



August 14, 2023

Mr. Ryan K. Bessey
Senior Program Analyst
Office of Servicewide Penalties
Internal Revenue Service
Ogden Campus, M/S 4951

RE: Improvements to Form 3520 and Form 3520-A and Instructions

Dear Mr. Bessey:

On behalf of the American Institute of CPAs (AICPA), we are writing to provide our suggestions for improvements to the 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, and instructions.

We appreciate the dialogue we have had with the Internal Revenue Service (“IRS”) Office of Servicewide Penalties regarding many of the issues with Form 3520 penalties that practitioners and taxpayers face.

We request that the Department of the Treasury (“Treasury”) and IRS consider the following recommendations regarding the Form 3520 and Form 3520-A and instructions.

1. In cases where a foreign trust did not appoint a U.S. agent, update [Form 3520 instructions](#) to agree with the directions provided on Form 3520, line 3, and Part I, Schedule B, lines 15 – 18.
2. Add to the instructions and to the Form 3520; Part III – for Line 29 - “If you are filing Form 3520 with respect to a foreign nongrantor trust, check N/A,” and for Line 30 - “If you are filing Form 3520 with respect to a foreign grantor trust, check N/A.”
3. Add to the instructions for Form 3520-A for Part III, Balance Sheet, a sentence such as “It is not necessary or required to reconcile any differences between the book and tax basis of assets and liabilities.” Also, add a sentence to clarify that it is not necessary to reconcile changes in the fair market value of assets and liabilities between the beginning and end of the tax year.
4. For Form 3520, clarify that if a U.S. person required to file a Form 3520 has filed their Form 1040, U.S. Individual Income Tax Return, on or before the original due date, it is still possible to extend the due date for filing a Form 3520 by filing an extension (in the case of an individual, a Form 4868, Application for Automatic Extension of Time to File U.S. Individual Income Tax Return) on or before the original due date of the U.S. person’s return (April 15 in the case of an individual).

5. Clarify that a Form 7004, Application for Automatic Extension of Time To File Certain Business Income Tax, Information, and Other Returns, can be electronically filed to extend a Form 3520-A, and a Form 4868 can be electronically filed to extend a Form 3520.
6. In cases where a substitute Form 3520-A will be filed, clarify that no extension for Form 3520-A needs to be filed. Also, state that it is acceptable, but not required, if a separate extension for Form 3520-A is filed in cases where a substitute Form 3520-A is filed.
7. Make additional AICPA recommended changes to the Form 3520 and Form 3520-A and instructions,¹ including:
 - Allow e-filing of the Form 3520 and Form 3520-A, which could reduce the number of returns incorrectly being assessed late filing penalties.
 - Make clear in the instructions to the Form 3520 when an employer identification number (EIN) is required. For example, clarify whether a foreign non-grantor trust needs to obtain an EIN if it has U.S. beneficiaries but otherwise does not derive any U.S. source income or have any connections to the United States.
 - Provide that the U.S. agent form only needs to be attached to Form 3520 and Form 3520-A every three years unless there has been a change.
 - Include an exemption from Form 3520 and Form 3520-A reporting for foreign pensions where deferral of tax on earnings is available under a tax treaty, as in the case of Form 8621, Information Return by a Shareholder of a Passive Foreign Investment Company or Qualified Electing Fund. See Treas. Reg. § 1.1298-1(c)(4).

Detailed Recommendations

1. **In cases where a foreign trust did not appoint a U.S. agent, update [Form 3520 instructions](#) to agree with the directions provided on **Form 3520, line 3, and Part I, Schedule B, lines 15 – 18.****

The IRS [Form 3520 instructions](#) and the actual Form 3520 are not in agreement as to when the taxpayer must complete lines 15 through 18 of Part I for a trust that does not appoint a US agent. Based on discussions with IRS, it is our understanding that the second sentence of line 3 on page 1 of Form 3520 and the “Note” found in the heading to Form 3520, Part I: Schedule B (found on page 3) provide the correct and current direction on when it is necessary to fill out lines 15 through 18. It is our understanding based on discussions with IRS that the instructions to line 3 of Form 3520 have not been updated to match the form, these instructions are currently incorrect, and IRS plans to update the 2023 Form 3520 instructions. It is our understanding that taxpayers should follow the form and not the instructions on this issue.

2. **Add to the instructions and to the Form 3520; Part III – for Line 29 - “If you are filing Form 3520 with respect to a foreign nongrantor trust, check N/A,” and for Line 30 - “If you are filing Form 3520 with respect to a foreign grantor trust, check N/A.”**

¹ See AICPA letter, “[Response to Request for Public Comments 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 \(OMB Number: 1545-0159\)](#),” February 13, 2023, and item 46 on page 32 of AICPA letter, [Recommendations for the 2023-2024 Guidance Priority List \(Notice 2023-36\)](#),” May 9, 2023.

As an example, when other parts of the Form 3520 make clear that the form is being filed for a grantor trust situation, if 'No' is checked on Line 30 instead of 'NA', a notice is generated incorrectly directing the taxpayer to complete Schedule A or B. IRS should consider revising the programming related to these line items. While the instructions do explain when to check 'NA', an honest answer can be 'No' and the consequences of differentiating between 'No' and 'NA' are not obvious resulting in time consuming incorrect notices. If IRS notice programming is not able to be adjusted for this, IRS should consider adding to the Form 3520 and the instructions, for Line 29, "If you are filing Form 3520 with respect to a foreign nongrantor trust, check N/A," and for Line 30 - "If you are filing Form 3520 with respect to a foreign grantor trust, check N/A."

- 3. Add to the instructions for Form 3520-A for Part III, Balance Sheet, a sentence such as "It is not necessary or required to reconcile any differences between the book and tax basis of assets and liabilities." Also, add a sentence to clarify that it is not necessary to reconcile changes in the fair market value of assets and liabilities between the beginning and end of the tax year.**

The current Form 3520 instructions provide that the balance sheet is required on a fair market value basis and the profit/loss statement is on a tax basis. These different requirements set up a disconnect (without the benefit of a reconciling M-1 schedule). Taxpayers sometimes express concerns about how to handle this disconnect given the draconian penalties where a substantially incomplete form is filed. Taxpayers are worried that somehow "improperly" handling this will produce an IRS notice. These concerns could be alleviated if IRS provided in the instructions that the required different accounting methods are intentional and that a reconciliation of the difference between book and tax basis is not necessary.

- 4. For Form 3520, clarify that if a U.S. person required to file a Form 3520 has filed their Form 1040, U.S. Individual Income Tax Return, on or before the original due date, it is still possible to extend the due date for filing a Form 3520 by filing an extension (in the case of an individual, a Form 4868, Application for Automatic Extension of Time to File U.S. Individual Income Tax Return) on or before the original due date of the U.S. person's return (April 15 in the case of an individual).**

The due date for filing Form 3520 for most individuals is April 15, the 15th day of the fourth month following the end of the individual's tax year. The filing of a Form 4868, Application for Automatic Extension of Time To File U.S. Individual Income Tax Return, to extend the due date of an individual's income tax return will automatically extend the filing of Form 3520. Based on our discussions with the IRS, in cases where an individual timely files an income tax return on or before the original due date, it remains possible to extend the filing date for a Form 3520 by filing a Form 4868. In many cases as a result of limitations presented by the electronic filing components of tax return preparation software (because the Form 1040 was already electronically filed), it may be necessary to paper file a Form 4868 in order to complete and properly extend the filing of Form 3520. Based on our discussions with the IRS, the paper filing a Form 4868 will in fact extend the due date for Form 3520.

5. Clarify that a Form 7004, Application for Automatic Extension of Time To File Certain Business Income Tax, Information, and Other Returns, can be electronically filed to extend a Form 3520-A and a Form 4868 can be electronically filed to extend a Form 3520.

While there may be practical issues and limitations presented by various tax return software systems since Form 3520 and Form 3520-A currently cannot be electronically filed, based on our conversations with, and follow-up from, IRS, it is our understanding that an extension form, Form 7004, can be electronically filed to extend the due date for Form 3520-A, and the individual income tax extension form, Form 4868, can be electronically filed to extend the Form 3520.

6. In cases where a substitute Form 3520-A will be filed, clarify that no extension for Form 3520-A needs to be filed. Also, state that it is acceptable, but not required, if a separate extension for Form 3520-A is filed in cases where a substitute Form 3520-A is filed.

In cases where a foreign trust will not separately file a Form 3520-A, the taxpayer is permitted to attach a substitute Form 3520-A to a properly completed and timely filed Form 3520 in accordance with the directions provided in the instructions to Form 3520. In such cases, the Form 3520-A is considered timely filed if filed as an attachment to a timely filed Form 3520. Based on our discussions with IRS, where a substitute Form 3520-A will be filed, it is not necessary to file an extension for Form 3520-A on or before the original due date, March 15 for a calendar year trust. Based on our discussions with the IRS, although not necessary, it will not interfere with IRS processing if a taxpayer does file a separate extension for Form 3520-A and then files a substitute Form 3520-A as an attachment to the timely filed Form 3520.

7. Make additional AICPA recommended changes to the Form 3520 and Form 3520-A and instructions.

The current only paper filing of Form 3520 and Form 3520-A is burdensome and time consuming for taxpayers, practitioners, and the IRS. It also sometimes causes late filing penalties to be incorrectly assessed. Allowing e-filing of the Form 3520 and Form 3520-A could reduce the number of returns incorrectly being assessed late filing penalties.

In addition, the current instructions to the Form 3520 are not clear when an employer identification number (EIN) is required, and this should be clarified in the instructions. For example, IRS should clarify whether a foreign non-grantor trust needs to obtain an EIN if it has U.S. beneficiaries but otherwise does not derive any U.S. source income or have any connections to the United States.

When there has been no change to the U.S. agent, it is currently burdensome for taxpayers to provide the U.S. agent form attached to the Form 3520 and Form 3520-A every year, and it is more for the IRS to process. We suggest instead that the IRS provide that the U.S. agent form

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only needs to be attached to Form 3520 and Form 3520-A every three years unless there has been a change.

It is burdensome for taxpayers and practitioners to report and for IRS to process the reporting for foreign pensions where deferral of tax on earnings is available under a tax treaty, as in the case of Form 8621, Information Return by a Shareholder of a Passive Foreign Investment Company or Qualified Electing Fund. See Treas. Reg. § 1.1298-1(c)(4). The IRS does not need this information for tax purposes as there is not tax currently due. Therefore, similar to Canadian pension plans under Rev. Proc. 2020-17, IRS and Treasury should provide an exemption from Form 3520 and Form 3520-A reporting for foreign pensions where deferral of tax on earnings is available under a tax treaty.

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The AICPA is the world's largest member association representing the CPA profession, with more than 421,000 members in the United States and worldwide, and a history of serving the public interest since 1887. Our members advise clients on federal, state and international tax matters and prepare income and other tax returns for millions of Americans. Our members provide services to individuals, not-for-profit organizations, small and medium-sized businesses, as well as America's largest businesses.

If you would like to discuss these issues further or have any questions, please contact Henry P. Alden II, Chair, AICPA Form 3520 Penalties Task Force, at (410) 571-0388, or Halden@eightax.com; Eileen Sherr, Director — AICPA Tax Policy & Advocacy, at (202) 434-9256, or Eileen.Sherr@aicpa-cima.com; or me at (830) 372-9692 or bvickers@alamo-group.com.

Sincerely,



Blake Vickers, CPA, CGMA
Chair, AICPA Tax Executive Committee