts). Proposed § 1.6048–5(c). The exception applies only if the U.S. individual who receives the distribution reports the distribution as compensation income on a Federal income tax return.

iii. Distributions Received by Certain Domestic Charitable Organizations

Proposed § 1.6048–5(d) implements the exception from section 6048(c) reporting provided in section V of Notice 97–34 for distributions received by a domestic organization described in section 501(c)(3). The exception applies only if the domestic organization has received a determination letter from the IRS that has not been revoked recognizing the domestic organization's exemption from Federal income tax under section 501(a) as an organization described in section 501(c)(3).

iv. Certain Trusts Located in a Mirror Code Possession

Proposed § 1.6048–5(e) provides an exemption from sections 6048(a)

through (c) for a trust located in a mirror code possession to the extent the responsible party (within the meaning of section 6048(a)(4)), U.S. owner, or U.S. recipient is a bona fide resident (within the meaning of § 1.937–1(b)) of the mirror code possession. For this purpose, a mirror code possession is a possession of the United States where, under the income tax system of the possession, the income tax liability of the residents of the possession is determined by reference to the income tax laws of the United States as if the possession were the United States, A trust is located in a mirror code possession if a court within such mirror code possession is able to exercise primary supervision over the administration of the trust and one or more bona fide residents of the mirror code possession have the authority to control all substantial decisions of the trust.

E. Special Rules

1. Dual Resident and Dual Status Taxpayers

Proposed § 1.6048–6(a)(1) provides that a dual resident taxpayer (within the meaning of § 301.7701(b)–7(a)(1)) who computes U.S. income tax liability as a nonresident alien and complies with the filing requirements of § 301.7701(b)–7(b) and (c) is not treated as a U.S. person for purposes of the proposed regulations for the portion of the year that the dual resident taxpayer is treated as a nonresident alien. Similarly, under proposed § 1.6048–6(a)(2), a dual status taxpayer who abandons U.S. citizenship or residence during the tax year or acquires U.S. citizenship or residence during the taxable year, as provided in § 1.6012–1(b)(2)(ii), is not treated as a U.S. person for purposes of the proposed regulations for the portion of the year that the dual status taxpayer is treated as a nonresident alien. As a result, these taxpayers are not subject to section 6048 reporting for the portion of the year during which they are treated as nonresident aliens for purposes of computing their U.S. income tax liability.

2. Reporting by all U.S. Transferors and Recipients

Section 6048(d)(1) provides that, ''For purposes of [section 6048], 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.'' The Treasury Department and the IRS are of the view that it is necessary to receive information about transfers to, and distributions from, foreign grantor trusts with regard to all U.S. transferors and U.S. recipients, including the U.S. owner, in order to administer the foreign trust provisions and to determine a taxpayer's U.S. tax liability with respect to foreign trusts. For example, the IRS uses this information to determine whether the transferor should be treated as the owner of the foreign trust, the value of the foreign trust's corpus at the end of the year for purposes of assessing penalties under section 6677, and the tax consequences of distributions in later years, such as distributions of corpus or UNI, if the foreign trust becomes a nongrantor trust (because, for example, the grantor dies). Therefore, proposed § 1.6048–6(b) clarifies that, pursuant to section 6048(d)(1), a transfer to, or a distribution from, a foreign trust is reportable under section 6048(a) and (c) and the proposed regulations without regard to whether the trust is a grantor trust or a nongrantor trust, and whether or not there are any U.S. income tax consequences associated with the transfer or distribution.

3. Domestic Trust With Substantial Foreign Activities or Assets

Proposed § 1.6048–6(c) is reserved for rules under section 6048(d)(2). Section 6048(d)(2) provides that, to the extent provided in regulations, a domestic trust is treated as a foreign trust for purposes of sections 6048 and 6677 if the trust has substantial activities, or holds substantial property, outside the United States. See section III.D.4 of the Background.

4. Joint Filers

Proposed § 1.6048–6(d) provides that married U.S. persons, each of whom is subject to the information reporting requirements under proposed § 1.6048–2(a) (as a grantor or transferor required to file Part I of Form 3520), proposed § 1.6048–3(a)(2) (as a U.S. owner of a foreign trust required to file a substitute Form 3520–A), or proposed § 1.6048–4(a) (as a U.S. recipient of a distribution from a foreign trust required to file Part III of Form 3520) for the same foreign trust, may file one Form 3520 for purposes of proposed §§ 1.6048–2 through 1.6048–4, but only if they file a joint income tax return under section 6013 for the tax year for which reporting is required.

V. Section 6677—Civil Penalties for Failure To File Information With Respect to Certain Foreign Trusts

Proposed § 1.6677–1 provides rules for civil penalties that may be assessed if any notice or return required to be filed under proposed §§ 1.6048–2 through 1.6048–4 is not timely filed or contains incomplete or incorrect information. The proposed regulations provide for three separate civil penalties that correspond to each separate reporting requirement under proposed § 1.6048–2, § 1.6048–3, and § 1.6048–4. The Treasury Department and the IRS interpret section 6677 as assessing a penalty based on a percentage of a gross reportable amount, a term that is defined separately under section 6677(c) and in the proposed regulations with respect to each corresponding section 6048 reporting requirement. This interpretation is consistent with the plain text of sections 6048 and 6677 and the purpose of the 1996 Act's modifications to these sections, which is to discourage U.S. persons from using foreign trusts to avoid their U.S. tax obligations.

A. General Rules

Proposed § 1.6677–1(a)(1) provides that, as a general rule, a person who fails to timely file a required notice or return, or fails to provide complete and correct information, is subject to a penalty equal to the greater of $10,000 or 35 percent of the applicable gross reportable amount (defined in proposed § 1.6677–1(c)) for each such failure (or for each year, in the case of a failure under proposed § 1.6048–3 relating to information reporting about U.S. owners of foreign trusts). If a person reports an amount that is less than the gross reportable amount, the penalty is based on the amount that is unreported.

Proposed § 1.6677–1(a)(2) provides that, if the failure to comply with the applicable reporting requirement continues for more than 90 days after the day on which the IRS mails notice of the failure to the U.S. person required to pay the penalty, the person is required to pay an additional penalty of $10,000 for each 30-day period (or fraction thereof) during which the failure continues.

Proposed § 1.6677–1(a)(3)(i) addresses maximum penalties. Proposed § 1.6677–1(a)(3)(i) provides that the aggregate amount of the penalties imposed by proposed § 1.6677–1(a)(1) and (2) (as modified by proposed § 1.6677–1(b), if applicable) with respect to any single failure may not exceed the gross reportable amount with respect to that failure (provided that the IRS receives

enough information to accurately determine the gross reportable amount). In some cases, the IRS can begin to assess penalties before it has received enough information to determine the gross reportable amount. If the aggregate amount of the penalty collected exceeds the applicable gross reportable amount (because the penalty was assessed and collected before the IRS was able to determine the gross reportable amount), the IRS will refund the excess amount pursuant to section 6402.

Proposed § 1.6677–1(a)(3)(ii) provides that the limitations period for claims for refund under section 6511(a) and (b) applies to the refund of any excess amount.

B. Failures To Comply With Proposed § 1.6048–3

Proposed § 1.6677–1(b) makes two modifications to the rules of proposed § 1.6677–1(a) in the case of a notice or return required to be filed under proposed § 1.6048–3 (relating to information reporting about U.S. owners of foreign trusts). First, in the case of a notice or return required to be filed by a foreign trust under proposed § 1.6048–3(a), the U.S. owner, rather than the foreign trust, must pay the penalty. Second, the amount of any penalty that initially is imposed under proposed § 1.6677–1(a)(1) is the greater of $10,000 or five percent (rather than 35 percent) of the gross reportable amount.

C. Gross Reportable Amount

Proposed § 1.6677–1(c)(1) provides that the term *gross reportable amount* means (i) the gross value of the property involved in the reportable event (determined as of the date of the event) in the case of a failure relating to proposed § 1.6048–2, (ii) the gross value of the portion of the foreign trust's assets (at the close of the trust's taxable year) treated as owned by the U.S. person in the case of a failure relating to proposed § 1.6048–3, and (iii) the gross amount of the distribution or deemed distribution in the case of a failure relating to proposed § 1.6048–4. Proposed § 1.6677–1(c)(2) provides guidance on how to determine the gross value or gross amount of property for purposes of proposed § 1.6677–1(c)(1).

D. Reasonable Cause

Proposed § 1.6677–1(d) provides that the penalty does not apply if the person required to file the notice or return (including a U.S. person who is treated as an owner of a foreign trust that fails to comply with proposed § 1.6048–3(b)) shows that the failure to file is due to reasonable cause and not due to willful neglect. The determination of whether a failure is due to reasonable cause and not due to willful neglect will be made under the principles set out in § 1.6664–4 and § 301.6651–1(c) and will be made on a case-by-case basis, taking into account all pertinent facts and circumstances. The fact that a foreign jurisdiction would impose a civil or criminal penalty on any person for disclosing the required information will not satisfy the reasonable cause exception. In addition, refusal on the part of a foreign trustee to provide information for any reason, including difficulty in producing the required information or the existence of provisions in the trust instrument that prevent the disclosure of required information, does not constitute reasonable cause.

E. Inapplicability of Deficiency Procedures

Proposed § 1.6677–1(e) provides that deficiency procedures do not apply in the case of the assessment or collection of a penalty imposed under section 6677.

F. Joint Filers

Proposed § 1.6677–1(f)(1) provides that married U.S. persons who jointly file Form 3520 for purposes of proposed §§ 1.6048–2 through 1.6048–4 and jointly file an income tax return under section 6013 (as described section IV.E of this Explanation of Provisions) are treated as a single U.S. person for purposes of assessing section 6677 penalties.

In addition, proposed § 1.6677–1(f)(2) provides that the IRS may treat married U.S. persons who file a joint income tax return under section 6013, but who did not file an information return as required under §§ 1.6048–2 through 1.6048–4, as a single U.S. person for purposes of assessing section 6677 penalties, unless the IRS determines that, based on all the facts and circumstances, only one of the spouses was subject to the information reporting requirement (for example, because only one spouse had an interest in the property constituting the transfer to, or receipt from, a foreign trust). In these cases, it can be difficult for the IRS to determine who, between spouses, should be treated as the transferor, grantor, or owner of, or the recipient of a distribution from, a foreign trust (because, for example, a transfer of property to, or the receipt of property from, a foreign trust was made from (or to) a joint bank account). By enabling the IRS to assess section 6677 penalties on a joint and several basis against married U.S persons who do not file information returns required under section 6048, proposed § 1.6677–1(f)(2) allows the IRS to properly enforce section 6048, while still allowing each spouse to demonstrate that they should not be jointly and severally liable for the section 6677 penalties assessed (for example, because one spouse did not have an interest in the underlying property giving rise to a reporting requirement under proposed §§ 1.6048–2 through 1.6048–4).

The liability of married U.S. persons treated as a single person is joint and several pursuant to proposed § 1.6677–1(f)(3).

VI. Proposed Applicability Dates

These regulations are proposed to apply to transactions with foreign trusts and the receipt of foreign gifts in taxable years beginning after the date on which the final regulations are published in the **Federal Register**. However, a taxpayer may rely on these proposed regulations for any taxable year ending after May 8, 2024 and beginning on or before the date that final regulations are published in the **Federal Register**, provided that the taxpayer and all related persons (within the meaning of sections 267(b) and 707(b)(1)) apply the proposed regulations in their entirety and in a consistent manner for all taxable years beginning with the first taxable year of reliance until the applicability date of the final regulations.

Special Analyses

I. Regulatory Planning and Review—Economic Analysis

Pursuant to the Memorandum of Agreement, Review of Treasury Regulations under Executive Order 12866 (June 9, 2023), tax regulatory actions issued by the IRS are not subject to the requirements of section 6 of Executive Order 12866, as amended. Therefore, a regulatory impact assessment is not required.

II. Paperwork Reduction Act

The Paperwork Reduction Act of 1995 (44 U.S.C. 3501–3520) (*PRA*) generally requires that a Federal agency obtain the approval of the Office of Management and Budget (*OMB*) before collecting information from the public, whether such collection of information is mandatory, voluntary, or required to obtain or retain a benefit.

The estimated number of taxpayers impacted by these proposed regulations is 58,000. This is the number of taxpayers who currently file Form 3520 and Form 3520–A to report information required by sections 643(i), 679, 6039F, and 6048 as reflected under OMB

control numbers 1545–0074 (for individual filers), 1545–0123 (for business filers), and 1545–0159 (for trust and estate filers). However, the Treasury Department and the IRS estimate that 58,000 is the upper bound because the proposed regulations exempt certain taxpayers from information reporting under sections 6039F and 6048. See, *e.g.,* proposed §§ 1.6039F–1(c) and 1.6048–5.

The collections of information in the proposed regulations are in proposed §§ 1.643(i)–1(b)(2)(ii), 1.643(i)–1(c)(2)(ii), 1.679–2(d)(1), 1.679–4(d)(1)(ii), 1.6039F–1(a), 1.6039F–1(e), 1.6048–2(a), 1.6048–3(a), 1.6048–4(c), and 1.6677–1(d). In general, the collections of information contained in these proposed regulations are currently reflected in the collection of information for Form 3520 and Form 3520–A, which have been reviewed and approved by the OMB in accordance with the PRA under control numbers 1545–0074 (for individual filers), 1545–0123 (for business filers), and 1545–0159 (for trust and estate filers). Thus, the burden estimates for OMB control numbers 1545–0074, 1545–0123, and 1545–0159 will be updated to reflect the collections of information associated with the proposed regulations.

An agency may not conduct or sponsor and a person is not required to respond to a collection of information unless it displays a valid OMB control number.

III. Regulatory Flexibility Act

When an agency issues a rulemaking proposal, the Regulatory Flexibility Act (5 U.S.C. chapter 6) (*RFA*) requires the agency ''to prepare and make available for public comment an initial regulatory flexibility analysis'' that will ''describe the impact of the proposed rule on small entities.'' See 5 U.S.C. 603(a). Section 605 of the RFA provides an exception to this requirement if the agency certifies that the proposed rulemaking will not have a significant economic impact on a substantial number of small entities. A small entity is defined as a small business, small nonprofit organization, or small governmental jurisdiction. See 5 U.S.C. 601(3) through (6).

The Treasury Department and the IRS do not expect the proposed regulations to have a significant economic impact on a substantial number of small entities within the meaning of sections 601(3) through 601(6) of the RFA. The proposed regulations generally reflect the existing collection of information requirements for Form 3520 and Form 3520–A. However, because the proposed regulations generally apply to any U.S. person, including small entities, that engage in certain transactions with foreign trusts or receive large foreign gifts, an initial regulatory flexibility analysis has been prepared for this notice of proposed rulemaking under 5 U.S.C. chapter 6 and is provided below. The Treasury Department and the IRS request comments on the number of small entities that may be impacted and whether that impact will be economically significant.

A. Statement of the Need for, and Objectives of, the Proposed Regulations

As discussed in the Background and Explanation of Provisions, the proposed regulations implement sections 643(i), 679, 6039F, 6048 and 6677 (the *foreign trust and gift provisions*), which were added to the Code or significantly modified to address the use of foreign trusts and similar offshore arrangements by United States persons to avoid U.S. tax. These provisions also enhance the IRS's ability to obtain information regarding these offshore arrangements, including the receipt of large foreign gifts by United States persons. The proposed regulations address potential uncertainty under current law, including the necessary requirements for complying with the foreign trust and gift provisions, and the relevant tax consequences and potential penalties for compliance failures.

B. Small Entities To Which the Proposed Regulations Will Apply

The proposed regulations generally define a United States person using the definition in section 7701(a)(30), which includes domestic partnerships and domestic corporations, subject to exceptions for certain entities that are exempt from taxation under chapter 1 of the Code. See, *e.g.,* proposed §§ 1.643(i)–1(d)(12), 1.679–1(c)(2), 1.6039F–1(a), and 1.6048–1(b)(7). Because the number of small businesses that file Form 3520 and Form 3520–A is reflected in the taxpayer compliance burden provided for U.S. business income tax returns under OMB 1545–0123, an estimate of the number of small businesses affected by the proposed regulations is not currently feasible, and, therefore, this initial regulatory flexibility analysis assumes that a substantial number of small businesses will be affected. The Treasury Department and the IRS do not expect that the proposed regulations will affect a substantial number of small nonprofit organizations or small governmental jurisdictions.

C. Projected Reporting, Recordkeeping, and Other Compliance Requirements

The proposed regulations generally do not impose additional reporting, recordkeeping, or other compliance obligations. The proposed regulations are substantially similar to the existing guidance in Notice 97–34, Revenue Procedure 2014–55, and Revenue Procedure 2020–17 and the existing instructions to Form 3520 and Form 3520–A. The proposed regulations include certain limited clarifications to the existing guidance and also provide additional taxpayer relief, including with respect to small entities. Moreover, even without the proposed regulations, small entities would continue to be required to file Form 3520 or Form 3520–A to comply with the statutory requirements. Therefore, these regulations generally are not expected to impose new compliance burdens, other than the time necessary for small entities to read the proposed regulations.

D. Duplicate, Overlapping, or Relevant Federal Rules

The Treasury Department and the IRS are not aware of any Federal rules that duplicate, overlap, or conflict with the proposed regulations.

E. Alternatives Considered

The foreign trust and gift provisions apply to any United States person, and the statutes do not establish different rules for small entities. Because the foreign trust and gift provisions are intended to address the use of foreign trusts and similar arrangements to avoid U.S. tax, which can be structured using large and small business entities, the Treasury Department and the IRS are of the view that the proposed regulations should apply uniformly to all business entities. The Treasury Department and the IRS did not consider any significant alternatives. The proposed regulations address potential uncertainty under current law without imposing additional economic burdens on these entities. Therefore, the proposed regulations adopt the approach with the least economic impact.

IV. Section 7805(f)

Pursuant to section 7805(f) of the Internal Revenue Code, this regulation will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

V. Unfunded Mandates Reform Act

Section 202 of the Unfunded Mandates Reform Act of 1995 requires that agencies assess anticipated costs

and benefits and take certain other actions before issuing a final rule that includes any Federal mandate that may result in expenditures in any one year by a State, local, or Tribal government, in the aggregate, or by the private sector, of $100 million in 1995 dollars, updated annually for inflation. The proposed regulations do not include any Federal mandate that may result in expenditures by State, local, or Tribal governments, or by the private sector in excess of that threshold.

VI. Executive Order 13132: Federalism

Executive Order 13132 (entitled *Federalism*) prohibits an agency from publishing any rule that has federalism implications if the rule either imposes substantial, direct compliance costs on State and local governments, and is not required by statute, or preempts State law, unless the agency meets the consultation and funding requirements of section 6 of the Executive Order. The proposed regulations do not have federalism implications, do not impose substantial direct compliance costs on State and local governments, and do not preempt State law within the meaning of the Executive order.

Comments and Requests for a Public Hearing

Before these proposed amendments to the regulations are adopted as final regulations, consideration will be given to any comments regarding the notice of proposed rulemaking that are submitted timely to the IRS, as prescribed in this preamble under the ''Addresses'' heading. The Treasury Department and the IRS request comments on all aspects of the proposed rules. Comments are specifically requested in Section I.B. of the Explanation of Provisions, regarding whether qualified obligation rules are needed for loans of marketable securities and regarding the scope and application of the exception from section 643(i) distribution treatment for certain loans made by a foreign corporation. All comments will be made available at *www.regulations.gov.* Once submitted to the Federal eRulemaking Portal, comments cannot be edited or withdrawn.

A public hearing has been scheduled for August 21, 2024, at 10 a.m. ET, in the Auditorium at the Internal Revenue Building, 1111 Constitution Avenue NW, Washington, DC. Due to building security procedures, visitors must enter at the Constitution Avenue entrance. In addition, all visitors must present photo identification to enter the building. Because of access restrictions, visitors will not be admitted beyond the immediate entrance area more than 30 minutes before the hearing starts. Participants may alternatively attend the public hearing by telephone.

The rules of 26 CFR 601.601(a)(3) apply to the hearing. Persons who wish to present oral comments at the hearing must submit an outline of the topics to be discussed and the time to be devoted to each topic by July 8, 2024. Outlines must be submitted electronically via the Federal eRulemaking Portal at *www.regulations.gov* (indicate IRS and REG–124850–08). A period of 10 minutes will be allotted to each person for making comments. An agenda showing the scheduling of the speakers will be prepared after the deadline for receiving outlines has passed. Copies of the agenda will be available free of charge at the hearing. If no outline of the topics to be discussed at the hearing is received by July 8, 2024, the public hearing will be cancelled. If the public hearing is cancelled, a notice of cancellation of the public hearing will be published in the **Federal Register**.

Individuals who want to testify in person at the public hearing must send an email to *publichearings@irs.gov* to have your name added to the building access list. The subject line of the email must contain the regulation number REG–124850–08 and the language TESTIFY in Person. For example, the subject line may say: Request to TESTIFY in Person at Hearing for REG–124850–08.

Individuals who want to testify by telephone at the public hearing must send an email to *publichearings@irs.gov* to receive the telephone number and access code for the hearing. The subject line of the email must contain the regulation number REG–124850–08 and the language TESTIFY Telephonically. For example, the subject line may say: Request to TESTIFY Telephonically at Hearing for REG–124850–08.

Individuals who want to attend the public hearing in person without testifying must also send an email to *publichearings@irs.gov* to have your name added to the building access list. The subject line of the email must contain the regulation number REG–124850–08 and the language ATTEND In Person. For example, the subject line may say: Request to ATTEND Hearing in Person for REG–124850–08. Requests to attend the public hearing must be received by 5:00 p.m. ET on August 19, 2024.

Hearings will be made accessible to people with disabilities. To request special assistance during a hearing please contact the Publications and Regulations Branch of the Office of Associate Chief Counsel (Procedure and Administration) by sending an email to *publichearings@irs.gov* (preferred) or by telephone at (202) 317–6901 (not a toll-free number) by at least August 16, 2024.

Statement of Availability of IRS Documents

IRS Revenue Procedures, Revenue Rulings, Notices and other guidance cited in this document are published in the Internal Revenue Bulletin or Cumulative Bulletin and are available from the Superintendent of Documents, U.S. Government Publishing Office, Washington, DC 20402, or by visiting the IRS website at *https://www.irs.gov.*

Drafting Information

The principal authors of these proposed regulations are Lara A. Banjanin, Tracy M. Villecco, and S. Eva Wolf of the Office of Associate Chief Counsel (International), and M. Grace Fleeman, formerly of the Office of Associate Chief Counsel (International). However, other personnel from the Treasury Department and the IRS participated in their development.

List of Subjects

26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

Proposed Amendments to the Regulations

Accordingly, the Treasury Department and IRS propose to amend 26 CFR part 1 as follows:

PART 1—INCOME TAXES

■ **Paragraph 1.** The authority citation for part 1 is amended by adding entries in numerical order and revising entries for §§ 1.679–1, 1.679–2, and 1.679–4 to read in part as follows:

Authority: 26 U.S.C. 7805 * * *

Section 1.643(i)–1 also issued under 26 U.S.C. 643.

Sections 1.643(i)–2 through 1.643(i)–4 also issued under 26 U.S.C. 643 and 6048.

Section 1.643(i)–5 also issued under 26 U.S.C. 643.

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Section 1.679–1 also issued under 26 U.S.C. 643 and 679.

Section 1.679–2 also issued under 26 U.S.C. 643 and 679.

Section 1.679–4 also issued under 26 U.S.C. 643 and 679.

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Section 1.6039F–1 also issued under 26 U.S.C. 6039F.

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Sections 1.6048–1 through 1.6048–6 also issued under 26 U.S.C. 643 and 6048.

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Section 1.6677–1 also issued under 26 U.S.C. 643 and 6048.

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■ **Par. 2.** Sections 1.643(i)–1, 1.643(i)–2, 1.643(i)–3, 1.643(i)–4, and 1.643(i)–5 are added to read as follows:

§ 1.643(i)–1 Loans from and use of trust property of foreign nongrantor trusts.

(a) *Loans and use of trust property*—(1) *In general.* For purposes of subparts B, C, and D of part I of subchapter J of chapter 1 of the Internal Revenue Code, a loan or use of trust property described in paragraph (b) or (c) of this section is treated as a section 643(i) distribution from a foreign trust to a U.S. grantor or beneficiary of the foreign trust under subchapter J of chapter 1 of the Internal Revenue Code, as provided in such paragraphs. Paragraph (d) of this section provides definitions for this section and §§ 1.643(i)–2 through 1.643(i)–5. Section 1.643(i)–2 provides exceptions to the general rules of this section. Section 1.643(i)–3 provides rules relating to the determination of the amount treated as a section 643(i) distribution and the tax consequences of a section 643(i) distribution. Section 1.643(i)–4 provides examples, and § 1.643(i)–5 provides the applicability date for the rules in this section and §§ 1.643(i)–2 through 1.643(i)–4.

(2) *Interaction with section 6048(c).* For rules relating to information reporting of loans from foreign trusts and the use of property of a foreign trust, see § 1.6048–4. That provision applies without regard to whether the loan or use of property is treated as a section 643(i) distribution or has any other tax consequences, and without regard to whether the foreign trust is a nongrantor or grantor trust.

(b) *Loan of cash or marketable securities from foreign nongrantor trust generally treated as a distribution*—(1) *In general.* Except as provided in § 1.643(i)–2, any direct or indirect loan of cash or marketable securities from a foreign nongrantor trust (whether from trust corpus or income) to any U.S. grantor or beneficiary of that trust or any U.S. person related to such a U.S. grantor or beneficiary is treated as a section 643(i) distribution to the U.S. grantor or beneficiary on the date such loan is made. For these purposes, a loan from a nongrantor trust to a grantor trust or to a disregarded entity is treated as a loan to the owner of the grantor trust or of the disregarded entity, respectively. For example, a loan to a single member LLC treated as a disregarded entity is treated as a loan to the owner of the LLC.

(2) *Indirect loans*—(i) *In general.* Except as provided in paragraph (b)(2)(ii) of this section, an indirect loan of cash or marketable securities from a foreign nongrantor trust includes a loan of cash or marketable securities made by an intermediary, agent, or nominee of the trust, as well as a loan made to an intermediary, agent, or nominee of a U.S. grantor or beneficiary or of a U.S. person related to a U.S. grantor or beneficiary. For example, such indirect loans include:

(A) Loans made by any person other than the trust to either a U.S. grantor or beneficiary of a foreign trust or any U.S. person related to a U.S. grantor or beneficiary if the foreign trust provides a guarantee (within the meaning of § 1.679–3(e)(4)) for the loan;

(B) Loans made by any person related to a foreign trust, to either a U.S. grantor or beneficiary of the trust, or a U.S. person related to a U.S. grantor or beneficiary; and

(C) Loans made by a foreign trust to a foreign person, other than to a nonresident alien individual grantor or beneficiary of the trust, if the foreign person is related to a U.S. grantor or beneficiary of the trust.

(ii) *Limitation.* The loans described in paragraphs (b)(2)(i)(B) and (b)(2)(i)(C) of this section will not be treated as a section 643(i) distribution if the U.S. grantor or beneficiary:

(A) Satisfies the information reporting requirements of § 1.6048–4 with respect to the loan, and

(B) Includes an explanatory statement attached to the U.S. grantor or beneficiary's Federal income tax return that demonstrates to the satisfaction of the Commissioner that the loan would have been made without regard to the fact that the U.S. grantor or beneficiary is a grantor or beneficiary of the foreign trust.

(iii) *Effect of indirect loans*—(A) *In general.* In the case of a loan described in paragraph (b)(2)(i)(A) or (B) of this section, the person making the loan is treated as an agent of the foreign trust.

(B) *Loans to a foreign person related to a U.S. grantor or beneficiary.* In the case of a loan described in paragraph (b)(2)(i)(C) of this section, the foreign person related to the U.S. grantor or beneficiary is treated as an agent of the U.S. grantor or beneficiary, and the date the loan is made to the foreign person is treated as the date the loan is made to the U.S. grantor or beneficiary.

(3) *Rule for nonresident alien individual grantors or beneficiaries of a foreign trust who become U.S. persons.* If a nonresident alien individual who is a grantor or beneficiary of a foreign trust receives a loan from the trust and, while the loan is outstanding, becomes a U.S. resident (within the meaning of section 7701(b)) or a U.S. citizen within two years after the date the loan was made, the loan will be treated as a section 643(i) distribution with respect to the outstanding amount of the loan as of the date the individual acquires U.S. residence or citizenship unless an exception described in § 1.643(i)–2 applies.

(c) *Use of trust property generally treated as a distribution*—(1) *In general.* Except as provided in § 1.643(i)–2, any direct or indirect use of property of a foreign trust, other than a loan of cash or marketable securities, by any U.S. grantor or beneficiary of the trust or any U.S. person related to a U.S. grantor or beneficiary is treated as a section 643(i) distribution to the U.S. grantor or beneficiary in the taxable year in which the use occurs. For these purposes, use of property of a nongrantor trust by a grantor trust or by a disregarded entity is treated as use by the owner of the grantor trust or of the disregarded entity, respectively. For example, use of trust property by a single member LLC treated as a disregarded entity would be treated as use by the owner of the LLC.

(2) *Indirect use of trust property*—(i) *In general.* Indirect use of property of a foreign trust includes use by an agent or nominee of a U.S. grantor or beneficiary of the trust or an agent or nominee of a U.S. person related to a U.S. grantor or beneficiary. Indirect use of trust property also includes use by a foreign person, other than a nonresident alien individual beneficiary of the trust, if the foreign person is related to a U.S. grantor or beneficiary of the trust, unless paragraph (c)(2)(ii) of this section applies.

(ii) *Limitation.* The use of trust property described in the second sentence of paragraph (c)(2)(i) of this section is not treated as a section 643(i) distribution to the U.S. grantor or beneficiary if the U.S. grantor or beneficiary:

(A) Satisfies the information reporting requirements of § 1.6048–4 with respect to the use; and

(B) Includes an explanatory statement attached to the U.S. grantor's or beneficiary's Federal income tax return that demonstrates to the satisfaction of the Commissioner that the use of trust property would have been allowed without regard to the fact that the U.S. grantor or beneficiary is a grantor or beneficiary of the foreign trust.

(iii) *Effect of indirect use of trust property.* In the case of the use of trust property by a foreign person related to the U.S. grantor or beneficiary described in paragraph (c)(2)(i) of this section, such foreign person is treated as an agent of the U.S. grantor or beneficiary.

(d) *Definitions.* The following definitions apply for purposes of this section and §§ 1.643(i)–2 through 1.643(i)–5:

(1) *Beneficiary.* The term *beneficiary* means a person to whom or for whose benefit, under the terms of the trust instrument or applicable local law, at any time during the term of the trust or upon termination, trust income or corpus may be paid (including pursuant to a power of appointment that has been exercised in favor of that person) or accumulated, directly or indirectly. All references to a U.S. beneficiary mean a beneficiary who is a U.S. person.

(2) *Cash.* The term *cash* includes foreign currencies and cash equivalents.

(3) *Disregarded entity.* The term *disregarded entity* means an entity that, under §§ 301.7701–1 through 301.7701–3 of this chapter, is disregarded as an entity separate from its owner.

(4) *Foreign person.* The term *foreign person* means any person who is not a U.S. person within the meaning of section 7701(a)(30).

(5) *Grantor trust.* The term *grantor trust* means a trust or any portion of a trust that is treated as owned by any person under subpart E of part I of subchapter J of chapter 1 of the Internal Revenue Code.

(6) *Loan of cash.* Except as provided in § 1.643(i)–2(a)(1), the term *loan of cash* includes an extension of credit.

(7) *Marketable securities.* The term *marketable securities* means marketable securities within the meaning of section 731(c)(2)(A), but not including foreign currencies.

(8) *Nongrantor trust.* The term *nongrantor trust* means a trust or any portion of a trust that is not treated as owned by any person under subpart E of part I of subchapter J of chapter 1 of the Internal Revenue Code.

(9) *Related.* A person will be considered to be related to another person if the relationship between such persons would result in a disallowance of losses under section 267 or 707(b). In applying section 267 for purposes of the previous sentence, section 267(c)(4) is applied as if the family of an individual includes the spouses of the members of the individual's family.

(10) *Section 643(i) distribution.* The term *section 643(i) distribution* means a transaction described in paragraph (b) or (c) of this section.

(11) *U.S. grantor.* The term *U.S. grantor* means a U.S. person described in § 1.671–2(e).

(12) *U.S. person*—(i) *In general.* Subject to paragraph (d)(12)(ii) of this section, the term *U.S. person* means a United States person as defined in section 7701(a)(30) but does not include an entity that is exempt from tax under chapter 1 of the Internal Revenue Code.

(ii) *Special rules*—(A) *Dual resident taxpayers.* If a dual resident taxpayer (within the meaning of § 301.7701(b)–7(a)(1) of this chapter) computes U.S. income tax liability as a nonresident alien on the last day of the taxable year and complies with the filing requirements of § 301.7701(b)–7(b) and (c) of this chapter, the dual resident taxpayer is not treated as a U.S. person for purposes of section 643(i) with respect to the portion of the taxable year the dual resident taxpayer was treated as a nonresident alien for purposes of computing U.S. income tax liability.

(B) *Dual status taxpayers.* Except as provided in paragraph (b)(3) of this section, if a taxpayer abandons U.S. citizenship or residence during the tax year or acquires U.S. citizenship or residence during the taxable year as provided in § 1.6012–1(b)(2)(ii), the taxpayer is not treated as a U.S. person with respect to the portion of the taxable year the taxpayer was treated as a nonresident alien for purposes of computing U.S. income tax liability.

§ 1.643(i)–2 Exceptions

(a) *In general.* A loan of cash or use of trust property will not be treated as a section 643(i) distribution if the loan of cash or use of trust property is one of the following:

(1) *Loan of cash in exchange for a qualified obligation.* A loan of cash that is in exchange for a qualified obligation (within the meaning of paragraph (b)(2)(iii) of this section).

(2) *Compensated use of trust property*—(i) *In general.* Use of trust property, other than a loan of cash or marketable securities, to the extent that the trust is paid the fair market value of such use within a reasonable period from the start of the use of the property. A determination as to the fair market value of the use of such property and as to whether a fair market value payment is made within a reasonable period must be based on all the facts and circumstances, including the type of property used and the period of use. In appropriate cases, such as rental of real property, payments may be made on a periodic basis consistent with arm's length dealings between unrelated parties.

(ii) *Safe harbor.* For purposes of paragraph (a)(2)(i) of this section, a payment is made within a reasonable period if the payment is made or periodic payments commence within 60 days of the start of the use of trust property.

(3) *De minimis use of trust property.* Use of trust property, other than a loan of cash or marketable securities, if such use is de minimis. Use of trust property will be considered de minimis if aggregate use by members of the group consisting of the U.S. grantors, U.S. beneficiaries, and the U.S. persons related to any U.S. grantor or beneficiary does not exceed 14 days during the calendar year.

(4) *Certain loans made by a foreign corporation.* A loan of cash that is made by a foreign corporation to a U.S. beneficiary of the foreign trust to the extent the aggregate amount of all such loans to the beneficiary does not exceed undistributed earnings and profits of the foreign corporation attributable to amounts that are, or have been, included in the beneficiary's gross income under section 951, 951A, or 1293.

(b) *Qualified obligations*—(1) *In general.* The rules in this paragraph (b) apply to determine whether a loan of cash is in exchange for a qualified obligation.

(2) *Definitions.* The following definitions apply for purposes of this section and §§ 1.643(i)–1 and 1.643(i)–3 through 1.643(i)–5:

(i) *Obligation.* The term *obligation* means any instrument or contractual arrangement that constitutes indebtedness under general principles of Federal income tax law (for example, a bond, note, debenture, certificate, bill receivable, account receivable, note receivable, open account, or other evidence of indebtedness), and any annuity contract that would not otherwise be classified as indebtedness under general principles of Federal income tax law.

(ii) *Obligor.* The term *obligor* means the person who issues an obligation to a foreign trust in exchange for a loan of cash.

(iii) *Qualified obligation*—(A) *General requirements.* The term *qualified obligation* means an obligation that at all times satisfies all of the following requirements:

(*1*) The obligation is reduced to writing in an express written agreement.

(*2*) The term of the obligation does not exceed five years. For purposes of determining the term of an obligation, the obligation's maturity date is the last possible date that the obligation can be outstanding under the terms of the obligation.

(*3*) All payments on the obligation must be made in cash in U.S. dollars.

(*4*) The obligation is issued at par and provides for stated interest at a fixed rate or a qualified floating rate within the meaning of § 1.1275–5(b).

(*5*) The yield to maturity of the obligation is not less than 100 percent

of the applicable Federal rate and not greater than 130 percent of the applicable Federal rate. The applicable Federal rate for an obligation is the applicable Federal rate in effect under section 1274(d) for the day on which the obligation is issued, as published in the Internal Revenue Bulletin (see § 601.601(d)(2) of this chapter). The yield to maturity and the applicable Federal rate must be based on the same compounding period. If an obligation is a variable rate debt instrument that provides for stated interest at a qualified floating rate, the equivalent fixed rate debt instrument rules in § 1.1274–2(f)(1) or § 1.1275–5(e), whichever is applicable, apply to determine the obligation's yield to maturity.

(*6*) All stated interest on the obligation is qualified stated interest within the meaning of § 1.1273–1(c).

(B) *Additional requirements to remain a qualified obligation.* An obligation will remain a qualified obligation only if, for the first year and each succeeding year that the obligation remains outstanding, the following requirements are satisfied:

(*1*) The U.S. grantor or beneficiary timely extends the period for assessment of any income tax attributable to the obligation and any consequent income tax changes for each year that the obligation is outstanding to a date not earlier than three years after the maturity date of the obligation. This extension of the period for assessment is not necessary with respect to the taxable year of the U.S. grantor or beneficiary in which the maturity date of the obligation falls, provided that the obligation is paid in cash in U.S. dollars within that year. The period of assessment is extended by completing and filing Part III of Form 3520, *Annual Return to Report Transactions with Foreign Trusts and Receipt of Certain Foreign Gifts,* for every year that the obligation is outstanding. The waiver in Part III of Form 3520 shall also contain such other terms with respect to assessment as may be considered necessary by the Commissioner to ensure the assessment and collection of the correct tax liability for each year for which the waiver is required. When Part III of Form 3520 is properly executed and filed, the consent to extend the period for assessment of tax will be deemed to be agreed upon and executed by the Commissioner for purposes of § 301.6501(c)–1(d).

(*2*) The U.S. grantor or beneficiary timely reports the status of the obligation, including principal and interest payments, on Part III of Form 3520 for each year that the obligation is outstanding.

(*3*) The obligor timely makes all payments of principal and interest on the obligation according to the terms of the obligation (which may include a reasonable grace period of no more than thirty days for a late payment).

(3) *Modification of a qualified obligation.* If the terms of a qualified obligation are modified and the modification is treated as an exchange under § 1.1001–3, the new obligation that is deemed issued in the exchange under § 1.1001–3 must satisfy all the requirements in paragraph (b)(2)(iii) of this section to be a qualified obligation using the original obligation's issue date. If the modification is not treated as an exchange under § 1.1001–3, then the obligation must be retested as of the date of the modification to determine whether the obligation, as modified, continues to satisfy the requirements in paragraph (b)(2)(iii) of this section to be a qualified obligation.

(4) *Additional loans.* If a qualified obligation is outstanding and the obligor directly or indirectly issues an additional obligation to the foreign trust in exchange for cash, the outstanding obligation is deemed to have the maturity date of the additional obligation in determining whether the outstanding obligation exceeds the specified five-year term. The outstanding obligation must be retested as of the issue date of the additional obligation to determine whether it would have satisfied, as of the outstanding obligation's issue date, all the requirements in paragraph (b)(2)(iii) of this section to be a qualified obligation. If there is more than one qualified obligation outstanding, the determination is made based on the outstanding obligation with the earliest issue date. The additional obligation also must be separately tested to see if it satisfies the requirements in paragraph (b)(2)(iii) of this section to be a qualified obligation.

(5) *Anti-abuse rule.* Notwithstanding paragraphs (b)(3) and (4) of this section, if the Commissioner determines, based on all of the facts and circumstances, that two or more obligations issued by a U.S. obligor are structured with a principal purpose to avoid the application of section 643(i), the Commissioner may treat the obligations as a single obligation that is not a qualified obligation.

(6) *Obligations that cease to be qualified*—(i) *In general.* If an obligation ceases to be a qualified obligation (for example, because an obligation is modified so that the term of the obligation exceeds 5 years), the U.S. grantor or beneficiary is treated as receiving a section 643(i) distribution from the trust.

(ii) *Amount of section 643(i) distribution.* Except as otherwise provided in this paragraph (b)(6)(ii), the amount of the section 643(i) distribution treated as received pursuant to paragraph (b)(6)(i) of this section is equal to the obligation's outstanding stated principal amount plus any accrued but unpaid qualified stated interest (within the meaning of § 1.1273–1(c)) as of the date of the event that causes the obligation to no longer be a qualified obligation. In the case of an obligation that ceases to be a qualified obligation because the Commissioner treats two or more obligations as a single obligation pursuant to paragraph (b)(5) of this section, the amount of the section 643(i) distribution will not exceed the sum of the outstanding stated principal amount plus any accrued but unpaid qualified stated interest on each of the obligations as of the date determined by the Commissioner under paragraph (b)(6)(iii) of this section.

(iii) *Date of section 643(i) distribution.* In general, the U.S. grantor or beneficiary is treated as receiving a section 643(i) distribution on the date of the event that causes an obligation to no longer be a qualified obligation. However, based on all of the facts and circumstances, if an obligation (or obligations) is structured with a principal purpose to avoid the application of section 643(i), the Commissioner may deem a section 643(i) distribution to have occurred on any date on or after the issue date of the obligation(s).

(c) *Trust property attributable to nongrantor trust portion*—(1) *In general.* A loan or use of trust property from a partial nongrantor trust must be apportioned between the nongrantor and grantor portions of the trust in a manner that is reasonable in light of all the facts and circumstances, including the terms of the governing instrument, local law, and the practice of the trustee if it is reasonable and consistent.

(2) *Specific property.* If a loan of cash or marketable securities, or a use of trust property, can be made from only one portion of the foreign trust because the type of property loaned or used is held only by that portion, then the loan or use of property is deemed to be attributable to that portion.

(d) *Reporting.* A loan of cash or marketable securities from, or the use of any property of, a foreign grantor or nongrantor trust to or by a U.S. person is a distribution for purposes of § 1.6048–4(b)(3) or (4), as applicable, and must be reported by the U.S.

person, and if the trust is a foreign nongrantor trust, by the U.S. grantor or beneficiary, under § 1.6048–4(a), irrespective of whether the loan or use of trust property is a section 643(i) distribution.

(e) *Examples.* The following examples illustrate the rules of paragraphs (b) through (d) of this section:

(1) *Example 1: Loan of cash not in exchange for qualified obligation.* Y, a nonresident alien, created and funded a foreign nongrantor trust, FT, for the benefit of X, a U.S. person. X is the sole beneficiary of FT. In Year 1, FT makes a loan of cash to X in exchange for a demand note that permits FT to require repayment by X at any time. The demand note issued by X is not a qualified obligation within the meaning of paragraph (b)(2)(iii) of this section because X's obligation to FT could remain outstanding for more than five years. Accordingly, the qualified obligation exception in paragraph (a)(1) of this section does not apply. Under § 1.643(i)–1(b) and § 1.643(i)–3(a), X is treated as receiving a section 643(i) distribution from FT. X must determine the tax consequences of the distribution under § 1.643(i)–3(c). Under § 1.6048–4(a), X is required to report the section 643(i) distribution on Part III of Form 3520 for Year 1, as a distribution from a foreign trust.

(2) *Example 2: Beneficiary fails to extend period of assessment and fails to report loan on Form 3520.* Y, a nonresident alien, created and funded a foreign nongrantor trust for the benefit of X, a U.S. person. On June 30, Year 1, FT makes a loan of cash to X in exchange for an obligation that satisfies the requirements of paragraph (b)(2)(iii)(A) of this section. However, X fails to timely file Form 3520 and did not request an extension to file. As a result, X has failed to extend the period for assessment of any income tax attributable to the loan through the filing of Form 3520 by its due date as required under paragraph (b)(2)(iii)(B)(*1*) of this section. X also has failed to report the status of the loan on Form 3520 as required under paragraph (b)(2)(iii)(B)(*2*) of this section. Either one of X's failures is sufficient to cause the loan to be treated as a section 643(i) distribution under § 1.643(i)–1(b). Because the loan fails to continue to be treated as a qualified obligation, the loan is treated as a section 643(i) distribution from FT as of April 15, Year 2, the date that X's Form 3520 was due.

(3) *Example 3: Effect of subsequent obligation on original obligation.* Y, a nonresident alien, created and funded a foreign nongrantor trust for the benefit of X, a U.S. person. On January 1, Year 1, FT makes a loan of cash to X in exchange for Note 1, an obligation with a maturity date of January 1, Year 6, that satisfies the requirements of paragraph (b)(2)(iii) of this section. On June 30, Year 1, FT makes an additional loan of cash to X in exchange for Note 2, an obligation with a maturity date of June 30, Year 6. Under paragraph (b)(4) of this section, Note 1 will be deemed to have a maturity date of June 30, Year 6 (*i.e.,* a greater than five-year term) and will cease to be a qualified obligation. Under paragraph (b)(6)(ii) of this section, X will be treated as receiving a section 643(i) distribution equal to Note 1's outstanding stated principal amount plus any accrued but unpaid qualified stated interest (within the meaning of § 1.1273–1(c)) as of June 30, Year 1. Note 2 will be separately tested to determine whether it satisfies the requirements of paragraph (b)(2)(iii) of this section.

(4) *Example 4: Anti-abuse rule.* Y, a nonresident alien, created and funded a foreign nongrantor trust for the benefit of X, a U.S. person. On January 1, Year 1, FT makes a loan of cash to X in exchange for Note 1, an obligation with a maturity date of January 1, Year 4 that satisfies the requirements of paragraph (b)(2)(iii) of this section. On January 1, Year 4, FT makes another loan of cash to X in exchange for Note 2, an obligation with a maturity date of January 1, Year 7, but otherwise has the same terms as Note 1. Based on all of the facts and circumstances, the Commissioner determines under paragraph (b)(5) of this section that Notes 1 and 2 are structured with a principal purpose to avoid the application of section 643(i). Therefore, under paragraph (b)(5) and paragraph (b)(6)(ii) and (iii) of this section, the Commissioner may treat Notes 1 and 2 as a single obligation (with a six-year term) that is not a qualified obligation and may treat X as receiving a section 643(i) distribution equal to the combined outstanding stated principal amounts of Note 1 and Note 2 plus any accrued but unpaid qualified stated interest as of any date determined by the Commissioner.

(5) *Example 5: Allocation of trust property attributable to partial grantor trust.* In Year 1, Y, a nonresident alien, creates and settles a foreign trust, FT, for the benefit of X, a U.S. beneficiary. Y funds the trust with a vacation home valued at $500,000 and $500,000 cash. Under the trust document, Y has the power to revoke the trust as to the vacation home and any income earned by the vacation home at any time without the consent of any person. This power to revoke results in Y being treated as the owner of the portion of the trust comprising the vacation home (the grantor trust portion) under section 676 (after application of § 1.672(f)–3(a)). Y has no powers that would cause Y to be treated as the owner of the portion of the trust comprising the cash Y contributed or any income earned by that cash. X uses the vacation home for 2 months in Year 2 and does not compensate the trust for the use of the vacation home. Under paragraph (c)(2) of this section, the use of the vacation home will be deemed to be attributable to the grantor trust portion and thus will not be treated as a section 643(i) distribution to X. Under paragraph (d) of this section, X must comply with the reporting requirements of § 1.6048–4 with respect to the use of the vacation home. Under § 1.6048–4(b)(4), X is required to report the use of the vacation home on Part III of Form 3520 for Year 2 as a distribution from FT.

§ 1.643(i)–3 Consequences of section 643(i) distribution.

(a) *Amount treated as section 643(i) distribution*—(1) *Loan of cash.* Except as provided otherwise, in the case of a loan of cash treated as a section 643(i) distribution, the amount of the section 643(i) distribution is the issue price of the loan, as determined under § 1.446–2(d)(1), § 1.1273–2 or § 1.1274–2 (whichever is applicable), as of the date (described in § 1.643(i)–2(b)(6)) the loan is treated as a section 643(i) distribution.

(2) *Loan of marketable securities.* In the case of a loan of marketable securities treated as a section 643(i) distribution, the amount of the section 643(i) distribution is the fair market value of the securities as of the date the loan is treated as a section 643(i) distribution.

(3) *Uncompensated use of trust property.* In the case of the use of trust property treated as a section 643(i) distribution, the amount of the section 643(i) distribution is the fair market value of the use of the property less the amount of any payments made within a reasonable period (described in § 1.643(i)–2(a)(2)) for the use of such property. The fair market value of the use of the property is based on all the facts and circumstances, including the type of property used and the period of use.

(b) *Allocation of section 643(i) distribution among multiple U.S. grantors and beneficiaries.* If a U.S. person who is not a U.S. grantor or beneficiary of a foreign trust but who is related to more than one U.S. grantor or beneficiary of the trust receives a loan of cash or marketable securities, or uses

trust property, that is treated as a section 643(i) distribution, then each U.S. grantor and beneficiary who is related to the U.S. person receiving the loan or using trust property is treated as receiving an equal share of the section 643(i) distribution. For purposes of this allocation, the term U.S. beneficiary includes only those beneficiaries who must or may receive a current distribution from the foreign trust.

(c) *Tax consequences of a section 643(i) distribution*—(1) *In general.* A U.S. grantor or beneficiary who is treated as receiving a section 643(i) distribution must determine the tax consequences of the distribution under either the actual calculation method (as defined in § 1.6048–4(d)(2)) or the default calculation method (as defined in § 1.6048–4(d)(3)). A U.S. grantor or beneficiary may not use the actual calculation method to determine the tax consequences of a section 643(i) distribution in a tax year in which the U.S. grantor or beneficiary has not received a Foreign Nongrantor Trust Beneficiary Statement (see § 1.6048–4(d)(2)) from the foreign trust before completing the U.S. grantor's or beneficiary's return, knows or has reason to know that the information in the Foreign Nongrantor Trust Beneficiary Statement is incorrect, or previously has used the default calculation method for the same trust. A U.S. grantor or beneficiary who previously has used the default calculation method must consistently use the default calculation method to determine the tax consequences of any subsequent distribution (within the meaning of § 1.6048–4(b)) from the same trust in all future years, except in the year in which the trust terminates. See § 1.6048–4(d)(3)(iii).

(2) *Consequences to foreign trust*—(i) *Treatment of amount under section 661(a)(2).* In the case of a section 643(i) distribution, regardless of whether a U.S. grantor or beneficiary uses the default calculation method or the actual calculation method of computing the tax consequences of a distribution, the foreign trust must treat the section 643(i) distribution as an amount properly paid, credited, or required to be distributed by the trust as described in section 661(a)(2).

(ii) *Distribution of marketable securities.* If the section 643(i) distribution is of marketable securities, the trust will be deemed to have made an election to have section 643(e)(3) apply with respect to all section 643(i) distributions of marketable securities made by the trust during the taxable year, and any resulting capital gain is included in the trust's distributable net income pursuant to section 643(a)(6)(C).

(iii) *Foreign Nongrantor Trust Beneficiary Statement.* The foreign trust may issue a Foreign Nongrantor Trust Beneficiary Statement (as described in § 1.6048–4(c)(2)) to each U.S. person who receives a loan of cash or marketable securities, or uses trust property other than a loan of cash or marketable securities, during the taxable year of the trust, without regard to whether a U.S. person would be required to take the amount of the loan or use of trust property into account as a section 643(i) distribution. If a U.S. person to whom a statement is issued is not a U.S. grantor or beneficiary but is related to a U.S. grantor or beneficiary, the foreign trust may issue a duplicate statement to the U.S. grantor or beneficiary.

(3) *Consequences to U.S. grantor or beneficiary*—(i) *Actual calculation method.* If a U.S. grantor or beneficiary is eligible to use, and uses, the actual calculation method, the U.S. grantor or beneficiary must treat a section 643(i) distribution as an amount properly paid, credited, or required to be distributed by the trust as described in section 662(a)(2) using information about the foreign trust as provided in the Foreign Nongrantor Trust Beneficiary Statement and applying the rules of subparts C and D of part I of subchapter J of chapter 1 of the Internal Revenue Code.

(ii) *Default calculation method.* Under the default calculation method, a U.S. grantor or beneficiary must apply the rules provided in § 1.6048–4(d)(3).

(d) *Subsequent transactions for loans or use of trust property*—(1) *In general.* Any subsequent transaction regarding the principal of any loan of cash or marketable securities treated as a section 643(i) distribution (including complete or partial repayment, satisfaction, cancellation, discharge, or otherwise, but not including the payment of interest) or the return of trust property the use of which was treated as a section 643(i) distribution has the consequences described in paragraphs (d)(2) and (3) of this section.

(2) *Consequences to foreign trust.* Any subsequent transaction regarding the principal of any loan of cash or marketable securities or the return of trust property treated as a section 643(i) distribution has no tax consequences to the trust. However, any payment to the trust other than the repayment of principal of any loan treated as a section 643(i) distribution, including the payment of interest, is treated as income to the trust.

(3) *Consequences to obligor*—(i) *In general.* Any subsequent transaction regarding the principal of any loan of cash or marketable securities or the return of trust property treated as a section 643(i) distribution is treated as a transfer that is not a gratuitous transfer by a U.S. person for purposes of § 1.671–2(e)(2)(i) and chapter 1 of the Internal Revenue Code.

(ii) *Satisfaction of loan with property.* Any transfer of property to a foreign trust in satisfaction of any amount due under a loan of cash or marketable securities treated as a section 643(i) distribution causes the obligor to recognize as gain or loss the difference between the fair market value of the property transferred and the adjusted basis of such property in the hands of the obligor in accordance with the rules of section 1001 and the regulations under section 1001 in this part.

§ 1.643(i)–4 Examples.

(a) *Scope.* The examples in this section illustrate the rules of §§ 1.643(i)–1 through 1.643(i)–3.

(b) *Example 1: Loan to contingent remainder beneficiary treated as loan to U.S. beneficiary.* Y, a nonresident alien, created and funded a foreign nongrantor trust, FT, for the benefit of Y's two children from Y's first marriage, A and B, who are both nonresident aliens. FT's governing trust instrument provides that, upon the death of the second to die of A and B, the trust may make a distribution to any of Y's surviving children, in the discretion of the trustee. In Year 1, X, a U.S. person who is Y's daughter from Y's second marriage, receives a loan of $100,000 from FT in exchange for an obligation that is not a qualified obligation within the meaning of § 1.643(i)–2(b)(2)(iii). Under § 1.643(i)–1(d)(1), X is a U.S. beneficiary of FT because X is a U.S. person to whom, at some point before the termination of the trust, the trust income or corpus may be paid at the discretion of the trustee. Under §§ 1.643(i)–1(b)(1) and 1.643(i)–3(a)(1), X is treated as receiving a section 643(i) distribution from FT in the amount of $100,000. X must determine the tax consequences of the distribution under § 1.643(i)–3(c). Under § 1.6048–4(a), X is required to report the section 643(i) distribution on Part III of Form 3520 for Year 1 as a distribution from a foreign trust.

(c) *Example 2: Loan from foreign nongrantor trust to a foreign grantor trust treated as section 643(i) distribution to U.S. owner.* The facts are the same as in paragraph (b) of this section (*Example 1*), except that instead of a loan to X, in Year 1, FT makes a loan of $100,000 to GT, a foreign grantor trust treated as wholly owned by X, in

exchange for an obligation that is not a qualified obligation within the meaning of § 1.643(i)–2(b)(2)(iii). Under § 1.643(i)–1(d)(1), X is a U.S. beneficiary of FT as explained in paragraph (b) of this section (*Example 1*). Under §§ 1.643(i)–1(b)(1) and 1.643(i)–3(a)(1), X, who is treated as the owner of GT, is treated as receiving a section 643(i) distribution from FT in the amount of $100,000. X must determine the tax consequences of the distribution under § 1.643(i)–3(c). Under § 1.6048–4(a), X is required to report the section 643(i) distribution on Part III of Form 3520 for Year 1 as a distribution from a foreign trust.

(d) *Example 3: Loan by a person related to a foreign nongrantor trust treated as a section 643(i) distribution.* X, a U.S. person, is a beneficiary of FT, a foreign nongrantor trust. FT owns 55% of the stock of FC, a foreign corporation that is not a controlled foreign corporation within the meaning of section 957 or a passive foreign investment company within the meaning of section 1297. FC is related to FT within the meaning of § 1.643(i)–1(d)(9). On January 2, Year 1, FC lends cash to X in exchange for an obligation that is not a qualified obligation within the meaning of § 1.643(i)–2(b)(2)(iii). Under § 1.643(i)–1(b)(2)(iii), FC is treated as the agent of FT with respect to the loan, and under § 1.643(i)–1(b)(1) and (2)(i), X is treated as receiving the loan from FT on January 2, Year 1. Nevertheless, under § 1.643(i)–1(b)(2)(ii), the loan is not treated as a section 643(i) distribution if X satisfies the reporting requirements of § 1.6048–4 and attaches a statement to X's income tax return that demonstrates to the satisfaction of the Commissioner that the loan would have been made without regard to X's relationship with FT. Otherwise, X is treated as receiving a section 643(i) distribution and must determine the tax consequences of the distribution under § 1.643(i)–3(c). Regardless of whether X claims the exception described in § 1.643(i)–1(b)(2)(ii), under § 1.6048–4(a), X is required to report the loan on Part III of Form 3520 for Year 1 as a distribution from a foreign trust.

(e) *Example 4: Guaranteed loan by an unrelated person treated as a section 643(i) distribution.* X is a U.S. beneficiary of FT, a foreign nongrantor trust. On January 2, Year 1, X borrows $100,000 from Bank in exchange for an obligation that is not a qualified obligation within the meaning of § 1.643(i)–2(b)(2)(iii), and FT provides a guarantee (within the meaning of § 1.679–3(e)(4)) for the loan. Under § 1.643(i)–1(b)(1) and (2)(i), X is treated as receiving a loan from FT on January 2, Year 1, in the amount of $100,000 because FT guaranteed the loan from Bank to X. On January 2, Year 1, X is treated as receiving a section 643(i) distribution. X must determine the tax consequences of the distribution under § 1.643(i)–3(c). Under § 1.6048–4(a), X is required to report the section 643(i) distribution on Part III of Form 3520 as a distribution from a foreign trust.

(f) *Example 5: Loan to a foreign person related to a U.S. beneficiary.* X is a U.S. beneficiary of FT, a foreign nongrantor trust. X is also the sole shareholder of CFC, a foreign corporation, treated as a controlled foreign corporation under section 957. On January 2, Year 1, FT lends $100,000 to CFC in exchange for an obligation that is not a qualified obligation within the meaning of § 1.643(i)–2(b)(2)(iii). CFC is related to X within the meaning of § 1.643(i)–1(d)(9). Under § 1.643(i)–1(b)(1) and (2)(i), X is treated as receiving a loan from FT on January 2, Year 1, in the amount of $100,000 because FT made the loan to CFC, a foreign person related to X. Under § 1.643(i)–1(b)(2)(ii), the loan is not treated as a section 643(i) distribution if X reports the loan consistent with the requirements of § 1.6048–4 and attaches a statement to X's income tax return that demonstrates to the satisfaction of the Commissioner that the loan from FT to CFC would have been made without regard to X's relationship with FT. Otherwise, X is treated as receiving a section 643(i) distribution and must determine the tax consequences of the distribution under § 1.643(i)–3(c). Regardless of whether X claims the limitation described in § 1.643(i)–1(b)(2)(ii), under § 1.6048–4(a), X is required to report the loan on Part III of Form 3520 for Year 1 as a distribution from a foreign trust.

(g) *Example 6: Loan to wholly owned corporation of U.S. beneficiary.* Y, a nonresident alien, created and funded a foreign nongrantor trust, FT, for the benefit of Y's child, X, a U.S. person. X is a U.S. beneficiary within the meaning of § 1.643(i)–1(d)(1). X wholly owns XYZ Corp, a domestic corporation. On July 1, Year 1, FT lends $100,000 to XYZ Corp in exchange for an obligation that is not a qualified obligation within the meaning of § 1.643(i)–2(b)(2)(iii). Under § 1.643(i)–1(d)(9) and (12), XYZ Corp is a U.S. person related to X. Under § 1.643(i)–1(b)(1) and (2)(i) and § 1.643(i)–3(a)(1), X is treated as receiving a section 643(i) distribution from FT in the amount of $100,000. X must determine the tax consequences of the distribution under § 1.643(i)–3(c). Under §§ 1.6048–4(a), X and XYZ Corp are required to report the loan on Part III of Form 3520 for Year 1 as a distribution from a foreign trust.

(h) *Example 7: Subsequent transactions with respect to loan treated as a section 643(i) distribution.* The facts are the same as in paragraph (g) of this section (*Example 6*). In Year 1, XYZ Corp makes a payment to FT that it characterizes in part as a partial repayment of principal and in part as interest on its obligation to FT. Under § 1.643(i)–3(d)(3)(i), the portion of the payment that is characterized as a repayment of principal will be treated as a transfer that is not a gratuitous transfer by a U.S. person for purposes of § 1.671–2(e)(2)(i) and chapter 1 of the Internal Revenue Code. Under § 1.643(i)–3(d)(2), the transfer of principal will have no tax consequences to FT. Furthermore, under § 1.643(i)–3(d)(2), the portion of the payment that is characterized as interest by XYZ Corp will be treated as income to FT.

(i) *Example 8: Uncompensated use of trust property.* Y, a nonresident alien, created and funded a foreign nongrantor trust, FT, for the benefit of Y's daughter, A, a U.S. person. A is a U.S. beneficiary of FT within the meaning of § 1.643(i)–1(d)(1). FT owns real property that could be rented to an unrelated person at fair market value for $10,000 a month. During all of Year 1, A lives in the property rent-free. Under §§ 1.643(i)–1(c) and § 1.643(i)–3(a)(3), A is treated as receiving a section 643(i) distribution from FT in Year 1 in the amount of $120,000 ($12 \times $10,000). A must determine the tax consequences of the distribution under § 1.643(i)–3(c). Under § 1.6048–4(a), A must report the section 643(i) distribution on Part III of Form 3520 for Year 1 as a distribution from FT.

(j) *Example 9: Partially compensated use of trust property.* The facts are the same as in paragraph (i) of this section (*Example 8*) except that A pays FT $2,000 on the first of each month for the use of the property even though the fair market value is $10,000. Under §§ 1.643(i)–1(c), 1.643(i)–2(a)(2), and 1.643(i)–3(a)(3), A is treated as receiving a section 643(i) distribution in Year 1 from FT in the amount of $96,000 ($12 \times ($10,000 - $2,000)$). A must determine the tax consequences of the distribution under § 1.643(i)–3(c). Under §§ 1.6048–4(a), A must report the entire fair market value of $120,000 on Part III of Form 3520 for Year 1 as a distribution from FT even through only a portion of the fair market value is treated as a section 643(i) distribution due to partial compensation.

(k) *Example 10: Uncompensated use of trust property treated as distribution*

from accumulated income. On January 1, Year 1, Y, a nonresident alien, creates and funds a foreign nongrantor trust, FT, for the benefit of Y's son, X, a U.S. person. X is a U.S. beneficiary of FT within the meaning of § 1.643(i)–1(d)(1). FT has $60,000 of distributable net income (DNI), as defined under section 643(a), in Year 1, $80,000 of DNI in Year 2, and $90,000 of DNI in Year 3. FT has never made any distributions. FT owns real property that could be rented to an unrelated person for $10,000 a month. During all of Year 3, X occupies the property rent free. Under § 1.643(i)–1(c) and § 1.643(i)–3(a)(3), X is treated as receiving a section 643(i) distribution from FT in Year 3 in the amount of $120,000, the fair market value use of the trust property (12 × $10,000). Under § 1.6048–4(a), X must report the section 643(i) distribution on Part III of Form 3520 for Year 3 as a distribution from FT. X receives a Foreign Nongrantor Trust Beneficiary Statement from FT and uses the actual calculation method under § 1.643(i)–3(c)(3)(i) to determine the tax consequences of the section 643(i) distribution. The $120,000 is treated as an amount properly paid, credited, or required to be distributed by the trust as described in section 662(a)(2). As a result of X's uncompensated use of FT's property, X's section 643(i) distribution consists of a distribution of DNI of $90,000 (FT's DNI in Year 3) and an accumulation distribution of $30,000 under subpart D of subchapter J of chapter 1 of the Internal Revenue Code.

(l) *Example 11: Use of property of partial grantor trust not treated as section 643(i) distribution.* X and Y are married. X is a U.S. person and Y is a nonresident alien. X and Y have three children, A, B, and C. A and B are both nonresident aliens. C is a U.S. person. In Year 1, X and Y created a foreign trust, FT, for the benefit of A and B to which X contributed a vacation home and Y contributed cash and securities. Neither X nor Y retained any powers described in sections 673 through 677. In Year 2, C lived in the vacation home rent free. Although C is not a beneficiary of FT under the terms of the trust, under § 1.679–2(a)(5), C's uncompensated use of the vacation home causes FT to be treated as having a U.S. beneficiary. Thus, under § 1.679–1(a), X will be treated as the owner of the portion of FT attributable to the vacation home. Under § 1.643(i)–2(c)(2), C's use of the vacation home will be treated as the use of property from the grantor trust portion of FT. C will not be treated as receiving a section 643(i) distribution. Under §§ 1.6048–4(a), C must report the use of the vacation home on Part III of Form 3520 for Year 2 as a distribution from FT.

(m) *Example 12: Use of trust property by exempt entity not treated as section 643(i) distribution.* In Year 1, X, a nonresident alien, creates a foreign nongrantor trust, FT, and funds the trust with cash and a valuable painting. In Year 1, pursuant to the terms of the trust instrument, FT lends the painting to E, a U.S. organization described in section 501(c)(3) with a valid determination letter from the Commissioner. E exhibits the painting and does not reimburse FT for the use of the painting. E is not a U.S. person within the meaning of § 1.643(i)–1(d)(12) because E is an entity that is exempt from tax under chapter 1 of the Internal Revenue Code. Accordingly, E's use of the painting is not a section 643(i) distribution under § 1.643(i)–1(c). E's use of the painting, however, is a distribution within the meaning of § 1.6048–4(b). Nevertheless, under § 1.6048–5(d), E is not required to report the use of the painting on Part III of Form 3520 because E is a section 501(c)(3) entity that has received a determination letter from the Commissioner that recognizes that E is exempt from Federal income tax under section 501(a) as an organization described in section 501(c)(3), and the determination letter has not been revoked.

§ 1.643(i)–5 Applicability date.

The rules of §§ 1.643(i)–1 through 1.643(i)–4 apply to loans of cash or marketable securities made from, and to the use of any other property of, a foreign trust after the [date of publication of the final regulations in the **Federal Register**].

■ **Par. 3.** Section 1.679–0 is amended by:

■ a. Revising entry for § 1.679–1(c)(2).
■ b. Adding new entry for § 1.679–2(a)(5).
■ c. Redesignating the entry for § 1.679–2(b)(3) as the entry for § 1.679–2(b)(4).
■ d. Adding new entry for § 1.679–2(b)(3).
■ e. Adding new entries for § 1.679–2(b)(4)(i) through (vi).
■ f. Adding new entry for § 1.679–2(d).
■ g. Revising the entries for § 1.679–4(d)(1) through (6).
■ h. Removing the entry for § 1.679–4(d)(7).
■ i. Revising the entry for § 1.679–7.

The revisions and additions read as follows:

§ 1.679–0 Outline of major topics.

* * * * *

§ 1.679–1 U.S. transferor treated as owner of foreign trust.

(c) * * *

(2) U.S. person.

(i) In general.

(ii) Special rules.

(A) Dual resident taxpayers.

(B) Dual status taxpayers.

* * * * *

(6) Obligation.

§ 1.679–2 Trusts treated as having a U.S. beneficiary.

(a) * * *

(5) Loan or uncompensated use of trust property treated as paid or accumulated for the benefit of a U.S. person.

(i) In general.

(ii) Indirect loans.

(iii) Exceptions.

(iv) Safe harbors.

(A) Reasonable period.

(B) De minimis use.

(v) Interaction with section 643(i).

(vi) Examples.

(A) Example 1: Loan of cash to U.S. person.

(B) Example 2: Use of trust property by U.S. person.

(C) Example 3: Use of trust property by church.

(D) Example 4: Indirect loan of cash to a U.S. person.

(E) Example 5: Interaction with section 643(i) and with section 6048(c) information reporting.

* * * * *

(b) * * *

(3) Loans to, or uncompensated use of trust property by, indirect beneficiaries.

(4) * * *

(i) Example 1. Trust benefiting foreign corporation.

(ii) Example 2. Trust benefiting another trust.

(iii) Example 3. Trust benefiting another trust after transferor's death.

(iv) Example 4. Indirect benefit through use of debit card.

(v) Example 5. Other indirect benefit.

(vi) Example 6. Indirect benefit through an indirect loan.

* * * * *

(d) Presumption that foreign trust has U.S. beneficiary.

(1) In general.

(2) Authority of Commissioner to request information.

§ 1.679–4 Exceptions to general rule.

* * * * *

(d) * * *

(1) In general.

(i) Requirements of the obligation.

(ii) Additional requirements to remain a qualified obligation.

(2) Modification of a qualified obligation.

(3) Additional loans.

(4) Anti-abuse rule.

(5) Obligations that cease to be qualified.

(i) In general.

(ii) Amount transferred to the trust.

(iii) Timing of transfers resulting from failed qualified obligations.

(6) Examples.

(i) Example 1: Demand loan.

(ii) Example 2: Private annuity.

(iii) Example 3: Transfer to unrelated foreign trust in exchange for an obligation.

(iv) Example 4: Transfer for an obligation with term in excess of 5 years.

(v) Example 5: Transfer for a qualified obligation.

(vi) Example 6: Effect of modification treated as an exchange.

(vii) Example 7: Effect of subsequent obligation on original obligation.

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§ 1.679–7 Applicability dates.

* * * * *

■ **Par. 4.** Section 1.679–1 is amended by revising paragraphs (c)(2) and (c)(6) to read as follows:

§ 1.679–1 U.S. transferor treated as owner of foreign trust.

* * * * *

(c) * * *

(2) *U.S. person*—(i) *In general.* Subject to paragraph (c)(2)(ii) of this section, the term *U.S. person* means a United States person as defined in section 7701(a)(30).

(ii) *Special rules*—(A) *Dual resident taxpayers.* If a dual resident taxpayer (within the meaning of § 301.7701(b)–7(a)(1) of this chapter) computes U.S. income tax liability as a nonresident alien on the last day of the taxable year and complies with the filing requirements of § 301.7701(b)–7(b) and (c) of this chapter, the dual resident taxpayer will not be treated as a U.S. person for purposes of section 679 with respect to the portion of the taxable year the dual resident taxpayer was treated as a nonresident alien for purposes of computing U.S. income tax liability.

(B) *Dual status taxpayers.* If a taxpayer abandons U.S. citizenship or residence during the tax year or acquires U.S. citizenship or residence during the taxable year as provided in § 1.6012–1(b)(2)(ii), the taxpayer will not be treated as a U.S. person with respect to the portion of the taxable year the taxpayer was treated as a nonresident alien for purposes of computing U.S. income tax liability.

* * * * *

(6) *Obligation.* The term *obligation* means any instrument or contractual arrangement that constitutes indebtedness under general principles of Federal income tax law (for example, a bond, note, debenture, certificate, bill receivable, account receivable, note receivable, open account, or other evidence of indebtedness), and an annuity contract that would not otherwise be classified as indebtedness under general principles of Federal income tax law.

* * * * *

■ **Par. 5.** Section 1.679–2 is amended by:

■ a. Adding paragraph (a)(5).

■ b. Redesignating paragraph (b)(3) as paragraph (b)(4).

■ c. Adding new paragraph (b)(3).

■ c. In newly redesignated paragraph (b)(4), designating Examples 1 through 5 as paragraphs (b)(4)(i) through (v).

■ d. Adding paragraph (b)(4)(vi).

■ e. Adding paragraph (d).

The revisions and additions read as follows:

§ 1.679–2 Trusts treated as having a U.S. beneficiary.

(a) * * *

(5) *Loan or uncompensated use of trust property treated as paid or accumulated for the benefit of a U.S. person*—(i) *In general.* Except as provided in paragraph (a)(5)(iii) of this section, any direct or indirect loan of cash or marketable securities from a foreign trust or portion of a foreign trust (whether from trust corpus or income) as described in paragraph (a)(5)(ii) to, or the direct or indirect use of any other property of a foreign trust or portion of a foreign trust by, any U.S. person (whether or not a beneficiary under the terms of the trust) is treated as causing trust income or corpus to be paid or accumulated for the benefit of a U.S. person for purposes of paragraph (a)(1) of this section. For these purposes, a loan from a foreign trust to, or the use of property of a foreign trust by, a grantor trust (as defined in § 1.643(i)–1(d)(5)) or a disregarded entity (as defined in § 1.643(i)–1(d)(3)) is treated as a loan to or use by the owner of the grantor trust or of the disregarded entity, respectively. For example, a loan to a single member LLC treated as a disregarded entity is treated as a loan to the owner of the LLC.

(ii) *Indirect loans.* For purposes of paragraph (a)(5)(i) of this section, an indirect loan of cash or marketable securities from a foreign trust or portion of a foreign trust includes:

(A) Loans of cash or marketable securities made by any person to a U.S. person, if the foreign trust provides a guarantee (within the meaning of § 1.679–3(e)(4)) for the loan; and

(B) Loans of cash or marketable securities made from a foreign trust to a U.S. person through an intermediary, such as an agent or nominee of the foreign trust, or from a person related (within the meaning of § 1.643(i)–1(d)(9)) to the foreign trust.

(iii) *Exceptions.* Paragraph (a)(5)(i) of this section does not apply if—

(A) The U.S. person who receives the loan of cash or marketable securities, or who uses trust property, is an entity described in section 501(c)(3),

(B) The loan of cash received by the U.S. person is in exchange for a qualified obligation within the meaning of § 1.643(i)–2(b)(2)(iii) (but without regard to § 1.643(i)–2(b)(2)(iii)(B)(*1*) and (*2*)), or

(C) The U.S. person who uses trust property, other than a loan of cash or marketable securities, pays the trust the fair market value of the use of such property within a reasonable period from the date of the start of the use of the property. A determination as to the fair market value of the use of such property and as to whether a fair market value payment is made within a reasonable period will be based on all the facts and circumstances, including the type of property used and the period of use. In appropriate cases, such as rental of real property, payments may be made on a periodic basis, if doing so would be consistent with arm's-length dealings between unrelated parties.

(iv) *Safe harbors.* The following safe harbors apply for purposes of paragraph (a)(5)(iii)(C) of this section.

(A) *Reasonable period.* A payment is made within a reasonable period if the payment is made or periodic payments commence within 60 days of the start of the use of trust property.

(B) *De minimis use.* Use of trust property will be disregarded if the aggregate use by all U.S. persons (within the meaning of § 1.679–1(c)(2)) does not exceed 14 days during the calendar year.

(v) *Interaction with section 643(i).* If a foreign trust or a portion of a foreign trust is treated as having a U.S. beneficiary pursuant to the rules of this paragraph (a)(5) and a U.S. transferor is thus treated as the owner of the foreign trust or a portion of the foreign trust under section 679, section 643(i) does not apply to the trust or portion of the trust of which the U.S. transferor is treated as the owner.

(vi) *Examples.* The following examples illustrate the rules of paragraph (a)(5) of this section. In these examples, X, Y, and E are U.S. persons (within the meaning of § 1.679–1(c)(2)), and FT is a foreign trust. In addition, FT's trust instrument provides that no U.S. person can benefit either as to income or corpus of FT.

(A) *Example 1: Loan of cash to U.S. person.* In Year 1, X transfers cash and real property to FT. X is not treated as the owner of any portion of FT under sections 673 through 679. In Year 2, Y receives a loan of cash from FT that is not in exchange for a qualified obligation within the meaning of § 1.643(i)–2(b)(2)(iii) and thus does not qualify for the exception under paragraph (a)(5)(iii)(B) of this section. Y is not an entity described in section 501(c)(3) and thus does not qualify for the exception under paragraph (a)(5)(iii)(A) of this section. Under

paragraph (a)(5) of this section, the loan is treated as paid or accumulated for the benefit of a U.S. person for purposes of paragraph (a)(1) of this section, and under § 1.679–1(a), X is treated as the owner of FT. Under paragraph (c)(1) of this section, FT is treated as acquiring a U.S. beneficiary in Year 2.

(B) *Example 2: Use of trust property by U.S. person.* The facts are the same as in paragraph (a)(5)(vi)(A) of this section (*Example 1*) except that, instead of receiving a loan of cash in Year 2, Y occupies real property owned by FT in exchange for monthly payments of $2,000. FT could rent the property to an unrelated party at fair market value for $10,000 a month. Under paragraph (a)(5) of this section, Y's use of FT's property is treated as paid or accumulated for the benefit of a U.S. person for purposes of paragraph (a)(1) of this section because Y has not paid fair market value for the use of the real property. Under § 1.679–1(a), X is treated as the owner of FT. Under paragraph (c)(1) of this section, FT is treated as acquiring a U.S. beneficiary in Year 2.

(C) *Example 3: Use of trust property by church.* In Year 1, X transfers cash and a valuable painting to FT. X is not treated as the owner of any portion of FT under sections 673 through 679. In Year 2, FT lends the painting to E, a U.S. church described in section 501(c)(3). E's use of the painting is not treated as paid or accumulated for the benefit of a U.S. person for purposes of paragraph (a)(1) of this section because the exception in paragraph (a)(5)(iii)(A) of this section applies, and thus FT is not treated as having a U.S. beneficiary in Year 2.

(D) *Example 4: Indirect loan of cash to a U.S. person.* In Year 1, X transfers property to FT. In Year 2, Y borrows $100,000 from Bank in exchange for an obligation that is not a qualified obligation within the meaning of § 1.643(i)–2(b)(2)(iii) and thus does not qualify for the exception under paragraph (a)(5)(iii)(B) of this section. FT provides a guarantee (within the meaning of § 1.679–3(e)(4)) for the loan. Under paragraph (a)(5)(ii)(A) of this section, Y is treated as receiving a loan from FT because FT guaranteed the loan from Bank to Y. Under paragraph (a)(5) of this section, the loan is treated as paid or accumulated for the benefit of a U.S. person for purposes of paragraph (a)(1) of this section. Under § 1.679–1(a), X is treated as the owner of FT. Under paragraph (c)(1) of this section, FT is treated as acquiring a U.S. beneficiary in Year 2.

(E) *Example 5: Interaction of grantor trust rules with section 643(i) and with section 6048(c) information reporting.* In Year 1, X created and funded a foreign nongrantor trust, FT. During Year 1 and Year 2, FT accumulates income in the amount of $110,000. Before Year 3, neither X nor any other person is treated as owning FT under the rules of sections 673 through 679. In Year 3, Y receives a loan of $100,000 cash from FT that is not in exchange for a qualified obligation within the meaning of § 1.643(i)–2(b)(2)(iii) and thus does not qualify for the exception under paragraph (a)(5)(iii)(B) of this section. Under paragraph (a)(5) of this section, the loan to Y is treated as paid for the benefit of a U.S. person for purposes of paragraph (a)(1) of this section. Under § 1.679–1(a), X is now treated as the owner of FT. Under paragraph (a)(5)(v) of this section, section 643(i) does not apply to the loan from FT to Y. Under paragraph (c)(1) of this section, FT is treated as acquiring a U.S. beneficiary in Year 3. Pursuant to § 1.6048–4(b)(3), Y is treated as receiving a distribution from FT and must comply with the reporting requirements in § 1.6048–4 with respect to the loan.

(b) * * *

(3) *Loans to, or uncompensated use of trust property by, indirect beneficiaries.* For purposes of paragraphs (a)(1) and (a)(5) of this section, a loan of cash or marketable securities or the use of trust property shall be treated as paid or accumulated for the benefit of a U.S. person if—

(i) The loan is made to, or the trust property is used by, a foreign entity described in paragraph (b)(1) of this section; or

(ii) The loan is made through, or the use of trust property is made available to, an intermediary described in paragraph (b)(2) of this section, or such loan or use of trust property is made by any other means where a U.S. person may obtain an actual or constructive benefit.

(4) * * *

(vi) *Example 6. Indirect benefit through an indirect loan.* A, a U.S. person, transfers property to FT. The trust instrument provides that no U.S. person can benefit either as to income or corpus. However, FT maintains an account with FB, a foreign bank, and FB issues a loan to B, a U.S. person, against the account maintained by FT. Under paragraphs (a)(1), (a)(5), and (b)(3) of this section, FT is treated as having a U.S. beneficiary.

* * * * *

(d) *Presumption that foreign trust has U.S. beneficiary*—(1) *In general.* If a U.S. person directly or indirectly transfers property to a foreign trust other than a trust described in § 1.679–4(a)(2) or (3), the Commissioner may treat the trust as having a U.S. beneficiary for purposes of § 1.679–1(a), unless the U.S. person—

(i) Satisfies the reporting requirements of § 1.6048–2 with respect to the transfer; and

(ii) Includes an explanatory statement attached to the U.S. person's Federal income tax return that demonstrates to the satisfaction of the Commissioner that the trust satisfies the requirements of paragraph (a)(1) of this section immediately after the transfer.

(2) *Authority of Commissioner to request information.* The Commissioner may request information related to the trust described in paragraph (d)(1) of this section and its potential beneficiaries to determine whether the trust satisfies the requirements of paragraph (a)(1) of this section. Unless such additional information is provided upon the Commissioner's written notice and request to the U.S. person, the trust will be deemed to have a U.S. beneficiary. The U.S. person will have 60 days (90 days if the notice is addressed to a person outside the United States) to respond to the notice and request.

■ **Par. 6.** Section 1.679–4 is amended by revising paragraph (d) to read as follows:

§ 1.679–4 Exceptions to general rule.

* * * * *

(d) *Qualified obligations*—(1) *In general*—(i) *Requirements of the obligation.* For purposes of this section, an obligation is treated as a qualified obligation only if the obligation at all times satisfies all of the following requirements—

(A) The obligation is reduced to writing in an express written agreement;

(B) The term of the obligation does not exceed five years. For purposes of determining the term of an obligation, the obligation's maturity date is the last possible date that the obligation can be outstanding under the terms of the obligation;

(C) All payments on the obligation must be made in cash in U.S. dollars;

(D) The obligation is issued at par and provides for stated interest at a fixed rate or a qualified floating rate within the meaning of § 1.1275–5(b);

(E) The yield to maturity of the obligation is not less than 100 percent of the applicable Federal rate and not greater than 130 percent of the applicable Federal rate. The applicable Federal rate for an obligation is the applicable Federal rate in effect under section 1274(d) for the day on which the obligation is issued, as published in the Internal Revenue Bulletin (see § 601.601(d)(2) of this chapter). The

yield to maturity and the applicable Federal rate must be based on the same compounding period. If an obligation is a variable rate debt instrument that provides for stated interest at a qualified floating rate, the equivalent fixed rate debt instrument rules in § 1.1274–2(f)(1) or § 1.1275–5(e), whichever is applicable, apply to determine the obligation's yield to maturity; and

(F) All stated interest on the obligation is qualified stated interest within the meaning of § 1.1273–1(c).

(ii) *Additional requirements to remain a qualified obligation.* An obligation will remain a qualified obligation only if, for the first year and each succeeding year that the obligation remains outstanding, the trust timely makes all payments of principal and interest on the obligation according to the terms of the obligation (which may include a reasonable grace period of no more than thirty days for a late payment) and the U.S. transferor fulfills the requirements of this paragraph (d)(1)(ii):

(A) The U.S. transferor timely extends the period for assessment of any income tax attributable to the obligation and any consequent income tax changes for each year that the obligation is outstanding to a date not earlier than three years after the maturity date of the obligation. This extension of the period for assessment is not necessary with respect to the taxable year of the U.S. transferor in which the maturity date of the obligation falls, provided that the obligation is paid in cash in U.S. dollars within that year. The period of assessment is extended by completing and filing Part I of Form 3520, Annual Return to Report Transactions with Foreign Trusts and Receipt of Certain Foreign Gifts, for every year that the obligation is outstanding. Part I of Form 3520 also may contain such other terms with respect to assessment as may be considered necessary by the Commissioner to ensure the assessment and collection of the correct tax liability for each year for which the extension of the period of assessment is required. When Part I of Form 3520 is properly executed and filed, the consent to extend the period for assessment of tax will be deemed to be agreed upon and executed by the Commissioner for purposes of § 301.6501(c)–1(d); and

(B) The U.S. transferor timely reports the status of the obligation, including principal and interest payments, on Part I of Form 3520 for each year that the obligation is outstanding.

(2) *Modification of a qualified obligation.* If the terms of a qualified obligation are modified and the modification is treated as an exchange under § 1.1001–3, the new obligation that is deemed issued in the exchange under § 1.1001–3 must satisfy all the requirements in paragraph (d)(1) of this section to be a qualified obligation using the original obligation's issue date. If the modification is not treated as an exchange under § 1.1001–3, then the obligation must be retested as of the date of the modification to determine whether the obligation, as modified, continues to satisfy the requirements in paragraph (d)(1) of this section to be a qualified obligation.

(3) *Additional loans.* If a qualified obligation is outstanding and the U.S. transferor directly or indirectly obtains an additional obligation issued by the foreign trust in exchange for cash, or if the U.S. transferor directly or indirectly obtains an additional obligation issued by a person related to the trust, the outstanding obligation is deemed to have the maturity date of the additional obligation in determining whether the outstanding obligation exceeds the specified five-year term. The outstanding obligation must be retested as of the issue date of the additional obligation to determine whether it would have satisfied, as of the outstanding obligation's issue date, all the requirements in paragraph (d)(1) of this section to be a qualified obligation. If there is more than one qualified obligation outstanding, the determination is made based on the outstanding obligation with the earliest issue date. The additional obligation also must be separately tested to see if it satisfies the requirements of (d)(1) of this section to be a qualified obligation.

(4) *Anti-abuse rule.* Notwithstanding paragraphs (2) and (3) of this section, if the Commissioner determines, based on all the facts and circumstances, that two or more obligations issued by a foreign trust or a person related to the trust are structured with a principal purpose to avoid the application of section 679, the Commissioner may treat the obligations as a single obligation that is not a qualified obligation.

(5) *Obligations that cease to be qualified*—(i) *In general.* If an obligation ceases to be a qualified obligation (for example, because an obligation is modified so that the term exceeds 5 years), the U.S. transferor is treated as making a transfer to the foreign trust.

(ii) *Amount transferred to the trust.* The amount that the U.S. transferor is treated as having transferred to the trust will be equal to the obligation's outstanding stated principal amount plus any accrued but unpaid qualified stated interest (within the meaning of § 1.1273–1(c)) as of the date of the event that causes the obligation to no longer be a qualified obligation. In the case of an obligation that ceases to be a qualified obligation because the Commissioner treats two or more obligations as a single obligation pursuant to paragraph (d)(4) of this section, the U.S. transferor is treated as making a transfer to the trust in an amount not to exceed the sum of the outstanding stated principal amount of the obligations plus any accrued but unpaid qualified stated interest for each of the obligations as of the date determined by the Commissioner under paragraph (d)(5)(iii) of this section.

(iii) *Timing of transfers resulting from failed qualified obligations.* In general, a U.S. transferor is treated as making a transfer to the foreign trust on the date of the event that causes an obligation to no longer be a qualified obligation. However, based on all of the facts and circumstances, if an obligation (or obligations) is structured with a principal purpose to avoid the application of section 679, the Commissioner may deem a transfer to have occurred on any date on or after the issue date of the obligation(s).

(6) *Examples.* The following example illustrates the rules of this paragraph (d). In these examples, A and B are U.S. residents and FT is a foreign trust.

(i) *Example 1: Demand loan.* A is a related person (as defined in § 1.679–1(c)(5)) with respect to FT. A transfers $50,000 to FT in exchange for a demand note that permits A to require repayment by FT at any time. Because FT*'s* obligation to A could remain outstanding for more than five years, the obligation is not a qualified obligation within the meaning of paragraph (d)(1) of this section and, pursuant to paragraph (c) of this section, it is not taken into account for purposes of determining whether A's transfer is eligible for the fair market value exception of paragraph (a)(4) of this section. Accordingly, § 1.679–1 applies to treat A as the owner of the portion of FT attributable to the full $50,000 transfer to FT.

(ii) *Example 2: Private annuity.* A is a related person (as defined in § 1.679–1(c)(5)) with respect to FT. A transfers $40,000 to FT in exchange for an annuity from FT that will pay A $100x per year for the rest of A's life. Because FT's obligation to A could remain outstanding for more than five years, the obligation is not a qualified obligation within the meaning of paragraph (d)(1) of this section and, pursuant to paragraph (c) of this section, it is not taken into account for purposes of determining whether A's transfer is eligible for the fair market value exception of paragraph (a)(4) of this section. Accordingly, § 1.679–1 applies

to treat A as the owner of the portion of FT attributable to the full $40,000 transfer to FT.

(iii) *Example 3: Transfer to unrelated foreign trust in exchange for an obligation.* B is not a related person (as defined in § 1.679–1(c)(5)) with respect to FT. B transfers $10,000 to FT in exchange for an obligation of the trust. The term of the obligation is fifteen years. Because B is not a related person with respect to FT, paragraph (c) of this section does not apply. The fair market value of the obligation received by B is taken into account for purposes of the fair market value exception of paragraph (a)(4) of this section even though the obligation is not a qualified obligation within the meaning of paragraph (d)(1) of this section.

(iv) *Example 4: Transfer for an obligation with term in excess of 5 years.* A is a related person (as defined in § 1.679–1(c)(5)) with respect to FT. A transfers property that has a fair market value of $50,000 to FT in exchange for an obligation of FT. The term of the obligation is ten years. Because the term of the obligation exceeds five years, the obligation is not a qualified obligation within the meaning of paragraph (d)(1) of this section, and pursuant to paragraph (c) of this section, it is not taken into account for purposes of determining whether A's transfer is eligible for the fair market value exception of paragraph (a)(4) of this section. Accordingly, § 1.679–1 applies to treat A as the owner of the portion of FT attributable to the full $50,000 transfer to FT.

(v) *Example 5: Transfer for a qualified obligation.* The facts are the same as in paragraph (d)(6)(iv) of this section (*Example 4*), except that the term of the obligation is three years. Assuming the other requirements of paragraph (d)(1) of this section are satisfied, the obligation is a qualified obligation, and its stated principal amount is taken into account for purposes of determining whether A's transfer is eligible for the fair market value exception of paragraph (a)(4) of this section.

(vi) *Example 6: Effect of modification treated as an exchange.* A is a related person (as defined in § 1.679–1(c)(5)) with respect to FT. A transfers property that has a fair market value of $10,000 to FT in exchange for an obligation with a term of four years that satisfies the requirements of paragraph (d)(1) of this section. Two years later, a significant modification of the obligation within the meaning of § 1.1001–3, including an extension of the obligation by an additional term of three years, occurs, and the modification is treated as an exchange under § 1.1001–3. The new obligation that is deemed issued in the exchange under § 1.1001–3 must satisfy the requirements of paragraph (d)(1) of this section to be a qualified obligation as of the original obligation's issue date. Because the new obligation would not satisfy the five-year requirement of paragraph (d)(1), the obligation ceases to be treated as a qualified obligation.

(vii) *Example 7: Effect of subsequent obligation on original obligation.* A is a related person (as defined in § 1.679–1(c)(5)) with respect to FT. On January 1, Year 1, A transfers $100,000 to FT in exchange for Obligation 1 from FT, an obligation with a maturity date of January 1, Year 6, that satisfies the requirements of paragraph (d)(1) of this section. On June 30, Year 1, A transfers an additional $50,000 to FT in exchange for Obligation 2, an obligation with a maturity date of June 30, Year 6, that independently satisfies the requirements of paragraph (d)(1) of this section. Under paragraph (d)(3) of this section, Obligation 1 will be deemed to have a maturity date of June 30, Year 6 (*i.e.,* a greater than five-year term) and will cease to be a qualified obligation under paragraph (d)(1) of this section. Pursuant to paragraph (c) of this section, because Obligation 1 is not a qualified obligation, it is not taken into account for purposes of determining whether A's transfer of $100,000 is eligible for the fair market value exception of paragraph (a)(4) of this section. Accordingly, § 1.679–1 applies to treat A as the owner of the portion of FT attributable to the $100,000 transferred to FT. Obligation 2 is separately tested to determine whether it satisfies the qualified obligation rules of paragraph (d)(1) of this section and to the extent it does, A is treated as eligible for the fair market value exception of paragraph (a)(4) of this section and is not treated as the owner of the portion of FT attributable to the $50,000 transferred to FT.

■ **Par. 7.** Section 1.679–7 is amended by:

■ a. Revising the section heading.

■ b. Adding paragraphs (b)(4) through (b)(7).

The revision and additions read as follows:

§ 1.679–7 Applicability dates.

* * * * *

(b) * * *

(4) The amendments to §§ 1.679–1(c)(2) and 1.679–1(c)(6) apply for taxable years beginning after the [date of publication of the final regulations in the **Federal Register**].

(5) The rules of § 1.679–2(a)(5) apply to loans and the use of trust property after the [date of publication of the final regulations in the **Federal Register**].

(6) The rules of § 1.679–2(d) apply to transfers of property after the [date of publication of the final regulations in the **Federal Register**].

(7) Section 1.679–4(d) applies to obligations issued or modified after the [date of publication of the final regulations in the **Federal Register**]. If an obligation issued on or before the [date of publication of the final regulations in the **Federal Register**] is modified after that date, and the modification is a significant modification under § 1.1001–3, the new obligation that is deemed issued in the exchange is treated as issued after the [date of publication of the final regulations in the **Federal Register**]. If the modification is not a significant modification under § 1.1001–3, then the original obligation must be retested as of the date of the modification to determine whether the obligation, as modified, satisfies the requirements in paragraph (d)(1), as amended, to be a qualified obligation.

■ **Par. 8.** Section 1.6039F–1 is added to read as follows:

§ 1.6039F–1 U.S. recipients of foreign gifts.

(a) *Reporting of foreign gifts*—(1) *In general.* Except as provided in paragraph (c) of this section, and subject to paragraph (a)(2) and (3) of this section, each U.S. person (within the meaning of section 7701(a)(30)) who receives a foreign gift (within the meaning of paragraph (b) of this section) during a taxable year must report such gift (including the additional information required under paragraph (c) of this section if, after applying the aggregation rules, the foreign gift exceeds certain reporting thresholds) on Part IV of Form 3520, Annual Return To Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts, by the fifteenth day of the fourth month after the close of the U.S. person's taxable year. In the case of a U.S. person who has been granted an extension of time to file the U.S. person's income tax return pursuant to section 6081, an extension of time for filing Form 3520 is granted to the fifteenth day of the tenth month following the close of the U.S. person's taxable year. No further extension of time to file Form 3520 is allowed. For special rules concerning the treatment of dual resident taxpayers (within the meaning of § 301.7701(b)–7(a)(1) of this chapter) and dual status taxpayers (described in § 1.6012–1(b)(2)(ii)) as U.S. persons for purposes of this section, see paragraph (f) of this section.

(2) *Reporting by U.S. citizens and residents residing abroad.* In the case of a U.S. person who is an individual and

who qualifies for an automatic extension to file their income tax return under section 6081 and § 1.6081–5(a)(5) because the U.S. person resides outside of the United States and Puerto Rico and the U.S. person's main place of business or post of duty is outside of the United States and Puerto Rico, the U.S. person must report the foreign gifts received by the U.S. person during the taxable year on Part IV of Form 3520 by the fifteenth day of the sixth month after the close of the U.S. person's taxable year. If the U.S. person has been granted an extension of time to file the U.S. person's income tax return pursuant to section 6081, an extension of time for filing Form 3520 is granted to the fifteenth day of the tenth month following the close of the U.S. person's taxable year. No additional extension of time to file Form 3520 is allowed.

(3) *Reporting for deceased U.S. persons.* In the case of a deceased U.S. person, the executor (within the meaning of section 2203) of the U.S. person's estate must report the foreign gifts received by the U.S. person during the U.S. person's final taxable year on Part IV of Form 3520 by the fifteenth day of the fourth month following the close of the 12-month period which began with the first day of the U.S. person's final taxable year. If the executor of the U.S. person's estate has been granted an extension of time to file the U.S. person's final income tax return pursuant to section 6081, an extension of time for filing Form 3520 is granted to the fifteenth day of the tenth month following the close of the 12-month period which began with the first day of the U.S. person's final taxable year. No additional extension of time to file Form 3520 is allowed.

(b) *Definition of foreign gift*—(1) *In general.* The term *foreign gift* means any amount received from a non-U.S. person that the recipient (including a spouse) treats as a gift, bequest, devise, or inheritance for income tax purposes, but does not include any qualified transfer within the meaning of section 2503(e)(2) (relating to certain transfers for educational or medical expenses) or any transfer that is treated as a distribution (within the meaning of § 1.6048–4(b)) from a foreign trust and that is reported on a return under § 1.6048–4. A U.S. person who receives a transfer from a foreign trust must treat that transfer as a distribution from the trust that is reportable under § 1.6048–4, rather than as a foreign gift that is reportable under paragraph (a) of this section, even if the U.S. person treats the transfer as a gift for another purpose (such as computing the person's Federal income tax liability). For example, although a covered gift or bequest described in section 2801(e) is a foreign gift, a U.S. person who receives a covered gift or bequest from a foreign trust must report the covered gift or bequest as a distribution (within the meaning of § 1.6048–4(b)) under § 1.6048–4.

(2) *Anti-avoidance rule.* The term foreign gift includes any amount received by a U.S. person from a non-U.S. person that meets all of the following requirements—

(i) Based on all the facts and circumstances, the Commissioner determines that the amount received is in substance a gift;

(ii) The recipient does not treat the amount received as a gift, bequest, devise, or inheritance; and

(iii) The recipient does not treat the amount received as taxable income (such as a purported loan).

(c) *Exceptions*—(1) *Section 501(c) recipient.* Paragraph (a) of this section does not apply if the recipient of the foreign gift is an organization described in section 501(c) and exempt from tax under section 501(a).

(2) *Reporting threshold rules*—(i) *Foreign gifts from foreign individuals or foreign estates*—(A) *Reporting threshold.* Except as provided in paragraph (c)(2)(ii) of this section, paragraph (a) of this section does not apply to a foreign gift received by a U.S. person from a non-U.S. person who is an individual (a *foreign individual*) or a foreign estate (within the meaning of section 7701(a)(31)(A)) if, during the U.S. person's taxable year, the aggregate amount of foreign gifts received, directly or indirectly, from that foreign individual or foreign estate (the *transferor*) does not exceed $100,000, as modified by cost-of-living adjustments pursuant to paragraph (c)(2)(v) of this section.

(B) *Aggregation rule.* To determine whether paragraph (c)(2)(i)(A) of this section applies to foreign gifts received from a transferor, each U.S. person must aggregate foreign gifts, including covered gifts and bequests described in section 2801(e), received from all foreign individuals, foreign estates, and any other foreign person (such as corporations or partnerships) that the U.S. person knows or has reason to know are related to the transferor within the meaning of § 1.643(i)–1(d)(9). If the aggregate amount of all these foreign gifts exceeds the $100,000 reporting threshold, the U.S. person must separately identify each foreign gift in excess of $5,000 received from the transferor and from each foreign person related to the transferor and must provide identifying information (for example, name and address) about the transferor and each such foreign person, including a foreign individual or a foreign estate.

(ii) *Covered gifts and bequests.* Subject to paragraph (h)(2) of this section, paragraph (a) of this section does not apply to a foreign gift that is a covered gift or bequest described in section 2801(e) if the aggregate amount of covered gifts and bequests received by the U.S. person during the calendar year does not exceed the section 2801(c) amount, which is the dollar amount of the per-donee exclusion in effect under section 2503(b). For purposes of this paragraph (c)(2)(ii), the aggregate amount of covered gifts and bequests received by the U.S. person during the calendar year does not include transfers from a foreign trust (as described in paragraph (b)(1) of this section), as such transfers are reportable as distributions (within the meaning of § 1.6048–4(b)) under § 1.6048–4.

(iii) *Other foreign gifts*—(A) *Reporting threshold.* Paragraph (a) of this section does not apply to a foreign gift received by a U.S. person from a foreign corporation or a foreign partnership if, during the U.S. person's taxable year, the aggregate amount of foreign gifts from that corporation or partnership (the *transferor*), when aggregated with foreign gifts received from other foreign persons that the U.S. person knows or has reason to know are related to the transferor as described in paragraph (c)(2)(iii)(B) of this section, does not exceed $10,000, as modified by cost-of-living adjustments pursuant to paragraph (c)(2)(v) of this section.

(B) *Aggregation rule.* To determine whether paragraph (c)(2)(iii)(A) of this section applies to foreign gifts from a transferor, the U.S. person must aggregate foreign gifts received from all foreign corporations, foreign partnerships, and any other foreign person that the U.S. person knows or has reason to know are related to the transferor within the meaning of § 1.643(i)–1(d)(9). If the aggregate amount of these foreign gifts exceeds the reporting threshold, the U.S. person must separately identify each foreign gift from the transferor and from each foreign person related to the transferor and provide identifying information (for example, name and address) about the transferor and each such foreign person, including a foreign individual or foreign estate.

(iv) *Joint returns.* In the case of married U.S. persons who file joint income tax returns under section 6013 for a tax year, the reporting threshold under paragraph (c)(2)(i)(A) of this section applies separately to each spouse. Thus, married U.S. persons who

file a joint income tax return will not be subject to paragraph (a) of this section if the aggregate amount of foreign gifts received by each spouse, directly or indirectly from any one foreign individual or foreign estate, taking into account the aggregation rule of paragraph (c)(2)(i)(B) of this section, does not exceed $100,000 during the taxable year.

(v) *Cost-of-living adjustments.* The reporting thresholds under paragraph (c)(2)(i)(A) and under paragraph (c)(2)(iii)(A) of this section are increased by an amount equal to the product of the amounts specified in such paragraphs and the cost-of-living adjustment for the taxable year of the gift under section 1(f)(3), except that paragraph (A)(ii) thereof is applied by substituting ''1995'' for ''2016.''

(d) *Valuation principles.* The amount of a foreign gift is the value of the property at the time of its transfer. The value of the property is the price at which such property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell, and both having reasonable knowledge of relevant facts. Accordingly, the value of the property is determined in accordance with the Federal gift tax valuation principles of section 2512 and sections 2701 through 2704 (chapter 14 of the Internal Revenue Code) and the regulations under section 2512 and sections 2701 through 2704 in this part.

(e) *Penalty for failure to file information*—(1) *In general.* If a U.S. person fails to furnish information required under paragraph (a) of this section with respect to any foreign gift by the due date provided under paragraph (a)—

(i) The tax consequences of the receipt of such foreign gift may be determined by the Commissioner based on all the facts and circumstances, and

(ii) Notwithstanding the tax consequences under paragraph (e)(1)(i) of this section, such U.S. person must pay (upon notice and demand by the Commissioner and in the same manner as tax) an amount equal to 5 percent of the amount of such foreign gift for each month (or portion thereof) for which the failure to report the foreign gift as a gift on Form 3520 continues (not to exceed 25 percent of such amount in the aggregate).

(2) *Reasonable cause exception.* Paragraph (e)(1) of this section will not apply to any failure to report a foreign gift if the U.S. person submits a reasonable cause statement to the Commissioner under penalties of perjury and demonstrates to the satisfaction of the Commissioner that the failure is due to reasonable cause and not due to willful neglect. The determination of whether a taxpayer acted with reasonable cause and not with willful neglect is made under the principles set out in § 1.6664–4 and § 301.6651–1(c). This determination is made on a case-by-case basis, taking into account all pertinent facts and circumstances.

(f) *Special rules*—(1) *Dual resident taxpayers.* If a dual resident taxpayer (within the meaning of § 301.7701(b)–7(a)(1) of this chapter) computes U.S. income tax liability as a nonresident alien on the last day of the taxable year and complies with the filing requirements of § 301.7701(b)–7(b) and (c) of this chapter, the dual resident taxpayer will not be treated as a U.S. person for purposes of section 6039F with respect to the portion of the taxable year the dual resident taxpayer was treated as a nonresident alien for purposes of computing U.S. income tax liability.

(2) *Dual status taxpayers.* If a taxpayer abandons U.S. citizenship or residence during the taxable year or acquires U.S. citizenship or residence during the taxable year as provided in § 1.6012–1(b)(2)(ii), the taxpayer will not be treated as a U.S. person with respect to the portion of the taxable year the taxpayer is treated as a nonresident alien for purposes of computing U.S. income tax liability.

(g) *Examples.* The following examples illustrate the rules of this section. In these examples and unless otherwise stated, assume that the reporting threshold under paragraph (c)(2)(i)(A) of this section is $100,000:

(1) *Example 1: Qualified transfer exception.* X, a U.S. person, attends Private University, an accredited college in the United States. X's grandparents, who are not U.S. persons, pay X's tuition directly to Private University. The tuition payment is a qualified transfer within the meaning of section 2503(e)(2). Under paragraph (b)(1) of this section, X is not treated as receiving a foreign gift from X's grandparents. Accordingly, X is not required to report the tuition payment under paragraph (a) of this section.

(2) *Example 2: Charitable donee.* XYZ, a U.S. person, is an organization described in section 501(c) and is exempt from tax under section 501(a). XYZ receives a bequest of $200,000 from a foreign estate. Because XYZ meets the exception under paragraph (c)(1) of this section for organizations described in section 501(c) and exempt from tax under section 501(a), XYZ is not required to report the bequest under paragraph (a) of this section.

(3) *Example 3: Gift from dual resident taxpayer.* X is a lawful permanent resident of the United States within the meaning of § 301.7701(b)–1(b) of this chapter and is a resident of Country F under the domestic law of Country F. X is a resident of Country F under the residence article of the U.S.-Country F income tax treaty and notifies the United States by taking such a position on Form 1040NR and Form 8833 for Year 1. Pursuant to § 301.7701(b)–7 of this chapter, X is treated as a nonresident alien for purposes of computing X's U.S. income tax liability for Year 1. During Year 1, X makes a gift of $150,000 to Y, a U.S. citizen. Under paragraph (f)(1) of this section, X is not treated as a U.S. person for purposes of this section. Because X is not treated as a U.S. person for Year 1, the gift is a foreign gift within the meaning of paragraph (b) of this section. Y must report the foreign gift on Part IV of Form 3520 under paragraph (a) of this section.

(4) *Example 4: Gifts from related foreign individuals.* X, a U.S. citizen, is married to Y, a nonresident alien. Y has three brothers, A, B, and C, who also are nonresident aliens. In Year 1, Y makes a gift of $90,000 to X, A makes a gift of $40,000 to X, B makes two gifts to X (one of $4,000 and one of $3,000), and C makes a gift of $4,000 to X. X knows or has reason to know that A, B, and C are related to Y within the meaning of § 1.643(i)–1(d)(9). X treats all five transfers as gifts. Under paragraphs (c)(2)(i)(A) and (B) of this section, to calculate the $100,000 reporting threshold, X must aggregate foreign gifts from Y, A, B, and C. For Year 1, X must report the receipt of $141,000 in foreign gifts. In addition, under paragraphs (a) and (c)(2)(i)(B) of this section, X must separately identify and report information regarding the $90,000 foreign gift from Y, the $40,000 foreign gift from A, and the aggregated $7,000 foreign gifts from B because each person's foreign gift for Year 1 exceeds $5,000. X is not required to identify the $4,000 gift from C separately because it does not exceed $5,000.

(5) *Example 5: Covered gift within meaning of section 2801(e).* Z is a resident of Country F and relinquishes U.S. citizenship on July 1, Year 1, becoming a covered expatriate within the meaning of section 877A(g)(1). On December 31, Year 10, a date after the date final regulations under section 2801 are published in the **Federal Register**, Z gives $50,000 to Z's son, X, who is a U.S. person. The transfer is a covered gift within the meaning of section 2801(e) and a foreign gift within the meaning of paragraph (b) of this section. Because the value of the foreign

gift exceeds the threshold specified in paragraph (c)(2)(ii) of this section (assuming that for Year 10 this amount is under $50,000), X must report receipt of the foreign gift on Part IV of Form 3520 under paragraph (a) of this section. X also is subject to tax and separate reporting requirements under section 2801.

(6) *Example 6: Gifts from foreign individual and related corporation.* X, a U.S. citizen, is married to Y, a nonresident alien. Y is the sole shareholder of FC, a foreign corporation. During Year 1, Y makes a gift of $11,000 to X, and FC makes a gift of $9,000 to X. Because X knows or has reason to know that Y and FC are related, X must aggregate the gifts from Y and FC ($20,000). Although the $20,000 aggregate amount deemed received from Y does not exceed the $100,000 reporting threshold with respect to foreign gifts from foreign individuals, the $20,000 aggregate amount received from FC exceeds the applicable reporting threshold for foreign gifts from foreign corporations under paragraph (c)(2)(iii) of this section for Year 1 (assume that for Year 1 this amount is $18,000). Accordingly, X must report receipt of the foreign gift on Part IV of Form 3520 under paragraph (a) of this section. In addition, X must separately identify each foreign gift from Y and FC and must provide identifying information about Y and FC.

(7) *Example 7: Penalties for failure to report information.* The facts are the same as in paragraph (g)(6) of this section (*Example 6*). X fails to report the amounts received from Y and FC on Form 3520 and does not demonstrate to the satisfaction of the Commissioner that such failure is due to reasonable cause and not due to willful neglect. Under paragraph (e)(1)(i) of this section and § 1.672(f)–4(a)(2), the Commissioner may determine that, based on all the facts and circumstances, the gift of $9,000 from FC to X should be treated as a dividend from FC to X and included in X's gross income. Under paragraph (e)(1)(i) of this section, the Commissioner also may determine that there are no tax consequences to X upon receiving the gift of $11,000 from Y. Without regard to the tax consequences determined under paragraph (e)(1)(i) of this section, under paragraph (e)(1)(ii) of this section, X must pay (upon notice and demand by the Commissioner and in the same manner as tax) $1,000, an amount equal to 5 percent of the aggregate amount of $20,000 for each month for which the failure to disclose the foreign gifts on Form 3520 continues (not to exceed $5,000, an amount equal to 25 percent of the aggregate amount of $20,000).

(h) *Applicability date*—(1) *In general.* Except as provided in paragraph (h)(2) of this section, the rules of this section apply to amounts received after the [date of publication of the final regulations in the **Federal Register**].

(2) *Covered gifts and bequests.* Paragraph (c)(2)(ii) of this section is effective on the date final regulations under section 2801 are published in the **Federal Register** and applies to covered gifts or bequests received on or after that date.

■ **Par. 9.** Sections 1.6048–1 through 1.6048–7 are added to read as follows:

§ 1.6048–1 Scope.

(a) *In general.* Sections 1.6048–1 through 1.6048–7 provide rules concerning information that must be reported under section 6048 with respect to foreign trusts. This section provides general definitions for purposes of §§ 1.6048–1 through 1.6048–7. Section 1.6048–2 provides rules requiring a responsible party to provide notice of a reportable event that occurs during the taxable year with respect to a foreign trust. Section 1.6048–3 provides rules applicable to a U.S. owner of a foreign trust to ensure that the trust provides certain information about the trust's activities and operations for the year to the Commissioner and to any U.S. person (within the meaning of section 7701(a)(30)) who is treated as an owner of the trust or who receives a distribution from the trust. Section 1.6048–4 provides rules requiring a U.S. person to report the receipt of a distribution from a foreign trust during the U.S. person's taxable year. Section 1.6048–5 provides exceptions to the rules of §§ 1.6048–2 through 1.6048–4. Section 1.6048–6 provides certain special rules, including rules concerning dual resident taxpayers (within the meaning of § 301.7701(b)–7(a)(1) of this chapter) and dual status taxpayers (described in § 1.6012–1(b)(2)(ii)) who compute their U.S. income tax liability as nonresident aliens for part or all of the taxable year. Section 1.6048–7 provides applicability dates. For civil penalties that apply for failure to comply with the requirements of §§ 1.6048–2 through 1.6048–4, *see* § 1.6677–1. For penalties that apply to understatements of tax that are attributable to transactions involving undisclosed foreign financial assets, including assets with respect to which information was required to be provided under section 6048 but was not provided, *see* section 6662(b)(7) and (j). For suspension of the statute of limitations when required information has not been provided under section 6048, *see* section 6501(c)(8).

(b) *Definitions.* The following definitions apply for purposes of this section and §§ 1.6048–2 through 1.6048–7:

(1) *Executor.* The term *executor* means an executor within the meaning of section 2203.

(2) *Foreign person.* The term *foreign person* means any person who is not a *U.S. person* within the meaning of paragraph (b)(4) of this section.

(3) *Foreign trust.* The term *foreign trust* means a foreign trust within the meaning of § 301.7701–7.

(4) *Grantor trust.* The term *grantor trust* means a trust or any portion of a trust that is treated as owned by any person under subpart E of part I of subchapter J of chapter 1 of the Internal Revenue Code.

(5) *Grantor trust rules.* The term *grantor trust rules* means the rules under subpart E of part I of subchapter J of chapter 1 of the Internal Revenue Code.

(6) *Nongrantor trust.* The term *nongrantor trust* means a trust or any portion of a trust that is not treated as owned by any person under subpart E of part I of subchapter J of chapter 1 of the Internal Revenue Code.

(7) *U.S. person.* The term *U.S. person* means any person who is a U.S. person within the meaning of section 7701(a)(30) but not including certain dual resident taxpayers and dual status taxpayers as described in § 1.6048–6(a).

§ 1.6048–2 Notice of reportable events.

(a) *In general*—(1) *Filing requirement.* Unless an exception in § 1.6048–5 applies, a responsible party (as defined in paragraph (c) of this section) must provide written notice of any reportable event (as defined in paragraph (b) of this section) that occurs during the taxable year of the U.S. person described in paragraph (b) of this section on Part I of Form 3520, Annual Return To Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts. If a responsible party must report a reportable event with regard to more than one foreign trust during the taxable year, the responsible party must file a separate Form 3520 for each such foreign trust. *See* §§ 1.679–1 and 1.684–1 for additional rules regarding transfers to foreign trusts by U.S. persons. *See* § 1.6048–6(d) for information reporting by married U.S. persons who file a joint income tax return.

(2) *Due dates*—(i) *General rule.* Subject to paragraph (a)(2)(ii) and (iii) of this section, the responsible party must file Form 3520 by the fifteenth day of

the fourth month after the close of the responsible party's taxable year. If the responsible party has been granted an extension of time to file the responsible party's income tax return pursuant to section 6081, an extension of time for filing Form 3520 is granted to the fifteenth day of the tenth month following the close of the responsible party's taxable year. No additional extension of time to file Form 3520 is allowed beyond the fifteenth day of the tenth month following the close of the responsible party's taxable year.

(ii) *Filing by U.S. persons residing outside the United States.* In the case of a grantor or transferor (described in paragraph (c)(1) or (c)(2) of this section, respectively) who qualifies for an automatic extension to file the grantor's or transferor's income tax return under section 6081 and § 1.6081–5(a)(5) because the grantor or transferor resides outside of the United States and Puerto Rico and the grantor's or transferor's main place of business or post of duty is outside of the United States and Puerto Rico, the grantor or transferor must file Form 3520 by the fifteenth day of the sixth month after the close of the grantor's or transferor's taxable year. If the grantor or transferor has been granted an extension of time to file the grantor's or transferor's income tax return pursuant to section 6081, an extension of time for filing Form 3520 is granted to the fifteenth day of the tenth month following the close of the grantor's or transferor's taxable year. No additional extension of time to file Form 3520 is allowed.

(iii) *Filing by executor of grantor's or transferor's estate.* In the case of a deceased grantor or transferor, the executor of the grantor's or transferor's estate (within the meaning of paragraph (c)(3) of this section) must file Form 3520 by the fifteenth day of the fourth month following the close of the 12-month period which began with the first day of the grantor's or transferor's final taxable year. If the executor of the grantor's or transferor's estate has been granted an extension of time to file the grantor's or transferor's final income tax return pursuant to section 6081, an extension of time for filing Form 3520 is granted to the fifteenth day of the tenth month following the close of the 12-month period which began with the first day of the grantor's or transferor's final taxable year. No additional extension of time to file Form 3520 is allowed.

(b) *Reportable event.* Subject to § 1.6048–5, for purposes of this section, the term *reportable event* means any of the events described in paragraphs (b)(1) through (3):

(1) The creation of any foreign trust by any U.S. person.

(2) Any direct, indirect, or constructive transfer, within the meaning of § 1.679–3 or § 1.684–2, of property (including cash) to a foreign trust by a U.S. person, including a transfer by reason of death. In addition, a reportable event includes an outbound migration of a domestic trust, as described in § 1.684–4, without regard to whether any gain is taxable under § 1.684–1, and a U.S. person's transfer of property in exchange for any obligation of the foreign trust or of a person related to the trust, as described in § 1.679–4, without regard to whether the obligation is a qualified obligation.

(3) 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 subpart E of part I of subchapter J of chapter 1 of the Internal Revenue Code, or

(ii) Any portion of a foreign trust was included in the gross estate of the decedent for Federal estate tax purposes.

(c) *Responsible party.* For purposes of this section, the term *responsible party* means each of the following:

(1) The grantor (within the meaning of § 1.671–2(e)) in the case of the creation of an inter vivos trust.

(2) The transferor in the case of a reportable event described in paragraph (b)(2) of this section other than a transfer by reason of death.

(3) The executor of the deceased grantor's or transferor's estate in any other case (whether or not the executor is a U.S. person).

(d) *Examples.* The following examples illustrate the rules of this section.

(1) *Example 1: Creation and funding of foreign trust.* A, an attorney, creates a foreign trust, FT, on behalf of B, A's client. A and B are both U.S. persons. Shortly thereafter, B transfers $100x to FT. A and B are both grantors of FT under § 1.671–2(e), even though only B transferred property to FT. Under paragraph (b)(1) of this section, the creation of FT is a reportable event, and under paragraph (c)(1) of this section, A and B are responsible parties. Under paragraph (b)(2) of this section, the funding of FT is a reportable event, and under paragraph (c)(2) of this section, B is the responsible party. Accordingly, under paragraph (a) of this section, A must report the creation of FT and B must report the creation and the transfer to FT, respectively, on Part I of Form 3520.

(2) *Example 2: Transfers to two foreign trusts.* The facts are the same as in paragraph (d)(1) of this section (*Example 1*). B also transfers $100x to a second foreign trust, FT2, during the same taxable year. Under paragraph (a)(1) of this section, B must file two Forms 3520, one for the creation and funding of FT and one for the funding of FT2.

(3) *Example 3: Transfer by domestic trust to foreign trust.* Under the grantor trust rules, B is treated as the owner of a domestic trust, DT. B is a U.S. person and funds DT with $1,000x. Subsequently, B causes DT to transfer $600x to FT, an existing foreign trust. Under § 1.679–3(b), B is treated as transferring $600x to FT. Under paragraph (b)(2) of this section, the transfer is a reportable event. Under paragraph (c)(2) of this section, B is a responsible party. Accordingly, under paragraph (a) of this section, B is required to report the transfer to FT on Part I of Form 3520.

(4) *Example 4: Transfer by reason of death.* C, a U.S. person who files on a calendar year basis, is treated as the owner of a domestic trust, DT, under the grantor trust rules. The trust instrument provides that, upon C's death, DT will terminate and the trustee must distribute the trust corpus to a foreign trust, FT, for the benefit of C's children. C dies in Year 1. The trustee of DT distributes the trust corpus to FT in Year 1. The transfer to FT is a reportable event under paragraph (b)(2) of this section as a transfer by reason of C's death. Under paragraph (c)(3) of this section, the executor of C's estate is the responsible party. Accordingly, under paragraph (a) of this section, the executor of C's estate is required to report the transfer on Part I of Form 3520 by April 15, Year 2, the fifteenth day of the fourth month after the close of the 12-month period which began with the first day of C's final taxable year, as described in paragraph (a)(2)(ii) of this section. If C's executor is granted an extension of time to file C's final income tax return, then C's Form 3520 will have a 6-month extension and be due by October 15, Year 2.

(5) *Example 5: Death of U.S. citizen who was the owner of a foreign trust.* The facts are the same as in paragraph (d)(4) of this section (*Example 4*), except that C dies in Year 1 while C is treated as the owner of FT. Under paragraph (b)(3)(i) of this section, C's death is a reportable event. Under paragraph (c)(3) of this section, the executor of C's estate is a responsible party. Accordingly, under paragraph (a) of this section, the executor of C's estate is required to report C's death on Form 3520 by April 15, Year 2, the fifteenth day of the fourth month after the close of the 12-month period which began with the first

day of C's final taxable year, as described in paragraph (a)(2)(ii) of this section. If C's executor is granted an extension of time to file C's final income tax return for the year of decedent's death, then C's Form 3520 will also have an extension and be due by October 15, Year 2.

(6) *Example 6: Transfer in exchange for less than fair market value.* X, a U.S. person, sells property worth $1,000x to a foreign trust, FT, in exchange for $100x in cash. Under § 1.671–2(e)(2)(ii), the $900x excess amount is a gratuitous transfer by X to FT. Under § 1.679–3(a), X is treated as making a transfer of $900x to FT. Under paragraph (b)(2) of this section, the transfer is a reportable event. Under paragraph (c)(2) of this section, X is a responsible party. Accordingly, under paragraph (a) of this section, X is required to report the $900x transfer to FT on Part I of Form 3520.

(7) *Example 7: Creation and funding of trust in Puerto Rico by U.S. citizen.* X is a U.S. citizen and a bona fide resident of Puerto Rico. X creates and funds a trust, T, in Puerto Rico. T is subject to the primary jurisdiction of the Puerto Rican courts. Because T fails the court test of § 301.7701–7(a)(i), it is classified as a foreign trust under § 301.7701–7. Under paragraph (b)(1) and (2) of this section, the creation and funding of T are reportable events. Under paragraph (c)(1) and (2) of this section, X is a responsible party. Accordingly, under paragraph (a) of this section, X is required to report the creation and funding of T on Part I of Form 3520.

(8) *Example 8: Indirect transfer.* X, a U.S. person, creates FT, a foreign trust, for the benefit of X's children, who are U.S. citizens. On July 1, Year 1, X transfers ABC stock to X's brother, Y, a nonresident alien, for no consideration. Y immediately sells the ABC stock and uses the proceeds to purchase DEF stock. On January 5, Year 2, Y transfers the DEF stock to FT. X is related to Y within the meaning of § 1.679–3(c)(4). X cannot demonstrate to the satisfaction of the Commissioner that Y, as the intermediary, has a relationship with the beneficiaries of the trust that establishes a reasonable basis for concluding that the intermediary would make a transfer to FT, that Y acted independently of X, or that Y is not an agent of X. Thus, the transfer is deemed to be for the principal purpose of tax avoidance under § 1.679–3(c)(2). Under § 1.679–3(c)(1), X is treated as having made an indirect transfer of the DEF stock to FT on January 5, Year 2. Under § 1.679–3(c)(3), Y is treated as an agent of X, and the DEF stock is treated as transferred to FT by X. Under paragraph (b)(2) of this section, the transfer is a reportable event. Under paragraph (c)(2) of this section, X is a responsible party. Accordingly, under paragraph (a) of this section, X is required to report the transfer on Part I of Form 3520.

(9) *Example 9: Constructive transfer.* FT, a foreign trust, owes $100x to F Corp, an unrelated foreign corporation, for the performance of services by F Corp for the benefit of FT. In satisfaction of FT's liability to F Corp, X, a U.S. person, transfers to F Corp property with a fair market value of $100x. By satisfying FT's obligation, under § 1.679–3(d)(1), X is treated as having made a constructive transfer of property to FT. Under paragraph (b)(2) of this section, the transfer is a reportable event. Under paragraph (c)(2) of this section, X is a responsible party. Accordingly, under paragraph (a) of this section, X is required to report the transfer on Part I of Form 3520.

(10) *Example 10: Partial guarantee of foreign trust obligations.* F Corp, a foreign corporation, lends $100x to FT, a foreign trust, in exchange for FT's obligation to repay the loan. Knowing that F Corp would not have made the loan without a guarantee, X, a U.S. person related to FT under § 1.679–1(c)(5), gratuitously guarantees the repayment of $60x of FT's obligation. Under § 1.679–3(e), X is treated as having transferred $60x to FT. Under paragraph (b)(2) of this section, the transfer is a reportable event. Under paragraph (c)(2) of this section, X is a responsible party. Accordingly, under paragraph (a) of this section, X is required to report the transfer on Part I of Form 3520.

(11) *Example 11: Dual resident taxpayer.* The facts are the same as in paragraph (d)(10) of this section (*Example 10*) except that X is a dual resident taxpayer (within the meaning of § 301.7701(b)–7(a)(1)) who computes his U.S. tax liability as a nonresident alien for the taxable year during which he is treated as making the transfer. Pursuant to § 1.6048–6(a)(1), X is not treated as a U.S. person for that taxable year and is not required to report the transfer on Part I of Form 3520.

(12) *Example 12: Outbound migration of domestic nongrantor trust.* X, a U.S. person, transfers property to an irrevocable domestic trust, DT, for the sole benefit of X's daughter. DT is not treated as owned by X or any other person under the grantor trust rules. DB, a domestic bank, resigns as trustee when X dies, and FB, a foreign bank, becomes the replacement trustee under the terms of the trust. Pursuant to § 301.7701–7(d), DT becomes a foreign trust, FT. Under § 1.684–4(a), DT is treated as having transferred all of its assets to FT and is required to recognize gain on the transfer under § 1.684–1(a). Under paragraph (b)(2) of this section, the transfer is a reportable event. Under paragraph (c)(2) of this section, DT is the responsible party. Accordingly, under paragraph (a) of this section, DT is required to report the transfer on Part I of a Form 3520.

(13) *Example 13: Outbound migration of domestic grantor trust.* On January 2, Year 1, X, a U.S. person, transfers property with a fair market value of $100x and an adjusted basis of $40x to a revocable domestic trust, DT, for the benefit of A, a U.S. person. X is treated as the owner of DT under section 676. On January 15, Year 2, when the fair market value of all property transferred to DT by X is $150x, DT acquires a foreign trustee who has the power to determine whether and when distributions will be made to A. Under sections 7701(a)(30)(E) and 7701(a)(31)(B) and § 301.7701–7(d)(1)(ii)(A) and (d)(2)(i), DT becomes a foreign trust, FT, on January 15, Year 2. Under § 1.684–2(d), X is treated as transferring property with a fair market value of $150x to FT on January 15, Year 2, without regard to whether FT is a foreign grantor trust. Under paragraph (b)(2) of this section, the transfer is a reportable event. Under paragraph (c)(2) of this section, X is the responsible party. Under paragraph (a) of this section, X is required to report the transfer on Part I of Form 3520.

§ 1.6048–3 U.S. owners of foreign trusts.

(a) *U.S. owner requirement to ensure foreign trust information is provided*—(1) *In general.* Unless an exception in § 1.6048–5 applies, any U.S. person who is treated as an owner (*U.S. owner*) of a foreign trust or of any portion of a foreign trust under subpart E of part I of subchapter J of chapter 1 of the Internal Revenue Code during any taxable year is responsible for ensuring that, by the fifteenth day of the third month after the end of the foreign trust's taxable year, with a maximum extension of a 6-month period pursuant to section 6081, the foreign trust—

(i) Files Form 3520–A, Annual Information Return of Foreign Trust With a U.S. Owner (under section 6048(b)), under an identification number assigned to the trust (or portion of the trust) with the Commissioner in accordance with the instructions for Form 3520–A, and attaches copies of the statements required by paragraphs (a)(1)(ii) and (iii) of this section,

(ii) Furnishes a Foreign Grantor Trust Owner Statement in accordance with

the instructions for Form 3520–A for the taxable year to each U.S. owner; and

(iii) Furnishes a Foreign Grantor Trust Beneficiary Statement in accordance with the instructions for Form 3520–A for the taxable year to each U.S. person, other than the U.S. owner, to whom the trust has made a distribution (within the meaning of § 1.6048–4(b)), either directly or indirectly, during the trust's taxable year (each a *U.S. beneficiary*).

(2) *Substitute Form 3520–A filed by the U.S. owner.* If the foreign trust does not comply with the requirements of paragraph (a)(1) of this section, the U.S. owner must—

(i) Complete and file Part II of Form 3520, Annual Return To Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts, in accordance with the instructions for Form 3520 by the due date of the U.S. owner's Form 3520, as described in § 1.6048–2(a)(2) but as if ''U.S. owner'' replaces ''responsible party'' in § 1.6048–2(a)(2)(i) and as if ''U.S. owner'' replaces ''grantor or transferor'' in § 1.6048–2(a)(2)(ii) and (iii), as applicable; and

(ii) Complete Form 3520–A and related statements for each U.S. owner and U.S. beneficiary on behalf of the foreign trust and file them with the U.S. owner's Part II of Form 3520 by the due date of the U.S. owner's Form 3520 as provided in paragraph (a)(2)(i) of this section. Further, unless paragraph (a)(3) of this section applies, the U.S. owner must furnish the Foreign Grantor Trust Beneficiary Statement in accordance with the instructions for Form 3520–A to each U.S. beneficiary by the due date of the U.S. owner's Form 3520.

(3) *Certain fixed investment trusts.* A U.S. owner who is subject to the rules of this section is not required to provide information about the other persons who are treated as owners of the foreign trust if the foreign trust meets all requirements to qualify as a widely held fixed investment trust within the meaning of § 1.671–5(b)(22) other than the requirement that it be a U.S. person under section 7701(a)(30)(E).

(b) *Consistency rule*—(1) *In general.* Subject to paragraph (b)(2) of this section, U.S. owners or U.S. beneficiaries who receive a Foreign Grantor Trust Owner Statement or Foreign Grantor Trust Beneficiary Statement from a foreign trust must treat any item reported by the trust to such U.S. person in a manner that is consistent with the trust's treatment of such item on the Foreign Grantor Trust Owner Statement or Foreign Grantor Trust Beneficiary Statement.

(2) *Notification of inconsistent treatment.* If a U.S. owner's or U.S. beneficiary's treatment on such U.S. owner's or U.S. beneficiary's return is (or may be) inconsistent with the treatment of the item reported on a Foreign Grantor Trust Owner Statement or Foreign Grantor Trust Beneficiary Statement, then the U.S. owner or U.S. beneficiary must notify the Commissioner about the inconsistent treatment. The notification of inconsistent treatment must be made on a Form 8082, Notice of Inconsistent Treatment or Administrative Adjustment Request (AAR). Rules similar to the rules of section 6034A(c) (generally requiring beneficiaries of estates or trusts to file their returns in a manner that is consistent with information received from the estate or trust) will apply, including the rules for any adjustments required to make the treatment of reported items consistent in the case of a U.S. owner's or U.S. beneficiary's failure to notify the Commissioner about the inconsistent treatment.

(c) *Income tax determinations for foreign grantor trusts without U.S. agents.* If a foreign trust with a U.S. owner does not have a U.S. agent as described in paragraph (d) of this section, or if otherwise provided pursuant to paragraph (d)(5) of this section, then the amounts required to be taken into account with respect to the trust by the U.S. owner under the grantor trust rules are determined by the Commissioner based on all the facts and circumstances.

(d) *Authorization of a U.S. agent*—(1) *In general.* Paragraph (c) does not apply if a U.S. owner of a foreign trust ensures that the foreign trust authorizes a U.S. person to act as the trust's limited agent as described in paragraph (d)(2) of this section solely for purposes of applying sections 7602, 7603, and 7604 with respect to—

(i) Any request by the Commissioner to examine records or produce testimony related to the proper treatment of amounts required to be taken into account under the grantor trust rules, or

(ii) Any summons by the Commissioner for such records or testimony.

(2) *Requirements.* In order to authorize a U.S. person to act as an agent under paragraph (d)(1) of this section, a U.S. owner of a foreign trust must ensure that the trust and the agent enter into a binding authorization agreement that is executed by the foreign trust and the U.S. agent before the due date of Form 3520–A or substitute Form 3520–A (as described in § 1.6048–3(a)(1) and (2), respectively) for the taxable year that the U.S. owner is considered the owner of the trust. The authorization must remain in effect for as long as the statute of limitations remains open for the U.S. owner's relevant taxable year. If the agent resigns or liquidates or if the agent's responsibility is terminated, the U.S. owner of the foreign trust must ensure that the foreign trust notifies the Commissioner within 90 days, by filing an amended Form 3520–A. This notification must contain the name, address and Taxpayer Identification Number of the new U.S. agent.

(3) *Limitations.* The appearance of persons or production of records by reason of a U.S. person being an agent described in paragraph (d)(1) of this section will not subject such persons or records to legal process for any purpose other than determining the correct treatment of the amounts to be taken into account by the U.S. owner under paragraph (c) of this section.

(4) *No office, permanent establishment, or trade or business.* A foreign trust that appoints a U.S. agent described in paragraph (d)(1) of this section will 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 agent's activities as an agent pursuant to this section.

(5) *Summons issued to a U.S. agent*—(i) *In general.* Paragraph (c) of this section applies if a summons is issued to a U.S. person (either directly or as a limited agent of a foreign trust who is appointed pursuant to paragraph (d)(1) of this section) or to a foreign trust (where service of the summons can be effectuated) to produce any records or testimony in order to determine the amounts required to be taken into account under the grantor trust rules, and if—

(A) The summons is not quashed in a proceeding, if any, begun not later than the 90th day after the summons was issued and is not determined to be invalid in a proceeding, if any, begun under section 7604 to enforce the summons; and

(B) The Commissioner has sent by certified or registered mail a notice to the U.S. person or foreign trust of its determination that the U.S. person or foreign trust has not substantially and timely complied with the summons, and a proceeding to review the determination is not begun any later than 90 days after the notice is mailed. If such a proceeding is not begun on or before such 90th day, the determination by the Commissioner will be binding.

(ii) *Enforcement proceeding not required.* The Commissioner is not required to begin an enforcement

proceeding to enforce the summons in order to apply the rules of paragraph (d)(5) of this section.

(iii) *Suspension of statute of limitations.* If the U.S. person or foreign trust to which a summons is issued brings a proceeding to quash the summons not later than the 90th day after the summons was issued, or begins a proceeding to review a determination under paragraph (d)(5)(i)(B) of this section not later than the 90th day after the day on which the notice referred to in paragraph (d)(5)(i)(B) of this section was mailed, the running of any period of limitation under section 6501 (relating to assessment and collection of tax) or under section 6531 (relating to criminal prosecutions) for the taxable year or years to which the summons that is the subject of such proceeding relates will be suspended for the period during which the proceeding, and appeals therein, are pending. In no event will any such period expire before the 90th day after the day on which there is a final determination in the proceeding.

(e) *Examples.* The following examples illustrate the rules of this section.

(1) *Example 1: Fixed investment trust.* X, a U.S. person, is treated as an owner of a foreign trust, FT, that would be a widely held fixed investment trust within the meaning of § 1.671–5(b)(22) if it were a domestic trust. FT does not file a Form 3520–A for Year 1. Under paragraph (a)(2) of this section, X is required to complete and file Part II of Form 3520 by the due date for X's Year 1 Form 3520. In addition, under paragraph (a)(2) of this section, X is required to complete a substitute Form 3520–A and related statements and file them with X's Year 1 Form 3520. Under paragraph (a)(4) of this section, X is not required to provide information about the other owners of FT.

(2) *Example 2: Substitute Form 3520–A.* X, a U.S. person, is treated as the owner of a foreign trust, FT. FT's taxable year ends on December 31. On November 1, Year 1, FT makes a distribution to Y, a U.S. beneficiary of the trust. FT fails to comply with the requirements of paragraph (a)(1) of this section for its taxable year ending December 31, Year 1. Under paragraph (a)(2) of this section, X is required to complete and file Part II of Form 3520 by the due date for X's Year 1 Form 3520. In addition, under paragraph (a)(2) of this section, X is required to complete a substitute Form 3520–A and related statements and file them with X's Year 1 Form 3520. X must furnish a Foreign Grantor Trust Beneficiary Statement to Y by the due date for X's Year 1 Form 3520.

(3) *Example 3: Failures to appoint U.S. agent and to respond to summons.* X, a U.S. person, is treated as the owner of a foreign trust, FT. FT does not appoint a U.S. agent described in paragraph (d)(1) of this section. The Commissioner issues a summons to X for the production of records of FT related to the proper treatment of amounts required to be taken into account by X under the grantor trust rules. Neither X nor FT responds to the summons. Under paragraph (c) of this section, the Commissioner may determine the amount that X must take into account under the grantor trust rules based on all the facts and circumstances.

(4) *Example 4: Multiple trusts and multiple transactions.* X, a U.S. person, is treated as the owner of two foreign trusts, FT1 and FT2. During Year 1, X transfers cash to FT1 and receives a distribution from FT2. FT1 and FT2 fail to comply with the requirements of paragraph (a)(1) of this section for their taxable years ending in Year 1. Under § 1.6048–2 and paragraph (a)(2) of this section, X must report X's transfer to, and ownership of, FT1 on one Form 3520, and under § 1.6048–4 and paragraph (a)(2) of this section, X must report X's ownership of, and distribution from, FT2 on a second Form 3520. In addition, under paragraph (a)(2)(ii) of this section, X must complete a substitute Form 3520–A for each trust, FT1 and FT2, and file them with X's Year 1 Form 3520 for each trust.

(5) *Example 5: Dual resident taxpayer.* (i) X is a lawful permanent resident of the United States within the meaning of § 301.7701(b)–1(b) of this chapter and a tax resident of Country F under the domestic tax law of Country F. X is treated as a resident of Country F under the residence article of the U.S.-Country F income tax treaty (the treaty). Pursuant to § 301.7701(b)–7 of this chapter, X is treated as a nonresident alien for purposes of computing X's U.S. income tax liability for Year 1. During Year 1, X transfers $100x to a foreign trust, FT, for the benefit of X's children, who are U.S. citizens. Under § 1.6048–6(a), X is not treated as a U.S. person and is not required to report the transfer under § 1.6048–2 on a Form 3520 for Year 1.

(ii) In Year 2, X waives any benefits to which X would have been entitled under the treaty and computes X's U.S. income tax liability as a resident alien. Under § 1.679–5(a), X is treated as having made a transfer to FT on January 1, Year 2, in the amount of the fair market value of FT as of that date. Under § 1.679–1(a), X is treated as the owner of FT as of January 1, Year 2. Under § 1.6048–2(a), X is required to file a Form 3520 for Year 2 on which X reports the transfer to FT. If FT fails to comply with the requirements of paragraph (a)(1) of this section for FT's taxable year ending in Year 2, under paragraph (a)(2) of this section, X also must complete and file Part II of Form 3520, and complete and file a substitute Form 3520–A with the related statements attached to X's Year 2 Form 3520.

§ 1.6048–4 Reporting by U.S. persons receiving distributions from foreign trusts.

(a) *Reporting of trust distributions.* Unless an exception in § 1.6048–5 applies, any U.S. person who receives directly or indirectly any distribution from a foreign trust (without regard to whether any person is treated as the owner of the foreign trust under the rules of subpart E of part I of subchapter J of chapter 1) must file Part III of Form 3520, Annual Return To Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts, by the due date of the U.S. person's Form 3520, as described in § 1.6048–2(a)(2) by replacing ''responsible party'' with ''U.S. person'' in § 1.6048–2(a)(2)(i) and by replacing ''grantor or transferor'' with ''U.S. person'' in § 1.6048–2(a)(2)(ii) and (iii), as applicable. *See* § 1.6048–6(d) for information reporting by married U.S. persons who file a joint income tax return.

(b) *Distribution*—(1) *In general.* Except as provided in paragraphs (b)(5)(ii) and (b)(6)(ii) of this section, a *distribution* means any transfer of property (including cash) from a foreign trust received directly or indirectly by a U.S. person to the extent such property exceeds the fair market value of any property or services received by the foreign trust in exchange for the property transferred, without regard to whether any portion of the foreign trust is treated as owned by the grantor or another person under the rules of subpart E of part I of subchapter J of chapter 1, whether the recipient is designated as a beneficiary by the terms of the foreign trust, or whether the distribution has any income tax consequences. A distribution includes any amount, including without limitation a gift or bequest described in section 663(a), actually or constructively received by a U.S. person. For these purposes, a transfer of property from a foreign trust to a grantor trust or to a disregarded entity (as defined in § 1.643(i)–1(d)(3) of this chapter) is treated as a distribution to the owner of the grantor trust or of the disregarded entity, respectively. For example, a

transfer of property from a foreign trust to a single member LLC treated as a disregarded entity is treated as a distribution to the owner of the LLC. For distributions through intermediaries, see paragraph (b)(2) of this section; for distributions from entities owned by a foreign trust, see paragraph (b)(3) of this section; for inbound migrations of foreign trusts, see paragraph (b)(4) of this section; for loans of cash or marketable securities, see paragraph (b)(5) of this section; for use of trust property, see paragraph (b)(6) of this section; and for the receipt of covered gifts or bequests from a foreign trust, see paragraph (b)(7) of this section.

(2) *Distributions from foreign trusts through intermediaries*—(i) *In general.* A distribution includes any transfer of property from a foreign trust received by a U.S. person through an intermediary, nominee, or agent. In such a case, except as otherwise provided in paragraph (b)(2)(ii) of this section, the intermediary, nominee, or agent is treated as an agent of the foreign trust and the property is treated as distributed from the foreign trust to the U.S. person in the year the property is received by or made available by the intermediary, nominee, or agent to the U.S. person.

(ii) *Special rule.* If the Commissioner determines that the intermediary, nominee, or agent is an agent of the U.S. person, the property is treated as distributed from the foreign trust to the U.S. person in the year the property is received by the intermediary, nominee, or agent. In such case, the intermediary, nominee, or agent is not treated as distributing the property to the U.S. person when the property is subsequently received by or made available by the intermediary, nominee, or agent to the U.S. person.

(iii) *Reporting indirect transfers of property.* An indirect transfer of property from a foreign trust must be reported on Part III of Form 3520 without regard to whether the receipt of such property would be treated as having any income tax consequences to the U.S. person receiving such property, to a U.S. grantor or beneficiary of the foreign trust, or to a U.S. owner of the foreign trust.

(3) *Distributions from entities owned by a foreign trust.* A distribution includes any transfer of property from an entity in which a foreign trust directly or indirectly holds an ownership interest that is received by a U.S. person who is a related person (as defined in § 1.679–1(c)(5)) with respect to the foreign trust. In such case, the transfer of the property by the entity owned by the foreign trust to the U.S. person is treated as a distribution of such property by the entity to the foreign trust followed by a distribution of the property from the foreign trust to the U.S. person, unless the U.S. person demonstrates to the satisfaction of the Commissioner that the distribution from the entity is properly attributable to the U.S. person's ownership interest in the entity.

(4) *Inbound migrations of foreign trusts.* A distribution includes an inbound migration of a foreign trust. An inbound migration of a foreign trust occurs when a foreign trust becomes a domestic trust. In such case, the foreign trust is treated as distributing the trust corpus and income to the domestic trust on the date the foreign trust becomes a domestic trust.

(5) *Loans of cash or marketable securities*—(i) *In general.* A distribution includes any loan of cash or marketable securities made from a foreign trust (whether from trust corpus or income) directly or indirectly to a U.S. person. For these purposes, a loan to a grantor trust or to a disregarded entity (as defined in § 1.643(i)–1(d)(3) of this chapter) will be treated as a loan to the owner of the grantor trust or of the disregarded entity, respectively. For example, a loan to a single member LLC treated as a disregarded entity will be treated as a loan to the owner of the LLC. Loans from a foreign trust include:

(A) A loan of cash or marketable securities made by any person to a U.S. person, if the foreign trust provides a guarantee (within the meaning of § 1.679–3(e)(4)) for the loan, and

(B) A loan of cash or marketable securities made by any intermediary, nominee or agent of a foreign trust to a U.S. person.

(ii) *Section 643(i) loans of cash or marketable securities.* A distribution includes a direct or indirect loan of cash or marketable securities from a foreign nongrantor trust to any U.S. grantor or beneficiary (within the meaning of § 1.643(i)–1(d)(11) or (1), respectively) or a U.S. person related (within the meaning of § 1.643(i)–1(d)(9)) to a U.S. grantor or beneficiary regardless of whether the loan was made in exchange for a qualified obligation within the meaning of § 1.643(i)–2(b)(2)(iii). For these purposes, indirect loans include loans described in § 1.643(i)–1(b)(2).

(iii) *Reporting loans of cash or marketable securities.* A loan of cash or marketable securities made from a foreign trust must be reported by the U.S. person described under paragraph (b)(5)(i) of this section and by the U.S. grantor or beneficiary described under paragraph (b)(5)(ii) of this section on Part III of Form 3520, Annual Return to Report Transactions with Foreign Trusts and Receipt of Certain Foreign Gifts, without regard to whether the loan would be treated as having any income tax consequences to a U.S. grantor or beneficiary (within the meaning of § 1.643(i)–1(d)(11) or (1), respectively) of the foreign trust.

(6) *Use of trust property*—(i) *In general.* A distribution includes the fair market value of the direct or indirect use of any property of a foreign trust by a U.S. person. For these purposes, use of property of a foreign trust by a grantor trust or by a disregarded entity (as defined in § 1.643(i)–1(d)(3)) will be treated as the use of trust property by the owner of the grantor trust or of the disregarded entity, respectively. For example, use of trust property by a single member LLC treated as a disregarded entity will be treated as use of trust property by the owner of the LLC.

(ii) *Section 643(i) use of trust property.* A distribution includes the fair market value of the direct or indirect use of any property of a foreign nongrantor trust by a U.S. grantor or beneficiary (within the meaning of § 1.643(i)–1(d)(11) or (1), respectively) or a U.S. person related (within the meaning of § 1.643(i)–1(d)(9)) to a U.S. grantor or beneficiary without regard to whether the foreign trust is paid the fair market value for such use. For these purposes, indirect use of trust property includes the use described in § 1.643(i)–1(c)(2).

(iii) *Reporting use of trust property.* The use of trust property must be reported by the U.S. person described under paragraph (b)(6)(i) of this section and by the U.S. grantor or beneficiary described under paragraph (b)(6)(ii) of this section on Part III of Form 3520, Annual Return to Report Transactions with Foreign Trusts and Receipt of Certain Foreign Gifts, without regard to whether the use of trust property would be treated as having any income tax consequences to a U.S. grantor or beneficiary (within the meaning of § 1.643(i)–1(d)(11) or (1), respectively) of the foreign trust.

(7) *Certain covered gifts or bequests.* A distribution includes any covered gift or bequest (described in section 2801(e)) that is received as a distribution from a foreign trust.

(c) *Statements provided by foreign trust*—(1) *Foreign grantor trust with U.S. owner*—(i) *Owner statement.* Pursuant to § 1.6048–3(a)(1)(ii), a U.S. owner of a foreign trust (or portion of a foreign trust) should receive a Foreign Grantor Trust Owner Statement.

(ii) *Statement for U.S. person receiving a distribution.* Pursuant to

§ 1.6048–3(a)(1)(iii), a U.S. person, other than a U.S. owner, who receives a distribution from a foreign grantor trust (or portion of a foreign grantor trust) should receive a Foreign Grantor Trust Beneficiary Statement.

(2) *Foreign nongrantor trust.* A foreign nongrantor trust may issue, by the fifteenth day of the third month after the end of the trust's taxable year, a Foreign Nongrantor Trust Beneficiary Statement to each U.S. person who receives a distribution from the foreign trust during the trust's taxable year.

(3) *Foreign grantor trust with foreign owner.* A foreign trust that is treated as owned by a foreign person under the grantor trust rules may issue, by the fifteenth day of the third month after the end of the trust's taxable year, a Foreign-Owned Grantor Trust Beneficiary Statement to each U.S. person who receives a distribution.

(d) *Tax consequences of distributions*—(1) *In general.* Subject to paragraph (e) of this section, a U.S. person (other than a U.S. person described in § 1.6048–4(c)(1)(i)) who receives a distribution (other than a distribution described in § 1.6048–4(b)(5) or (6) that is not treated as a section 643(i) distribution under § 1.643(i)–1) from a foreign trust must determine the tax consequences of the distribution as follows, unless the distribution is received in a year that the foreign trust terminates. For rules determining the tax consequences of a distribution in the year a foreign trust terminates, *see* paragraphs (d)(3)(i)(B) and (d)(3)(iii) of this section.

(i) A U.S. person who receives a Foreign Grantor Trust Beneficiary Statement or a Foreign-Owned Grantor Trust Beneficiary Statement before the due date of the U.S. person's income tax return (including extensions) must determine the income tax consequences of the distribution from the trust as a distribution being made from a grantor trust.

(ii) A U.S. person who receives a Foreign Nongrantor Trust Beneficiary Statement before the due date of the U.S. person's income tax return (including extensions) may determine the income tax consequences of the distribution under either the actual calculation method described in paragraph (d)(2) of this section or the default calculation method described in paragraph (d)(3) of this section, unless the U.S. person knows or has reason to know that the information in the statement is incorrect or the U.S. person has previously used the default calculation method with respect to distributions from the same foreign trust.

(iii) In all other cases, including when a U.S. person does not receive a statement described in § 1.6048–4(c) before the due date of the U.S. person's income tax return (including extensions), the U.S. person must use the default calculation method described in paragraph (d)(3) of this section.

(2) *Actual calculation method.* Under the actual calculation method, the tax consequences of the distribution are determined by using actual information about the foreign trust as provided in the Foreign Nongrantor Trust Beneficiary Statement described in § 1.6048–4(c)(2) and applying the rules of subparts C and D of Part I of subchapter J of chapter 1 of the Internal Revenue Code.

(3) *Default calculation method*—(i) *Consequences to U.S. person who receives a distribution from a foreign trust*—(A) *In general.* Under the default calculation method, the tax consequences of the distribution are determined by allocating the distribution between a distribution of current income and a distribution of accumulated income under the rules of this paragraph (d)(3). The portion of the distribution that is treated as a distribution of current income is 125% of the average distribution that the U.S. person received from the foreign trust during the immediately preceding three taxable years (or the number of years during which the trust has been a foreign trust, if fewer than three years). The remainder of the distribution, if any, is treated as an accumulation distribution within the meaning of section 665(b) that is subject to an interest charge under section 668. For purposes of computing the interest charge (in the absence of actual information provided on a statement described in § 1.6048–4(c)), the U.S. person must assume that the applicable number of years the trust has been in existence is ten years and that no taxes described in section 665(d) have been imposed on the trust in any applicable previous year (even if a distribution had been made and tax under section 665(d) had been imposed).

(B) *Year of trust termination.* Unless paragraph (d)(3)(iii) of this section applies, the tax consequences of a distribution in the year a foreign trust terminates are determined by treating the distribution as an accumulation distribution within the meaning of section 665(b) that is subject to an interest charge under section 668 for any amount in excess of the portion of the distribution that is treated as a distribution of current income described in paragraph (d)(3)(i)(A) of this section.

(ii) *Consequences to trust.* A foreign trust must determine the income tax consequences of distributions to U.S. persons by applying the applicable rules of part I of subchapter J of chapter 1 of the Internal Revenue Code.

(iii) *Actual calculation method in year of foreign trust termination after using the default calculation method.* A U.S. person who has previously used the default calculation method with respect to distributions from a foreign trust may, for the year in which the foreign trust terminates, determine the tax consequences of a distribution from the same trust by using the actual calculation method provided that, before the due date of the U.S. person's income tax return (including extensions), the trust provides to the U.S. person complete and accurate information about all previous distributions from such foreign trust. The U.S. person must use this information to recalculate the tax effect of all previous distributions from such foreign trust under the actual calculation method in order to determine the portion attributable to current income, accumulated income, and principal in the year that the foreign trust terminates. A U.S. person described in this paragraph (d)(3)(iii) may not use the actual calculation method for the year that the foreign trust terminates if the U.S. person knows or has reason to know that the information provided by the foreign trust is incorrect.

(iv) *Example.* The following example illustrates the rules of paragraph (d)(3)(i) of this section. B, a U.S. person, is a beneficiary of a foreign nongrantor trust, FT, that was established in Year 1. In Year 2, Year 3, and Year 4, B received distributions from FT of $100x, $200x, and $300x respectively. In Year 5, B receives a $400x distribution from FT. To determine the tax consequences of the Year 5 distribution, B applies the default calculation method. Under the default calculation method, the average distribution that B received from FT during the preceding three years is $200x and 125% of such average distribution is $250x. Therefore, $250x of the Year 5 distribution is treated as a distribution of current income and the remaining $150x is treated as an accumulation distribution. The $150x that is treated as an accumulation distribution is subject to an interest charge under section 668. B must report the distribution and the default calculation on Part III of Form 3520 for Year 5.

(e) *Distribution treated as accumulation distribution if records are not provided.* If adequate records are not

provided to the Commissioner to determine the proper treatment of any distribution from a foreign trust (within the meaning of paragraph (b) of this section) other than a loan or use of trust property that is not treated as a section 643(i) distribution under § 1.643(i)–1, the entire distribution will be treated as an accumulation distribution includible in the gross income of the U.S. person who received the distribution under chapter 1 of the Internal Revenue Code. However, if the trustee of a foreign trust authorizes a U.S. person to act as the trust's limited agent under rules prescribed in § 1.6048–3(d), then the tax consequences of the distribution may be determined under the rules described in paragraph (d)(1) of this section.

(f) *Interaction with § 1.6039F–1.* If a U.S. person receives a distribution from a foreign trust, the U.S. person must report the distribution under paragraph (a) of this section and not under § 1.6039F–1(a), regardless of whether the distribution is taxable to the U.S. person receiving the distribution. *See* § 1.6039F–1(b).

(g) *Examples.* The following examples illustrate the rules of this section. In each example, X is a U.S. citizen, FT is a foreign trust, and FC is a foreign corporation.

(1) *Example 1: Payment of liability treated as distribution.* X owes $1,000x to Y for services that Y performed for X. In satisfaction of X's liability to Y, FT transfers to Y property with a fair market value of $1,000x. Under paragraph (b)(1) of this section, FT's transfer of property to Y is constructively received by X from FT, and is a distribution in the amount of $1,000x to X for purposes of this section. Under paragraph (a) of this section, X must report the distribution on Part III of Form 3520.

(2) *Example 2: Assumption of liability treated as distribution.* The facts are the same as in paragraph (g)(1) of this section (*Example 1*) except that FT assumes X's liability to pay Y. The result is the same as in paragraph (g)(1) of this section (*Example 1*).

(3) *Example 3: Trust's partial guarantee of U.S. person's obligation treated as distribution from foreign trust.* Y lends $1,000x of cash to X in exchange for X's obligation to repay the loan. X is a U.S. person. FT guarantees the repayment of $600x of X's obligation. Under paragraph (b)(5)(i)(A) of this section, FT's guarantee of X's obligation is a distribution from FT to X in the amount of $600x. Under paragraph (a) of this section, X must report the distribution on Part III of Form 3520.

(4) *Example 4: Section 643(i) loan not in exchange for qualified obligation.* X's sister, A, and A's husband, B, are both U.S. citizens. X, A, and B are U.S. persons within the meaning of § 1.643(i)–1(d)(12), and X is related to B under § 1.643(i)–1(d)(9). B is a beneficiary of FT, a nongrantor trust. In Year 1, FT lends $100x to X in exchange for a demand note that permits FT to require repayment by X at any time. The demand note issued by X is not a qualified obligation within the meaning of § 1.643(i)–2(b)(2)(iii) because X's obligation to FT could remain outstanding for more than five years. Accordingly, the loan from FT to X is treated as a section 643(i) distribution of $100x to B under § 1.643(i)–1(a). The loan is a distribution from FT to X and B under paragraph (b)(5)(ii) of this section. Under paragraphs (a) and (b)(5)(iii) of this section, X and B each must report the distribution on Part III of Form 3520.

(5) *Example 5: Section 643(i) loan in exchange for qualified obligation.* The facts are the same as in paragraph (g)(4) of this section (*Example 4*) except that the loan cannot remain outstanding for more than five years and it is a qualified obligation within the meaning of § 1.643(i)–2(b)(2)(iii). Although the loan is not a section 643(i) distribution within the meaning of § 1.643(i)–1(a), the loan nevertheless is a distribution from FT to X and to B under paragraph (b)(5)(ii) of this section. Under paragraphs (a) and (b)(5)(iii) of this section, X and B each must report the distribution on Part III of Form 3520.

(6) *Example 6: Distribution through intermediary.* Y, a nonresident alien, created FT in 1980 for the benefit of Y's children and their descendants, all of whom are U.S. persons. FT's trustee, T, determines that $100x of accumulated income should be distributed to X, one of Y's children. Pursuant to a plan with a principal purpose of avoiding the interest charge that would be imposed on an accumulation distribution from a foreign trust by section 668, T makes a gratuitous transfer from FT of $100x to N, a foreign person. N subsequently makes a gratuitous transfer of $100x to X. Under § 1.643(h)–1(a)(1), FT is deemed to have made an accumulation distribution of $100x to X. The distribution through N as the intermediary is treated as a distribution under paragraph (b)(2)(i) of this section. Under paragraphs (a) and (b)(2)(iii) of this section, X must report the distribution on Part III of Form 3520.

(7) *Example 7: Excess payment in exchange for property.* X transfers to FT property with a fair market value of $200x in exchange for a payment of $500x. Under paragraph (b)(1) of this section, the excess amount of $300x is treated as a distribution from FT to X. Under paragraph (a) of this section, X must report the distribution of $300x on Part III of Form 3520.

(8) *Example 8: Excess payment in exchange for services.* X receives a payment of $100x from FT purportedly in exchange for X's performance of services as a trustee of FT. The fair market value of the services performed is $20x. Under paragraph (b)(1) of this section, X is treated as receiving a distribution of $80x from FT. Under paragraph (a) of this section, X must report the distribution of $80x on Part III of Form 3520.

(9) *Example 9: Distribution from entity owned by foreign trust.* FT owns all of the outstanding stock of FC. FC distributes $100x directly to X, a related person within the meaning of § 1.679–1(c)(5) with respect to FT. Because FT is the sole shareholder of FC, X is unable to demonstrate to the satisfaction of the Commissioner that the distribution is properly attributable to X's ownership interest in FC. Accordingly, under paragraph (b)(3) of this section, X is treated as receiving a distribution of $100x from FT. Under paragraph (a) of this section, X must report the distribution of $100x on Part III of Form 3520.

(10) *Example 10: Distribution from entity co-owned by foreign trust.* FC has 100 outstanding shares of stock. FT owns 25 shares of FC stock, X owns 50 shares, and N, a nonresident alien, owns the remaining 25 shares. In Year 1, FC distributes a dividend of $25x to each of FT and N and $50x to X. Because the distribution was made to FT, X, and N in proportion to their ownership interests in FC and X reports $50x as a dividend on X's timely filed income tax return for Year 1, X is able to demonstrate to the satisfaction of the Commissioner that the distribution is properly attributable to X's ownership interest in FC. Accordingly, under paragraph (b)(3) of this section, X is not treated as receiving a reportable distribution of $50x from FT.

(11) *Example 11: Foreign trust becomes domestic trust.* FB, a foreign bank, resigns as trustee of FT, and DB, a domestic bank, becomes the new trustee of FT. Pursuant to section 7701(a)(30)(E), FT becomes a domestic trust, DT. Under paragraph (b)(4) of this section, DT is treated as receiving a distribution of the trust corpus and income from FT. Under paragraph (a) of this section, DT must report the deemed distribution of the trust corpus and income on Part III of Form 3520 for the

year in which the inbound migration occurs.

(12) *Example 12: Distribution received by domestic trust.* T, as trustee of FT, has the power to decant. Exercising that power, T distributes the trust corpus and income of FT to DT, a domestic trust. Neither FT nor DT is a grantor trust. Under paragraph (b)(1) and (4) of this section, DT receives a distribution of the trust corpus and income from FT. Under paragraph (a) of this section, DT must report the distribution of the trust corpus and income on Part III of Form 3520 for the year in which the decanting occurs.

(13) *Example 13: Distribution received by U.S. owner.* X is treated as the owner of FT under section 679. X receives a distribution from FT. Under paragraph (a) of this section, X must report the distribution on Part III of Form 3520.

(14) *Example 14: Distribution from trust owned by another person.* X receives a distribution from FT. Y, a nonresident alien, is treated as the owner of FT under the grantor trust rules. X receives a completed Foreign-Owned Grantor Trust Beneficiary Statement. Under paragraph (a) of this section and § 1.6048–6(b), X must file Form 3520 for the year of the distribution.

(15) *Example 15: Use of default calculation method if statement not provided.* The facts are the same as in paragraph (g)(14) (*Example 14*) except that X does not receive a Foreign-Owned Grantor Trust Beneficiary Statement from FT. Pursuant to paragraph (d)(3) of this section, X must determine the tax consequences of the distribution using the default calculation method. Under the default calculation method, X must include the distribution in income in accordance with rules prescribed in paragraph (d)(3) of this section and in the Instructions for Form 3520 for the applicable taxable year.

(16) *Example 16: Distribution attributable to covered gift.* Z relinquishes Z's U.S. citizenship on September 15, Year 1. Z is a covered expatriate within the meaning of section 877A(g)(1). On August 1, Year 2, Z creates and transfers $300x to a foreign trust, FT, for the benefit of Z's son, S, a U.S. citizen. On December 30, Year 3, S receives a $40x distribution from FT. Whether or not the entire amount of the distribution is a covered gift within the meaning of section 2801(e), under paragraph (b)(7) of this section, the $40x is a distribution. Under paragraph (a) of this section, S must report the distribution on Part III of Form 3520. S also may have additional reporting requirements under section 2801 for the covered gift.

§ 1.6048–5 Exceptions.

(a) *Exceptions under section 6048(a)(3)(B).* For purposes of § 1.6048–2, a reportable event does not include any of the following:

(1) Any transfer of property to a foreign trust to the extent the transfer is a transfer for fair market value within the meaning of § 1.679–4(b), provided that the transfer is not one made by a U.S. person that is a related person (as defined in § 1.679–1(c)(5)) with respect to the foreign trust in exchange for an obligation of the trust or of a related person (without regard to whether such obligation is a qualified obligation described in § 1.679–4(d));

(2) Any transfer of property to a foreign trust described in section 402(b), 404(a)(4), or 404A; and

(3) Any transfer of property to a foreign trust, provided that the trust has received a determination letter from the Commissioner that has not been revoked recognizing that the foreign trust is exempt from Federal income tax under section 501(a) as an organization described in section 501(c)(3).

(b) *Exceptions for certain tax-favored foreign trusts*—(1) *In general.* Sections 6048(a) through 6048(c) and §§ 1.6048–2 through 1.6048–4 do not apply to any eligible individual's transactions with, or ownership of, a tax-favored foreign retirement trust as defined under paragraph (b)(2) of this section or a tax-favored foreign non-retirement savings trust as defined under paragraph (b)(3) of this section. For purposes of this paragraph (b)(1), an *eligible individual* means an individual who is, or at any time was, a U.S. person and who, for any period during which an amount of tax may be assessed under section 6501 (without regard to section 6501(c)(8)), is compliant (or comes into compliance) with all requirements for filing a Federal income tax return (or returns) covering the period such individual was a U.S. person, and to the extent required under U.S. tax law, has reported as income any contributions to, earnings of, or distributions from an applicable tax-favored foreign trust on the applicable return (including on an amended return).

(2) *Tax-favored foreign retirement trust.* For purposes of this section, a *tax-favored foreign retirement trust* means a foreign trust that is created, organized, or otherwise established under the laws of a foreign jurisdiction (*the trust's jurisdiction*) as a trust, plan, fund, scheme, or other arrangement (collectively, a *trust*) to operate exclusively or almost exclusively to provide, or to earn income for the provision of, pension or retirement benefits and ancillary or incidental benefits, and that meets the following requirements established by the laws of the jurisdiction governing the trust:

(i) The trust generally is exempt from income tax or otherwise is tax-favored under the laws of the trust's jurisdiction. For purposes of this section, a trust is tax-favored under the laws of the trust's jurisdiction if it meets any one or more of the following conditions:

(A) Contributions to the trust that otherwise would be subject to tax are deductible or excluded from income, are taxed at a reduced rate, give rise to a tax credit, or otherwise are eligible for another tax benefit (such as a government subsidy or contribution); or

(B) Taxation of investment income earned by the trust is deferred until distribution or the investment income is taxed at a reduced rate (including exempt from tax).

(ii) Annual information reporting with respect to the trust (or of its participants or beneficiaries) is provided, or otherwise is available, to the relevant tax authorities in the trust's jurisdiction.

(iii) Generally, only contributions with respect to income earned from the performance of personal services are permitted (with allowances made for limited contributions made by unemployed individuals).

(iv) The trust meets either the value threshold in paragraph (b)(2)(iv)(*1*) or any one of the contribution limitations in paragraph (b)(2)(iv)(*2*) of this section:

(*1*) *Value threshold.* The aggregate value of the trust(s) in the trust's jurisdiction is limited to no more than $600,000 at any point during the taxable year (as adjusted under paragraph (b)(2)(iv)(*3*) of this section) regardless of the number of trusts established.

(*2*) *Contribution limitations.* The contributions to the trust(s) in the trust's jurisdiction are limited to any one of the following:

(*i*) A percentage of earned income of the participant,

(*ii*) An annual limit of $75,000 (as adjusted under paragraph (b)(2)(iv)(*3*) of this section) or less, or

(*iii*) A lifetime limit of $1,000,000 (as adjusted under paragraph (b)(2)(iv)(*3*) of this section) or less.

(*3*) *Dollar limitations subject to adjustments*—(*i*) The value threshold in paragraph (b)(2)(iv)(*1*) and contribution limits in paragraph (b)(2)(iv)(*2*) of this section are determined using the U.S. Treasury Bureau of Fiscal Service foreign currency conversion rate on July 1 of the tax year (available at *https://fiscaldata.treasury.gov/datasets/*

treasury-reporting-rates-exchange/treasury-reporting-rates-of-exchange).

(*ii*) In the case of calendar years beginning on or after January 1, 2025, the amounts under paragraph (b)(2)(iv)(*1*) and paragraph (b)(2)(iv)(*2*) of this section will be adjusted at the same time and in the same manner as the amounts are adjusted under section 415(d), except that the base period will be the calendar quarter beginning July 1, 2024.

(v) Withdrawals, distributions, or payments from the trust are conditioned upon reaching a specified retirement age, disability, or death, or penalties apply to withdrawals, distributions, or payments made before such conditions are met. A trust that otherwise meets the requirements of this paragraph (b)(2)(v), but that allows withdrawals, distributions, or payments for in-service loans or for reasons such as hardship, educational purposes, or the purchase of a primary residence, will be treated as meeting the requirements of this paragraph.

(vi) In the case of an employer-maintained trust:

(A) The trust is nondiscriminatory insofar as a wide range of employees, including rank and file employees, must be eligible to make or receive contributions or accrue benefits under the terms of the trust (alone or in combination with other comparable plans);

(B) The trust (alone or in combination with other comparable plans) actually provides significant benefits for a substantial majority of eligible employees; and

(C) The benefits actually provided under the trust to eligible employees are nondiscriminatory.

(3) *Tax-favored foreign non-retirement savings trust.* For purposes of this section, a *tax-favored foreign non-retirement savings trust* means a foreign trust that is created, organized, or otherwise established under the laws of a foreign jurisdiction (*the trust's jurisdiction*) as a trust, plan, fund, scheme, or other arrangement (collectively, a *trust*) to operate exclusively or almost exclusively to provide, or to earn income for the provision of, medical, disability, or educational benefits, and that meets the following requirements established by the laws of the trust's jurisdiction:

(i) The trust generally is exempt from income tax or otherwise is tax-favored under the laws of the trust's jurisdiction as defined in paragraph (b)(2)(i) of this section.

(ii) Annual information reporting with respect to the trust (or of its participants or beneficiaries) is provided, or otherwise is available, to the relevant tax authorities in the trust's jurisdiction.

(iii) Contributions to the trust are limited to $10,000 (multiplied by the cost-of-living adjustment determined under section 1(f)(3) for the calendar year by substituting ''calendar year 2020'' for ''calendar year 2016'' in section 1(f)(3)(A)(ii) and rounding to the nearest multiple of $1,000) or less annually, or $200,000 (multiplied by the cost-of-living adjustment determined under section 1(f)(3) for the calendar year by substituting ''calendar year 2020'' for ''calendar year 2016'' in section 1(f)(3)(A)(ii) and rounding to the nearest multiple of $1,000) or less on a lifetime basis, determined using the U.S. Treasury Bureau of Fiscal Service foreign currency conversion rate on the last day of the tax year (available at *https://fiscaldata.treasury.gov/datasets/treasury-reporting-rates-exchange/treasury-reporting-rates-of-exchange*).

(iv) Withdrawals, distributions, or payments from the trust are conditioned upon the provision of medical, disability, or educational benefits, or apply penalties to withdrawals, distributions, or payments made before such conditions are met.

(4) *Tax-favored foreign de minimis savings trusts.* For purposes of this section, a *tax-favored foreign de minimis savings trust* means a foreign trust that is created, organized, or otherwise established under the laws of a foreign jurisdiction (*the trust's jurisdiction*) as a trust, plan, fund, scheme, or other arrangement (collectively, a *trust*) to operate as a savings vehicle, that is not treated as a *tax-favored foreign retirement trust,* as described in paragraph (b)(2) or a *tax-favored foreign non-retirement savings trust,* as described in paragraph (b)(3), and that meets each of the following requirements:

(i) The trust generally is exempt from income tax or otherwise is tax-favored under the laws of the trust's jurisdiction as defined in paragraph (b)(2)(i) of this section;

(ii) Annual information reporting with respect to the trust (or of its participants or beneficiaries) is provided, or otherwise is available, to the relevant tax authorities in the trust's jurisdiction pursuant to the laws of the trust's jurisdiction; and

(iii) The aggregate value of the trust(s) in the trust's jurisdiction is limited to no more than $50,000 at any point during the taxable year (multiplied by the cost-of-living adjustment determined under section 1(f)(3) for the calendar year by substituting ''[the year of the date of publication of the final regulations in the **Federal Register**]'' for ''calendar year 2016'' in section 1(f)(3)(A)(ii) and rounding to the nearest multiple of $1,000) regardless of the number of trusts established. The $50,000 is determined using the U.S. Treasury Bureau of Fiscal Service foreign currency conversion rate on the last day of the tax year (available at *https://fiscaldata.treasury.gov/datasets/treasury-reporting-rates-exchange/treasury-reporting-rates-of-exchange*).

(5) *Certain rollovers and transfers.* A trust that otherwise meets the requirements of paragraphs (b)(2) or (b)(3) of this section will not fail to be treated as a tax-favored foreign retirement or non-retirement savings trust within the meaning of this paragraph (b) solely because it may receive a rollover of assets or funds transferred from another tax-favored foreign retirement or non-retirement savings trust established and operated under the laws of the same jurisdiction, provided that the trust transferring assets or funds also meets the requirements of this paragraph (b)(2) or (b)(3), as applicable (but this paragraph does not apply to transfers between tax-favored retirement trusts and non-retirement savings trusts).

(c) *Exception for distributions from certain foreign compensatory trusts.* Section 6048(c) does not apply to a distribution received by a U.S. person from a foreign trust described in § 1.672(f)–3(c)(1) provided that the U.S. person includes in income any amounts accumulated on behalf of, or distributed by the trust, to the U.S. person to the extent such amounts are required to be included in income (other than amounts that are exempt from Federal income tax under a bilateral income tax treaty or any other bilateral agreement to which the United States is a party) of the U.S. person, including pursuant to section 409A(b).

(d) *Exception for certain distributions received by domestic section 501(c)(3) organizations.* Section 6048(c) does not apply to a distribution from a foreign trust received by a domestic organization, provided that the organization has received a determination letter from the Commissioner that has not been revoked recognizing that the domestic organization is exempt from Federal income tax under section 501(a) as an organization described in section 501(c)(3).

(e) *Exception for certain mirror code possession trusts.* Sections 6048(a) through 6048(c) do not apply to a trust located in a mirror code possession to the extent the responsible party (within the meaning of section 6048(a)(4)), U.S. owner, or U.S. recipient is a bona fide

resident (within the meaning of § 1.937–1(b)) of such mirror code possession. For purposes of this paragraph (e), a mirror code possession is a possession of the United States where, under the income tax system of the possession, the income tax liability of the residents of the possession is determined by reference to the income tax laws of the United States as if the possession were the United States, and a trust is located in a mirror code possession if a court within the mirror code possession is able to exercise primary supervision over the administration of the trust and one or more bona fide residents of the mirror code possession have the authority to control all substantial decisions of the trust.

§ 1.6048–6 Special rules.

(a) *Special rules*—(1) *Dual resident taxpayers.* If a dual resident taxpayer (within the meaning of § 301.7701(b)–7(a)(1) of this chapter) computes U.S. income tax liability as a nonresident alien on the last day of the taxable year and complies with the filing requirements of § 301.7701(b)–7(b) and (c) of this chapter, the dual resident taxpayer is not treated as a U.S. person for purposes of section 6048 with respect to the portion of the taxable year the dual resident taxpayer is treated as a nonresident alien for purposes of computing U.S. income tax liability.

(2) *Dual status taxpayers.* If a taxpayer abandons U.S. citizenship or residence during the taxable year or acquires U.S. citizenship or residence during the taxable year as provided in § 1.6012–1(b)(2)(ii), the taxpayer will is not treated as a U.S. person for purposes of §§ 1.6048–1 through 1.6048–7 with respect to the portion of the taxable year the taxpayer was treated as a nonresident alien for purposes of computing U.S. income tax liability.

(b) *Effect of ownership under the grantor trust rules.* The fact that a portion of a foreign trust is treated as owned by the grantor or another person under subpart E of part I of subchapter J of chapter 1 of the Internal Revenue Code is irrelevant for purposes of determining whether a U.S. person makes a transfer to, or receives a distribution from, a foreign trust that must be reported under §§ 1.6048–2 through 1.6048–4. *See* § 1.6048–4(g)(13) and (14).

(c) [Reserved]

(d) *Married U.S. persons filing a joint income tax return.* Married U.S. persons who file a joint income tax return under section 6013 for a tax year, and each of whom is subject to the information reporting requirements under §§ 1.6048–2(a) (as a grantor or transferor under §§ 1.6048–2(c)(1) and (2) required to file Part I of Form 3520), 1.6048–3(a)(2) (as a U.S. owner of a foreign trust required to file a substitute Form 3520–A), or 1.6048–4(a) (as a U.S. recipient of a distribution from a foreign trust required to file Part III of Form 3520) for the same foreign trust, may together file a single Form 3520, Annual Return to Report Transactions with Foreign Trusts and Receipt of Certain Foreign Gifts, for that year at the time and in the manner described in §§ 1.6048–2 through 1.6048–6. For purposes of filing a substitute Form 3520–A under § 1.6048–3(a)(2), a separate Foreign Grantor Trust Owner statement must be completed and attached for each married U.S. person. *See* § 1.6677–1(f) with respect to liability for penalties.

§ 1.6048–7 Applicability dates.

(a) *In general.* The rules of §§ 1.6048–1 through 1.6048–4 and § 1.6048–6 apply as follows:

(1) Section 1.6048–1 applies after the [date of publication of the final regulations in the **Federal Register**].

(2) To the extent related to § 1.6048–2, including the relevant portions of § 1.6048–6, the rules apply to reportable events occurring after the [date of publication of the final regulations in the **Federal Register**].

(3) To the extent related to § 1.6048–3, including the relevant portions of § 1.6048–6, the rules apply to taxable years of U.S. persons beginning after the [date of publication of the final regulations in the **Federal Register**].

(4) To the extent related to § 1.6048–4, including the relevant portions of § 1.6048–6, the rules apply to distributions received after the [date of publication of the final regulations in the **Federal Register**].

(b) *Special rule for § 1.6048–5.* Section 1.6048–5 applies as follows—

(1) To the extent related to reportable events under section 6048(a) and the regulations under section 6048 in this part, the rules apply to reportable events occurring after the [date that final regulations are published in the **Federal Register**].

(2) To the extent related to ownership of a foreign trust under section 6048(b) and the regulations under section 6048 in this part, the rules apply to taxable years of U.S. owners beginning after the [date that final regulations are published in the **Federal Register**]; and

(3) To the extent related to distributions from a foreign trust under section 6048(c) and the regulations under section 6048 in this part, the rules apply to distributions received after the [date that final regulations are published in the **Federal Register**].

■ **Par. 10.** Section 1.6677–1 is added to read as follows:

§ 1.6677–1 Failure to file information with respect to certain foreign trusts.

(a) *Civil penalty*—(1) *In general.* In addition to any criminal penalty provided by law, and subject to the rules of paragraph (b) of this section (concerning reporting required under § 1.6048–3) and the rules of paragraph (a)(3) of this section (regarding the maximum penalty that may be assessed), if any notice or return required to be filed by §§ 1.6048–2 through 1.6048–4 is not timely filed, or contains incomplete or incorrect information, then with respect to each failure to comply with §§ 1.6048–2 through 1.6048–4, the person required to file such notice or return must pay a penalty equal to the greater of $10,000 or 35 percent of the gross reportable amount (within the meaning of paragraph (c) of this section).

(2) *Penalty for continuing failure.* Subject to the rules of paragraph (a)(3) of this section (regarding the maximum penalty that may be assessed), if any failure described in paragraph (a)(1) of this section continues for more than 90 days after the day on which the Commissioner mails notice of such failure to the person required to pay the penalty, the person must pay an additional penalty (in addition to the amount determined under paragraph (a)(1) of this section) of $10,000 for each 30-day period (or fraction thereof) during which the failure continues after the expiration of the 90-day period.

(3) *Maximum penalty*—(i) *Limited to gross reportable amount.* At such time as the gross reportable amount with respect to any failure can be determined by the Commissioner, the aggregate amount of the penalties imposed under paragraphs (a)(1) and (2) of this section will be reduced as necessary to ensure that the amount does not exceed the gross reportable amount with respect to that failure (and to the extent that the aggregate amount already collected exceeds the gross reportable amount, the Commissioner will refund the excess amount pursuant to section 6402).

(ii) *Period of limitations on refund of excess amounts.* The limitations period provided for claims for refund under section 6511(a) and (b) applies to the refund of any excess amount.

(b) *Special rules for returns under § 1.6048–3.* In the case of a Form 3520–A or a substitute Form 3520–A, including attached statements, that are required to be filed and furnished under § 1.6048–3(a)—

(1) The U.S. person who is treated as the owner of the foreign trust (or a

portion of the foreign trust) is liable for the penalty imposed by paragraph (a) of this section for the failure to comply with § 1.6048–3(a), and

(2) Paragraph (a) of this section is applied by substituting ''5 percent'' for ''35 percent.''

(c) *Gross reportable amount*—(1) *In general.* For purposes of paragraph (a) of this section, the term *gross reportable amount* means—

(i) The gross value of the property involved in the reportable event (determined as of the date of the event) in the case of a failure relating to § 1.6048–2,

(ii) The gross value of the portion of the trust's assets at the close of the trust's taxable year treated as owned by the U.S. person in the case of each applicable failure relating to § 1.6048–3, and

(iii) The gross amount of the distribution in the case of a failure relating to § 1.6048–4.

(2) *Gross value and gross amount.* The gross value or gross amount of property is determined in accordance with the valuation principles of sections 2512 and 2031 and the regulations under sections 2512 and 2031 in this part, though, in all events, without regard to any taxes, expenses, liabilities, or restrictions on the sale or use of the property.

(d) *Reasonable cause exception*—(1) *In general.* Paragraph (a) of this section does not apply to any failure to file information with respect to a foreign trust if the person required to file such information submits a reasonable cause statement to the Commissioner under penalties of perjury and demonstrates to the satisfaction of the Commissioner that the failure is due to reasonable cause and not due to willful neglect. The determination of whether a taxpayer acted with reasonable cause and not with willful neglect is made under the principles set out in § 1.6664–4 and § 301.6651–1(c) of this chapter. This determination is made on a case-by-case basis, taking into account all pertinent facts and circumstances.

(2) *Examples of situations that do not satisfy the reasonable cause exception.* Examples of facts that do not constitute reasonable cause for purposes of this paragraph (d) include but are not limited to the following:

(i) The fact that a foreign jurisdiction would impose a civil or criminal penalty on such person (or any other person) for disclosing the required information.

(ii) Refusal on the part of a foreign trustee to provide information for any reason, including difficulty in producing the required information or the existence of provisions in the trust instrument that prevent the disclosure of required information.

(e) *Deficiency procedures do not apply.* Subchapter B of chapter 63 (relating to deficiency procedures for income, estate, gift, and certain excise taxes) does not apply in respect of the assessment or collection of any penalty imposed under this section.

(f) *Married U.S. persons filing a joint income tax return*—(1) *In general.* For purposes of this section, married U.S. persons who file one Form 3520 with respect to the same foreign trust under § 1.6048–6(d) for a tax year are treated as if they are a single U.S. person for that year.

(2) *Anti-abuse rule.* For purposes of this section, the Commissioner may treat married U.S. persons who file a joint income tax return under section 6013 for a tax year as a single U.S. person for that year, unless the Commissioner determines that, based on all the facts and circumstances, only one of the married individuals was subject to the information reporting requirement under §§ 1.6048–2 through 1.6048–4 (for example, because only one spouse had an interest in the property constituting the transfer to, or receipt from, a foreign trust).

(3) *Joint and several liability.* If married U.S. persons are treated as a single U.S. person for a tax year, such married U.S. persons have joint and several liability with respect to any penalties imposed under this section.

(g) *Examples.* The following examples illustrate the rules of this section. In each example, X is a U.S. person and FT is a foreign trust.

(1) *Example 1: Partial reporting.* X transfers property worth $100,000 to FT but reports only $40,000 of that amount on Part I of Form 3520 pursuant to § 1.6048–2. X does not demonstrate to the satisfaction of the Commissioner that X's failure to report the correct amount was due to reasonable cause and not due to willful neglect. Under paragraph (a)(1) of this section, penalties will be imposed only on the unreported $60,000.

(2) *Example 2: Maximum penalty limited to gross reportable amount.* X receives a distribution of $100,000 from FT in Year 1 but fails to report the distribution as required by § 1.6048–4(a). The Commissioner learns about the distribution but does not have enough information to determine the gross reportable amount. On January 2, Year 4, the Commissioner mails a notice of the reporting failure to X and assesses a penalty of $10,000 under paragraph (a)(1) of this section. X does not comply with X's reporting requirement within 90 days after the day that the Commissioner mails the notice (by April 2, Year 4), so the Commissioner begins to assess additional penalties of $10,000 under paragraph (a)(2) of this section for each 30-day period (or fraction thereof), beginning on April 2, Year 4, during which the failure continues. By the time X complies with X's reporting requirement, the aggregate penalties assessed with respect to X's failure to report the distribution total $150,000. Under paragraph (a)(3)(i) of this section, the maximum penalty that the Commissioner may assess with respect to this failure is $100,000 (the applicable gross reportable amount determined under paragraph (c)(1)(iii) of this section), and the Commissioner must abate the excess $50,000 of assessed penalties.

(3) *Example 3: Maximum penalty limited to gross reportable amount below $10,000 minimum.* Assume the same facts as in Example 2 above except that instead of a $100,000 distribution, X receives a distribution of $4,000 from FT. By the time X complies with X's reporting requirement, the aggregate penalties assessed with respect to X's failure to report the distribution total $20,000. Under paragraph (a)(3)(i) of this section, the maximum penalty that the Commissioner may assess with respect to this failure is $4,000 (the applicable gross reportable amount determined under paragraph (c)(1)(iii) of this section), and the Commissioner must abate the excess $16,000 of assessed penalties.

(4) *Example 4: Multiple failures over multiple years.* X created FT in Year 1 and is treated as the owner of FT under the grantor trust rules. The trustee of FT fails to file a Form 3520–A with respect to FT for Year 2 and Year 3 as required by § 1.6048–3(a)(1), and X fails to file a substitute Form 3520–A and a Form 3520 (as required by § 1.6048–3(a)(2)) for the same period. (In Year 4, X replaces the trustee, and the new trustee files a Form 3520–A for Year 4.) Under paragraphs (a)(1) and (b) of this section, X is subject to one penalty for Year 2 and one penalty for Year 3 for the failure to comply with § 1.6048–3(a)(1) and (a)(2) for those years.

(5) *Example 5: Distribution from foreign-owned grantor trust through an intermediary.* Y, a nonresident alien, is treated as the owner of FT under section 676, after the application of section 672(f). X receives a distribution from FT through an intermediary as described in § 1.6048–4(b)(2)(i). X does not include the distribution in gross income and does not report the distribution on Part III of Form 3520 as required by § 1.6048–4(a). Even if the Commissioner

determines that X was not required to include the distribution in gross income, X is liable for penalties imposed by paragraph (a)(1) of this section based on the gross reportable amount determined under paragraph (c)(1)(iii) of this section because X is required to report indirect transfers of property under § 1.6048–4(b)(2)(iv).

(6) *Example 6: Multiple failures in multiple years.* (i) *Facts.* On December 31, Year 1, X creates FT and makes a gratuitous transfer of property with a value of $100,000 to FT. X is treated as the sole owner of FT under the grantor trust rules. During Year 2, X makes no transfers to FT and receives no distributions from FT. At the end of Year 2, the value of FT's assets is $110,000. During Year 3, X makes no transfers to FT, but X receives a distribution of $30,000. At the end of Year 3, the value of FT's assets is $85,000. X does not file any Forms 3520 or substitute Forms 3520–A for Year 1 through Year 3. The Trustee of FT does not file any Forms 3520–A for Year 1 through Year 3.

(ii) *Analysis*–(A) *Year 1.* For Year 1, X is subject to two penalties under paragraphs (a)(1) and (b) of this section: a $35,000 penalty (the greater of $10,000 or $35,000 (35% of $100,000)) for failure to comply with § 1.6048–2(a) and a $10,000 penalty (the greater of $10,000 or $5,000 (5% of $100,000)) for failure to comply with § 1.6048–3(a). If X does not comply with X's reporting requirements for Year 1 within 90 days after the day on which the Commissioner mails notice of the reporting failures to X, X will be subject to additional penalties under paragraph (a)(2) of this section of $10,000 per failure per 30-day period (or fraction thereof) ($20,000 in the aggregate per 30-day period (or fraction thereof)) during which the failure continues. Under paragraph (a)(3)(i) of this section, the aggregate amount of the penalty imposed under paragraphs (a)(1) and (2) of this section with respect to each failure will not exceed the gross reportable amount for that failure.

(B) *Year 2.* For Year 2, X is subject to one penalty under paragraphs (a)(1) and (b) of this section: a $10,000 penalty (the greater of $10,000 or $5,500 (5% of $110,000)) for failure to comply with § 1.6048–3(a). If X does not comply with X's reporting requirements for Year 2 within 90 days after the day on which the Commissioner mails notice of the reporting failures to X, X will be subject to additional penalties under paragraph (a)(2) of this section of $10,000 per failure per 30-day period (or fraction thereof) ($10,000 per 30-day period (or fraction thereof)) during which the failure continues. Under paragraph (a)(3)(i) of this section, the aggregate amount of the penalty imposed under paragraphs (a)(1) and (2) of this section with respect to each failure will not exceed the gross reportable amount for that failure.

(C) *Year 3.* For Year 3, X is subject to two penalties under paragraphs (a)(1) and (b) of this section: a $10,000 penalty (the greater of $10,000 or 4,250 (5% of $85,000)) for failure to comply with § 1.6048–3(a), and a penalty of $10,500 (the greater of $10,000 or $10,500 (35% of $30,000)) for failure to comply with § 1.6048–4. If X does not comply with X's reporting requirements for Year 3 within 90 days after the day on which the Commissioner mails notice of the reporting failures to X, X will be subject to additional penalties under paragraph (a)(2) of this section of $10,000 per failure per 30-day period (or fraction thereof) ($20,000 in the aggregate per 30-day period (or fraction thereof)) during which the failure continues. Under paragraph (a)(3)(i) of this section, the aggregate amount of the penalty imposed under paragraphs (a)(1) and (2) of this section with respect to each failure will not exceed the gross reportable amount for that failure.

(iii) *Conclusion.* X is subject to aggregate penalties of $75,500 under paragraphs (a)(1) and (b) of this section: $45,000 for Year 1, $10,000 for Year 2, and $20,500 for Year 3. X may be subject to additional penalties under paragraph (a)(2) of this section if X fails to comply with X's reporting requirements within 90 days after the day on which the Commissioner mails notice of each failure to X. Under paragraph (a)(3)(i) of this section, the aggregate amount of the penalty imposed under paragraphs (a)(1) and (2) of this section with respect to each failure will not exceed the gross reportable amount for that failure.

(7) *Example 7: Interaction with § 1.6039F–1.* In Year 1, X receives $500,000 from FT that X treats as a gift. Under § 1.6048–4(d) and § 1.6039F–1(b), X is required to report the amount as a distribution under § 1.6048–4 and not as a foreign gift under § 1.6039F–1(a). However, based on the advice of X's tax advisor, X reports the distribution under § 1.6039F–1(a) and not under § 1.6048–4. X's failure to report the distribution under § 1.6048–4 is subject to penalties under § 1.6677–1(a) unless X demonstrates to the satisfaction of the Commissioner that such failure is due to reasonable cause and not due to willful neglect. The fact that X reported the distribution under § 1.6039F–1(a) based on the advice of X's tax advisor is a factor that may be taken into account in determining whether X's failure to report the distribution under § 1.6048–4 was due to reasonable cause. X's reliance on X's tax advisor's advice can only constitute reasonable cause, however, if, under all the circumstances, the reliance was reasonable within the meaning of § 1.6664–4(c).

(8) *Example 8: Presumption that FT has a U.S. owner.* X created FT in Year 1 and transferred $100,000 to FT. X reported the transfer to FT on Part I of Form 3520 for Year 1, but did not complete the other parts of Form 3520. X did not file any Forms 3520 with respect to FT in Year 2 or subsequent years. FT has not filed any Forms 3520–A with respect to FT (and X has not filed any substitute Forms 3520–A). Pursuant to § 1.679–2(d)(2), the Commissioner sends a written notice to X requesting additional information related to the trust and its potential beneficiaries. X does not respond. Under § 1.679–2(d)(1), FT is treated as having a U.S. beneficiary. Under § 1.679–1(a), X is treated as the owner of FT. Under paragraphs (a) and (b) of this section, X is subject to penalties for Year 1 and subsequent years for failure to comply with § 1.6048–3(a).

(9) *Example 9: Penalty for failure to report loan that is not treated as a section 643(i) distribution.* FT is not treated as being owned by X or any other person under the grantor trust rules. X receives a loan of cash from FT and in exchange issues an obligation to FT that is a qualified obligation within the meaning of § 1.643(i)–2(b)(2)(iii). Provided the obligation does not cease to be a qualified obligation, the loan will not be a section 643(i) distribution under § 1.643(i)–1(a) and therefore will not be taxable to X. However, the loan is a distribution within the meaning of § 1.6048–4(b)(3) that must be reported on Part III of Form 3520 under § 1.6048–4(a). X fails to report the loan. X is subject to penalties under § 1.6677–1(a) unless X demonstrates to the satisfaction of the Commissioner that such failure is due to reasonable cause and not due to willful neglect.

(10) *Example 10: Joint and several penalties.* X and Y are married U.S. persons who file a joint income tax return under section 6013. In Year 1, X and Y create FT and fund the trust with $100,000 for the benefit of their U.S. children. X and Y jointly file their income tax return for the Year 1 tax year but fail to file a Form 3520 reporting the transfer of assets to a foreign trust pursuant to § 1.6048–2. In addition, FT has not filed any Forms 3520–A with respect to FT (and X and Y have not filed any substitute Forms 3520–A)

pursuant to § 1.6048–3(a). For the Year 1 tax year, X and Y are jointly and severally liable for penalties under paragraph (a) of this section pursuant to paragraph (f)(2) and (3) of this section.

(h) *Applicability dates*—(1) *Reportable events.* To the extent related to § 1.6048–2, this section applies to reportable events occurring after the [date of publication of the final regulations in the **Federal Register**].

(2) *U.S owners of foreign trusts.* To the extent related to § 1.6048–3, this section applies to taxable years of U.S. persons beginning after the [date of publication of the final regulations in the **Federal Register**].

(3) *Reporting by U.S. persons receiving distributions from foreign trusts.* To the extent related to § 1.6048–4, this section applies to distributions received after the [date of publication of the final regulations in the **Federal Register**].

Douglas W. O'Donnell,

Deputy Commissioner.

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